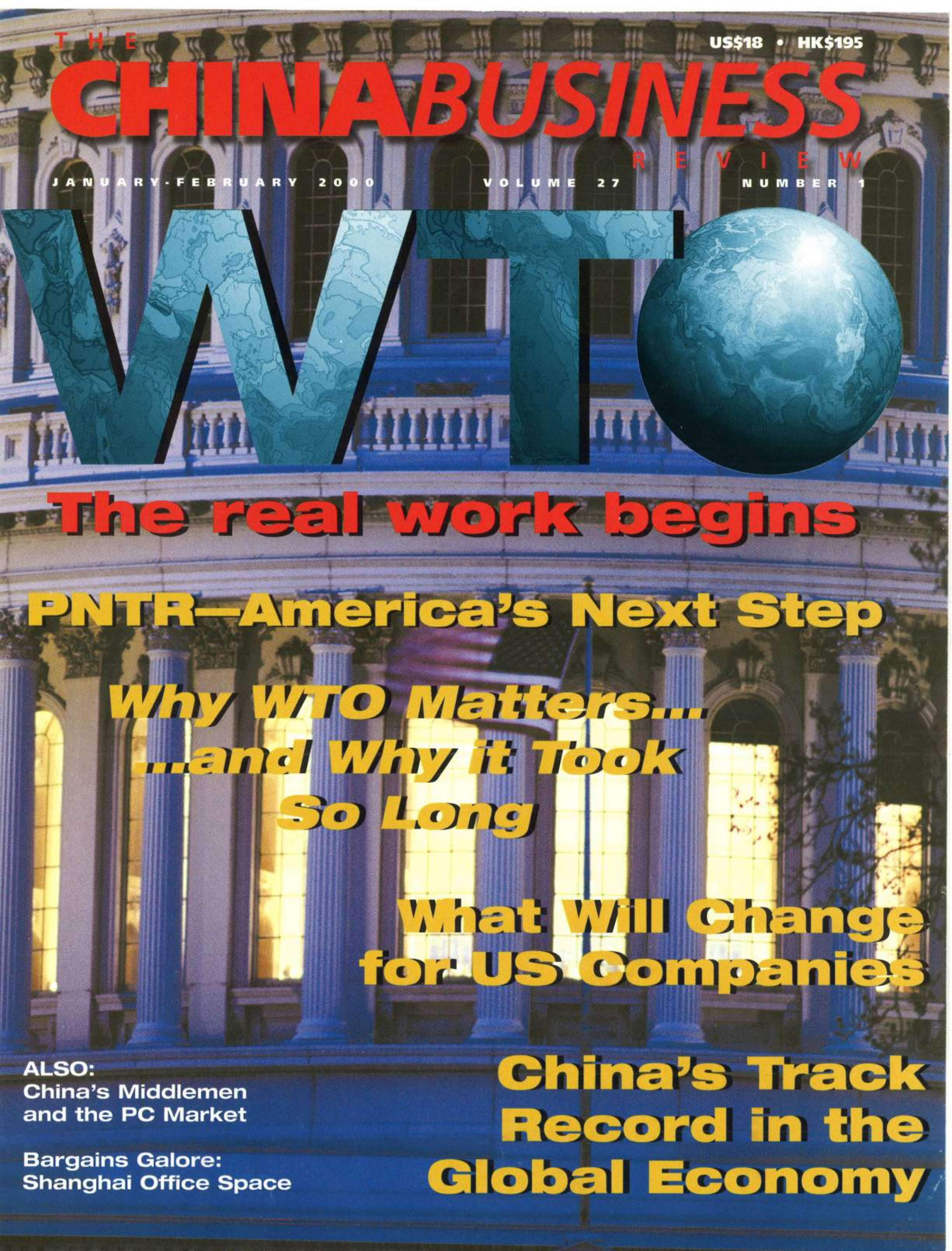


THE CHINA BUSINESS REVIEW

US$18 • HK$195

JANUARY-FEBRUARY 2000 VOLUME 27 NUMBER 1

WTO
The real work begins

PNTR—America's Next Step

Why WTO Matters... ...and Why it Took So Long

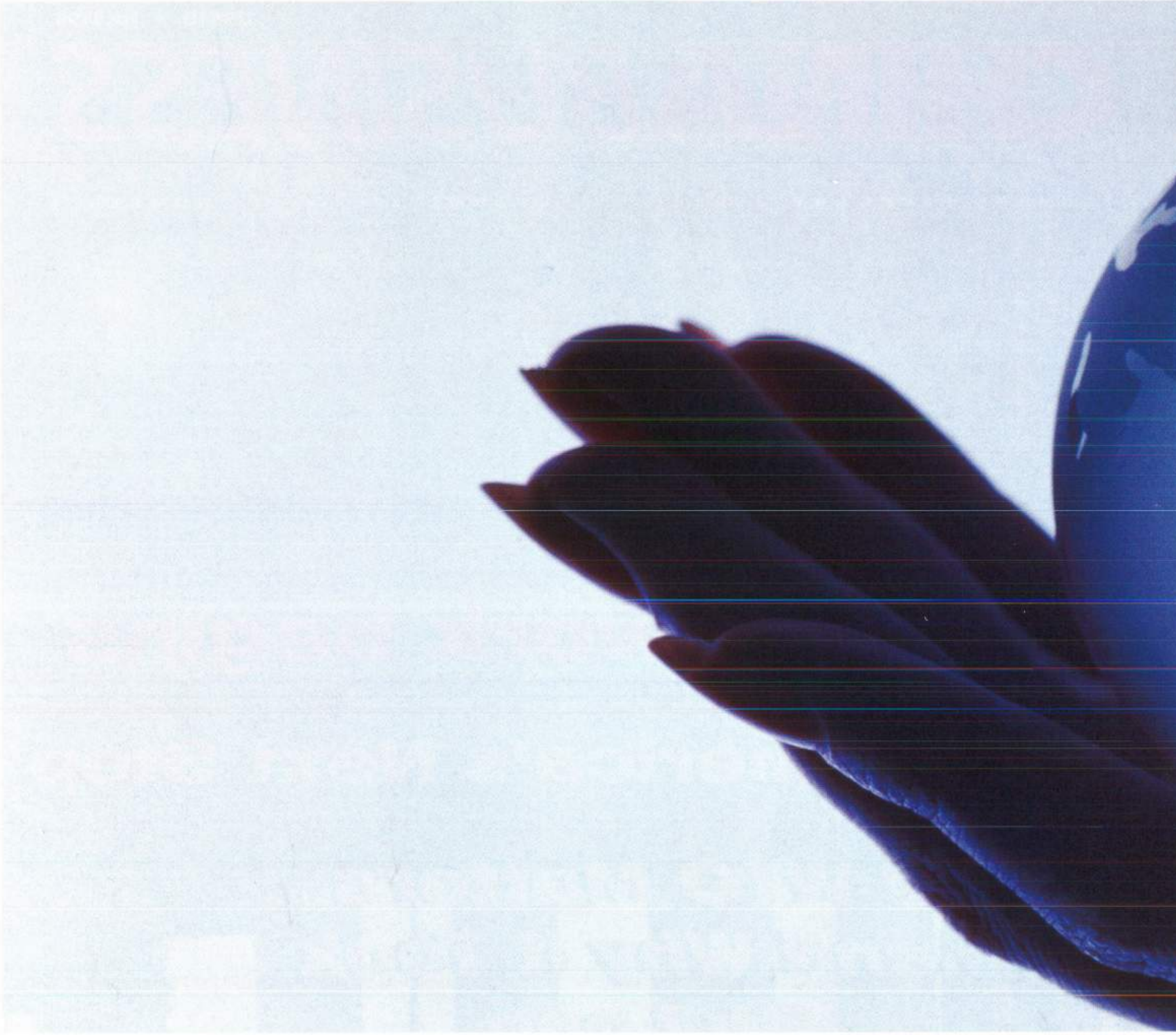
What Will Change for US Companies

China's Track Record in the Global Economy

ALSO:
China's Middlemen and the PC Market

Bargains Galore: Shanghai Office Space

THE MAGAZINE OF THE US-CHINA BUSINESS COUNCIL



Small world.

THE WTO

WTO SPECIAL REPORT: THE REAL WORK BEGINS

WHAT NEXT FOR THE UNITED STATES?

WHAT NEXT FOR CHINA?

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Why China's entrance into the WTO is important to Xerox.

At Xerox, there's a deep commitment to customers. So deep that we pioneered Customer First and forged Quality into the underlying principle of our business. In the 1980s (about the same time we entered the Chinese market), the Commerce Department recognized these achievements with one of the earliest Malcolm Baldrige Awards.

However, we didn't stop with Quality.

Throughout the 1990s, using our Quality Process (and while we expanded our business and investments in China), we re-engineered our corporation. We simplified our business, empowered our people, redesigned our facilities and advanced our information systems with one goal in mind: customer service and responsiveness.

But there's one problem.

Some customers are harder to support than others. Trade barriers, market access rules and bureaucracy keep them at arms length. These restrictions have prevented us from offering Chinese customers the same array of products and services we offer elsewhere around the world.

China's decision to become a member of the World Trade Organization and be part of a rules-based international trading system means that Xerox can provide Chinese customers a world-class level of solutions, service and support. With fewer restrictions and less red tape, our customers stand only to benefit.

Which improves relationships. Which improves business. Which brings growth. And advances progress.

That's why China's membership in the WTO is important to Xerox. And to our customers.

It should be important to you, too.

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Letter from the editor

This issue of *The CBR* is going to press amid the celebrations of Christmas and the last new year of the millennium. It is a flush holiday season for many Americans, as the US economy ends on another high note.

China's economy, in contrast, is in the throes of an increasingly wrenching overhaul. Reforms that have gone on for two decades are forcing changes in some of the most tender areas of the Chinese economy. Deflation is more than two years old and unemployment is reaching all-time highs.

It is in these very different contexts that China and the United States reached agreement on China's World Trade Organization (WTO) accession. Even a quick look at the agreement reveals that China's leadership sees opening its markets on a grand scale to foreign companies as good for China's economy. Yong Wang points out in this issue that these leaders overcame influential opposition to arrive at this decision.

China's central government now must not only keep the economy on track. It must ensure that China's WTO obligations are met in the provinces, counties, and townships across the country. How well it implements WTO obligations will help determine whether the Chinese economy and legal system become fully open, efficient, and effective, and able to meet the needs of Chinese citizens. The WTO's rules and requirements dovetail with China's efforts to reform its economy and legal system, and as Margaret Pearson notes in her article on the PRC's track record in the international economy, China's reformers have relied on pressure from global economic organizations to facilitate domestic change.

We at *The CBR*, and The US-China Business Council, have worked to provide a thorough, if preliminary, assessment of the US-China agreement—and of what China's now virtually imminent WTO accession may mean both for the United States and for China. As an introduction to this effort, we are honored to share with readers statements from His Excellency Jiang Zemin, President of the People's Republic of China, and Ambassador Charlene Barshefsky, US Trade Representative.

This special report also kicks off a regular series in *The CBR* on China's WTO accession. Each issue will feature stories on how China's entry into the WTO will affect the economies, businesses, and citizens of China and the United States.

On a separate note, this issue marks the start of some changes in *The CBR's* look and content. We have switched typefaces and layouts, changed the focus of some of our departments, and plan more changes in future issues to help make *The CBR* more accessible and, ultimately, more useful to our readers. As always, please feel free to contact me with any comments at cgelb@uschina.org.

Sincerely,

Catherine Gelb
Editor

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www.chinabusinessreview.com

PRINTED IN THE USA

The China Business Review welcomes articles from outside contributors. Manuscripts submitted for consideration should be sent to the editor at the address above.

The China Business Review, ISSN No. 0163-7169, is published bimonthly by the US-China Business Council, 1818 N Street NW, Suite 200, Washington DC 20036-2470, USA (Tel: 202/429-0340), a nonprofit organization incorporated under the laws of the District of Columbia. Periodicals postage paid at Washington, DC, and additional mailing offices. Postmaster, please send address changes to *The China Business Review*, 1818 N Street NW, Suite 200, Washington DC 20036-2470, USA.

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

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

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Premier Zhu Rongji speaks with Butler Manufacturing Chairman Don Pratt at a reception.

China's Accession to the WTO Serves the Common Interests of China, the United States, and the World

His Excellency Jiang Zemin,
President of the People's Republic of China

On 15 November 1999, the governments of China and the United States concluded the bilateral agreement on China's accession to the World Trade Organization (WTO) following consultations on an equal footing and in the spirit of mutual understanding and mutual accommodation. This "win-win" outcome is testimony to the strategic vision and perspective with which the two sides view the long-term interests of the two peoples and their persistence in overcoming numerous difficulties and obstacles along the way. The success bears significantly on China-US relations and the development of the world economy and trade.

Joining the WTO serves China's development. China was one of the original contracting parties of the General Agreement on Tariffs and Trade (GATT), which entered into force in 1948. Owing to historical reasons, New China did not participate in GATT activities for some time after its founding. Without China's participation, any world trade body would not be complete. Firmly pursuing the policy of reform and opening up under the guidance of Deng Xiaoping Theory, China has achieved rapid economic growth, continuous social progress, steadily improved living standards and other achievements marveled at around the world. China's WTO membership will facilitate not only its own economic expansion, but also greater economic cooperation, trade, and exchanges between China and the other countries in the world.

The development of the world also needs China's participation. As the world's largest developing country with 1.25 billion people, the seventh-largest economy and the tenth-largest trading nation, China will help strengthen and improve the multilateral trading system after becoming a WTO member. When that happens, China will earnestly fulfill its obligations while enjoying its rights and, together with other WTO members, make positive contributions to the development of the global economy and trade, the building of a complete and open international trading system and the establishment of a new and fair international economic order.

China's WTO accession serves the fundamental interests of both China and the United States. China is the fourth-largest trading partner of the United States while the US is the second-largest trading partner of, and the second-largest overseas investor in China. The potential for the two countries to trade and engage in economic cooperation is enormous and prospects broad. Once in the WTO, China will offer American merchandise, technologies and capital even greater access to the Chinese market, which will help the expansion of bilateral trade and economic ties across the board as well as introduce fresh impetus to the improvement and growth of overall China-US relations.

The early realization of permanent normal trade relations between China and the United States accords with the common interests of the two countries. It is also the necessary requirement if stability and growth in bilateral trade and economic relations are to be maintained. I appreciate the longstanding and unremitting efforts made by the American business communities in advancing China-US relations and bilateral trade and economic cooperation. And I also appreciate the important role played by the US-China Business Council over the years towards these ends.

The new century is dawning on us. China will firmly press ahead with its reform and opening up, continue to expand mutually beneficial cooperation with all the other countries in the world and make still greater contributions to the lofty cause of world peace and development.

Greeting to The China Business Review

Ambassador Charlene Barshefsky,
United States Trade Representative

A century ago, President Theodore Roosevelt oversaw the initiation of America's Open Door Policy to China. This policy rested upon open and fair trade; but in larger terms helped to assert American leadership in the Pacific, advance core American values, and strengthen peace.

These same principles have guided President Clinton to completion of the historic agreement on China's accession to the World Trade Organization. While a significant amount of work remains ahead as I write, including multilateral work at the WTO, this agreement marked the decisive moment in a 13-year negotiating process.

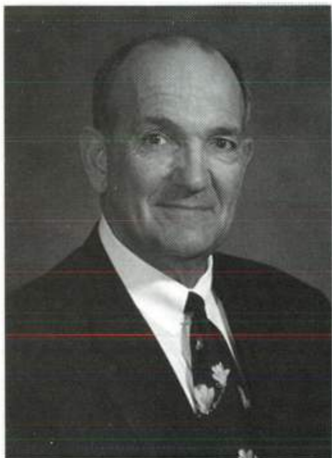
Through a set of comprehensive, detailed and enforceable commitments, stretching from agricultural commodities through manufacturing, high technology industries, finance and other services industries, to electronic commerce and the Internet, our agreement with China will open new opportunities in the world's second-largest economy, and strengthen guarantees of fairness for Americans on the job and on the farm.

On another level, the agreement represents the commitment by the governments of the United States and China to find common ground and work toward a peaceful and mutually beneficial relationship in the years to come. This is fundamentally important not only for our two countries, but for the entire Pacific region.

To win the full benefits of this agreement, both in concrete economic terms and in terms of its potential to contribute to our strategic interests in Asia, we must in the months ahead ensure congressional passage of permanent Normal Trade Relations—that is, the tariff levels guaranteed to virtually all our trading partners today. I look forward to working with you to finish the job; and to open a new century with the same degree of optimism, confidence and American leadership that the Open Door gave us a century ago.

Letter from the Chairman of The US-China Business Council

Michael R. Bonsignore
Chief Executive Officer, Honeywell



It has been my distinct privilege to serve as chairman of The US-China Business Council during one of the most exciting periods in the Council's history. With the November agreement between the United States and China, we stand tantalizingly close to an objective that many business and government leaders have pursued for more than a decade—China's accession to the World Trade Organization.

Now, for the US to reap the many benefits of the agreement, we must ensure that the US Congress grants permanent Normal Trade Relations (PNTR) status to China this year.

The economic benefits of trade with China are well documented. It is clear that American consumers welcome the opportunity to buy goods made in China and that US companies and their employees have much to gain from freer access to China's rapidly growing markets.

But American companies export more than their products to China. They also export their values, operating standards, management practices and commitment to the community—a fact that many critics of globalization and free trade overlook.

The reality is that global corporations are a powerful force for positive social change, influencing how people live, work and treat each other around the world. One of the most intriguing benefits of Normal Trade Relations with China is the potential to help improve the quality of life for Chinese citizens.

As the decision on PNTR comes to the table this year, let's make our elected officials and employees mindful of the full range of positive effects—economic, social and environmental—that Normal Trade Relations with China can have.

Thank you for your support of The US-China Business Council and the cause of PNTR.

Letter from the President of The US-China Business Council

In Full and On Time

Robert A. Kapp

Bring the Benefits of Chinese WTO Accession Home to Americans

After ten years of furious but sporadic activity on the periphery of the US-China relationship, the US Congress has arrived at its moment in the sun. It, and only it, will decide in the year 2000 a critical issue of American international economic and foreign policy, an issue with powerful implications for American national security as well. This decision entails more than the enjoyment of critical economic opportunities for Americans in the international economy. Much, much larger questions about the future of the US-China relationship and China's role in world affairs—and about China's evolution along paths that all Americans hope China will choose—revolve around this fateful legislative decision.

The decision is, of course, whether to accord to the People's Republic of China Full WTO Member Treatment, in the form of PNTR—permanent Normal Trade Relations treatment for imports from China.

The US-China WTO agreement of November 15, 1999

The US-China agreement on the terms of China's WTO accession reached in November 1999 is the single most significant example of positive US influence on China's behavior since the establishment of diplomatic relations in 1979. It demonstrates the power of effective negotiation, and the value of *real*, hard-nosed, and professional engagement with China on issues of substance and detail. "Sending messages to China" has never brought about the level of commitment to internal change that this carefully wrought and wide-ranging agreement has accomplished.

With the remarkable US-China bilateral agreement in hand, China's full-fledged participation in the global rules-based trading system is a very big step closer. The United States will now support China's WTO entry when the WTO makes its final decision, since Uncle Sam secured from China the concessions and commitments necessary to defend and advance the interests of US producers, farmers, exporters, service providers, investors, and consumers.

***The market-opening commitments secured by American negotiators in November will be included in the final documents defining China's WTO accession, and* cannot be weakened.**

With China's accession to the WTO now in view, the rest of the WTO's 135 members are ready to enjoy the broad array of opportunities opening to them. From Day One of China's WTO membership, they will automatically provide to China and receive from China *Full WTO Member Treatment* in all areas defined by the WTO's own codes and by China's specific commitments.

Will the United States now grasp the opportunities our own negotiators have wrought, or will the United States choose to turn away from key elements of that package of opportunities, even as our competitors enjoy them?—That is the question before Congress.

The WTO: the rule of law in international trade

The WTO, like its predecessor the General Agreement on Tariffs and Trade (GATT), is the world's common defense against international trade anarchy and economic chaos, which helped drive the world to totalitarianism and war in the 1930s. WTO rules and commitments liberate market forces and open markets, while providing safeguards against predatory trade practices that violate agreed-upon norms of openness and reciprocity.

At the core of the WTO compact are the common extension of WTO rights to, and the common acceptance of WTO obligations by, all members.

This is PNTR—Permanent Normal Trade Relations, as we call it in the United States. The first lines of the first provision of WTO rules require each WTO member to extend to all other WTO members the best trade treatment it offers to any of them—in other words, Permanent NTR. Giving and receiving PNTR is the cornerstone of the WTO relationship among members, a relationship that in its turn extends far, far beyond tariffs.

To fail to extend PNTR to another WTO member is to refuse to extend Full WTO Member Treatment—and to forfeit, in turn, the member-to-member WTO relationship.

For other countries, this is a non-problem; Full WTO Member Treatment is automatic for any new WTO member.

For the United States, it's different. In 1974, seeking to compel the now-defunct Soviet Union to permit the emigration of certain Soviet citizens, the United States enacted into law the Jackson-Vanik Amendment to that year's Trade Act. Jackson-Vanik mandates one-year-at-a-time extension by the White House of plain-vanilla tariffs on goods from non-market economies, with the presidential extension vulnerable in any year to congressional overturn on any grounds.

After the United States and China opened diplomatic relations and signed a bilateral trade agreement in 1979, US-China relations developed in a Cold War environment of common concern over Soviet intentions. Jackson-Vanik's provisions for possible cancellation of standard American tariffs lay dormant for ten years.

Since 1990, following the televised tragedy of Tiananmen, the nation has witnessed a decade of annual summer fireworks over an inevitable legislative proposal to kill NTR, close American markets to Chinese imports, and push US-China relations onto the rocks.

Each year, however, those who have led the fight to kill US-China trade have failed. In recent years the strong margin of victory in the United States for advocates of continued *non-preferential* trade relations with China has reflected the broad bipartisan consensus that stable economic engagement with China offered a more promising avenue for the pursuit of American material and ethical interests with the PRC than did a unilateral declaration of economic war.

A critical choice

With the US and Chinese governments now agreed in writing on China's remarkable commitments to market-opening and internal economic reform as conditions of WTO accession, however, Congress faces new issues.

Now, Congress must decide *not* whether to destroy existing economic relations with China, but whether to sustain Normal Trade Relations over the long term, *and* whether to support the building of a more secure and durable US economic relationship with a China now bound by its obligations to WTO rules and standards.

As China approaches WTO accession, heavily on American terms, the US Congress has the choice:

Do we bring home to American exporters, farmers, workers, and consumers the benefits of China's massive commitments to open its markets, permit foreign participation in formerly closed economic sectors, reduce tariff and non-tariff barriers, reform its standards of economic conduct, and submit to the binding obligations of WTO rules and regulations that the United States has done so much to design?

Or do we say to China,

"Thanks for the concessions; we don't want them after all.

"Thanks for the detailed commitments rapidly to open your markets and dismantle the apparatus of discrimination against us, rooted in ancient history and Leninist secrecy and Maoist dreams of self-sufficiency. We don't want those commitments, either.

"Thanks for the historic decisions you have made—at our insistence—to drive the Chinese economy rapidly away from Stalin-Mao economics and toward market economics, whose principles lie at the core of Americans' conceptions of social and economic justice. Those decisions, on second thought, don't merit our endorsement.

"And, by the way, about all those iniquities we've objected to for so long: the partiality of your legal and judicial system, the intolerable bureaucratic obstacles to economic cooperation, the opacity of your decisionmaking processes—we prefer to live with them after all. We know you're going to improve your behavior toward the rest of the WTO's members, including our toughest competitors. But don't worry about us: we'll stick to the old system, arm wrestling alone with you to the brink of trade war instead of turning to the world's dispute-resolution mechanisms when we've got a gripe."

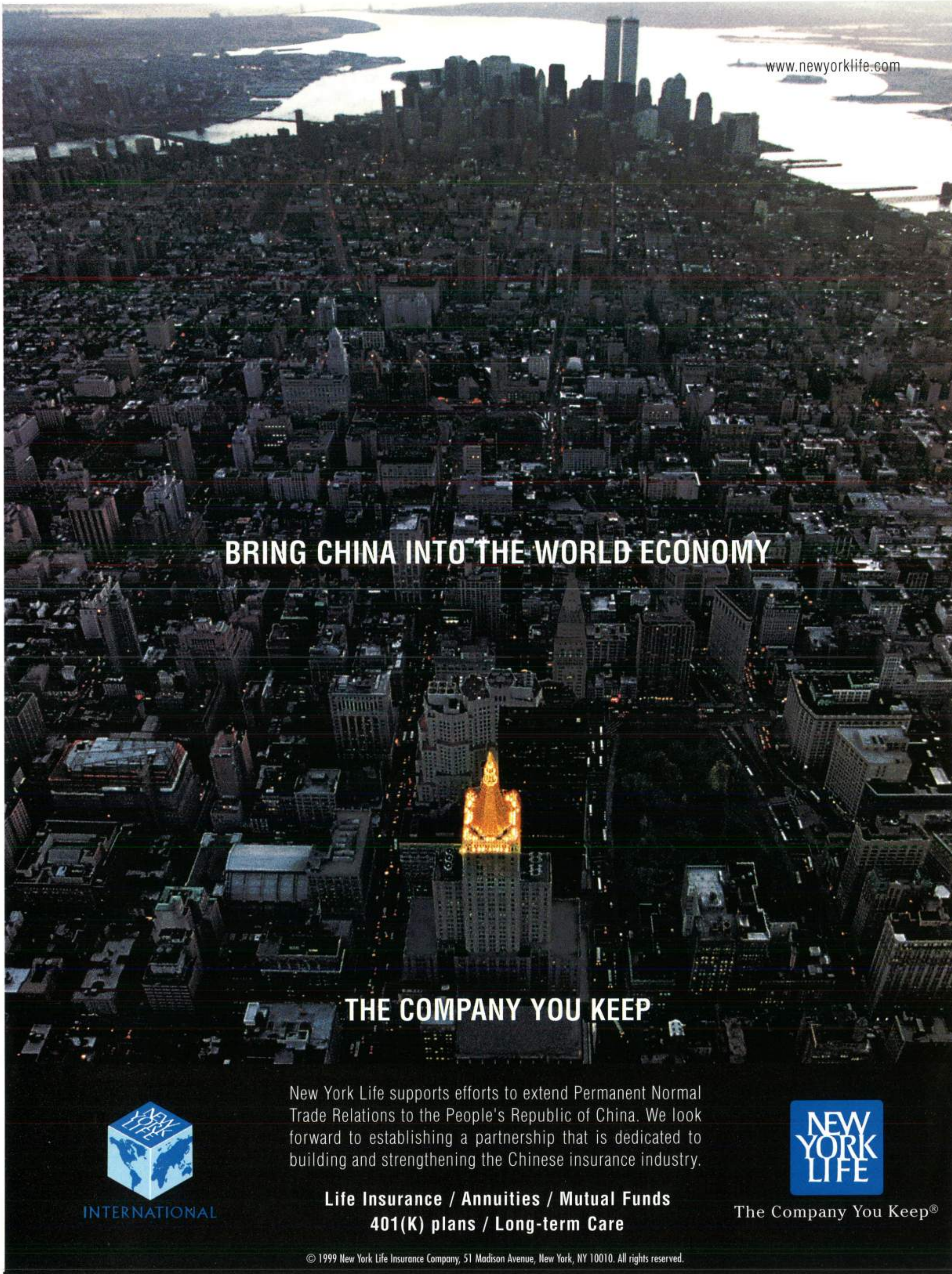
That is America's choice as we approach the PNTR decision.

The choice is about delivering to Americans the fruits of what we have ourselves achieved at the negotiating table.

It is about realizing American opportunities in the global economy, instead of "sending messages" abroad while handing hard-won, real opportunities to our competitors.

It is about encouraging the evolutionary changes within China that American critics of the PRC have long demanded, instead of providing aid and comfort to the defenders of a beleaguered status quo inside China that congressional critics have denounced unremittingly for more than a decade.

It is time to approve PNTR, end the numbing annual NTR exercise, and bring home to American producers, farmers, exporters, investors, and consumers the benefits our negotiators have finally won—**IN FULL AND ON TIME.**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WTO Special Report: The Real Work Begins

After 13 years, China's accession is finally within reach

THE NOVEMBER 15 AGREEMENT BETWEEN THE GOVERNMENTS OF THE United States and China on the terms of China's accession to the World Trade Organization (WTO) has moved China closer than ever to joining the world trading body. China now must complete the WTO accession process, which involves a series of bilateral and multilateral negotiations to develop a final Protocol of Accession that takes the concerns of all other WTO members into account. This process could take at least six months.

Separate from this process, and because of US law, the United States may only benefit fully from China's accession once Congress grants China permanent Normal Trade Relations (PNTR) status.

