
Current Condition and Prospects for Investments in China by Japanese and ROK Enterprises

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1. Current Condition of Investments in China by Japanese and ROK Enterprises

(1) Development of investments in China by foreign enterprises

Since 1979, the use of foreign capital in China has developed in two stages:

The first stage was the period from the 1980's to the beginning of the 1990's. During this period, foreign capital was used mainly based on loans, and direct investments were rare.

Direct investments by foreign investment enterprises in China amounted to US\$ 25.1 billion during the period 1979 to 1991, and the amount of foreign loans in the same period was US\$ 54.7 billion, which is 2.18 times the amount of foreign direct investments. The amount of foreign direct investments that China has received since 1992 exceeds the external loan amount. For a period of eight years from 1992 to 1999, the amount of investments by foreign capital reached US\$ 282.6 billion, which is 11.3 times the amount of foreign direct investments for the period of 13 years from 1979 to 1991. During the 1990's,

foreign direct investment in China has increased rapidly.

The amount of external loans for the period of 8 years from 1992 to 1999 was US\$114.2 billion, and the amount of foreign direct investments is 2.47 times that amount. Since the 1990's, the focus of the introduction of foreign capital in China has shifted to foreign direct investments.

(2) Active influence on China of investment by foreign enterprises

1) Foreign direct investment is a significant component of fixed asset investment in China

As far as China is concerned, foreign direct investment is a supplementary source of funds necessary to the modernization of the Chinese economy. In China's previous economy-building measures, there was little use of foreign investment, but from the 1980's, the introduction of foreign investment increased little by little. At the initial stage, the focus was on foreign loans, but from the 1990's, foreign direct investment has taken on a major role. Foreign direct investment is continually

increasing as a proportion of China's fixed asset investment. In 1991, the ratio was 4.15%, but in 1994 it had reached 17%. Although after that it declined, it is still above 11%.

2) Manufacturing output resulting from investment by foreign enterprises between 1990 and 1999 as a proportion of total national manufacturing output

The active condition of foreign direct investment is also visible in the continued increase in manufacturing output from foreign enterprises as a proportion of total national manufacturing output. In 1990, this proportion was only 2%, but by 1999 it had risen to almost 28%. With regard to the commencement of operations or the achievement of production capacity by additional foreign investor enterprises, the output of foreign investor enterprises is probably still rising as a proportion of China's manufacturing output.

3) Continual increase in extranational tax revenue (excluding customs duties and land charges) between 1992 and 1999

Since the 1990's, taxes paid to the Chinese government by foreign investor enterprises have increased every year. In 1992, extranational tax revenue excluding customs duties and land use charges accounted for 4.25% of China's total tax revenue, however by 1999, this had increased to 16%. At present, a not-insignificant number of foreign investor enterprises are still covered by a business income tax incentive policy, so as this grace period comes to an end, the contribution made by foreign investor enterprises to China's tax revenues will increase further.

(3) Investments in China by Japanese and the ROK Enterprises

Japan and the ROK are important investors in China. By the end of 1999, the amount invested in China by Japanese enterprises was the second largest, following the USA (except for Hong Kong and Taiwan), and the amount invested by the ROK was the fourth largest. The amounts invested by Japan and the ROK account for 8.1% and 2.9% respectively of the total amount of foreign direct investments in China.

According to our examination, 20 major Japanese

manufactures among the top 500 enterprises mentioned in the FORTUNE magazine in the USA have already invested their capital in China by building factories, except for only a small number of enterprises. Major Japanese general trading firms are also investing in the same way. Some banks and insurance companies have already acquired permission to establish business organizations in China.

Since the resumption of diplomatic relations between the ROK and China in August 1992, several thousand ROK enterprises have advanced into China. Up to the present, many ROK enterprises have been operating in business. The world's top 500 enterprises mentioned in the FORTUNE magazine include 12 ROK enterprises. All of these enterprises except for one insurance company are investing in China on a large scale. The amount invested by enterprise groups such as Samsung, Daewoo, and LG exceeds 1 billion dollars. The investment scale also exceeds that of many European, American and Japanese enterprises.

