

CHAPTER ONE

HISTORICAL BACKGROUND

I. Historical Background of China-Malaysia Relations.

According to the historical records of China, contact between Malaysian and Chinese peoples date back as early as 1500 years ago during Jin Dynasty (265-420)(Wang Gungwu 1988: 53). This is the first time the Malay Archipelago was mentioned with regard to trade. Chinese merchants then traded porcelain and cotton goods in exchange for spices, gems and other native products. However, large numbers of Chinese merchants began trading in the *South Seas* (refer to region south of China, which today comprises the ASEAN countries, also known in Chinese as *Nanyang*) only in the eleventh century (Wang Gungwu 1988: 209).

The political relations between these two countries developed much later. The founding of the Ming Dynasty (1368-1644) led to the resumption of the Tributary Trade System (Fairbank and Teng 1941: 135-264) reinitiated by Emperor Yonglo (1403-1425) who began to send diplomatic envoys to this region (Wang Gungwu 1988: 211). Later, Dean Yin Ch'ing, a eunuch in the palace, was ordered to go to Malacca in 1403 with presents of silk brocade, five years before the arrival of the famed Chinese Admiral Cheng Ho (Purcell 1967: 17). Thus, with its very first mission to China in 1405, Malacca became the first foreign nation to receive the emperor's inscription (Wang Gungwu 1992:

140). The close relationship between China and Malacca continued until 1435 when the Ming court finally abandoned Yunglo's policy of state trading.

Despite government prohibition, trading between China and the *South Seas* did not stop. There was a strong demand for *South Sea* products in China as well as a market for Chinese products outside China. Merchants kept coming and going, although their numbers varied from time to time. However, this situation began to change with European ventures in the Indian Ocean. The aggressive western powers changed the trade pattern between China and *Nanyang*.

In 1511, Malacca fell into the hands of the Portuguese. On top of this, Japan was aggressively expanding its sphere of influence into China with a view to capture economic products. In view of this, the Ming Dynasty banned trade with the Nanyang region in an effort to stem the entry of foreign powers into China. Although the ban was lifted after 1566 (Wang Gungwu 1988: 216), the Ming Dynasty was on the brink of collapse because of the invasion of the Manchus. Obviously, without the support of *Hua Ch'iao* (Overseas Chinese) (Wang Gungwu 1992: 1-10), parts of China under the Ming Dynasty, especially the coastal areas would have fallen into the hands of the Manchus 38 years earlier (Wang Gungwu 1988: 219-220). Consequently when the Manchus established the Qing Dynasty (1644-1911), they banned trading and applied scorched earth policy in the southern coastal areas to clean up the remaining Ming Dynasty supporters. Those who traded and supplied food to the remnants of former Dynasty were

deemed to have committed treason and were sentenced to death (Wang Gungwu 1988: 221). However, the Qing Dynasty finally reopened the country to foreign trade .

Studies have shown that Chinese immigrants began to settle in Peninsular Malaya as early as the 15th century. They established communities mainly in the port cities. An ancient Chinese tomb dated 1622 at Bukit Cina in Malacca provides one of the strongest evidence of Chinese settlement in Malaysia (Tan Chee Beng 1993: 60). It is also recorded that in 1459, when the Princess Hong Li-Po of China was married to Sultan Mansur Shah of Malacca, “500 handmaidens accompanied her, and they were part of the marriage dowry” (Chia Felix 1980: 3). Although this story was recorded in *Sejarah Melayu*, historical records from China does not reflect on this, nor does it offer any evidence of a permanent settlement of Chinese in Malacca in the fifteen century (Tan Chee Beng 1993: 61). Undoubtedly, the first wave of massive influx of the Chinese occurred only in the nineteenth century when the Europeans colonized Asia and when the control of the Manchu government was waning. When Penang Island was established as a British colony by Captain Francis Light in 1786, the British encouraged the Chinese to work there (Purcell 1967: 39). The abominable living conditions in China encouraged a large number of Chinese immigrants from the Guangdong and Fujian Provinces, to migrate to Peninsular Malaya, gradually transforming the ethnic landscape here.

When the American Civil War broke out in 1861, the need for canned food exploded and triggered demand for tin. Output of tin in Malaya jumped from 6 000 tonnes a year in 1850's to 43 000 tonnes by the turn of the century (Murray Heibert 1999: 64). The first wave of Chinese miners to Malaya began in the 1850s as a result of the

expansion of tin mining. This is reflected in the number of Chinese settled in the Straits Settlement increased from about 40 000 in 1842 to more than 610 000 in 1931 (Table 1.1).

Table 1.1 Number of Chinese in the Straits Settlements

<u>Malacca</u>								
Year	1678	1750	1766	1812	1842	1860	1931	1941
Population								
Total		9635	7216	19627	46097	67267	186711	236087
Chinese	850	2161	1390	1006	6882	10039	65179	92125
%		22	19	5	15	15	35	39
<u>Penang Island</u>								
Year	1812	1820	1830	1842	1851	1860	1931	1941
Population								
Total	23418	28849	33959	40499	43143	59956	218463	247460
Chinese	7291	8270	8963	9715	15457	28018	131855	166974
%	31	29	26	24	36	47	69	67
<u>Province Wellesley</u>								
Year	1812	1820	1833	1844	1851	1860	1931	1941
Population								
Total	3692	6185	45953	51509	64801	64816	141388	171587
Chinese	267	325	2259	4107	8731	8204	44663	63705
%	7	5	5	8	13	13	32	37
<u>Singapore</u>								
Year	1821	1830	1850	1860	1911	1921	1931	1941
Population								
Total	4724	16834	52886	81734	311985	425912	567453	769216
Chinese	1159	6555	27988	50043	222655	317491	421821	599659
%	25	39	53	61	71	75	74	78

Source: Purcell 1967: x, xi.

These immigrants created a favourable market for goods from China, hence intensifying business activity between the two countries. Many Chinese started off as poorly paid contract labourers in the tin mines and in commercial agriculture. They worked very hard and lived frugally. However, some of them eventually began to set up their own businesses. This led to the establishment of many Chinese business groups that are still in operation today (NYSP, 4/5/98), although many of them remained bound-up with their traditional small scale activities and services (Table 1.2).

Table 1.2 Selected Chinese Business Groups in Traditional Businesses

Name	Location	Year Established	Business Nature
Eu Yan-Sang	Kampar	1879	traditional medicine
Nan Long	Penang	1880's	vegetable wholesaler
Chop Hong Huat	Penang	1880's	dried food wholesaler
Skt. Ban Seng	Penang	1890's	chinese merchandiser
Kwong Yik Bank	Singapore	1903	banking
Yu Li Zan	K.Lumpur	1906	winery
Kwang Hua Daily	Penang	1910	newspaper publishing
Thean Seng Tong	Penang	1920's	traditional medicine
Nam Yik	K.Lumpur	1920's	rubber estate
Mei Li	K.Lumpur	1920's	tin mine machinery
Chan Kee	K.Lumpur	1930's	restaurant
Tong Ann Tong	T.Intan	1930's	traditional medicine
Gnee Hong	Penang	1934	carpet, bicycle, sewing machine, steel furniture
Ban Hin Lee Bank	Penang	1935	banking

Sources: 1)NYSP, 4/5/98, 6/7/74 and Star, 24/6/96;
2)Interviews.

Some of them, by forging close links with centres of Malay power, became successful tycoons. Three out of seven of the Chinese businessmen who received “Entrepreneurs of the Year” awards in 1985, namely Chong Kok Lim, Lim Goh Tong and Loh Boon Siew were penniless immigrants from China (Sieh-Lee 1992: 128-129). Despite lacking accurate figures, it is significant that Chinese businessmen have played a vital role in Sino-Malaysian economic relations since then.

In the late nineteenth century, British Malaya’s share in the China trade fluctuated between one to two per cent annually (Wong 1974: 3). On the one hand, China-made goods and merchandise (mainly foodstuff, herbs, medicines and textiles) were imported into Malaya while on the other hand, China was considered an important buyer of Malayan rubber, an important commodity at that time. The peak of trade achieved the height of US\$50 million in 1926 (Wong 1974: 3). Basically, before Malaya gained its independence in 1957, its economic relations with China tended to rise and fall constantly, mainly due to the clear-cut pro-western foreign policy. For example, Malaya obeyed the United Nations strategic embargo on China and implemented a policy of a complete halt of rubber to China in 1952.

However, the ban on shipments of Malayan rubber to China was finally relaxed in June 1956 (Wong 1974: 4). Similarly, a few years later during the period of confrontation in 1960s between Malaya and Indonesia, China supported Indonesia and changed the source of rubber from Malaysia to Indonesia and Ceylon (now known as Sri Lanka).