As *The CBR* goes to press, only the broad outline of the bilateral agreement has been made public. But the details that are available reveal the depth of the PRC leadership's commitment to bringing China's economy into line with WTO obligations. The steps China has declared itself willing to take would significantly overhaul not only the environment for foreign investment and trade in China, but also the Chinese economy. These steps will open the PRC market across the board to imports of foreign goods, and open currently closed sectors to foreign participation. Among the key sectors that the bilateral agreement addresses are agriculture, telecommunications, and financial services.

Contents

This report marks the start of ongoing coverage in *The China Business Review* of the implications of China's WTO accession for the PRC economy and business environment, and for foreign firms.

The US-China Business Council *(www.uschina.org)* is the principal organization representing US companies engaged in trade with and investment in the People's Republic of China. Founded as the National Council for US-China Trade in 1973, the Council is a private, non-profit membership organization based in Washington, DC, with offices in Beijing, Shanghai, and Hong Kong. The Council provides information and analysis on the China market through consulting services, programs, and publications, including *The China Business Review;* and represents member firms in policy-related work in the United States and the PRC.

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US-China Trade Timeline *1971-99*

June 1971 United States ends 21-year trade embargo with China

February 1972 The Boeing Co. signs first aircraft deal with China

September 1972 First US grain sale to China

October 1972 US firms attend Canton Trade Fair (now Guangzhou Export Commodities Fair) for the first time

May 1973 Chinese Liaison Office opens in Washington, DC; US Liaison Office opens in Beijing

May 1973 Inaugural meeting of the National Council for US-China Trade (name changed to The US-China Business Council in 1988)

February 1975 National Council hosts a delegation from the China National Textiles Import and Export Corp., the first Chinese delegation to the United States

November 1978 Coastal States Gas Corp. signs an agreement to become the first US company to import crude oil from China

December 1978 The Coca-Cola Co. signs first deal, with Chinese enterprise CEROILS, to distribute in China

January 1979 United States and China establish diplomatic relations

October 1979 First US-PRC joint-venture contract, signed by ES Pacific Development Co. and China International Travel Service, to build the Great Wall Hotel in Beijing

January 1980 United States awards Most Favored Nation (now Normal Trade Relations in US law) status to China, subject to annual renewal

January 1980 China assumes seat in the International Monetary Fund and World Bank

April 1982 First US-PRC manufacturing joint-venture contract approved between Foxboro Co. and Shanghai Instrument Industry Co.

September 1982 Atlantic Richfield Co. becomes the first foreign company awarded a contract to explore and develop PRC offshore oil and gas fields

October 1982 Squibb Corp. sets up Shanghai Squibb Pharmaceuticals Ltd., becoming the first US company to invest in China's health-care products sector

December 1983 China joins the Multi-Fiber Arrangement

November 1984 3M sets up first US wholly foreign-owned enterprise in China

March 1985 Sheraton Corp. takes over management of the Great Wall Hotel, becoming the first foreign hotel chain to operate in China

July 1985 The National People's Congress promulgates the Foreign Economic Contract Law

January 1986 United States and China sign bilateral tax treaty

July 1986 China applies for membership in the General Agreement on Tariffs and Trade

March 1988 The National People's Congress promulgates Contractual Joint Venture Law

June 1989 United States imposes sanctions after PRC government suppresses pro-democracy demonstrations

December 1990 PRC opens stock markets in Shanghai and Shenzhen

January 1992 United States and China sign memorandum of understanding (MOU) on intellectual property rights

September 1992 AIG, Inc. receives license to operate first wholly foreign-owned insurance business in China

October 1992 United States and China sign MOU on market access

October 1992 Brilliance China Automotive Holding Ltd. becomes the first PRC company to list on the New York Stock Exchange

March 1993 Merrill Lynch & Co. opens representative office in Shanghai, becoming first US securities firm to operate in China

January 1994 China unifies its currency, eliminating Foreign Exchange Certificates

July 1994 New PRC Foreign Trade Law takes effect

February 1995 United States and China sign Accord on Protection of Intellectual Property Rights, Market Access

July 1996 China's currency becomes convertible on the current account

October 1997 PRC President Jiang Zemin and President Clinton agree to take steps to initiate civilian nuclear trade at a Washington, DC, summit

October 1997 China announces purchase of 50 planes worth $3 billion from The Boeing Co.

June 1998 Clinton trip to China produces agreements on US high-tech exports; initiatives on infrastructure development, e-commerce, and Internet applications; and labor- and market-standards policies

July 1998 US Congress votes to change references to MFN in US law to Normal Trade Relations (NTR)

April 1999 United States and China fail to reach agreement on PRC accession to the World Trade Organization during Premier Zhu Rongji's trip to Washington

April 1999 United States and China sign bilateral agriculture agreement

November 1999 In Beijing, the United States and China sign agreement on the terms of China's WTO accession

Congratulations On Another Great Accomplishment.

Anheuser-Busch salutes China and the United States on their WTO agreement.

WTO SPECIAL REPORT The Bilateral Agreement and the United States

"Whether it's improved market access, distribution rights for US exporters, new access for companies from banks to insurance companies to telecommunications companies, or even China's new commitment to abide by the WTO settlement process, this agreement will increase opportunities for American manufacturers and their workers."
Jerry Jasinowski, President,
National Association of Manufacturers

The US chemical industry is the nation's largest exporter, [accounting] for more than $1 of every $10 in US exports...[This bilateral agreement] will expand opportunities for the US chemical industries and the more than 1 million American men and women who work in [them].
The Chemical Manufacturers Association

China represents a huge potential market for US telecommunications equipment suppliers.... [China bought] telecommunications infrastructure amounting to more than $21 billion in 1998. This figure is up from $1.2 billion in 1990.
Telecommunications Industry Association

[The WTO agreement's] market-opening measures...offer our industry a genuine opportunity to compete for China's $63 billion forest products market.
American Forest & Paper Association

The US-China agreement on China's WTO accession lays out a substantial set of commitments that China will have to meet as a WTO member. The commitments in this bilateral will appear in China's final Protocol of Accession, unless they are supplanted by better terms arising out of future bilateral and multilateral WTO negotiations.

The following tables, organized by sector, detail the agreement's terms as they appeared in the summary released by the White House Office of Public Liaison on November 17, 1999 (with the exception of thc information on the audiovisual sector, which was updated more recently). The tables also highlight the areas of the US economy that will be most affected by the agreement. These include:

- **Agriculture** China has agreed to eliminate export subsidies, permit agricultural trade outside of government-controlled channels, slash tariffs, and eliminate sanitary and phytosanitary barriers not based on scientific evidence. A tariff-rate quota system for bulk commodities will provide a share for private traders. Agricultural firms will have the right to import into China and distribute products directly.

- **Industry** China has agreed to phase out quotas, and phase out or cut tariffs dramatically on a broad range of industrial goods. China will also allow non-bank auto financing and participate in the Information Technology Agreement (ITA), which calls for elimination of tariffs on IT products.

- **Services** China has made commitments in all major service categories to eliminate most foreign-equity and geographic restrictions. The PRC will accede to the WTO's Basic Telecommunications and Financial Services agreements, and will "grandfather" current market-access benefits. China's service sector accounts for one-third of its GDP. US service companies will be well positioned to compete.

- **Trading and distribution rights** China has agreed to define "distribution" broadly to include wholesaling, retailing, maintenance, repair, and transportation. US firms will be able to trade, distribute, and sell goods themselves, as well as engage in auxiliary services such as leasing, air-courier, warehousing, advertising, and packaging. This is a critical factor in US business success in international markets, but China currently denies these rights to US companies in China.

Effects of WTO accession

After China completes its accession process, and once the US Congress grants China permanent Normal Trade Relations status, the United States could see benefits in the areas of

- **Employment** Current US trade with China directly supports more than 200,000 manufacturing and service-sector jobs in the United States; add Hong Kong and the number reaches 400,000. US trade with China helps generate employment in the United States in transportation, distribution, retail, and financial services, among other sectors. Small US companies in particular are likely to find new opportunities in China after accession.

- **Rule of law** The WTO is a rules-based international trading system. The WTO's dispute-settlement mechanism provides a credible and effective tool to enforce US economic rights, backed up by the threat of WTO-authorized sanctions for non-compliance.

- **Integration into the global economy** Integrating China further into the global trading system will strengthen the economic and political forces already changing Chinese society. US trade and investment will benefit from a more open and stable China.

US-China WTO Agreement: Industry

Market-Access Issue/Industry	Current Conditions	Post-Accession Conditions	Impact on the United States
Industrial Products	Tariffs: 1997 average: 24.6% Quotas: currently apply to a wide range of goods	• Average tariff: 9.4% by 2005. • Average tariff for priority products: 7.1%, with majority of cuts by 2003. • Existing quotas will be eliminated upon accession for the top US priority goods (e.g. fiber-optic cable). Most remaining quotas will be phased out by 2003, but no later than 2005. • From current trade level, quotas will grow 15% annually, ensuring that market access increases progressively.	Elimination of broad systemic barriers to US exports, such as licenses and limits on import and distribution rights, will open up trade opportunities across all industries.
Autos	Tariff range: 80-100% Quotas	• Tariff: 25% by July 1, 2006, with the largest cuts in the first years after accession. • Quotas will be phased out by 2005. Base-level quota of $6 billion (the level prior to China's industrial auto policy) will grow by 15% annually until eliminated.	New opportunities for US auto exporters. Foreign manufacturers in China will also benefit from the right to distribute products, and conduct marketing and after-sales services (*see services table*).
Auto Financing	Not permitted	• Non-bank foreign financial institutions will be able to provide auto financing upon accession.	
Auto Parts		• Average tariff: 10% by 2006	
Chemicals	Tariffs: up to 35%	• Tariffs: 0, 5.5%, and 6.5% for products in each chemical harmonization initiative category.	An increase in US chemical exports to China.
Electronics	Average tariff: 13.3%	• Tariff: 0 by 2005. • China will participate in the Information Technology Agreement (ITA), and eliminate tariffs on semiconductors, computers, and all Internet-related equipment by 2005.	New opportunities for the rapidly growing US information technology sector. Elimination of cumbersome distribution and retailing regulations will provide new opportunities for US exporters and foreign manufacturers in China (*see services table*).
Wood & Paper	Tariffs: wood: 12-18% paper: 15-25%	• Tariff range: 5-7.5% (both wood and paper).	New opportunities to export wood and wood products to China's $63 billion forest-products market.

SOURCE: The White House Office of Public Liaison

WTO Websites

For more information on China and the WTO, as well as the PNTR issue, visit these sites:

www.uschina.org/public/wto
The US-China Business Council's WTO/PNTR page features links to articles, reports, and other documents from a range of sources. Council members can also visit: **www.uschina.org/members** for more analysis.

www.nbr.org/publications
The National Bureau of Asian Research has posted the full text of several papers on China and the WTO, including: *China and the WTO: The Politics Behind the Agreement; China's Accession to the WTO: A Candid Appraisal from US Industry;* and *Coming to Terms with the "WTO Effect" on US-China Trade and China's Economic Growth.*

www.asiasource.org
AsiaSource, run by the Asia Society, features a report entitled *China and WTO: Battles Ahead,* as well as links to other WTO analysis.

www.sinopolis.com/Archives/Focus/WTO.htm
Sinopolis presents a collection of articles on the WTO agreement, mostly translated from Chinese sources.

www.iie.com/FOCUS/focchina.htm
The Institute for International Economics has several WTO-related papers on its site, including *China and the World Trade Organization: An Economic Balance Sheet.*

www.freetrade.org/pubs/briefs/tbp5.pdf
The Washington-based CATO Institute's Center for Trade Policy Studies has made *Trade and the Transformation of China: The Case for Normal Trade Relations* available on its site in PDF format.

www.cid.harvard.edu/cidtrade
Harvard University's Center for International Development has launched the Global Trade Negotiations Home Page, which contains trade-negotiation information arranged by actor and issue.

fullcoverage.yahoo.com/fc/Business/Trade/
Yahoo's section on WTO and International Trade contains links to news stories and related websites.

US-China WTO Agreement: Agriculture

Market-Access Issue/Product	Current Conditions	Post-Accession Conditions	Impact on the United States
Sanitary and Phytosanitary Measures (SPS)	China regularly imposes unscientific SPS barriers on US agricultural exports.	• Elimination of unscientific SPS barriers. (China agreed in April 1999 to lift unjustified SPS bans on citrus, fruit, meat, and wheat.)	Greater access to PRC markets for US wheat, citrus, fruit, and meat.
Subsidies	China subsidizes its agricultural sector. Many of China's agricultural exports are sold in the global market at prices significantly below those in the domestic market.	• Elimination of export subsidies on agricultural products.	Elimination of export subsidies is particularly beneficial to US corn, cotton, and rice producers because they compete with similar Chinese products in international markets.
Tariffs	Average tariffs on US priority products: 31.5%	• China will reduce tariffs immediately upon accession. • Average tariffs will fall to 14.5% for US priority products, and 17% for all other products, by January 2004. • All agricultural tariffs cuts will be bound (cannot be increased) and will be fully phased in by 2004.	PRC tariffs will fall below those of most American trade partners, with greatest reductions in the areas of top priority to US producers.
Trading Rights	Only state enterprises or entities designated by the PRC government can engage in import and export activities.	• Introduction of private trade (trade between private parties) in agriculture. • Establishment of new rights to import and distribute products without going through a state-trading enterprise or middleman.	An increase in US export opportunities.
Bulk Commodities	Restrictive quotas and their non-transparent application limit market access for US bulk commodities. Out-of-quota tariff rates are as high as 121.6%.	• Expanded access for bulk agriculture commodities, including barley, corn, cotton, rice, soybean oil, and wheat. • Establishment of a tariff-rate quota system (TRQ) that provides a share of the TRQ for private traders. Significant and rising quota quantities will be subject to tariffs that average between 1-3%.	Greater access to PRC markets. Specific operating rules for the TRQ system and the greater transparency of this process will help secure imports.
	Corn: 250,000 metric tons (mt)	• Increased to 4.5 million mt (mmt) upon entry, rising to 7.2 mmt. • 10% (40% by 2004) of quota and any unused state portion reserved for China's private sector.	
	Cotton: 200,000 mt	• Increased to 743,000 mt upon entry, rising to 894,000 mt by 2004.	
	Rice: 250,000 mt	• Increased to 2.6 mmt upon entry, rising to 3.3 mmt by 2005; TRQ to be eliminated by 2006. • 50% of quota reserved for China's private sector.	
	Soybean Oil: 1.5 mmt	• Increased to 1.7 mmt upon entry, rising to 3.3 mmt by 2005; TRQ to be eliminated by 2006. • 50%, rising to 90%, of quota reserved for China's private sector.	
	Wheat: Less than 2 mmt	• Increased to 7.3 mmt upon entry, rising to 9.3 mmt. • 10% of quota and any unused state portion reserved for China's private sector.	
Dairy	Current Tariffs **Cheese:** 50% **Ice Cream:** 45%	2004 Tariffs 12% 19%	Greater access to PRC markets for US cheese and ice cream exporters.
Fruits	Current Tariffs **Almonds:** 30% **Apples:** 30% **Citrus:** 40% **Grapes:** 40%	2004 Tariffs 10% 10% 12% 13% • China will end its ban on US grapefruit, orange, and other citrus fruit imports.	Greater access to PRC markets for US fruit exporters. The citrus industry estimates that trade will reach $1.2 billion in the first year after the ban ends, a $700 million increase over current imports through informal channels.
Meats	Current Tariffs **Beef:** 45% **Pork:** 20% **Poultry:** 20%	2004 Tariffs 12% 12% 10% • China will accept US Department of Agriculture certification for meat safety.	Greater access to PRC markets, particularly for variety meats.
Soybeans	(Tariff not available)	• 3% tariff bound on accession.	Greater access to PRC markets for US soybean exporters.
Wine	Current Tariff: 65%	2004 Tariff: 20%	Greater access to PRC markets for US wine exporters.

SOURCES: The White House Office of Public Liaison, US Trade Representative, US State Department, Charles Schwab & Co.

Gongxi Facai *

United Technologies Corporation, on behalf of its 145,000 employees worldwide, applauds the U.S. and Chinese governments for reaching an unprecedented agreement to expand trade, ensure our common prosperity, enhance economic freedom and advance the rule of law. The agreement is likely to result in:

- **A substantial increase in U.S. exports to China**
- **The creation of higher-paying, quality, export-related American jobs**
- **A stronger U.S. economy**
- **New opportunities for Chinese citizens, and**
- **The acceleration of market-oriented reforms in China**

In order for the United States to take advantage of the impressive series of unilateral, market-opening concessions agreed to by the Chinese government, it is now up to Congress to extend normal trade relations (NTR) to China on a permanent basis.

United Technologies Corporation, whose $200 million in U.S. exports to China in 1998 supported more than 3,000 American jobs, urges Congress to pass permanent NTR and open the door wider to the world's largest emerging market for American products.

*Mandarin for "Congratulations and May You Prosper"

United Technologies

Carrier   Hamilton Sundstrand   Otis   Pratt & Whitney   Sikorsky

"One of the key benefits of the new accession deal will be the ability of American companies to own their distribution chains in China.... Currently, companies must use 'middle men' and can only place goods produced in China on Chinese store shelves. Control of the distribution chain will allow American companies to place American products on store shelves in China."

Robert J. Verdisco, President, International Mass Retail Association

"Opening up China's telecommunications sector, including the Internet services market, will not only deepen Internet penetration in China, but also accelerate the growth of e-commerce throughout the region. The Internet has the potential to serve as a catalyst for growth across key sectors of China's economy and this agreement makes real progress in unlocking that potential."

George Vradenburg, Senior Vice President for Global and Strategic Policy, America Online, Inc.

US-China WTO Agreement: Services

Market-Access Issue/ Sector	Current Conditions
General	Restrictive investment laws, lack of transparency in administrative procedures, and arbitrary application of regulations and laws severely limit US service exports and investment in China, especially in the audiovisual, distribution, financial services, professional services, telecommunications, and travel and tourism sectors.
Telecommunications	Closed to foreign investment.
Insurance	Foreign companies may operate only in Guangzhou and Shanghai. Restrictive licensing practices have limited the number of foreign insurers in China's market to less than 20, and restricted each company to a narrow range of operations. Foreign companies must join with government-approved Chinese partners, and are unable to sell group or pension policies.
Banking	Local-currency business with Chinese clients is prohibited. China has severe restrictions on where foreign banks may operate. US financial institutions require approval—granted on a discretionary, case-by-case basis—for new representative offices and branches.
Securities	Closed to foreign investment. Underwriting by foreign banks of domestic securities and foreign-currency denominated securities is prohibited.
Trading and Distribution Rights/ Services Auxiliary to Distribution	Foreign firms have no right to distribute products other than those they make in China, or to own or manage distribution networks, wholesaling outlets, or warehouses. China severely restricts trading rights (the right to import and export) and distribution rights (wholesaling, retailing, maintenance and repair, transportation, etc.). Business licenses frequently limit the ability of US firms to conduct marketing, after-sales service, maintenance and repair, and customer support.

Post-Accession Conditions	Impact on the United States
China has made commitments in all major service categories with reasonable transition periods, and will: • Eliminate most foreign-equity restrictions, especially in sectors where the United States has a strong commercial interest. • Accede to the WTO Basic Telecommunications and Financial Services agreements. • Grandfather current market-access activities in all services sectors.	Sales in China and opportunities for foreign investment will rise. Greater numbers of small and medium-sized US companies will be able to enter the PRC market for the first time. US companies already in China may streamline and integrate their operations within China and globally. Grandfathering will protect American distribution, financial, and professional and other service providers in China (including those operating under contractual or shareholder agreements or a license) from restrictions as Chinese commitments are phased in.
• **Regulatory Principles:** China has agreed to implement pro-competitive regulatory principles embodied in the WTO Basic Telecommunications Agreement (including cost-based pricing, interconnection rights, and the establishment of an independent regulatory authority). China has agreed to technology-neutral scheduling. • **Scope of Service:** China will phase out all geographic restrictions for paging and value-added services within 2 years of accession; mobile/cellular within 5 years; and domestic wireline services within 6 years. China's key telecom services corridor in Beijing, Shanghai, and Guangzhou, which carries about 75% of all domestic traffic, will open immediately on accession in all telecommunications services. • **Investment:** China will allow 49% foreign ownership in mobile services within 5 years of accession; 49% in international and domestic land and sea (not mobile) services within 6 years; 49% in most other services upon accession; and 50% in value-added services within 2 years.	China's commitments mark the first time it has agreed to open its telecommunications sector, both to direct investment in telecommunications businesses and to a broad range of services. Relaxation of restrictions on investment and distribution will increase demand for foreign telecommunications goods and services in China. China is already US telecom exporters' seventh-largest foreign market. Foreign suppliers will be able to use any technology they choose to provide telecom services.
• **Geographic Scope:** China will permit foreign property and casualty firms to insure large-scale risks nationwide immediately upon accession, and will eliminate all geographic limitations in 3 years. • **Product Scope:** China will expand the scope of activities for foreign insurers to include group, health, and pension lines of insurance (about 85% of total premiums) over 5 years. • **Prudential Criteria:** China has agreed to award licenses solely on the basis of prudential criteria, with no economic needs test or quantitative limits on the number of licenses issued. **Investment:** • *Life Insurance*: China will allow 50% foreign ownership in life insurance joint ventures. Life insurers will be able to choose their own joint-venture partners. • *Non-life*: Upon accession, China will allow the establishment of branches, or 51% ownership in joint ventures, and will permit the formation of wholly foreign-owned subsidiaries in 2 years. • *Reinsurance*: Reinsurance will be completely open to foreign providers upon accession (100%, no restrictions).	Current license holders will be able to expand their scopes of business, and newcomers will be able enter the market with a broader range of product offerings. New opportunities will emerge for US insurance companies to provide life, non-life, and reinsurance products and services in China.
• US banks will: –Gain full market access within 5 years of accession. –Be able to conduct local-currency transactions with Chinese enterprises 2 years after accession. –Be able to conduct local-currency transactions with Chinese individuals 5 years after accession. • Foreign banks will have the same rights (national treatment) as Chinese banks within designated geographic areas. • Geographic and customer restrictions will be removed 5 years after accession.	US banks will gain substantially greater access to the PRC market.
• Foreign financial institutions will be allowed a 33% stake in fund management enterprises upon accession. The stake will rise to 49% after 3 years. • Foreign underwriters will also be allowed to invest up to 33% in joint ventures. • Joint ventures in which US firms have minority stakes will be allowed to underwrite domestic securities issues as well as underwrite and trade in foreign-currency denominated securities (debt and equity); and will be allowed to engage in fund management on the same terms as Chinese firms.	US firms will gain unprecedented access to China's capital markets.
Trading and Distribution Rights: • Commitments in this area address all current restrictions—including wholesaling, sales away from a fixed location, retailing, maintenance and repair, and transportation. • Trading rights will be phased in within 3 years of accession. • China will phase out all restrictions on distribution services for most products within 3 years of accession. **Services Auxiliary to Distribution:** • China will permit foreign firms to provide services auxiliary to distribution including renting and leasing, air courier, freight forwarding, storage and warehousing, advertising, technical testing and analysis, and packaging. • All restrictions will be phased out in 3-4 years, at which time US service suppliers will be able to establish 100% foreign-owned subsidiaries.	US firms will be able to trade, distribute, and sell goods themselves, allowing for better control and greater market access. Companies will be able to streamline their operations in China and eventually integrate their China operations into their global networks. Small and medium-sized US companies will be able to enter the PRC market for the first time. US firms will gain control over after-sales services and find opportunities in freight forwarding and logistics, and other auxiliary activities.

China could account for 37 percent of growth in US agricultural exports by 2003.

The US Department of Agriculture

US-China WTO Agreement: Services

Market-Access Issue/Sector	Current Conditions
Professional Services	China tightly restricts operation of foreign law and accounting firms. Accounting representative offices in China may only offer consulting services. China also requires localization of foreign partners in accounting firms.
Audiovisual	Distribution of books, magazines, movies, sound recordings, and videos is highly restricted.
Travel and Tourism	Activities of foreign firms are highly restricted.

SOURCE: The White House Office of Public Liaison

Post-Accession Conditions	Impact on the United States
• China has made a broad range of commitments that cover legal, accounting, management consulting, architectural, engineering, urban planning, medical and dental, and computer-related services. • China will permit foreign majority control of professional services ventures except in the practice of Chinese law. • In the area of accountancy, China has agreed to eliminate the mandatory localization requirement, to permit licensed professionals unrestricted access to its market, and to follow transparent procedures.	Foreign providers of professional services will gain new freedom to provide services in China.
• China will permit the distribution of video and sound recordings, as well as cinema ownership and operation. • China will allow 49% foreign participation in joint ventures engaged in the distribution of video and sound recordings. • China will allow 20 films annually, on a revenue-sharing basis, upon accession.	The Chinese commitment to import 50 foreign movies over three years amounts to a 300% increase in foreign film exports to China. Expanded equity-investment rights will also boost sales. In 1997, US film industry revenues in China totaled only $18 million, in contrast to $12 billion worldwide.
• China will allow unrestricted access to its market for hotel operation—majority ownership will be permitted on accession, and 100% foreign ownership will be phased in within 3 years.	US firms will be able to participate in China's growing travel and tourism market.

WTO SPECIAL REPORT

PNTR—The Next Step for The United States

NTR is neither a special privilege nor a reward—it is the standard tariff treatment nearly all US trading partners enjoy.

China's formal accession to the WTO is separate from the US legislative process of granting permanent Normal Trade Relations (PNTR) to China. The United States must extend unconditional PNTR to China for American companies to be eligible to receive full WTO benefits from China once it accedes. China will join the WTO regardless of what Congress decides—with other WTO members enjoying the full range of WTO-induced benefits in their business dealings with China.

What is NTR?

Normal Trade Relations (NTR, formerly known as Most Favored Nation tariff status) refers to the standard or non-discriminatory tariff treatment the United States extends to other trading partners in return for reciprocal tariff treatment for US exports. NTR is neither a special privilege nor a reward—it is the standard tariff treatment nearly all US trading partners enjoy. Over 160 countries have NTR tariff status with the United States. The only countries to which the United States currently does not grant NTR are Afghanistan, Cuba, Laos, North Korea, Serbia/Montenegro, and Vietnam.

The United States provides special tariff treatment, *more favorable* than NTR, to more than 30 countries and territories under special tariff programs, including the North American Free Trade Agreement (NAFTA); the Agreement on Trade in Civil Aircraft; the Automotive Products Trade Act; the Caribbean Basin Economic Recovery Act; the United States-Israel Free Trade Area; and the Andean Trade Preferences Act. Under these programs, designated products may be imported at reduced or duty-free rates. China is not eligible for any of these programs.

Why PNTR?

The 1994 Marrakesh Agreement establishing the WTO requires members to extend NTR to other WTO members, mutually and without conditions. However, under the Jackson-Vanik amendment to the United States Trade Act of 1974, the United States may not grant NTR status to non-market economies unless the President waives ineligibility, which he must do each year. This amendment was originally directed at the Soviet Union because of restrictions on emigration of certain Soviet citizens. But the Jackson-Vanik amendment applies to all non-market economies. Thus, for the United States to enjoy WTO benefits with respect to China after PRC accession, Congress must amend or repeal Jackson-Vanik to permit extension of PNTR to China.

Should Congress fail to do so, at the time of its accession China could elect to invoke the WTO's Article 13, which permits China not to apply WTO benefits to the United States. Under WTO rules, the United States also may invoke Article 13. In either case, however, non-application of WTO benefits by either country would deny US firms the greater access to China's markets that WTO accession would bring.

WTO and the US Trade Deficit

The US trade deficit with China often assumes center stage in discussions of the US-China commercial relationship. In 1998, the US Department of Commerce (USDOC) put the bilateral deficit at \$56.9 billion—but eminent US economists have argued that a more accurate figure would be \$35 billion. As the United States evaluates whether benefiting from China's WTO accession is in its interest, it is useful to remember that China's WTO obligations call for reduction or elimination of many of the PRC barriers to US goods and services that contribute to the trade imbalance. Moreover, the deficit is not the most important barometer of US economic health or of the benefits to either side of US-China trade, for a number of reasons:

● **US figures overstate the trade deficit by not accounting for entrepôt trade through Hong Kong.** Economist Nicholas Lardy estimates that current USDOC methodology overstates the deficit by 30 percent.

● **Different US measurements for exports and imports further skew the trade-deficit figures.** US exports are calculated on a free-along-side (FAS) basis and US imports are measured on a cost, insurance, and freight (CIF) basis. According to Stanford University economist Lawrence Lau and University of California economist K. C. Fung, US exports should be adjusted up by 1 percent, and US imports adjusted down by 10 percent to achieve equivalent values. Such adjustments yield a deficit of \$36.9 billion.

● **Merchandise trade figures tell only part of the story—they exclude trade in services.** The overall bilateral US trade deficit with China is even smaller when bilateral trade in services is included—according to Lau and Fung, the 1998 deficit falls to \$35 billion after this additional adjustment.