2. Problems and Obstructions that Japanese and ROK Enterprises Face in China

(1) Deterioration of the Influence of Japanese and ROK Enterprises in China

Throughout the 1990's, Japanese enterprises have led other enterprises in terms of investments in China. Japan had consistently been the largest investor in China. However, from 1999, the USA became the largest investor in China, replacing Japan.

Since 1992, the amount invested in China by ROK enterprises has been increasing constantly. The proportion of the amount invested in China by ROK enterprises to the amount of foreign capital introduced to China (execution base) is increasing. The ratio of investment by ROK enterprises to China in 1992 was 1.09%, and increased each year, reaching 4.73% in 1997. However, the share has decreased gradually from 1998.

At the same time, appreciation towards Japanese and the ROK enterprises in China is deteriorating. Since the Asian financial crisis, appreciation towards American and European enterprises, particularly USA enterprises, has improved dramatically in China. On the contrary, Japanese and the ROK enterprises seem to be left behind in the new economic environment.

Table 1: Amount of foreign capital introduced in China (calendar year)
(Unit: 100 million dollars)

Year	Foreign Direct Investments	External loans	Year	Foreign Direct Investments	External loans
1979 - 1983	26.85	119.38	1992	110.08	79.11
1984	14.19	12.86	1993	275.15	111.89
1985	19.56	44.62	1994	337.67	92.67
1986	22.44	50.15	1995	375.21	103.27
1987	23.14	58.05	1996	417.26	126.69
1988	31.94	64.87	1997	452.57	120.21
1989	33.93	62.86	1998	454.63	110.00
1990	34.87	65.35	1999	403.19	102.12
1991	43.66	68.88	2000	362.40	—
			Total	3438.71	1392.96

(Source) Chinese Ministry of Foreign Trade and Economic Cooperation,
"Statistics of Foreign Investments"

※Year 2000 in the table indicates the period from January 2000 to November 2000.

(2) Obstructions that Japanese and ROK Enterprises are Facing in China

Operation conditions of Japanese and ROK enterprises in China are less active than expected initially. One third of the investment projects of some large enterprise groups are profitable while another one third result in losses. There are many aspects causing such results. Many people blame problems in the investment environment in China. For instance, there are too many restrictions in the foreign investment field, so that knowledge intensive services such as finance, insurance, wholesale, retail, and external trade, have basically not been launched. Even if they are launched, the scale will still be small and operation still in the experimental stage. In addition, in the policy constitution process, the degree of transparency of the legal system and the financial system is low and protection of intellectual properties is inadequate. The road towards the improvement of the investment environment in China is still long.

The problem lies in the fact that European and American enterprises are successful in the same investment environment. In addition, some Japanese and ROK enterprises are successful in individual projects. Based on these facts, we must find out the problems that lie within the foreign investment enterprises themselves and mistakes that were made.

The operation stagnation of foreign investment enterprises stems from the following causes: The Chinese market size is smaller than expected. Competition is too fierce due to concurrent advancement by the same type of

prominent enterprises worldwide. Foreign investment enterprises underestimated the degree of competitiveness in the Chinese market, so that the technology and management that were put in were inadequate.

Although the US enterprises advanced to China later than Japanese enterprises, they promoted localization of management personnel at the relationship enhancement stage, and at the same time, promoted localization of research and development. At present, many distinguished Chinese persons hold the most responsible positions in US enterprises in China. GE, HP, IBM, MOTOROLA, and LUCENT are some examples. These enterprises employ many excellent local staff members in China by focusing on the enterprise culture and management with emphasis on performance results, not seniority. Enterprise competition in the era of information and globalization is human resource competition. Japanese and ROK enterprises are inferior in this regard.

In addition, US enterprises attempt full-scale development using their developed consultation service system in China. Many management consultation companies including management advisors, advertisement companies, financial companies, legal offices, and human resource agents, are advancing in China. Other US enterprises can receive cooperation from these enterprises for investment and operation. Investment of one US enterprise in China operates through one investment system in practice. Japanese and ROK enterprises lack such a system.