However, China resumed import of Malayan rubber after 1965 when there was a reversal of relations with Indonesia.

Although political factors characterized the trade between China and Malaya in late 1950s and early 1960s, prospects for steady expansion were good, especially after 1970s. In 1956, two months after the Malayan Government announced the relaxation of the ban on shipment of Malayan rubber to China, the first Malayan Trade Delegation was sent to Beijing (Wong 1974: 4), which paved the way for a rapid increase of two-way trade in the following years (Table 1.3).

Table 1.3 Malaysia's Trade With China, 1950-69

Year	Exports to China	Imports from China	Total Trade(RM m)	Surplus(+)/ Deficit(-)
1950	124.0	95.8	219.8	+12.8
1951	84.0	127.1	211.3	-20.3
1952	*	120.8	120.8	-100.0
1953	5.7	105.2	110.9	-89.7
1954	19.5	87.1	106.6	-63.4
1955	12.8	115.7	128.5	-80.1
1956	23.7	132.0	155.7	-69.6
1957	74.2	159.7	233.9	-36.6
1958	116.4	195.4	311.8	-25.3
1959	121.7	166.5	288.2	-15.5
1960	86.9	174.8	261.7	-33.6
1961	11.5	172.2	183.7	-87.5
1962	2.5	201.7	204.2	-97.6
1963	16.5	287.6	304.1	-89.1
1964	1.0	302.5	303.5	-99.3
1965	22.5	325.7	348.2	-87.1
1966	2.5	173.2	175.7	-97.2
1967	20.2	266.2	286.4	-85.9
1968	76.4	243.0	319.4	-52.2
1969	138.1	243.2	381.3	-27.6

Notes: 1.* = insignificant (< 0.1m).

2. Surplus/Deficit = for Malaysia

3. figure 1950→1965 including Singapore's trade with China.

Source : Lin 1996

Due to the pro-western foreign policy stance in the early days after independence, the newly formed Alliance government of Malaya chose to continue the British policy of trading with China despite ideological differences. However, Sino-Malaysian economic relations had no significant breakthrough and were conducted through third countries such as Hong Kong and Macao. The trade balance, however, had always been in China's favour. Since both China and Malaysia did not recognize each other, commercial transactions remained unofficial and relations between two countries showed little improvement until Tun Abdul Razak succeeded Tunku Abdul Rahman as Prime Minister after the May Riots in 1969 (NYSP, 29/9/70).

With the decreasing involvement of Britain and the United States in Indochina, Tun Abdul Razak believed that the neutralization of Southeast Asia could only be guaranteed by China. He distinctly knew that any move from a pro-western foreign policy towards the proposal of ZOPFAN (zone of peace, freedom and neutrality) of the Association of Southeast Asian Nations (ASEAN), links with superpowers, especially China as the biggest power in the region had to be forged. He first disclosed that Malaysia would recognise China if the PRC recognized the legitimacy of Malaysia (SCJP, 20/9/70). Malaysia would also support China in its effort to regain its seat in the UN (SCJP, 27/10/71). Tun Abdul Razak later sent a letter to Premier Chou En-Lai expressing his views in November 1971 (SCJP, 30/5/94). There had been rumours that

Malaysia took the initiative to resume diplomatic relations with China in December 1972 (NYSP, 3/12/72). Malaysian and Chinese diplomats started meeting in New York to work out the details of setting up diplomatic relations in June 1973 (FEER, 9/7/73). Malaysia finally became the first country among ASEAN to resume diplomatic relations with China (SCJP, 1/6/74). Both governments “consider all foreign aggression, interference, control and subversion to be impermissible” and “do not recognize dual nationality” (Appendix A).

In January 1971, heavy rainfalls flooded the Peninsular Malaya and China responded by donating RM 625 000 worth of aid through the China Red Cross Society (NYSP, 24/2/71). In May of the same year, Permodalan Nasional Berhad (PERNAS) chairman Tunku Razaleigh led a 19 member trade mission to Beijing for an unofficial visit and successfully established direct trade between the two countries (NYSP, 22/5/71). Since then, bilateral trade between the two countries have shown small but steady increases (Table 1.4). PERNAS was given charge of issuing licenses of trade and imposed a 0.5% procedural fee on Chinese merchandise (SCJP, 23/10/71). Malaysian Chinese businessmen were then allowed to participate in the Canton Trade Fair through PERNAS. The total number of visitors to the Canton fair increased annually (Table 1.5). Chinese goods were favoured because of their low prices and comparatively high quality and were popular among Malaysian consumers. Businessmen introduced more and more selections and not surprisingly, Malaysia began to import more and more Chinese goods.

Table 1.4 Malaysia's Trade With China, 1970-94

Year	Exports to China	Imports from China	Total Trade(RM m)	Surplus(+)/ Deficit(-)
1970	67	229	295	-54.8
1971	53	138	191	-44.2
1972	72	144	215	-33.5
1973	193	262	454	-15.2
1974	191	332	523	-26.9
1975	128	356	483	-47.2
1976	113	341	455	-50.1
1977	287	245	532	+7.8
1978	237	367	604	-21.6
1979	398	485	882	-9.9
1980	471	551	1 023	-7.8
1981	204	632	835	-51.2
1982	258	649	907	-43.0
1983	364	626	990	-26.4
1984	387	668	1 056	-26.4
1985	399	621	1 020	-21.9
1986	422	728	1 150	-26.7
1987	703	946	1 649	-14.8
1988	1 089	1 266	2 356	-7.5
1989	1 302	1 650	2 952	-11.8
1990	1 675	1 521	3 196	+14.8
1991	1 761	2 213	3 970	-11.3
1992	1 961	2 482	4 440	-11.7
1993	3 094	2 818	5 911	+4.6
1994	5 060	3 570	8 630	+17.3

Note: Surplus/Deficit = for Malaysia.

Source: Lin 1996 with rounding off of figures

Table 1.5 Malaysian Businessmen to the Canton Trade Fair, 1971-76

Year	Spring Fair	Autumn Fair
1971	--	47
1972	46	69
1973	75	115
1974	80	87
1975	157	100
1976	171	148

Note: Figures included officials of PERNAS

Sources: 1)SCJP, 2/10/75, 10/4/75;

2)NYSP, 11/10/74, 1/1/73, 13/4/76, 24/10/76.

The greatest obstacle to economic relations between the two countries before 1974 undoubtedly was the absence of formal channels and diplomatic relations. But the fact that although Malaysia and China resumed diplomatic relations in 31 May 1974, despite state visits by successive Prime Ministers, the economic relations between the two countries did not blossom until 1985 (Lin 1996: 106). At least two reasons can be explain this slow development of Sino-Malaysian trade relations.

Firstly, communist revolutionary movements throughout Southeast Asia had been supported by the People's Republic of China (PRC). The Malayan Communist Party (MCP) still received official Chinese support in 1965 although the Emergency was over in 1960. The Chinese Communist Party (CCP) even sent a congratulatory note to the MCP on 29 April 1975 when the latter celebrated its 45th anniversary (Shin Ming Daily News, 5/5/75). Communist insurgency constituted a serious threat to regime stability and legitimacy and cessation of PRC support for insurgency was a prime goal of Malaysian government. Although the PRC emphasized the Principle of "separation of Party and

Country” repeatedly after Deng’s 1978 official visit, the Malaysian government had reason to doubt the sincerity of the PRC in their pursuit of diplomatic relations.

Secondly, the Malays had always viewed the cultural and ethnic ties between the Malaysian Chinese and Mainland China with suspicion. Although PRC wound up the Oversea Chinese Affairs Bureau indicating how far it was willing to go on improving relations with Asean countries with large Overseas Chinese communities (FEER, 9/10/71: 8). The question of dual nationality and political allegiance remained unresolved for Malaysian Chinese as the latter’s primary loyalty is unclear. The fact that the MCP was largely Chinese in composition (Purcell 1954: 135) was even more problematic for Sino-Malaysian relations.

Despite the two factors mentioned above, developments in China itself also affected its foreign relations, which in turn determined the shape of Sino-Malaysian relations. Mao Zedong’s strategy of the Peoples’ War was successful and resulted in the CCP’s take-over of China in 1949. Other Third World countries wishing to free themselves from colonialist oppression chose to adopt that strategy (Van Ness 1970: 11). Thus the CCP endorsed a policy of explicit and implicit support for various “national liberation movements” in the region (Taylor 1976: 332) and the militant activities of the MCP were supported by CCP without exception. Relations between Malaysia and China deteriorated during this period.

However, China later changed its foreign policy of advocating armed revolution. During the Asian-African Conference in Bandung in 1955, China promoted a policy of peaceful coexistence. It urged a negotiated settlement to the insurrection in Malaya and recognition of the MCP (Taylor 1974: 277). A meeting was held in December 1955 between MCP and Alliance government in Baling, but failed to bring about peace between the communists and the government in Malaya.