In the 1990s, the United States has enjoyed a small but growing surplus in trade in services with China. In 1998 alone, US exports of private services to China grew by 8 percent, among the most rapid rates in the region. Once China joins the WTO and its market-access commitments kick in, US-China trade in services will expand even more quickly.

● **Imports from China substitute for other imports, not US-made goods.** According to an Institute for International Economics study, 90 percent of US imports from China are substitutes for US imports from other low-wage economies, largely in East and Southeast Asia. Top US imports from China are low-tech electrical machinery, toys, footwear, and apparel. Only 10 percent of imports from China compete directly with US-made goods.

● **China's 1987-97 export growth reflects the relocation of export-processing ventures from Southeast Asia to China.** Processed exports accounted for 57 percent of total PRC exports in 1998, of which foreign-invested enterprises produced more than 21 percent. Imports accounted for 60 percent of the content in PRC processed exports in 1998, according to PRC Customs statistics. And the combined annual US trade deficit with Hong Kong, Singapore, South Korea, and Taiwan declined from \$34 billion in 1987 to around \$22.7 billion in 1997, while the deficit with China climbed from \$3 billion to \$57 billion, according to US official (unadjusted) figures.

● **Does the deficit matter to the US economy's health?** While China's WTO accession is important to key industries in the United States, trade with China accounts for less than 1 percent of US GDP, which was \$8.5 trillion in 1998.

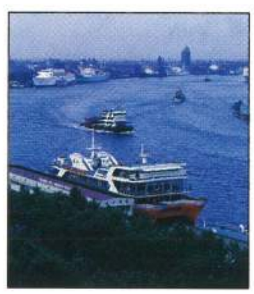
China: A Commitment To Growth

Phillips Petroleum Company's Cooperative Effort with Chinese Partnerships Leads the Way to Accelerating Development and Maximizing Returns

When Chinese authorities and Phillips Petroleum Company combined efforts, cohesive, multi-disciplined teams were created. These teams leverage projects, experience and technology to implement aggressive growth plans throughout China's energy and petrochemical industries.

Phillips China, Inc.'s successful exploration and production operations is now driving investment toward expanded downstream opportunities. The expansion of China's oil & gas industry is a shared vision of Phillips and Chinese partners to further promote progress of China's growing economy.

Phillips Petroleum is eager to explore new opportunities that will lead the way to accelerating development and maximizing growth in China.



PHILLIPS PETROLEUM COMPANY

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WTO SPECIAL REPORT

What Will Change for US Companies

Companies will be able to use China's WTO phase-in schedules to develop better investment strategies.

The full details of the China-US bilateral have yet to be made public, and China's full accession package has yet to be completed. So it is premature to make concrete projections about the impact of China's WTO accession on China's business environment, much less the impact on US companies. It is, however, possible to suggest what changes US firms might face in the lead-up to accession and once China accedes, and what strategies companies might consider, both in the shorter and longer terms.

Assuming that implementation of WTO obligations occurs relatively smoothly, companies can expect a few changes in China's business environment.

An investment rebound

The prospect of China's accession will probably renew investor confidence in China's markets in the coming year. But dislocation from China's ongoing economic restructuring; protectionism by local governments; and the graduated phase in of WTO obligations will moderate investment and trade flows, both before and after accession.

New competition—and opportunities

As soon as China accedes, US companies will encounter competition in some sectors and from some foreign counterparts, particularly from companies in South Korea and Taiwan involved in raw materials and electronics.

Once China completes the phase-in of WTO commitments, US firms will find themselves adapting to greater competition at the same time that they are able to operate with greater efficiency in China.

US service providers in financial, insurance, and telecommunications services, as well as distribution-related industries such as freight forwarding, will see the biggest changes in their China business.

New options for small and medium-sized companies

Lower barriers to entry and a more transparent investment environment will provide small and medium-sized US companies with investment opportunities for the first time.

Greater predictability

Companies will be able to use China's WTO phase-in schedules to develop better investment strategies. The granting of PNTR to China will also improve US firms' ability to plan for long-term commercial interaction with the PRC.

A stronger legal framework

The WTO's dispute-resolution mechanism will offer a multilateral outlet for trade disputes. Though it will take some time for the government to build up key laws and enforcement procedures, in the longer term, China's development of a legal system that incorporates WTO norms may make it easier to resolve disputes in China.

WTO and Company Strategies

Companies are already considering ways to adapt their existing operations in China to WTO-induced changes. The majority of US companies with established operations in China will gradually expand, and are likely to restructure. Many companies, particularly advertising, telecommunications, and express-services firms, may wait for the WTO obligations in their sector to take effect to ensure that they can negotiate the best arrangements.

Specific strategies may include:

- **Shifts in investment vehicles**

The phase-in of new rules on the restructuring of legal entities—particularly new freedom to set up wholly foreign-owned subsidiaries in once-restricted sectors—will drive some firms to seek joint-venture partner buyouts, intensifying a trend that began in 1997.

Companies will also be able to centralize management of finance, sales, marketing, and human resources.

- **Rationalization of company operations**

The ability to control distribution and after-sales services in China is among the most long-awaited of WTO benefits. Once these WTO provisions are phased in, companies are likely to consider a number of strategies to make their operations more efficient in China and worldwide. These could include constructing internal transportation networks and warehousing and storage facilities; expanding directly controlled distribution networks; expanding nationwide sales offices; and establishing nationwide networks of after-sales service providers.

- **Reassessment of trade and investment incentives**

Tariff reductions will grant US manufacturing firms new opportunities to export products to China. The reduction, however gradual, of non-tariff measures such as quotas, licensing and inspection requirements, and of investment-related barriers such as local-content and technology-transfer requirements, will give US firms more flexibility in their trade and investment decisions. Some companies may reduce their direct investments, and instead increase their exports to China.

It is too soon to tell whether China will eliminate the investment incentives now available to companies in Special Economic Zones, or whether China will extend those benefits to domestic firms as well, in keeping with the WTO's

> China's entry into the WTO will accelerate its movement toward a market and consumer-oriented economy with a corresponding increase in motor vehicle sales in China.
>
> General Motors Corp.

principle of national treatment. Some investment incentives, particularly in the interior, may remain even as they are phased out elsewhere.

- **Integration of China more fully into global operations**

Companies may restructure their China operations to improve performance and to integrate China ventures into global operations. Though a China presence will remain critical, most firms will continue to see the country more as a market with long-term growth potential than as a short-term revenue generator.

The jury is out

Though the accession process appears to be moving along smoothly, China is still anywhere from six months to one year from acceding to the WTO. A number of factors could slow this process further; others could delay the benefits of China's WTO accession, including:

- **For US firms, PNTR**

Whether the US Congress grants China PNTR will be critical to determining whether US firms benefit from China's WTO accession along with other WTO members.

- **A protracted implementation process in China**

Certain tariff reductions and non-tariff measures will take effect upon accession, but others will be phased in over three to six years. Throughout this period, the government will need time to implement the terms of China's Protocol of Accession in accordance with its commitments. The WTO's transitional review mechanism also monitors an incoming member's progress.

- **The legal framework**

Over the last 20 years, China has established a solid body of laws and regulations. But its legal system, particularly in the area of enforcement, is incomplete.

- **Domestic economic forces**

While foreign direct investment and trade are important to China's overall economic growth, domestic actors still primarily drive the economy. Non-tradable services account for one-third of China's GDP. State-sector restructuring, the resulting unemployment, and the government's ef-

"The WTO agreement would allow after-sales service of Kodak equipment, such as x-ray equipment, sold to Chinese customers. It would...significantly increase the number of foreign movies (most distributed on Kodak print film) shown in China.

Eastman Kodak Co.

"We believe opening the telecommunications service industry will be good for consumers, good for business, and good for the industry overall."

Art Kobler, President, AT&T China

"The agreement to bring China into the World Trade Organization...opens up vast new markets for US goods and services, and I have supreme confidence that America's highly skilled and productive workforce will win substantial new business in those markets in years to come."

Philip M. Condit, Chairman and CEO, The Boeing Co.

forts to strengthen its social safety net, will continue to be drags on economic growth in the short term and even after accession.

The test of success

In general, corporate reaction to the agreement has been positive. But a number of questions remain, mainly over the details, definitions of key terms, and, of course, the speed of China's eventual implementation—and these questions apply as much to Chinese as foreign firms. Most US companies currently operating in China are taking a wait-and-see approach, pending public release of further details of the bilateral agreement; the eventual accession protocol terms; and the granting of PNTR to China by the US Congress.

WTO accession offers a window of opportunity for US firms. But it is up to the companies to take advantage of it, and work closely with PRC regulatory officials. Both established American companies in China and newcomers will have to define their investment objectives clearly in China's changing marketplace—at the same time securing the resources to build and maintain strong local organizations. Even though WTO rules may enable foreign firms to enjoy far more market access and flexibility than in the past, the absence of a well-thought-out business plan that takes the realities of the PRC market into account will still result in disappointment.

WTO Accession: China's Next Steps

The Protocol of Accession package

WTO rules permit any country or separate customs territory to accede to the organization if the country or customs territory exercises autonomy over its external commercial relations and other matters covered by the WTO Agreement. The applicant government begins the process by providing a working party of WTO members with a memorandum covering all WTO-related aspects of its economic and trade policies. The working party then examines the application on the basis of the information in this memorandum. The applicant and working-party members negotiate and conclude a Protocol of Accession (POA), which includes the legally binding terms and conditions that will govern the applicant's accession.

The POA package consists of three parts: the Protocol itself; the Working-Party Report; and the market-access schedules for agricultural goods, manufactures, and services. The applicant and working-party members negotiate the protocol and working-party report multilaterally.

- **The Protocol** includes the applicant's specific commitments on particular issues that the working party believes are not addressed adequately in the WTO Agreement. Working-party members also agree on special transition periods or other special conditions.
- **The Working-Party Report** includes so-called "commitment paragraphs" as referred to in the Protocol; these legally binding commitments may be enforced through the WTO dispute-settlement mechanism. The report also describes the applicant's trade regime, makes statements regarding the applicant's intentions to implement the protocol and the WTO Agreement, and contains statements from working-party members regarding the applicant's various commitments.
- **The market-access schedules** cover commitments on agricultural products, industrial manufactured goods, and services. Negotiated bilaterally, these schedules focus on goods and services of particular interest to each working-party member. After these bilateral negotiations end, the WTO Secretariat consolidates the schedules by incorporating the applicant's best offer on each item into the Protocol.

Submission of the Working-Party Report, Council Vote, and Deposit of Instrument of Ratification

Working-party members must reach consensus on the draft POA package before it can be sent to the WTO General Council for approval. Although the General Council typically approves protocols by consensus—meaning no member present objects—any WTO member may request a vote by the entire WTO membership. If a member requests a formal vote, two-thirds of the membership must vote in favor to approve an applicant's accession. After receiving approval, the applicant must make any policy, legal, or regulatory changes necessary to implement the Protocol, as well as those WTO Agreement provisions that become effective immediately upon accession.

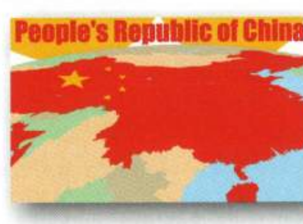
When that process is complete, the applicant then files its Instrument of Ratification—a document accepting the Protocol and WTO Agreement—and becomes a WTO member 30 days later.

The status of China's accession

An original signatory to the 1947 General Agreement on Tariffs and Trade (GATT), China was represented by the Nationalist government until it withdrew in 1949. The PRC applied to resume China's status as a contracting party in 1986. China's working party was established in 1987 and to date has met formally more than 20 times. When the WTO was established to succeed the GATT on January 1, 1995, China asked that its GATT working party be converted to consider China's terms of accession to the WTO. In the ensuing years, Chinese negotiators and working-party members made substantial, steady progress on both the Protocol and the Working-Party Report.

On November 15, 1999, US and Chinese negotiators reached agreement on bilateral market-access and selected protocol commitments, setting the stage for the remaining members that have requested negotiations with China. As of November 15, 1999, some 22 members had made such requests, but most analysts expect the bilateral negotiations between China and Brazil, the European Union, India, and Norway to be the most substantive and time-consuming. With the US bilateral agreement setting the parameters of China's commitments for most sectors, and the negotiations with the European Union and large trading nations perhaps improving China's offer in some areas, most of the remaining members are expected either to sign bilateral agreements quickly or withdraw their requests.

After the conclusion of these negotiations the working party can move to the next stage of China's accession process, as described above.



Taiwan's accession

An important trade power in its own right, Taiwan has also sought membership in the WTO, which does not require statehood for membership.

The accessions of the PRC and Taiwan have been entangled in political delicacy since PRC (GATT) negotiations began in 1986. The tacit understanding among key WTO trading countries and customs territories has been that the PRC and Taiwan should enter simultaneously, or, failing that, at virtually the same time, with China entering first and Taiwan shortly after. With the US-China agreement signaling that the PRC accession process will now move forward, some political obstacles to Taiwan taking the same steps now seem to have been cleared.

According to Taiwan authorities, Taiwan has concluded bilateral market-access agreements with all WTO members that requested such negotiations, except the Hong Kong Special Administrative Region. Hong Kong does not necessarily have to sign as long as it joins the consensus in the Taiwan working party and in the General Council. Taiwan trade authorities were hoping to convene a working-party meeting in December 1999 to move the island's accession process forward.

China's Accession to the WTO and PNTR

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WTO SPECIAL REPORT

WTO Basics

The WTO was founded January 1, 1995, to replace the GATT. Though foreign companies may differ over what they consider the most important WTO obligations for their China business, the PRC will have to abide by all of the agreements below, subject to certain phase-in periods. The agreements address not only trade in goods and services, but also trade in agricultural goods and textiles, as well as a range of non-tariff barriers. The WTO consists of agreements that ensure Most Favored Nation status (Normal Trade Relations [NTR] in US law), national treatment, and transparency.

NTR, national treatment, and transparency

The WTO requires that members not discriminate against any trading partners and that members accord national treatment to foreign goods and services. All agreements under the WTO are designed to protect these principles.

Article I of the GATT spells out the Most Favored Nation principle, namely that members are bound to provide the products of each member tariff treatment no less favorable than that accorded the products of any other member. Article III of the GATT requires that once imports have entered a market, they be treated no less favorably than equivalent domestically produced goods. The General Agreement on Trade in Services (GATS) and the Agreement on Trade-Related Aspects of Intellectual Property (TRIPs) also incorporate these concepts into their obligations. The GATS permits members to include in their schedules of commitments the service sectors to which they will accord national treatment. The GATS does not require that members accord national treatment for any service, including distribution. This must be negotiated.

Transparency, or full access to information on the laws and regulations with which a host government requires compliance, is another principle taken into account in many WTO agreements.

Country status

The WTO has defined categories, based on levels of economic development, to allow members some flexibility in phasing in certain obligations. More than three-quarters of WTO members are developing or transition economies. The definitions of these terms—developed, developing, and least-developed—are less than clear-cut, however. Where China's negotiations are concerned, whether the WTO confers developing country status on China will mainly affect the length of the phase-in periods for certain obligations.

Tariff agreements

The Uruguay Round agreement of the GATT mandates the reduction of developed-country tariffs to a trade-weighted average of 3.8 percent by 2000. By that time, 44 percent of developed-country imports of industrial goods will be duty free. The Information Technology Agreement calls for a phase-out of import duties on information-technology products by 2000, though some members will have until 2005.

Additional agreements address various categories of products. For instance, many of the major industrialized countries have agreed to tariff harmonization for selected chemicals and "zero-for-zero" tariff commitments that would reduce to zero tariffs on certain beer, construction equipment, distilled spirits, farm machinery, furniture, medical equipment, paper, pharmaceuticals, steel, and toy products. Developing countries' tariff rates on industrial products were cut 30 percent to a 6.3 percent weighted tariff rate by 1999, unless otherwise specified in the member's schedule.

The Uruguay Round also attempted to reduce uncertainty surrounding future tariff levels by increasing the number of products subject to "bound" tariff rates, or rates that members cannot raise above designated levels without compensating affected parties. All agricultural tariff levels are bound. For developed countries, nearly all imports (99 percent) enter under bound rates, while for developing countries, 61 percent of imports by import value (73 percent of tariff lines) enter at bound rates. Economies in transition will raise their binding rates from 73 percent to 98 percent.

Agreements on trade in goods

- **The Agreement on Agriculture** requires WTO members to convert non-tariff measures into tariffs ("tariffication") and bind commitments in the areas of market access, domestic support measures, and export subsidies over a six-year implementation period from 1995-2000. Other requirements include curtailing the use of subsidies and other special treatment for domestic producers. Developing countries may have some flexibility in implementing reductions over a 10-year period.
- **The Agreement on the Application of Sanitary and Phytosanitary Measures** ensures that when members exercise their sovereign right to protect food safety, and plant and animal health, they do so based on objective scientific data, while ensuring these rights are not used for protectionist purposes.
- **The Agreement on Textiles and Clothing** establishes rules for liberalizing trade in textiles and clothing over a 10-year period beginning January 1, 1995, and integrates the Multi-Fiber Arrangement (MFA) into the rules of the WTO. Members can impose a "transitional safeguard" or temporary quota against import surges (of a specific product) that threaten to cause serious damage to domestic producers.
- **The Agreement on Trade-Related Investment Measures (TRIMs)** requires investment measures to be consistent with WTO provisions on national treatment (Article III, GATT 1994) and calls for the elimination of quantitative restrictions (Article XI, GATT 1994) within two years, unless there is a justifiable exception.

TRIMs explicitly listed in the agreement as inconsistent with national treatment include regulations that tie imported inputs to the amount of final product exported; restrict access to foreign-exchange based on foreign-exchange earnings; or that restrict exports either by volume or value.

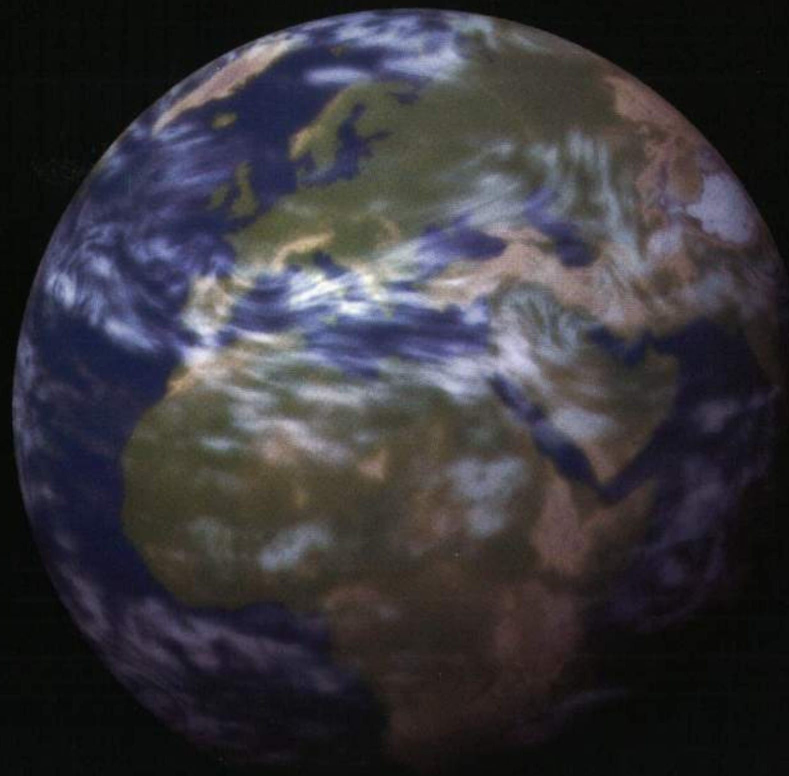
- **The Information Technology Agreement (ITA)** The Ministerial Declaration on Trade in Information Technology Products entered into force in 1997. The ITA, with 48 participants—including the 15 European Union members—addresses only tariffs on IT products. There are no binding commitments concerning non-tariff barriers, though there is room for review. ITA participants must agree to cover all products listed in the ITA declaration and to eliminate the tariffs for these products. All other duties and charges must be bound at zero. Participants may phase in implementation of sensitive products over a longer period of time.

Agreements on trade facilitation

- **The Agreement on Implementation of Article VI of GATT 1994 [Antidumping]** provides rules for calculating dumping margins and conducting investigations to protect exporters from protectionist measures.
- **The Agreement on Implementation of Article VII [Customs Valuation]** attempts to unify procedures for customs valuation by laying out, in hierarchical order, five methods to determine the customs value of imported goods:

1. The transaction value of the good itself;
2. The transaction value of identical goods;
3. The transaction value of similar goods;
4. The deductive method; and
5. The computed method.

Upon the request of importers, countries can value imports on the basis of the unit price of post-import sale if goods undergo further processing in the country of import.



● **The Agreement on Import Licensing Procedures** aims to prevent unfair trade barriers by simplifying import-licensing procedures.

The agreement includes provisions on neutral application and equitable administration of licensing procedures, transparency, application-submission timetables, foreign-exchange allocation for licensed imports, and the protection of confidential information.

The agreement outlines two types of import licensing—automatic and non-automatic. Under automatic import licensing, approval is granted in all cases, and there are no restrictive effects on imports. Such systems may be maintained as long as underlying administrative goals cannot be achieved in a more appropriate way. Under non-automatic import licensing, the country should ensure transparency by publicizing information concerning administration of restrictions, licenses granted over the most recent period, and, where practicable, import statistics of the products concerned.

● **The Agreement on Preshipment Inspection** provides a framework of rights and obligations to ensure that inspection requirements are not used as trade barriers. The agreement includes provisions on national treatment, non-discrimination, and transparency (including procedures and criteria for inspection). All information collected in the course of preshipment inspection should be treated as confidential, and procedures must be established to protect confidentiality and avoid conflicts of interest.

● **The Agreement on Rules of Origin** attempts to unify rules covering MFN, antidumping and countervailing actions, safeguard measures, and discriminatory restrictions to ensure they are not used to restrict or distort trade flows.

● **The Agreement on Safeguards** establishes ground rules for imposing safeguard measures against import surges that threaten to cause "serious injury" to domestic industry.

● **The Agreement on Subsidies and Countervailing Measures** strengthens the GATT rules and expands the scope of prohibited subsidies. The agreement is constructed to ensure that "specific" subsidies do not harm the interests of members, and that countervailing measures do not unjustifiably impede trade. The agreement also offers guidelines for providing relief to producers adversely affected by subsidies.

● **The Agreement on Technical Barriers to Trade** establishes transparency and consultation requirements for members' development of technical standards to ensure that industrial standardization, safety, and environmental regulations are not used as non-tariff barriers to trade.

● **The Regulation of State Trading Enterprises (STEs)** is addressed under Article XVII of GATT 1994. The article defines STEs and requires that their operation not violate WTO principles or rules.

Services agreements

● **The General Agreement on Trade in Services** extends GATT conditions on national treatment, market access, and MFN to trade in services and establishes a framework for liberalization. It contains specific annexes on air transport, basic telecommunications, and financial services. The scope of GATS is limited, and members have considerable flexibility in identifying which specific services will be obligated to meet MFN requirements. To enhance transparency, however, each member must establish within two years a liaison office to provide information on laws, regulations, and guidelines that affect trade covered by specific commitments.

Within GATS, there is some flexibility for members to specify temporary exemptions from MFN treatment in certain services and with certain trading partners that benefited from favorable treatment before WTO accession. These exemptions are subject to review and cannot be extended or added to.

Since the Uruguay Round, additional negotiations have taken place on:

● **Basic Telecommunications Services**, which led to an annex to GATS that took effect in 1998. Under this annex, members agree to provide schedules that state which services they will open to foreign participation.

● **The Financial Services** agreement took effect in 1997. This agreement similarly calls for members that sign on to the protocol to provide liberalization schedules.

Other discussions that have taken place have addressed maritime transport, and movement of natural persons (temporary stay of foreign service providers in a member territory), with mixed results. Talks on subsidies, government procurement, and safeguard measures; and qualification requirements, technical standards, and licensing requirements are also on the drawing board. A working party on professional services has issued non-binding guidelines for members negotiating accounting-sector qualifications.

Other key agreements

● **The Agreement on Trade-Related Aspects of Intellectual Property Rights, Including Trade in Counterfeit Goods (TRIPs)** requires WTO members to provide MFN, national treatment, and high levels of IPR protection and enforcement for copyrights, trademarks, geographical indications, industrial designs, patents, layout designs of integrated circuits, and trade secrets. Members must implement TRIPs within one year of accession.

The minimum standards of protection build upon existing international conventions negotiated under the World Intellectual Property Organization, including the Berne Convention on Protection of Literary and Artistic Works, the Paris Convention on the Protection of Industrial Property, and the Washington Treaty on Intellectual Property in Respect of Integrated Circuits.

● **The Dispute Settlement Understanding** lays out a timetable for the WTO's multilateral dispute-resolution mechanism. The Dispute Settlement Body (DSB), which is responsible for carrying out the process, establishes panels to consider each case, and either accepts or rejects the panels' findings.

The process consists of two stages. The first, consultation stage, is supposed to take 60 days and involve direct talks between the two sides. The second stage calls for formation of the panel (45 days) and hearings and rebuttals over six months, after which the panel submits its final report to the disputing parties. Three weeks later its final report is due to the WTO membership; unless a party appeals, the DSB adopts the report 60 days later. The complete process can take one year, without any appeals. Appeals can lengthen the process another three months.

Other agreements include the Trade Policy Review Mechanism, and two plurilateral trade agreements, which are binding only on members that voluntarily accept them:

● **The Agreement on Trade in Civil Aircraft** provides internationally recognized disciplines on aircraft trade and calls for the binding of tariffs on aircraft and the elimination of duties on aircraft components.

● **The Agreement on Government Procurement** lays out general rules and obligations to ensure non-discrimination and open competition for government contracts in goods and services.

SOURCES: "Joining the World's Trading Club," *The China Business Review*, May-June 1997 (*www.uschina.org/cbr/members/9705/gelb.html*); *China and the WTO: A Reference Guide*, The US-China Business Council, 1996 (*www.uschina.org/members/washington/position/wtoref.html*); the World Trade Organization website (*www.WTO.org*).

WTO SPECIAL REPORT

The Impact of WTO Accession on China

China will benefit from entering the WTO, but the benefits will not be equal in all industries. Because import quotas on food and agriculture products will be removed, domestic production will drop by 2005.... But even when China opens the market, China will still be able to supply over 92 percent of its food needs.

Economic Impact on Entering WTO, report by the State Council Development Research Center

The demand of some industries in the international market may lead to PRC capital outflows.... Because of tariff reductions, Chinese products will have more opportunities to enter international markets... Demand for consulting services will increase.... Organizations that address anti-dumping and international conflict management may be established.

Translated from "The Big Turning Point" by Cheng Gong, June 1, 1999 issue of China City Publication

While the direct effects of the bilateral agreement on China may take some time to emerge, one thing is clear: China will have to pick up the pace of reform to meet WTO requirements. China's ongoing reforms of its financial sector, state-owned enterprises (SOEs), and social-welfare system have slowed growth considerably, though recent improvements in the export picture could provide some relief next year. But many sectors will experience even sharper pain before the economy benefits from WTO membership.

The procedures China must complete before acceding to the WTO will take at least six months, however. It will also take time for China to reconcile its domestic laws and regulations with its international commitments. The pre-accession period will allow the PRC government to educate the population and bureaucracy about the commercial implications of WTO accession, and will give Chinese businesses a bit of breathing room to prepare.

The WTO effect

Employment

According to the World Bank, China has 140 million surplus workers and an estimated 16 to 18 million unemployed urban workers. In addition, 100 million rural workers are estimated to be out of work seasonally. Workers in China's state- and collectively owned sectors have been hit the hardest since the mid-1990s, and farmers will suffer greatly from foreign competition once China joins the WTO. An estimated 10 million will be pushed out of agriculture. Boosting employment, and building a social safety net, will remain top priorities for the central leadership.

In the long run, opening China's economy should generate employment, particularly in labor-intensive service industries. The service sector is expected to gain 2.7 million jobs over the next seven years, while industries in which China has a competitive advantage, such as garments, textiles, shoes, and toys, are expected to add another 5.4 million jobs. As China downsizes the state-owned sector, foreign firms will be a key source of new, well-paying jobs for local Chinese. Entrepreneurs will also benefit from new business opportunities generated by the overall expansion of the market.

Industry restructuring

Severely inefficient industries plagued with overcapacity include aluminum, autos, cement, light industry, petrochemicals, and steel. These sectors will continue to struggle in the months and years leading up to the WTO's implementation in China, which will bring phase-outs of state subsidies and greater competition. Many small or inefficient firms will sink or be swallowed by

Wang Yang, president of the Orient International (Holding) Co., Ltd., a state-owned foreign trade company, said that China's accession to the WTO will further prompt Chinese enterprises to operate according to international practices and will sharpen China's competitive edge in the global market.... Wang Yaotian, director of the WTO Shanghai Research Center, China's first institution specializing in WTO research, said that China's entry into the WTO will benefit the country in nine areas: overseas investment, exports, state-owned-enterprise reform, increased domestic demand, job creation, raised living standards... and a thriving stock market.

