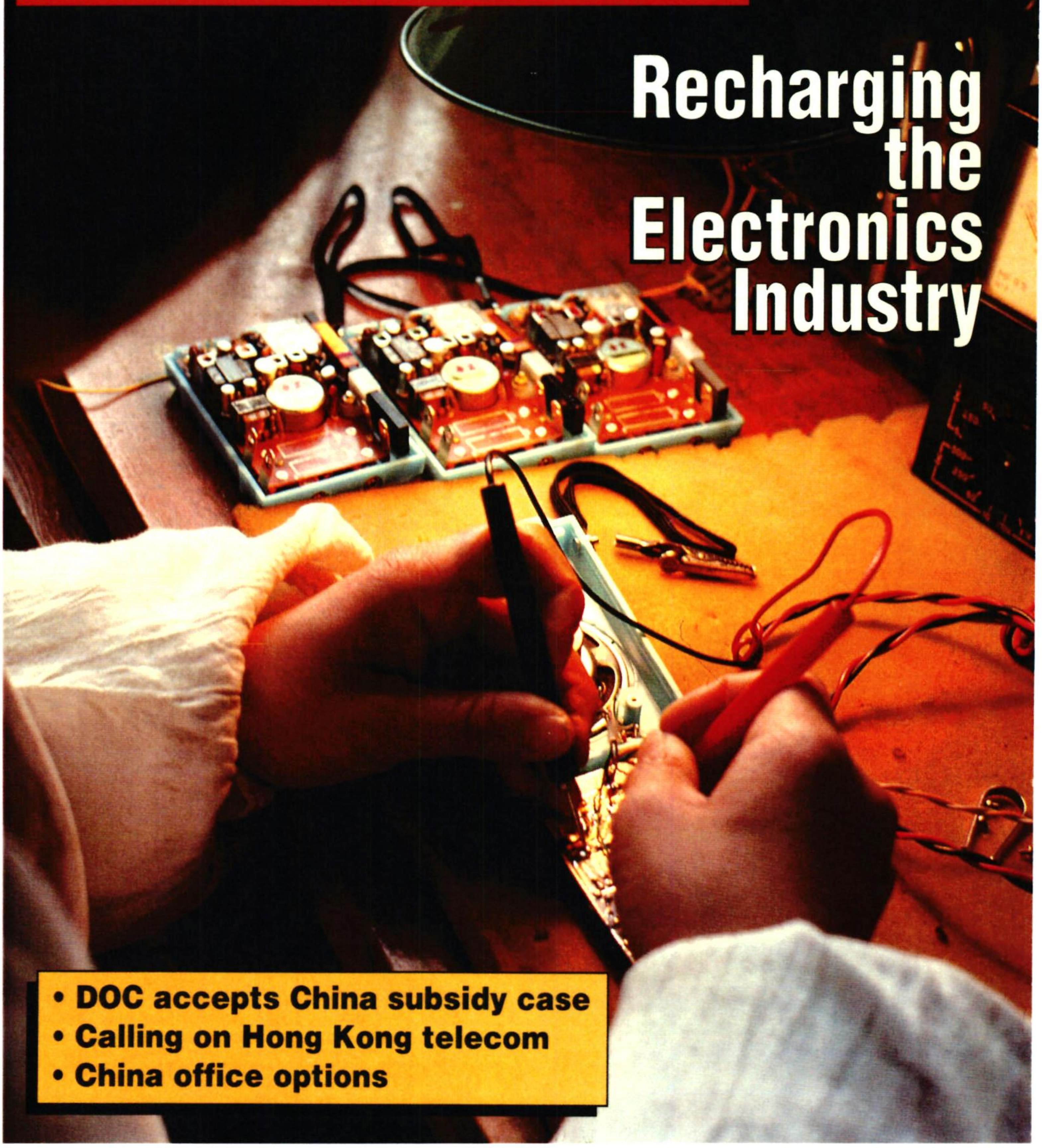
THE CHINA BUSINESS REVIEW

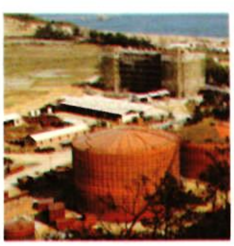
JANUARY-FEBRUARY 1992 VOLUME 19, NUMBER 1



Recharging the Electronics Industry

- DOC accepts China subsidy case
- Calling on Hong Kong telecom
- China office options

TIAN AN: PLANTING THE SEEDS OF SUCCESSFUL INVESTMENT IN CHINA



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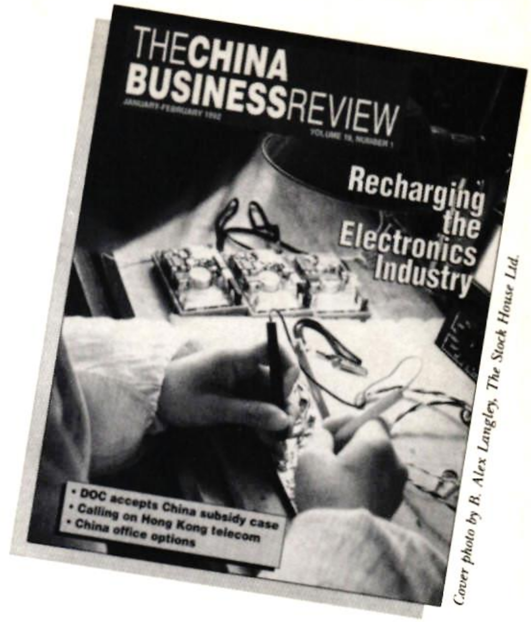

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Features

Departments

Importer Records Seized

In early December, US Customs and Internal Revenue Service special agents seized corporate records of 18 financial institutions and 63 importers of Chinese textiles and apparel. Though no charges have yet been filed against individual companies, the sweep was part of a continuing Customs investigation into illegal imports of Chinese textiles and apparel (*see The CBR*, November-December 1991, p. 6). —VLW

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(Signed) Pamela Baldinger, Editor

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Total No. of Copies Printed	4,166	4,000
Paid Circulation		
Sales through Dealers and Carriers, Street Vendors, and Counter Sales	—0—	—0—
Mail Subscriptions	3,006	3,007
Total Paid Circulation	3,006	3,007
Free Distribution by Mail, Carrier, or Other Means; Samples, Complimentary and Other Free Copies	471	610
Total Distribution	3,477	3,617
Copies not Distributed; Office use, left over, unaccounted, spoiled after printing	689	383
Return from News Agents	—0—	—0—
Total	4,166	4,000

(Signed) Pamela Baldinger, Editor

House Votes on MFN Legislation

In a surprise move at the close of the 1991 legislative session, a House-Senate Conference Committee agreed on legislation attaching conditions to extension of China's Most Favored Nation (MFN) trade status. The compromise bill, which requires the President to certify that China has made "significant progress" on such issues as human rights and nonproliferation, passed the House by a 409-21 margin. The Senate did not vote on the measure before Congress adjourned for the holidays, but can consider the legislation at any time before the 102nd Congress ends in October. In election-year politicking, Senator Mitchell may bring the bill up for a vote in the Senate to put the President on record as having vetoed the measure. —Richard Brecher

China Eyes GATT

China has stepped up its efforts to gain entry into the General Agreement on Tariffs and Trade (GATT), announcing several new trade measures designed to demonstrate the increasing openness of China's economy and move it toward GATT compatibility.

Effective January 1, 1992, China's Customs Administration will reduce import duties on 225 items, including raw materials, pesticides, machinery and parts, and food items. The goods account for about 4.4 percent of China's total imports. At the same time, China will begin conforming to the international Harmonized Commodity Description and Coding System, bringing its foreign trade reporting in line with that of most other countries.

—PB

US Grants Hong Kong COCOM-Member Treatment

In October, the United States conferred COCOM member benefits on Hong Kong, which will enable the territory to import high-technology items beyond 1997, when it reverts to Chinese sovereignty. With a few key exceptions such as supercomputers and crime control equipment, US companies will be able to ship most items to Hong Kong without an export license. Mainland-owned companies based in Hong Kong, however, will still be subject to licensing controls. —PB

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Short Takes

The Cordless Rage

Cellular phones have arrived in China—with startling success. In a country where few homes have telephones and the wait for installation can be long, portable communications are increasingly viewed not just as a status symbol, but as a necessity.

Official estimates put the total number of cellular telephones at nearly 30,000, and the figure could rise to 150,000 by 1995. More than 6,000 such phones are reportedly in use in Beijing, where those unable to foot the purchase price have resorted to a cheaper alternative—pagers.

Costs for buying and using portable telecommunications services are prohibitive by Chinese standards; some models run upwards of ¥20,000, with additional costs of over ¥1 per minute of use. Budding Chinese entreprenuers, however, show no signs of sticker shock.

CCP Plenum Addresses Rural Issues

China's Fifth Plenary Session of the 13th Communist Party Central Committee concluded in Beijing in early December. High on the agenda were water conservation and flood control plans, and an agreement to convene the next party congress in late 1992.

World Bank, ADB Projects Back on Track

A number of new China projects were approved by the World Bank and Asian Development Bank (ADB) in the last half of 1991, indicating that multilateral lending for China is approaching pre-Tiananmen levels. The ADB gave its approval for projects ranging from railway to thermal power plant construction. World Bank project lending also featured a number of power projects, and more approvals for power sector loans are likely in 1992.

Shipping Investigation on Hold

The US Federal Maritime Commission's (FMC) investigation of alleged shipping violations in China has been extended until February, following a Memorandum of Consultation signed by both countries in late October. According to the Memorandum, US carriers will now be permitted to establish joint ventures or wholly foreign-owned enterprises in China, and Chinese and US carriers are to be charged the same port and handling fees—though US carriers will have to pay in foreign exchange, rather than *renminbi*. The FMC will make its final determination based on how the Memorandum is being implemented.

USTR Weighs Sanctions

US and Chinese negotiators failed to reach an agreement on intellectual property protection for US products in China by the stipulated November deadline (*see The CBR*, July-August 1991, p. 7). Following several months of talks, US Trade Representative Carla Hills announced on November 26 that "China's proposals were ultimately insufficient" to warrant termination of the Special 301 investigation authorized under the Trade Act. Accordingly, the office of the US Trade Representative (USTR) subsequently published a preliminary list of 106 Chinese export products that may be subject to retaliatory tariffs, and warned the Chinese government that failure to reach agreement with USTR could result in retaliation against selected items from the list (*see* below). As *The CBR* goes to press, there appears little chance of a last-minute resolution to the dispute, and specific US retaliatory tariffs could be announced by mid-January.

Meanwhile, USTR's investigation into market access barriers in China continues, though no breakthrough appears imminent. USTR has until October 10, 1992, to conduct its inquiries into China's trade practices, though US negotiators hope to wrap up the investigation by May (*see The CBR*, November-December 1991, p. 6). —VLW

Products included in the USTR Special 301 Retaliatory List

(by harmonized tariff system number)

2203.00.00	6101.90.00	6106.90.20	6115.99.20	6203.39.40	6207.99.60	6213.10.10	7307.93.30	8519.91.00
2606.00.00	6102.90.00	6107.19.00	6116.99.80	6203.49.30	6208.19.40	6214.10.10	7315.11.00	8520.20.00
2710.00.15	6103.19.40	6107.29.40	6117.10.40	6204.19.30	6208.29.00	6215.10.00	7318.15.20	8520.31.00
2710.00.30	6103.39.20	6107.99.40	6117.20.00	6204.29.40	6208.99.60	6217.10.00	7318.16.00	8525.20.50
2844.10.20	6103.49.30	6108.19.00	6117.80.00	6204.39.60	6209.90.40	6217.90.00	7318.22.00	8527.11.60
2921.42.24	6104.19.20	6108.29.00	6117.90.00	6204.49.10	6211.11.20	6403.91.60	8001.10.00	8527.21.10
2921.42.70	6104.29.20	6108.39.20	6201.19.00	6204.59.40	6211.12.30	6403.91.90	8001.20.00	8527.31.50
2936.27.00	6104.39.20	6108.99.40	6201.99.00	6204.69.30	6211.39.00	6403.99.60	8425.49.00	8527.39.00
2941.30.00	6104.49.00	6109.90.20	6202.19.00	6205.90.20	6211.49.00	6405.20.90	8505.11.00	8528.20.00
4202.11.00	6104.59.20	6110.90.00	6202.99.00	6206.10.00	6212.10.10	7117.90.50	8509.80.00	9102.12.80
4202.31.60	6104.69.30	6112.19.20	6203.19.40	6207.19.00	6212.10.20	7118.90.00	8516.71.00	
4203.10.40	6105.90.30	6114.90.00	6203.29.30	6207.29.00	6212.90.00	7307.91.50	8516.79.00	

Letter from the President

The uncertainty hanging over US-China commercial relations is unlikely to ease in 1992, as election-year politics are certain to keep China issues in the spotlight. While China is an easy target for critics of all stripes, long-term US interests dictate that the two countries remain engaged both economically and politically.

The Year Ahead

As we embark upon a new year, it is appropriate to reflect on the year just ended before we try to forecast what lies ahead. In the case of US-China relations, it appears that the friction that characterized the relationship in 1991 will likely continue.

The number and breadth of issues that confronted US-China relations reached unprecedented lengths last year; there were over 30 bills containing China-related provisions before Congress when it recessed in November. Alleged Chinese violations on a wide range of topics prompted investigations by the US Customs Service, the US Trade Representative, the Department of Commerce, the Federal Maritime Commission, and other federal agencies. Many of these investigations are still underway, meaning the uncertainty permeating the relationship will continue well into 1992.

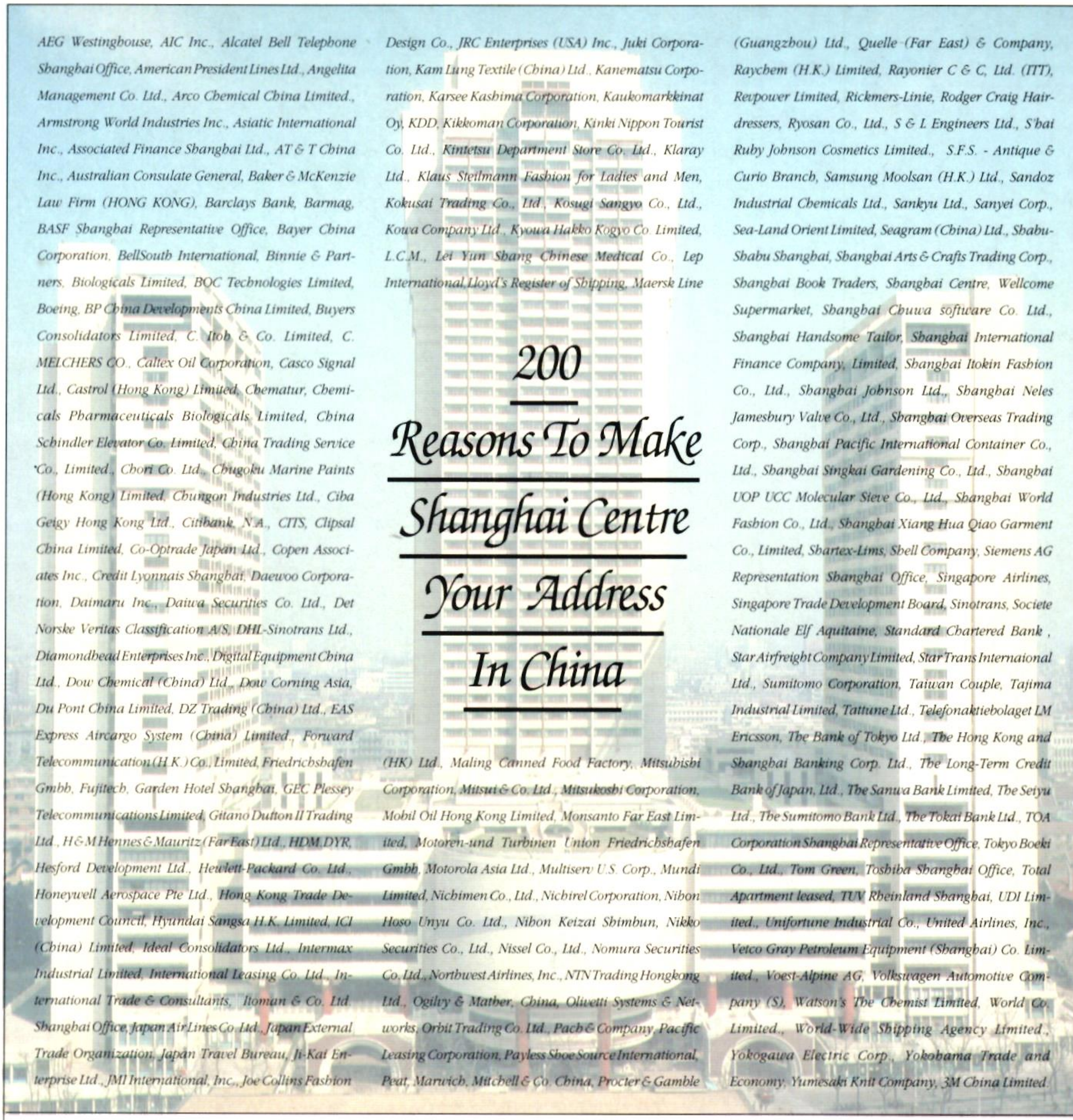
It would be going too far, however, to characterize 1991 as wholly negative in terms of the US-China bilateral relationship. I believe that Secretary of State Baker's November trip to China represented a positive move, an impression supported by discussions I had with US company representatives, Hong Kong business leaders, and senior officials in Beijing and Hong Kong in November. Members of all the groups I met with, particularly the Chinese, felt strongly that resuming a high-level dialogue was the first step in resolving Sino-US bilateral problems. Whether we now see real progress on these issues, however, will depend on Beijing, which must give concrete form to the agreements reached in principle during the Baker visit. For example, resolution of the remaining differences on intellectual property protection, announcement of a firm memorandum of understanding on exports of goods produced by prison labor, and most important, a commitment that China will adhere to international arms control treaties, would all help to ease the pressure in Congress to punish China.