Table 2: Foreign direct investment as a proportion of total fixed asset investment in China 1991-1999

Year	Total fixed asset investment (million dollars)	Foreign investment (million dollars)	Proportion of fixed asset investment (%)
1991	105,097	4,366	4.15
1992	146,522	11,008	7.15
1993	226,871	27,515	12.13
1994	197,734	33,737	17.08
1995	239,723	37,521	15.65
1996	276,322	41,726	15.10
1997	305,997	45,257	14.79
1998	343,729	45,462	13.23
1999	360,800	40,318	11.17

Table 3: Output by foreign investor enterprises as a proportion of total national manufacturing output (Unit: Million yuan)

Year	Total national manufacturing output	Output by foreign investor enterprises	Proportion (%)
1990	1970,104	44,895	2.28
1991	2313,556	122,332	5.29
1992	2914,925	206,559	7.09
1993	4051,368	370,435	9.15
1994	7686,725	864,939	11.26
1995	9196,328	1315,416	14.31
1996	9959,555	1507,753	15.14
1997	5614,970	1042,700	18.57
1998	5819,523	1416,200	24.00
1999	6377,524	1769,600	27.75

Table 4: Extranational tax revenue 1992-1999 (Unit: 100 million yuan)

Year	Total tax revenue	Rate of increase (%)	Extranational tax revenue	Rate of increase (%)	Proportion (%)
1992	2,876		122		4.25
1993	3,971	38.05	227	85.31	5.71
1994	4,729	19.10	403	77.72	8.51
1995	5,516	16.64	604	50.12	10.96
1996	6,436	16.69	764	26.40	11.87
1997	7,548	17.31	993	29.97	13.16
1998	8,552	13.30	1,230	25.94	14.38
1999	10,312	13.40	1,649	33.78	15.99

3. China's Participation in the WTO and New Opportunities for Economic Cooperation between China, Japan, and the ROK

(1) China's Participation in the WTO and Perspectives for External Economic Cooperation

China continues to make progress towards its aim of opening-up and reforming its economy in order to cope with the globalization of the world economy. As a result of hard consultations over 14 years, China achieved consultation regarding participation in the WTO with the absolute majority countries of the WTO, including the USA, the EU, and Japan. After participating in the WTO, the Chinese Government will agree to a dramatic reduction of tariffs on agricultural products and industrial products in stages, expansion of the opening of the market, and permission for the advancement of foreign investment enterprises into knowledge-intensive service industries such as telecommunications, banking, insurance, wholesale, and retail. The opening of the service field is beneficial to the development of foreign investment enterprises in China as well as the modernization of the Chinese economy. The Chinese Government has introduced a series of new foreign investment encouragement measures. They are technological developments, innovations of foreign investment enterprises, investment in the central and western region by foreign investment enterprises, staged expansion of the opening of the service trade field, listing of foreign investment enterprises that satisfy requirements in the A share market and B share market, and the expansion of the operating range of holding companies in China. The Chinese Government is actively studying permission for investment by foreign investment enterprises in China with new methods such as merging and acquisition.

Through affiliation and competition with foreign invested enterprises, Chinese enterprises have understood the basic principles of international management and have changed their traditional conservative concept. At the same time, by experiencing many affiliations and competitions with foreign investment enterprises, the

competitive position has improved. Currently, more Chinese enterprises are actively participating in global economic cooperation and are looking for foreign investment enterprises as partners for affiliation.

Foreign investment enterprises, particularly multinational enterprises, will expand their investments in China. Foreign investment enterprises started to look for new investment opportunities after adjusting the existing investment projects in stages, and reviewing the experiences and the lessons they have learned. After the 1990's, overseas multi-national enterprises have concentrated their investments in the manufacturing field. Currently, these enterprises delay large investments in the general manufacturing industries, but are actively searching for investment into the information concentrated service industry, basic raw material industry and high-tech industry, and have started investment in the research and development field. These enterprises are looking for partners for affiliation. For instance, the partners can be private enterprises that are growing rapidly.