Xinhua News Agency

Li Zhengqin, of the China Light Motorcycle Group, said WTO entry would have little impact on domestic motorcycle enterprises. With the lowering of tariffs and the gradual elimination of quotas, the cost of imported spare parts and accessories for the motorcycle sector will be reduced, and the prices of motorcycles will also be reduced.

Beijing China News Agency

...Intensified competition following the country's entry into the World Trade Organization (WTO) will force the country's airlines to fly high. But...in the near future, foreign airlines may be flying even higher. To support the country's WTO accession talks, the Civil Aviation Administration of China has promised to open its aircraft-maintenance and computerized seat-booking system services to the world.

China Daily

"As long as we improve our attitude and the quality of service, I think ordinary Chinese people will be willing to buy domestic insurance," said Ma Yongwei, chairman of China Insurance Regulatory Commission [CIRC]. Local insurance firms currently enjoy a nearly 99 percent market share thanks to restrictions on foreign companies.... Ma said there was a "big gap" between Chinese and foreign insurers in terms of service, experience, and managerial know-how, but domestic firms need not lose out. "As long as CIRC works hard, insurers set stringent requirements for themselves, make rules more complete, and nurture more professionals, I don't think China needs 10 or 15 years to catch up with foreign insurers," he said.

Reuters

Guangdong must be gradually, and in a truly all-round manner, incorporated into the global economy.... Guangdong will develop under a new policy setting and law of development. A full assessment of these [issues] is more important than merely estimating which industries will gain and which industries will be shattered.

Beijing People's Daily

"The fierce competition in the economic sector inspired by China's entry into the WTO will require China to further improve its services and readjust its financial structure and operational system," said Dr. Pei Ping, dean of Finance Department, Nanjing University.

Xinhua News Agency

larger ones, but those that survive will be better able to compete internationally.

Sectors now under tight government control, such as telecommunications, will eventually be cut loose. Firms that are already profitable will almost certainly do well, but even lagging firms and sectors could benefit from new investment, whether domestic or foreign.

● Private industry

If competition—from both foreign and private Chinese firms—serves to hasten the restructuring already under way, Chinese private and entrepreneurial companies could find the business environment much more hospitable. The key will be whether banking reform and WTO obligations combine to improve the funding sources available to non-state firms.

● Financial-sector reform

China has taken a number of steps in recent months to relieve the banks of severe indebtedness (*see The CBR*, November-December 1999, p.16). Though domestic banks remain technically insolvent, greater foreign participation is unlikely to destabilize the banking system. In fact, WTO-induced liberalization should aid China's reform efforts. Foreign players will bring greater transparency and will improve liquidity. Foreign firms will also bring internationally standard models of financial management.

● Economic efficiency

According to the PRC State Council-affiliated Development Research Center (DRC), implementation of the WTO agreement will raise economic efficiency and contribute to GDP. The changes brought about by WTO would "lift total investment by 1.75 percent in 2005 over what it would be that year without WTO membership." Some analysts forecast that by 2005 China's GDP could increase three percentage points, to create nearly 10 million jobs, and nearly double trade to $600 billion.

● More diverse sources of growth

Once China completes its implementation of WTO obligations, the economy could end up less reliant on foreign trade. Though there will be significant gains for exporters, the export-oriented economy is already internationally competitive. The greatest efficiency and output gains will occur in domestically oriented, non-tradable sectors—namely services.

● Consumption

The big winners in the short term will be China's consumers. Low tariffs will make foreign goods, and eventually services, more widely available and affordable. In addition, competition will lead to lower costs and better service overall, especially in telecommunications and finance.

● Rural economic growth

China's rural economy supports over 900 million Chinese citizens. WTO-induced restructuring will force millions off the farm, but could bring investment to rural areas and generate non-agricultural employment opportunities. Many analysts expect investment incentives for rural and remote areas to remain in place even after China accedes to the WTO.

The economy and enforcement

Accession will lock in China's reform program by binding the country to WTO obligations. These obligations will present Beijing with an added authority with which to compel domestic industry and government ministries to comply with reforms. Central-government efforts could meet pockets of resistance in particular ministries, sectors, and localities, however. Indeed, some foreign investors are preparing for implementation to progress slowly at the local level. No matter what the pace, however, China's implementation of WTO obligations will contribute to the dramatic economic changes sure to occur over the next decade.

EMPLOYEE BENEFITS

After China enters the WTO, massive imports of turbine compressors, top-loading washing machines, air-conditioner compressors, and magnetrons may impact domestic manufacturers...[and] the internationalization of the domestic market for light-industry products will intensify market competition and accelerate enterprise restructuring. Some may go bankrupt....

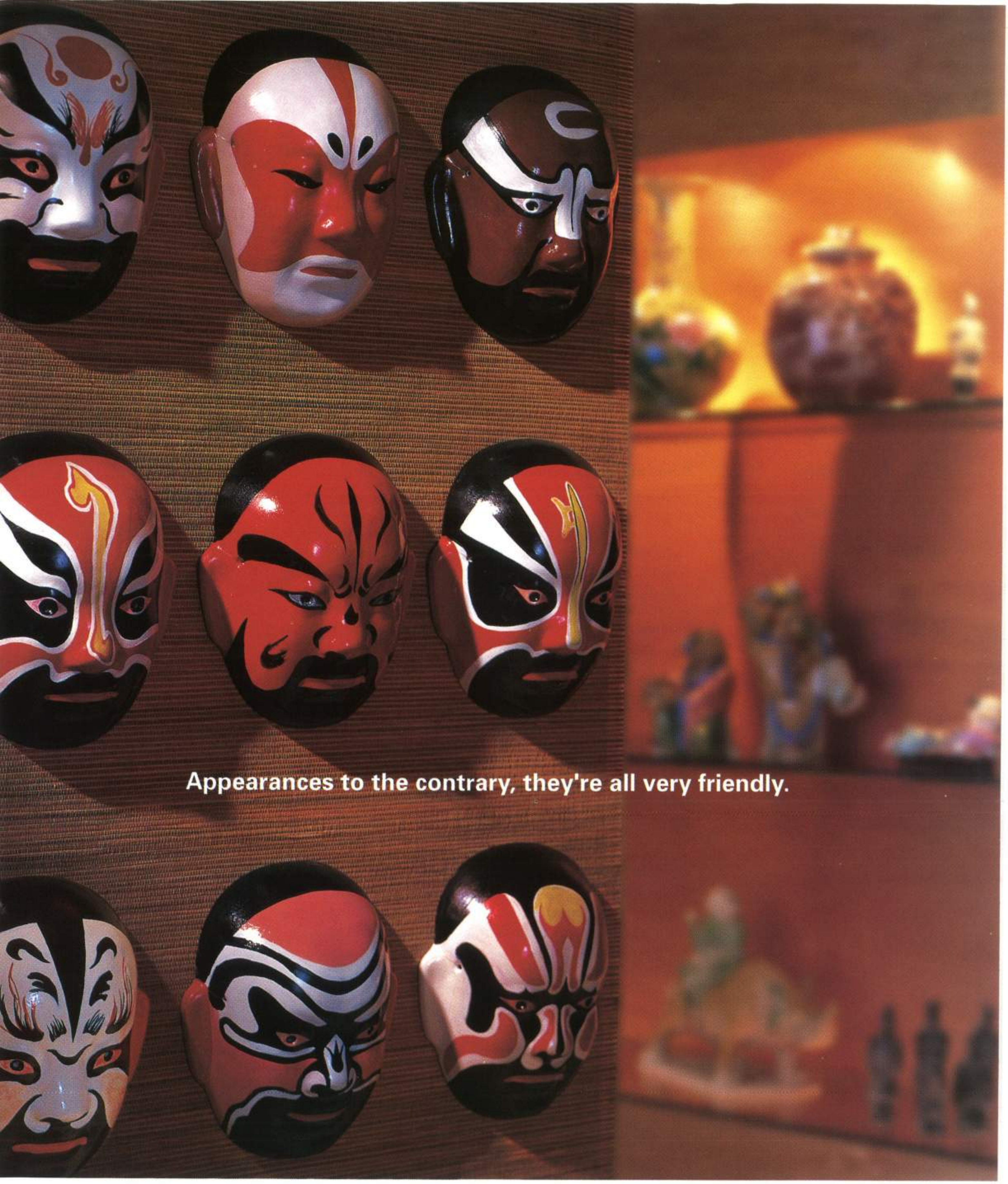
China Business Times, as translated and published by Sinofile Information Services Ltd.

"Changing state ownership into some kind of shareholding company may enhance corporate governance and improve management," said Zhou Xiaochuan, chief executive officer and president of the China Construction Bank.... A shareholding structure would also create the preconditions for possible joint ventures with foreign banks, and for stock-market listing.

Financial Times

Liu Chuanzhi, president of Legend Co., which has the largest share in China's computer market, says domestic companies will not lose to foreign giants.... He says though foreign companies have advantages over domestic counterparts in regards to capital and technology, domestic companies know China's market better.

Beijing Youth Daily, as translated and published by Sinofile Information Services Ltd.



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WTO SPECIAL REPORT

China's Track Record in the Global Economy

Margaret M. Pearson

China's past behavior in the global economy shows that the country is likely to conform to WTO norms

Debate rages over whether China will be a cooperative player in the World Trade Organization (WTO), or whether it will attempt to thwart the rules of the game established by the existing WTO members. As the world and the US Congress consider China's likely behavior in the WTO, it is often forgotten that post-Mao China does in fact have a track record in the global economy that dates back two decades. Rather than ignore that track record, it is instructive to examine it for both the confidence it can offer in predicting China's future behavior and the hints it provides as to where difficulties may arise.

China has acted in its own interest...

It would be naïve to think that China's rapid integration into the global economic system has been driven by anything but self-interest. As Yong Wang's article (*see* p.54) makes clear, even economic liberals in China believe that the first goal of economic policy should be to create a strong industrial economy that can carry China into the future. There is continual debate within the PRC, at all levels of government and society, over how best to achieve this goal. In this respect, China is no different from any other country, including the United States.

...but has not been a "system buster"

Yet in its attempt to create a modern economy through economic integration with the outside world, China has not been a disruptive power. China has adapted to the existing system, not vice versa. Moreover, throughout the integration process thus far, the global trade, investment, financial, and institutional systems have remained stable, and have proven quite capable of handling this newcomer.

In understanding China's track record, it is useful to look at three distinctive types of interaction: business-to-business transactions, PRC policymaking on trade and investment, and the PRC's posture in international economic organizations.

Business transactions

A simple and powerful—but too-often overlooked—point can be made about China's commercial dealings: in merely 20 years, the volume of business-to-business transactions engaged in by PRC firms has risen from zero or nearly zero to among the highest in the world. Its annual foreign trade rose from a mere $21 billion in 1978 to $324 billion in 1998. Even more dramatic, the amount of incoming capital rose from zero in 1978 to a high of about $110 billion in 1993, though it has hovered around $50 billion in each of the past several years. In the early and mid-1990s China was second only to the United States as a recipient of foreign direct investment (FDI).

Granted, a significant portion of this amount was (and to some degree still is) attributable to "round-tripping"—efforts by PRC firms to send money abroad and then reinvest it in China under the more favorable terms offered to foreigners. Yet the basic point—that the amount has increased dramatically—cannot be ignored. China's investment abroad has also risen from a handful of politically motivated aid projects to commercial business ventures.

In the last 10 years, China has become a commercial borrower of note in the financial markets, though it experienced some fallout from the Asian financial crisis. And China has participated in international capital markets by issuing both stocks and bonds overseas. In the 1990s it became one of the few transition economies with an investment-grade credit rating on its sovereign external debt, currently rated "BBB" by Standard and Poor's Corp.

Beyond the story told by the sheer volume of activity, there is also evidence of the *kind* of actor China has been. The market is a natural, quick, and unbiased enforcer of its own rules. It is an enforcer that the Chinese, for the most part, accept; in stark contrast to the days of Mao, current Chinese leaders tend to view market norms and market enforcement as neutral and apolitical. Indeed, the Chinese are keenly aware that there is nowhere else but the established international market for them to go.

Moreover, the rapidity of China's integration into the world economy has not torn the global system apart or even made it list unsteadily. It is the Chinese who have traveled up the learning curve. Of course, there have been market dislocations to some producers as competition from Chinese goods has emerged, particularly in East and Southeast Asia. Yet this is a natural occurrence in global markets.

Evolution of PRC policies

When China first decided in the late 1970s to open its economy to the outside world, Chinese leaders argued to internal critics that by using strong regulatory controls it would be able to absorb the benefits of integration while avoiding the harmful effects on China's economy, sovereignty, and culture. In pursuit of this goal, the government established a host of regulations designed both to attract and control foreign business.

Since that time, however, the overall pattern has been one of erosion of such controls and greater acceptance of the norms of the global

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The rapidity of China's integration into the world economy has not torn the global system apart or even made it list unsteadily. It is the Chinese who have traveled up the learning curve.

trade regime. Chinese reformers, disappointed in the levels and quality of incoming investment—particularly from the West and Japan—not only clarified but also eased controls. Changes have occurred in numerous sectors and functional areas, including restructuring and decentralization of the foreign-trade system, tariff reduction, liberalization of controls on foreign exchange and profit-repatriation, greater transparency, and the establishment of rules for dispute resolution and contract enforcement. Foreign companies have gained greater market access in sectors including light industry, foodstuffs, automobiles, petroleum, chemicals, and (more recently) financial and other information services.

Some liberalization came in the wake of acrimonious disputes with the United States. This was the case, for example, with changes made in the domestic regime for intellectual property rights (IPR) protection. What is often forgotten amid the ongoing tension is that China has made far-reaching changes in its basic conception of IPR protection, and the resources it has devoted to it, since 1979. The official norm has moved away from the view of intellectual creations as social goods subject to state control and toward the view of intellectual creations as the property of the creator. China has drafted numerous domestic regulations on copyright, trademarks, and patents; established institutions responsible for oversight and enforcement; and joined a number of international conventions and organizations, such as the World Intellectual Property Organization (*see The CBR*, January-February 1998, p.16).

Direct pressure was not the only impetus for many of China's policy changes; liberalization also took place with an eye toward China's bid for eventual WTO membership. Chinese leaders recognized that they not only had to "talk the talk" by promising changes at the negotiating table, they had to "walk the walk" by introducing concrete policy shifts. Indeed, while outside pressure has been instrumental at some junctures in influencing change in Chinese policy, virtually none of these changes would have occurred if economic reformers did not believe that, on the whole and in the long run, they were best for the Chinese economy.

Liberalization of the regulatory environment has not been without its ups and downs, of course, and some industries have benefited more than others. Moreover, China has by no means given up all efforts to tailor regulations to meet its development goals. Yet the effort to make China a more hospitable environment for foreign capital, both in terms of rules at the sovereign level and operations on the ground, has continued slowly and steadily. Even after the events at Tiananmen in 1989, government reformers made substantial efforts to protect foreign business from adverse reaction by conservatives, and made it a point to continue with liberalization.

China's behavior in international organizations

China's likely behavior in the WTO is also predictable based on its record in other international economic organizations, particularly the World Bank and International Monetary Fund (IMF). Here, the record is unambiguous. To use the terminology Samuel Kim, senior research scholar at Columbia University, applied to China's role in the United Nations, China has become a "system maintainer" rather than a "system transformer" (*see China Joins the World: Progress and Prospects*, Council on Foreign Relations, 1999).

The World Bank's experience with China is extensive. Since joining the bank in 1980, China has acquired long-term funding, technical assistance, and strategic advice on reforming its economy. The bank has become China's largest single source of long-term foreign capital, and China became the bank's largest client in 1993. As of June 1999, the bank had committed a total of $32.5 billion to China.

World Bank officials often cite China as a model member. The quality of the bank's project portfolio in China is one of its best. According to bank officials, China projects are well implemented, within budget, and on time, and China has grown from a quiet presence to a mature partner. Over time, the Chinese officials and economists posted to the bank have gained confidence as well as knowledge, and have become more able to contribute to the bank's daily operations.

China's profile has been lower in the IMF. The PRC has borrowed minimally and repaid immediately. More important, China has been an active recipient of IMF advice, particularly in the steps it has taken toward currency convertibility.

China is not perceived as a disruptive force in either of these institutions. Rather, China has absorbed the advice offered by experts in these organizations and has made institutional changes in its own governing structure to accommodate their presence. The World Bank and IMF have

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In domestic debates in particular, Chinese officials were able to use World Bank and IMF standards in conjunction with China's desire to be an accepted member of global organizations as an impetus for economic liberalization.

served as a kind of airlock between the Western financial world and China, providing Chinese reformers with a training ground and a cushion until they could bring their personnel and expertise up to speed. Far from resenting these foreign institutions, Chinese reformers often have benefited from China's participation in them. In domestic debates in particular, Chinese officials were able to use World Bank and IMF standards in conjunction with China's desire to be an accepted member of global organizations as an impetus for economic liberalization.

Problem areas should not be ignored

In understanding how much China has adapted to the existing global economic system, it is important to remember that reforms in the country's foreign economic and trade policy continue to be works in progress. The effective transmission and enforcement of central-level laws and policies to the local level remains a particular concern for businesspeople. This means that China's development of a legal environment supportive of contract enforcement and dispute adjudication must continue in all areas of the country. Such problems still plague efforts to support IPR protection in China, for example (*see The CBR*, January-February 1999, p.8).

Though China's legal enforcement record is improving, it remains spotty and haphazard. These changes take time, of course; the notion that major institutional and normative developments such as the rule of law can take place overnight is unrealistic.

The fractiousness within China over trade policy also remains a concern, and cannot be expected to wane soon. It is somewhat ironic that the more extensive the exposure of Chinese industries to the global economy, the more those industries that stand to be hurt by competition—such as automobiles and telecommunications—have mobilized to protect their own interests. This phenomenon contributed to the slow pace of China's WTO accession negotiations.

Because of China's complex political environment and its still less-than-ideal state of institutional development, there will continue to be a role for pressure from external institutions. At the same time, having China as a member of global institutions allows for a partnership with government reformers and businesspeople inside the PRC who have used and will continue to use external expectations to press for internal change.

Will China be a responsible WTO member?

Thus, despite the remaining problems and the clear role for continued monitoring of Chinese behavior by the WTO and its members, China's past record is quite clear: the country has shown itself able to meet the expectations of the global economic system, whether measured at the level of business transactions, government policy, or behavior in international financial institutions. China's integration into the world economy, far from being apocalyptic, has been accomplished with little of the friction predicted of a rising power.

It would be foolhardy to give Pollyanna-ish predictions about China's behavior, for China will continue to operate in its own interest. But China has gone far in its WTO offer to indicate that it is willing to play by the rules. And its behavior over the past 25 years gives foreign companies ample reason to expect strong efforts to live up to those commitments.

China's Domestic WTO Debate

Yong Wang

In the face of tough decisions, China has opted for greater openness—but an old debate remains unsettled

China's accession to the World Trade Organization (WTO) has not only been a source of concern within the PRC's political bureaucracy. It has also animated conflicts over national economic policy—namely, the ongoing debate over which economic development strategy will be most successful for China and the role foreign direct investment (FDI) plays in these strategies.

This internal discord has been the primary reason for the slow pace of China's bid for WTO accession, as WTO membership implies not only tariff reductions, but also greater market access for foreign investors. Some in China are concerned about the weakness of state-owned enterprises (SOEs) when faced with competition from foreign investors. Others see exposure to foreign competition as the only way for the PRC economy to develop successfully.

Though China has moved ahead with its WTO bid, these debates are far from over and will continue to play out as China completes WTO accession and moves to implement its obligations. It is therefore useful for China business observers and practitioners to keep a close watch on the impact of these debates on Chinese economic policy.

The foreign investment juggernaut

Since the early 1990s, FDI has been the major form foreign capital has taken in China. According to PRC statistics, China has used $242.4 billion in FDI since 1992, ranking only behind the United States as a destination for investment. According to a PRC State Statistical Bureau study, before 1992 international indirect investment, including foreign loans, was as high as 60-70 percent of all foreign capital entering China. FDI reached 72 percent of all foreign capital in the country between 1992 and 1996, and was nearly 78 percent in 1998. More than 200 *Fortune 500* companies have entered China. Together, they operate approximately 45,000 factories, branches, and offices on the mainland.

The government faces strong domestic pressure to balance opening against the need for protection, and has regularly had to launch information campaigns to educate the general population on how FDI has helped power the growth of the Chinese economy. Nevertheless, FDI inflows, though supported by the PRC government, have provoked a rise in economic nationalism at all levels of society, from economists, government officials, and the media elite to entrepreneurs and common citizens.

Despite its conservatism, this economic nationalism does not support simply closing the nation's door to foreign investment. Rather, it advocates economic independence and the idea that Chinese must be the masters of their own economy. In general, economic nationalists believe that China must encourage domestic investment and indigenous economic development because the goal of most foreign investors is to profit from, not strengthen, China's developing economy.

Liberals, on the other hand, believe that foreign investment may be the best and quickest way to develop the Chinese economy and strengthen the country as a whole. Proponents of this view are also found at all levels of society.

Three rounds of debate

In an attempt to analyze the pros and cons of FDI, economic nationalists and liberals have fought three rounds of debate over the past five years, which have focused on the following questions:

- Should China protect SOEs or the national economy from the competitive threat that FDI represents?
- Should the government open markets to domestic investors before opening them to foreign investors?
- What benefits do FDI and multinationals bring to the country?

The different answers each side gives to those questions have influenced both China's economic development strategy and its policy toward WTO accession.

The first round of heated debate on the role of FDI, which began in 1994 and culminated in 1996, was set in motion by great numbers of foreign-invested enterprises (FIEs) winning large shares of the PRC market. FIEs began to enjoy dominant positions in the auto, electronics, detergent, and beverage sectors, among others. The 15th Communist Party Congress closed this round of debate in 1997 by declaring certain strategic sectors off-limits to foreign investors. One manifestation of this conservatism was the Catalogue Guiding Foreign Investment in Industry, originally drawn up in 1995 and updated and revised in 1998. The catalogue seeks to direct investment to sectors that need it most and prevent further investment in sectors nearing, or beyond, saturation. Investments in "encouraged" sectors—generally high-tech projects and those in less-developed regions—receive preferential treatment, while those in "restricted" sectors are only approved under certain conditions. "Restricted" sectors are further divided into "A" and "B" lists, requiring provincial and national ap-

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proval, respectively. A third category prohibits foreign investment in services and internal trade, including distribution. Perhaps more important, the government began to encourage mergers and acquisitions among SOEs in all industries to improve economies of scale, as well as create competition in industries, such as telecom, which were virtual monopolies (*see* box).

In early 1998, the second round of the debate was triggered by the Asian financial crisis and the Chinese economy's downturn. Some economists and policy analysts believed that the financial failure throughout Asia justified their argument that economic globalization is dangerous and that Western financial speculators were conspiring to sabotage Asian economies. Economic nationalists seized the offensive by raising the critical issue of economic security, which naturally put liberals on the defensive. Liberals argued that the internationalization of China's economy should not be put on hold because of worries about economic security; rather, China should seek a balance between economic security and openness. They continued to urge that China work to attract more FDI and involve international financial organizations more actively in the economy.

The third and latest round of the debate began in April 1999 and is directly related to the US-China WTO negotiations. Some Chinese policymakers voiced strong reservations about the WTO offer Premier Zhu Rongji made in Washington last April. The NATO bombing of the Chinese embassy in Belgrade in May 1999 further fueled their suspicions, and even caused some liberal thinkers and officials to doubt the wisdom of their own position.

Economic nationalists advocate economic independence and the idea that Chinese must be masters of their own economy. Liberals, on the other hand, believe that foreign investment may be the best and quickest way to develop the Chinese economy and strengthen the country as a whole.

Tit for tat

The recent US-China bilateral agreement signals that the liberals have won this latest round. But a number of questions remain unresolved, including:

1 Are the concepts of "national economy" (*minzu jingji*) and "national industry" (*minzu gongye*) still meaningful today?

These two concepts were developed in the late nineteenth and early twentieth centuries, when China lost sovereignty to Western powers in regulating the trade and banking sectors, as well as tariffs. The PRC government has long embraced these concepts, with strong support from ordinary citizens. Today in China, a national economy—or national industry—is understood as one owned and run by Chinese citizens. To economic nationalists, SOEs represent the basis of China's national economy.

Economic nationalists argue that these concepts are still meaningful in the age of globalization. In their view, FDI must be limited to prevent harm to the national economy and SOEs. They insist that whether an industry is national or colonial depends on who owns a trademark, who controls and innovates technology, and who holds decisive economic power. The concept of national economy addresses the issue of who has economic sovereignty—implying majority control by the Chinese government or Chinese companies rather than FIEs or foreign governments.

Liberals argue that these concepts must be discarded because the political and economic conditions that led to the coining of these concepts have all but disappeared. Industrial integration, they contend, is an irreversible economic trend worldwide. National industry, if there is such a concept, should be based on the local content of products (some liberals suggest 50 percent or higher) or ownership share of enterprises.

2 Who takes advantage of whom?

Official PRC policy advocates the use of FDI to obtain know-how, management skills, and access to international markets. But economic nationalists harbor deep doubts about this policy. They argue that China's decentralized political and economic power structure allows leading foreign investors to dominate China's economy. Ministries and localities compete to offer preferential treatment for foreign joint ventures. As a result, venture negotiations tend to underestimate the value of Chinese patents, trademarks, and other property. Corrupt officials even reduce these values further, diverting funds intended for the central government to their own pockets. Thus, economic nationalists maintain that it is not Chinese enterprises that take advantage of foreign investors, but foreign investors that take advantage of Chinese enterprises.

Liberals counter that both sides benefit—the Chinese side gains access to capital, technology, and jobs, while the foreign side makes a profit. Liberal economists say failure makes for a steep learning curve, and Chinese inexperience in the global marketplace is temporary. FDI, they contend, is a normal economic activity, and only profits can attract and keep foreign investment.

3 Does the strategy of trading market access for technology work?

The government's strategy to attract FDI is to "trade markets for technology." Liberals are confident that granting market access to foreign investors will stimulate technology transfer to China. But economic nationalists ridicule this strategy as naïve.

Nationalists contend that foreign firms never sell the most-advanced technologies to China; instead, technology transfer wipes out China's capacity to develop indigenous—and possibly competitive—technologies. Foreign firms, they say, envision China as a market for Western second-class equipment and assembly lines. They

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cite examples of foreign firms' reluctance to support local suppliers of components and other manufactured inputs.

Nationalists point to post-WWII Japan and South Korea as successful models for China to copy. They see these two countries as having borrowed money to buy technologies that they then integrated into their economies. The nationalists praise this strategy of building economies from within rather than relying on FDI.

4 Are MNCs benign investors?

Liberals argue that China should concentrate on attracting capital from MNCs rather than from smaller-scale investors from Taiwan and Hong Kong. According to liberals, MNCs bring economies of scale to the industry they enter; continuous introduction of advanced technologies; accelerated industrial upgrades; and access to international production and marketing networks for domestic enterprises. MNCs also give Chinese professionals international business experience. Some liberal-minded officials even urge Chinese not to be afraid to work (*da gong*) for MNCs. Only those who learn the ropes inside an MNC will be able to lead an MNC in the future, they contend.

Nationalists argue that the final objective of multinationals is to dominate the Chinese market. It is impossible, they say, to build a strong and independent economy by relying only on FDI, especially investment from MNCs. Though MNCs stress free competition at this stage, nationalists believe MNCs will not abandon their instinct to dominate the market.

5 Is China a capital-scarce country?

It is a firmly held liberal notion that China is a capital scarce country. To develop the economy, liberals say, China has to attract foreign capital. (Liberals also point out structural barriers to domestic funding, such as the fact that most investment funds are funneled to SOEs through government directed lending.) Nationalists argue the opposite—that the absorption of excessive FDI crowds out domestic capital.

It is a firmly held liberal notion that China is a capital-scarce country. To develop the economy, liberals say, China has to attract foreign capital.

China's domestic savings rate runs as high as 30-50 percent of GDP—enough to support economic growth of 8-9 percent each year. Since 1992 the volume of nationwide deposits has exceeded the volume of loans. In 1994, savings deposits exceeded loan volume by ¥405.3 billion ($48.0 billion). In 1995, this difference was ¥361.7 billion ($43.5 billion). By 1998, the difference had climbed to ¥917.4 billion ($110.8 billion).

Nationalists, including several policy analysts and State Development Planning Commission (SDPC) officials, argue that excess foreign capital has gone into projects that would have been funded by domestic capital. They also blame FDI for contributing to inefficient utilization of domestic capital. And, on an even more controversial note, the nationalists claim it contributed to inflation in 1994-95.