The support of China towards MCP further distanced Malaya from China after independence. Malaya condemned China's invasion of Tibet in 1959 as well as Chinese aggression against India in October 1962. The opening of a clandestine radio station called the Voice of Malayan Revolution apparently based in Hunan Province, China in November 1969 further exacerbated Sino-Malaysian relations (O'Neill 1984: 106).

However, power struggle in China which ended with the triumph of Chou En-lai over Lin Piao in 1971 facilitated the return of China to the diplomatic approach (Taylor 1974: 335). China switched to a so-called dual-track policy of state to state relations with the Malaysian government and party to party relations with the MCP. The People's Daily of China carried editorials reasserting the "never exploit Chinese overseas for subversive activities" manifesto (SCJP, 4/7/78). However, this contributed little towards the bilateral relations of both countries. In an official visit to China, the Malaysian foreign minister Ghazali Shafie frankly admitted that China's refusal to renounce its links with the MCP

represented an obstacle to the improvement of the people to people relationship between the two countries (Star, 2/6/84).

The bilateral relationship between China and Malaysia has been affected not only by the changes in the two countries' own, cultural, economic and political policies but also by those in the international economic and political environment. The international environment was a very important factor when Malaysia made its critical decisions in 1974 and 1985.

There was a change in the international political climate in the early 1970s. From the late 1960s, the United States (US) began reducing its presence in Southeast Asia and began to concentrate in its domestic affairs when it lost the war in Vietnam in 1975. Relations between China and Russia experienced a downturn following the March 1969 Sino-Soviet border clashes; while on the other hand, the US lifted its trade embargo with China after 21 years (FEER 19/6/71: 4). 1972 marked a new era in China's foreign relations policy. Following President Nixon's visit to China in February 1972 (NYSP, 22/2/72), the US eventually resumed diplomatic ties with China in March 1972 (NYSP, 24/3/72). This was followed by Japan in September (SCJP, 30/9/72). In December, Australia and New Zealand joined the move (SCJP, 28/12/72). This development encouraged Malaysia to resume diplomatic relations with China.

In sum, the international political environment played a very important role in determining Sino-Malaysian relations during the period before, and also after 1974.

In Lin Jin Zhong's masters dissertation, "A Study On Malaysia-China Economic Relations With Special Reference To Bilateral Trade", Lin divided Sino-Malaysian trade into three phases according to the changes in policy. The first phase was the period between 1950s and 1960s, shadowed by Cold War political antagonism between the two countries. This was followed by a period when there were policy shifts in the late 1960's, leading to the normalization of diplomatic ties in 1974, which started a modestly cool phase of bilateral relationship that continued till the mid 1980's. Finally, Prime Minister Mahathir's official visit to China in 1985 led to the third phase of more active economic relations (Lin 1996 : 31-32).

Lin's study shows that the pattern of commodity composition of Malaysian exports to China is structurally narrow, concentrated on mineral and agricultural products, whereas China's exports to Malaysia are more diverse (Lin 1996: 54). The same study also indicated that the pattern of bilateral trade between Malaysia and China in the years 1970-1990 is virtually characterized by horizontal complementarity (Lin 1996: 93). He pointed out that between 1974 and 1985, the growth of trade between Malaysia and China was slower than the rate of Malaysia's total trade (Lin 1996: 106). However, the situation changed as trading between these two countries between 1985 and 1990 grew faster than the rate of Malaysia's total trade (Lin 1996: 107). Bilateral trade in services and investments emerged only in the late 1980's and were insignificant prior to the 1990's (Lin 1996: 151).

However, as his study is focused on trade, there is a gap with reference to investment trends. This study aims to complement Lin's research towards a more complete picture of Sino-Malaysian economic relations. The writer will try to understand to what extent and how Malaysian businessmen became involved in investment ventures in China, with special references to public listed companies (PLCs).

II Recent Political and Economic China-Malaysia Relations

In response to the rapid economic and political changes in the 1980's at the global and national level, the Malaysian Government shifted from its hitherto cool and passive relations with China to one that was more positive and pragmatic. The issue of CCP-MCP link which had been the major political stumbling block to better Sino-Malaysian relations were side-stepped, and trade issues were instead being highlighted to improve the unbalance of foreign trade (Tong Pao, 29/6/85). This new China policy took shape after a high-level inter-departmental study entitled, "Managing a Controlled Relationship with the People's Republic of China," in early 1985 (FEER, 4/7/85, 12-14), which, in fact, formed the basic policy premises of Prime Minister Dr Mahathir's visit to China in November 1985 (Wong 1987: 9). The radical shift in the diplomatic strategic position will no doubt be followed by a shift in trade policy.

Mahathir paid an official visit to China in November 1985 accompanied by a large group of businessmen. The two-way trade between Malaysia and China in the following year rose to the record level of RM1149.8 million from RM1019.9 million in the year before. In the following year, China's Vice-Premier Tian Jiyun made a trip to Malaysia (NYSP, 15/10/86). Although there was no significant breakthroughs achieved during the visit, it signified that both sides were making serious efforts to strengthen their relations. Since 1985, a few major trade agreements were signed between the two countries. Some of the trade agreements included the Avoidance of Double Taxation Agreement (23/11/85), the Shipping Agreement (9/9/87), the Aviation Agreement (16/6/88), the Bilateral Trade Agreement (1/4/88), the Investment Guarantee Agreement (21/11/88) and the Economic Trade Joint Committee Contract (22/11/88). The much controversial 0.5% procedural fee by PERNAS on all China merchandise was also abolished in early 1988 (SCJP, 13/1/88), 17 years since its enforcement.

At the same time, Chinese trade delegations led by high-level officials also increased (Table 1.6). The number of Malaysians going to China increased tremendously since 1986. With the easing of travel restrictions in May 1989, Malaysian tourists to China in year 1990 doubled from the previous year (Table 1.7). Meanwhile, Chinese tourists to Malaysia also increased steadily since 1990 (Table 1.8). The number of delegations which have visited Malaysia in 1991 increased five-fold. The number again doubled in the following year (Table 1.9).

Table 1.6 List of High Level Officials Who Visited Malaysia From 1978-94

Date	Name		Post
9/11/78	Deng Xiaopeng	邓小平	Vice Premier
9/11/78	Huang Hua	黄华	Foreign Minister
14/3/80	Huang Hua	黄华	Foreign Minister
9/ 8 /81	Zhao Ziyang	赵紫阳	Premier
25/11/82	Peng Cong	彭冲	People's Congress Vice Chairman
25/2/84	Wu Xueqian	吴学谦	Foreign Minister
25/8/84	Lin Hua	林华	Vice Industrial Metallurgy Minister
8/7/85	Wei Yuming	魏玉明	Vice External Trade Minister
14/10/86	Tian Jiyun	田纪云	Vice Premier
23/6/87	Tian Yinong	田一农	Vice Agricultural Minister
27/11/87	Zheng Tuobing	郑拓彬	Foreign Minister
21/11/88	Zheng Tuobing	郑拓彬	External Trade Minister
28/12/88	Lin Hanxiong	林汉雄	Construction Minister
30/8/89	Hu Ping	胡平	Commercial Minister
10/12/90	Li Peng	李鹏	Premier
10/12/90	Qian Qichen	钱其琛	Foreign Minister
10/12/90	Li Lanqing	李岚清	Vice External Trade Minister
10/12/90	Tao Siju	陶驷驹	Public Security Minister
10/1/92	Yang Shangkun	杨尚昆	State Chairman
14/3/92	He Guangyuan	何光远	Electrochemical Minister
10/8/92	Yao Yilin	姚依林	Vice Premier
10/8/92	Li Lanqing	李岚清	External Trade Minister
10/8/92	Xu Dunxin	徐敦信	Vice Foreign Minister
2/9/92	Bai Meiqing	白美清	Vice Commercial Minister
4/9/92	Cai Cheng	蔡诚	Judiciary Minister
11/92	Shi Dazen	史大桢	Vice Energy Minister
12/92	He Jiesheng	何界生	Vice Health Minister
10/2/93	Ai Zhisheng	艾知生	Broadcast, TV, Film Minister
27/4/93	Wu Shaozu	伍绍祖	Sport Minister
24/5/93	Chi Haotian	迟浩田	Defence Minister
25/7/93	Qiao Shi	乔石	People's Congress Chairman
13/8/93	Zhu Xun	朱训	Geology and Mineral Minister
21/9/93	Hou Jie	侯捷	Construction Minister
17/1/94	Tie Muer	铁木尔	People's Congress Vice Chairman
14/9/94	Chi Haotian	迟浩田	Defence Minister
23/9/94	Wang Guangying	王光英	People's Congress Vice Chairman
14/10/94	Wu Yi	吴仪	External Trade Minister
10/11/94	Jiang Zemin	江泽民	State Chairman

Sources: NYSP and SCJP of one day later than given in the table.