China's actions on these issues may well decide whether US-China relations deteriorate further, or slowly start to improve. At present, relations are tenuous—a dangerous position to be in during an election year, as China policy is bound to be a contentious issue in the presidential campaign. US economic woes will inevitably result in protectionist cries to "Buy American," and China, which has a huge trade surplus with the United States, will surely be singled out in this context. Such an environment will probably force the Administration into taking a very hard line on the trade-related investigations currently underway, as well as in any future rifts that may arise between now and November.

What does all this mean for US businesses with interests in China? The US business leaders with whom I met in China and Hong Kong were generally quite bullish about their Chinese business prospects in 1992, though fully aware of the difficulties in operating in the current political and economic climate. US and Chinese analysts alike forecast vigorous economic growth in China in 1992, and senior Chinese officials privately told me that the PRC would again increase its imports this year, including those from the United States.

However, there was also concern among the American businesspeople with whom I met that the contentiousness and uncertainty surrounding the US-China relationship was placing them at a disadvantage with their European and Japanese competitors, who are stepping up their presence in China. As one American businessman put it, "The Europeans and Japanese are applauding our tough measures against the Chinese . . . all the way to the bank."

Clearly, the United States should work with China to resolve sensitive issues in such areas as arms control, trade, and human rights. But unless we manage this difficult period with care and pragmatism, it could cost us dearly in the growing Chinese market. In the year ahead, the Council will strive to ensure that government and political leaders on both sides of the Pacific are fully informed of the business community's views on all aspects of US-China relations, and that our member companies are fully informed of the potential impact of US and Chinese government activities on their China operations.



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Hunting for China Office Space

Finding the best deals in Beijing, Shanghai, and Guangzhou

John Frisbie and Dan Reardon

Gone are the days when foreign companies resorted to dark, cramped hotel rooms in which to set up their representative offices in China. In the past few years, Beijing, Shanghai, and Guangzhou have all witnessed tremendous growth in construction of office buildings, giving foreign companies an ever-wider range of facilities from which to choose.

Though finding the ideal office space in China still requires some legwork, foreign company representatives will find that their options and—in Beijing, at least—their negotiating strength have never been greater. Nearly all office buildings catering to foreigners now feature such basic amenities as a post office, bank, restaurant, and domestic airline-ticketing service. Other standard services include office cleaning, garage or surface parking, cafeteria and shower facilities for local staff, and international direct-dial (IDD) phone services (although some sites require tenants to make separate telecommunications arrangements with the telephone bureau). Many buildings also house business centers where tenants can use support services and fax machines, if necessary.

Lease terms generally range from one to three years, and deposits of one to six months are standard. Actual rental rates, however, vary greatly from facility to facility, as do the dimensions of available space. In addition, some facilities charge monthly fees for such services as management, electricity, telecommunications, cleaning, and parking on top of the basic rental fee (*see* chart). Prospective tenants must thus carefully compare these factors when selecting a site. Few properties—the SCITE Tower in Beijing is one exception—provide furnished offices, so furniture and equipment costs must also be factored in when assessing total costs.

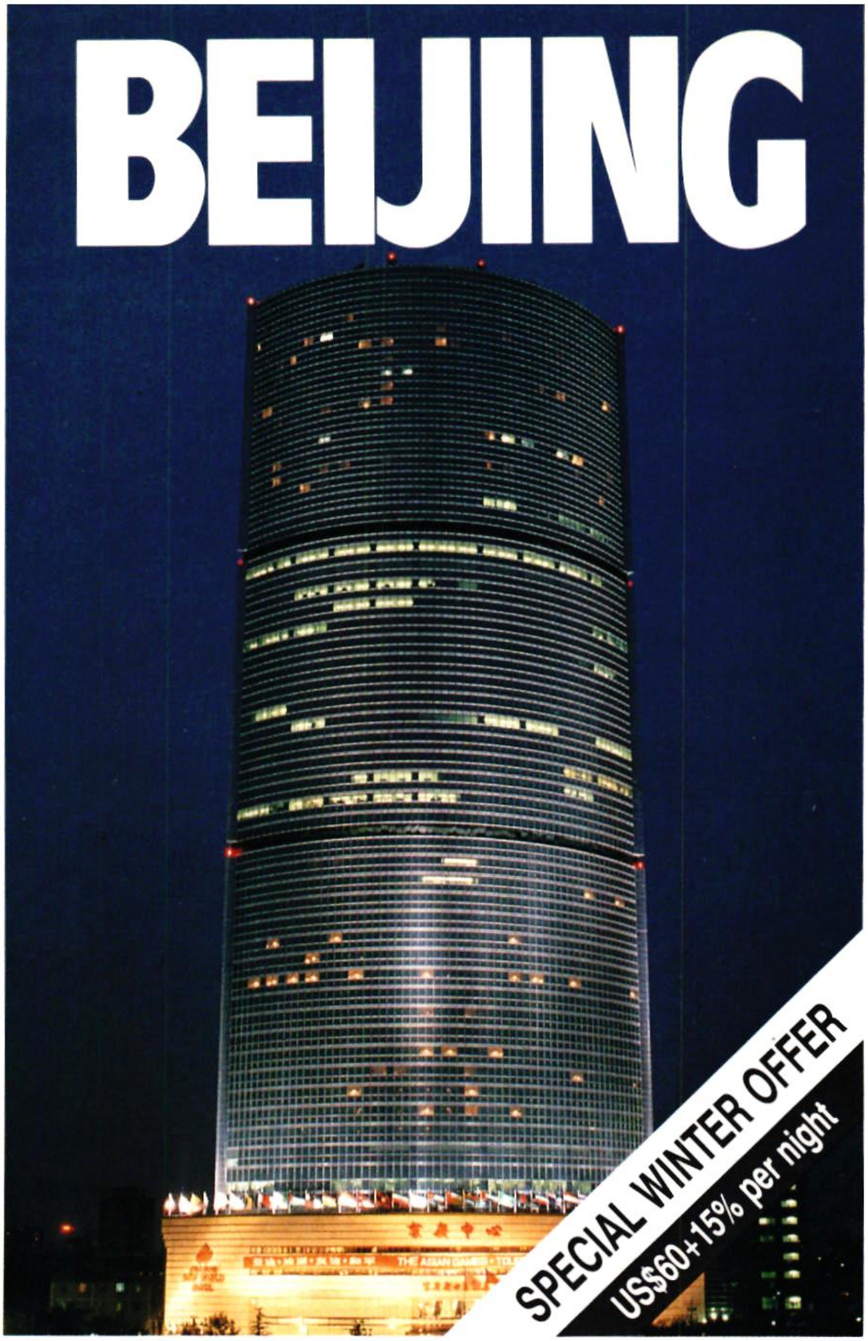
Though finding the ideal office space in China still requires some legwork, foreign company representatives will find that their options and their negotiating strength have never been greater.

John Frisbie is director of the US-China Business Council's Beijing office. Dan Reardon is business manager of The China Business Review.

Variation among properties is most obvious in Beijing, which now offers foreign companies more than a dozen sites from which to choose. Prices are very competitive as five new buildings have opened during the last two years and two more are due to open this year. Top-of-the-line office facilities can be leased for $32-39 per sq m per month, while space at the bottom end of the price scale can be had for as little as $22 sq m per month, or perhaps even lower. Rental rates, contract lengths, early cancellation policies, and customization costs are open to negotiation at most locations.

Companies looking to set up offices in Shanghai or Guangzhou will have fewer sites from which to choose than in Beijing, but should be able to find more than adequate facilities. Shanghai offers foreigners office space in the Jinjiang Club, the Ruijin Building, the Shanghai Centre, the Shanghai International Trade Centre, and the Union Building. Rental rates range from $30-40 sq m per month.

Options decrease as one heads further south, reflecting the smaller number of foreign companies setting up offices in that part of the country. Guangzhou facilities providing office space include the China Hotel Office Tower, the Dongfang Hotel, the Garden Hotel Office Tower, and Guangzhou's newest—and China's tallest—office complex, the GITIC Plaza. Rental rates in Guangzhou range from $23-37 sq m per month.



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Office Space Options

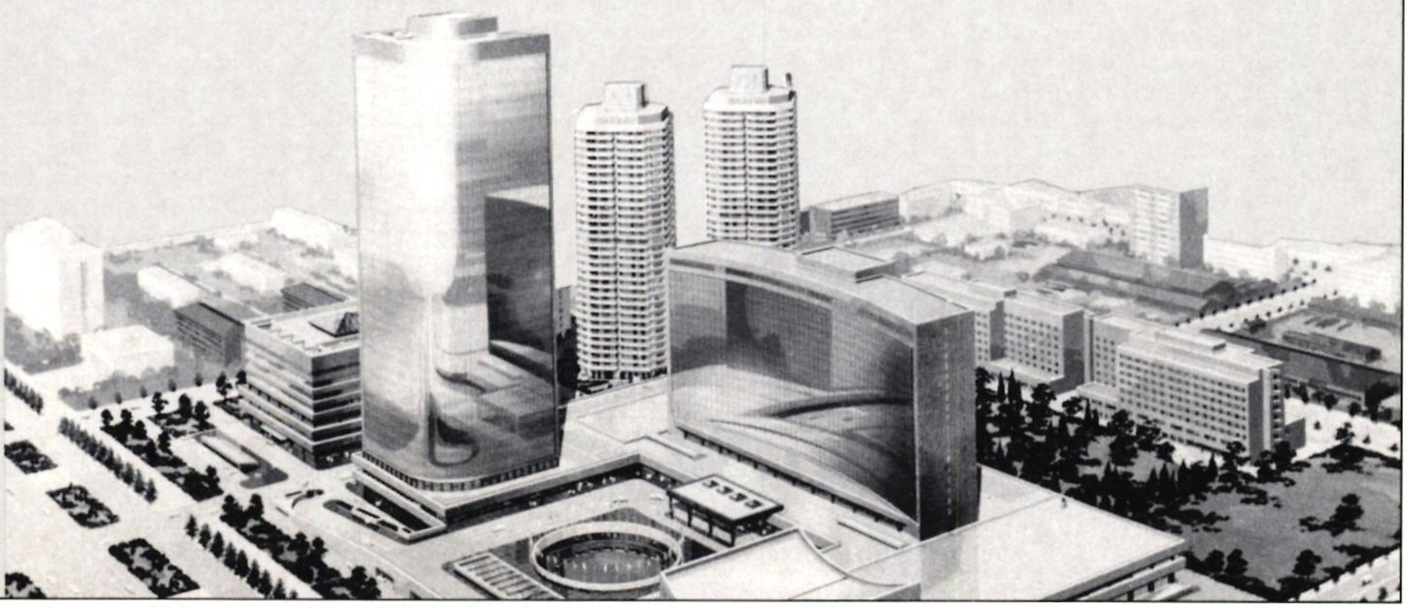
Property (Management company)	Rental Rates: Office Dimensions sq m	Rental Rates: Rate sq m/month	Telecommunications**: Phone line per month	Telecommunications**: Telex line per month	Additional Fees: Electricity per kwh	Additional Fees: Cleaning per month	Additional Fees: Parking per month
BEIJING							
Asia Pacific (privately managed)	63-211	$22	$40 ($400 to install)	$15	$.15	0	$30-50
Beijing Fortune Building (Nomura Bldg. Mgmt. Co.)	52-234	$32	$15	*	¥40	$.50/sq m	$30-40
Beijing Lufthansa Center (Kempinski Hotels)	56-230	$29 (plus $2 mgmt fee)	$33	$33	$1.50/sq m	NA	NA
CITIC Building (CITIC)	84, 120	$24	$10 (¥5,000 deposit)	$10	¥40	$30	$30-70
Changfugong (New Otani Int'l)	40-170	$40	$15 (¥200 to install)	*	¥40	0	$50
China World Trade Center (Shangri-La Int'l)	65-2,500	$32-39	$29	$29	¥10	$.50/sq m	$50-70
Hong Kong/Macau Center (Swissotel)	65-143	$27	$35 ($1,600 deposit)	*	0	$2/sq m	0
Jingguang Centre (New World Hotels Int'l)	60-120	$30 (plus $3 mgmt fee)	$27 (¥5,000 deposit)	0	¥40	0	0
Landmark (Liangmahe) Building (Mandarin Oriental)	55-120	$25	$27	$27	¥10	$70	$0-40
Lido Commercial Center (Holiday Inn)	60, 90	$24 (plus $1.65 mgmt fee)	¥30 (¥5,000 to install)	*	0	¥400	0
SCITE (formerly Noble) Tower (State Science & Technology Commission)	60-300	$31	*	*	0	0	$30
Yanshan (Vista Int'l Mgmt Co)	30, 60, 90	$28-37	*	*	0	0	0

* Tenant must contact the telephone or telex bureau to arrange service.

** All telecommunications charges listed in chart are in addition to long-distance and other usage fees. All phone charges are for direct lines.

Charts compiled by Li Huiping.

Property	Rental Rates		Telecommunications**		Fees		
(Management company)	Office Dimensions sq m	Rate sq m/month	Phone line per month	Telex line per month	Electricity per kwh	Cleaning per month	Parking per month
SHANGHAI							
Jinjiang Club (Jinjiang Group)	22, 25	$30	*	*	0	0	¥100
Ruijin Building (Longhua Travel Co.)	60-222	$39 (plus 5% mgmt fee)	*	*	actual consumption	¥.17-.22/ sq m	$45
Shanghai Centre (Seacliff Ltd)	50, 90, 120	$40 (plus 3% mgmt fee)	$50 ($400-600 to install)	NA	actual consumption + 2%	0	$100
Shanghai Int'l Trade Centre (investor-managed)	67-400	$30 (plus 5% mgmt fee)	*	*	actual consumption	NA	$30-60
Union Building (Jinjiang Group)	60-94	$33	*	*	divided among all users + 5%	¥1.5/sq m	¥220
GUANGZHOU							
China Hotel Office Tower (New World Hotels Int'l)	155-576	$27-30	¥30 (¥1,000 to install)	¥30 (¥1,000 to install)	¥.50	¥.50/sq ft	¥200
Dongfang (Dongfang Hotel)	31, 70	$34-37	*	*	0	0	¥250
GITIC Plaza (Donner Hotel Mgmt Co.)	50-176	$30-32 (plus 10% mgmt fee)	NA (¥5,000 to install)	NA (¥5,000 to install)	NA	NA	NA
Garden Hotel Office Tower (Lee Gardens Int'l Group)	30	$23	*	*	0	0	$50



A Dumping Breakthrough?

A recent DOC ruling holds out prospects for lower dumping margins, but may introduce a new danger—countervailing duties

Jeffrey S. Neeley

A September ruling by the US Department of Commerce (DOC) provides the first real glimmer of hope for successful defense against the onslaught of dumping cases filed against Chinese products in the last two years. The decision in the case of chrome-plated lug nuts belatedly recognizes China's market reforms by accepting actual costs for inputs in China, rather than assigning "surrogate country" costs to these goods. Despite the positive precedent set by DOC in this case, however, the ruling also gives rise to the specter of another problem for China traders—countervailing duty cases against Chinese goods.

Acknowledging Chinese reforms

DOC's surrogate country methodology has been a disaster for Chinese exports. Under the surrogate country approach, DOC searches the world for a country at the same level of economic development to calculate what it believes costs would be in China, if China were a market-economy country. DOC then uses these costs to determine what "fair value" is for Chinese exports to the United States. Results using this approach have been very unpredictable, as the surrogate countries selected in cases involving China have ranged from Paraguay to India (*see The CBR*, July-August 1991, p.34). Because Chinese exporters and US importers do not know in advance which country will be chosen as the surrogate for their industry, they cannot determine whether the DOC will decide that the prices charged for Chinese products in the US market are fair. The lug nuts case goes a long way toward minimizing the guesswork to which defenders of dumping cases against China have had to resort.

In the lug nuts case DOC belatedly recognized China's market reforms by accepting Chinese—rather than surrogate—costs for inputs.

DOC adopted the new methodology in the lug nuts case after answering two questions: whether China is still a non-market economy, and if so, whether the lug nuts sector qualifies as a "bubble of capitalism." A bubble of capitalism is a sector within a centrally-planned economy in which reforms have progressed to the point that *all* prices and costs faced by the producer in that sector are determined by the market. In such cases, DOC may abandon the surrogate country approach and employ normal dumping methodology.

In the lug nuts case, DOC determined that China still constitutes a non-market economy, and furthermore, that the lug nuts sector does not represent a bubble of capitalism. DOC thus could not determine fair value by examining Chinese home-market prices or prices in third countries, the standards in most market-economy dumping cases. Instead, it constructed fair value by using the traditional non-market economy "factors of production" approach, which involves calculating the costs to a Chinese company of manufacturing a given product, and then adding a minimum of 10 percent for general selling and administrative expenses and 8 percent for profit. Rather than turn to a surrogate country to determine all of the costs of production, however, DOC used Chinese prices for the key inputs.

