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China's economic interactions with Asian countries

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CHINA'S ECONOMIC INTERACTIONS WITH ASIAN COUNTRIES

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Today, the ancient Asian nations of the Pacific Rim are home to the most vital and dynamic trading in the world: Japan and the "Four Little Dragons"--South Korea, Taiwan, Hong Kong and Singapore--combined do not make up even one percent of the world's land surface, and their populations are no more than four percent of the world total. China's great leap forward over the past few years--especially the economic reforms in southern China--is evidence that the transition from socialism to capitalism need not be all that lengthy.

The implications of this paper are, first, that increased economic interdependence between China and Taiwan reduces their political interdependence and encourages separatism on Taiwan's side, at least in the short run.

Second, the bargaining advantages for Taiwanese investors over China's local leaders which, due to the dominance of localism in China will not last long, because of their relatively modest invest and increasing investments from other countries.

Third, since China has turned from its consistent conservatism, it has actively worked toward improving political and economic relations with Asian countries. The resulting economic interaction and integration within this area is having far-reaching consequences.

Fourth, having reaped the benefits of free trade, East Asian nations are not about to take retrogressive steps to form or create trade blocs. It would be antithetical to their very survival. Whatever they undertake as a regional initiative must necessarily be predicated upon the consistency of their contributions to more liberal, multilateral trade.

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CHAPTER ONE

INTRODUCTION

In real terms, growth at average rates per annum between 4 and 7.5 percent means a doubled GNP per capita in a span of 10 to 18 years, resulting in a fourfold GNP per capita increase in less than a generation. This is what has happened to Japan since the Fifties; to Singapore, Hong Kong, Taiwan, and South Korea since the Sixties; to Malaysia, Brunei, Macao, North Korea, Thailand, the Phillippines, and Indonesia since the Seventies; and to China and possibly also Vietnam, Sri Lanka, and Burma in the Eighties. China is still indicated in the official statistics as one of the world's poorest countries in terms of per-capita income, but this is due to a gross underestimation of its economy. Its announced goal of quadrupling the value of its agricultural and industrial production between 1980 and 2000 does not now seem out of line, in light of the performance of the Chinese economy in the last few years (and taking into account longer life expectancy and population increases).

The impact this growth in East Asia had on the economy of the world is twofold: 1) the manufacturing capacity of the area has expanded considerably, resulting in a reduction of the export of primary goods, and 2) the East Asia area has become much more commercially active, both within the region and internationally. There has been a great measure of economic integration between China and neighboring industrialized areas, including areas that may yet come under its sovereignty, like Hong Kong and Taiwan, as well as Japan, Singapore, and South Korea. Japan, characterized by reduced growth rates if compared to its neighbors, has become compelled to become a technology source in order to remain competitive, contributing to technology diffusion in the area in a direct way. The neighboring countries, growing at higher rates, have reduced current economic differentials, and an alliance is likely to develop in the area, enhanced by the common cultural heritage of Sinic origin.

The purpose of this paper is to show the particulars of the conditions described above. The basics of politics and economics for the last but by no means smallest entrant into the arena, China, will be closely examined. Trade relations, especially as regards foreign investment, between China and other East Asia nations will be examined, too, with special attention given to China's unique relationship with Taiwan. Finally, the possibility of a consolidated, cooperative effort by these countries will be evaluated.

Research scope

The main objects of study focused upon in researching this paper were China, Taiwan, Japan, South Korea, and some of the Association of Southeast Asian Nations (ASEAN) countries. The time period is basically from 1978 when China began its open door policy to 1992--13 years. The data sources included those from China, Taiwan, Japan, South Korea, Hong Kong, and the United States. In the process of collecting these data, some problems are encountered: 1) the official statistics issued by China are not the same as those of the Taiwan government, because some Taiwanese businessmen bypass registration with the government, and 2) most data relative to connections between China and South Korea before they established diplomatic ties are simply not available.

Research Method

This research proceeded from reviewing newspapers, business journals, and scholarly research, and from application of statistics for comparative and evaluative purposes. As the nature of this paper is non-experimental, secondary sources are applied. Monetary units are U.S. dollars unless otherwise noted.

CHAPTER TWO

CHINA'S RECENT ECONOMIC HISTORY

Political Background

China's current economic circumstances are the result of a chain of political events. The basic Stalinist political system and economic development model adopted by China in the 1950's was a highly centralized version of the Leninist system, similar to Lenin's own communism of 1918. All key economic, cultural, and social entities were nationalized, and, along with the national party and state organs, they were run as a single party-social bureaucracy. In such a pyramidic hierarchical structure, lower-level entities were absolutely dependent upon higher levels and were subordinate to their command.

Efforts to reform this basic model began early and continued throughout the next thirty years. Two competing modifications of the Stalinist model emerged: a radical, decentralized Stalinism associated with Mao Zedong, and a moderate Leninism identified with Zhou Enlai and Chen Yun.[1] By 1969, the "moderates" gathered around Zhou Enlai and Deng Xiaoping were able to convince Mao that the almost total isolation of China from the rest of the world had driven the country into a very precarious and vulnerable position. A series of policy modifications in the 1970's led to China's normalization of relations with the United States, Japan and many other countries. The major consequence of this policy change was a dramatic expansion of economic transactions between China and the capitalist countries.

The death of Mao in 1976 and the subsequent downfall of the "Gang of Four" paved the way for the return to power of the twice-purged Deng Xiaoping and the official launching of the Four Modenizations in 1977.[2] A more relaxed and flexible approach to self-reliance and interdependence soon evolved. Establishing contacts in all spheres with foreign countries came to mean "absorbing the good experience and techniques from abroad for our own use so as to enhance our self-reliance capabilities and build China into a powerful, modern socialist country before the end of this century."

China has now recognized that self-reliance can only be a long-term goal and can only be realized through the short-term importation of elements of production such as technology, capital and management expertise from the developed countries. These imports are meant to tackle the current problems of China's economy. Participation in the international division of labor, borrowing from foreign banks and governments and setting up of Special Economic Zones (SEZ) are conceived as means, under the "open door" policy, for financing these imports and are thus given much weight in the current drive toward the modernization of China.

However, since 1978, recognition of the inefficiency of the trading system has stimulated new and more innovative methods of trading. The adoption of less rigid trading policies and trade financing represent a new attempt to give the, necessary flexibility to China's trading system and to its rapidly increasing import trade.

China's Trade in 1991

Under the open door policy and related reforms launched in 1978, China has forged strong ties with foreign businesses. These foreign businesses now export from China and are concentrated in the coastal provinces and cities; at the year end 1991, they were reportedly over 41,000 strong.[3] According to Chinese customs clearance statistics, total 1991 exports and imports by these foreign ventures rose 43.8 percent from the previous year to reach $28.9 billion. Of this total, exports rose 54.2 percent to $12.0 billion, breaking through the $10 billion level for the first time ever. Foreign ventures accounted for 12.6 percent of China's total exports in 1990; that share rose to 16.7 percent in 1991. The biggest growth in exports among the foreign ventures in 1991 was by wholly-owned foreign enterprises, which doubled their exports from 1990 to $2.47 billion in 1991.[4]

Foreign ventures accounted for a considerable share of China's exports: 28.8 percent of China's total machinery and electronic exports; 16.6 percent of textile exports; 50 percent of shoes, 20 percent of toys and aquatic products; and 44 percent of luggage and bag exports. The primary markets for these exports are Hong Kong, the United States, Japan, and the European Community.

Arguably the biggest success in China's new open door policy has been the creation of five Special Economic Zones. These SEZs are designed largely for export manufacture and have their own liberal rules, tax laws and preferential terms for foreign and joint enterprises. However, industrial growth has been accorded top priority, and industrial production will form the basis of the zone's economy. Total exports and imports from the five SEZs rose 25.6 percent from the year 1990 to $19.67 billion (14.5 percent of China's overall imports and exports). SEZ 1991 exports were $9.01 billion, up 19.4 percent from 1990; imports were $10.06 billion in 1991, up 32.2 percent from the previous year. Thus, the SEZs had higher rates of growth than the national average. Foreign ventures in the SEZs accounted for 47.3 percent, almost half, of total SEZ imports and exports in 1991. Finished industrial goods accounted for 89.2 percent of the export products of the five SEZs, far higher than the national average.[5]

After seven years of development, China's 14 coastal economic and technical development zones are finally entering the productive stage.[6] These fourteen coastal cities were opened in 1984 to complement China's SEZ development plans. Their economies are more developed, and advanced technology is more easily accessible and transportation more conveniently available than in other areas in China. Special privileges are also granted to foreign investors in these zones, as in the SEZs. By year end 1991, total cumulative exports (foreign ventures and domestically promoted enterprises) in the 14 coastal economic and technical development zones reached $2.6 billion. Much of the increase occurred in fiscal 1991 alone.