Table 1.7 Number of Malaysian Visitors to China, 1987-94

Year	number
1987	1 900
1988	2 743
1989	10 600
1990	40 000
1991	80 000
1992	105 000
1993	125 000
1994	140 000

Note: estimated number except 1988

Sources: 1)NYSP, 10/12/94;
2)SCJP, 14/2/92, 11/1/95.

Table 1.8 Number of Chinese Visitors to Malaysia, 1990-1997

Year	number
1990	9 883
1991	17 000
1992	46 811
1993	81 874
1994	95 789
1995	103 130
1996	135 743
1997	158 678

Sources: 1)SCJP, 9/2/99;
2)NYSP, 9/9/92.

Table 1.9 Number of Chinese Delegations to the K L And Selangor CCCI

Year	Number
1986	2
1987	4
1988	2
1989	5
1990	6
1991	26
1992	46
1993	103

Source: K.L. and Selangor CCCI

With relations developing at a rapid pace, the economic ties between the two countries also strengthened. For example, Dreamland Spring Sdn Bhd's (DSSB) investment in China was prominently featured in all the newspapers. Besides the notable increase in bilateral trade since the signing of the Bilateral Trade Agreement in April 1988, there were now new possibilities of investment.

Although Malaysia was the first country in ASEAN to resume diplomatic relations with China, compared with Singapore and Thailand, Malaysian investors were latecomers to China. However, following the disbanding of the MCP in 1989 (NYSP, 3/12/89), the political hurdle was finally cleared, allowing economic relations to take off.

1989 was the year of the relaxation of the restriction on entering China and direct flight of both countries. Restriction on entering China was finally fully abolished in September 1990 (NYSP, 8/9/90). In line with the improving political climate, the momentum of Malaysian investment was picking up fast. In 1992, Malaysian companies became the tenth largest investor in China, with total investment of about RM1.3 billion. According to the former Malaysian Deputy Minister of International Trade and Industry, Chua Jui Meng, since China opened its doors to foreign investment, "the government estimated total investment to be more than RM1.54 billion in hotel, food processing and manufacturing industries."(NYSP, 14/7/93)

There are no complete official statistics on Malaysian investments in China. Firstly, Malaysian companies are not obliged to report to any Malaysian governmental or statutory body. Secondly, businessmen, especially the Malaysian Chinese *taukes* (owner of a business) have always kept a low profile on their business activities. However, from the news reported in the papers, an ordinary reader can observe an increase of Malaysian investment in China. Since 1985, news about China in the Chinese papers have been on the rise. Reports of investment in China on the (PLCs) have also received significant coverage. In interviews with the spokesman of any company, inevitably answers such as "we will consider China" or "we are eyeing on China" were given. The "Chinese Fever" rose to a peak when Mahathir paid a second official visit to China in 1993. 36 memorandums of understanding (MoUs) were signed, which comprised RM1.494 billion worth of business contracts (SCJP, 14/7/93). The visit was described by Prime Minister Mahathir as a "leap forward" in Sino-Malaysian relations (NST, 22/6/93). He further

elaborated that “China has been and will be the main attraction for Malaysian companies as opportunities still abound in China” when he addressed Malaysian and Chinese businessmen at the China World Hotel (BT, 18/6/93). However, no study on Malaysian investment to China, as far as the writer know, has been conducted. Therefore, the main objective of this dissertation is to depict the general view of it, with special emphasis on the participation of PLCs.

Although it is extremely difficult to distinguish between Chinese and Malay capital in Malaysia, especially after the implementation of the New Economic Policy (NEP) in 1971 (Sieh Lee 1992: 109-110), there have been increasing incidence of involvement of Bumiputra businessmen into business in China beginning from 1990s (Hara Fujio 1994: 153). However, the “Chinese Fever” began to cool down after 1994. Foreign investment in China began to fall in the first half of 1994 (SCJP, 15/8/94). Despite the fact that there were more than 100 trade delegations from China in 1994 (SCJP, 25/12/94) and top officials from both countries still exchanged visits frequently in the same year (Table 1.10), there were also an increase in announcements by more and more PLCs that they are giving up their negotiations on joint venture projects in China. A year after Mahathir’s visit to China, according to International Trade and Industry Minister, Rafidah Aziz, only seven out of the 36 MoUs signed were implemented (SCJP, 27/7/94). This prompted her to remark that the term “MoU” should be given a new meaning. Instead of “memorandum of understanding”, the MoU should mean “memorandum of undertaking” (Malaysian Business, 6/94, 58). Later, many companies have even ended their investments in China or have sold their stakes to a third party.

Among the companies that signed MoUs during Prime Minister Mahathir's visit to China, Resort World and Renong were the first to announce their intention to withdraw the highway proposal in Fujian Province (SCJP, 29/10/94).

Table 1.10 List Of High Level Officials Who Exchanged Visits In 1994

Date	Name		Post
<u>Chinese officials who visited Malaysia</u>			
17/1/94	Tie Muer	铁木尔	People's Congress Vice Chairman
14/9/94	Chi Haotian	迟浩田	Defence Minister
23/9/94	Wang Guangying	王光英	People's Congress Vice Chairman
14/10/94	Wu Yi	吴仪	External Trade Minister
10/11/94	Jiang Zemin	江泽民	State Chairman
10/11/94	Wu Yi	吴仪	External Trade Minister
10/11/94	Qian Qichen	钱其琛	Vicw Premier
<u>Malaysian officials who visited China</u>			
22/2/94	Kerk Choo Ting	郭洙镇	Vice Construction Minister
14/7/94	Rafidah Aziz		International Trade and Industrial Minister
17/8/94	Samy Vellu		Energy, Telecommunication and Post Minister
25/8/94	Anwar Ibrahim		Deputy Prime Minister
25/8/94	Fong Chan Onn	冯镇安	Vice Education Minister
21/9/94	Barisan Natioanal		
29/9/94	Chan Kong Chai	陈广才	Vice Cultural, Art and Travel Minister

Sources: NYSP and SCJP of one day later than given in the table.

In the following year, more companies called off their ventures in China. To name a few of them: SBC, Talam, Larut, Mycom. Statistics show that new PLCs which intended to invest in China has been declining since 1993 (Table 1.11). Malaysian investments in China had entered into a consolidation period where businessmen seriously considered the question of feasibility and are no longer clouded by euphoria. The features of PLC investment in China will be discussed in the following chapter.

Table 1.11 New PLCs Venture into China, 1990-96

Year	Number of PLCs
1990	1
1991	2
1992	8
1993	28
1994	25
1995	20
1996	19

Sources: estimated by author from a survey of reports in newspapers on investment in China.

On the whole, there have been signs of Malaysian investment in China declining since 1995. However there has been quite a considerable amount of reinvestment by more experienced companies such as DSSB. There are various factors which have contributed to the bottleneck of Malaysian investment in China and the bureaucratic walls and barriers are believed to be the biggest obstacle. To what extent China can continue to attract more Malaysian investment and to induce more reinvestment, depends on how successfully the country handles this problem. Of course, we must not lose sight of the international economic and political climate, which is equally, if not more important.

CHAPTER TWO

CHINA IN THE WORLD ECONOMY

I. The Contemporary World Situation

Although trade and exchange existed since pre-historical times, international trade, in the more complex sense, can be traced back to the sixteenth century with the emergence of modern nation states in Europe (Walter 1975: 4). The seed of modern international trade theory comes from Adam Smith (Winters 1994: 15). Smith's theory proposes that it is advantageous for a country to produce goods that could provide absolute advantage. He generalised that:

It is the maxim of every prudent master of a family, never to attempt to make at home what it will cost him more to make than buy....
What is prudent in the conduct of every private family, can scarce be folly in that of a great kingdom. If a foreign country can supply us with a commodity cheaper than we ourselves can make it, better buy of them with some part of the product of our own industry, employed in a way in which we have some advantage. (Smith 1961 reprint: 424)

Some 40 years after Smith, David Ricardo analysed the advantage of international trade with his justly famous law of comparative advantage to demonstrate the superiority of free trade over autarky (no trade or economic self-sufficiency). He proved that it was also an advantage to concentrate in the production of those goods that offered a comparative advantage (Ricardo 1971 reprint: 147-167).