6 Is there too much FDI for the Chinese economy to absorb?

Economic nationalists insist that current FDI inflows are overwhelming Chinese firms in key industries. But liberals argue that China's per capita foreign investment is relatively small, and does not exceed the internationally recognized "alert line." They point out that the 1998 debt-service ratio (debt servicing obligations divided by foreign-exchange receipts) of 10.9 percent and liability ratio (foreign debt divided by GDP) of 15.2 percent were far lower than 25 percent and 20 percent, the respective alert lines for these figures.

And the majority of "foreign" investment in China, liberals argue, comes from overseas Chinese, mainly from Hong Kong, Taiwan, and Macao. Between 1991 and 1998, FDI from these sources totaled $139.4 billion, accounting for 56 percent of all the FDI in that period. Moreover, liberals cite PRC State Statistical Bureau figures to back up their contention that about 25 percent of FDI in this period was domestic capital "round-tripping" through Hong Kong to take advantage of preferential conditions for foreign investment (*see* Table 1). Thus, a substantial portion of "foreign" investment is actually domestic capital re-entering China.

7 Does FDI encourage SOE reform?

Economic nationalists stress that excessive FDI and the methods used to attract it are detrimental to SOE reform. The preferential tax rates that FIEs receive have helped them gain dominant market share. In addition, FIEs do not shoulder the same level of responsibility as SOEs for social-welfare services, including housing and health care for current and retired employees.

But liberals argue that SOEs' problems are basically structural, and stem from government regulations, lack of oversight, and poor management. FIEs, they contend, should not become scapegoats for SOE failures.

8 Should China open markets to domestic investors first?

Some nationalists accuse liberals of ignoring domestic investors while opening markets to FDI. One of the fatal flaws in national economic policy, according to nationalists, is that China failed to remove the unreasonably strict rules on private investment in the telecommunications, banking, financial, and cultural sectors. The nationalists point out that stunting domestic market development in this way has contributed to domestic capital flight, excessive foreign economic influence, and heavy dependence on trade to spur growth. Economic nationalists suggest

that the government should offer SOEs to domestic investors first, before opening them up to foreign ones.

9 Should China allow foreigners to hold majority shares of FIEs, and does China need a concept of "industrial security"?

Liberals insist that majority control of China-based foreign companies should be perceived in economic, rather than political, terms. In other words, they see majority foreign ownership as a natural feature of capital movement in a market economy.

Nationalists argue that a foreign majority share will restrain China's independent development and will integrate the country into the overseas network of MNCs. They fear profits will go abroad. Nationalists suggest the government should retain the current standards of industrial security that prevent FDI from dominating strategic industries.

FIEs' Share of Chinese Industry (percent)

Indicator	FIEs* 1995	FIEs* 1998	Hong Kong-, Taiwan-, and Macao-invested enterprises 1995	Hong Kong-, Taiwan-, and Macao-invested enterprises 1998
Industrial sales revenue	8.4	12.5	8.6	11.8
Industrial value-added	7.7	10.3	7.9	10.6
Total assets	8.4	10.1	7.9	9.5

Source: PRC State Statistical Bureau, 1997; *China Statistical Yearbook, 1999*
* Excluding Hong Kong-, Taiwan-, and Macao-invested enterprises

Standing reluctant before the WTO gatekeepers

The three rounds of debate on the role of FDI have coincided with China's bid to enter GATT/WTO. Given these policy debates, it is much easier to understand China's love-hate relationship with the WTO and why WTO accession has proceeded so slowly.

The top leadership has long hoped to accede quickly, because accession will address difficult trade issues and attract more FDI. This was the key reason the liberal-minded top leadership was willing to take the risks embodied in China's April 1999 WTO offer. Unfortunately, domestic and international developments in mid-1999, particularly the NATO bombing, soured US-China relations and caused a resurgence of economic nationalism. Even some liberals found their faith in economic globalization shaken; the top leadership hesitated.

Many policymakers and economists were able to voice their concerns about the scale and competitiveness of the Chinese economy. They pointed out that a 1999 PRC study in *China Management Journal* put Microsoft's market capitalization at $386 billion (¥3,200 billion), or 1.5 times that of the combined value of the Shanghai and Shenzhen stock markets (¥2,100 billion).

Tug on government policy

Generally speaking, liberal thought has had the upper hand in China's FDI policy. But it is easy to discern the influence of economic nationalism in China's development strategy and competition policies. Economic nationalism enjoys support among policymaking bodies, including the State Development Planning Commission (SDPC) and the State Economic and Trade Commission (SETC), as well as key think tanks. To allay the fears of economic nationalists, the government has, since 1992:

- **Formulated industrial policy in "pillar" industries.** To support the rapid development of the auto industry, the SDPC issued China's first auto-industrial policy in 1994. International negotiators protested that some provisions of this policy are incompatible with WTO norms. Efforts to formulate mechanical and electronics industrial policies were aborted due to budget constraints.
- **Encouraged M&A among SOEs.** Pressured by the new wave of industrial mergers and acquisitions in Western economies, China has organized its own "aircraft carriers"—large companies—to improve economies of scale and better compete with foreign companies. The government is becoming more active in the M&A process, often playing the role of coordinator, promoter, or even leader. M&A is a feature of the restructuring in every industrial sector.
- **Implemented a grand trade strategy.** The Ministry of Foreign Trade and Economic Cooperation (MOFTEC) formulated this policy in 1994 to prepare Chinese trading firms for accession to the General Agreement on Tariffs and Trade. It encourages trade-related sectors—including technology development, manufacturing, financing, and labor—to join forces to increase economies of scale and improve efficiency through better coordination. The ultimate objective of this policy is to prepare Chinese firms for the entry of more MNCs into the Chinese market. As part of this policy, MOFTEC launched an ambitious plan to build 100 trading conglomerates.
- **Promoted technological innovation and a "knowledge economy."** Since 1988, the term "knowledge economy" has become a buzzword among Chinese leaders. Because it perceives technological innovation as the most important force behind the sustained growth of the United States, the PRC government has launched major programs in research and development and commercialization.
- **Broken monopolies by opening markets to domestic competitors.** The most obvious examples of this policy are in the telecommunications and insurance sectors. In April 1999, the monopoly giant China Telecom was officially restructured into four competing companies. China United Telecommunications Corp. (Unicom) and four other large, self-supporting, independent entities will compete in China's telecom market. By 2001, the newly organized companies are expected to enter each other's business spheres. This process echoes that of the deregulation of the insurance industry several years ago.
- **Adopted a gradual and experimental market-opening strategy,** especially in service industries, such as banking and financial sectors.

—Yong Wang

The three rounds of debate on the role of FDI have coincided with China's bid to enter GATT/WTO. Given these policy debates, it is much easier to understand China's love-hate relationship with the WTO and why WTO accession has proceeded so slowly.

And the 1998 annual sales revenue of Wal-Mart Stores, Inc. was equivalent to nearly 40 percent of China's entire sales revenue. These comparisons alarm even WTO advocates.

They also warned the government of the possible side effects of radical reform, especially in this period of economic slowdown. The government has decided to proceed cautiously on SOE restructuring. Some analysts have voiced the fear that fast-track WTO membership would conflict with this strategic adjustment.

As money-losing SOEs are pushing the banking and financial system toward the brink of crisis, it is no surprise that market access to China's banking and financial sectors became one of the most sensitive topics in WTO negotiations. Despite nationalist fears that a hasty opening may trigger another Asian-style economic crisis, the terms of the bilateral are quite far-reaching.

Finally, there is concern about how the WTO regime may constrain China's freedom to solve its problems. WTO membership requires policy transparency and will require China to change its laws to comply with WTO obligations, but China's economic reformers worry that these rules will inhibit decisionmakers' flexibility.

Despite these worries, China reached agreement with the United States on the terms for China's WTO accession on November 15, 1999—the single most important step for China so far in the accession process (*see* p.17). The Chinese government has made a political and strategic decision that reflects the leadership's firm commitment to better US-China relations as well as to ongoing reform and liberalization policies.

It will take time to diminish the influence of economic nationalism, however. Implementation of China's eventual WTO protocol will not be entirely smooth. The debate between the liberals and nationalists will continue and will still play a role in setting the pace of China's incorporation into the world economy. But two things are sure—with enhanced competitiveness of Chinese enterprises and more visible benefits from the global economy, China's self-confidence will increase, and China will, eventually, open its door much wider.

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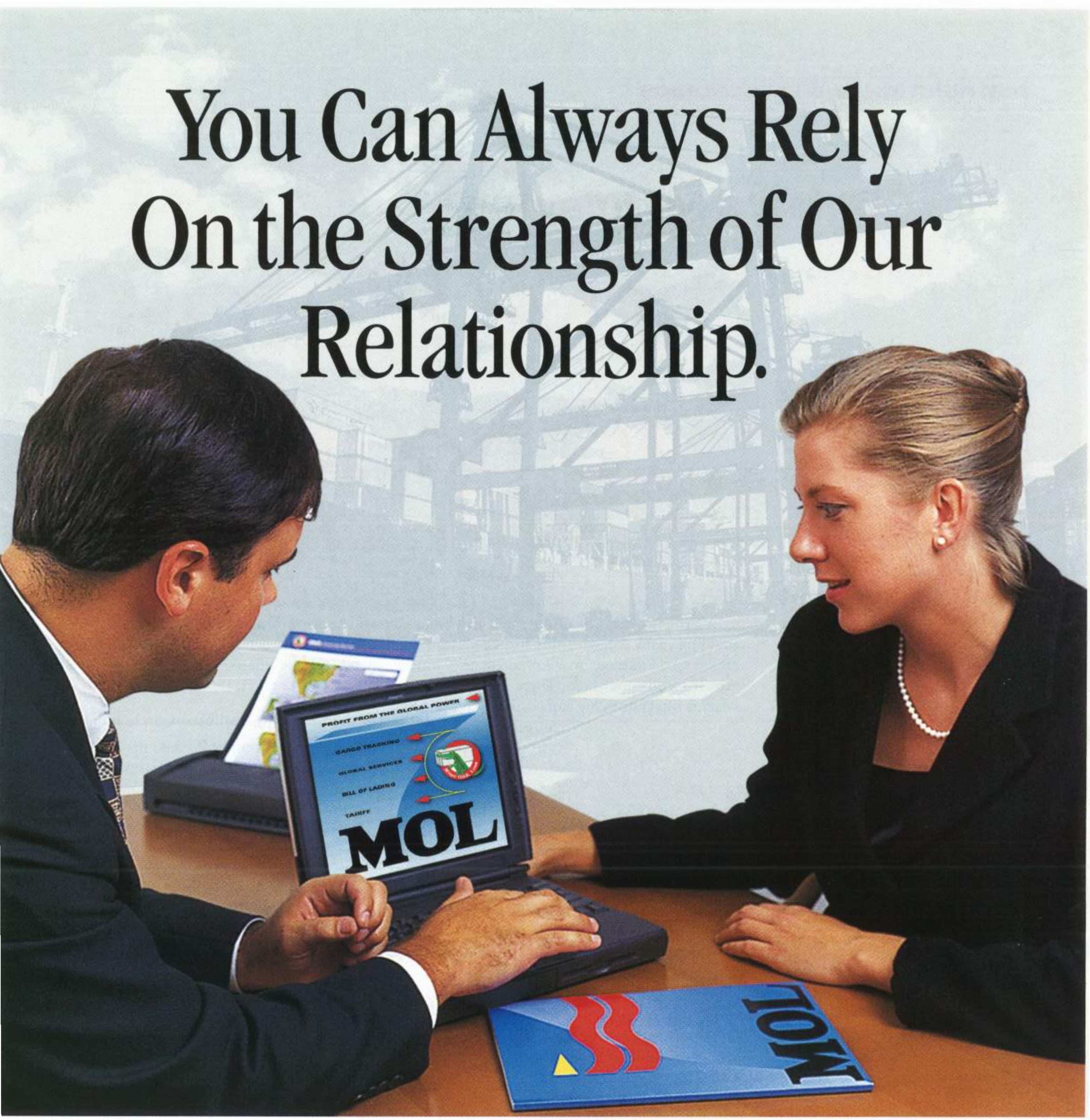

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China's Middlemen—New Paths to Market

Tina Helsell

Foreign companies, particularly in the PC industry, find that working with systems integrators is the secret to success

A growing class of middlemen in China is enabling many foreign firms to penetrate small and remote markets to gain access to China's growing consumer base. These middlemen, or systems integrators, are companies that assemble completely integrated systems and/or outsourced components, and sell finished products primarily through retail outlets. Though not an unfamiliar or especially sophisticated concept in developed countries, technically adept systems integration is a fairly new phenomenon in China.

Systems integrators have emerged and thrived as a result of economic reform and foreign participation in market development. They range in size and scope from former state research institutes that have commercialized their services to very small mom-and-pop shops that assemble PCs in the back room. Foreign firms have turned to systems integrators partly because PRC law forbids foreign firms from owning or managing distribution networks, wholesaling outlets, or warehouses. They must use local companies to handle importation and transportation logistics, and distributors or other intermediaries to conduct transactions with local customers.

According to the November 15 agreement between China and the United States on the terms of China's World Trade Organization (WTO) accession, foreign firms will be able to participate more fully in the sales and distribution sectors once the PRC accedes. These firms will be able to control more effectively their wholesaling, retailing, maintenance and repair, and transportation logistics operators. All restrictions on distribution services for most goods will be phased out within three years of accession (*see* p.17).

Tina Helsell
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In the meantime, all business is local

China's economic reforms, particularly reforms of state-owned enterprises and subsequent large-scale layoffs, have combined with low entry barriers to create a new pool of local businesses, including small-scale assemblers and systems integrators.

Considered manufacturers by the Chinese government, local assemblers and systems integrators did not emerge as a force in China until the early 1990s, when local governments, eager to support small businesses and foster employment, relaxed restrictions on manufacturing licenses. Many foreign firms have since taken such companies under their wings, training them in product methods, technologies, and systems in an attempt to build a customer base and assist grassroots promotion efforts. Such cooperation has resulted in strong strategic alliances in China—but has also sparked a new group of enterprises capable of applying product knowledge and technical skills to competing lines.

Increasingly technically sophisticated and generally able to offer the lowest market prices in certain industries, systems integrators pose a major threat to their larger and more established foreign and Chinese competitors. As a group, they are making a major impact in local markets, where decentralization has given local governments more decisionmaking and purchasing power. Local telecommunications agencies, for instance, are no longer subject to central-level mandates and thus are purchasing equipment and systems based on local needs. They are turn-

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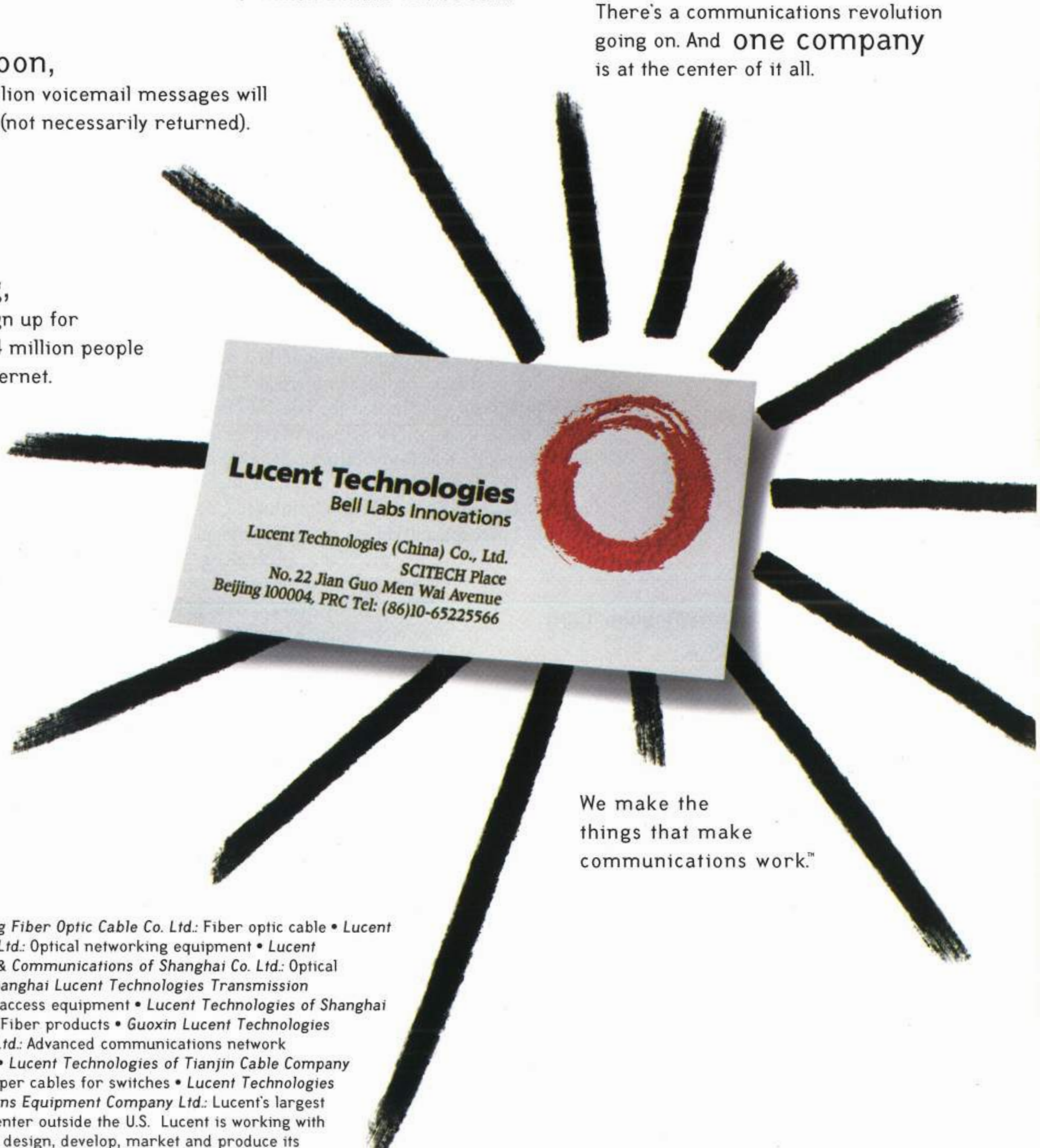

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In the PC sector, small-scale systems integrators have succeeded by catering to the growing number of individual Chinese consumers willing to forgo warranties and service for low prices. And they are making quality improvements in hopes of attracting commercial buyers looking for low-cost technological solutions that are "good enough."

ing to low-cost, small-scale local companies with access to imported equipment and the ability to integrate systems assembled from a variety of sources and suppliers. These suppliers are poised to become an even greater force as the trickle-down effect starts influencing China's developing information technology (IT) infrastructure. And as the current centralized series of IT networks reaches down to government organizations and corporations at the provincial and municipal levels, they will grow more.

Foreign suppliers' ability to compete now depends on their understanding of the channels through which local assemblers and systems integrators source finished goods and components, and whether they can develop effective sales, distribution, and service channels.

The PC market: Who's got the most market share?

Small-scale local assemblers and systems integrators have proliferated in the nation's booming consumer-electronics sector. Those that sell PCs, for example, hold a slightly greater share of China's PC market than major local original equipment manufacturers (OEMs). Of the estimated 5 million PCs sold in China in 1999, local assemblers and systems integrators accounted for sales of close to 2 million units, or 40 percent of the market (*see* figure). Major Chinese PC OEMs such as Legend Group Corp., Founder Electronics Co., and Great Wall Computer Co. had a 37 percent market share, while foreign PC makers, including Compaq Computer Corp., Dell Computer Corp., Hewlett-Packard Co., and IBM Corp., claimed 24 percent in 1999. International Data Corp. forecasted foreign market share to fall to 23 percent in 1999 from over 30 percent in the early 1990s as local OEMs and assemblers grow more sophisticated.

In the PC sector, small-scale systems integrators have succeeded by catering to the growing number of individual Chinese consumers willing to forgo warranties and service for low prices. And they are making quality improvements in hopes of attracting commercial buyers looking for low-cost technological solutions that are "good enough." Chinese consumers—government and individuals alike—tend to favor local electronics brands as long as quality is comparable to that of foreign brands.

Households will constitute the next big wave of demand for PCs in China. PC sales to individuals and households have been doubling annually since 1995, according to the Ministry of Information Industry (MII), the government regulator of China's electronics and IT sectors. MII predicts that once the average price of a PC falls below $500, sales to individuals and households will surpass sales to the commercial sector.

As a result, major OEMs that have traditionally focused on commercial and government accounts are now competing with local systems integrators for shares in this market. The systems integrators that currently hold dominant positions are maintaining their edge by improving quality and offering prices that are equally, if not more, competitive than OEMs. Price wars are common; some local players have been selling well below cost—a key reason foreign competitors are losing market share.

Imports play a large role

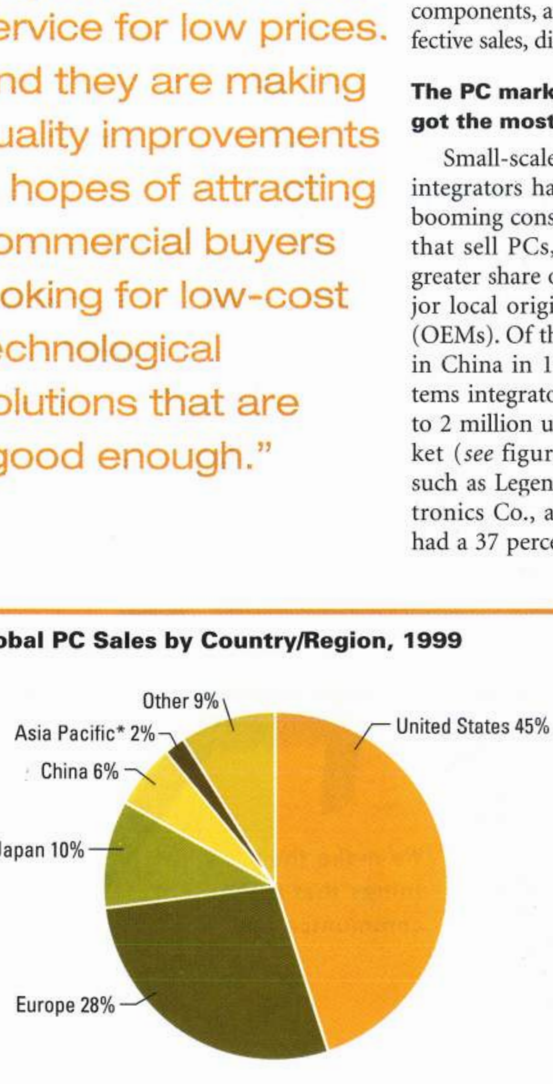
Foreign companies serving China's PC manufacturing sector have followed major global PC OEMs into China. By value, computers assembled in China today rely heavily on imported parts. A high percentage of suppliers—up to 100 percent for certain products—source products abroad. Of total computer-related imports today, over 80 percent are components and peripherals. Importing parts and components to large-scale PC OEM accounts is relatively straightforward. But, as local assemblers and systems integrators represent almost half of total demand for these imports, securing OEM accounts is only part of what it takes to be successful in the China PC market. Systems integrators are a key target market for foreign PC parts suppliers.

Barriers to entry

As more companies move component production facilities to China, a slowdown of component imports is inevitable. But parts localization has only just begun, and is not expected to supplant imported components in the near-to-medium term, particularly high value-added components such as CPUs, drives, and motherboards. There are a number of reasons for this slow rate of localization, including the relatively small size of China's PC market. China's 1999 sales accounted for 6 percent of global demand. In comparison, US sales totaled 40 million units, or 45 percent of world demand. PC sales in China are estimated to grow 25 percent this year, and may overtake Japan. While the China PC market is growing quickly, it is doing so from a very low base. For most suppliers of individual components and peripherals, China's still-small market does not yet justify the investment required to build a local facility.

Other economic barriers, however, deserve even more of the blame for the high level of

Global PC Sales by Country/Region, 1999



Country/Region	Units (Millions)	Global Demand (%)
United States	40	45
Europe	25	28
Japan	9	10
China	5	6
Asia Pacific*	2	2
Other	8	9

SOURCE: International Data Corp.
*Malaysia, Indonesia, the Philippines, Singapore, and Thailand


Trade with China helps America's economy take off.
Every time a new Boeing aircraft leaves the U.S. for delivery in China, thousands of American companies and tens of thousands of American workers chalk up another success in that fast growing market.
Over the next 20 years, China's airlines will buy more commercial jets than any other nation outside the U.S. — an estimated 1,600 aircraft valued at $120 billion.
China recently agreed to open its market to a vast new range of U.S. goods and services. A vote for Permanent Normal Trade Relations with China is a vote for America's economic future.
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Fragmented Markets: Not Only the PC Industry

The Automotive Industry

Original-equipment manufacturers in the automotive industry in China today source at least 60 percent of their parts locally—with the average at 70-80 percent. Auto parts that are sold in the retail market are often imported, even if foreign-invested enterprises are producing such parts in China.

Representing over 60 percent of the retail market, auto-parts vendors, like systems integrators and local assemblers, are small, entrepreneurial, and extremely fragmented. But, unlike systems integrators and assemblers, auto-parts vendors typically source and sell a very limited variety of parts. This is changing, however, and as in the PC and electronics sectors, many of these vendors are growing more sophisticated, providing a channel for multiple products and even services.

The Animal-Feed Industry

Foreign firms sell animal-feed additives to thousands of small-scale Chinese farmers who buy in low volumes. These firms employ elaborate distribution channels whereby small bags of feed additives are sold to fragmented, regional markets through many layers of distribution. One company, for instance, imports animal feed by the container-load into Shanghai, where the feed is off-loaded and then re-packaged into small units for resale to local farmers. Though this market is starting to change as animal farms consolidate, for now, gaining market access means being able to reach remote customers who make small-scale purchases.

—*Tina Helsell*

overseas sourcing in this market: Chinese laws that prohibit foreign participation in distribution and services; firmly entrenched Hong Kong Special Administrative Region (SAR) "converter" channels—trading companies that are able to move foreign goods into mainland China at low cost; and the extremely fragmented nature of the market. Successful foreign firms have gained what influence they can by investing heavily in dedicated networks and value-added services that they do not own.

By law in China, MNCs can only distribute products that they manufacture locally. Many have, however, established trading companies in specially designated economic zones through which they import and ship products to customers directly, and issue invoices and receive payments legally. MNCs that have adopted this method report that while working through a trading company in China has taught them how business is done locally, they continue to use established—and ultimately more cost-effective—channels, particularly for imports.

The Hong Kong way

Before 1990, foreign firms sold components and peripherals destined for the China retail market only through Hong Kong traders, without regard for where the product ended up, or at what prices. This system resulted in a number of problems for foreign suppliers and their customers, most notably wildly fluctuating enduser prices. The distance from customers also made it difficult to access customer feedback and other important market information, much less build brand-name recognition or customer loyalty.

Foreign firms that have sought to replace this channel with a more direct sales route have discovered that doing so is economically difficult. Hong Kong converters are able to move products from the SAR into southern China more cheaply than most competitors. The government crackdown on smugglers a year ago closed down some of these "gray" channels, but many have re-opened.

Foreign firms manufacturing in China for the local market do not necessarily have the privileged access to markets and customers that localization would suggest. With Hong Kong channels in place, it actually costs more for manufacturers to sell Chinese customers locally produced goods than imports. This is especially true of the PC sector, with its high percentage of imported inputs. The retail price of locally sourced products reflects import duties and value-added tax (VAT) on any imported content, plus a domestic VAT of 17 percent.

Players in a fragmented market

China's systems-integrator market is comprised of thousands of small-scale operations across the country. Foreign suppliers importing parts must access these retail accounts through complex and multi-layered channels involving up to five intermediaries. These include Hong Kong trading companies, authorized distributors, local transportation and logistics companies, dealers, and resellers. The system reflects not only the extremely fragmented PC retail market, but also China's weak physical distribution infrastructure and the lack of a national network:

- **Authorized distributors'** primary role is to take title to goods in Hong Kong, arrange for their transportation into China, and manage extensive networks of local dealers and resellers.
- **Dealers** are local Chinese companies, typically with a storefront, that sell directly to systems integrators and consumers seeking replacement parts.
- **Resellers** perform the same function as dealers but are located in small and/or remote markets where most foreign suppliers have not yet built up either a presence or a sales network.

To better control product flow and pricing, and to get closer to retail accounts, some foreign firms in the early 1990s started appointing distributors—primarily from Hong Kong, Japan, Singapore, Taiwan, and Thailand—to represent them in China. These distributors ensure that goods hook up with their channels once exported from Hong Kong. In addition to managing export and domestic sales channels, distributors keep foreign firms informed of market conditions and customer feedback. These relationships are typically not exclusive, but authorized distributors usually have the best access to inventory and technical support from their OEM clients.