Based on these conditions, a bright future is awaiting China in the foreign investment field in the 21st Century. After participating in the WTO, the Chinese Government has promised to expand the investment field and investment areas for foreign investment enterprises, to diversify the investment methods, and expand the investment methods. During the period from 1992 to 1998, foreign investment enterprises, particularly internationally well-known multinational enterprises, invested in China one after another, causing a foreign direct investment boom. Through this adjustment and expansion of the investment fields, areas, and methods, investments in China by foreign investment enterprises will further be positive and active. A boom in direct investment in China by foreign investment enterprises will occur at the beginning of the 21st Century

(2) Promotion of Economic and Trade Cooperation Between China and Japan/ the ROK

Prior to China's participation in the WTO, Japanese

Table 5: Amount invested in China by major investing countries by the end of 1999
(Unit: 100 million dollars)

	USA	Japan	Singapore	ROK	U.K.	Germany
Number of projects that were permitted	29,063	18,738	8,498	12,827	2,547	2,126
Contract base amount (100 million dollars)	527.10	350.32	332.55	163.74	160.90	94.22
Execution base amount (100 million dollars)	258.19	249.42	148.01	90.11	76.31	47.85
Proportion of the entire amount of foreign investment in China that was actually used (%)	8.34	8.09	4.82	2.87	2.47	1.56

Table 6: Share of direct investment in China of Japanese and ROK Enterprises
(Execution base) (Unit: %)

	1992	1993	1994	1995	1996	1997	1998	1999
Japan	6.45	4.81	6.15	8.28	8.82	9.56	7.48	7.37
ROK	1.09	1.36	2.14	2.78	3.25	4.73	3.97	3.16

and ROK enterprises have been important trade partners for China, and Japan and the ROK have been important investing countries. After participating in the WTO, China should enhance the positions of investing countries recognizing Japanese and ROK enterprises as major trading partners. At the end of 2000, the Chinese Government clarified active promotion for economic cooperation of “10+3” (ASEAN 10 countries and 3 countries comprising China, Japan, and the ROK). In fact, promotion of “10+3” means dramatic promotion of economic cooperation among three Northeast Asian countries, namely China, Japan, and the ROK.

Due to historical and political factors, these three countries in Northeast Asia, China, Japan, and the ROK, are in practice contacting and cooperating. However, the economic cooperation between the three countries has not been taken up as a joint promotion project by the governments. Facing the surge of recent globalization and information, the joint economic cooperation system in Northeast Asia beyond the historical and political problems is the objective of these three countries.

There are some problems in achieving true full-scale economic cooperation among the three countries, China, Japan, and ROK.

Firstly, all three countries are in the stage of economic adjustment and reformation.

The Japanese economy has been stagnant since the beginning of the 1990's. Strategic adjustment inside enterprises and serious reformation of the management structure are necessary. This process has just started. For the ROK economy, a series of problems in the economic structure were revealed as a result of the crisis in 1997. Large enterprise groups in ROK are also implementing reformation to cope with globalization and information technology. The road to structural reformation for some enterprise groups is difficult. Government owned cooperatives in China should make further efforts towards reformation. In the last few years, reformation of government-owned cooperatives has been progressing substantially. However, there is still a long way to go before they find out how to implement enterprise reformation and reconstruction based on the requirements of globalization and information technology, according to the market economic rules.

By proceeding further towards adjustment of the economic structure and enterprise reformation, new economic cooperation at a high level can be achieved among these three countries. Mutual cooperation should be promoted and the competitive positions of these three countries should be enhanced.

Secondly, the three countries should improve mutual trust by adjusting the awareness of mutual cooperation and ideas.

As described above, historical and political factors often create elements that influence the continuing trusting relationship necessary for mutual economical cooperation. Since China has been oppressed by strong countries including Japan for more than 100 years, it is a sensitive problem how Japanese political circles behave regarding the historical facts of the Japanese invasion of China. The Japanese economy has led Asia for a long time and the

Japanese will be most interested in maintaining their economic superiority in competition for the growth in China, which has a different political and economical system. The ROK faces a problem regarding how to achieve its ideal as a strong country against the pressure from China, which is growing along with pressure from Japan. These conflicts caused by history, politics and the economy may have adverse effects on joint economic cooperation among the three countries, unless they are appropriately dealt with.