The arguments and trade theories of these classical economists offer one explanation of why world trade developed in the period of the Industrial Revolution

when economic activities flourished in a variety of forms. During the Mercantilist era, which dates from about 1500 to the middle of the eighteenth century, the governments maximised exports and minimised imports in order to achieve a favourable trade balance which was paid in gold or silver. To facilitate the pursuit of the Mercantilist goal for a continuing accumulation of bullion as wealth, they colonized enclaves in their respective trading areas, thus giving birth to the age of colonial and imperial expansion (Walter 1975: 5-6). In the nineteenth century, world economy can be viewed in two domains—a centre of industrialized countries which produced manufactured products and the peripheral countries which provided the necessary raw materials and markets. This clear-cut international division of labour between developed countries and developing countries continued until the Second World War.

After the Second World War, most Western colonies achieved independence and world economy was in a completely new shape. On the one hand, there were the Socialist economic systems led by the Soviet Union or “Eastern bloc” and on the other hand, there were the capitalist economic systems led by the United States or the “Western bloc”. Due to the divergence in ideology, with these two blocs competing and confronting each other, the world entered into a phase named the “Cold War”. In this period, embargoes and economic sanctions were used by both parties. Basically, the two blocs were isolating each other.

There was hardly any East-West trade. The United States established the IMF (International Monetary Fund)-GATT (General Agreements on Tariff and Trade) systems after World War II to promote free trade and the free flow of financial resources within the non-socialist countries. It also carried out strategic embargoes

and economic blockades, with higher import duties, quantitative restrictions and licensing against socialist countries. Stalin promoted the “two camps, two systems, two parallels and opposites” world market theory. Between 1955 and 1967, the Soviet Union's foreign trade nearly tripled reaching US\$18.2 billion in 1967, with two-thirds of the trade with socialist countries (Khachaturov 1972: 89). Trade between socialist countries was conducted through the Council for Mutual Economic Assistance (CMEA)(Khachaturov 1972: 95). Nearly 80% of Soviet exports of machinery and equipment went to the other CMEA members within the period (Khachaturov 1972: 94).

Beginning from the mid 1960 s, the leadership positions of United States and the Soviet Union in the world economic arena began to decline. The planned economic structure of the socialist countries was relatively rigid. With the passage of time, the disadvantages of the socialist economic system were increasingly revealed with the fall of economic growth rates of the Soviet Union. This is reflected by the GDP growth rate of 6.9% between the years 1961-1970 and 2.8% between the years 1981-1985 (Xue 1996: 10). Although the United States implemented the free market system with higher rates of economic efficiency, huge military expenses also held back development and depleted the country's fortunes.

At the same time, growth rates in Western Europe and Japan began to pick up and playing an increasing role in the world economy. The European Economic Community (EEC) was formed by six industrial countries of Western Europe and was the first and most forceful manifestation of regionalisation of world trade (Marchal 1972: 176). The United States provided the military protective umbrella for both

Western Europe and Japan, which enabled them to reduce their military expenses. As funds were not required for military purposes, they were used instead for economic and social development. This in turn strengthened their economic power. The enhanced role of Western Europe and Japan resulted in the emergence of a multi-polar world economy. European and Japanese firms began to internationalize very rapidly, quickly reducing the relative dominance of the USA and Britain. While US and Britain controlled 70.4% of all overseas investment in 1967, this had been reduced to 58.8% in 1976 (Brett, 1985: 85).

Moving into the 1980 s, the world economy took a step further towards multi-polarization. Some Newly Industrialized Countries (NICs)(according to the OECD Classification System) that had implemented correct economic development strategies in the 1960 s experienced rapid economic development, especially in their industrial and export sectors. Among the 11 NICs, Korea, Singapore, Taiwan and Hong Kong were the four East Asian nations which achieved remarkable success in exporting manufactured products. In 1965, these four countries together accounted for 30% of total developing countries' manufactured exports. In 1983, the figure rose to 77.2% (Todaro 1989: 371). They also recorded an average of 8% annual growth rate within the period 1960-1990 and were called "The Four Tigers" or "The Four Dragons" . They were also responsible for the so-called "East Asian Miracle" .

Basically, the successive 25 years after the Second World War (1948-1973) was the period of rapid development of the world economy. For example, according to various studies, for one and a half-century in the period 1800-1950, Western

European family incomes increased 1% annually. In contrast, between 1950 and 1975, the annual increment recorded a significant 4.5% (Xue 1996: 15).

However, after 1973, the world economy entered a period of severe global recession. There was an Energy Crisis and a Currency Crisis in this period. In the ten years after 1973, inflation soared to new heights, foreign exchange rates fluctuated frequently, the Bretton-Woods System collapsed, and GATT was found wanting. The world has slipped into a “non-system” in which no country was required to agree to any “substantial curtailment of their freedom of action” (Williamson, 1987, 18). Many countries experienced a slowdown in their overall economic growth and unemployment rates soared to new heights. In order to overcome these problems, developing countries tried to get a share of the world market, which intensified competition. Multinational companies (MNCs) attempted to maintain their competitive edge by investing overseas in order to reduce costs and overcome trade barriers set up by different countries. The ability to go multinational is crucial for survival in this modern monopolistic capitalist world and thus a company with ‘global reach’ is always likely to outperform any purely national company (Brett 1985: 84). Foreign direct investment (FDI) expanded on an unprecedented scale. In 1960, total FDI amounted to US\$66.7 trillion and US capital was the major source. In 1985, the figure rose to US\$ 644.6 trillion although the relative dominance of the US was reduced (Jun Nishikawa 1988: 37). In the same period of 1960-1985, capital resources were rapidly growing and being dispersed to maximize the returns of their owners throughout the world. The enormous international movement of capital and skills played a crucial role in international economic relations.

FDI induced trade and deepened interdependence among nations. The sense of mutual dependence between home and host countries was heightened. The recipient countries of FDI benefited from structural changes and industrial adjustments in advanced countries, which led to the relocation of industries offshore. In fact, few developments played as critical a role in the extraordinary growth of international trade and capital flows during the 1960s and 1970s as the rise of the Multinational Corporation (MNC)(Todaro 1989: 469). An MNC refers is a firms which has production units in two or more countries, that engages in both international trade and international factor transfers. Besides bringing in funds or establishing factories, they carried with them technologies of production and managerial culture that influenced the countries in which they invested. By opening their economies and societies to FDI, the recipient country invited not only the transfer of goods, services, and financial resources, but also production technologies, consumption patterns, institutional and organizational arrangements and lifestyles of the developed nations. The world we live in is increasingly borderless due to the influence of the MNCs.

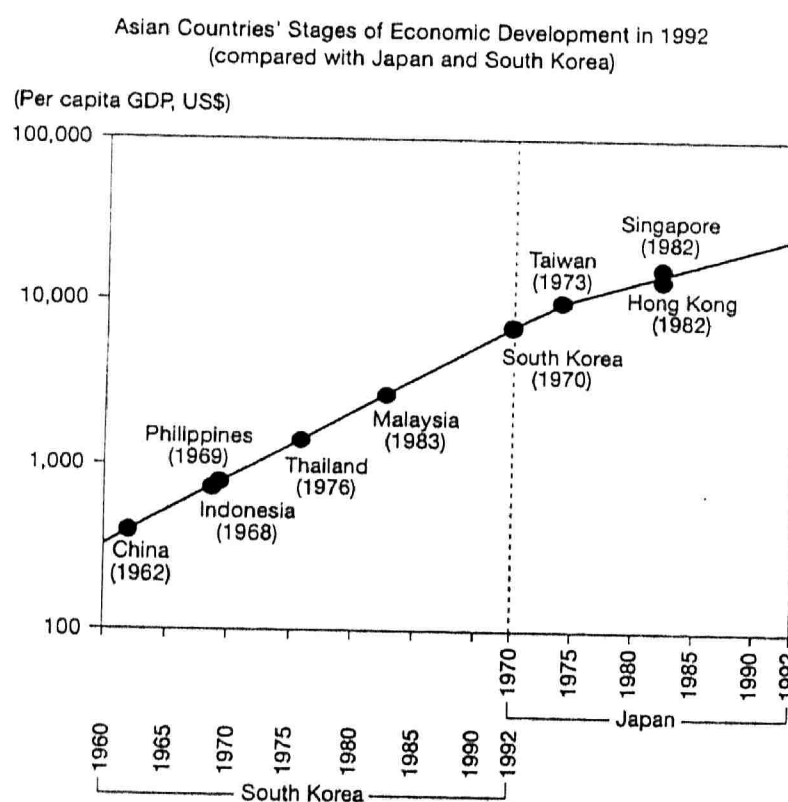
The characteristics of MNCs are their large size, cross-border and centrally controlled operations. Traditionally, MNCs operating in developing nations focused on extractive and primary industries (Brett 1985: 86), for example, Shell and Rothmans in Malaysia. Some of these companies might have existed even during the Colonial period. Recently, MNCs have increased their participation in manufacturing, for example, National and Motorola in Malaysia. In short, the overall importance of MNCs in the economies of Third World Nations, especially in the manufacturing and service sectors, is rapidly growing (Todaro 1989: 474).