These prices were accepted because DOC found that the costs to the producer of steel and chemicals—two crucial inputs for the manufacture of lug nuts—were determined by market forces. This finding is particularly significant because the steel and chemicals were purchased from government-owned enterprises. In the case of steel, DOC ruled that although the State-owned steel company was required to sell 45 percent of its production at State-controlled prices to buyers named by the government, the remaining production, including that purchased by the lug nut producer, was sold on the open market. For chemicals, DOC found no evidence that the lug-nut producer's suppliers—enterprises owned by local governments—were influenced by the State in making business decisions. Costs for which there was no or little evidence to prove market derivation—such as labor and overhead—were based on prices in Pakistan, the surrogate country selected for the investigation.

DOC's acceptance of Chinese costs for the key inputs resulted in a drastic reduction in the dumping margins in the lug nuts case. In the preliminary determination, in which only surrogate prices were used, DOC found a 66 percent dumping margin. By accepting the Chinese prices in the

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final determination, DOC found a 4 percent dumping margin.

Lessons learned

Given DOC's findings that market forces were at work for some factors but not others in lug nuts production, exporters can be assured that in future cases DOC will carefully examine evidence on each input when determining whether to use actual Chinese costs or surrogate country costs. The key to success in meeting DOC's requirements for accepting Chinese costs will be careful presentation of all evidence proving the market orientation of the producer's input prices.

Though the type of documentation necessary to convince DOC will vary from case to case, several specific pieces of information should always be considered. For instance, comparisons of input costs in China to similar costs in market-economy countries, comparisons of market and State-set costs in China, and a thorough description of the negotiation process between the Chinese producer and his suppliers could all help demonstrate that the costs of inputs are market determined. Manufacturers in labor-intensive industries should also try to document that their employees' wages were determined by market mechanisms, though this will undoubtedly be a hard sell.

DOC's acceptance of Chinese costs resulted in a drastic reduction in the dumping margins assessed against lug nuts.

Out of the frying pan—and into the fire?

While the logic employed in the lug nuts ruling should bring some rationality to dumping cases involving

Setting a Precedent

Jing Wang, an international law consultant with Reed Smith Shaw & McClay in Washington, DC, represented the Chinese manufacturer and exporter in the lug nuts dumping case. He spoke with Editor Pamela Baldinger about his strategy and the importance of the lug nuts case with regard to future Department of Commerce (DOC) findings involving China.

CBR: *How did you present your case to the DOC? Did you employ any special tactics?*

Wang: I think our approach was a little different than most. Typically, the lawyer of the Chinese manufacturer tries to coordinate verification of the information requested by DOC. But from the outset we decided we not only had to ensure that this information was provided in an accurate and timely manner, we also had to argue that China's economy was one in transition, with marked differences between sectors and regions. We argued that for these reasons China should not be viewed simply as a non-market economy. We got the impression that DOC was interested in exploring this "bubble of capitalism" idea; their preliminary findings left open the possibility that the factors of production in the lug nuts sector might be market driven. So we pursued this avenue.

CBR: *How were you able to convince DOC?*

Wang: We provided them documentation showing the arms-length negotiations over inputs—letters, faxes, hand-written records. We also got the suppliers of the inputs to cooperate and document the dual-price system for their products. Initially we had difficulty getting these companies to cooperate. When we went to the ministries overseeing steel and chemical production in Beijing, they were very unhelpful—they said they'd never heard of lug nuts, and the case had nothing to do with them. We then went to the local level, where there was much more cooperation. Once we explained everything to the local authorities and companies involved, they could see their interest in helping us with this case.

CBR: *What impact do you think the lug nuts ruling will have on future dumping cases involving China?*

Wang: It has already set an important precedent by enabling DOC to make similar rulings in the future. Even though DOC found that China is still a non-market economy, it acknowledged that market forces are at work. It is now up to Chinese exporters to show how they started producing—i.e., whether they were established by the State or self-initiated—the prices they pay for their inputs, and how they price their output.

I think this case may serve as a deterrent against the rash of dumping cases against China; there was only one new case filed in the two months after the lug nuts ruling.

CBR: *But the lug nuts case has also opened the door to countervailing duty cases against China. Could the lug nuts ruling be a Pyrrhic victory?*

Wang: It's true some people believe we may have opened a Pandora's box. But my personal view is that there is still room for legal argument on the countervailing duty case. In the lug nuts case, DOC found that China is still a non-market economy—and DOC has long maintained that it is impossible to identify or quantify subsidies in such economies. It would be extremely difficult for DOC to identify a subsidy applied to any one particular exporter or manufacturer in China. It will be very interesting to see how this case turns out.

China, it also introduces a new, potentially even more disruptive element into trade relations—countervailing duty cases. These cases are based on the assumption that foreign-subsidized products have an unfair price advantage over their non-subsidized US competitors. Investigation of the existence and extent of subsidization is carried out by the DOC's International Trade Administration. Unlike dumping cases, however, in which all cases are referred to the US International Trade Commission (ITC) to determine whether the exports in question are causing or threatening material injury to a US industry, only signatories to the Subsidies Code of the General Agreement on Tariffs and Trade (GATT) are entitled to an injury finding in countervailing duty cases. Therefore, countries like China that are not signatories to the code are almost certain to have duties assessed against them should DOC find that their products are subsidized—even if the goods have little or no effect on the relevant US industry.

The US subsidy/countervailing duty law has not been applied to non-market economies since a 1986 ruling by the US Court of Appeals for the Federal Circuit, which upheld a DOC decision to reject countervailing duty cases against non-market economies. The lug nuts case, however, may undercut much of the rationale of that ruling.

The 1986 decision was based on the premise that it is impossible to establish what constitutes a "subsidy" in an economy in which the State controls prices and production through central planning. The lug nuts ruling, however, implicitly recognizes that central planning no longer dominates all sectors of the Chinese economy. DOC may thus believe that it can sort out what is—and is not—a subsidy in China.

DOC was well aware that in the lug nuts case it was undercutting its previous stance against conducting countervailing duty cases against non-market economies. Shortly after the final ruling, DOC Assistant Secretary for Import Administration Eric Garfinkel told a leading US lug nut producer "We are willing to consider a countervailing duty petition which alleges that subsidies on these (steel and chemical) inputs benefit lug nuts." On October 17,

The countervailing duty case could have disastrous effects on Chinese exporters who use the swap centers for currency conversion.

1991, a US company that had earlier filed a dumping case against Chinese ceiling and oscillating fans became the first petitioner to follow up on Garfinkel's invitation.

The bulk of the alleged subsidies in the electric fans case derive from China's multiple exchange rate/currency retention programs. According to the petitioner, the difference between the "swap center" exchange rate and the administered official rate confers a subsidy on exporters who receive the swap center rate. The petitioner alleges that access to the centers is limited to firms with foreign investment and to exporting enterprises that earn foreign currency. The amount of foreign exchange that can be retained—and hence the level of the benefit—also varies among enterprises.

On November 6, 1991, DOC instituted a countervailing duty investigation against Chinese fans based on the October petition. If DOC accepts all of the allegations in the petition, countervailing duties of 26-52 percent could be imposed on US imports of these products. More importantly, the precedent set by the case could have disastrous effects on exporters who use the swap centers for currency conversion. Barring any extensions, DOC must issue a preliminary determination by January 10, 1992; the final determination will be due 75 days later.

Until the outcome of the countervailing duty case is certain, it would appear that the lug nuts ruling should increase the predictability of the methodology DOC employs in dumping cases involving China, and thus help Chinese exporters defend themselves against such charges. But it may yet open the door to a slew of subsidy allegations against a broad array of Chinese products in the future. 完

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The Making of China Policy Since Tiananmen

Can Congress and the Bush Administration reach a new consensus?

Kerry Dumbaugh

The weeks following China's 1989 Tiananmen Square crackdown ended a decade of consensus on China policy in the United States. For the past two and one-half years US policy on China has been characterized by confrontation between the legislative and executive branches, not just over the issues involved, but over the respective roles of each branch in setting US policy. The Bush Administration has accused Congress of being obstructionist and partisan on China issues, while Congress has criticized the President for ignoring congressional initiatives and prematurely giving away important US leverage without receiving concessions in return.

Some of the blame for the new contentiousness in China policy can be laid at the door of the US Constitution, which provides overlapping institutional mandates to the two branches of government over foreign policy decisions. The executive branch has comprehensive jurisdiction over foreign policy issues, with the President retaining broad powers to respond swiftly and unilaterally to unfolding international events. As the US government body that actually formulates and conducts foreign policy, the executive branch is usually motivated by pragmatism and the pursuit of broad US interests in its foreign policy dealings. President Bush, who is confident of his judgments in the foreign policy arena, has consistently used these comprehensive constitutional powers, particularly on China issues.

Congressional jurisdiction, on the other hand, is more specifically defined. When considering foreign policy issues, Congress seeks to balance broader US foreign policy goals with the domestic and international concerns of the constituencies of individual members. For the most part, Congress accommodates the President's constitutional prerogative to take the lead in foreign policy—provided that it retains the right to oppose, alter, or restrict presidential initiatives. Although Congress lacks the constitutional authority to participate formally in the negotiation of foreign policy issues with foreign powers, it does have the ability to influence the policy process, particularly through its control of government funding.

Operating under these very different mandates, Congress and the Bush Administration have clashed repeatedly over the conduct of US China policy in the last two years. Although at first glance these clashes may appear intermittent and without pattern, a closer examination of the policy process reveals trends which may shed light on future decisions. Generally speaking, this period may be divided into three phases, characterized by the breakdown of consensus, policy impasse, and emerging alternatives, respectively.

Despite evidence that criticism—and support—for the President's China policy came from members of both political parties, accusations of political partisanship contributed to the increasing rancor of the China policy debate.

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Phase I: Loss of consensus, June 1989-March 1990

In the immediate aftermath of the Tiananmen Square crackdown, President Bush moved quickly to seize the initiative on China policy decisions. Within a day of the violent Tiananmen suppression, and again two weeks later, the President announced a series of sanctions to protest Beijing's actions. These included the suspension of defense equipment sales to China, visits and exchanges between military personnel, high-level visits between US and Chinese officials, and new loans by multilateral development banks. Initially, these actions were commended by many in Congress. By late June, however, this support had already begun to unravel, due to a number of factors.

First, despite the swift sanctions, presidential rhetoric about China's actions was mild. Shortly after the Tiananmen crackdown, Bush Administration officials began to temper negative comments about Beijing's actions with positive references about China's continuing importance to US interests. Many in Congress and elsewhere were disturbed by their perception that the Administration lacked fervor in protesting China's repressive policies. Chinese leaders' heated defense of their actions in Tiananmen Square did nothing to ease congressional concerns about the potential effectiveness of the President's actions. These concerns grew with widespread press attention to human rights abuses in China and the activism of human rights organizations and Chinese students in the United States. Members of Congress found themselves under increasing public pressure to take a stronger stance on China-related issues.

US domestic politics may also be viewed as a factor contributing to the breakdown of consensus. The President's close association with China policy prompted allegations that congressional Democrats were using the China issue as a political tool to undermine the President and his Republican supporters. Despite evidence that criticism—and support—for the President's China policy came from members of both political parties, accusations of political partisanship contributed to the increasing rancor of the China policy debate.

In an attempt to apply more US leverage on China without unduly jeopardizing US interests, Congress enacted a series of bills from June-December 1989. Legislative provisions concerning China were included in the State Department Authorization bill (H.R. 1487); the Appropriations bill for the departments of Commerce, Justice, State, and the judiciary branch (H.R. 2991); the International Development and Finance Act (H.R. 2494); the Foreign Operations Appropriations bill (H.R. 3743); and the Emergency Chinese Immigration Relief Act (H.R. 2712), among others.

Having exhausted other legislative avenues by 1990, Congress looked to MFN as the key to expanding congressional influence over the general direction of US China policy.

These China-related provisions, however, were often pre-empted or overturned by presidential action. The most egregious example involved the immigration bill, which would have made it possible for Chinese students studying in the United States to extend their stays for up to four years rather than have to return to possible punishment in China. The President vetoed this bill, but took similar measures shortly afterward by Executive Order. To many in Congress the message was clear: the President was willing to prevent legitimate congressional initiatives against which he had no substantive objections, simply in order to keep the upper hand in the formulation of foreign policy.

At the same time as he appeared to be foiling Congress' desire to act on China policy, the President engaged in selective enforcement of the sanctions he himself had imposed. Having announced the prohibition of US military-related sales to China on June 5, 1989, the President waived the prohibition in July 1989 for the sale of Boeing jets and again in December 1989 for the export of US communications satellites to China. In the latter case, the President also waived a legislative restriction on satellite exports which Congress had imposed in several enacted bills. The President's June 20 prohibition on high-level contact with China also seemed permeable; by December 18, 1989, National Security Advisor Brent Scowcroft and Deputy Secretary of State Lawrence Eagleburger had both made trips to Beijing, with Scowcroft first visiting only one month after the crackdown.

Though these actions made clear that President Bush could successfully dominate US policy decisions on China, he did so at a cost. By early 1990 the President had alienated many in Congress by appearing to prevent the legislative branch from serving as an equal partner in the policy process. Moreover, he had eroded the credibility of his position on China by having failed to markedly influence Beijing's policy direction.

Phase II: Impasse, March 1990-March 1991

The increasingly contentious dialogue between the executive and legislative branches on China policy reached a stalemate by the beginning of 1990. Throughout the year, the White House, Congress, and Beijing appeared tucked into their respective positions and preoccupied with the dramatic developments in the Soviet Union and the Persian Gulf. The result was an effective impasse in US policy on China, during which matters neither deteriorated nor improved.

By the beginning of 1990, the dominance which the executive branch had established on China matters led a frustrated Congress to turn to its chief remaining weapon for influencing the policy process—approval of China's Most Favored Nation (MFN) status (*see The CBR*, July-August 1991, p. 12). Renewal of MFN does not require specific congressional approval, but can be blocked by a joint resolution of disapproval by Congress within a specified time frame.

Significantly, the President's 1989 MFN request for China, coinciding almost precisely with Beijing's Tiananmen Square crackdown, received minimal congressional attention. But having exhausted other legislative avenues by 1990, many members of Congress looked to the annual MFN request as the key to expanding congressional influence over the general direction of US China policy.

Throughout the year and into 1991, Washington's struggle over

China policy was debated almost exclusively on the question of China's MFN status. Congress concentrated on legislation which would have made China's eligibility to receive MFN contingent on a number of new conditions requiring presidential certification. Nearly all of the proposed conditions involved human rights issues, such as the release of political prisoners, recognition of political freedoms, and elimination of religious persecution.

The President contributed significantly to the impasse. Confident in his ability to dominate the process, the President's commitment to his policy direction on China in 1990 appeared unshakeable. This strong stand helped provide a larger rhetorical and legislative stage for Congress on the MFN issue. The President's repeated assertions that he would veto any legislation denying or placing further conditions on China's MFN eligibility made any potential congressional action on conditionality appear more symbolic than substantive. The near-certainty of a veto probably contributed to the lopsided votes in the House of Representatives in favor of measures to deny China's MFN status (H.J.Res. 647, passed by a vote of 247-174) and to condition China's future eligibility (H.R. 4939, passed by a vote of 384-30). Moreover, the House acted on these bills on October 18, too late in the session for the Senate to act. Thus, despite eight months of heated debate on the MFN issue, by the end of 1990 no legislation had been sent to the President.

Other factors also contributed to the policy impasse. By late summer, the United States was preoccupied with Iraq's invasion of Kuwait. The impending Gulf War distracted the attention of the US press and the policy community from other contentious foreign policy issues. In addition, China's acquiescence in critical United Nations votes on the Persian Gulf elevated China's immediate importance to US foreign policy objectives and helped mute overt US criticism of China's domestic policies. Finally, economic and political troubles in the Soviet Union, including declarations of sovereignty and independence by some Soviet republics, may have contributed to a sense in the United States that Beijing was becoming increasingly isolated politically and would eventually reassess its repressive policies.

The Bush Administration assessed the Baker visit's results with a cautious and somewhat cynical pragmatism that had been missing from earlier Administration actions.

Phase III: Broader debate, less rancor, April 1991-present

By the spring of 1991 the Gulf War had ended, and US attention focused once again on China and other important foreign policy issues. But the character of the US policy debate on China appeared to be changing, leading many to speculate that perhaps the stalemate had ended. Congress began to expand on and diversify its approach to issues involving China, while the Bush Administration appeared to take a tougher line on a number of new issues arising in the bilateral relationship.

As in 1990, Congress again reached for legislation seeking to condition China's MFN status (H.R. 2212) as its primary vehicle to influence US China policy in 1991. But the conditions debated differed in important respects from those in the previous year's legislation. In addition to general human rights-related measures, the conditions in 1991 dealt with nuclear non-proliferation and missile sales issues, sterilization programs, prison labor policies, and the accession of Taiwan to the General Agreement on Tariffs and Trade (GATT), among others. The substantive nature of these new issues encouraged members of Congress to launch legislative efforts separate from the MFN legislation to ensure their passage. These efforts included bills to strengthen the US stand on nuclear non-proliferation, address the export of Chinese products made with forced labor, and legislate specific US policies toward Hong Kong.