Facing the wave of globalization and information technology, Northeast Asian countries will have some difficulty in coping with the North American Free Trade Agreement and competition with the EU if the three countries have to operate individually. China, Japan or the ROK cannot cope alone. China, Japan, and the ROK should enhance their cooperative ties as soon as possible, unite with the Russian Far East region, the Democratic People's Republic of Korea (DPRK), Mongolia, and South East Asian countries, and form a regional economic union in order to face up to international competition.

(3) Promotion of Economic Trade Cooperation between Japanese and ROK Enterprises and the North East and Bohai Sea Rim region in China

To promote economic cooperation among Japan, China and the ROK, we must realize actual cooperative projects.

The North East region and Bohai Sea Rim region in China are the most active trading regions.

The proportions of the amounts of trade targeted for Japan and ROK to the amounts of external trade of three provinces; Heilongjiang, Jiling, Liaoning, are 1/4, 1/3, and 1/2 respectively. 50% of the external trade of Heilongjiang accounts for the trade with Russia. Among the four provincial cities of the Bohai Sea Rim region, trade with Japan and the ROK accounts for 20% of the external trade of Beijing City, 36.5% of the external trade of Tianjin City, 26.3% of external trade of Hebei Province, and about 50% of the external trade of Shandong Province.

At the same time, investments by Japan and ROK are an important source of foreign capital for both regions. In Jiling Province, investments by Japanese and ROK enterprises account for 60% of foreign capital that was introduced into the province.

Investments by Japanese and ROK enterprises and trading with both Japan and ROK are the important motive force for the economic development of the North East and Bohai Sea Rim regions in China. In other words, economic cooperation with the North East and Bohai Sea Rim regions in China will have a positive influence on the economic development of Japan and the ROK.

However, what should be noted is that investments made by Japanese and ROK enterprises in the seven provinces of the North East and Bohai Sea Rim regions are not substantial. As shown in Table 7, the share of Japanese and ROK enterprises in proportion to the foreign capital that was introduced in each region is not so high. Investments made by enterprises of both countries are not so large in comparison to the volume of trade that is carried out by the countries in these regions.

From the beginning of the 1990's, economic

cooperation in Northeast Asia has been discussed among concerned parties. However, cooperation in the region still remains at the discussion stage. Economically concerned parties and entrepreneurs of Northeast Asian countries hold the key for actuating cooperation in Northeast Asian countries and putting the idea into practice in this new century.

In the past, the main subject of cooperation, which is enterprise cooperation among China, Japan and the ROK, has not been sufficiently focused. Recently, Pohang Iron & Steel Co., Ltd. (POSCO) in the ROK and China's largest iron and steel company, Shanghai Bao Steel Group, established a strategic partnership, and POSCO obtained shares equivalent to 25 million dollars. In August last year, Japan's largest iron and steel company, Nippon Steel Corporation (the second largest in the world) concluded a strategic affiliation contract with POSCO in the ROK by exchanging shares. As a result, a cooperative

framework of three iron manufacturers in China, Japan, and the ROK has been established.

Cooperation in the iron and steel industry in China, Japan, and the ROK is enterprise conduct according to the market mechanism. This cooperation model can easily succeed, since the practical operation stage has been started, passing the logistics.

Enterprises in these three countries; China, Japan, and ROK, suggest promotion of a 3-country joint development project in the North East and Bohai Sea Rim regions of China. For instance, it is possible for the three countries to establish a joint development district and establish a joint-venture enterprise region or a joint-venture project. In actual cooperation, mutual understanding and harmony must be promoted by demonstrating the advantages to each country. The joint economic prosperity of China, Japan, and the ROK will be promoted through the success of these actual projects.

Table 7: Economic and trade cooperation with Japan and the ROK by the seven provinces of the North East and Bohai Sea Rim regions.

	Beijing	Tianjin	Hebei	Shandong	Heilongjiang	Jiling	Liaoning
Amount of external trade (100 million dollars)	84.42	126	45.8	182.7	21.9	22.2	137.3
Proportion occupied by trade with Japan and ROK (%)	20.4	36.5	26.3	47.9	23.2	31.8	53.0
Amount of contract foreign capitals that were permitted (100 million dollars)	18.2	36.2	8.9	31.1	9.3	4.5	44.4
Proportion occupied by investments by Japan and ROK (%)	7.4	3.8	13.6	18.6	7.0	60.0	18.1