China recorded a surplus in its foreign trade for the first time in seven years in 1990 and maintained a surplus in 1991 as well (see Table 1). According to Chinese customs clearance statistics, 1991 foreign trade grew 17.6 percent from the previous year, to $135.7 billion. Exports accounted for $71.91 billion, up 15.8 percent, and imports accounted for $63.79 billion, up 19.5 percent. Both export and import totals in 1991 were record highs; and the import showing represented a recovery from the decline in 1990 (the first in eight years since 1982). As a result, in 1991, China enjoyed a large surplus ($8.11 billion) in its foreign trade (slightly lower than 1990's $8.71 billion surplus). Viewed in terms of foreign currency receipts, the surplus reached $12.45 billion. Thanks to this improvement in the trade balance, China's foreign currency reserves rose $14.07 billion from the end of 1990 to reach $42.77 billion in 1991, an upsurge attributable to the improved trade balance.

Clearly, behind this healthy increase in foreign trade were the reforms of the trade system and the measures taken for increasing exports and imports, along with continued

Table 1. Trends in China's Foreign Trade

(Unit:$ billion)

Year	Total imports/ exports	Growth over previous year (%)	Exports	Imports	Balance
1985	69.60	30.0	27.35	42.25	-14.9
1986	73.85	6.1	30.94	42.90	-11.96
1987	82.65	11.9	39.44	43.22	-3.78
1988	102.78	24.4	47.52	55.27	-7.75
1989	111.68	8.7	52.54	59.14	-6.60
1990	115.41	3.3	62.06	53.35	8.71
1991	135.70	17.6	71.91	63.79	8.12

source: China Customs Statistics, No. 1, 1992.

expansion of the Chinese economy. The recovery in imports, in particular, was due to the effect of (1) the lifting or easing of economic sanctions on China by the industrially advanced Western nations, (2) China's lowering of tariffs on some products, (3) the dispatch of large-scale buying missions, and (4) a lowering of interest rates, resulting in increased investment by enterprises seeking to improve their technology, which in turn created import demand.[7]

CHAPTER THREE

TAIWAN'S ADVANTAGES AND PROBLEMS

Political Background

The communist government of the People's Republic of China (simply "China" in this discussion) considers Taiwan to be a renegade province temporarily controlled by the exiled remnants of the Kuomintang, the government ousted by Mao in 1949. The capitalist government of the Republic of China ("Taiwan" in this discussion) claims still to be the legal government of all China, being only temporarily confined to Taiwan and the associated islands of Quemoy, Matsu and the Pescadores. Although both governments have the goal of China's reunification, their political differences do not argue for its imminence, let alone its plausibility.[8]

In the meantime, Taiwan is indeed successful in its separateness. Today, the people of Taiwan are among the world's richest: the GNP per person is above Saudi Arabia's; schooling and health care are universal; life expectancy is high and rising; foreign exchange reserves are the largest in the world. By almost every measure, Taiwan has long since outstripped China. While China had to put up with the Great Leap Forward, the Cultural Revolution, and sundry other madness of Mao, Taiwan had careful planning, good friends--especially America--and the will to work hard. These made Taiwan one of Asia's economic "Dragons," along with South

Korea, Singapore and Hong Kong.

Taiwan is also remarkably well-adjusted for an international orphan.[9] It has had plenty of time to get used to diplomatic ostracism and ultimately carries too much economic weight for anyone to completely ignore it, resulting in an international attitude of "flexible diplomacy." Powerful countries may prefer to recognize the People's Republic of China, but they accept that it is in their own best interests to exchange quasi-official "representative" or "trade" offices with Taiwan.

Although the government of Taiwan resists the communist emphasis on the imperatives of economics, the two governments have compatible economic desires. Taiwan's 20 million people are crammed onto an island of 13,885 square miles, the size of Holland (see Table 2), and its businessmen crave the cheap land and labor of the China--whose economic reformers covet Taiwan's money and expertise. Both sides anticipate direct air and sea links across the Taiwan Straits, instead of the indirect trade through Hong Kong their political differences would dictate. The economic integration of Taiwan and China is ultimately desirable, irresistible and inevitable.

The Price of Being a Miracle

Taiwan's imperfections are obvious enough: its air, water and soil are horribly--often dangerously--polluted; housing is cramped, with only 3 percent of the population served by

Table 2. Basic Statistics: Taiwan & China Contrasted (1990)

	Taiwan	China
Population (x 1,000)	20,156	1,143,330
Area (Square mile)	13,885	3,705,390
Population Density (Per square mile)	1,451	306
Urban Residents (%)	72	46
GNP (US$ 100 mil.)	1,620	3,770
GNP Per Capita (US$)	7,990	330
Exports (US$ 100 mil.)	672.14	620.6
Imports (US$ 100 mil.)	547.19	533.50

Source: China's Foreign Trade and Economy Research. No. 357, May 16, 1991, Published by R.O.C. Foreign Trade Bureau, Ministry of Economic Affairs.

modern sewage systems; leisure facilities are rare; and roads are inadequate for the island's 9 million motorcycles and over 3 million cars and trucks. Such is the price of Taiwan's economic miracle. Last year the government announced a "Six-Year National Development Plan" to perpetuate the miracle and to polish away its little imperfections (at a cost of $303 billion).[10]

The only way Taiwan can go economically is up; to do otherwise would be to fall victim to its own success. In the 1950's Taiwan's economy grew by an annual average of 8.2 percent, in the 1960's by 9.7 percent, 1970's by 8.9 percent, and 1980's by 8.2 percent. For the past two decades exports have exceeded imports in every year except 1974 and 1975 (when Taiwan was briefly left reeling by OPEC's first oil-price shock and the world recession). Wages are rising, and consequently land is becoming more expensive and environmental controls more strict. Taiwan can no longer compete in making sports shoes, handbags, plastic toys, and all the other low-tech paraphernalia of international trade. Taiwan's manufacturers must move upmarket, to the high-tech areas where the cost of labor matters less because brain power and capital matter more.

Of course, since the autumn of 1985, when the New Taiwan dollar started its 50 percent rise against the American dollar, thousands of Taiwan's businessmen have found a different answer to their rising costs: instead of moving upmarket, they have moved offshore. Taiwan now has tangible assets worth more than $5 billion on the Chinese mainland, $5 billion in Malaysia, $3.4 billion in Thailand, $2.8 billion in Indonesia, and at least $500 million in Vietnam. Stick a pin in the map of southeast Asia and it is likely to hit a Taiwanese businessman putting up a factory to make the umbrellas, toys, wigs or textiles that he can no longer be produced profitably in Taiwan.[11]

China Fever and Taiwan Favor

Officially the "Three Nos"--no contact, no negotiation, no compromise--still underpin Taiwan's policy towards China. But on May Day last year when the "Period of National Mobilization for Suppressing Communist Rebellion" was ended by President Lee, Taiwan was not only renouncing the implied right to recover China by force; it was also ending the "temporary provisions" which, because of the "rebellion," had allowed its leaders to suspend parts of the constitution and exercise emergency powers. The message was clear to the electorate in general and to the businessmen in particular who counted on new policy for relationship with China. Implicit permission to trade with China had come in August 1988, albeit through a third party. Virtually the only restriction Taiwan has kept in place is a ban on direct air and sea link with China.[12]

Last year the value of Taiwan's indirect trade with China through Hong Kong--almost all of it in Taiwan's favor--was estimated at $5.8 billion, compared with about $3.5 billion in 1990; this year's total is likely to be $7 billion. Why so many Taiwanese businessman have set up shop in China (as mentioned above) is obvious: labor at a tenth the price of Taiwan's and easy to train; land at sometimes a thousandth of the price; already existing factories readily available. In the long run, China offers an enormous domestic market; in the short run, China's policy of depreciating its currency (the yuan or renminbi) could hardly be better for Taiwan's export-oriented investments in China.

The worry for the Kuomintang, Taiwan's ruling party, is that the businessmen are going too far, too fast. Already, mainland trade accounts for a tenth of Taiwan's exports. Add that to the investments made by its private sector, and Taiwan's economy begins to look dangerously dependent on China. The government could hardly accept the political implications--economic and psychological--if Beijing should suddenly decide to boycott Taiwan's exports--many of them destined for use in Taiwanese factories in China--of cloth, machinery, electronic components, and chemical fibers. Imagine the damage to Taiwan!

As things stand, while many businesses with low-technology, labor-intensive operations no longer make commercial sense in expensive Taiwan, investment in China does make good business sense, if not political sense. The government cannot buy the businessmen off, nor, short of banning business transactions with Hong Kong, can it intimidate them. Its only realistic option, therefore, is to make the best of things: to regulate the trade and investment links and to provide protection for Taiwan's businessmen in China.

But if the Kuomintang abandons the artifice of its Three Noes, it may lose the only cards it can play in the game of achieving one China. The terms for reunification would then be dictated by Beijing, which regards the Taiwan government in Taipei as a "local authority," not even a "political entity."

They envisage negotiations between not two governments but merely two political parties. The best a generous China will offer is an extension of senior communist leader Deng Xiaoping's conceptualization of the absorption by China of capitalist Hong Kong in 1997: "one country, two systems."