Thus, foreign firms have been forced to add extra layers to the distribution process rather than move toward replacing converters. Though costs remain unaffected—Hong Kong channels offset any extra margins—such layers keep foreign suppliers that much more removed from final customers. Most foreign suppliers have found local representation through authorized distributors key to managing dealer and reseller relationships, as well as to collecting payment.

Foreign firms successful in using authorized distributors have selected their representatives carefully. The best distributors are able to navigate the complex and fragmented dealer and reseller networks through which most systems integrators source goods. They also have strong financial backgrounds, sales and marketing skills, transportation networks, technical skills, and connections. Many of these are state-owned distribution companies that have survived the cut-off of government subsidies and guaranteed sources of income. Unlike their private counterparts, these companies have the advantage of long-established sales and distribution networks, including truck fleets; distribution centers in strategic regions and markets; a relationship with the Ministry of Railways and local rail bureaus; and connections with key decision-makers in many industries.

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WINDMERE-DURABLE HOLDINGS, INC. SUPPORTS PNTR AND WTO MEMBERSHIP FOR CHINA

Windmere-Durable Holdings, Inc. fully supports *Permanent Normal Trade Relations* with the People's Republic of China and their entry into the World Trade Organization.

Granting permanent NTR status to China is vital to our national interest. Without it, U.S. businesses will not benefit from China's commitment to roll back trade barriers, while China's other trading partners do.

We believe that Congress should join with the Administration in granting China permanent NTR status in connection with China's accession to the WTO. This action will secure an unprecedented opening of China's market to U.S. agricultural products, services and manufactured goods.

We must embrace this landmark agreement. Greater openness with China is important to our country, to our national security and to our trading position in the world. It represents tremendous opportunity for the United States of America as well as economic prosperity and better living standards around the globe.

A number of distribution companies that previously reported to the Ministry of Internal Trade (now the Bureau of Internal Trade) and trucking companies that used to report to the Ministry of Communications continue to operate successfully. Some foreign firms in the PC and related sectors have formed distribution relationships with domestic competitors. Legend serves as a distributor for many foreign suppliers, including Canon Inc., IBM, Intel Corp., Motorola Inc., Seiko Epson Corp., and Toshiba Corp.

Many foreign companies are finding that most local distribution companies have neither the ability nor the focus to provide the value-added services and support that are more and more critical to success. Retail customers in the PC sector today are expecting price, quality, and service levels that formerly only large-scale OEM customers could command.

Successful distributors typically also have the resources to meet foreign suppliers' usually strict payment terms, as well as the influence and clout needed to collect payment from dealers and resellers. The most effective distributors enforce strict and uniform pricing policies across their dealer and reseller networks. This is becoming more important to foreign firms, the reputations of which have suffered in the past from fluctuating retail prices.

Localizing service

Many authorized distributors claim to provide customer service, technical support, and routine repair and maintenance services. Many foreign companies are finding that most local distribution companies have neither the ability nor the focus to provide the value-added services and support that are more and more critical to success. Retail customers in the PC sector today are expecting price, quality, and service levels that formerly only large-scale OEM customers could command.

A number of foreign companies are exerting greater control over their distributors than before, directing the efforts of distributors into areas where they excel—namely, channel management. Also, as foreign suppliers introduce more sophisticated and higher-end products to China, they must support those sales with better training and repair services than their distributors and dealers can provide.

Until the market-access gains that will come with WTO accession kick in, foreign firms will only be able to service products and parts that they manufacture in China, and then only through the warranty period. Goods in need of repair or damaged during shipment must be exported back to the original OEM, repaired offshore, and re-imported, at considerable cost.

MNCs seeking to streamline repair and maintenance services in China have found legitimate ways of establishing national service networks. Firmly established MNCs in China, for example, have set up ventures to provide management services. They recruit, train, accredit, and closely monitor the activities of the thousands of local-level service, repair, and maintenance providers they need to perform even the most basic levels of service.

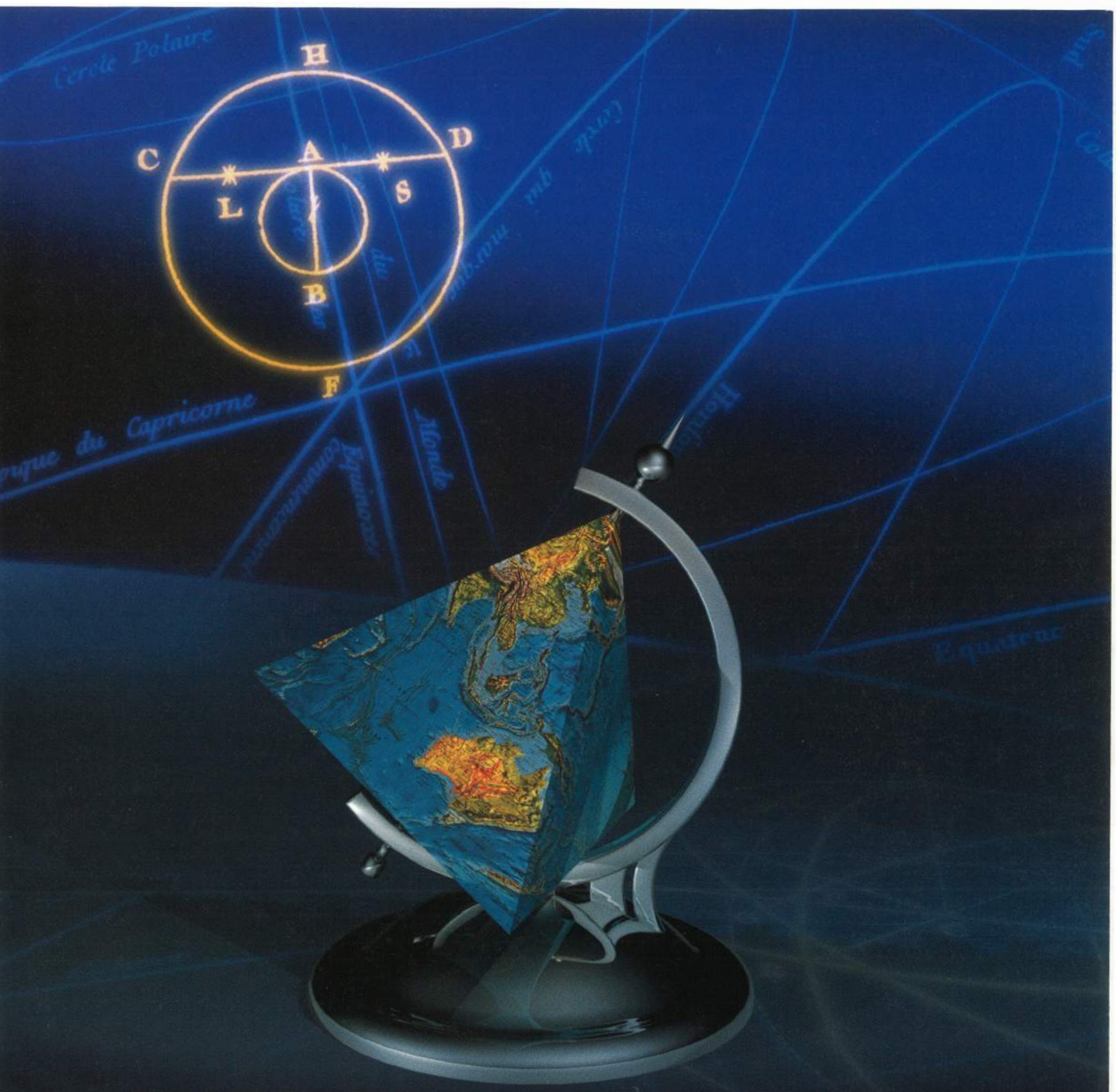
Though far from ideal and costly to maintain, MNCs that have chosen this option report that it brings them closer to local customers, makes for more effective and economic repair and maintenance services, and provides an opportunity to differentiate products through value-added services rather than price alone. These MNCs view their service joint ventures and networks as important precursors to wholly foreign-owned and independent ventures engaged in both sales and services, which they anticipate will be possible three to five years after China accedes to the WTO.

Opening the distribution door

Now that the United States and China have finally reached an agreement paving the way for China's WTO accession, the time is ripe for foreign firms to take the measured risks and assume the costs required to secure authorized distributors skilled at managing complex, multi-layered sales and distribution channels. Foreign companies also would do well to invest heavily in sales and service networks through joint ventures with Chinese partners. Foreign firms that engage in such joint ventures can differentiate themselves from the competition, and could be first in line to launch wholly foreign-owned service ventures in China once these are permitted.

Whether WTO accession will ultimately lead to unprecedented access to China's distribution and service networks for foreign firms depends largely upon the Chinese government's ability to implement forceful, rational, and consistent trading and business mechanisms. It is one thing to establish and publish reduced tariff rates, but quite another to eradicate, through strict law enforcement, barriers to entry that are more difficult to verify, such as Hong Kong converter channels.

Converters—so well-entrenched and providing income to many Chinese people—will likely continue to play a key role in the system for the foreseeable future, even after WTO-induced tariff reductions whittle away their cost advantage. But only after China eliminates such obstacles to the establishment of streamlined, competitive sales, distribution, and service channels for both foreign and Chinese companies will foreign firms be able to access China's fragmented marketplace fully. China's enforcement of transparent, consistent trading practices is crucial to the country's goal of developing the economy by attracting foreign direct investment in infrastructure, systems, technology, and training.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The Shanghai Office Market Turns a Corner

Andrew Ness

After years of downturn, Shanghai's office market faces a brighter future

After nearly four years of steady decline, the Shanghai office market appears to be taking a turn for the better. While the level of new office space is still dropping, the rate of this decline is slowing: the estimated 637,000 sq m of new, prime office space created in 1999 is 37 percent and 46 percent below 1998 and 1997 figures, respectively *(see figure 1)*. While originally over 1 million sq m of office space was scheduled for completion by year-end 1999, some 11 developments providing roughly 380,000 sq m have been delayed. Many developers deliberately slowed construction in hopes that market conditions would be more favorable by the time they were finished.

Many office properties that entered the market in 1998-99 were built on sites granted to developers during the boom of 1994-95. However, in third quarter 1997, the Shanghai Municipal Government, concerned about the rising imbalance between supply and demand for office facilities, imposed a moratorium on the further assignment of land for the development of high-end commercial property.

The moratorium echoed the spirit of the 1995 State Council Directive Concerning Exercising Strict Control Over High-End Real Estate Projects, which severely restricted the granting of approvals for office towers and luxury residential developments, defined as having construction costs more than 100 percent above those of ordinary-quality developments. As it takes three to five years to develop a commercial building or complex, this restraining order is not expected to affect the market fully until 2000-03. Beginning this year, the total stock of new office properties hitting the Shanghai market is forecasted to drop significantly on an annual basis. This tightening in supply, combined with the resurgence in demand for office facilities from both overseas and domestic companies engaged in finance, securities, insurance, and professional services industries, should set the stage for the eventual rebound of the Shanghai office market.

Some 18 office properties were slated to come on stream in 1999—seven properties in Puxi providing 317,900 sq m and eleven in Pudong providing 320,000 sq m of office facilities. Even this batch of new property, though markedly below the levels of the three previous years, has contributed to oversupply and depressed Shanghai prime office rental values. Rental values for prime office properties in Puxi and Pudong have declined 75 percent since peaking in 1995, or an average of 18.8 percent per year. The rate of decline in asking rentals for prime office properties, however, clearly began slowing in 1999—there are now signs that supply and demand for office facilities in Shanghai have finally begun to approach equilibrium.

The fact that prime net office rents in both Puxi and Pudong are at all-time lows has sparked a surge in demand for such facilities; both overseas and domestic firms took advantage of the market's soft conditions to expand or upgrade their office premises. Led by multinational and large domestic corporate groups, such firms absorbed 470,000 sq m of office space between January and October 1999. Major office-leasing transactions included PricewaterhouseCoopers' relocation from the Shui On Plaza to Central Plaza on Huai Hai Middle Road, and J. Walter Thompson's move from an older, lower-grade office property to the prestigious Kerry Center on Nanjing West Road. A number of major domestic firms and joint ventures also signed new leases. Shenzhen Huawei Technology Co. Ltd., Bank of China, and Shanghai Schindler, for example, all committed to lease substantial amounts of new office floor area in 1999.

To lease or to buy?

This resurgence in demand substantially reduced large pockets of vacancy in many recently

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is departmental director, Global Research and Consulting, Greater China, CB Richard Ellis. CB Richard Ellis is a multinational real estate services company, offering property sales and leasing, property management, corporate services, mortgage banking, investment management, capital markets, appraisal/valuation, research, and consulting services.

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Harold McGraw III
President and
Chief Executive Officer

*The **McGraw·Hill** Companies*

December 21, 1999

The Honorable Charlene Barshefksy
U.S. Trade Representative
600 17th Street, N.W.
Washington, DC 20508

Dear Ambassador Barshefsky:

On behalf of The McGraw-Hill Companies, I congratulate you and your team on negotiating a marketing-opening trade agreement with China.

While less than one percent of our company's business is currently conducted in China, we welcome this agreement because, properly enforced, it can offer full access to Chinese markets, which is in America's long term best interests. As a leading global information services provider, we look forward to the opportunity to provide information to the Chinese people through our many products and services including *BusinessWeek*, Standard & Poor's and the McGraw-Hill imprint in educational and professional publishing.

Increased Chinese consumer demand for American goods and services can spur significant growth for many American companies, leading to more U.S. jobs.

In addition to the obvious economic benefits, continued engagement with China is the best way to ensure the survival and success of the fledgling political and economic reform movements there.

For the United States to realize all of the benefits of the agreement you have reached, it is essential that China be granted Permanent Normal Trade Relations status by the Congress and full membership in the World Trade Organization. The McGraw-Hill Companies looks forward to working with you on achieving this next year.

Sino-American relations have always presented unique challenges. Yet with each challenge comes an opportunity. By seizing the opportunity to conclude an agreement which can so fundamentally alter the global economic landscape, you and your team have performed a most valuable public service – one which can ultimately enable people on both sides of the Pacific to reach his or her highest potential.

Sincerely,

Harold McGraw III

Harold McGraw III

Investment in the Shanghai office sector is appealing only to a select group of domestic occupational investors and a small number of contrarian investors specializing in the acquisition of distressed assets under favorable conditions.

completed prime buildings in Puxi and Pudong. The average vacancy rate fell from 48.2 percent to 44.7 percent in Puxi, and from 53.6 percent to 48.6 percent in Pudong during the third quarter of 1999 *(see figure 2)*. According to the CB Richard Ellis Shanghai Prime Office Rental Index, net asking prices for prime office properties stood at $18.1 per square meter (psm) per month in Puxi and at $12.5 psm in Pudong last October—declines of 4.1 percent and 4.5 percent over the previous quarter, respectively.

Asking prices for office properties for sale have also dropped. In Puxi and Pudong, respectively, sales prices have fallen 29.4 percent and 24 percent, or 7.3 percent and 6 percent per annum, since peaking in fourth quarter 1995 and first quarter 1996. While more stable than the office-leasing market, the capital market showed signs of accelerated decline in the third quarter of 1999; prices dropped 4.1 percent in Puxi and 3.7 percent in Pudong compared to the previous quarter. This resulted from the low supplementary premiums local developers paid to convert a number of domestic-sale office buildings (which can only be sold to Chinese individuals or PRC legal entities) into overseas-sale office properties (which can only be sold to foreign individuals or companies). The introduction of this new, cheaper stock of office property has triggered a sizeable correction in office asking prices. Prime office properties have now been adjusted downwards to $1,948 psm in Puxi and $1,636 psm in Pudong.

The greater overall stability of the capital market is attributable to the fact that quite predictably the vast majority of companies in Shanghai have only been willing to consider leasing, not purchasing, office space. This, in turn, is attributable to a number of factors. First is simply the continuous decline of the Shanghai office-leasing market since fourth quarter 1995.

Second is the accompanying drop in the nominal yield on Shanghai office investments, as rental values have fallen far more rapidly than asking sales prices. The gross yield in Puxi fell from 20 percent in first quarter 1995 to 7.9 percent in third quarter 1999. The respective figures for Pudong are 16.9 percent in first quarter 1996 and 10 percent in third quarter 1999.

Third is the subdued state of Shanghai's economy combined with a sharp drop in foreign investment, which was down by 34 percent year-on-year by the third quarter of 1999. The drop has enforced an attitude of extreme caution with respect to investment, and especially with respect to relatively illiquid investments in fixed assets.

All of these factors have combined to make investment in the Shanghai office sector appealing only to a select group of domestic occupational investors and a small number of contrarian investors specializing in the acquisition of distressed assets under favorable conditions. Examples of such assets are prime development sites for office properties that were never built; completed, but unoccupied, properties; and partially built properties. Under these conditions, even occupational investors who might consider acquiring properties entirely for their own use have become cautious.

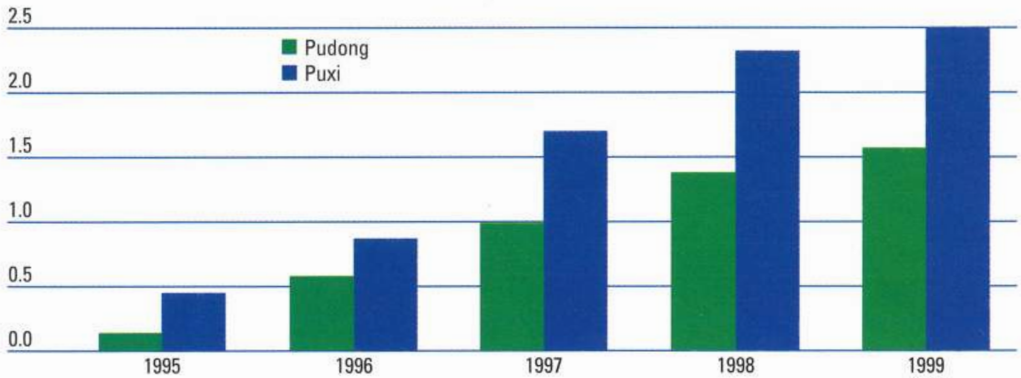
In 1996, when major corrections to the Shanghai office-leasing market were initiated, there were virtually no en bloc office property transactions—acquisitions of entire properties or a significant portion of them. But in 1997 Itokin of Japan acquired the China Silk Building, and OOCL of Hong Kong secured 6,800 sq m in the Dongfang Haiwai Dasha (OOCL Plaza). Two major acquisitions took place in 1998—the Shan Shan Group of Ningbo purchased the Pumao Building, and the Baogang Group bought the Shanghai Materials Mansion. In the first 11 months of 1999, only one major transfer of interest in an office property has taken place. The Guangdong Development Bank assumed equity in the Tai Qi Feng Building, a mixed-use property providing 49,000 sq m of gross floor area in the Xuhui District, in lieu of outstanding, unpaid debt.

The Shanghai office market has many sellers but very few purchasers willing to consider acquiring property on a non-distressed basis. Consequently, the continuous small shifts and downward adjustments in the asking sales prices of office properties have little galvanizing effect on the office-sales market.

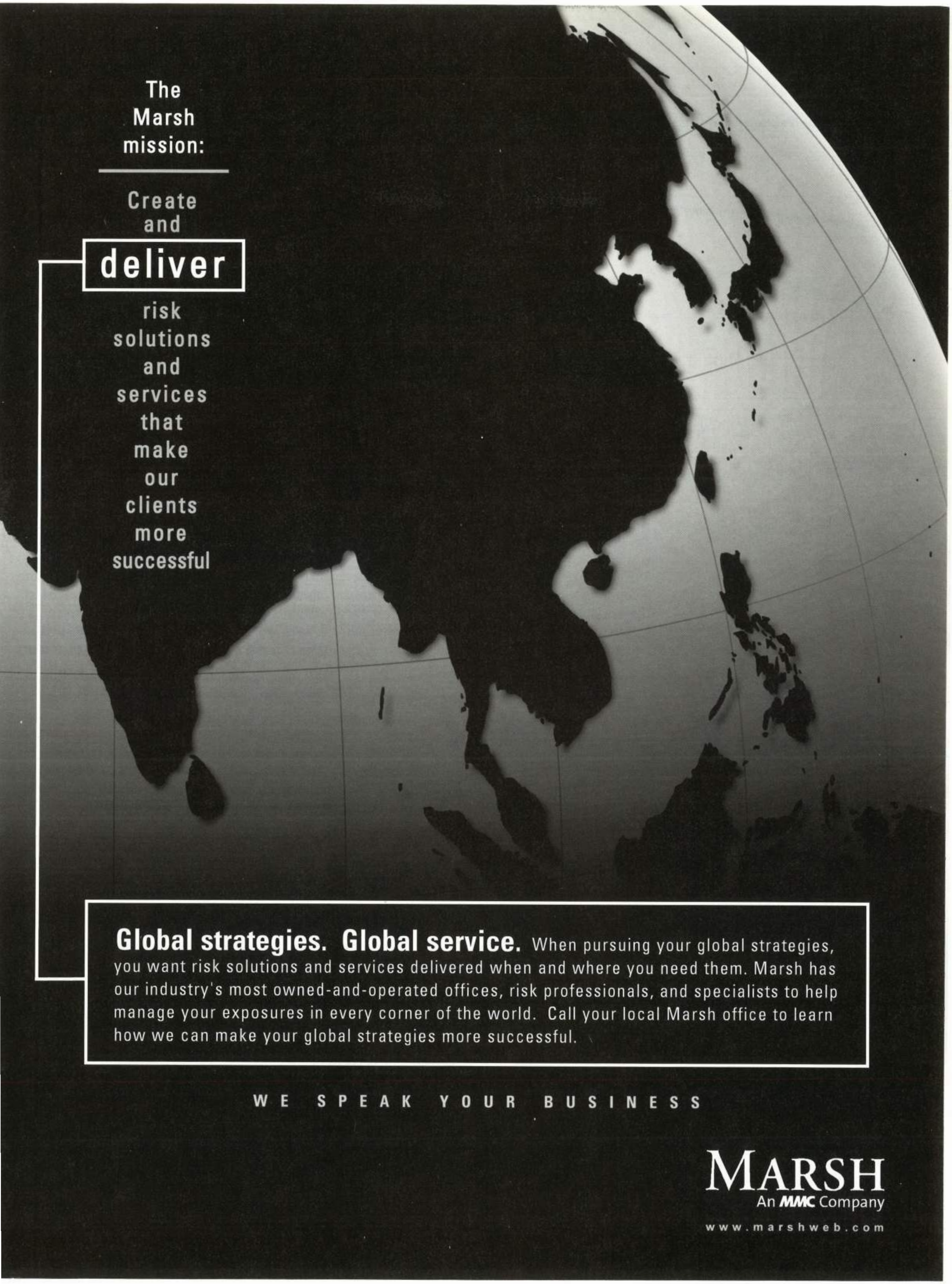
Bottoming out

Since peaking in 1995, Shanghai prime office rentals have basically been in a state of continuous consolidation and are now rapidly approaching the bottom of the cycle. The supply of new office facilities should shrink in 2000, along with developers' markedly waning enthusiasm for bringing new office space on

Figure 1
Office Supply in Shanghai (cumulative million sq m)



SOURCE: CB Richard Ellis
NOTE: 1999 figures are estimates.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Global strategies. Global service. When pursuing your global strategies, you want risk solutions and services delivered when and where you need them. Marsh has our industry's most owned-and-operated offices, risk professionals, and specialists to help manage your exposures in every corner of the world. Call your local Marsh office to learn how we can make your global strategies more successful.
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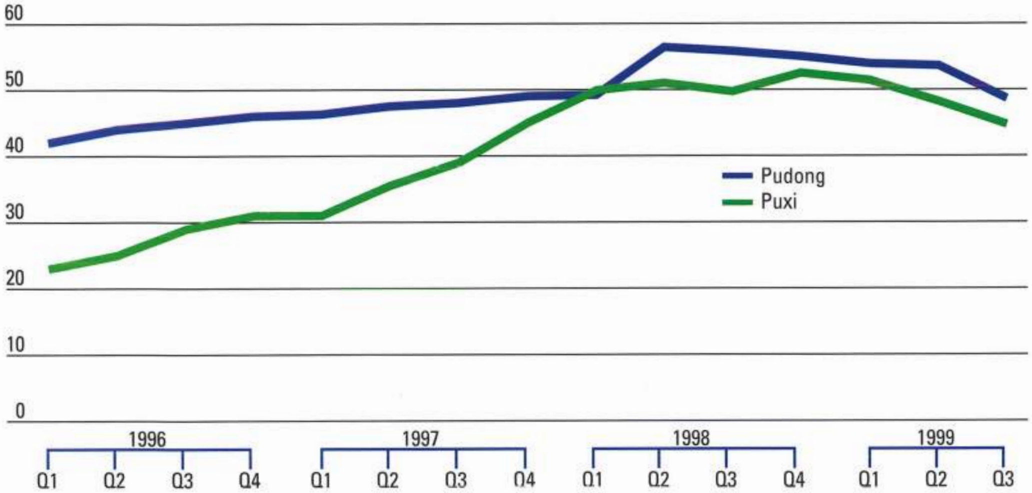
Figure 2
Prime Office Vacancy Rate in Shanghai, percent



SOURCE: CB Richard Ellis

stream in such a depressed market. While this will not lead to the immediate rebound of either the Puxi or Pudong prime office markets, it will certainly help them regain stability. As the late 1990s government clampdown on new office development begins to be felt in 2000, the gross disparity between supply and demand for office facilities will diminish over the next five years. When the Shanghai office market finally does improve, the prime office areas—the Lujiazui financial district in Pudong and Nanjing West Road and Huai Hai Middle Road in Puxi—are expected to rebound before other Shanghai micromarkets, and eventually drag other, more laggard office areas up with them.

The completion of Metro Line No. 2, linking Lujiazui to the downtown Puxi area; the opening of Pudong International Airport last October; and the occupation of several soon-to-be-completed office buildings in Pudong core central business district by a number of major PRC financial institutions will boost the Lujiazui financial district area and tighten available supply.

The speed with which the Shanghai office market regains strength, however, particularly where tight supply is matched by escalating rentals, depends largely upon external factors. China's impending admittance to the World Trade Organization (WTO) is expected to prompt another spurt of foreign investment in China. This will in turn pump up the demand for office space in Shanghai and other major cities throughout China. The sectors to be stimulated most by China's WTO entry will be tertiary sector industries that are the most intensive users of prime

office space, including banks and financial, insurance, securities, professional services, and consulting firms. China's accession, while favorable to the entire Shanghai office market, will be especially favorable to the Lujiazui financial district in Pudong, which has been earmarked by the PRC government to serve as a headquarters for the financial industry in Shanghai. Nanjing West Road and Huai Hai Middle Road will also see demand increases.

However, China's formal accession to the WTO is not expected to occur until later this year. Even then China's compliance with WTO requirements will be phased in sector-by-sector. In most service sectors, China has two to five years to phase out current restrictions.

It is useful to think of China's accession to the WTO as a process, rather than an event, and one that is likely to be protracted, involving not merely rolling out the schedule for phasing in compliance with WTO provisions, but also addressing the far more thorny enforcement issues. Because the implementation process is likely to take some time, it may not be until 2002 that oversupply is completely absorbed, the office market fully regains stability, and Shanghai office occupancy levels improve.

If office occupancy levels in Puxi and Pudong over the coming year keep rising by 2.16 percent and 2.2 percent per quarter, respectively, it is quite plausible that by year-end 2000, prime office buildings in Pudong and Puxi will have average occupancy rates of 70-80 percent. Under these conditions, the market would see a strong rebound in 2003-05. Nonetheless, the strength and timing of the recovery depends on how smoothly China can implement its WTO entry terms.

Commentary

Finding Good Consultants in China

Consultants in China are a dime a dozen
—here's how to find the one right for your company

Bonnie Furst-Mueller

When I followed the "silk route" to China 10 years ago, I thought "maybe, if I'm lucky, I'll be able to make a living as a consultant here by the year 2010." Chinese companies when I arrived had little use for Western-style paid consultants. Many general managers in China of both Chinese and foreign ventures, wisely doubtful that consultants could add to their already thin bottom lines, were reluctant to engage consulting services.

So nothing could have convinced me then that consultants would develop a presence in China as quickly as they have since I've been here. I would not have predicted that by 1999, until November not a great year for US-China relations or business, most large international consulting firms would have at least representative offices in China. But they are here, and they are making their presence known.

On a more personal level, this month a researcher from an international think tank asked a friend of mine if he could provide her with a list of domestic Chinese consulting firms. Until last year, however, there weren't many Chinese consulting firms to speak of. Now there are many. Early in 1999, I was asked to join a China-based, foreign-owned consulting firm that had, to my surprise, been doing business in China for several years already. This past fall, one of the "big eight" American consulting firms tried to recruit two of this firm's consultants. On the one hand, it was a compliment. On the other, it was a wake-up call.