In the context of the Asia Pacific region, the role of MNCs and their significance in the international division of labour could be seen in a framework of three layers, represented by the US and Japan at the top, followed by the NICs and members of Association of South East Asian Nations (ASEAN). After the Second World War, the US engaged in large-scale investment and increased imports from Japan. Japan made full use of its comparative advantage, i.e. lower production costs, and succeeded in achieving rapid development. After 1970, both the US and Japan invested heavily in and imported substantially from some East Asian countries such as Korea, Taiwan, Hong Kong and Singapore, which then emerged as NICs. In 1975, 74% of all MNCs' investments were in developed countries and only 26% in Less Developed Countries (LDCs) (Brett 1985: 87). Since the 1980's, both the US and Japan (the first layer) and the NICs (the second layer) have invested in and imported from the ASEAN countries, and indirectly contributed to forming the third layer. (Tan L. H. 1994: 47) In general, the rapid increase in intra-regional FDI was one of the most noticeable phenomenon in the economic development of the Asia Pacific region since the mid 1980's (Chen K.Y. 1994: 11).

From early 1993, there has been a surge of FDI not only from Japan to many parts of Asia but also among many countries and regions within Asia (Fukushima and Kwan 1995: 7). The focus of FDI in Asia since the 1985 Plaza Accord has shifted from the Asian NIEs to ASEAN and further to China, broadly in line with the flying-geese pattern (Nomura 1995: 14) whereby industries and technologies are passed from more advanced to less advanced countries in response to the shift in comparative advantages (Akamatsu, 1962). It is estimated that the economic gap between Japan and the NIEs is between ten years (for Singapore and Hong Kong) and twenty-two

years (for Korea). While the economic gap is nine years between Korea and Malaysia and thirty years for China (Figure 1.1). Since 1990, Japanese FDI to the ASEAN countries has declined except for the electronics sector, in part because economic difficulties and the stock market slump in Japan, and in part because many firms have completed most of their offshore expansion, while FDI to China has grown tremendously (Pang 1994: 42).

Figure 2.1 Asian Countries Stages of Economic Development in 1992



Source: Normura Research Institute, in Fukushima and Kwan 1995: 16.

Since Vietnam hastened its rapprochement with the West after the collapse of the Soviet Union, FDI to Vietnam has grown very rapidly since 1991. Ever since

Malaysian Prime Minister Mahathir Mohamad led a business delegation to Vietnam in 1992, many Malaysian companies have flocked to Vietnam to invest (Forbes 4/94: 62-69). In the mean time, the FDI level also rose in India since the Rao administration changed the planned economic policy to economic liberalization and stabilization (Fukushima and Kwan 1995: 23-24). While Taiwan and Hong Kong were the largest investors in both China and Vietnam, the US played the same role in India. The shift in FDI suggests that the forth layer has been formed or in some areas are in the process of being formed. The rise of Malaysian investments in China since 1990's supports this observation, although neither in terms of scale nor variety does it matches Taiwan, Hong Kong or Singapore's investments in China.

II. Development of China's Economy After 1949: the Mao Era

On October 1, 1949, when Mao Zedong announced at Tiananmen: "the Chinese people stood up!" the PRC was established officially (FEER 14/1/99: 12). Thus 1999 marks the CCP's fiftieth year as ruler of China. In the eye of some scholars, the history of the PRC can be divided into the Mao Zedong era (1949-1976) and the Deng Xiaoping era (after 1979), with the Hua Guofeng interval between them (Yabuki Susumu 1995: 1).

Between the year 1949 and 1957, the supremacy of Mao Zedong was unchallenged. The thought of Mao Tse-tung was enshrined in the CCP's new constitution. Despite the emphasis of collective leadership, Mao was granted powers to make decisions independently (MacFarquhar 1987a: 60). Under his supervision,

PRC “tilted toward the USSR” and pursued the Soviet model in developing the economy.

Land reform was launched in 1951. It was in this period that the landed classes were exposed and criticized. Subsequently, land was reallocated to the majority of the population in villages. After that, individual farms were reorganized in a three-step process: first into mutual aid teams where labor was pooled but ownership retained by individual peasants; then into the low-stage Agricultural Producers’ Cooperatives (APCs), where property was controlled by the collective and each peasant received a dividend base on his/her contribution of material; and finally into high-stage APC where payment was given based on labour (MacFarquhar 1987a:110-113).

As for the industrial sector, the PRC implemented nationalization. In late 1952, 70-80% of China’s heavy industry and 40% of its light industry had been nationalized. State trading agencies and cooperatives handled more than half of the total business turnover (MacFarquhar 1987a: 93).

After a few years of recovery, the PRC successfully launched the First Five-Year Plan in mid 1952. The plan was similar to the Soviet Union Plan of 1928-1937 (MacFarquhar 1987a: 157). The strategies of the plan included:

- 1) A rise in the investment rate from about 5% to more than 20%,
- 2) Overwhelming allocation of investment in the industrial sector, with only 8% of total investment in agriculture,
- 3) preference for large scale and capital intensive manufacturing projects.

Although agricultural collectivization did not speed up the development of agriculture as expected, development in the industrial sector has been far more encouraging. Industrial output rose by 130% against the targeted 100% benchmark (MacFarquhar 1987a: 174). It was this period that the PRC relied critically on USSR capital goods and technology (e.g. 28 000 Chinese technicians and skilled workers were sent to Moscow for training). The importance of Soviet technical assistance and capital goods is undeniable (MacFarquhar 1987a:174-184).

Generally speaking, nearly all the problems faced by the PRC when it was just established, such as inflation and unemployment, were solved by the mid 1950's. With the economy back on the right track after years of turmoil, the PRC's China was impressive.

However, when the National Planning Committee tried to reduce the speed of agricultural collectivization and increase the investment in agriculture and light industrial sector in the Second Five-Year Plan, Mao launched the Anti-Rightist Struggle to regain his power. He suggested "Great Leap Forward" to replace the First Five Year Plan in mid 1958 and proclaimed to "overtake Britain" in 15 years (MacFarquhar 1987a: 319).

The Great Leap Forward ended with one of the twentieth century's most devastating famine causing the deaths of around 16 to 27 million Chinese lives (MacFarquhar 1987a: 318, 370-373). The failure of the Great Leap Forward is said to be mainly due to a failure to understand the dynamics of the agricultural sector

(MacFarquhar 1987a: 363). During this period, old peasant techniques were blindly introduced and mass mobilization of labour was instituted in a frenetic pursuit of increased production. The mistakes in policy making coupled with natural disasters and abrupt termination of Soviet assistance, plunged the PRC into an economic crisis.

In order to overcome the situation, several measures were introduced to revive the peasants' motivation to work (e.g. peasants were once again allowed to have their own piece of land for cultivation). They were also allowed to conduct sideline household production, which was banned since the introduction of people's commune (MacFarquhar 1987a: 389). The economy recovered quickly, for example grain production in 1965 rose again to the level of 1957, and the industrial sector recovered even faster (MacFarquhar 1987a: 392).

Studies by various scholars suggest that the economy within the period of the Great Leap Forward was nearly stagnant. There were wide fluctuations in the various productivity indicators (Ishikawa 1972: 324). Comparisons of the 1966 figures with those of 1957 are shown in Table 2.1.

Table 2.1 Estimates of Net Domestic Product (NDP)
by Components: 1957 and 1966

	1957		1966	
	Liu-Yeh	Ishikawa	Liu	Ishikawa
NDP	40.5	47.4	50.6	55.8
Traditional Sector				
Total	21.1	24.9	19.8	22.3
Agriculture	15.8	19.7	14.6	16.9
Modern Sector				
Total	19.4	22.5	30.9	33.5
Government	2.1	--	2.4	2.4

Consumption				
Private	28.6	37.9	34.5	35.2
Government	3.9	--	4.5	4.5
Domestic Investment	7.7	8.9	11.2	15.6
Export Excess	0.2	0.6	0.3	0.5
Per Capita NDP (US\$)	63.6	74.6	68.9	75.8

Source: Ishikawa 1972: 326

1966 marked the start of the Third Five-Year Plan as well as the ten-year long Cultural Revolution. During the period of the Cultural Revolution, the PRC had no clear economic strategy mainly due to the chaos in the political arena (MacFarquhar 1987b: 475). Mao, who judged that China was changing into a "revisionist society", launched the Cultural Revolution. Nearly all the first line members of the party leadership were vilified as "bosses walking the capitalist road" and "Chinese revisionists" and were overthrown. The "Gang of Four" (Jiang Qing, Wang Hongwen, Zhang Chunqiao, Yao Wenyuan) rose abruptly.