The Kuomintang, bound by its claim to be a national government, will accept no such subordination. Before it allows direct links, it has "Three Musts": the mainland must renounce use of force as a means of reunification, must treat Taipei as an equal, and must allow Taiwan to enter international organizations, be they General Agreement on Tariffs and Trade (GATT) or the World Bank. The Kuomintang's answer to "one country, two systems" is "one country, two areas, two political entities."

China is in no hurry to force the pace: the more Taiwan's capital and trade flow into China, the less struggle will be put up for Taiwan's independence. In time the economic links will make the political links inevitable--and they will be forged to China's specifications simply because China is bigger and stronger.

China's Trade with Taiwan

In the past two years, China's trade with Taiwan has escalated strikingly. In 1991 Taiwan rose to fifth place (fourth in imports) as a two-way trade partner with China (see Table 5 in page 23). According to Taipei, indirect trade with

China in 1991 rose 43.3 percent from the previous year to $5.80 billion--historical highs both in growth rate and value (see Table 3).[13] Exports accounted for $4.67 billion, up 42 percent, and imports for $1.13 billion, up 47 percent. By product, the main items exported to China include synthetic yarn, woven fabrics, and plastic feedstock, while the main items imported from there are spices, down, and cigarettes.

Investment from Taiwan also continued to increase, although the boom has probably passed. According to Chinese reports, cumulative investment from Taiwan as of the end of 1991 had reached over $3.4 billion (about 3,800 projects), making Taiwan the second largest investor in China, after Hong Kong. By the end of 1990, there were 2,000 Taiwanese investors, contracting for 1,117 projects in China, up 105 percent--worth $984 million. This placed Taiwan ahead of the U.S. and Japan and second only to Hong Kong in terms of both project numbers and value. It is perhaps worth considering whether all businesses that had hoped to invest there have already done so; therefore, while investment by Taiwan might continue to increase, growth would decline. Currently, it appears stable.

Coastal regions head the list of areas Taiwan companies invest in: Guangdong Province ($1,460 million or 41.9 percent of the total); Fujian Province, where Taiwanese companies are concentrated ($290.02 million); and in third Municipality ($276.95 million). Due to a surge of Japanese investment in

Table 3. Indirect Investment between China and Taiwan via Hong kong (1979-1991)

(Unit: $ mil./%)

	Taiwan indirect exports	Growth rate	Taiwan indirect imports	Growth rate
1-2, 1991	571.19	45.04	141.85	53.91
1-2, 1990	393.80	-7.39	92.16	17.88
1990	3,278.25	13.18	765.36	30.41
1989	2,896.49	29.18	586.90	22.60
1988	2,242.22	82.81	478.69	65.68
1987	1,226.53	51.17	288.94	100.35
1986	811.33	-17.78	144.22	24.43
1985	986.83	131.36	115.90	-9.51
1984	425.45	170.73	127.75	42.92
1983	157.84	-2.84	89.85	28.00
1982	194.45	-42.08	84.02	27.89
1981	384.15	81.08	75.18	9.35
1980	234.97	1,031.83	76.21	39.86
1979	21.47	----	56.29	----

Source: Hong Kong Census and Statistics Department, as reported in China Foreign Trade and Economic Research, No. 358, June 1, 1991, Issued by Foreign Trade Bureau, Ministry of Economic Affairs, Taiwan.

Dalian, Liaoning Province has moved into fourth place ($243.73 million), followed by Shanghai Municipality, and Shandong and Jiangsu Provinces. By industry, over 90 percent is in production projects, a good share of them export-oriented and high-tech, in the fields of textiles, electronics, machinery, chemicals and apparel (a field which China is increasingly interested in).

Despite Chinese encouragement of investment from Taiwan and the eagerness of Taiwanese companies to invest there, Taipei has reportedly begun considering investment controls. On the one hand, it has, for example, conditionally lifted the ban on indirect imports of semifinished goods from China, but on the other, it has also hinted that, among other things, it might start monitoring trade of 50 index items and, if it were judged that Taiwan-based companies were becoming overly reliant on the Chinese market,[14] would warn the companies concerned to diversify. A plan for construction of a petrochemical complex in Xiamen (Amoy), announced by Taiwan Plastic and worth some $7 billion, was ultimately shelved due to opposition from the Taiwan authorities.[15] All in all, Taipei remains very wary of Beijing and there are still many problems which have to be resolved in relations across the Straits.

CHAPTER FOUR

CHINA'S OTHER PARTNERS IN ASIA

The World and Regional Stance for China

In 1991 China was intent upon establishing its identity in the international economic community. The time seemed ripe, given the major increases in foreign trade exports and imports. However, trade friction with the West, particularly the United States, increased, and events abroad brought other problems. Although Chinese policy stresses diversification of its trade partners, 1991 saw it lean heavily toward its nearby Asian partners, developing even closer economic ties with them.

The trade friction was the result of sanctions imposed by the industrially advanced Western countries and other international institutions after the June 1989 Tianmen Square incident. These sanctions were eased or lifted starting around the autumn of 1990 but only gradually. U.S. military aggressiveness during the Persian Gulf Crisis (1990-91) and the dramatic changes on the international scene--namely, the collapse of socialism in Eastern Europe in the latter half of 1989, and the attempted coup d'etat and collapse of the Communist Party in the Soviet Union in August 1991--led Beijing into political postures that undercut its economic interests. To avoid isolation and to keep its budding trade economy alive, China could only strengthen its partnership with the neighboring countries of Asia.

China's tilt toward Asia was encouraged by the general reduction of tension in that region, as well as China's stance of positive participation in the Asian regional economy.[16] From the late 1980's into the 1990's, the problematic (and sometimes explosive) relations within southeast Asia have improved, enhancing economic growth. Currently, the Newly Industrializing Economies (NIEs) of South Korea, Taiwan, Hong Kong, and Singapore, and the ASEAN countries are the most dynamic productive economies in the world, developing ever closer, interdependent economic relations among themselves. Then, in November 1991, China formally joined the Asian Pacific Economic Cooperation Forum (APEC), along with Hong Kong and Taiwan, thus making manifest its policy of building new relations with the rest of Asia.

China's Trade in 1991 by Partner

Statistics show, first, that in China's recent trade with its major partners in Asia--Hong Kong, Japan, Taiwan, South Korea, Singapore, and the four ASEAN countries of Thailand, Indonesia, Malaysia and the Philippines--the shares of Hong Kong, Taiwan, and South Korea are rising, while that of Singapore is declining (see Table 4). The ASEAN's collective share has been steadily increasing, but China's total world exports, up from 68.6 in 1988, and 58.9 percent-- up from 50.1 in 1988--of its total imports.

Table 4. Main Asian Trade Partners in China's Foreign Trade by Share

Trade partner	Year	Hong Kong	Japan	Taiwan	South Korea	Singa-pore	ASEAN
Share in total exprts and imprts (%)	1989	30.9	16.9	---	---	2.9	3.1
	1991	35.4	14.4	2.2	1.7	2.5	3.3
	1992	36.6	14.9	3.1	2.4	2.3	3.6
Share in total exprts (%)	1989	41.8	15.9	---	---	3.2	2.5
	1991	42.9	14.5	0.5	2.0	3.2	2.8
	1992	44.7	14.3	0.8	3.0	2.8	2.9
Share in total imp-orts (%)	1989	21.2	17.8	---	---	2.5	3.6
	1991	26.7	14.2	4.2	1.3	1.6	3.9
	1992	27.4	15.7	5.7	1.7	1.7	4.3

Notes: Figures for ASEAN include Thailand, Indonesia, Malaysia and the Philippines but not Singapore and Brunei.
Source: China Customs Statistics, various issues.

China's current trade partners (on a two-way basis) have remained the same as 1990 in the first four places: Hong Kong first, then Japan, the U.S., and the European Community respectively (see Table 5). Taiwan, however, claims fifth place and South Korea seventh. Meanwhile, the former Soviet Union fell from fifth to sixth place and Singapore from sixth to eighth place. A look at the top eight partners shows that, except for Taiwan and South Korea, the growth of imports