Why the recent rush of big consultancies to China? Like other multinational corporations, no one wants to be left out, especially once China accedes to the World Trade Organization (*see* table). MNCs in China are grappling with larger and more complicated issues and technology as China progresses toward developed country status. And other firms, feeling profit pressure, are looking for alternatives to hiring full-time expatriates to handle many of these more complex technical and global tasks. Moreover, while localization is under way, it will still be some time before local PRC staff are qualified to handle such tasks independently.

So, for better or worse, the consulting business is growing in China and the competition is heating up. As the number of foreign and local consultants swells in China, general and other senior managers find themselves spending more time sorting through messages and sales calls to determine which consultant they should use and why.

At best, managers in China will learn from the experience of their counterparts in the United States and avoid some of the big mistakes that have been made there. In their 1998 bestseller *Dangerous Company* (Penguin USA), James O'Shea and Charles Madigan warn executives in the United States and elsewhere to beware of consulting firms. And with good reason: too many consultants promise that which they cannot deliver; fail to practice what they preach; and waste more money than they make or save for their clients.

The book's last chapter, "Keeping Dangerous Company: Caveat Emptor," should be required reading for every manager, especially those now in Asia, as the big consulting firms head eastward and younger Asian-owned consulting firms try their hand at the consulting business. This chapter sums up the lessons learned and provides practical guidelines managers can use to determine if consulting is for them and to sort the good consultants from the bad. In China, where there is so little experience with consultants, the danger of managers making the mistakes highlighted in the chapter, if not bigger ones, is quite real.

Below is some advice I have developed that may help companies steer their way clear of unnecessary and incompetent consulting providers.

● Why seek outside advice?

In general, consultants provide assessments and evaluations; hands-on assistance in creating or changing policies or procedures; training; project management; and staff-development

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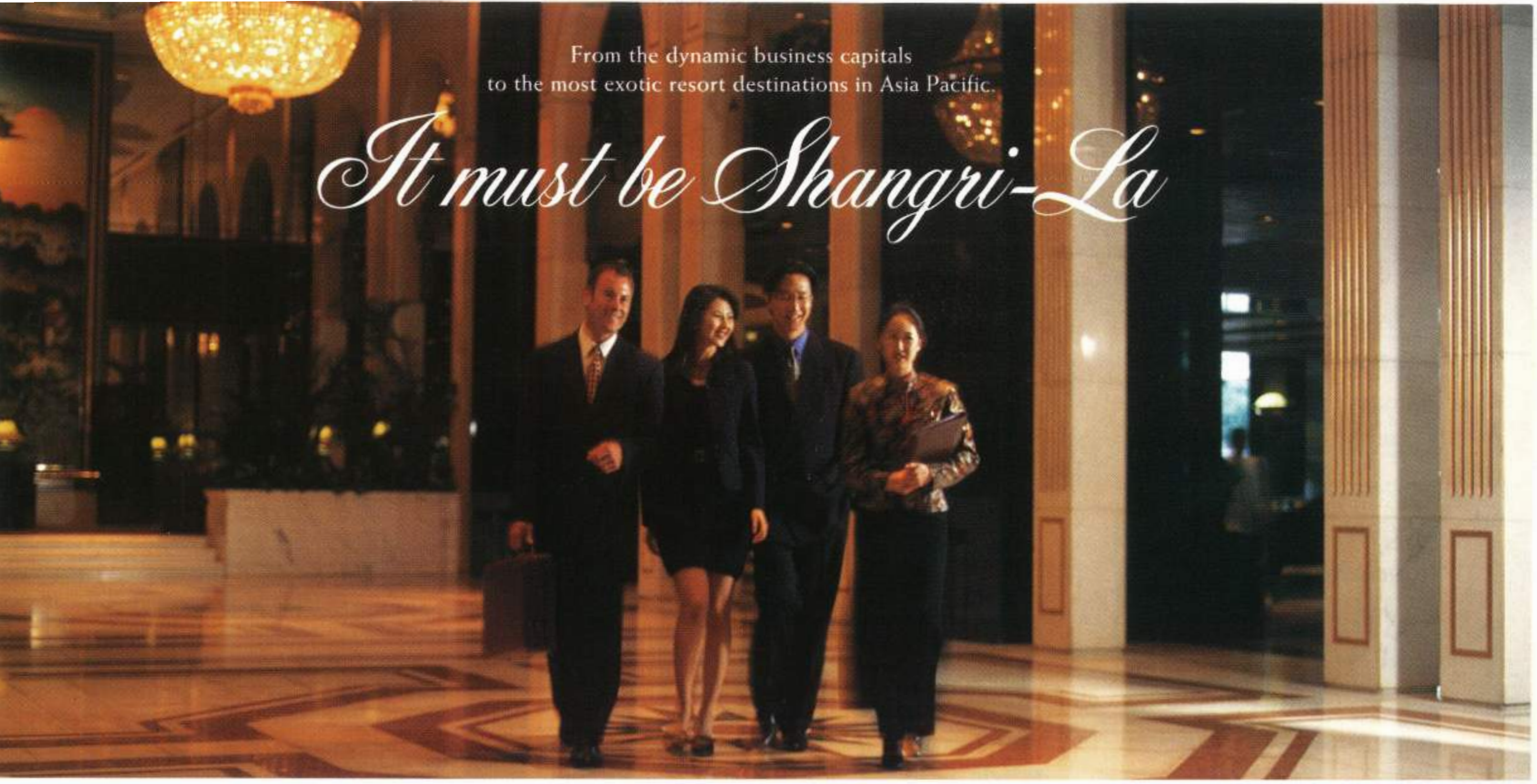
(*bfurst@mailhost.cinet.com.cn*) is a Beijing-based human resources consultant with Universal Ideas, a China-focused training and education consulting firm. She has worked in China for over six years as an HR executive trainer and consultant. A graduate of Harvard University and the Wharton School of the University of Pennsylvania, she has developed personnel- and quality-management systems for over 12 years for companies in China, Hong Kong, Japan, Korea, and the United States, and managed HR functions in the manufacturing and service industries.



Shangri-La Hotel, Beihai, China | Shangri-La Hotel, Beijing, China | China World Hotel, Beijing, China | Traders Hotel, Beijing, China | The Kerry Centre Hotel, Beijing, China | Shangri-La Hotel, Changchun, China

Shangri-La Hotel, Dalian, China | Shangri-La Hotel, Hangzhou, China | Shangri-La Hotel, Harbin, China | Shangri-La Hotel, Qingdao, China | Pudong Shangri-La, Shanghai, China | Traders Hotel, Shenyang, China

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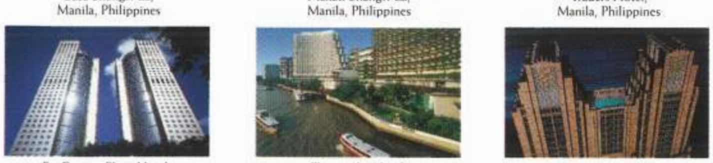
Shangri-La Hotel, Kuala Lumpur, Malaysia | Shangri-La Hotel, Penang, Malaysia | Shangri-La's Golden Sands Resort, Penang, Malaysia | Shangri-La's Rasa Sayang Resort, Penang, Malaysia | Traders Hotel, Yangon, Myanmar | Shangri-La's Mactan Island Resort, Cebu, Philippines

Edsa Shangri-La, Manila, Philippines | Makati Shangri-La, Manila, Philippines | Traders Hotel, Manila, Philippines | Shangri-La Hotel, Singapore | Shangri-La's Rasa Sentosa Resort, Singapore | Traders Hotel, Singapore



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In developing economies, it is not unusual to seek outside help for general management services—quality and information systems; tax, accounting, and legal support; and recruiting and human resources.

support. Companies can benefit from consulting help when they need:

- **Skills that are lacking in country**

Companies entering Chinese markets with new products that use special technologies commonly import experts to explain to local employees how the technologies work and how to use them. Large MNCs often bring staff from their operations in other countries to China as consultants, particularly to complete technology transfers.

In developing economies, it is not unusual to seek outside help for general management services—quality and information systems; tax, accounting, and legal support; and recruiting and human resources. In the last few years, Chinese managers have quickly acquired competency in many of these areas. Often all they need is the perspective of mature consultants able to provide examples from other companies and industries, and increase their confidence by providing real-time feedback on the approaches they are using to solve their companies' problems.

- **Help on a short-term project but cannot add or import staff**

Consulting assignments that assist with specific projects that a company cannot complete on its own can be a real win-win situation for both the consultant and the company. The consultant comes to understand the organization in depth and appreciate its business problems, internal politics, and culture. And the temporary nature of the relationship allows the company flexibility over its costs that it might not otherwise enjoy with full-time staff. While it is true that a company can often assign extra work or projects to existing staff, there are times when this is impossible. In these instances, using a consultant to handle the short-term project is a practical alternative.

Many multinationals import their own staff from abroad—but for some companies, the travel and lodging costs of this option can be prohibitive, and the staff may not be able to communicate in Chinese. In these cases companies may opt for locally based consultants (both foreign and Chinese) with the appropriate China experience, and technical and consulting skills. These consultants can also act as liaisons with visiting expatriates, keeping a given project on track between visits.

- **An objective perspective or unbiased feedback on sensitive projects**

When the board of directors or top management requires a fresh or objective perspective on proposals under consideration, they often call in outside consultants. Companies are in many ways like families; employees must feel comfortable working together, and this puts constraints on how willing they will be to speak their minds about sensitive issues to the very people who make decisions about their pay, bonuses, and promotions.

Similarly, outside consultants are useful for sensitive projects that can generate bad feeling or compromise teamwork among in-house staff. Independent placement agencies and other human resource consultants often help with downsizing or other sensitive employment-termination situations. And in cases where an unbiased third party should be involved, such as in arbitration or other types of separations, the consultant can serve both as a witness and a calming force.

- **New ideas or to know what others are up to**

Consultants can also be sources of new ideas. In-house employees are sometimes too close to their work to find new approaches to solving problems or getting things done. As members of employee teams, consultants can ask questions that might not have occurred to existing staff.

When companies need to know other companies' strategies and solutions, consultants can sponsor benchmarking studies that allow for an exchange of information among companies. Consultants can also make suggestions in a general way based on their experiences with other companies.

- **To jump-start change**

Sometimes organizations want to shake people up, especially if the company has been doing well and the staff has become complacent. Consultants can kick off initiatives and forums for discussion, training, and other employee activities that can lead to change.

Where to go from here?

Deciding whether or not to use a consultant may be difficult, but finding one that is right for your organization can be even more so. Companies should require the following in any consultant they hire:

- **A track record that provides evidence of the consultant's ability to assist with their situation.**

In particular, the consultant must have relevant industry, product, or market experience to succeed in the project.

- **Appropriate and verifiable academic, technical, and professional credentials**
- **Credible and positive references**
- **Technical competencies, including the necessary language skills**
- **Interpersonal skills to work constructively and productively with in-house staff.**

These skills must include demonstrated familiarity with staffs' respective cultural and national backgrounds. Many consultants, otherwise extremely capable technically, may be woefully poor at communicating and working with people to get things done.

Other considerations that may be important include finding out what people in your organization think of the consultant— before making any hiring decisions. Indeed, companies should beware of consultants who look good in suits. Just because a person claims to be a consultant doesn't mean he or she has the skills, abilities, or track record to back up those claims. In China, people tend to trust, and hire, their friends. Don't be afraid to ask to see credentials, get ref-

erences, and check them during a thorough due diligence process. Unfortunately, in China, many consultants put more energy into marketing than quality control, and some have "played the fool's game." Consulting is still new to China and even foreigners can be fooled by consultants who speak a little Chinese and have been here for a while. Checking project references and doing due diligence is just as important in China as it is in the West, if not more so.

It is also important to identify the true costs of using an external consultant, an internal consultant, or no consultant. Compare costs for travel and related lodging, meals, and local transportation; long-distance telecommunications (faxes and long-distance calls); and other out-of-pocket expenses that existing staff would not incur.

Companies should evaluate any guarantees or warranties the consultant offers. Experienced

Selected US Consulting Companies with Offices in China

Company	Beijing	Shanghai
ABC Business Consulting, Inc.	x	
Alpha Ultima, Inc.	x	
Altman Companies	x	
Amer-China Partners Ltd.	x	
Andersen Consulting	x	
Aon Corp.	x	
APCO Associates Inc.	x	
Arthur Andersen-Hua Qiang, CPA	x	x
Asia Systems Media	x	
A.T. Kearney	x	
Bain & Co. China Inc.	x	
Batey Burn & Co., Inc.	x	
BDA China Ltd.	x	
Booz-Allen & Hamilton Inc.		x
Chelbi Engineering Consultants (unit of Louis Berger International, Inc.)	x	
China-Europe International Business School (CEIBS)	x	
China Business Group	x	x
China Concept Consulting	x	
China-US Business Advisors, Inc.	x	
Clear Thinking	x	
CMG Mahon (China) Investment Management Ltd.	x	
Deleuw Cather Int'l., Inc.		x
Deloitte Touche Tohmatsu Accounting office	x	
Delta Staffing Services	x	
Drake Beam Morin (Hong Kong)	x	
Dun & Bradstreet International Consultant (Shanghai) Co.		x
Eastsky LLC	x	
EDS Hong Kong Ltd.	x	
Egon Zehnder Int'l., Ltd.	x	
Environmental Resources International	x	
Ernst & Young Hua Ming	x	x
Euro Group International, Inc.	x	
Gallup Research Co., Ltd.	x	
GML Consulting, Ltd., Beijing	x	
Gnix Transpacific Inc./China Business Update	x	
Great Poplars Co.	x	
Hewitt Associates LLC	x	x
I Will Not Complain	x	
I.T. Unicorp Information Technologx (Beijing) Co., Ltd.	x	
Intercedent Int'l Ltd.	x	
Jett Group, Inc. (China)	x	
Kamsky Associates, Inc.	x	
KPMG Peat Marwick Huazhen	x	
Kroll Associates (Asia) Inc.	x	
Lynton John & Associates	x	
McKinsey & Co., Inc. China	x	
MTI Beijing Rep. Office	x	
Nicholson International	x	
Norman Broadbent International	x	
Pacific Business Development, Inc.	x	
Pacific Resources International, LLC	x	
Pacific Rim Resources		x
Pepper International Associates	x	
Pinkerton (China) Inc.	x	
PricewaterhouseCoopers	x	x
Pro Re Nata (PRN)	x	
RSA Media Relations	x	
Steelcase Asia Inc.	x	
Sterling Enterprise (China) Inc.	x	
Tory Haythe (formerly Haythe & Curley)	x	
Times Mirror Pte. Ltd.	x	
U.I. Consultants	x	
Unison International	x	
Watson Wyatt Worldwide	x	
Wilbur Smith Associates	x	
William Kent International (WKI)	x	

SOURCES: *American Chamber of Commerce PRC 1999-2000 Membership Directory, American Business in China 1998-1999,* US-China Business Council files

Note: This is listing is not meant to be comprehensive and in most cases has not been independently verified by *The CBR.*

consultants will not make impossible promises, nor will they be afraid to make part of their remuneration dependent upon achieving measurable, satisfactory results.

Finally, networks and *guanxi* are everything in China. The bad news is you need to watch out for people hiring friends who may not be qualified to help you with your projects. The good news is you can check instantly with several established networks to hear about other people's experiences with most consultants.

As China integrates further into the international economy, and companies operating there face more sophisticated problems, company managers will increasingly need to consider using consulting services. But sorting the good ones from the bad will remain just as much of a challenge. Proceed with caution, look for consultants who are flexible and willing to work on specific projects with clearly defined deliverables, and hold them to it. Obtain proposals from at least three sources and compare. There are many talented and experienced people waiting to help in China. With a little effort, you can find good guides to help you along today's silk route.

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To Avoid Common Pitfalls, Look Before You Leap

China's October 1999 celebration of its 50th birthday was a time for many to reflect on the country's tremendous achievements. Yet behind the revelry, many chief executives had been thinking long and hard about the inability of their businesses to turn a real profit in China. And some equity investors had reportedly been pulling back because of poor profits and fraud. Chinese authorities over the past year indeed reported an upsurge in fraud, and officials have been probing possible criminal aspects of the notorious Guangdong International Trust and Investment Corp. (GITIC) bankruptcy, an event that put much lending to China on hold indefinitely (*see The CBR*, May-June 1999, p.36). Foreign direct investment fell dramatically in 1999, leading some analysts to declare that the China investment honeymoon was over.

The mood might now shift more in favor of investment again, with China's World Trade Organization (WTO) entry now within its grasp. China's effort to join the WTO and to restructure, or quasi-privatize, state-owned enterprises (SOEs) has prompted many companies and investors to eye potential new opportunities. China's accession to the WTO implies a reduction in trade barriers and tariffs, and a liberalized business environment—especially in the services sector—that could unleash a new stampede into the China market from overseas. The bottom-fishing investment and acquisition opportunities that tend to emerge from restructuring and privatization programs could also spark such a gold rush. Such was the case when China began serious reforms in the 1980s, and such was the case in Russia after the collapse of the Soviet Union. But as recent reports have shown, many multinationals were chasing a mirage during those steamy investment years.

China's advancement towards the rule of law and a modern market economy is a development in which the world has a great stake, and that spurs participants to seek ways to develop new business links that will enrich both sides. Events such as Deng Xiaoping's rise to power can speed along this process of development and create opportunities. But other events, such as the Tiananmen upheaval of 1989 or the more recent anti-US protests in Beijing over NATO's bombing of the Chinese embassy in Belgrade, can lead to setbacks. Businesspeople, whether from China or overseas, must heed both the opportunities and the risks that these events and issues present.

Minimizing risk

All sides should be reminded of the need for caution—"due diligence," if you like—when trying to exploit the new opportunities that arise. Due diligence is not merely a tick-the-box examination of balance sheets and legal documents, however. Rather, it is about scrutinizing people and organizations (*see The CBR*, January-February 1999, p.32). It doesn't matter whether you are a Western multinational plunging into what you think is a lucrative deal with a Chinese partner, or a Chinese corporation developing new partnerships and markets overseas. Both sides must examine not only the business environment—but also each other—carefully. In an increasingly global economy, business leaders often conduct business with people they do not know well, without complete information, or with salespeople who oversell their product or distort the real situation.

Off-the-books due diligence provides accurate, timely information on the business management of potential partners, and can help avoid risks resulting from business decisions based on incomplete or faulty information. Through the skillful use of data resources and the discreet use of human sources in industry, government, regulatory bodies, and others close to the potential partner, it is possible to gain a comprehensive understanding of the partners-to-be and make well-informed business decisions. Thorough due diligence should answer the following questions:

- What is the real corporate structure of the company? Who are its key officers, shareholders, and subsidiaries?
- What are the company's true background and current activities?
- What is the potential partner's reputation among its competitors and industry trade organizations?
- What is the company's reputation among its suppliers and its own employees?
- What is the current status of other international joint ventures in which it has been involved? What happened to the last five deals it completed?
- What are the activities and background of the company's management?
- What are the character, integrity, and reputation of key individuals, owners, and key officers?
- What level of political support do they enjoy? Can they really get things done?
- What are the professional and personal relationships like between these individuals?
- Does the available financial information stand up to scrutiny when measured against the human aspects of the organization?
- Does the company have any hidden liabilities? (This is important in a region of the world where many deals have been sealed with a handshake rather than a written contract.)
- Has the company ever been involved in any messy legal disputes?
- Has it ever run into trouble with regulatory bodies, and what do the regulators think of this company?
- Does the company have a history of labor troubles, strikes, or disputes?
- Does the company comply properly with required ethical and social standards? For example, has it ever employed child labor? Do workers get the legally mandated amount of time off?
- Does it comply with environmental regulations, or will it one day be prosecuted for polluting the environment? How would this affect profits or your own corporate principles?

In modern industrial countries, much of this information is relatively easy to obtain using conventional research into media and public records. But in emerging-market economies in Asia and elsewhere, due diligence inquiries rely heavily on the discreet use of professional investigators. In the past, international companies neglected the need for even the most basic human due diligence at their peril: the Asian meltdown two years ago exposed many large-scale frauds, white-collar crime situations, and bad deals that could have been avoided. If those firms had done their due diligence, they might not have lost their shirts when the Asian economies collapsed. The recent economic crisis was a stunning lesson in myopia on the part of international investors and an indictment of the emphasis that they placed on quick profits.

Perform thorough due diligence, find the right partners, and the opportunities that China now presents may really turn out to be golden. Investors should not turn their backs on China. But nor should they rush into deals without knowing their prospective partners well, which is what many did until now. This time, they have the opportunity to get it right.

—*Peter Humphrey*

Peter Humphrey is based in Beijing as the chief representative of Kroll Associates, a US consulting company specializing in business risk mitigation and security solutions. He has spent two decades focused on China and Eastern Europe.

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We strongly endorse the agreement between the United States and the People's Republic of China on that country's accession to the World Trade Organization. This historic agreement underscores the promise of the relationship between our two countries.

China's formal entry into the global trading system will greatly expand long-term opportunities for American and Chinese enterprises and, most importantly, our workers. Citigroup therefore urges early US Congressional approval of permanent Normal Trade Relations status for the People's Republic of China.

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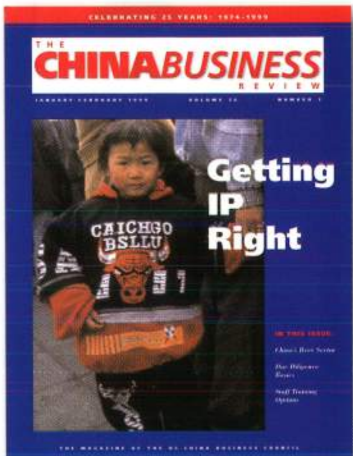

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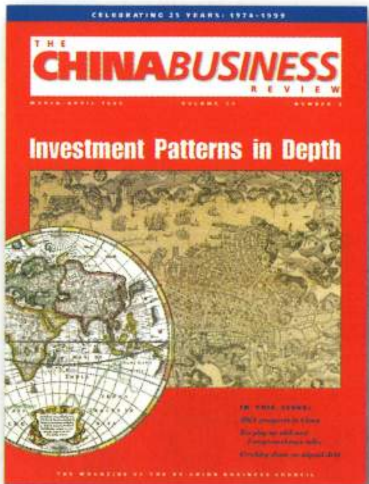
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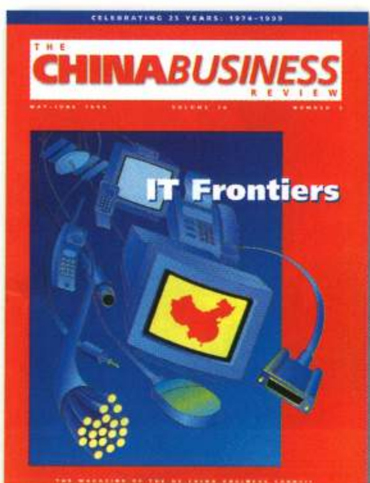
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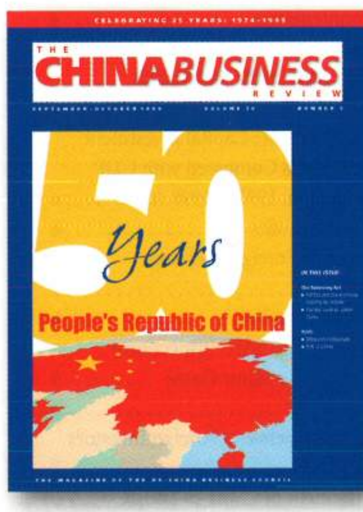
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50 Years
People's Republic of China


THE CHINA BUSINESS REVIEW
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25 Years

Council Bulletin

Upcoming Events

Forecast 2000, Washington

January 25 Evening Reception

January 26 Meeting

Topics: China's Economy: Looking Ahead; China in the WTO: New Business Strategies for US Investors

Speakers: Edward Steinfeld, The Massachusetts Institute of Technology; Joseph Battat, International Finance Corp., the World Bank; John Frankenstein, Asia Research Center, Copenhagen Business School; Sheila Melvin, The US-China Business Council; Patrick Powers, The US-China Business Council; Denis Fred Simon, China Strategy Group, Andersen Consulting LLP

China Business 2000: Trends and Market Opportunities

January 28 Boston

January 31 San Francisco

February 1 Silicon Valley

Topics: New Chinese Approaches to Raising Investment; China's Tenth Five-Year Plan (2001-05): Implications for Business; and China in the WTO: New Trade and Investment Strategies

Featuring: Patrick Powers and Sheila Melvin, The US-China Business Council

China Operations 2000

March 8-9 Beijing

The Council has been working with member companies and PRC officials over the past several months to clarify the implications of a number of new regulations including:

Encryption regulations

State Council Order No. 273, passed in early October, requires that the State Encryption Management Commission (SEMC) (*Guojia Mima Guanli Weiyuanhui*) approve the production and importation of all encryption products. Though the rules are intended to protect China's national security, the regulations, as written, would hinder the import of any software with password options—including common office applications. E-commerce could also be dramatically affected.

To help clarify these and other points, the Council's Beijing staff has been meeting with SEMC officials. It seems that while SEMC registration and approval may be necessary, foreign endusers will be allowed to use foreign encryption products as long as these products are not used to harm China's national interests or security.

Council members can read more about the encryption regulations in the November and December 1999 issues of *China Market Intelligence* (*www.uschina.org/members/publications/cmi*).

Market-research survey regulations

Regulations the PRC State Statistical Bureau (SSB) issued last August on the market-research industry continue to cause confusion. According to the Provisional Management Regulations on Foreign Survey Activities, all domestic survey agencies employed by foreign institutions or individuals; domestic social groups and non-government institutions with missions of conducting social polling; and foreign-funded survey firms and joint ventures with majority foreign stakes must obtain a Foreign Survey License from SSB or its provincial-level branches.

The Council has been discussing with member companies the possible effect of the regulations on business, which remain unclear. The Council has also met with PRC government agencies to learn how the regulations will be implemented (*see below*). Council members may read more about these regulations in the September and November 1999 issues of *China Market Intelligence* (*www.uschina.org/members/publications/cmi*).

Event Wrap-Up

Washington

December

Issues Lunch: A Preparatory Session for the Council's Work in the Year 2000 Featured Council President Robert A. Kapp.

Meeting: China's Aviation Sector Featured Elizabeth Keck, senior representative for China, Mongolia, North Korea, South Korea, and Macao, US Federal Aviation Administration.

Briefing: World Bank Officials on China's Financial Sector Featured Jacques Loubert, director of the Financial Sector Development Unit for the East Asia and Pacific Region; and Akihiko Nishio, country program coordinator for China.

Briefing: China's WTO Accession: Implications for Hong Kong's Economy & US Companies' China Operations Featured Michael F. Martin, former assistant chief economist at the Hong Kong Trade Development Council in Hong Kong.

November

Issues Lunch: US-China WTO Agreement Featured Robert Cassidy, assistant US Trade Representative for China, Hong Kong, Taiwan, and Mongolia; and Robert T. Novick, general counsel in the Office of the USTR.

Legal Interest Group Meeting: Hong Kong's Legal System after the Turnover Featured Justice Barry Mortimer, non-permanent judge of the Court of Final Appeals of the Hong Kong Special Administrative Region.

Beijing

December

Issues Lunch: An Update of Market-Research Regulations Featured Xiong Zhennan, director of the Department of Policies and Legislation, State Statistical Bureau.

Shanghai

December

Issues Lunch: What the WTO Means for China Featured Butch Almstedt, international trade law specialist with O'Melveny & Myers in Washington, DC; and Howard Chao, a Shanghai-based partner with O'Melveny & Myers.

China Business

Sales and Investment

SEPTEMBER 15, 1999 - NOVEMBER 15, 1999

Compiled by Jessica Huang

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

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

Accounting and Insurance

INVESTMENTS IN CHINA

Prudential Plc (UK)/BOC

Formed joint venture to provide asset-management and administrative services for the Mandatory Provident Fund in Hong Kong. 11/99.

OTHER

Royal & SunAlliance (UK)

Increased funding for the Educational Foundation in China for professional development of the Chinese insurance industry. $250,000. 10/99.

Advertising and Public Relations

INVESTMENTS IN CHINA

American Champion Entertainment/Great Wall International Sports Media Co. (Beijing)

American Champion Entertainment will acquire 80% of Great Wall Sports Media. $6 million. 10/99.

OTHER

CARMA International, Inc. (US)

Extended media content analysis services to China market. 9/99.

Agricultural Commodities and Technology

INVESTMENTS IN CHINA

New Holland NV (the Netherlands)/Heilongjiang Beidahuang State Farm Group

Formed Harbin New Holland Beidahuang Tractor Ltd., a joint venture, to produce high-horsepower tractors. 9/99.

Banking and Finance

CHINA'S IMPORTS

Hypercom Corp. (US)

Will provide card payment terminals and smart-card pads to facilitate the Agricultural Bank of China's expansion of credit and debit transactions. 10/99.