Concurrent with this new multidimensional congressional effort, the Bush Administration also took a tougher stance toward China in 1991. For instance, the President authorized the designation of China under the 301 and Special 301 provisions of the Trade Act for barriers to market access and violation of US intellectual property rights; US Customs officials seized Chinese textile products suspected of having been transshipped illegally to the United States or in violation of quota limits; and the President stated that the United States would drop its hands-off approach to Taiwan's application for GATT membership.

Since the introduction of these new initiatives, the two branches appear to have resumed a tentative dialogue on China policy. The President generally has seemed more sensitive to congressional views, and appears to have linked the Administration's new initiatives directly to congressional concerns, as evidenced in a July 1991 exchange of letters with some members of Congress. The renewed dialogue has added a new dimension to the policy process, prompting many observers to wonder whether a new US consensus on China policy might be possible.

Moving the bilateral relationship forward

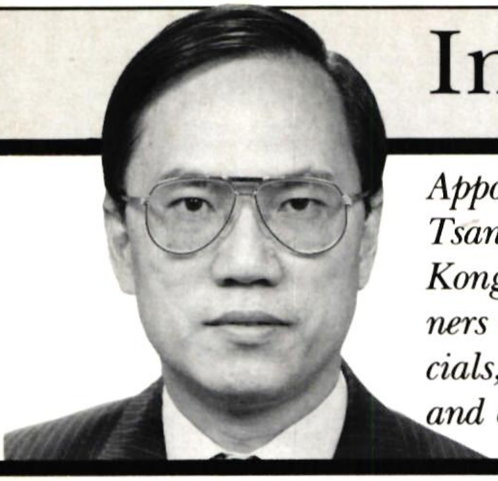
Careful observation of US policy toward China since Tiananmen reveals that contention in the policy process has not been the result of differing views over long-term US policy goals; there remains widespread sentiment within Congress and throughout the US policy community that close relations with a stable, reforming China will best serve US interests. But views have differed—sometimes sharply—over the means of achieving these goals and the role that Congress should play in shaping them.

With this in mind, a renewed US consensus over the future course of policy toward China will require flexibility, sensitivity, and realism from both the legislative and executive branches of government. Having established himself as the primary actor in crafting US policy decisions on China, President Bush bears the greater burden. The decisive actions that the Administration has taken over the past year—on trade, human rights, and non-proliferation issues—have helped reduce tensions between the White House and Congress and provide some breathing room for both to work toward a more cooperative approach on the future course of US China policy. However, the President must be willing to follow through with promised consequences if US concerns on these contentious issues are not met, if he is to re-establish congressional trust in the Administration's objectives and reaffirm Congress's role in the policy process.

The consequences of Secretary of State Baker's November 1991 visit to China may serve as a critical test for this new, cooperative approach. Preliminary reports on the Secretary's trip have been mixed: on the positive side, the Administration was open and direct about the nature of the Baker visit, raised the right issues with Chinese leaders, and assessed the visit's results with a cautious and somewhat cynical pragmatism that had been missing from earlier Administration actions. On the negative side, the visit produced few immediate concessions substantive enough to demonstrate to critics within Congress Beijing's interest in, and commitment to, its relations with the United States.

The two branches appear to have resumed a tentative dialogue on China policy, prompting many observers to wonder whether a new US consensus on China policy might be possible.

For its part, Congress also has important interests in working toward a more cooperative US approach on China. To avoid the appearance of partisanship and obstructionism, congressional leaders may wish to concentrate on a legislative agenda for China which emphasizes near-term US objectives on specific issues—such as non-proliferation—with the longer-term US policy goals of reducing bilateral tensions and re-establishing beneficial relations. Members of Congress who remain deeply concerned about the repressiveness of China's current regime and wish to maximize US influence may find their purposes best served best by supporting a frank US dialogue with Beijing, while continuing to apply strong legislative pressure for significant changes on specific contentious issues. 完



Interview

Appointed Hong Kong Director General of Trade in August, Donald Tsang, a career civil servant, has taken on the task of safeguarding Hong Kong's interests as relations between the territory's two main trading partners deteriorate. In Washington last fall to meet with key US trade officials, Tsang spoke with Editor Pamela Baldinger about MFN, GATT, and other challenges to Hong Kong's trade performance.

Caught in the Crossfire

Q *With whom have you met in Washington?*

A The purpose of my trip is to touch base with US officials involved in bilateral and multilateral trade activities, either here or in Geneva. So I've been visiting officials in the departments of State and Commerce and at the office of the US Trade Representative (USTR). I've also met a number of people representing Hong Kong's interests here, like the major importers. Today I went up to Capitol Hill, and met senators Roth and Shelby and congressmen Gibbons and Archer. They were all very sympathetic to Hong Kong's cause. I also plan to meet with the US Customs Service.

Q *What did you talk about on the Hill?*

A I talked about two major issues. One was renewal of Most Favored Nation (MFN) trading status for China, and the other was also a China-related issue, the ongoing 301 actions against China. Both of these are essentially bilateral issues, but the fallout could be horrendous for Hong Kong. For that reason we have expressed our concern. On the MFN side, I got a readout from the legislators that they do not know how things might proceed beyond a House-Senate conference to come up with a single MFN bill. The natural course of events would be to send the bill to the President, who we understand will veto it, and then Congress will vote on the override of that veto. The timing of all of this is unclear, as the Congress has other preoccupations.

"It seems to me that a 'bash China' syndrome has emerged in the United States."

The other issue I discussed is the 301 investigation of China's trade practices. I can see the arguments on both sides. As a free trader, I can appreciate the American sentiment that China should open up her markets more. But it's also important to look at the issue from the point of view of a developing country. They have problems making radical changes overnight, as such changes have enormous implications for them. What I'm worried about is the Chinese reaction to the rhetoric that comes out of the American side in regard to the 301 investigation. The fact of the matter is that 60 percent of China's trade with the United States comes through Hong Kong. So, we don't want to be hurt in the crossfire.

Q *What can Hong Kong do?*

A We are caught in the middle. It's not a question of what we can or can't do. What we want is for people to understand the possible consequences of their actions. This is all we ask. We are not able to defend China because it would be unwelcome in the United States. Nor do we wish to defend the American initiative—that would be totally misunderstood by the Chinese. What we want is to ensure that if it all boils down to retaliatory measures, that Hong Kong interests will not be unintentionally harmed.

Q *Is your message getting through in Washington?*

A I'm a newcomer to this job, but it seems to me that a "bash China" syndrome has emerged in the United States. With the changes and reforms in Russia, attention has focused on China. The prison labor issue is a case in point. Again, I can see the arguments on both sides. We try to do what we can to help, but this is the sort of thing where Hong Kong can be caught in the crossfire.

Q *What are your concerns about the re-opening of the antidumping case against synthetic sweaters from Hong Kong?*

A This case has generated so much attention—and resentment—in Hong Kong, that it's something that we, as the Trade Department, have had to address. The issue is seen by Hong Kong manufacturers as an unadulterated form of protectionism. In this trade, Hong Kong occupies a fraction of the US market. We all know that Hong Kong manufacturers receive absolutely no subsidies from the Hong Kong government. It is well nigh impossible for any of them to dump in the United

States—there'd be no purpose in it.

The problem with cases like this is that they introduce great uncertainty into trade. The large manufacturers are able to respond to these investigations comfortably and prove beyond a doubt that they are not dumping. Unfortunately, the small ones are in serious trouble, because they cannot afford the legal costs to respond to the dumping charges—it costs at least $150,000 for a company to clear its name.

Q *What role is the Hong Kong government playing in this case?*

A We have found some structural defects in the way the case was originally conducted, and we have tried to address these defects in bilateral talks. We are not entirely happy with the outcome of the talks, so we may ask a GATT panel to investigate the case.

Q *Some months ago the Hong Kong Exporter's Association established a Fair Trade Fund to solicit private-sector donations to fight dumping cases. It was then proposed that the government take over adminstration of this fund. What is the status of the Fair Trade Fund?*

A The government must not forget that it is a signatory to the antidumping code of the GATT. For that reason, I do not think it is proper for the Hong Kong government to help individual firms counter properly instituted investigations. I'm not saying that the present proceedings are entirely proper. What I am saying is, it would be perceived as wrong by others if we tried to counter antidumping activities.

It is difficult for Hong Kong people to accept that they can be accused of dumping anywhere, particularly in the United States, a major market. But I think it would be difficult for the Hong Kong legislature to sanction use of taxpayer money for subsidizing a fund of this sort.

Q *So you don't see the government raising money to help fight such charges?*

A Not for antidumping cases. *[Editor's note: In late December the government-mandated Hong Kong Trade Development Council contributed $1.3 million to the fund.]*

Q *What concerns have the US Customs raids on Chinese textile companies in the United States raised in Hong Kong?*

A I'm not concerned at all. If there is any evidence of them shipping illegally through Hong Kong, we will certainly try to find out. We support the US initiative to punish illegal transshipment through Hong Kong.

Q *What is the Hong Kong government doing to prevent illegal transshipment through the territory?*

A We are applying all the resources we have at our disposal. We have increased the volume of checks on textile goods crossing the border; for firms that we've blacklisted, we do individual shipment checks. We do what we can. Our efforts have been recognized by the US Customs Service as the best that can be given by any government.

Q *Have any companies been prosecuted?*

A Oh yes. Not only do we prosecute them, we take away their quotas.

Q *What are your goals for your term as Hong Kong Director General of Trade?*

A My goals are to see that healthy growth in export trade continues and that the GATT Uruguay Round is brought to a satisfactory conclusion. I would also like to see understanding in the United States that some of the measures it has adopted are not productive. In the sweater dumping case, for example, small Hong Kong companies may be forced out of business, or at least out of this line of trade. Their quotas will go to the larger companies, who will continue to export. Although the total amount of exports may stay the same, they will come from a handful of suppliers, rather than from 300. Prices might be less competitive than before. At the end of the day, who will win? The lawyers. And who will pay? American consumers and small manufacturers in Hong Kong.

Sparking the Electronics Industry

The technological gap between China and the industrialized countries is still widening

Denis Fred Simon

Since the arrival of Alvin Toffler's *The Third Wave* into China in the early 1980s, China's top leaders—regardless of political inclination—have sought to promote the development of the country's electronics industry. In their desire to take part in the technological revolution, Chinese leaders have steadily increased funding for the modernization of both research and development and manufacturing capabilities for semiconductors and integrated circuits, the basic building blocks of the global electronics industry. They realize that if China is to achieve a strong competitive position in the world economy, it will have to establish a strong foundation in a range of informatics-linked technologies.

Current Chinese policy emphasizes foreign investment and technology import as the primary mechanisms for both upgrading manufacturing capabilities and increasing local content. While export promotion is encouraged as a means of earning hard currency to pay for such purchases, Chinese leaders stress that they do not want to import components simply to export them again in low value-added processed goods; the thrust of the strategy is to improve domestic capacity through import substitution. The success of American "smart weapons" in the Gulf War has further strengthened the Chinese government's determination to make high technology in general, and microelectronics in particular, a serious national priority.

Past successes . . .

In both quantitative and qualitative terms, China's electronics industry has shown marked improvement since the mid- to late 1980s. Total output value in 1990 was ¥69.1 billion, a 7 percent increase over 1989. During the first five months of 1991, electronics output totalled ¥35.4 billion, an increase of about 35 percent over the same period the year before. Growth in computer production was particularly strong in 1991, with overall output exceeding 1990 levels by about 57 percent. Microcomputer production during the first nine months of 1991 reached 58,209 units, up 88 percent from the same period in 1990.

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Electronics' role in foreign trade also expanded in the late 1980s. In 1985, electronics accounted for only 6 percent of total exports, but by 1990 its share had climbed to 18 percent. Consumer electronics, which accounted for 57.9 percent of total electronics production in 1990, made up the bulk of these exports. Computers, which accounted for 12.5 percent of total output, and components (29.6 percent of total output) were sold primarily on the domestic market.

China also made considerable improvements in product quality during the past six years. In 1985, for example, only 25 percent of electronic products were classified by the State Planning Commission as "high quality;" by 1990, the number had increased to 35 percent. The improvements in quality were achieved concurrently with increases in local content, particularly in consumer electronic products, such as televisions.

The industry has also continued to make progress in the area of structural reform, creating a large number of industrial conglomerates that link together research and development, production, and marketing and sales (*see The CBR*, July-August 1988, p.27). Perhaps the best example of such a conglomerate is the Great Wall Computer Group, which is now China's premier producer of personal computers and related peripherals. All of these improvements can be attributed in part to increases in funding from State, local, and foreign sources, particularly in the area of technical renovation. In 1990, over ¥40 billion was invested in upgrading electronics-manufacturing facilities, accounting for 6.3 percent of all funds invested in Chinese industry that year.

. . . and failures

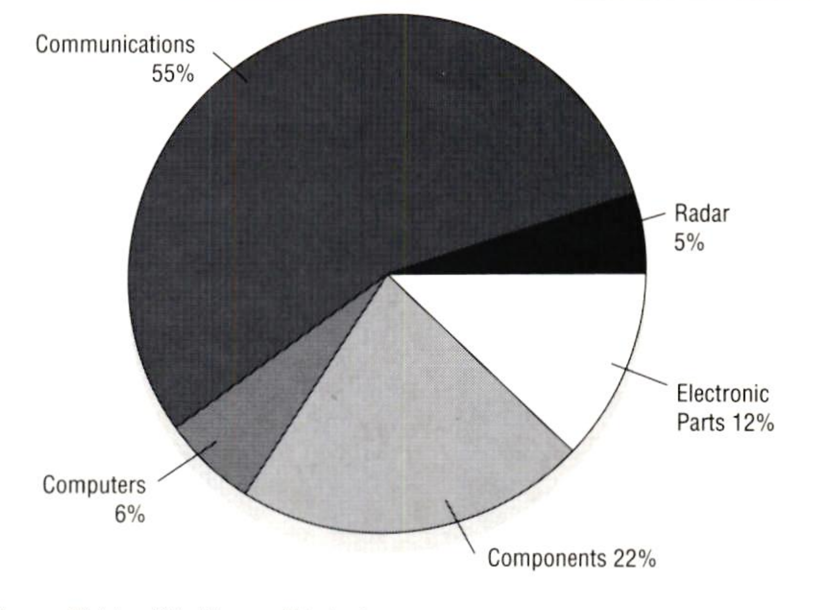
Despite these gains, the gap between China and the rest of the world in electronics continues to widen. This is primarily due to inefficient and duplicate production, aging equipment, low labor productivity, and shortages of foreign exchange, parts, and components.

Duplication of production stems primarily from decentralization of the industry in the mid-late 1980s. As authority devolved from the central to the local levels, each province strove to create its own electronics sector. The result has been the creation of numerous factories—few of which are able to attain economies of scale—producing the same goods. For example, there are about 30 factories producing integrated circuits in China, but only one is currently able to produce more than 10 million units per year, well below the standard capacity of factories in the West and Japan. The proliferation of factories, moreover, has led to excessive importation of certain types of foreign equipment, wasting scarce foreign exchange. In the television sector, for instance, China has imported 113 color-television lines, many of which cannot be used either because China cannot produce—or afford to import—the components and parts needed to run them.

The electronics industry suffers from inefficient and duplicate production, aging equipment, low labor productivity, and shortages of foreign exchange, parts, and components.

Structural obstacles have also hampered performance. The contract responsibility system has created a tendency among managers to concentrate on short-term revenues rather than long-term gains in productivity and the introduction of new products. Accordingly, many managers are unwilling to take their present earnings and invest in new technology. The fact that demand usually exceeds supply for most better-quality consumer products in China exacerbates this situation, as managers need only increase capacity to increase sales. Even if managers have the foresight to attempt to upgrade their facilities and increase quality, the weak technical foundation of most enterprises makes it difficult for them to embark upon even the most modest research and development efforts. This problem has also been evident with respect to imported technologies; though their applica-

Sectoral Composition of China's Electronics Industry, 1989



Source: *Ministry of Machinery and Electronics*

The central government is looking to consolidate and focus its resources by concentrating production in key enterprises.

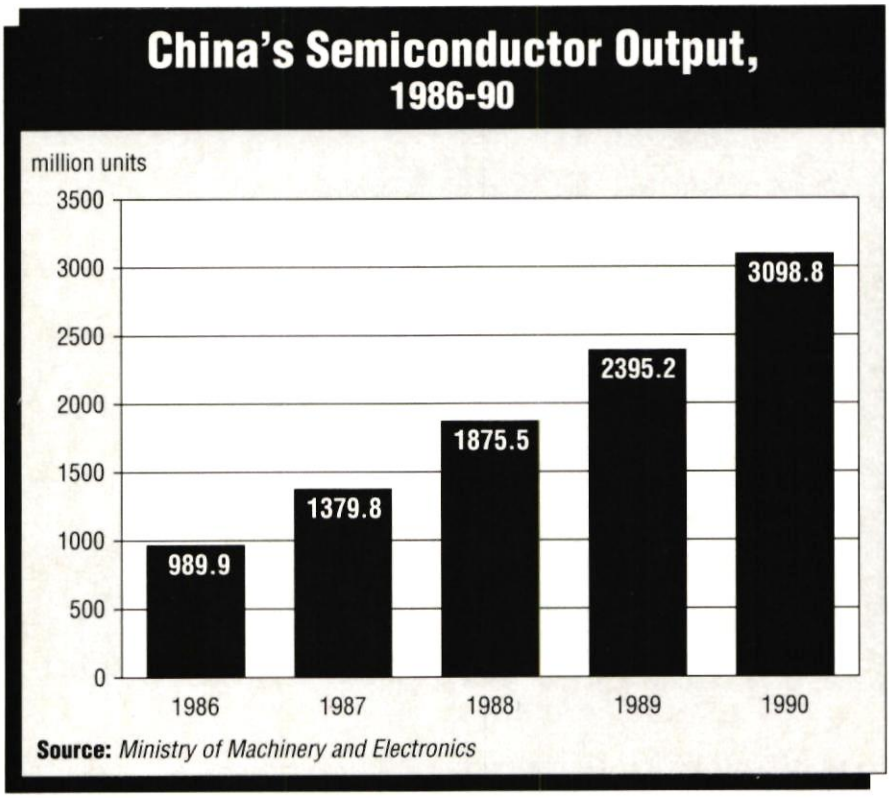
tion has increased production, there has been very little indigenization of the imported technologies, let alone new technical innovations.