Table 5. China's 1991 Trade by Main Partners

Unit: US$ million

Partner	Exports	Increase	Imports	Increase	Total	Balance	Order Ex.	Order Im.	Order Tot.	Order Bal.
Hong Kong	32,137.19	20.5	17,463.05	22.5	49,000.24	14,674.14	1	1	1	
Japan	10,251.58	13.7	10,031.55	32.2	20,283.13	220.03	2	2	2	
Taiwan	594.84	86.0	3,639.01	61.3	4,233.85	-3,044.17		4	5	1
N. Korea	524.78	46.5	85.67	-31.2	610.45	439.11				
S. Korea	2,178.71	72.9	1,066.17	55.8	3,244.88	1,112.45	5		7	
(ASEAN)	4,135.29	10.6	3,824.36	29.3	7,959.65	310.93				
Singapore	2,014.19	2.0	1,062.54	24.9	3,076.73	951.65	6		8	
Thailand	847.81	2.9	421.66	13.6	1,269.47	426.15				
Malaysia	527.895	4.9	804.00	-4.5	1,331.89	-276.11				
Indonesia	481.14	26.9	1,403.34	74.7	1,884.48	-922.20				5
Philippines	253.49	20.6	130.48	53.4	383.97	123.01				
Viet Nam	21.40	454.1	10.83	221.6	32.23	10.57				
India	144.48	-13.3	120.34	23.6	264.82	24.14				
Iran	293.18	-7.9	20.51	-52.8	313.69	272.67				
Pakistan	598.09	20.8	89.22	-0.9	687.31	50887				
Saudi Arabia	387.42	14.8	138.24	70.2	525.66	249.18				
U.A.E	408.04	49.8	69.33	83.3	477.37	338.71				
(EC)	6,738.92	15.5	8,401.80	0.6	15,140.72	-1,6628.8				
Germany	2,355.59	15.7	3,048.72	3.8	5,404.31	-693.13	4	5	4	7
Italy	931.61	11.5	1,458.31	36.3	2,389.92	-526.70				8
France	732.93	13.5	1,571.83	-5.4	2,304.76	-838.90				6
U.K.	2727.56	13.1	941.62	-31.9	1,669.18	-214.06				
Netherlands	1,062.74	17.0	429.30	7.5	1,492.04	633.44				
U.S.S.R	1,823.38	18.5	2,080.87	-2.7	3,904.25	-257.49		6	6	
U.S.A.	6,193.67	19.5	3,007.83	21.5	14,201.50	-1,814.16	3	3	3	2
Canada	555.03	28.9	1,646.25	11.3	2,201.28	-1,091.22				3
Australia	554.17	21.7	1,556.36	14.9	2,110.53	-1,002.19				4
Brazil	68.03	-36.2	345.81	-34.2	413.84	-277.78				
Cuba	224.40	17.4	201.65	-34.1	426.05	22.75				
Total	71,910.71	15.8	63,791.38	19.5	135,702.09	8,119.33				

Source: Haiguan Tongji [Customs Statistics] No. 1, 1992 (year-on-year) was higher than that of exports.

Hong Kong, South Korea, and the ASEAN

Trade with Hong Kong, China's biggest partner, increased by over 20 percent in both exports and imports over the previous year, with textiles and related products by far in the lead in both categories. Hong Kong's share of China's total exports reached 44.7 percent in 1991. Imports from Hong Kong rose by a whopping 22.5 percent in 1991 over the previous year (during which it had already risen 13.7 percent) due to the rapid increase in re-exports from Hong Kong, a result of improved investment and consignment processing in Hong Kong-based businesses in China (re-exports constituted 14.6 percent by themselves).[17] The related trade surplus broke through the $10 billion mark in 1990 for the first time, then rose further to $14.7 billion in 1991, establishing Hong Kong as a key source of precious foreign currency.

Reportedly, about 80 percent of Hong Kong manufacturers are moving at least some of their production lines to neighboring Guangdong Province. The main products which are consigned for production in China are shoes and other footwear, toys, watches, travel accessories, and sporting and game goods. Also, trade with Taiwan through Hong Kong has been expanding--there is a surge in investment by Taiwanese companies in southern China. The outlook for a continued increase in Hong Kong's share in China's foreign trade is very bright.

In the past two years, China's trade with South Korea has been growing rapidly. In 1991, South Korea rose to seventh place in two-way trade and fifth place in exports. According to South Korean figures, two-way trade with China (including indirect trade) also increased 36.6 percent to $5.2 billion (see Table 6). The main products exported to China from South Korea include machinery, electrical products, and food, while the main imports from China are coal and oil. During that year, the two countries set up trade representative offices in each other's capital (Beijing and Seoul) and in January 1992 signed a trade agreement including, among other things, extension of most-favored-nation treatment. Obviously, the two nations are laying the groundwork for further trade growth.

Investment in China by South Korea reached $78.56 million (112 projects) in 1991, not as high as that of Taiwan, but still a 39.5 percent increase in value and a 195 percent increase in projects (primarily in northern China) compared with the previous year (see Table 7). Beijing is pushing a plan for building an industrial park exclusively for South Korean companies, as well as taking other steps to attract investment from South Korea. For example, an agreement on investment guarantees was initialed in April 1992.[18] Moreover, developing trade relations between Taiwan and South Korea, largely due the influence of Beijing's promotion of investment

Table 6. South Korean Trade with China

(Unit: $ mil.; % rate of change in brackets)

Year	Exports	%	Imports	%	Total	%	Balance
1987	817	13.7	886	30.1	1,679	20.3	-53
1988	1,700	109.1	1,887	60.2	3,087	83.9	313
1989	1,438	-15.4	1,705	22.9	3,143	1.8	-267
1990	1,553	7.9	2,268	33.0	3,821	21.6	-715
1991	2,119	86.4	3,102	36.8	5,221	36.6	-988

Note: Exports to China include direct exports plus Hong Kong-routed goods from Hong Kong government statistics.
Sources: 1987-1990 figures are from Yonhap Yongam [Yonhap Yearbook] various years. Figures for 1991 are based on 2 estimated values for January-November reported by Tong'A Ilbo (Seoul) Jan. 25, 1992.

under its open door policy, are having a significant effect. The growth of China's trade with both countries depends on their future investment in China.

For the rest of southeast Asia (including Oceania), with the exception of imports from Malaysia, trade with ASEAN as a whole advanced generally in 1991, up 19.0 percent from the previous year. China normalized relations with Indonesia and Singapore in 1990 and with Brunei in 1991, a year which also saw a succession of positive diplomatic exchanges between China and the ASEAN nations. China has announced its intention to support the East Asian Economic Caucus (EAEC) proposed by Prime Minister Mahathir of Malaysia (but opposed by the U.S.) to promote an independent economic strategy forthe region.[19] China has never before shown this much interest in strengthening economic relations with ASEAN (see

Table 7. South Korean Investment in China

(Unit: $1,000)

	1988	1989	1990	1991	Total
No.of cases	2	9	38	112	161
Value	4,350	6,500	56,320	78,580	145,780

Note: Figures include only cases approved by the South Korean government.
Source: JETRO China Newsletter, No. 97, which cites South Korea's Ministry of Finance.

Table 8).

In China's trade with ASEAN nations (other than Singapore and Brunei), the leading export products, in order of value, are ferrous metals, animal feed, oil-bearing seeds, petroleum and petroleum products, yarn, woven fabrics and other textile products, special industrial machinery, and grains and grain products. The leading import products are travel goods, petroleum and petroleum products, vegetable oil, raw rubber, cork and lumber, and fertilizers.

Trade with Japan

In spite of trade friction (see above), in 1991 Japan continued to be China's second largest trade partner in exports, imports, and two-way trade, as in 1990. Exports to Japan have been rising steadily, while imports from it have been recovering more gradually. The combined total (exports and imports) has risen 22.3 percent, to $20.28 billion.

According to Japanese customs statistics, exports to

Table 8. China's Trade with ASEAN Nations

(Unit: $ mil.)

		1990	1989	1988
Singapore	Export	1,974.4	1,692.8	1,481.6
	Import	857.8	1,498.9	1,018.4
Malaysia	Export	340.8	352.2	308.2
	Import	835.0	692.4	568.9
Thailand	Export	823.5	499.9	509.7
	Import	370.3	756.3	632.5
Phillpns.	Export	210.1	257.1	269.5
	Import	85.0	82.9	134.9
Indonesia	Export	379.0	222.9	236.4
	Import	803.2	582.3	681.5
Brunei	Export	8.1	3.6	3.1
	Import	3.7	8.4	5.9
ASEAN (Total)	Export	3,736.2	3,028.5	2,808.5
	Import	2,955.2	3,621.2	3,042.1

Sources: China Customs Statistics Quarterly, No. 1, 1991.
China Statistical Yearbook, 1991, p. 644-646.

China recovered in 1991 and, as a result, trade with that country rose 25.4 percent from the previous year to $22.89 billion, breaking through the $20 billion mark for the first time ever. Exports rose 40.2 percent, to $8.59 billion, and imports 17.9 percent, to $14.22 billion. Japan suffered a deficit in its trade with China for the fourth straight year: after increasing from $380 million in 1988, to $2.63 billion in 1989, to $5.92 billion in 1990, it shrank somewhat, to $5.62 billion in 1991. Among Japan's trade partners, China rose from thirteenth to ninth place in exports and from fourth to second place (after the U.S.) in imports. In total trade, it rose from sixth to fifth place.

The reasons for the recovery in Japan's exports to China were (1) the increase in domestic demand in China due to favorable performance of the Chinese economy, (2) the easing of import restraints by China, (3) the increase in Chinese imports of machinery, equipment and materials relating to the increase in investment in China, (4) the easing or lifting of economic sanctions imposed by the Western nations after Tianmen Square incident, and (5) the start of projects under the eighth five-year plan. By product, Japanese exports of machinery and equipment, accounting for 47.6 percent of all its exports, rose 44.4 percent ($4.09 billion), while exports of ferrous metals rose 28.8 percent (to $1.36 billion, about 2 million tons), staging a strong recovery from the decline of the previous year. There was also an increase in chemical products (up 42.9 percent to $1.10 billion) and textile products (up 40.3 percent to $750 million) for use as materials for production.