Although there was political turmoil in the PRC, the negative effect of Cultural Revolution on the economy was minimal compared to the Great Leap Forward. Transportation and industry had recovered by 1970 though hit badly in 1967 and 1968 (Table 2.2, Table 2.3). The agricultural sector suffered but on a smaller scale (MacFarquhar 1987b: 481-482)(Table 2.4). Lin Biao, the proclaimed successor of Mao, died in an air clash in 1971 leading to another round of political uncertainty in China. However, the effects of this political incident on the economy was negligible. Even when Mao and Zhou Enlai died consecutively in 1976, with the "Tangshan Earthquake" happening in the same year, there was little discernible impact on the economy. We can attribute this to the subordinate officials who kept the guiding principle set before the Cultural Revolution (MacFarquhar 1987b: 488).

Table 2.2 **Indexes of Industrial Output During the Cultural Revolution (1966=100)**

	1957	1962	1965	1966	1967	1968	1969	1970	1975
Power	23	56	82	100	94	87	114	140	237
Steel	35	44	80	100	67	59	87	116	156
Coal	52	87	92	100	82	87	106	140	191
Petroleum	10	40	78	100	95	110	149	211	530
Cement	34	30	81	100	73	63	91	128	230
Machine tools	31	41	74	100	74	85	156	253	319
Fertilizer	6	19	72	100	68	46	73	101	218
Cloth	69	35	86	100	90	88	112	125	129
Bicycles	39	67	90	100	86	97	142	180	304

Source: State Statistical Bureau, Statistical Yearbook of China, 1981, 225-31, in MacFarquhar 1987b: 481.

Table 2.3 **Transport and Commerce During the Cultural Revolution**

	1957	1962	1965	1966	1967	1968	1969	1970	1975
Freight traffic (billion ton/km)	181.0	223.6	346.3	390.1	305.0	310.9	375.3	456.5	729.7
Rail traffic (billion ton/km)	134.6	172.1	269.8	301.9	226.9	223.9	278.3	349.6	425.6
Retail sales (billion yuan)									
Urban	23.84	31.85	33.89	36.28	38.20	37.32	39.35	40.00	60.69
Rural	23.58	28.55	33.14	37.00	38.85	36.41	40.80	45.80	66.42
Farm products purchases (billion yuan)	21.75	21.11	30.71	34.59	34.48	33.82	32.40	34.78	47.86
Grain purchases (million tons)	45.97	32.42	39.22	41.42	41.38	40.41	38.45	46.49	52.62
Foreign trade (billion US\$)									
Exports	1.60	1.49	2.23	2.37	2.14	2.10	2.20	2.26	7.26
Imports	1.51	1.17	2.02	2.25	2.02	1.95	1.83	2.33	7.49

Source: State Statistical Bureau, Statistical Yearbook of China, 1981: 283,333,345,357, in MacFarquhar 1987b: 481.

Table 2.4 Agricultural Outputs and Inputs During the Cultural Revolution (m. = million)

	1957	1962	1965	1966	1967	1968	1969	1970	1975
Grain (m. tons)	195	160	194.5	214	218	209	211	240	284.5
index	91	75	91	100	102	98	99	112	133
Cotton (m. tons)	1.64	0.75	2.10	2.34	2.35	2.35	2.08	2.28	2.38
index	70	32	90	100	101	101	89	97	102
Hogs (m. head)	145.9	100.0	166.9	193.4	190.1	178.6	172.5	206.1	281.2
index	75	52	86	100	98	92	89	107	145
Fertilizer (m. tons)									
production	0.15	0.46	1.73	2.41	1.64	1.11	1.75	2.44	5.25
imports	1.22	1.24	2.73	3.15	4.88	5.21	5.55	6.42	4.94

Source: State Statistical Bureau, Statistical Yearbook of China: 229, 386; Chung-kuo nung-yeh nien-chien, 1980: 34, 40, in MacFaquhar 1987b: 482.

As for foreign trade, before the late 1970's, imports as a percentage of national income fluctuated between 5-7% (Table 2.3). This was a reflection of the country's large size as well as the implementation of the close door policy (MacFaquhar 1987b: 489).

Although Hua Guofeng emerged as the leader of the PRC after the death of Mao in 1976, Deng Xiaoping was able to regain power in 1978. After Mao's death, the industrial strategy emphasized sending people abroad to learn foreign technology. There was also renewed reliance on material incentives to motivate workers and farmers (MacFaquhar 1987b: 495). With the economy under the charge of Deng, this marked the end of the Mao Zedong era. A series of reforms and an open door policy were set on track. Deng's pragmatic approach was encapsulated in his comment, "It does not matter whether the cat is white or black; if it catches mice it is a good cat."

RC under Deng's supervision gradually abandoned the thirty year old system of rigid, centralized economic planning and found ways to convert itself to the market system which the Beijing government aptly describes as "Socialism with Chinese Characteristics".

III. FDI and Joint Ventures in China after 1978: the Deng Era

For some 30 years since the establishment of the PRC, China operated under a system of economic planning which emphasized the principle of "self-reliance". The death of Mao in 1976 created the opportunity for the rehabilitation of Deng Xiaoping as well as the abandonment of central planning and allowed space for conversion to a market system.

The first step of this transformation was taken in December 1978 when the CCP adopted the policy of economic reform at the Third Plenum of the Eleventh Party Congress. Later, five documents were issued by the State Council shifting to an emphasis on market adjustment mechanism (Yabuki 1995: 41). In spring 1982, Chen Yun, vice president of CCP announced the concept of "birdcage economy". The concept was presented analogously by likening the planned economy to a cage within which the market adjustment mechanism, like a bird, could fly freely, thus vitalizing the economy. In other words, the system of economic planning continued as the basis for activity, but market forces were introduced and allowed to play an increasingly larger adjustment role (Yabuki 1995: 42-43).

Contemporaneous developments in the liberalization policy was the adoption of the “Law of the PRC on Joint Ventures Using Chinese and Foreign Investment”(Joint Venture Law) by the Fifth National People’s Congress in July 1979. Although the law fell far short of guiding both Chinese and foreign partners in crucial legal and operational matters (Pearson 1992: 71), it opened the door to direct foreign investment and provided a legal basis for establishing joint ventures. To facilitate the Joint Venture Law, some regulations and detailed rules such as The Income Tax Law, Regulations for Foreign Exchange Control and Procedures for Registration and Administration of Chinese-Foreign Joint Ventures were promulgated.

On 15 December 1979, the State Council of the PRC decided to develop Baoan county of Guangdong Province as an “export commodities production base”. Baoan County was now known as Shenzhen municipality, which was the first of four “special economic zones”(SEZs) announced in 1981 besides Zhuhai, Shantou in Guangdong and Xiamen in Fujian (Yabuki 1995: 243-244). Several packages of special policies were announced and special autonomy in fiscal affairs, planning, foreign trade and investment, finance, material allocations, commerce, labour management and price management were given to these zones.

In the pre-reform era, China stressed the development of industry and agriculture and neglected the development of the tertiary sector. The tertiary sector in 1980 made up only 21% of China’s Gross Domestic Product (GDP) (Table 2.5). As a result of the participation of foreign investors, many big hotels and restaurants and

other service facilities have been built in the SEZs, and later developed in different parts of the country. Development of the tertiary sector, especially tourism, was rapid in a relatively short period of time. In 1989, the share of the tertiary sector in China's GDP rose to 26.5% (Sung 1995: 92). The figure rose to more than 30% in 1997 (Lu Ji Ming 9/98: 102). Guangzhou, one of the very first cities that was opened to foreign investors, enjoyed an even higher percentage of growth in the tertiary sector (Sung Yun Wing et al. 1995: 92).

Table 2.5 Share of Gross Domestic Product by Sector (%)

	Sector	China	Guangdong	Total	Guangzhou	Other Areas	Shenzhen
1980	Primary	30.4	33.8	26	12	40	--
	Secondary	49	41.1	44	54	33	--
	Tertiary	20.6	25.1	30	34	27	--
1990	Primary	28.4	26.1	14.8	8.1	18.8	5.2
	Secondary	44.3	39.9	46.4	42.6	48.5	52.9
	Tertiary	27.2	34	38.8	49.3	32.7	42
1993	Primary	21.2	17.4	8.6	6.4	12.8	2.7
	Secondary	51.8	50.4	51.4	47.5	53.3	53.6
	Tertiary	27.0	32.3	40.0	46.1	33.9	43.7

Source: China Statistical Yearbook and Guangdong Statistical Yearbook, in Sung 1995: 93.