The behavior of managers is also constrained by government bureaucrats at both the national and local levels, for whom the electronics industry is too strategically important to be granted too much autonomy. Through their control over foreign exchange, tax policies, and allocation of inputs, bureaucrats constantly intervene in the operations of enterprises.

Understanding of these problems has increased with the ascension of Jiang Zemin, former minister of the Ministry of Electronics Industry, and Li Peng, former head of the State Council Leading Group for Electronics and Computers, to key decisionmaking positions in Beijing. To help overcome structural impediments, the central government is looking to consolidate and focus its resources by creating production "pockets" around the country, which will concentrate production in key enterprises (*see* p. 30). One of Beijing's top priorities for the foreseeable future will be to boost output and quality of critical components.

Overcoming component shortages

In 1989, China used some 350 million-400 million integrated circuits for production of various electronics goods. Domestic production, however, totalled only 114 million, so the rest had to be imported. This dependence has limited growth of the electronics industry not only by absorbing large amounts of foreign exchange that otherwise could be used for technical transformation, but by slowing innovation, as the Chinese find adapting foreign technologies very difficult.



Quantitatively, China has achieved some success in production of semiconductors, manufacturing approximately 3.1 billion semiconductor chips (worth $1.06 billion) in 1990, an increase of 24 percent over 1989 output (*see* graph). Production of integrated circuits, however, totalled 96.58 million pieces, a decrease of nearly 16 percent from the previous year (*see* p. 26). This decrease is probably a one-time phenomenon, and does not reflect improvements in yields (the proportion of circuits that are actually useable) achieved during the same period.

Qualitatively, however, deep-seeded problems plague this sector, with the result that China's semiconductor industry is at least 5-10 years behind the world leaders. The chief problems are China's obsolete manufacturing facilities and inability to utilize at the factory level technological advances made in the lab. These factors have fostered continued dependence on foreign-made components in most areas. China's rapidly growing microcomputer industry, for example, still requires imports to meet over 60 percent of its demand for semiconductors and integrated circuits.

To help overcome this dependence, China plans to establish two major semiconductor bases during the Eighth Five-Year Plan (FYP, 1991-95). One of the bases will be in Beijing and the other will be in Jiangsu Province, spread among Nanjing, Wuxi, and Shanghai. The ultimate goal is to build about 12 backbone enterprises in the zones. Among the 12 will be Sino-foreign joint ventures, and all will have advanced technology and large-scale manufacturing capability. By the end of the plan, integrated-circuit production is also to rise significantly, to 400 million-600 million circuits per year. Even at this level, however, China will still count on imports to fulfill one-half to two-thirds of demand.

Attracting foreign investment

Chinese officials are counting on a number of foreign investment projects to propel the components subsector during the next five years. The most ambitious of these involves Motorola Inc., which has agreed to set up an integrated circuit-manufacturing facility in Tianjin. The Motorola project, a wholly foreign-owned enterprise, involves the establishment of an assembly and manufacturing facility for multi-purpose integrated circuits. Motorola hopes to use Tianjin as its main operating

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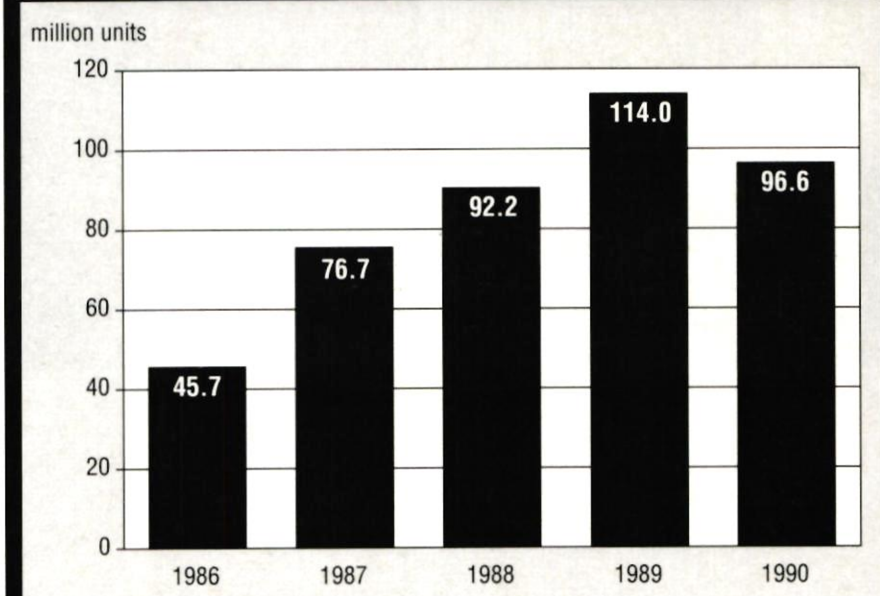
Another project of considerable importance involves NEC, which will invest in a $62 million joint venture with Beijing's Shoudu Iron and Steel Plant to produce integrated circuits in the 2-3 micron range. The Shoudu Iron and Steel Co. will hold 60 percent of the equity while NEC will hold the other 40 percent. The plant will have an annual capacity of 50 million circuits, and will supply another NEC joint venture in Tianjin that produces program-controlled telephone exchanges. The NEC joint venture is particularly significant as it represents the first Japanese investment in the electronics sector outside of television and home appliance production.

Additional projects for integrated-circuit production include a fabrication line for telecommunications switching in Wuxi, using technology transferred from Siemens. This project will nearly double the annual capacity of the Jiangnan #742 Factory—currently China's largest integrated-circuit producer—to about 100 million circuits. Philips of Holland also plans to establish an integrated-circuit production project, a joint venture with the Shanghai #7 Radio Factory. The venture will manufacture five-inch wafers for television and audio use, and will have an annual capacity of 70 million circuits. These two projects will join an already up-and-running integrated circuit-producing venture in Shanghai. This project, known as Beiling, involves ITT Belgium, and produces circuits for digital telecommunications switching devices. Another important foreign investment in the integrated circuit area is a project in Shanghai's Caohejing High Technology Zone involving technology from France's Air Liquid. The main objective of this project is to produce super high-purity gases for use in integrated-circuit manufacturing. The venture is part of a larger effort to boost Caohejing's Microelectronics Research and Development Center.

China's Output of Integrated Circuits, 1986-90



Source: *Ministry of Machinery and Electronics*

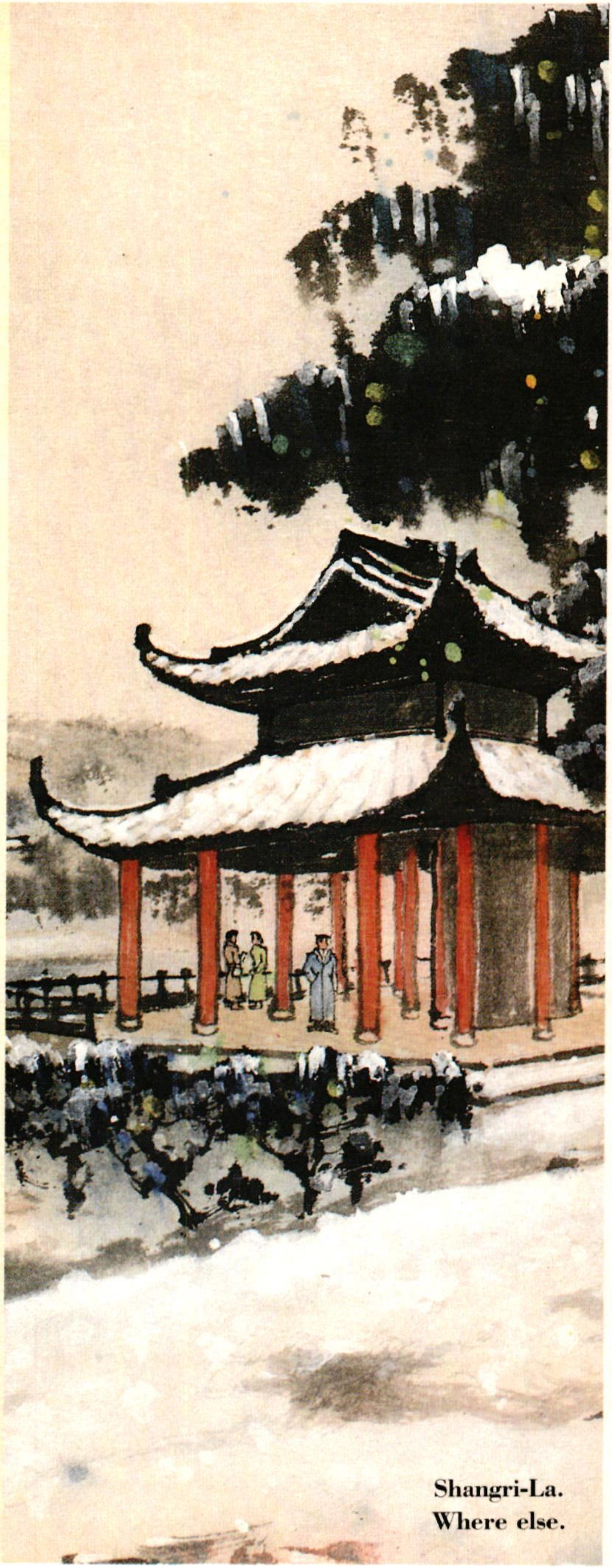
Eighth FYP goals

Though most of these projects won't be up and running until at least halfway through the Eighth FYP, Chinese leaders are counting on them to help fulfill the Plan's targets for the electronics industry. These targets include a 15 percent annual growth rate, which would put 1995 total output at around ¥100 billion. Exports are projected to grow at a slightly faster pace, reaching $6 billion-8 billion in 1995.

Four sub-sectors are to be singled out during the Plan to receive preferential State treatment, including tax exemptions and research and development subsidies: integrated-circuit production, computer production, computer software development, and program-controlled telephone switching. Central authorities are also counting on electronics to serve as the impetus for improvements in enterprise performance. Specifically, electronics-related technologies are to be used to:

- update existing equipment
- develop new products, such as programmable appliances
- manage electric power utilization
- develop computer-aided management systems and design techniques.

Approximately 300 key large- and medium-size State enterprises from around the country will take part in this program, and will receive preferential treatment in terms of access to credit and foreign technology. Shenyang has been designated the first city to carry out these policies of using high technology to promote technical transformation. The program will be overseen by the State Planning Commission and its local affiliates.



Opportunities for foreign companies

The priority being given to the electronics sector by the central government, coupled with the industry's current inability to meet demand and innovate technological advances, will ensure numerous trade and investment opportunities for foreign firms in the coming years. Companies exploring investment opportunities in the four areas targeted under the Eighth FYP will likely find themselves with strong negotiating positions. To date, however, few US companies—or other foreign firms, for that matter—appear to have thoroughly investigated manufacturing opportunities for higher-end products. In the semiconductor and integrated-circuit areas in particular, US companies have been too preoccupied with the markets in Japan and Europe to pay much attention to China. Although the Motorola and NEC projects may herald a new stage of higher-end foreign investment in the electronics industry, many foreign companies are clearly wary of introducing advanced technology into China, a potential future competitor.

Companies disinterested in manufacturing-related investments may still find good opportunities elsewhere in the industry, however, particularly in cooperative research and design efforts. China has several research institutes, for instance the Shanghai Institute of Metallurgy under the Chinese Academy of Sciences, which are doing excellent work in a number of electronics-related areas. Hong Kong and Japanese companies have already begun to establish relationships with such institutes in the areas of CAD/CAM and software engineering. US companies should also seek to harness the skills of such institutes, working with them to design new technologies that could be manufactured in the West.

US companies should seek to harness the skills of China's research institutes, working with them to design new technologies that could be manufactured in the West.

Consumer electronics constitute a growing percentage of China's exports.

Continuing dependence

Although China seeks to become a major player in the global electronics market, it lacks the means to be a first-rate player in the foreseeable future. If the pace of technological change in Japan, the United States, and Europe continues unabated, it is highly unlikely that China will even catch up to Taiwanese or South Korean levels by the end of the 1990s.

Nevertheless, China's electronics sector should achieve reasonable levels of growth—5-10 percent—during the Eighth FYP. It is improbable, however, that the industry will become the catalyst sought by the leadership, and dependence on foreign components will continue. This dependence will be felt most in the computer field, where China's lack of sophisticated manufacturing capability will prevent it from attaining the advanced technological levels it seeks. This in turn will affect the country's ability to meet defense-related electronics requirements, which is already an obvious concern of China's military establishment.

Although the industry as a whole will continue to lag far behind those of Japan and Western countries, facilities that stand out in terms of research and development, software design, and even manufacturing will emerge. These "pockets of excellence" will be created by a combination of nurture from the top and increased local initiative from below.

Domestic enterprises that have linked themselves to foreign firms may also help propel the industry forward. These firms should follow a strategy emphasizing "complementarities" with Western and Japanese companies, whereby they produce a certain piece of technology or equipment needed by the foreign partner. For instance, the Chinese could produce software and peripherals for a foreign mainframe manufacturer. By hooking up with foreign firms, Chinese enterprises will be forced to produce quality goods and interact at a higher level in the international marketplace—prerequisites for eventually striking out on their own. Like South Korea and Taiwan, China's hopes lie in a "learn by doing" approach that seeks to create greater economic interdependence, rather than national self-reliance. 完

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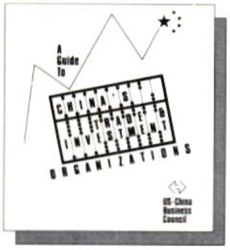

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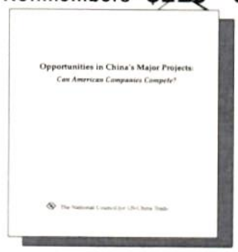

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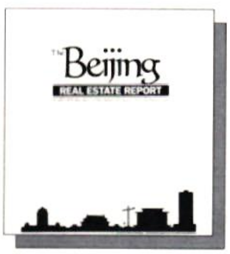

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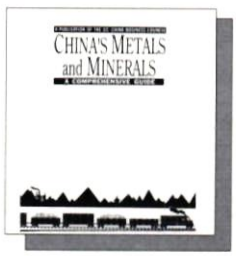

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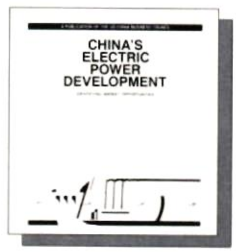

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Chinatron: Ghost of MEI?

The impact of this new, ministry-level corporation on foreign companies is not yet clear

John Frisbie

The past few years have seen Beijing try to reassert control over sectors of the economy it deems critical to economic modernization. One of the most recent moves involves the establishment of the China Electronics Industry Corp. (Chinatron) in June 1991.

The formation of Chinatron represents an attempt by central authorities to regain control over key enterprises in China's electronics industry. In Beijing's view, decentralization of this sector in 1986 led to the growth of inefficient, small-scale production facilities which neglected key technologies and products in favor of lower-technology goods (*see* p. 22). Chinatron was created to "concentrate" manufacturing and research and development efforts to develop larger-scale production and boost the technological level of the electronics industry—including technologies for military use—to allay concerns that China's technological capabilities lag behind those of other countries.

Undoing an arranged marriage

But Chinatron's formation also signals the re-found independence of the electronics bureaucracy at the central level. The 1988 merger of the Ministry of Electronics Industry (MEI) and the State Machine-Building Industry Commission into the Ministry of Machine-Building and Electronics Industries (MMEI) (*see The CBR*, July-August 1988, p. 30) was not universally supported within those bureaucracies or the State Council. The purpose of the merger was to integrate electronics and machinery engineering so that electronics could better serve what some deemed to be its most important application—machine building. In reality, the marriage subjugated the electronics bureaucracy to the machinery bureaucracy. The first MMEI minister was Zou Jiahua, (now vice premier), who has a strong background in machinery. Only two functional MEI departments—the computer and microelectronics bureaus—were left intact in the new ministry, and many cadre-level electronics personnel were reassigned.

Chinatron's formation signals the re-found independence of the electronics bureaucracy at the central level.

Contacting Chinatron

Foreign companies wishing to obtain more information on the new corporation or to meet with its staff should contact:

Chinatron Department of International Cooperation

27 Wanshou Road, Beijing 100846
Phone : (01) 8218528
Fax : (01) 8212801
Telex : 22383 MEI CN
Cable : 2193

John Frisbie is director of the US-China Business Council's Beijing office.