The increase in imports by Japan was due in large part to (1) the increase in reverse imports due to the progress in consignment processing and investment by Japanese companies and the resulting surge in imports of finished goods of 35.0 percent from the previous year (58.1 percent of total imports), (2) the progress made by China in reforming its trade system since 1990, (3) the effect of the devaluation of the Chinese renminbi, and (4) China's record agricultural production in 1990. Reflecting a strong interest on China's part in increasing exports of finished goods, textile products saw a 32.4 percent increase (to $4.09 billion) bolstered by the good performance in apparel. Electrical machinery (power generators, audio-visual equipment, and so on) and other machinery and equipment rose 60.0 percent (to $830 million), while ferrous metals, footwear and toys also rose by large margins. There were fears of a decline in food imports due to flood damage in the summer of 1991, but imports of corn surged 106.8 percent and vegetables 38.6 percent, with food imports as a whole rising 26.7 percent (to $2.43 billion). Mineral fuel imports fell 18.0 percent (to $2.47 billion) due to the decline in imports of crude oil.[20]

The Coming Boom in Japanese Investment

According to Chinese statistics, Japan had contracted for a cumulative total of 1,292 direct investments in China as of the end of 1990. These had an overall contract value of $8,092 million, of which $2.5 billion had been implemented.[21] Of these, 341 projects were contracted for in 1990 (up 16.0 percent compared with the previous year), with a contract value of $457 million (up 4.1 percent), of which $503.38 million had been implemented (up 41.3 percent). By contract type, there were 240 joint ventures, worth $113.5 million; 37

joint management operations, worth $42 million; and 63 wholly owned ventures, worth $134.9 million. (Another positive development from the Chinese point of view is the trend in recent years for Japanese companies to join with Taiwanese and South Korean firms to invest in China.)

A look at the figures for direct foreign investment reported by Japanese companies to the Japanese Ministry of Finance, on the other hand, shows only 165 investments made from Japan in China in fiscal 1990 (April 1, 1990 to March 31, 1991), up 31.0 percent from the previous fiscal year, worth $349 million--down in value 20.3 percent. While there was an increase in the number of projects, the size of investment per project shrank considerably, from the average of $3.5 million in the previous fiscal year to $2.1 million, which explains the decline in overall value. Investment in China in fiscal 1990 accounted for 0.9 percent of Japan's total investments, which was only 5.9 percent of its investment in the Asian region.

However, in November 1990, Japan resumed its yen-denominated loan program, after a one-year hiatus, with a first allocation of 36.51 billion yen. This was followed in January 1991 with a visit to China by then Minister of Finance Ryutaro Hashimoto and in following March with a visit by Minister of International Trade and Industry Eiichi Nakao. The Ex-Im Bank of Japan also resumed new loans. Recently, therefore, government-level relations between the two countries have been returning to normal, and private-level investments in China by Japanese businesses clearly have been picking up in consequence.

A look at the trends in Japanese businesses' investments in China, based on 1991 data, reveals, among other things, a remarkable number of investments in the computer software development field (in which there is a severe shortage of engineers in Japan). Also favored were such light industries as apparel, electrical components, medical goods, and daily necessities. As in the past, small businesses were particularly active, and investment was concentrated in the export-oriented manufacturing industries for which China offers numerous incentives. But China also encourages large-scale investment in the fields of high technology, energy, and raw materials, and these sectors have also seen steady growth as a result.

Singling out large-scale projects, in April agreement was reported on construction by a major Japanese firm in China--a joint venture worth a total of $3 billion. In addition, the construction of a joint venture import base for industrial liquefied petroleum gas by Iwatani Sangyo has been announced, as well as the manufacture of Chinese language word processors and printers (joint venture, Mitsui & Co. and Fujitsu), and the new combined Pudong zone of Shanghai and Yaohan has reached agreement on the establishment of a large-sized shopping center there. Evidently, Japanese firms are becoming more active in the financial and distribution fields as well.

In August 1991, then Prime Minister Toshiki Kaifu announced the extension of a 129.76 billion yen loan package as the fiscal 1991 portion of the third stage of yen-denominated loans. Along with the normalization of relations between China and Japan, large-scale economic cooperation projects such as the construction of an industrial estate in the Dalian economic and technical development zone, aid in dealing with Chinese environmental problems, and development of the Tarim oil fields are getting underway. When the dust of 1992 settles, even greater joint projects based on Japanese investment will lead to another boom in China.[22]

CHAPTER FIVE

FOREIGN INVESTMENT IN CHINA

Investment Trends

China's eighth Five-year Plan, begun in 1991, calls for the active introduction of foreign capital. This foreign investment is, of course, being promoted in accordance with the overall economic development of China. The areas in which the Chinese authorities are encouraging investment are: (1) general agricultural development and, specifically, development of new agricultural technology; (2) energy, transportation, communication, and other infrastructure and raw material sectors currently suffering from short supplies; (3) high technology and other sectors promoting the improvement of both product quality and quantity (higher productivity), reduced pollution, and greater economic efficiency; (4) export-oriented industrial sectors which meet actual demand in international markets, raise product sophistication, develop new markets, and generate hard currency through exports; (5) industrial sectors developing new products or producing new facilities or materials commensurate with market demand; (6) industrial sectors equipped with new technology and new facilities promoting existing resources and the recycling of resources; and (7) processing sectors which, while importing raw materials, export most of the resultant products.

Investment is concomitantly being reined-in in certain areas: (1) where the aim is to produce products to be sold domestically which are already produced (locally) in adequate supply; (2) where the aim is to assemble products of which imports are restricted; (3) where the aim is to produce traditional Chinese products; and (4) in hotels and some other tertiary industries. All in all, then, direct investment is progressing in line with China's industrial policy.

Foreign investment in China went through a dramatic transformation in 1990. In the first half of the year, investment, as anticipated, remained stagnant, still affected by China's economic retrenchment program and the lingering repercussions of the 1989 Tianmen incident. Beginning in the latter half, however, one project after another was resumed, and by 1991 the setbacks were rapidly being reversed. The year 1990 as a whole saw a total of 7,273 projects contracted for, up 25.9 percent from the previous year (see Table 9), for a total of $6,596.11 million, up 17.8 percent. Contracts implemented totaled $3,487.11 million, up 2.8 percent. Projects, both contracted and implemented, reached record highs.

A breakdown by contract type shows: 4,091 joint ventures, worth $2,703.95 million, up 1.7 percent; 1,317 joint management companies, worth $1,254.1 million, up 15.8 percent; 1,860 wholly foreign-owned companies, worth $2,443.81 million, up 47.8 percent; and 5 joint development projects (mainly oil

Table 9. Direct Investment

(Contract Basis)

(Unit: $ mil.)

	1988		1989		1990	
	Projs.	Value	Projs.	Value	Projs.	Value
Direct Foreign Investments	5,945	5,297.06	5,779	5,599.76	7,273	6,596.11
Joint ventrs.	3,909	3,133.89	3,659	2,659.02	4,091	2,703.95
Joint mgmt.	1,621	1,623.98	1,179	1,083.22	1,317	1,254.10
100% Foreign-owned	410	480.63	931	1,653.78	1,860	2,443.81
Joint devlop.	5	48.58	10	203.78	5	194.25

Sources: China Statistical Yearbook 1990 and 1991.

exploration and development), worth $194.25 million, down 4.7 percent. The big jump in wholly foreign-owned ventures--particularly striking, as it was in 1989--was due to (1) the relatively prohibitive costs and time involved in coordinating technology and management with the Chinese side in joint ventures and joint management firms, and (2) the achievement in some regions of an investment environment sufficiently hospitable to wholly foreign-owned ventures, reflecting their general acceptance by the Chinese. These conditions have attracted American and Japanese interest in investment, in addition to that of Taiwanese firms.

Hong Kong and Macao led in implementation of investment plans in 1990 (see Table 10), but this was down 7.9 percentfrom 1989, and 1989 was down 0.8 percent from 1988, making two straight years of decline, a reflection of the Tianmen incident and the subsequent problems in Sino-British

Table 10. Direct Investment in China by Country/Region (Implementation Basis)

(Unit: $ mil./%)

Country/Region	1989		1990		1991 1st half	
	Value	Share	Value	Share	Value	%Change
Hong Kong/Mac.	2,077.59	63.3	1,913.42	54.9	972.85	32.2
Taiwan	---	---	---	---	165.64	---
Japan	356.34	10.5	503.38	14.4	161.53	46.9
USA	284.27	8.4	455.99	13.1	129.78	43.9
West Germany	81.39	2.4	64.25	1.8	50.66	344.0
Singapore	84.14	2.5	50.43	1.4	1,592.00	49.9
Total	3,392.57	100.0	3,487.11	100.0	1,643.90	33.7

Source: China Statistics Yearbook, 1991.

negotiations over the construction of the new Hong Kong airport. Next in importance were Japan and the United States, which increased their investments by a massive 41.3 percent and 60.4 percent, respectively. The U.S. and China have been slow to normalize their relations; however, there has been steady progress in large-scale projects such as the construction of a chemical plant (joint venture, Amoco) and the development of an electronic industry zone (joint venture, KAMP), as well as the establishment of an agrochemical plant in the Pudong zone (joint venture, DuPont). These investment projects appear not to have been affected much at all by the political turmoil. Another notable development was the 357.9 percent leap in E.C. investments after the lifting of economic sanctions by France, which had maintained a tough stance against China after Tianmen.