Abbreviations used throughout text: ADB: Asian Development Bank; BOC: Bank of China; CAAC: Civil Aviation Administration of China; CNAIEC: China National Automotive Import-Export Corp.; CATIC: China National Aero-Technology Import-Export Corp.; CITIC: China International Trust and Investment Corp.; CITS: China International Travel Service; CNOOC: China National Offshore Oil Corp.; CNPC: China National Petroleum & Gas Corp. ETDZ: Economic and Technological Development Zone; ICBC: Industrial and Commercial Bank of China; MII: Ministry of Information Industry; NA: Not Available; NORINCO: China North Industries Corp.; P&T: Posts and Telecommunications; PBOC: People's Bank of China; SEZ: Special Economic Zone; SINOCHEM: China National Chemicals Import-Export Corp.; SINOPEC: China National Petrochemical Corp.; SINOTRANS: China National Foreign Trade Transportation Corp.; SPC: State Planning Commission; UNDP: United Nations Development Program; UNICOM: China United Telecommunications Corp.

Chemicals, Petrochemicals, and Related Equipment

CHINA'S IMPORTS

IMC Phosphates, a unit of IMC Global Inc. (US)/U.S. Agri-Chemicals Corp., subsidiary of SINOCHEM

Extended contract to sell SINOCHEM phosphate rock for an additional 20 years. 10/99.

INVESTMENTS IN CHINA

BP Amoco Plc (UK)

Will establish ethylene plant in Shanghai. $2 billion. 10/99.

Nippon Synthetic Chemical, Marubeni Corp. (Japan)/Guangdong Fortune Color Picture Tube

Will jointly build production unit. $15 million. 10/99.

Meteor Gummiwerke KH Badje GmbH (Germany), Sida Corp. (US)

Formed Qingdao Meteor Rubber and Plastics Co., a rubber manufacturing joint venture. 9/99.

Nanjing Yangzi Eastman Chemical Ltd., a joint venture between Eastman Chemical Co. (US) and Yangzi Petrochemical Industrial Corp. (Nanjing)

Completed construction of an adhesive production plant in Nanjing, Jiangsu Province. $29.5 million. 9/99.

Orgavyl Chemical Co. (Malaysia)/China Quanzhou Orgavyl Chemical Industries (Fujian)

Formed Fujian Orgavyl Chemical Industries to manufacture inks, paints, adhesives, and rubber products. (Malyasia:51%-PRC:49%). 9/99.

Prodair Corp., a subsidiary of Air Products and Chemicals, Inc. (US)/Chun Wang Industrial Gases Ltd. (Guangdong)

Prodair acquired remaining 50% of Chun Wang Industrial Gases. 9/99.

SAL Petrochemical Co., a joint venture between Asahi Chemical Industry Co. (Japan) and Dow Chemical Co. (US)

Will construct a polystyrene plant in Jiangsu Province. (Japan:50%-US:50%). 9/99.

Taoka Chemical (Japan), NA (Taiwan)

Formed production joint venture in Hangzhou, Zhejiang Province. (Japan:50%-Taiwan:50%). 9/99.

OTHER

Rohm and Haas Nantong Chemical Co., a joint venture between Rohm and Haas Co. (US) and Baoling Chemical (Zhejiang)

Will build new facility in Nantong, Zhejiang Province. (US:82%-PRC:18%). 10/99.

Royal Dutch/Shell Group (UK-the Netherlands)
Sold its 60% stake in its Chinese joint venture to Chinese partner, Jinling Petrochemical. 10/99.

Consumer Goods

CHINA'S IMPORTS

Chindex International, Inc. (US), C.B. Fleet Co., Inc. (US)
Chindex will market and distribute Fleet's feminine hygiene products in China. 11/99.

Hallmark Cards Inc. (US)
Set up plant in Jinqiao Export Processing Zone in Shanghai to manufacture cards. 11/99.

INVESTMENTS IN CHINA

Marubeni Corp. (Japan)/Shanghai Number One Department Store Group Corp.
Set up joint-venture wholesale store. $10 million. 10/99.

OTHER

Unilever Plc (UK)
Increased its stake in Unilever Co., Ltd., its Shanghai-based joint venture, from 50% to 76%. $100 million. 10/99.

Electronics and Computer Software

CHINA'S IMPORTS

ATI Technologies Inc. (Canada)
Will provide graphics and video services for new models of Legend computer systems in Beijing. 11/99.

DV Studio Technologies LLC (US)
Signed distribution agreement with Accelerated Computech International of Beijing to implement DVD technology. 9/99.

Samsung Electronics (Korea); OTI China, a subsidiary of On Track Innovations Ltd. (Israel)
OTI China won right to market Samsung chip products along with its own smart-card technology in Chinese market. 9/99.

SeaChange International, Inc. (US)
Will supply interactive television technology to Guangdong Cable Television. 9/99.

STM Wireless, Inc. (US)
Will supply Shanghai Automobile Industry Sales Co., a subsidiary of Shanghai Automobile Industry Corp., with video-conferencing technology. $1 million. 9/99.

INVESTMENTS IN CHINA

AMI DODUCO, a unit of Technitrol (US)/Tianjin Xinhao Investment Development Co.
AMI DODUCO completed acquisition of Tianjin Electrical Metal Works. 11/99.

EnReach Technology (US), Seagate Technology, Inc. (US)
Established partnership to bring personalized TV and video recording to China. 11/99.

Rainbow Technologies, Inc. (US)/Goldensoft Co. Ltd. (Beijing)
Formed Rainbow Goldensoft Co. Ltd., a joint venture to market e-business and software security in China. 11/99.

Zi Corp. (Canada)/Beijing OZ Education and Network System Co. Ltd.
Zi Corp. completed acquisition of Beijing OZ to enter the Chinese web-based education and career training market. 11/99.

Digiland Pte Ltd. (Singapore)/East China Computer Co. Ltd. (Shanghai)
Formed Shanghai East China Computer Liqi International Trading Co. Ltd., a trade-facilitation joint venture. (Singapore:52.5%-PRC:47.5%). $5 million. 10/99.

GES Pte Ltd. (Singapore)/East China Computer Co. Ltd. (Shanghai)
Established Shanghai East China Computer Qiyi Information Technology Co. Ltd., a joint venture to develop and produce computer parts. (Singapore:75%-PRC:25%). $8 million. 10/99.

ODS Networks Inc. (US)/SuperTech Systems Inc. (Hunan)
Formed joint venture to develop China's first domestic network switching equipment plant in Changsha, Hunan Province. $50 million. 10/99.

Shum Yip Investment (Hong Kong)
Will acquire 20% of Saige Hitachi, a Chinese television-set producer. $26.6 million. 10/99.

Brightpoint, Inc. (US)
Formed Sunrise International Ltd. in collaboration with Brightpoint China Ltd., its Chinese venture, to facilitate sourcing and distribution of wireless products. 9/99.

New World CyberBase Ltd. (Hong Kong)/Beida Jade Bird Co. Ltd. (Beijing)
Formed Internet hardware and software research and development joint venture. $9.8 million. 9/99.

Oy Nokia AB (Finland)
Formed Nokia-Citic Digital Technology Co. Ltd., a joint venture through its China unit, Nokia (China) Investment Co. Ltd., to make set-top boxes in Beijing. $29.9 million. 9/99.

Texas Instruments Inc.(US)/Great Wall Science and Technology Co. Ltd. (Beijing), China Putian Information Industry Group Co. (Fujian), Eastern Communications Co. Ltd. (Zhejiang)
Formed Changxiajia Information Technologies Co. Ltd., a joint venture in Beijing specializing in digital information design. (US:30%-PRC:70%). $10 million. 9/99.

OTHER

World Bank
Will finance collaboration between Legend Holdings Ltd. of Beijing and the China State Administration of Taxation for tax collection and administration information systems project. $24 million. 11/99.

Metrologic Instruments, Inc. (US)
Opened new facility, Metro Technologies Co. Ltd., in Singapore-Suzhou Industrial Park, Anhui Province. 10/99.

Philips Institutional TV, a unit of Royal Philips Electronics NV (the Netherlands), MyWeb Inc.com (US)
Unveiled new product aimed at the Chinese Internet market that combines set-top box, a TV portal, and a television. 10/99.

Quantum Corp. (US)
Established training facility for computer storage technology at Beijing University of Aeronautics and Astronautics. 10/99.

Dell Computer Corp. (US)
Opened Application Solution Center in Shanghai. 9/99.

Engineering and Construction

CHINA'S IMPORTS

Samsung Engineering Co. (Korea)
Will build chemical plant for Shanghai BASF Colorant Auxiliaries Co., a joint venture of BASF AG of Germany. $20 million. 10/99.

INVESTMENTS IN CHINA

AsiaTrak (Tianjin) Ltd., a joint venture among Caterpillar Inc. (US), SNT Corp. (US), and Itochu Corp. (Japan)
Opened new 18,000 sq m facility in Tianjin for undercarriage products. 10/99.

Daewoo Motor Co. (Korea)/China First Automobile Works Group Corp. (Shanghai), Shandong Automobile Corp.
Jointly opened three automobile component plants in Yantai, Weihai, and Qingdao, Shandong Province. $730 million. 10/99.

The Boeing Co., Hexcel Corp., Inc. (US)/Aviation Industries of China
Formed BHA Aero Composite Parts, to build a plant in Tanggu, Tianjin Municipality for research, development, and manufacturing of aircraft parts. 9/99.

OTHER

World Bank
Granted loan to Lafarge Dujiangyan Cement Co. Ltd., a Sino-French joint venture, to build a cement plant in Sichuan Province. $55.6 million. 10/99.

Environmental Technology and Equipment

CHINA'S IMPORTS

Euro Tech (Hong Kong), Royce Instrument Corp. (US)
Royce will use Euro Tech's manufacturing facility in Shanghai to assemble environmental technologies for sale in the China market. 11/99.

Dasibi Aeron Inc., a subsidiary of Pollution Research and Control Corp. (US)
Will market vehicle emission compliance programs and equipment in China. $5.2 million. 10/99.

INVESTMENTS IN CHINA

Pan Kai Development USA Inc., Quantum Environmental Systems LLC (US)
Formed joint venture to manufacture and distribute anti-pollution systems in China. 9/99.

Food and Food Processing

OTHER

Koninklijke Ahold NV (the Netherlands)
Sold stakes in its Chinese joint venture. 10/99.

McDonald's Corp. (US)
Announced plans to introduce a franchise network in China. 10/99.

Machinery and Machine Tools

INVESTMENTS IN CHINA

Sulzer Pumps, unit of Sulzer Technology Corp. (Germany)/NA (Liaoning)
Will form Sulzer Dalian Pumps and Compressors Ltd., a joint venture in Dalian, Liaoning Province. $1.9 million. 10/99.

Tamfelt Oy AB (Finland)/Tianjin Paper Net Factory
Formed joint venture to manufacture textile equipment. (Finland:60%-PRC:40%). $2.6 million. 10/99.

Savera Group (Spain)/Lanfang CABR New Development (Beijing), Beijing Shougang Machinery & Electric
Formed joint venture to manufacture steel guide rails. $9 million. 9/99.

Medical Equipment and Devices

CHINA'S IMPORTS

Coronado Industries Inc. (US), Everblooming Enterprises Co. (US)
Everblooming Enterprises will provide international marketing and distribution for Coronado's PNT medical devices in China. 10/99.

Dasibi Logan Technologies Inc., a subsidiary of Pollution Research and Control Corp. (US)
Will market asthma medical equipment in China. 10/99.

INVESTMENTS IN CHINA

Roche Holding AG (Switzerland)/Shanghai No. 6 Pharmaceutical Factory
Will open a vitamin A plant as part of its joint venture. (Switzerland:70%-PRC:30%). 10/99.

NA (US)/Nanjing Pharmaceutical Group (Jiangsu)
Formed Nanjing Huali Pharmaceutical Bioengineering Co. Ltd. to research and develop new drugs for the Chinese market. $10 million. 9/99.

OTHER

BioChem Pharma Inc. (Canada)
Completed development of first oral treatment for hepatitis B for the China market and received drug certificate for exclusive manufacture of the product in China. 10/99.

Shanghai Omni Gear, manufacturing unit of Omni U.S.A., Inc.
Received loan from PACCAR Inc. of the United States as part of power-transmission distribution agreement. $1 million. 10/99.

Metals, Minerals, and Mining

CHINA'S IMPORTS

Gemcom Software International (Canada)
Will supply state-owned China Gold with software to improve technical capability and help develop the Chinese gold industry. 9/99.

INVESTMENTS IN CHINA

Hoelter Technologies Holding AG (Germany)/Government of the PRC
Signed agreement with City of Fushun, Liaoning Province, to transfer technology for a coal treatment facility. $5.3 million. 10/99.

Latsis Group (Greece)/Kyriakidis (Shanghai)
Formed joint venture to process European marbles for sale in China. (Greece:53%-PRC:47%). $6 million. 10/99.

ECC International (UK)/Fujian Jiuzhou Longyan Gaolin Co.
Formed joint venture to produce 3.05 million tons of wire mesh. $19.02 million. 9/99.

Krupp Thyssen Stainless GmbH (Germany)/Shanghai Pudong Steel
Will jointly build a steel mill in Shanghai, with initial financing from the World Bank of $294.8 million. (Germany:60%-PRC:40%). $1.4 billion. 9/99.

Miscellaneous

INVESTMENTS IN CHINA

IMAX Corp. (Canada)/Shanghai Technology City
Signed agreement to build two theaters for a science-education and entertainment complex due to open in 2001 in Pudong, Shanghai. $181 million. 11/99.

International Smart Sourcing, Inc. (US)
Opened new facilities in Shanghai. $2 million. 9/99.

TPG Post Group NV (the Netherlands)/Government of the PRC
TPG set up joint venture with Chinese Postal Bureau to facilitate international express transport. 9/99.

OTHER

Government of Brazil/Government of the PRC
Will launch first series of joint scientific research satellites. $300 million. 10/99.

Ultrak, Inc. (US)/BOC
Will provide security for BOC's new headquarters in Beijing. 10/99.

MyWeb Inc.com (US)
Signed agreement with Beijing Yinjian Co. Ltd., a taxi operator, to provide delivery services for MyWeb's e-commerce goods. 11/99.

Petroleum, Natural Gas, and Related Equipment

INVESTMENTS IN CHINA

Royal Dutch/Shell Group (UK-the Netherlands)/CNPC
Formed joint venture to open up gas field in Inner Mongolia. $3 billion. 9/99.

OTHER

Government of South Korea
Will join Government of Russia; Russia Petroleum, a joint venture of BP Amoco (UK) and Sianko (Russia); and China National United Oil Corp. in the research and development of a gas pipeline from Eastern Siberia to China. 10/99.

Mondo Group (US), Nido Petroleum Ltd. (Australia)
Nido Petroleum will acquire 40% interest in the Zhongyuan Redevelopment Project oil field in Henan Province from the Mondo Group. 9/99.

Pendaries Petroleum Ltd. (US)
Increased interest in Bohai Bay project from 10% to 18.2%. 9/99.

Ports and Shipping

INVESTMENTS IN CHINA

FedEx, a unit of FDX Corp. (US)/Datian W. Air Service Corp. (Tianjin)
Formed joint venture in Beijing to allow direct service to clients. (US:50%-PRC:50%). 11/99.

OTHER

FDX Corp. (US)
Started service to Shenzhen, Guangdong Province. 11/99.

Norton Lilly International (US)/China Shipping Group
Formed China Shipping (North America) Agency Co., a joint venture, to expand capacity of Pacific trade. 10/99.

Power Generation Equipment

CHINA'S IMPORTS

Apollo International (US)
Will provide generators and protection equipment to Tianjin Datang Panshan Power Generation Co. Ltd. $304,000. 11/99.

INVESTMENTS IN CHINA

ABB AG (Switzerland)/Zhongshan Transformer Co. Ltd. (Guangdong)
Established joint venture to manufacture power transformers. $30 million. 10/99.

ABB Alstom Power, joint venture between ABB AG (Switzerland) and Alstom Energy (France)
Signed contract to build a hydro-electric power plant in China. $36.8 million. 10/99.

Singapore Power Ltd., Asia Pulp & Paper (Singapore)
Singapore Power acquired 51% stake in three Chinese plants owned by Asia Pulp & Paper. $197 million. 10/99.

BICCGeneral (US)/Jiangsu Baosheng Group Co. Ltd.
Formed joint venture to manufacture and market power cables. (US:66.7%-PRC:33.3%). $13 million. 9/99.

Metering Technology Corp. (US), Cisco Systems (US), China-American System Technology/MTC China, a joint venture between MTC and China State Power Corp.
Will equip nationwide energy accounting system with MTC electric metering systems. 9/99.

Property Management and Development

INVESTMENTS IN CHINA

Marubeni Corp. (Japan)/NA (Shanghai)
Formed joint venture to develop residential housing in Shanghai. $83 million. 10/99.

Telecommunications

CHINA'S IMPORTS

Nortel Networks Corp. (Canada)
Won GSM contracts in Henan and Anhui provinces. $63 million. 11/99.

Philips Consumer Communications, a business group of Philips Consumer Electronics, a division of Royal Philips Electronics (the Netherlands)
Will sell new wireless handset equipped with Chinese language databases for GSM networks in China. 11/99.

Aladdin Knowledge Systems (US)
Will distribute its Internet and software security products through the Chinese firm ZISCO Information & Technology Co. Ltd. 10/99.

Clarent Corp. (US)
Will supply IP telephony products to China Telecom. 10/99.

FORE Systems, a subsidiary of The General Electric Co. (US)
Will help Guangdong P&T Administration expand its broadband network. 10/99.

LM Ericsson AB (Sweden)
Will supply wireless solutions for UNICOM's GSM expansion in Sichuan Province. $55 million. 10/99.

LM Ericsson AB (Sweden)
Will supply GSM network technology to Shandong Mobile Communications Corp. $102 million. 10/99.

Lucent Technologies (US)
Will provide Konka Group Co. Ltd. of Guangdong with the latest mobile technologies to help Konka enter the Chinese mobile phone industry. 10/99.

Qualcomm Inc. (US)
Will provide satellite data services to Guangdong South Satellite Telecommunications Service Co. Ltd., a subsidiary of Guangdong Nanfang Communications Group. 10/99.

Symbol Technologies, Inc. (US)
Will provide on-campus LAN connection with wireless technology for Nankai University of Tianjin. 10/99.

Lucent Technologies (US), Mobicom Corp. (US)
Will jointly develop wireless handsets for China's GSM market. 9/99.

Network Equipment Technologies, Inc. (US)
Will help Shaanxi P&T and Jilin P&T administrations upgrade and expand their digital data networks to multiservice platforms through their distribution partner, Datacraft China. 9/99.

Nortel Networks Corp. (US)
Will assist in developing wireless network for Henan UNICOM. 9/99.

Nortel Networks Corp. (US)
Will assist Shandong P&T Administration with the development of a multimedia network. 9/99.

Texas Instruments Inc. (US)/Eastern Communications Co., Ltd. (Zhejiang)
Formed joint venture to research, develop, and design digital information products. $7 million. 9/99.

Zi Corp. (Canada)
Will provide software to Synchronization Inc., a subsidiary of Eastern Communications Co. Ltd. of Zhejiang Province, for integration with GSM mobile phones. 9/99.

INVESTMENTS IN CHINA

China Telecom (Hong Kong) Ltd.
Will acquire three mobile telephone networks in Fujian, Henan, and Hainan provinces from its parent company, China Telecom. $6.4 billion. 10/99.

The Hartcourt Co. Inc. (US)/Innostar HiTech Enterprises (Beijing)
Entered into joint venture to establish a nationwide ISP and IP phone service in China. $1.6 million. 10/99.

Macao Telecommunications/UNICOM
Formed joint venture to conduct automatic roaming for mobile communication. 10/99.

Oy Nokia AB (Finland)/CITIC Technology Co. Ltd., Academy of Broadcasting Science
Established joint venture to manufacture digital multimedia terminals for the Chinese market. $29.9 million. 10/99.

Tianrong Internet Products and Services, Inc. (US)/Chongqing Wordtech Technology Co. Ltd. (Chongqing)
Tianrong will acquire Chongqing Wordtech Technology Co., a Chinese ISP. 10/99.

United Media Holdings Ltd. (Hong Kong)
Established Chinese-language entertainment Internet portal, ChineseE.com. 10/99.

Oy Nokia AB (Finland)/Beijing Telecommunications Co., Eastern Communications Co. Ltd. (Zhejiang), BOC (Beijing)
Signed contract to expand GSM network in Beijing. $208 million. 9/99.

Radyne ComStream Inc. (US)/Beijing Aerospace Satellite Applications Co.
Signed contract to supply China Qingdao Hai'er Group with Radyne technology to facilitate nationwide Intranet. $375,000. 9/99.

OTHER

Greg Manning Auctions, Inc. (US)/GMAI-Asia.com (Beijing)
Jointly opened Internet service center in Beijing. 11/99.

Natural Microsystems Corp. (US)/Delta Telecommunications (Shanghai)
Natural Microsystems will provide support and services to Delta's Value-added Product Services Division. 11/99.

International Data Group (US)
Will invest $1 billion of venture capital in Internet-related companies in China. 10/99.

Oy Nokia AB (Finland)/Research Institute of Telecommunications Transmission, a unit of MII
Will cooperate to develop WCDMA technology in China. 10/99.

Teleglobe Communications Corp. (Switzerland)
Opened corporate office in Beijing. 10/99.

Twinbays International, Inc. (US)/Xidan Department Store Group (Beijing)
Twinbays will host Xidan's online auctions. $1.2 billion. 9/99.

Yahoo! Inc. (US)/Beijing Founder Electronics Co.
Cooperated to launch Chinese-language portal. 9/99.

Textiles and Apparel

INVESTMENTS IN CHINA

Valmet Corp., the Fiber and Paper Technology business of Metso Corp. (Finland)
Announced plans to open a new Technology Center in Jiangsu Province by 2001. $11.4 million. 11/99.

Acordis, subsidiary of Akzo Nobel NV (the Netherlands)/Wuxi Taiji Co. (Shanghai)
Will form joint venture to produce and sell polyester and other fabrics in China. (the Netherlands:60%-PRC:40%). 9/99.

Transportation

CHINA'S IMPORTS

Bombardier Aerospace, a unit of Bombardier Inc. (Canada)
Sold five jet aircraft to Shandong Airlines. $116 million. 11/99.

Airbus Industrie (France)/Government of the PRC
Government of PRC signed a deal for 28 Airbus planes. $2.5 billion. 10/99.

INVESTMENTS IN CHINA

Bombardier Transportation, a unit of Bombardier Inc. (Canada); Power Pacific Corp. Ltd., a subsidiary of Power Corp. (Canada)/Sifang, a subsidiary of the Ministry of Railways.
Formed joint venture to manufacture passenger coaches, subway cars, commuter cars, and other high-speed inter-city vehicles. (Canada:50%-PRC:50%). $235.7 million. 11/99.

Toyota Motor Corp. (Japan)/Tianjin Automotive Industrial Group Co.
Will form joint venture to produce Toyota models in China. 11/99.

Air International Co. Ltd. (Shanghai), unit of Futuris Corp. Ltd. (Australia)/Brilliance China Holding Ltd. (NA)
Formed joint venture to design and manufacture automotive systems and components. (Australia:60%-PRC:40%). 10/99.

Motorola Inc. (US)/Nanjing Public Transit IC Card Co. Ltd. (Jiangsu)
Will cooperate in the design and implementation of a smart-card system for use in public transportation. 9/99.

NA (Taiwan)/Fuzhou Automotive Works, a unit of the Fujian Auto Group
Completed the construction of Dongnan Auto City in Fujian Province with annual production capacity of 60,000 sedans. $230 million. 9/99.

Zexel Corp., a unit of Robert Bosch GmbH (Germany)
Formed Bosch Automotive Products Co. Ltd. to produce diesel injection pumps in Jiangsu Province. 9/99.

OTHER

The Boeing Co. (US)/Air China (Beijing)
Air China signed loans with ICBC and the US Export-Import Bank to purchase six Boeing aircraft. $505 million. 11/99.

Cathay Pacific Airways (Hong Kong)
Will lease three aircraft from Air China. 10/99.

Delphi Automotive Systems (US)
Delphi increased its stake from 53% to 100% in its joint venture with Baicheng Automotive Wire Factory in Jilin Province. 10/99.

GM China, a joint venture of General Motors Corp. (US)
Will start first dealership network in Shanghai. 10/99.

Motorola Commercial, Government and Industrial Solutions Sector, a unit of Motorola Inc. (US)
Completed systems integration for Beijing Capital International Airport. 10/99.

World Bank
Will provide funds to Beijing Jeep Co., a joint venture between Beijing Automotive Works and Daimler-Chrysler, to aid in the delivery of 333 automobiles to transport poverty-relief supplies. $7.52 million. 10/99.

Banque Francaise du Commerce Exterieur (France), Banque Nationale de Paris (France)
Granted loan to China Construction Bank for a rail transport system. $287 million. 9/99.

China Construction Bank
Will provide loans to purchase cars and engines from the Alstom Co. of France. $172 million. 9/99.

Los Angeles International Airport (US)/China Southern Airlines
Cooperatively launched Rapid Connection Service to improve efficiency for outbound connecting flights. 9/99.

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CONFERENCES

WTO and New Opportunities in China Insurance Summit 2000, 15 to 16 March 2000, Beijing. This timely summit will take stock of market responses to existing insurance products and the development of new and customized products suited for the China Market. It will touch on new opportunities for foreign insurers to operate in the life and general insurance sectors and discuss how you could capitalize on new and emerging business openings China's entry to the WTO can bring about.

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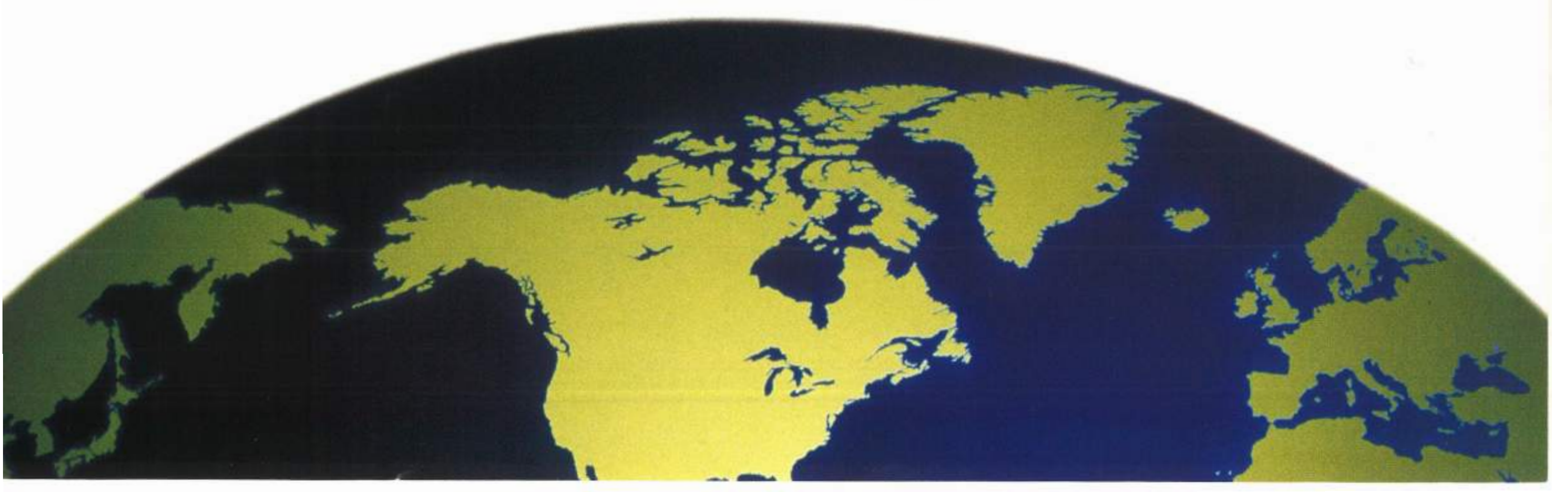

Together, these two characters mean "tomorrow." Separately they mean "bright" and "day."

Americans have long wondered about tomorrow's China. Strong or weak? Successful or unsuccessful? In step with the world or marching to its own music?

China's people, living with rapid change, have their eyes fixed on tomorrow as well, a tomorrow of modernity, prosperity, and world respect.

Now, as the new century dawns, China and America stand at the edge of tomorrow.

China will almost certainly enter the World Trade Organization in the year 2000, pledging to live by the rules and standards that the world's trading nations (led by the United States) have created.

The US stands to reap the benefits of our successful, principled negotiations with China. More open markets, lower trade barriers, greater adherence to law and transparent government decision-making are just a few of China's commitments as it approaches WTO membership.

But this brighter tomorrow also asks us for one step not yet taken: extension of Permanent Normal Trade Relations to China. To win the fruits of China's WTO membership commitments for Americans, we must establish full WTO member treatment for China as well.

A long-awaited tomorrow is at hand. Let's seize the moment. The time for PNTR is today.

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