Chinatron's formation has reversed some of the effects of the merger. Chinatron has reclaimed 170 former MEI employees, including former MEI and MMEI Vice Minister Zhang Xuedong, who now heads Chinatron. The State Council has designated 87 of China's largest electronics factories—including the Great Wall Computer Corp., Panda Electronics, Shaanxi Color Picture Tube Factory, Changhong Television Factory, and the Beijing Wire Communications Factory—to come under Chinatron supervision. The enterprises represent about half of the 170 factories formerly under MEI, and produce around 25 percent of China's total electronics output value.

In addition to the 87 enterprises, Chinatron will take over most research and development functions from MMEI. About 50 research institutes will be reclaimed by Chinatron, leaving only two or three under MMEI. Although initial reports indicated that military electronics-production facilities would also be grouped under Chinatron, it now appears the corporation will only be involved in the research and product development of military-related electronics. Chinatron officials say that 95 percent of the corporation's total output value will be for civilian use.

Ambitious goals

Chinatron's development focus in the Eighth Five-Year Plan (FYP, 1991-95) covers a wide variety of product areas. The top priority is the large-scale production of integrated circuits, principally for telecommunications applications. Systems engineering in communications and information processing is also to be emphasized, for such applications as traffic control systems, banking, and information transmission and processing for post, telecommunications, and media. Consumer electronics production will focus on large-screen color televisions, color picture tubes, and video-cassette recorders (VCRs). Communications targets include the development and production of telephone-switching equipment and satellite ground stations. Computer production will concentrate on microcomputers; mainframes will continue to be imported. Military electronics research and development will concentrate on satellite, radar, and mobile communications technologies.

The MMEI link

Chinatron, which has established itself in the old MEI offices in west Beijing, has ministry-level status and reports to the State Council. However, it will have to maintain a close working relationship with MMEI, which continues to fill the overall policy, planning, and administrative role for the industry. The creation of Chinatron has not resulted in any changes thus far in MMEI's bureaucratic structure; MMEI's computer bureau, for example, will continue to be responsible for computer software policy and regulations. The State electronics trading company, China National Electronics Import and Export Corp., also remains under MMEI and has not been placed under Chinatron as originally considered.

Chinatron will nominally handle planning and finances for itself and the enterprises under its umbrella, dealing directly with the State Council, State Planning Commission, and the Ministry of Finance for formal approvals. However, these activities will be closely coordinated with MMEI. Chinatron President Zhang Xuedong sits on MMEI's planning group (which includes the MMEI minister and vice ministers), while MMEI Vice Minister Zeng Peiyuan sits on Chinatron's planning group. Materials allocations to factories under Chinatron will still be handled through Ministry of Materials and MMEI channels. Finances, for this year at least, will also be coordinated with MMEI, which will designate a block of its funds for Chinatron. Chinatron can then re-allocate the monies to various projects through direct dealings with the Ministry of Finance.

In reality Chinatron has not achieved complete independence, since many responsibilities for electronics still lie within MMEI.

Uncertainties abound

Chinatron's ability to implement its mandate is unclear. Regaining control over the factories that come under its domain will prove no easy task; many of these enterprises have enjoyed relatively greater autonomy since 1986 and may resist efforts at recentralization. Local governments, which have been the prime investors in these factories since they were decentralized, can also be expected to resist Chinatron's grasp. The new corporation will have to negotiate revenue-sharing schemes with local governments to pay back local investments in each factory. It will also have to negotiate with local governments on such issues as taxation and utilities. These negotiations have begun, but according to Chinatron officials progress has been slow.

Even if such negotiations are concluded to the satisfaction of all parties, it is still far from clear what degree of control Chinatron will have over the factories beneath it. The current *chengbao* (contract) system will be continued for the time being, with Chinatron essentially replacing the local electronics bureaus. This means that Chinatron will be responsible for production planning and funding allocations to the factories, each of which is an independent accounting unit. Materials will be supplied through traditional channels and at allocated prices for in-plan production. Output levels will be specified in the contract and revenue-sharing will be divided according to agreement between the central and local governments. Chinatron's own operating budget will come not from a share of total profits, but from Ministry of Finance allocations, just as other ministry budgets do.

Ultimately, Chinatron has dreams of adopting a three-tier structure inspired by "large multinationals, such as IBM," according to one Chinatron official. At the top, Chinatron itself would be the "investment center," formulating development plans and allocating investment; underneath, "group" companies would be formed to combine similar producers (e.g., a consumer electronics group company would include television, picture tube, and VCR producers) and act as "profit centers;" and finally, the individual factories would be "cost centers."

Fine-tuning operations

Such an arrangement is clearly a long way off. In the near term, however, Chinatron's position in the central government hierarchy requires further adjustment. Chinatron's ministry-level status theoretically puts it on an equal footing with other central ministries and allows it to deal directly with the State Council, State Planning Commission, and other ministry-level organizations. In reality, though, complete independence has not been achieved, since many responsibilities for electronics still lie within MMEI. In key areas—such as planning, finance, project approvals, and materials allocation—Chinatron and MMEI are still linked in a manner that is likely to breed contention over control, particularly since both organizations carry ministry rank.

Some options to remedy this situation are apparently already being considered within the government. One proposal involves fully re-establishing the Ministry of Electronics Industry and placing Chinatron beneath it with vice-ministry status to act as the ministry's business arm. Another would keep Chinatron as a ministry-level organization, but would also create a State Informatics Commission to coordinate the various electronics-related central organizations, including MMEI, Chinatron, the Ministry of Aerospace and Astronautics, the State Science and Technology Commission, and the Ministry of Posts and Telecommunications. Chinatron officials hope the situation can be resolved this year, but any significant bureaucratic changes may have to wait until the spring of 1993, when the current State Council reaches the end of its

Chinatron Corporate Organization

President
Zhang Xuedong

Vice Presidents
Wang Jincheng
Lu Xinkui

Chief Engineer
Liao Youming

Deputy Chief Engineer
Su Xuezhi

Chief Economist
Wang Dianpu

Chief Accountant
Yang Xianxiang

Chief Supervisor
Xia Wenxiang

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term and an opportunity for bureaucratic reshuffling occurs.

Boon—or bane—for foreign companies?

It is still too early to tell how Chinatron will interact with foreign companies active in the electronics sector. The corporation certainly presents itself as a potential partner for foreign companies, as it is empowered to sign joint-venture contracts and make import decisions, and plans to boost exports in order to purchase production equipment and technology to upgrade facilities. With one-quarter of electronics production supposedly under its control, Chinatron cannot be ignored.

Some clarification may come in the near future, as a number of foreign companies currently have operating joint ventures with Chinatron-designated enterprises. The Beijing Wire Communications Factory, for example, has a joint venture with Siemens to produce telephone-switching equipment. Chinatron officials say the joint venture will not be tangibly affected by the Chinese partner's relationship with Chinatron; no changes are to be made in the venture's legal documents or operations. Rather, it appears likely that Chinatron will eventually become the joint venture's "department in charge," replacing the local electronics bureau as the project's bureaucratic "minder."

Foreign companies should closely monitor Chinatron's evolution to be on the lookout for cooperative opportunities—or competitive disadvantages.

For foreign companies not directly involved with Chinatron or its enterprises, the new corporation may be viewed as a potential competitor. In the area of integrated-circuit production, for instance, a Chinatron-designated factory in Wuxi is scheduled to produce integrated circuits using Siemens technology, while Motorola Inc., NEC, and Philips are all developing projects that will not feature Chinatron involvement. It is conceivable that Chinatron's ministry-level status might give a competitive advantage to the Wuxi project.

At this point, foreign companies should closely monitor Chinatron's evolution to be on the lookout for cooperative opportunities—or competitive disadvantages. Regardless of new developments in either direction, however, companies must still maintain their relationships with MMEI. Chinatron will only be responsible for what falls under its umbrella, but MMEI maintains overall guidance and planning authority for the industry and will continue to play a key role in the approval of contracts and proposals. 完

Project Notebook

A High-Tech Success

Despite high prices and market restrictions, Xerox Shanghai is tops in the copier market—and poised to expand

Kelly Nelson

It took about four years of somewhat roundabout negotiations for the Xerox Corp. to set up its Shanghai joint venture, but the project was apparently worth the wait. For Xerox, China has proved a good match, offering both low-cost design and labor and a growing market for copier machines and products. Formed in late 1987, the $30-million Xerox Shanghai joint venture is currently number one in China's copier market, and has ambitious plans to capture even greater market share.

Choosing China

The copier market in China is dominated by foreign companies, including Ricoh, Canon, Ubix, Minolta, and Toshiba, aside from Xerox. Many of these companies have a longer history of selling to China, but Xerox is the only copier manufacturer thus far to establish a joint venture in the country. Though it will take Xerox significantly longer than its competitors (some of which have signed technology transfer agreements with Chinese firms) to show a return on its $15 million investment, the company's dominant position in a restricted-size market undoubtedly reflects in part greater official support for the joint venture than for its competitors.

Xerox also initially considered penetrating the China market through a technology-transfer agreement, but soon decided to pursue a joint venture instead. Negotiations began in 1984, following establishment of the company's first representative office in China the year before. Previously, sales efforts were organized out of Hong Kong. Numerous

For Xerox, China has proved a good match, offering both low-cost design and labor and a growing market for copier machines and products.

sites were considered for the venture, but Xerox settled on Shanghai due to the large concentration of component suppliers in the area. Xerox's joint-venture partners are the Bank of Communications, which holds 5 percent of the venture, and the Shanghai Movie and Photo Industries Co. (SMPIC), a manufacturer of copiers and other items, which holds 44 percent of the project. The venture is located in the Minhang Economic and Technological Development Zone (ETDZ), which was selected for the tax and other benefits it offers foreign-invested enterprises.

Xerox Shanghai has a 30-year, renewable joint-venture contract, and a 10-year renewable technology license for production of desktop copiers and accessories and other copier products. The license gives Xerox Shanghai the right to use Xerox's desktop office-copier technology.

Three-in-one

Xerox Shanghai consists of three plants, all of which have been set up in the Minhang ETDZ. There is no exchange of money between plants—all function as a single venture. The first, a copier assembly plant, was established in 1988 and is expected to operate two lines and multiple shifts once it reaches capacity, which should occur in 1992. After a brief delay due to the Tiananmen Square crackdown, a $4.3 million toner plant and $2.5 million photoreceptor plant were also constructed. Both became operational in April 1991. These plants have considerably reduced Xerox Shanghai's imports, as the venture previously had to import toner and photoreceptors.

The photoreceptor plant is capable of producing 40,000 units annually at full capacity, which it should reach by 1994. The plant was designed as a low-capacity production facility due to rapidly changing photoreceptor technologies, and provides chemical treatment and vacuum coating for the 1027-model's photoreceptors. The toner plant, in contrast, has an annual capacity of over 1 million pounds, which will probably never be reached in China. It is the only toner plant in the world that produces toner for the 1027 model by an extrusion process. This process, together with up-to-date instrument controls and microprocessors, will allow Xerox Shanghai the flexibility to introduce new toner technologies

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for more sophisticated models in the future.

The three plants currently employ more than 600 people, six of whom are expatriates. When all facilities are running at full capacity, the venture expects to employ 900 workers.

Localizing production

One of the prime components of the Xerox Shanghai joint-venture contract is a stipulation that 70 percent of the venture's components be sourced locally by 1992. Xerox officials claim that the venture is currently on track to achieve this goal, though the process has been difficult since none of the suppliers initially had the technical expertise or equipment necessary to produce the quality components needed by Xerox Shanghai.

To overcome these obstacles, Xerox Corp., through the joint venture, has either transferred technology or provided technical support to approximately 60 suppliers, mostly in Shanghai. Aside from training the suppliers how to use the technology or equipment transferred, Xerox also educates them in materials management and handling, as well as in accounting. The Shanghai Economic Commission has helped Xerox improve the supplier base by providing funding to local companies to enable them to upgrade their factories and purchase the new technology.

Xerox estimates it has spent several million dollars in training, support, and monitoring of Chinese suppliers to ensure consistent quality and delivery. Some of these costs have been charged to the suppliers, and Xerox Shanghai has absorbed the rest. While the training has paid off in improved quality of locally supplied components over the past few years, Chinese components still tend to be produced at above world-market prices—thereby forcing up the final cost of Xerox Shanghai copiers. By Xerox estimates, locally supplied components cost on average about 25 percent more than imported ones.

Satisfied customers

All components used by the Xerox Shanghai venture are subject to quality standards set by Xerox Corp. The parent company has also instituted its corporate quality control culture in the venture, to ensure that Xerox Shanghai's output is on par with Xerox products manufactured in other countries. According to Frans Ryckebosch, former general manager of the venture and current manager of business strategy for Xerox Americas Operations (which includes China and Hong Kong), Xerox attempts to reinforce the concept of quality at all levels, not just in interaction with the enduser. The company's "LUTI"—learn, use, teach, and inspect—system is ongoing, with each management level teaching it to the level below, as well as to new employees.

A Customer Satisfaction Review

Board, which meets on a monthly basis, has also been established by the venture to ensure the reputation of Xerox Shanghai products. The board, composed of representatives from the venture's marketing, service, distribution, management, engineering, and quality control departments, examines complaints and conducts customer surveys to determine where improvement is needed. The results from the first post-installation survey, conducted in January 1990, indicated 90 percent customer satisfaction with the venture's products. Further proof of Xerox Shanghai's success in attaining high quality comes from the Shanghai municipal government, which awarded the venture the Shanghai Quality Award for 1990, and from Xerox China and South Pacific Operations, which awarded Xerox Shanghai an in-house quality award in 1990.

Capturing the market

The first Xerox Shanghai 1027 copier was produced in October 1988, little more than a year after the joint-venture contract was signed. A mid-range model, the 1027 does not incorporate the latest technology, but its "reliable, sturdy operation is very suitable for China," says Ryckebosch. The copier sells for both *renminbi* and foreign exchange, with the price varying according to which currency is used.

In order to meet demand outside Shanghai for its copiers, Xerox Shanghai—with help from SMPIC—has established a nationwide distribution, sales, and service network in China. This network includes over 100 dealers throughout China, all of whom have been trained by Xerox Shanghai. Three Xerox representative offices—in Beijing, Guangzhou, and Shanghai—provide additional dealer support in such areas as training, inventory, advertising, and collateral. This well-developed network helped Xerox Shanghai gain 32 percent of the Chinese desktop-copier market in 1989, and around 45 percent by late 1991. The strong performance has led the venture to accelerate the profitability projections made in the original feasibility study, even though other projections proved to be far off the mark.

Facing reality

According to Pat Martin, president of Xerox Americas Operations, the original feasibility study for Xerox Shanghai was overly optimistic in its assumptions of production costs and size of the copier market in China. These miscalculations were perhaps unavoidable, however, given the unforeseen nature of some of the factors that have affected Xerox Shanghai's performance.

First, the devaluation of the *yuan* and appreciation of the Japanese yen resulted in higher costs to the venture, though these have been partially offset by the higher prices Xerox Shanghai has been allowed to charge for its products. Perhaps more important, the introduction of government purchase controls in 1988 has led to a far smaller market than Xerox originally envisioned. Now, in order to purchase a copier, a prospective buyer must first obtain permission from several government agencies. This system seriously inhibits market forces; Xerox estimates the real market in China to be five times its present size.

Despite these problems, Xerox Shanghai's balance sheet for the first three years was about on target, thanks to tax concessions from the local government and the venture's capture of a larger percentage of the market than originally anticipated. In order to come up with more realistic sales and expense projections, however, Xerox updated its feasibility study in May 1990 to reflect current market conditions.

Looking ahead

Problems unrelated to the macroeconomic environment have also confronted Xerox Shanghai. For instance, the paper feeders initially produced by the venture malfunctioned due to the poor quality of Chinese paper. The feeders have since been redesigned to handle the low-grade paper used in most Chinese offices, and are reportedly functioning well.

In order to better handle such specific technological needs and to tap future demand, Xerox Shanghai is currently designing two new products—a low-end copier for developing markets, and a more sophisticated, high-end model. Xerox Shanghai engineers initially worked in conjunction with Xerox Corp. engineers to develop the prototypes for the two models, but total design responsibility has now been turned over to Xerox Shanghai. The first model of the low-end copier, which is expected to become a major product line in China, is scheduled to enter the Chinese market in 1993.

Whether other new product lines will also be manufactured by Xerox Shanghai has not yet been determined. Says Martin, "My inclination is to continue with Xerox Shanghai; we have a vendor base there and have spent a long time training people in quality control and other areas. But starting a new project is very taxing—I wouldn't let our joint ventures in India and Brazil, for example, even contemplate it. While there are advantages to keeping everything in one organization, it could be too much for them. I want to make sure that Xerox Shanghai continues to operate on a sound financial footing. This venture is already ahead of where our first venture in Japan was at the equivalent time. Eventually, I'd like to see it become like Fuji Xerox, a stand-alone operation with its own product lines."

Whether Xerox Shanghai can meet such lofty aspirations depends on several factors. First, the market will have to expand, which will require the abolition or liberalization of the government purchase-control system. Second, costs will have to come down, which will require further improvements in the local supplier network. The venture is already ahead of schedule in several areas, however, especially exports, which are necessary to help it balance foreign exchange. Xerox Shanghai exported some 2,000 products in 1991—including a shipment to Germany—compared to the 200 called for in its feasibility study. Though exports still account for a small percentage of total production, Xerox had not expected the venture to be able to export to developed nations for another two to three years. It is perhaps no wonder, therefore, that even as Xerox officials claim the future is "daunting," they also proclaim themselves "delighted" with the past three years.