Reports indicate that foreign-capital affiliated firms' productivity in China has been improving right along with the general upturn in the Chinese economy. In particular, their exports have been strong, rising 58.9 percent in 1990, to $7.81 billion--a growth rate far higher than that of China's exports as a whole (18.1 percent). As a result, the share of foreign affiliates in China's overall exports grew from 8.3 percent in 1989 to 12.6 percent. These exports, however, rely on imports for most of their raw materials and parts. Such foreign-oriented companies--seeking both their materials and their markets abroad--are located primarily in the south of China and form the majority of foreign affiliated firms.

Finally, direct investment up to the end of 1990 totaled a cumulative 29,049 contracts--worth $40.36 billion of which $18.98 billion were carried out. According to Chinese statistics, approximately 14,300 of these investment projects have started operations and employ over 2 million workers.

The Growth of Large-scale Projects in 1991

Investment in China began to pick up in the beginning of 1991, then soared. According to announcements by the Chinese Ministry of Foreign Economic Relations and Trade, direct investment contracted for by foreign companies in the first half of 1991 totaled 5,042 projects, up 79.3 percent from the same period of the previous year and worth $1,643.9 million, while projects implemented increased 33.7 percent. This growth is on a par with 1985 and 1988, renowned boom years for investment in China.

Among the more notable contracts was one for a joint venture automobile plant (Volkswagen) in Changchun, designated as a "state project" on the Chinese side. Agreement was also announced on the construction of a large-scale petrochemical plant (joint venture, Royal Dutch Shell). Such projects suggest that foreign businesses are getting serious about large-scale investments in the energy and high-tech fields. Also discernible is the beginning of a recovery in investment from Hong Kong, particularly, in Chinese infrastructure, such as railroads--a field not previously open to foreign firms. Investment from South Korea shows rapid growth (see Table 7 in page 27). Once the currently pending Sino-South Korean investment protection accord is concluded, investment from South Korea may well experience a boom.

Chinese Legislative Controls on Foreign Investment

A major factor promoting growth in investment in China in 1991 has been Beijing's firm adherence to policies of reform in opening-up to the West economically and improving the investment environment, despite the economic retrenchment program which China is now pursuing internally. China amended its joint venture law in April 1990, aimed, in principle, at abolishing restrictions on the duration of joint ventures. (In August 1991, based on this law, a Japanese company secured approval for the first indefinite-term joint venture in

China.) It enacted regulations legalizing the transfer and retransfer of usage rights for state-owned land in Chinese cities, as well as provisional regulations governing large-scale land development schemes by foreign investors in May 1990. In December 1990, it dealt with the surge in wholly foreign-owned businesses by promulgating regulations governing application of its foreign corporation law. Basically, the old joint venture and foreign corporation income tax laws were scrapped and in their place a new foreign affiliate and foreign corporation income tax law, with detailed regulations for its application, were enacted (effective July 1991). This resulted in a single income tax law for all foreign-affiliated firms, regardless of type, and also set standards for preferential tax rates for different regions and industries.

Other important steps included were implementation of set standards for labor union activities in foreign-capital affiliates (Beijing municipal joint venture labor union articles, January 1991); relief measures for foreign capital affiliates running deficits (provisions on deficit operations of joint ventures, July 1991); and rules clarifying the previously vague settlement procedures for foreign capital affiliates (Shanghai municipal foreign capital affiliate settlement articles, October 1991). The central authorities were also expected to promulgate and enforce provisions on labor management in foreign-capital affiliates which would guarantee autonomy of employment by foreign firms and would facilitate proper labor management.

In relation to the issue of intellectual property, in June 1991 the Chinese instituted their own copyright law and in October they came out with related articles protecting computer software. Investment in China's software industry has been soaring in recent years, and the Chinese have been hurrying to set up legal protections. Various steps have also been taken to improve access of foreign capital firms to raw materials (an area subject to considerable complaint) and to deal with the double system of prices. And while they cannot be said to be sufficiently effective yet, commodity supply service organizations are being set up one after another to preferentially supply materials to foreign-capital firms.

In addition to these measures improving the legal environment, state-sponsored high-tech industry development zones have been established, where special incentives are to be provided to high-tech companies. New bonded tax zones have some of the functions of free trade zones, such as exemption of duties, to help promote relay trade and facilitate consignment processing. One bonded zone was set up in the Waigaoqiao area of Shanghai's Pudong zone; others are to be set up in Shenzhen, Tianjin, Guangzhou, and Dalian. The development of high-tech and export-oriented companies is a key government program; much is expected from foreign capital in this area. For their part, foreign businesses will probably become more flexible vis-a-vis investment in China when these zones (21 in all), with their greater benefits, are in operation.

The vast, cheap labor force of China is, of course, a great attraction. Foreign investors also view as favorable China's basic stance toward opening up its economy to the outside. With the economic retrenchment program scheduled to end and the economy to be switched to an emphasis on growth in 1992, the outlook for investment in China continues to be bright, and steady growth is anticipated.

CHAPTER SIX

THREE MODELS FOR A NEW ASIAN ECONOMIC SPHERE (AND A THEORETICAL COMPARISON)

The Japan Sea Rim Economic Sphere

The possibility of initiating a "Japan Sea Rim Economic Sphere" is becoming more realistic due to the end of the Cold War and its ripple effects in northeast Asia. The geographical proximity and the deep historical and cultural ties make a good basis for economic cooperation. If Japanese and South Korean money, technology and markets, Soviet Far Eastern and Siberian resources, and northeast Chinese and North Korean labor and certain of their resources can be yoked, and if the troubled diplomatic relations between North and South Korea, Japan and the former Soviet Union, Japan and North Korea, and China and South Korea can continue on the path of resolution, there is a chance of the region becoming a major economic bloc.

One point of difference to be resolved is the area to be included by such an economic sphere. The Japanese generally consider this to be the Soviet Far East and Eastern Siberia, the three northeastern provinces of China (Liaoning, Jilin, and Heilongjiang), South Korea, North Korea, and Japan--specifically, the areas on the rim of the Japan Sea. The Chinese, on the other hand, usually include not only all of the above, but also Mongolia the Inner Mongolian Autonomous

Region, Hebei and Shandong provinces, Beijing, Tianjin, and three other parts of northern China. China is very resistant to its involvement being limited to just its three northeastern provinces, particularly in light of their history--those provinces were, of course, once forcibly torn away from China by Japan and redefined as "Manchukuo." There are differences of opinion within China as well, reflecting, among other things, the relative interests of Beijing and the individual provinces which could be affected.

Japan includes Eastern Siberia in the proposed sphere due in part to the long history of exchanges between Japan's Ishikawa prefecture and Irkutsk, but if Eastern Siberia is included, in spite of its being so far afield, then perhaps Mongolia, the Inner Mongolian Autonomous Region, Jiangsu Province, and Shanghai should be, too. If the area included does extend that far, then one could no longer call it the "Japan Sea Rim"--the Chinese usually talk about the sphere as the "Northeast Asia Economic Sphere." And then there are those who think in terms of a Japan Sea Rim economic sphere and a Bo Hai Rim and a Yellow Sea Rim as economic subspheres of the larger northeast Asian sphere.

Beyond the matter of basic identity, there are differences in conceptualizing such a sphere's basic nature. The Japanese generally talk about economic "exchanges," while the Chinese stress economic "cooperation"--as in "economic cooperation and development of northeast Asia." This issue--

will it be a medium of simple exchange or a more fluid cooperation--stems from the origin of the whole idea of the sphere. The Japanese side is now involved from the standpoint of Japan as a whole, but the people who originally proposed this concept and campaigned for it were primarily from those local Japanese economies on the Japan Sea side of the archipelago who sought greater economic exchanges across that sea.

China's interest arises from the growing global trend toward the creation of economic blocs such as the E.C. (European Community) and NAFTA (North American Free Trade Agreement). It seeks to counter possible disadvantages to itself--and Asia in general--by setting up its own regional economic cooperation bloc. This was what prompted it to join the East Asian Economic Caucus proposed by Malaysia (see above). The deterioration in Sino-American relations after the Tianmen incident, with its resultant trade frictions, is one of the factors pushing China to advance such causes.

Direct investment in each other's economy has helped create a deeper mutual dependence in the western Pacific region since the late 1980's. If China could combine with the former Soviet Union and North Korea, an investment environment capable of really promoting direct investment in the future could be developed. But cooperation from Japan and South Korea would be necessary. Japan's neighbors, particularly China and both Koreas, are very wary when it comes to Japan acquiring any special powers. There is fear of a revival of the "Greater East Asia Co-Prosperity Sphere" promoted by Japanese militarists before World War II as a cover for their imperialist aspirations.