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Asia's Telecommunications Hub

Changes in Hong Kong's telecom outlook could mean new opportunities for US business

Ivan H. Shefrin

Any recent visitor to Hong Kong can testify to the ubiquitous sight of portable phone-toting executives conducting business while they eat, drive, and walk. With approximately 2.3 million telephone lines, 90,000 facsimile machines, 700,000 paging units, and 120,000 mobile telephones in use, Hong Kong maintains some of the highest telecommunications penetration and usage rates in the world.

The territory is far more than a showcase of the latest technology, however. During the past decade, Hong Kong's emergence as the principal telecommunications center in Asia has been instrumental in cementing the territory's key role in the Pacific Rim. Successful telecom development in Hong Kong has led to significant spillover benefits for industries as diverse as financial services and manufacturing, and has given Hong Kong companies a clear competitive advantage in doing business around the clock and around the world. But given the territory's uncertain political future, it is vital that Hong Kong create an even more attractive telecom environment, especially in light of the growing number of cities competing for telecom preeminence in the region.

Singapore and Sydney, for example, offer competitive, sophisticated telecom facilities. Both are emerging as viable locations for regional headquarters, while sites in Japan are also strong contenders. Increasingly, multinational companies that need low-cost, state-of-the-art telecommunications are diversifying their corporate telecom operations within Asia to keep pace with policy liberalization and hedge their bets against the possibility of a more restrictive telecom environment in post-1997 Hong Kong.

HKT's franchise is due to expire in 1995, which could set the stage for increased competition and a greater US presence in the Hong Kong telecom market.

For US telecom equipment and service suppliers in particular, the next few years will likely present critical opportunities for active participation in future telecom growth in the region. Should an Asian trading bloc emerge, for example, Japanese telecommunications firms would probably gain a great advantage in negotiating regional telecom contracts. Under such a scenario, the progress made to date by US telecom firms in Hong Kong will be critical to maintaining a strong US presence in the region. The Hong Kong telecom market will also likely grow in importance as an entry point for US telecom firms seeking a piece of the market on the Chinese mainland.

Ivan H. Shefrin is a trade negotiator and policy analyst for the International Trade Administration of the US Department of Commerce. He is responsible for promoting US telecommunications exports, coordinating US trade policy, and analyzing the competitiveness of the US telecommunications industry.

The Cable & Wireless role

Since 1925, domestic telephone service in Hong Kong has been provided exclusively by Hong Kong Telephone Co., Ltd. (HKT). The majority share of HKT is owned by UK-based Cable and Wireless PLC, one of the most aggressive players in the international telecommunications services market. Though active in 40 countries, including the United Kingdom and the United States, Cable and Wireless earns two-thirds of its global profits from its Hong Kong operations. HKT's franchise, last renewed in 1975, is due to expire in 1995, which could set the stage for increased competition and a greater US presence in the Hong Kong telecom market.

A second Cable and Wireless subsidiary, Cable and Wireless (Hong Kong) Ltd. (CWHK), has handled Hong Kong's international communications services since 1981, includ-

The US-Hong Kong IVANS arrangement will likely expand to allow for full competition in international telecommunications services.

ing telephone, data, telex, electronic mail, and other services. CWHK also operates leased circuits for private voice and data networks. CWHK has enhanced Hong Kong's reputation as an Asian communications hub by helping fund and construct submarine fiber-optic systems directly linked to countries such as Japan, Taiwan, and South Korea. Though CWHK's 25-year exclusive international franchise extends to 2006, it too will find itself facing tougher competition in the years ahead, from such sources as private satellite systems and international value-added data networks.

Cable and Wireless has used its monopoly profits from Hong Kong to fund acquisitions and expansion around the globe, thus insuring itself against repercussions from Hong Kong's integration with China in 1997, as well as increased competition in the Hong Kong telecom sector. In a 1988 restructuring designed to streamline operations and meet corporate telecom demand more efficiently, Cable and Wireless formed a new holding company—Hong Kong Telecom—to hold the capital of both the domestic and international telecommunications operations in Hong Kong. Hong Kong Telecom is 75 percent-owned by Cable and Wireless, with the remainder held by private investors and the China International Trust and Investment Corp. (CITIC). The holding company's revenues, which were approximately $2.4 billion in 1990, will thus be of concern to China as well as to Cable and Wireless and the private shareholders.

Ringing up big profits

By all accounts, Cable and Wireless has ample reason to protect its stake in the Hong Kong telecommunications market, which is already lucrative and still has room to grow. HKT operates one of the most modern telecommunications systems in the world, possessing a 13,000-mile fiber-optic network encompassing almost 2 million lines. Local telephone revenues grew by 13 percent in 1990, and should continue to rise as HKT continues to modernize its network, which will likely be all-digital by 1993. The company has also implemented common-channel signalling (*see* glossary), a forerunner for the full introduction of the integrated services digital network (ISDN), which will provide users with a single line to carry voice, data, and video in digital form. In addition to local service, HKT provides data transmission facilities, Centrex-style services (Citinet), facsimile (Faxline), a packet-switched public data network (Datapak), and other services and equipment through a number of subsidiaries. Mobile phone service is another strong growth area for HKT, which saw its mobile phone revenues grow by 32 percent in 1990. Other competing mobile phone companies in Hong Kong have experienced similar growth.

Demand for long-distance telephone service is also on the rise; CWHK's revenues from international telephone service grew by 21 percent in 1990. Hong Kong showed its international outlook by making 98.6 million overseas calls in 1989, an average of 18 per person—one of the highest rates in the world.

Chipping away the monopoly

The terms of the HKT and CWHK franchises are broad, granting exclusivity to the two firms for all domestic and international telecommunications circuits. On paper at least, the scope of the monopoly has made it difficult for the Hong Kong government to liberalize the telecom sector, especially as the firms and their UK parent have been protective of the monopoly. In order to satisfy demands within the telecommunications industry for greater participation, however, the Hong Kong Post Office (the administrative body that oversees the operation of all telecommunications services in the territory) has used its authority to approve new, more liberal tariffs and to negotiate international agreements as a means of getting around the monopoly provisions. The dynamic between the Post Office and HKT has meant a slow but steady march to increased competition, though no radical breakthrough can be expected before expiration of HKT's franchise in 1995, when the Post Office may have the flexibility to authorize a competitive second network.

Foreign companies, in the meantime, are already finding their slice of the Hong Kong telecommunications pie. In particular, value-added network (VAN) services, such as electronic or voice mail, and store-and-forward facsimile services, can be provided on a competitive basis in Hong Kong. The Post Office has decided that such services fall beyond the scope of the HKT and CWHK franchises, which cover only basic telephony and the provision of circuit infrastructure. In order for a provider to receive a Public Non-Exclusive Telecommunications (PNETS) license to provide VAN services, the new services must add a computer-processing function to the underlying basic transmission. To date, the Hong Kong Post Office has issued about 40 such licenses, along with 17 radio licenses to suppliers of paging services, 3 to providers of mobile radio services, and 2 to operators of trunked radio systems.

During the past three years, Hong Kong, like other countries with significant telecom interests, has pursued value-added services on an international basis through negotiations for international value-added network services (IVANS) agreements. In November 1990, the United States and Hong Kong concluded an IVANS agreement negotiated pursuant to regulations of the International Telecommunications Union (ITU). The terms of the arrangement define the services for which competition is permitted; allow the third-party resale of international private-leased circuits for provision of value-added services; clarify procedures for securing a PNETS license from the Hong Kong Post Office; clarify the bounds of government regulation of the industry; and establish a regime of regulatory safeguards to ensure that CWHK refrains from anti-competitive behavior in the market for value-added services.

The specific value-added services covered by the US-Hong Kong IVANS arrangement include packet-switching services, store-and-forward electronic mail, database access and data communications services, and enhanced facsimile services. Excluded from the arrangement is the sale of international voice-mail services, but both governments have agreed to review the accord later with a view to including services involving voice communications. It is also probable that the arrangement will eventually expand to allow full competition in international telecommunications services, including the resale of private-leased circuits, which would enable direct competition with CWHK in voice telephony. In the meantime, the US-Hong Kong IVANS arrangement should increase opportunities for US firms, especially in the data communications and electronic messaging markets, where demand is growing quickly.

Calling US businesses

Prior to the IVANS arrangement with the United States, many value-added services, in particular enhanced facsimile, were reserved by franchise to monopoly provision by HKT. Now, US value-added service providers are able to compete more effectively with HKT. Soon after the arrangement was finalized, for example, American Telephone and Telegraph Co. (AT&T) concluded a telecommunications deal to form a joint venture with Hutchison Telecommunications to provide electronic mail and facsimile services.

Such developments could be good news for the US telecom trade deficit with Hong Kong, which reached $230.5 million in 1990. In the first six months of 1991, US telecom exports to Hong Kong were up slightly over the same period of the previous year, reaching $58.8 million. Most US exports of telecom equipment to Hong Kong consist of components for radio communications equipment.

Hong Kong's ongoing efforts to maintain a state-of-the-art network—Hong Kong Telecom is investing about $320 million a year to upgrade its network—should provide ample future opportunities in telecommunications, particularly for US producers, who are recognized in the territory for their high-quality products. The US Department of

Glossary of Telecommunications Terms

- **Centrex** A telephone company-provided service that gives business customers the ability to dial direct internally and externally without the need for a company-specific system, such as a private-switch or branch-exchange system.

- **Common-channel signaling** A signaling method that uses a separate channel to determine whether a connection can be made before a call goes through, thereby reducing network traffic and the level of call blocking.

- **CT2** A second-generation cordless telephone system, now being tested, in which power is boosted to give mobile telephones a range of several miles.

- **Integrated services digital network** (ISDN) An integrated digital network in which the same switches and transmission paths are used to establish a simultaneous interface for a variety of services, including telephone, data, video, telex, and facsimile.

- **Leased circuits** A dedicated circuit made available at bulk rate to users requiring exclusive or continuous capacity for high-speed transmission.

- **Packet-switched data network** An efficient data transmission system whereby messages are broken down into smaller units which are then individually addressed and routed to users on the network. This method improves data communications because lines are not tied up when no data is being transmitted.

- **Trunked radio system** A private radio system that shares frequencies among many different user groups so that each appears to have its own independent network. Often used by truck and taxi fleets for mobile communications.

- **Value-added network (VAN)** Generally based on packet-switching technology, VAN networks provide services such as electronic mail, voice mail, and store-and-forward facsimile.

—Ivan H. Shefrin

Commerce's Foreign Commercial Service (FCS) unit in Hong Kong has listed telecommunications as one of the top potential markets for American business in the territory. Specifically, FCS cites services and equipment for mobile cellular systems and CT2 telephone systems as the most promising areas for US companies. Growing demand for wide area networks (WAN) and local area networks (LAN) could also prove lucrative for US telecom firms. The number of multinational corporations with regional communications hubs in Hong Kong should also mean opportunities in the design, construction, and maintenance of private corporate telecom networks.

Communications services utilizing satellites should also grow significantly in the next few years, as satellite usage will increase at a yearly rate of 20 percent from 1990-93, according to FCS estimates. FCS asserts that US firms should have a significant advantage in this area. A recent study published by London-based CIT Research supports these projections, and indicates that the Asia-Pacific telecommunications market is one of the fastest-growing industries worldwide. By the end of the decade, the study predicts, revenues from Asia's value-added network services alone could approach $10 billion.

The picture is less clear for providers of subscription television services. There has been great interest on the part of telecom companies in pay-tv as a cable-based system could effectively provide the basis for a second telecom franchise. In late December, however, the government announced it would undertake a new six-month policy review of the subscription television question. It appears that officials want to separate the pay-tv from the telecom franchise issue; this would enable them to review the success or failure of pay-tv services, which initially will rely on microwave transmissions, before making a decision on whether to go ahead with a second telecom franchise.

Beyond 1995

Despite liberalization at the fringes of the industry, Hong Kong Telecom still maintains a monopoly over most aspects of Hong Kong's domestic and international telecommunications services. The breadth of the original franchise is such that the company has been able to withstand considerable pressure to introduce competition, reduce prices, and liberalize network access and interconnection policies. Nevertheless, the Hong Kong telecom policy environment still ranks as one of the most liberal in Asia, where telecommunications services tend to be provided by government monopolies. If Hong Kong wishes to hold on to its top position, however, it must introduce more competitive telecom prices and move toward an even more liberal policy on access to, and use of, the public telecom network.

Firms providing equipment and services directly to Hong Kong Telecom may find an indirect but effective marketing path to the mainland.

The US-Hong Kong IVANS arrangement is a first step, but further opening of the telecommunications sector will be instrumental to the territory's future economic success. Especially critical will be a move toward more competition in telecom facilities, not just services. Given global trends and the expanding role of Australia and Singapore in the Pacific region's economic and telecommunications infrastructure, Hong Kong's vitality could fade without further innovation in both services and facilities.

Other important issues include the renewal of HKT's franchise, which appears likely. The terms of the franchise, however, will probably not be as broad, and the Hong Kong government will probably allow a phase-in of competing services, such as the "simple" resale of private-leased circuits. This would bring more competition to international telephone services in Hong Kong, which would force Hong Kong long-distance telephone charges to fall. In the United States, for example, the introduction of competing long-distance carriers has driven prices down 45 percent since 1984.

By some estimates, competition in telecom facilities could force prices down by at least 15 percent. Hong Kong Telecom need not fear it would lose significant revenues under such conditions, however, as the US experience has shown that as telephone prices fall, usage rises exponentially, leading to strong growth in the overall size of the market. Thus, competition will likely increase the size of Hong Kong's telecommunications market, enabling both Hong Kong Telecom and its competitors to profit.

Increased competition should mean more opportunities for US business to sell telecommunications equipment and services. Moreover, establishing a presence in Hong Kong may also help US firms establish market share on the mainland. With recent technical cooperation between HKT and Guangdong Province in the cellular telephone and fiber optics areas, Hong Kong's network may eventually extend into contiguous regions in China. Firms providing equipment and services directly to Hong Kong providers may thus find an indirect but effective marketing path to supply China's telecom demand.

China's 20 percent ownership of Hong Kong Telecom, however, could create resistance to further liberalization of the Hong Kong market. While Hong Kong officials apparently were able to negotiate the IVANS agreement with the United States without having to receive Beijing's approval, it will probably be impossible not to include Chinese officials in future negotiations. The idea that competition increases revenues could be a difficult one for Beijing to accept, which could influence events in Hong Kong.

Aside from Beijing, telecom users will play a key role in determining the direction of Hong Kong telecom policy. If large corporate endusers feel they have a stake in Hong Kong, they should lobby hard for additional liberalization. If, however, the overall investment climate deteriorates and foreign firms lose interest in the territory, Hong Kong's telecom policy could end up being dictated by conservative elements in Beijing. 完

我会活动 Council Activities

MMEI Shares Eighth FYP Goals

On October 30, the Council hosted a senior Ministry of Machinery and Electronics Industry (MMEI) delegation visiting the United States to discuss possibilities for cooperation with US companies during the Eighth Five-Year Plan (1991-95). The delegation was led by Vice Minister Bao Xuding, who is responsible for basic machinery, instruments, and fundamental machine components. Bao highlighted 11 areas in which MMEI will seek foreign equipment in the coming four years:

- **Agriculture:** Machinery for large-scale irrigation, fodder production, and processing of industrial crops, as well as rice and corn harvesters.
- **Automation:** Automatic-control systems, quality control monitoring systems, laboratory instrumentation, environmental equipment, medical instrumentation, and office automation equipment.
- **Basic technology:** Precision casting machinery and machine tools, and forging and pressing equipment.
- **Construction:** Large-scale highway and construction equipment.
- **Energy efficiency:** High-speed optimizing control blowers, pumps, compressors, internal combustion engines, industrial boilers, and welding equipment.
- **Hydrology:** Basic hydraulic and pneumatic components, sealing materials, bearings, and electric controls.
- **Metallurgy:** Equipment to improve the manufacturing of iron and steel.
- **Mining:** Equipment to dress, wash, and transport output.
- **Petroleum:** Equipment for offshore and desert production, as well as petrochemical production.
- **Power generation:** Equipment to support 300 MW and 600 MW thermal power stations, and large hydro- and wind-power generating units.
- **Transmission:** Super high-power (at least 500 KV) transmission and distribution equipment.

Legal Committee Reviews China's Draft Trade Law

The Council's Legal Committee hosted a delegation from the treaty and law department of the Ministry of Foreign Economic Relations and Trade (MOFERT) on October 22. Led by Wang Zhenpu, the department's deputy director, the delegation was in the United States to distribute and discuss a draft foreign trade law.

The new law will define the scope and means for regulation of China's international trade, and is intended, in part, to codify the open policy and bring Chinese trade policy more in line with international practice. The proposed law will address a number of issues of major importance to MOFERT, including the relationship between legislation and economic reform, the regulation of domestic and foreign trade matters, and the integration of international and domestic law.

Legal Committee members commented on several key provisions in the draft, including the applicability of the law to foreign-invested enterprises. There was further discussion on fair competition clauses, as well as on articles which may be incompatible with the GATT. Formal comments on the draft legislation are being prepared by the committee and will be presented to MOFERT upon their completion.