The greatest obstacle to its creation is that whatever area is included in this proposed economic sphere, it will not be composed of entire countries. There are limits to interchanges and cooperation on a local governmental or private basis. Other stumbling blocks are that the Soviet Far East would have to shift to a market economy, as would North Korea, which occupies a key position geographically. These areas would finally have to open up to the outside world. Within China, while economic progress has been made, the three northeastern provinces, in particular Jilin and Heilongjiang, must reform and open up even more.

Whatever its focus, such an economic sphere is still in the initial stage of formation, and much of the talk about it is nebulous and usually at cross purposes. A specific example is that of the Tumen River area development scheme. The Soviets have agreed to the idea, but North Korea's attitude is still unclear. The Japanese are easy to talk to about it, but the Chinese side adopts a cool approach. If human resources, materials, money, and information could only be made to flow, then economic cooperation would readily follow on its own and the proposed sphere would form naturally.

The East Asia Economic Group

The Southeast Asia Treaty Organization (SEATO), which was organized to guard against communism, was dissolved in 1977. Japan, Malaysia, Thailand, and the Philippines normalized their diplomatic relations with China one after another between 1972 and 1975, and in 1979, America established diplomatic ties with China as well. In 1989, Singapore and Indonesia did the same. Pressed by the United Nations, nineteen countries in southeast Asia signed a "Cambodia Peace Agreement" in Paris in 1991, accepting the view of the rest of the world that the war in southeast Asia was over; whatever animosity had lingered toward China for its part in that war melted away. In northeast Asia, South Korea and North Korea had made progress in their dialogue, South Korea finally establishing diplomatic ties with China in September of 1991.

As the cold war ended in both hemispheres, the focus of the world's economy shifted from the Atlantic basin to the Pacific basin. The export-oriented economies of Asian countries, no longer dependent on tariffs, quotas and subsidized exports, became more free and open. To counter the growing global trend toward the creation of economic blocs like the E.C. and NAFTA, the East Asian Economic Group (EAEG--now the East Asian Economic Caucus or EAEC) came into being. It was proposed by Malaysia in 1990.[23]

The U.S. opposed this idea at first, reasoning that EAEG's limited membership--Japan, the six ASEAN countries

(Brunei, Indonesia, Malaysia, the Philippines, Singapore and Thailand), Vietnam, Cambodia, and Laos would hinder other Asian Pacific countries from economic expansion outside the region. Japan worried about its newly-established Asia Pacific Economic Cooperation Conference (APECC) being undermined and was afraid of trade revenge from the U.S. and Canada and from Australia, New Zealand and other nations excluded from EAEG. Other conflicts exist--between the two political systems involved, socialist and capitalist, and across the range of unequally developed economies: advanced, newly industrialized, and just emerging. Among these countries, economic and social priorities are not the same. And the matter of Vietnam invading Cambodia was never truly resolved, whatever public face was put on the matter. In light of these difficulties, it was optimistic but not realistic for EAEC to attempt to initiate an economic sphere, and it functions in name only. That is why Asia Pacific Economic Cooperation Conference can still convene talks, why Singapore promotes the idea of "Growth Triangles" with Malaysia and Indonesia.

The Southern China Economic Sphere

The unofficial but widely discussed "Southern China Economic Sphere" (SCES) encompasses three provinces in China--Guangdong, Fujian, and Hainan--as well as Hong Kong, Macao, and Taiwan. Its area of 370 thousand square kilometers and population of one hundred and twenty million are equivalent to Japan's. Its GNP per person was $1,300 in 1991, comparable to Malaysia, Mexico, and Argentina. The economic scale in this region is similar to the ASEAN countries (Brunei not included) or Australia.[24] At the center of eastern Asia's economic sphere (however it might be defined), SCES's future moves will be paid attention to.

SCES was born when the outward expansion of Hong Kong and Taiwan's economies attracted the attention of China, which was seeking relief from its economic difficulties. While China suffered with the Cultural Revolution and economic recession, Taiwan and Hong Kong were successfully industrializing and able to rely on their exports. The boom in their economies encouraged China to adopt the open door policy.[25]

Achieving this boom was not without its problems. Twice, oil crises have pushed Taiwan and Hong Kong forward into transition. Domestically, rapid growth has brought many problems: labor shortages, rising wages, rising property values, stricter environmental controls, and currency appreciation. Internationally, the trade friction resulting from export dumping by Taiwan, Hong Kong, and China--particularly into American markets--became more heated, making market diversification an urgent necessity. Still, Hong Kong and Taiwan in the 1950's and 1960's had none of the unemployment their neighbor experienced because their economic development policies depended upon intensive labor--a weakness subsequently adjusted through industrialization. Eventually, after about 1985, China, Hong Kong, and Taiwan have been able to develop more complementary economic relations.

Since China embarked on its economic open door policy in the late 1970's, Hong Kong has been reinvigorated in its function as a trade entrepot, further consolidating its position as an international financial center for the rapidly developing Asia-Pacific region. The most common types of business relationship between China and Hong Kong are consignment or commissioned processing and compensatory trade.[26] In the two years data have been collected, great changes have already been seen. According to the Hong Kong government's Census and Statistics Department, the rates of commissioned processing in the third quarter were (1) 77.9 percent domestic exports to China, (2) 52.6 percent re-exports to China, and (3) 62.3 percent imports from China. The profitability reflected in the increase in commissioned processing has lead to many Hong Kong industries transferring almost their entire production to China.

For all intents and purposes, since ninety percent of these Hong Kong companies' ventures are located in Guangdong Province, Hong Kong's economic relations with China are actually relations between Guangdong and Hong Kong. No one can consider the future of the Guangdong economy without reference to foreign capital and, more particularly, to cooperative relations with Hong Kong. An argument could be made that Guangdong and Hong Kong are already entering into a stage comparable to "economic integration," which puts a favorable spin on the viability of SCES. Guangdong, Hong Kong, and Macao are further developing their economic cooperation with an eye toward continued growth after the big changes of 1997 and on into the next century.

Taiwan faces economic circumstances similar to Hong Kong's. The export-oriented economy has accumulated foreign-exchange reserves up to $80 billion, but trade friction and appreciation of the New Taiwan Dollar, among other problems, have come along with it. The industrial infrastructure is in need of an overhaul, and, since 1987, labor available for manufacturing has steadily decreased. The wage index has risen far more than the production index has grown. The price of land, pushed by the bubble economy,[27] has turned into a social problem. Taiwan's remaining labor-intensive industries are now challenged by China and the ASEAN nations.

In general, Taiwanese businessmen are facing a deteriorating economic environment. Most of them reject measures to improve product quality and upgrade technology, resorting to investment in foreign countries in pursuit of lower costs and less stringent foreign trade restrictions. According to Taiwan's Committee on Investment and Examination (subsidiary to the Ministry of Economic Affairs), after foreign-exchange liberalization in 1987, Taiwan's foreign investments increased rapidly, accumulating $1.55 billion in

1990 and concentrated in the U.S. and the ASEAN nations. When Taiwan does invest in southeast Asian countries, it is primarily for their cheap labor (wages are a tenth of Taiwan's) and low production costs. It is estimated that the scale of investment in foreign countries will continue growth.

The enticements for Taiwan's businessmen to invest in China are many. With a common language and culture, there are fewer social barriers to trade than with any other country, but because the Taiwanese must invest in China through a third party, the actual extent to which Taiwan is involved in trade with China cannot be determined--the numbers are unavailable. By China's own accounts, Taiwanese business ventures in China total 2,750, worth $200.07 billion. (Almost half of these are in Fujian Province, 1,203 ventures but worth only $1.6 billion.) Taiwan businesses which have invested in China are enjoying a new lease on life.

That SCES is so prosperous must be attributed to Hong Kong and Taiwan businesses which market aggressively and actively develop ventures outside SCES. If political unification is forced, its economic vitality will be hindered and SCES may become a millstone around Hong Kong's neck after 1997.[28] However, Asia's great differences in political and economic power, not to mention in culture and race, mean that there are many variables in its pursuit of integration and development. The future cannot be predicted with certainty.

Is the European Common Market A Suitable Model for Asia?

With the Japan Sea Rim Economic Sphere only a dream at this point, the East Asian Economic Caucus a diplomatic facade, and the Southern China Economic Sphere a brew just starting to simmer, one more theory bears contemplation: Can the European Common Market serve as a model for Asian regional organization? The European Community is an historically unprecedented endeavor but, to date, a rather successful one. As generally conceived, the European edifice is built on three pillars: a single market, a single currency and a developing political union. Would this work in Asia? A single market? Yes. A single currency? Possibly, but only in some distant future. And a political union? Probably not.[29]

In regard to this, Asia, compared to Europe (see Table 11), has three major differences. The first is the inversion of the classical center-periphery relationship. The economic process in Europe started from the nucleus, that is from the Franco-German union, and extended itself outward in successive circles; this pattern can not be transposed to Asia. Up to now, the periphery in Asia has been much more active than the center. It produces 85 percent of Asia's total economic output--with less than a third of the population.