Importers Plan White Paper

The Council's Importer Committee met in New York on November 27, 1991, to discuss organizational plans for 1992. Committee members agreed to canvas the general Council membership for new members and suggestions for future committee attention. High on the Committee's list of priorities for the year is the drafting of a Council white paper on the mounting problems importers face in doing business in China. The paper, when completed, will be given to the relevant authorities in China. Some of the issues to be addressed include contract fulfillment, quality control, and claims resolution.

The committee also elected new officers for 1992. Outgoing Chairman Alan Chien (Abacus Group of America, Inc.) was replaced by former Vice Chairman Joseph Scarry (Howard Wagman Co., Inc.), and Pam Phipps (China Products Northwest, Inc.) was voted in as vice chair. Glen Steinman (Monarch Import Co.) assumed the position of secretary/treasurer.

1991 Index

The China Business Review

Compiled by Val Huston

中外貿易 China Business

Val Huston

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

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

中外贸易

SALES AND INVESTMENT THROUGH
November 15, 1991

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

Agricultural Technology

Investments in China

European Community (EC)/Ministry of Agriculture
Began construction of the China-European Community Agricultural Technology (CECAT) building in Beijing, a jointly managed organization designed to promote agricultural technology transfer and to provide training and information services. $7.6 million (ecu5.9 million) and ¥30 million. 9/91.

Other

European Community (EC)
Will provide loan to foster production of wheat, maize, and sunflower seeds in the Xinjiang Autonomous Region. $4.32 million. 11/91.

World Food Programme (WFP)
Will provide aid for grain production in Hunan, Hubei, and Hebei provinces by improving agricultural infrastructure. $40 million. 10/91.

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

Automobiles

Investments in China

NA (HK)/Beijing Automobile Furnishing Plant
Beijing Dongwei Automobile Furnishing Co. Ltd. joint venture began production of bolstered armchairs. $12.5 million. 9/91.

Other

Chrysler Corp. (US)/NA
Will develop new generation of the Cherokee jeep at the Beijing Jeep Corp. joint venture. 11/91.

Italy
Will provide loan to assist production of Iveco cooperatively produced light-duty vehicles. $210 million. 11/91.

Banking and Finance

Investments in China

ChinTung Ltd., the Hong Kong stockbroker for Standard Chartered Bank (UK)/China Venturetech Investment Corp.
Established research joint venture in Shenzhen to gather information on stock markets and business opportunities in China. 10/91.

Other

Hong Kong Overseas Chinese Commercial Bank
Opened a branch office in Shantou. 11/91.

Nomura Securities Co. and the Industrial Bank of Japan (Japan)/CITIC
Issued CITIC floating-rate bonds in the Tokyo capital market from Oct. 30-Nov. 8, 1991. $114 million. 10/91.

Compagnie Financiere De CIC et de l'Union (France)/ICBC and the Chinese Trade Promotion Organization
Signed agreements to finance cooperation between Chinese and French small- and medium-sized firms. 10/91.

Asian Development Bank (ADB)
Will provide a loan and grant package to enable the ICBC to relend to commercially-run State enterprises, collectives, and joint ventures. $100.8 million. 10/91.

Asian Development Bank (ADB)
Approved grant to develop a system of national accounts in line with the UN system for the State Statistical Bureau. $600,000. 10/91.

First Interstate Bank (US)
Opened a branch office in Shanghai. 10/91.

Banque Indosuez (France)
Opened a branch office in Shanghai. 10/91.

Barclays Bank (UK)
Opened a representative office in Shanghai. 9/91.

ABN AMRO Bank (Netherlands)
Opened representative office in Shanghai. 9/91.

International Monetary Fund (IMF)
Signed agreement to open representative office in Beijing. 10/91.

Chemicals and Petrochemicals

China's Imports

Snamprogetti Corp. (Italy)/CTIEC
Will sell equipment for production of EVA resin to be used in the Beijing ethylene project. $50 million. 11/91.

Tecnimont, a subsidiary of Ferruzzi-Montedison Group (Italy) and Intecsa Unde Industrial (Spain)/NA
Awarded contract to build 40,000 tonne/year polypropylene plant in Tianjin. $40 million. 10/91.

Tecnimont Engineering Co. (Italy)/SINOCHEM
Signed contract to supply Dalian West Pacific Petrochemical Co. with technology and equipment capable of producing 6,000 tonnes of polypropylene a year. 11/91.

Investments in China

Beston Petrochemical Co., a subsidiary of Chia Tai Co. Ltd. (Thailand)
Will establish Ningbo Beston Petrochemical Co., a wholly foreign-owned enterprise, to produce polyvinyl chloride powder. $11.25 million. 11/91.

Ciba-Geigy Ltd. Co. (Switzerland)/Ministry of Chemical Industry
Signed accord to establish joint venture with the Beijing No. 3 Chemical Plant to produce anti-oxidant agents. $45 million. 10/91.

BASF (Germany)/Shanghai Gao Qiao Petrochemical Corp.
Established joint venture to produce polymer dispersions for use in the paper, textile, and leather industries. 10/91.

Construction Materials and Equipment

Investments in China

Morgan Crucible Co. (UK)/Dalian Refractories
Opened the Dalian Morgan Refractories joint venture in Liaoning Province to produce high-resistance monolithic concrete. $8 million. (UK:40% - PRC:60%). 10/91.

Other

Denmark/Beijing Heat-Supply Co.
Will provide concessionary loan for the BHR-COWI Energy Co. to provide second-phase consulting services and sell computer-controlled facilities. $1.3 million (Kr 8.4 million). 9/91.

Consumer Goods

Investments in China

Benetton Japan, a subsidiary of the Benetton Group (Italy)/Hong Du Fashion Co.
Opened the Beijing Benetton Fashion Co. joint venture to produce and sell Benetton products. $400,000. (Japan:50% - PRC:50%). 10/91.

PepsiCo. (US)/NA
Established two assembly lines to produce Pepsi-brand sneakers in Guangdong Province. 10/91.

Other

The Upia Co. (Japan)
Opened a representative office in Beijing for cosmetics and health food. 10/91.

Computers and Computer Software

Investments in China

Apple Computer Co. (US)/Torch High-Tech Industrial Development Corp.
Signed agreement to co-produce Macintosh computers in Xiamen. 10/91.

Other

Shinkoh Software Inc., a subsidiary of the Shinkoh Group (Japan)
Opened representative office in Beijing to offer software services and consultations on electrical, telecommunications, and mechanical services. 10/91.

Consumer Electronics

Investments in China

Toshiba Corp. (Japan)/NA
Will establish Toshiba Dalian Co. in Liaoning Province to manufacture color TV picture-tube components, printed circuit boards, and VCRs. $18.8 million (J¥2.5 billion). 10/91.

Environmental Technology and Equipment

Other

Germany
Will provide concessionary loans and grant for environmental protection and afforestation projects. $120 million. 10/91.

Asian Development Bank (ADB)
Will provide grant for project to reduce environmental pollution in Qingdao, Shandong Province. $100,000. 10/91.

Food and Food Processing

Investments in China

Leaf Inc. (US)/NA
Will expand production of the Hua Mei Confectionary Co. chewing gum joint venture in Jiangsu Province. $3.5 million. 11/91.

Coca-Cola Inc. (US)/Hainan Cereals, Oils, and Foodstuffs Import-Export Corp.
Started production of 100,000 sq m Hainan Beverage and Food Co. Ltd. bottling joint venture in Hainan Province. $12 million. (US:25% - PRC:75%). 10/91.

Tokyo Maruichi Shoji Co. (Japan)/Kangle Dairy Factory (Fujian)
Established the Fuying Fuzhou Development Co. joint venture to produce and sell soybean milk. $1.15 million. (Japan:47.5% - PRC:52.5%). 9/91.

Other

Finland
Will provide soft loans for Finland's Algol Corp. to install water plant equipment in Guangdong Province. $4.6 million. 10/91.

China's Investments Abroad

The Republic of Trindad and Tobago/China
Signed technical cooperation pact to provide guidance and personnel training in fresh water shrimp farming and bamboo production. 9/91.

Foreign Assistance

Japan
Will provide part of J¥810 billion package for fiscal years 1990-95 for construction of a dam, several fertilizer plants, and a highway. $965 million (J¥130 billion). 10/91.

NA (Japan)
Will provide syndicated loan to CITIC for support of China's petrochemical and electrical power projects. $35 million. 10/91.

Italy
Will provide export credits for development of the Pudong New Area and to sell Italian technology and equipment for petrochemical, telecommunications, and energy projects. $450 million. 10/91.

Italy
Will provide grant for construction of hospital and agricultural, energy, and telecommunications projects. $100 million. 10/91.

Germany
Will provide concessionary loans for telephone projects in Guangxi Autonomous Region and for further development of a tire factory in Guizhou Province. $17 million. 10/91.

United Nations Development Programme (UNDP)/MOFERT
Will provide grant to help in the structural reform of the Chinese public sector. $2.14 million. 10/91.

Machinery and Machine Tools

China's Imports

Denmark/Dalian Freezer Factory
Will provide concessionary loan for The Disa Co. to sell a costing line. $4.2 million (Kr 27.9 million). 9/91.

Komrowski Ltd. (HK), a subsidiary of Ernst Komrowski & Co. (Germany)/Shanghai Volkswagen
Will sell 10 600-MT heavy-car body presses. $35.7 million (DM60 million). 9/91.

Investments in China

Hitachi Corp. (Japan)/NA
Opened the Shanghai Hitachi Electric Tools Co. Ltd. joint venture which will produce and sell electric tools, coal-mining equipment, electric motors, and appliances. $24 million. (Japan:25% - PRC:75%). 11/91.

Process Automation International (HK)/Beijing Electroplating Corp. and Ministry of Aerospace No. 14 Research Institute
Will establish joint venture to produce pollution-control systems and electroplating machines. $500,000. (HK:52% - PRC:48%). 10/91.

Ebara Corp. (Japan)/Wuhan Blower Works
Will establish joint venture to produce industrial fans. $31 million. (Japan:60% - PRC:40%). 10/91.

Other

Mannesmann Demag Baumanchinen (Germany)/Taiyuan Heavy Machinery Plant
Signed technology transfer contract for new model CC2000 crawler crane and is finalizing 10-year contract extension for production of the CC600 and CC1000 crawler crane. 10/91.

Medical Equipment

China's Imports

Philips Electronics N.V. (Netherlands)/Wuhai Union Hospital (Hubei Province)
Will sell magnetic resonance imaging system. $1.67 million (¥9 million). 10/91.

Investments in China

Medical Systems of Asia, a subsidiary of General Electric Corp. (US)/Beijing Changfeng Industrial Co., and China National Medical Equipment and Supplies Import-Export Corp.
Established Ge Hangwei Systems Co. Ltd. joint venture to produce and develop computerized- tomography and ultrasound scanners. $5 million. 11/91.

Metals, Minerals, and Processing Equipment

China's Imports

AEG Westinghouse Co. (US-Germany)/Beijing Cetic Computing and Engineering Corp.
Signed two contracts for equipment and computerization of the Taiyuan Iron and Steel Co.'s steel hot-rolling mill. $10 million. 10/91.

Denmark/China Non-Ferrous Import-Export Co.
Will provide concessionary loan for the Smidth Co. to sell a 1,200-tonne capacity aluminium roasting furnace to the Guangxi Pingguo Aluminium Factory. $4.6 million (Kr 30.5 million). 9/91.

China's Investments Abroad

Pakistan/China Metallurgical Construction Corp.
Will build copper-ore mining, dressing, and smelting facilities in the Saindak Area. $285 million. 11/91.

Chile/Shanghai Huada Electrical Co.
Established joint venture to use raw Chilean copper to produce cores and wires. $700,000. 10/91.

Cameroon/China
Will cooperate in the mining of Cameroon's mineral resources. 10/91.

Packaging, Pulp, and Paper

Other

Canada
Will provide concessionary loan to sell pulp equipment and Canadian technology to the Ya'an Paper Mill. $35.5 million. 11/91.

Sanwa Bank (Japan)
Will provide loan to Qingzhou Paper Mill in Fujian Province for construction of 150,000-tonne wood pulp installation. $10 million. 11/91.

Petroleum and Natural Gas

Other

France/Beijing Public Facilities Bureau
Will provide concessionary loan for French companies to sell computer-controlled gas coordinate system to improve natural gas supplies in Beijing. $4 million. 10/91.

Energy Development Corp. (US)/CNODC
Signed contract for oil exploration, to lay 1,500 km of seismic lines, and to drill at least four test wells in the Boyang Basin, Jiangxi Province. 10/91.

Anadarko Petroleum Corp. and Pecten Orient Co., a subsidiary of Shell Oil Co. (US)/CNOOC
Signed agreement for oil exploration and development in the 27/10 block off the Pearl River. 10/91.

Applied Automation Inc. (US)/CNTIMC and China Oil Geophysical Exploration Technique Import and Service Co.
Established a spare parts and technical service center in Beijing to promote the Opseis Radio Telemetry Digital Seismic Data Recording System. 10/91.

Pharmaceuticals

Investments in China

Glaxo Co. (UK)/China National Pharmaceutical Foreign Trade Corp. and the Southwest No. 3 Pharmaceutical Factory
Opened the Chongqing Glaxo Pharmaceuticals Ltd. joint venture to produce anti-asthma inhalers. $10 million. 10/91.

Other

NA (Spain)/Shanghai No. 3 and 4 Pharmaceutical Factories
Will provide Spanish technology to restructure pharmaceutical industry and to produce semi-synthetic penicillin. $8 million. 9/91.

Power Plants

China' Imports

Denmark/CNIEC
Will provide grant for the Smidth Co. to sell power generation equipment, parts, and technical services to the Guangzhou Light Haydite Factory. $620,000 (Kr 4.1 million). 9/91.

Investments in China

NA (US)/SEIC, Shenneng Electricity Development Corp., and Shanghai Municipal Electricity Corp.
Signed letter of intent to establish the Pudong Electricity Development Co. joint venture to supply foreign-invested firms in Pudong. $391 million. (US:50% - PRC:50%). 10/91.

Ships and Shipping

Investments in China

Jindo Corp. (ROK)/CCPIT
Established joint venture to manufacture 20-TEU maritime containers in Guangdong Province. $20 million. (ROK:51% - PRC:49%). 10/91.

Gearbulk Ltd. (Norway)/Tianjin Port Co.
The Tianjin Xingang Sinor Terminal Co. joint venture opened new wharf with handling capacity of 600,000 tonnes. $10 million. 10/91.

Other

New Sulzer Diesel (Switzerland)/China Ocean Shipping Co. (COSCO)
Signed contract to co-manufacture 22,380 hp marine diesel engine at the Dalian Marine Diesel Engine Plant in Liaoning Province. 9/91.

Telecommunications

China's Imports

France/NA
Will provide concessionary loan and export credits for Alcatel Cit Co. to sell 200,000 program-controlled telephone lines and microwave telecommunications facilities to Changsha, Hunan Province. $74.6 million (Ffr 440 million). 10/91.

Investments in China

AT&T (US)/Shanghai Telecommunications Equipment Factory
Established the China American Telephone & Telegraph Communications Equipment Corp. joint venture to produce digital subscriber-loop carrier systems (SLC). $9.82 million. (US:50% - PRC:50%). 10/91.

Seimens AG (Germany)/NA
Opened the Beijing International Switching System Corp. Ltd. joint venture to produce digital telephone switching systems. $25.5 million. 10/91.

Other

Switzerland
Will provide loan to install 80,000 telephone lines in Nanchang, Jiangxi Province. $20 million. 11/91.

Textiles

Investments in China

Taejon Leather Industry Co. (ROK)
Will build leather-processing plant in either Shanghai or Tianjin to be used for the manufacture of footwear and clothes. $3.5 million. 10/91.

Transportation

China's Imports

The Boeing Co. (US)/CAAC
Will sell 13 737-300 jetliners to the PRC. $500 million. 10/91.

Saab Aircraft (Sweden)/China Southern Airlines
Received order for 4 340B, 36-seater passenger aircraft. $50 million. 10/91.

Other

Asian Development Bank (ADB)
Will provide grant to railway project connecting Guangzhou and Shantou via Meizhou. $100,000. 10/91.

American Express Corp. (US)/Air China
Signed agreement to allow use of American Express credit cards for airline ticket purchases in Guangzhou, Shanghai, and Beijing. 9/91.

Miscellaneous

Other

Canadian Standards Association (CSA)/China National Import-Export Commodities Inspection Corp.
Opened trade standards coordination office in Shenzhen to assist Chinese manufacturers to obtain CSA quality approval for export goods. 10/91.

Malta/China
Signed maritime agreement providing for port access, most favored nation treatment in vessel loading/unloading fees, and exchange of technical assistance. 10/91.

Ethopia/China
Signed an economic and technical cooperation agreement. 10/91.

Portugal/Tianjin
Signed trade agreements. 9/91.

US GOVERNMENT OFFICES IN CHINA

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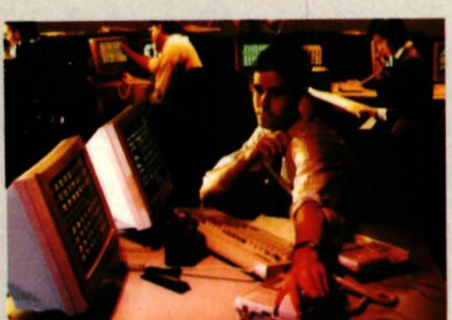

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