Secondly, the success of the EC is largely based on the balance of power between individual countries; the Japanese economy predominates in Asia. Taking into account only the market economies, Japan represents 80 percent of the total GNP

Table 11. A Comparison of the Developing Asia Pacific Trading Community with Two Existing Trade Communities (1988)

Region / Item	EC	(1) Asia-Pacific Region	(2) NAFTA
Population (x 10,000)	32,450	161,590	35,550
Totl. Product (US$ 100M)	48,408	21,076	55,300
Per Capita Product (US$)	14,917	1,304	15,555
Econ. Growth Rate (%)	3.5	7.4	3.2
IMPORTS: Totl. Value (US$ 100M)	10,789	5,787	5,846
Percentage of World Trade (%)	33.1	19.6	18.3
EXPORTS: Totl. Value (US$ 100 M)	10,559	6,958	4,576
Percentage of World Trade (%)	32.2	22.5	14.8
Percentage of Intra-Reginl. Trade Volume (%)	58.9	51.3	14.8
Degree of Regional Cooperation	Common mkt.	Ministerial level discussion	Free trade area

(1) Refers to Japan, Korea, Taiwan, Hong kong, Singapore, the Philippines, Indonesia, Thailand, Malaysia, New Zealand, Australia and China.
(2) The free trade area composed of the United States, Canada and Mexico.
Source: Taiwan's Pacific Strategy, published by the National Policy Center.

of the area. In terms of per capita GNP, the contrast is significant: $25,000 per person in Japan, compared with $5,000-10,000 in Korea and Taiwan, and less than $1,000 in Indonesia, the Philippines, and China (see Table 12).

The third difference is that the most important trading partners for each EC country are the other EC countries. For each member country, intra-EC trade represents over 50 percent of its total trade, and this proportion is constantly increasing. In Asia, even if Japan is the largest trading partner for many other Asian countries, trade is more diversified. For instance, half of Taiwanese exports are directed toward the American market. Asian economies are building market shares in North America, in the Pacific zone (especially in Australia), and in Europe. Intra-Asian trade represents only 40 percent of the total trade.

The implication is clear. Asian economies stand to gain more from global liberalization of trade than from regional. Probably, Asians should aim at a free trade area widely open to worldwide competition, rather than a common market. Thus a dynamic would be created within which Asia's economies would benefit first from regional free trade but then move on to full integration into the worldwide trade system.

The global tendency towards economic "bloc-ism" threatens to take us across a very slippery slope. In the 1930's, economic blocs meant discriminatory trade practices, leading to a period of prolonged economic stagnation. If this hard

Table 12. National Growth Rates for the Asian Region (1988-1991)

(Unit: %)

	1988	1989	1990	1991
China	11.4	5.0	3.5	5.0
Korea	11.3	7.3	7.1	7.0
Taiwan	7.1	7.4	6.6	7.6
Hong Kong	7.3	4.7	4.1	4.0
Singapore	11.0	9.4	8.9	7.2
Malaysia	8.1	8.0	6.5	4.9
Indonesia	5.7	5.8	5.0	4.7
Thailand	11.0	10.0	8.5	7.8
Philipns.	6.8	6.0	6.4	6.5
India	9.0	5.7	5.2	4.7

Source: Collected Data for the Asia-Pacific Region Published by the National Policy Center, Taiwan.

lesson from the past is taken into consideration, regional economic integration should by definition strive to promote world trade and economic growth. While perhaps beneficial for some countries in the short run, "bloc-ism" which suppresses global trade hurts everyone in the long run.

How then is the world trading system likely to develop? It is not realistic to expect an ideal system of completely free trade to emerge, because political considerations cannot be wished away by any government. Trade negotiations must aim for the best practical solution in a less-than-ideal world. The Uruguay Round talks have made considerable progress, in areas such as services, dispute settlements and intellectual property rights. However, an overall settlement has been held up by one outstanding thorny problem--agriculture.

Even though the Uraguary Round talks have not succeed, we can expect more orderly rules of negotiation, faster expansion of trade, and economic gains all around and should avoid the worst possible outcome in which countries revert to beggar-thy-neighbor policies--because leaders have learned the lessons of the past, it is less likely that the globe will break up into three trading blocs, one American, one European, and one Asian.

A three-way split would not yield a viable and stable world economic configuration. All the globe's individual economies are already so interlinked that three such blocs could not possibly become economically self-sufficient except at great cost. Nor would a three-bloc world eliminate trade frictions. Competition within each bloc would still force countries to make painful adjustments from time to time. In Europe, French and German workers have to compete against Spanish and Portuguese ones willing to work for a fraction of their wages, let alone against the hungry and unemployed of Eastern Europe. Already the U.S. fears that Mexico may lure away its jobs, and industry is holding back progress in NAFTA negotiations.

To return to the matter at hand, Asia has benefitted greatly from the multilateral trading system and has contributed commensurately to its growth and success. Its collective influence on the world trading system is not negligible. Hopefully, this will be brought to bear in negotiations to help bring about a good GATT agreement.

CHAPTER SEVEN

CONCLUSIONS

The extent to which the unprecedented economic changes described in this paper are a result of external forces shaping the international economic system is subject to debate. A matter of much greater importance is whether China's political environment will remain supportive of the policies that have been so successful to date. Over the next decade, what will happen in China itself when that huge nation begins its transition to a new leadership? There are many pitfalls in the way of smooth transition, but it may well be that the momentum of reform will be difficult to derail. If the political environment does remain supportive, there is every reason to believe that China will undergo an economic and social transformation with many features similar to those that have occurred elsewhere in East Asia. China's move to open its coast looks successful, and--providing the open door policy continues--this may lead to the creation of a Southern Chinese economic zone which would include both Taiwan and Hong Kong.

The economic growth in the Asia-Pacific area shows that the coexistent economic relations among these countries are becoming more and more closely intertwined, and economic and technological exchange and cooperation are ever expanding. However, the levels of economic development vary greatly in the Asia-Pacific area--there are both developed and developing countries. Many inconsistencies and contradictions exist. Moreover, as a result of the great changes in the world economic situation since the 1980's, the Asia-Pacific area is confronting many new challenges, such as the rapid development of new technology, increasingly intense international competition, the constantly building pressure of trade protectionism, and the heavy task of adjusting economic structures within the newly industrialized countries and other regions in this area.

China will certainly play a more important role in the world economy and the economy of the Asia-Pacific region. The prosperous economy in East Asia, especially in China, suggests that this will be very attractive for foreign firms during the rest of the 1990s. However, there are several unpredictable factors. One is market growth. While many advocate independent growth for Asia, it is tacitly understood that it will have to rely on the U.S. market as its safety net. As a matter of fact, Asian nations grew in the past because exports to the huge U.S. market filled their trade coffers. Political stability is another unknown. Besides China's leadership, other concerns involve North Korea and what may be its inevitable unification with the South--what form will that take? And what about the future of eastern Russia? Probably the greatest variable is the extent of U.S. involvement. The U.S. firmly believes that America's military commitment to the

Pacific Rim is essential to the region's security. Moreover, the Asia-Pacific area is America's largest trading partner. The U.S. will certainly want to maintain its military/economic position in Asia, but in its current state of political transition, what form that will take is unclear.

Even in light of these variables, if certain positive measures were taken, economic growth in this area would almost be guaranteed to increase in the long term at a higher pace. The countries of this area must exert themselves to promote mutual cooperation and mutual support. Economic cooperation in the tangible form of financial suppport and technical aid must be fostered between the developed countries and the devloping countries in this area. The developing countries themselves need to continuously work on increasing their economic strength to narrow the technological gap with the developed countries. In general, relations among the countries in this area and between it and other regions must pursue development of a peaceful and stable international environment. The countries of the Asia-Pacific area must play a part in the setting up of a new international economic order, if they are to participate as equal partners and not be left behind in the dust.

ENDNOTES

1. Chen Yun: The most senior veteran of the revolution, having joined the select handful of top leaders in the 1930s and 1940s, when he served as a China's leading economic official in the 1950s, early 1960s, and 1970s, with strong influence on economic and organization/personnel affairs through the 1980s despite age and illness. A consistent advocate of a balanced sectoral development strategy and financial caution, Chen's views put him on the liberal end of the poilitical spectrum in the Mao era and the conservative end of the spectrum by the late Deng era. By 1989, he was supporting Yao Yilin, Li Peng, and Song Ping.

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26. Commissioned Processing: The Chinese side is supplied with materials and parts by the outside company placing an order or it follows that company's specifications to assemble and process products. The products produced are all taken by the outside companies, which on the Chinese side is only for the processing work.

Compensation Trade: The outside company supplies the production facilities and is paid for them through labor or the products produced.

27. Bubble Economy: While the real economy thrived, the stockmarket bubble burst, as inflated equity prices fell heavily, a similar collapse in land prices followed. Profits of banks and securities houses were hit severely. But the impact on the rest of the economy was limited. Companies may no longer be able to raise cheap money from the market, as they did in the good time.

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