However, internal objections to liberalisation continued to emerge. Chen Yun, for example, sought to put an end to the special economic zones in December 1981. The CCP Party Central even launched a campaign against "spiritual pollution" in 1983. This impelled foreign investors to adopt a wait-and-see attitude and foreign investment dropped sharply (Kwan 1991:136). In defence of his opening policy, Deng toured Shenzhen, Zhuhai and Xiamen in early 1984 and endorsed the correctness of the liberalization policy. 14 more coastal cities from north to south (Table 2.6), were

opened in May 1984 to foreign participation (for location please refer to Appendix C). Some of the preferential policies adopted in SEZs were implemented and the local governments had more power in the establishment of foreign-funded enterprises. These cities provided virtually all of the port facilities in China and accounted for nearly 25% of China's industrial output (Sung 1995: 19-20). With that decision, a second surge of opening to the outside world began.

Table 2.6 List of 14 Coastal Cities

1.	Dalian	大连
2.	Qinhuangdao	秦皇岛
3.	Tianjin	天津
4.	Yantai	烟台
5.	Qingdao	青岛
6.	Lianyungang	连云港
7.	Nantong	南通
8.	Shanghai	上海
9.	Ningbo	宁波
10.	Wenzhou	温州
11.	Fuzhou	福州
12.	Guangzhou	广州
13.	Zhanjiang	湛江
14.	Beihai	北海

Source: Zhang Zuo Quan 1986: 222.

In early 1985, PRC further opened Changjiang (Yangtze) River Delta, Zhujiang (Pearl) River Delta and Southern Fujian Triangular Region (Xiamen-Zhangzhou-Quanzhou) as coastal open economic zones (Table 2.7), where some of the policies adopted in the 14 coastal open cities were implemented. Coastal area

remained the favourite places for FDI until the 1990's. In 1996, out of the top 500 foreign enterprises, 444 were located in coastal areas (Lu Ji Ming 9/98: 101).

Table 2.7 List of Coastal Open Economic Zones

1. Changjiang River Delta included:
 - Jiangsu Province: Suzhou City, Changshu City, Wu County, Shazhou County, Taicang County, Kunshan County, Wujiang County, Zhangjiagang County, Wuxi City, Wuxi County, Jiangyin County, Yixing County, Changzhou City, Wujin County, Jintan County, Liyang County;
 - Zhejiang Province: Jiaxing City, Jiashan County, Tongxiang County, Haining County, Huzhou City, Deqing County;
 - Shanghai City: Shanghai County, Jiading County, Baoshan County, Chuansha County, Nanjiang County, Fengxian County, Songjiang County, Jinshan County, Qingpu County, Congming County.
2. Pearl River Delta included:
 - Guangdong Province: Foshan City, Zhongshan City, Hainan County, Xunde County, Gaoming County, Jiangmen City, Kaiping County, Xinhui County, Taishan County, Heshan County, Enping County; Panyu County, Zencheng County; Baoan County; Dongguan County.
3. Southern Fujian Triangular Region included:
 - Fujian Province: Tongan County; Zhangzhou City, Longhai County, Zhangpu County, Dongshan County; Quanzhou City, Huian County, Nanan County, Jinjiang County, Anxi County, Yongchun County.

Source: Zhang Zuo Quan 1986: 235.

In April 1986, the National People's Congress adopted and promulgated the "Law Governing Wholly Foreign-owned Enterprises" to further boost the FDI.

Although there are 9 forms of enterprises in China (Wang Rui Tian 10/93: 105), most FDIs take three forms in China: Chinese-foreign joint venture (also known as equity joint venture)(EJV), Chinese-foreign cooperative joint venture (also known as contractual joint venture)(CJV) and wholly foreign-owned enterprises (WFOE). The CJV model was rather popular at the beginning of 1980s. From 1979-1982, it accounted for 87.2% of the total foreign-funded enterprises. However, after mid 1980's the EJV is the more popular form. Up to 1991, EJVs rose to 54% of total foreign investment in China. Since 1980's, WFOE has been growing steadily. Between 1979 and 1982, they accounted for 5.8% of the total FDI. In 1993, WFOE accounted for 24.2% of the total utilized foreign capital.

In the first half of 1986, for the first time since 1979, pledged FDI dropped as much as 20%. Foreign investors were complaining about the bureaucratic walls and also about tight foreign exchange controls (NYSP, 6/8/86). The descending trend of pledged FDI continued throughout the year. By the end of 1986, pledged FDI dropped another 48% to USD 3308million, down from 1985 figure of US\$6 600 million (NYSP, 24/1/87). Nevertheless, at the same time several problems became evident which included the issue of foreign exchange imbalance and the rampant incidence of economic crimes (Yabuki 1995: 246-247). This sparked debate over the special economic zones and the policies came under heavy fire and even Deng had to qualify his earlier support of Shenzhen. Hu Yaobang, the liberal general secretary of CCP was forced to resign in January 1987 (Sung Yun-Wing 1995: 20).

However, the liberalisation of the economy continued despite international doubt about the continuity of economic reforms. A third reform drive was then

launched. Besides new regulations governing foreign investment, Premier Zhao Ziyang granted permission allowing "foreign capital to directly manage the enterprise, respecting their management authority" in November 1987, which was seen as a bold concession to foreign capital (Yabuki 1995: 252). In December 1987, the Pearl River Delta Economic Development Zone was enlarged from the Inner Delta to the Outer Delta. Hainan island became a separate province in mid 1988 with a higher degree of autonomy and 18 additional coastal cities were opened (Sung Yun-Wing 1995: 21). The open areas form a three-tier structure in terms of increasing degrees of autonomy: coastal opened areas, coastal open cities and SEZs, as shown below (figure 2.2). The enlargement of opened areas stimulated another round of inflow of FDI. Between the year 1987 and 1991, contracted foreign investment amount to US\$33.16 billion, (i.e. average of US\$6.63 billion annually). This figure was 1.4 times higher than the average figure between the year 1979 and 1986 (Table 2.8).

Figure 2.2 Three Degrees of Autonomy

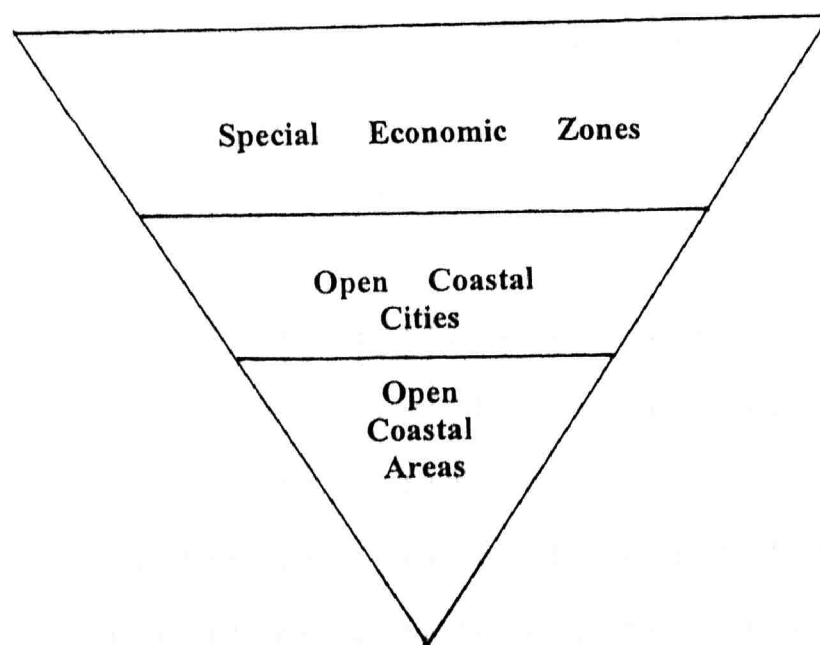


Table 2.8 FDI in China, 1979-1996 (US\$ billion)

Year	number of Investment	contracted investment	utilized investment
1979-1986	7 819	19.18	6.59
1987	2 233	3.71	2.32
1988	5 945	5.30	3.19
1989	5 779	5.60	3.39
1990	7 273	6.60	3.49
1991	12 978	11.98	4.37
1992	48 764	58.12	11.01
1993	83 437	111.44	27.52
1994	47 490	81.41	33.79
1995	37 014	91.23	37.52
1996	24 529	73.21	42.35
Total	283 261	467.75	1 75.46

Source: Xu Kang Ning 5/1997: 95 with amendments.

Another noticeable event of 1988 was price reforms. Price liberalization on meat, sugar, eggs and vegetables were tested in May 1988, followed by cigarettes and liquor in July (SCJP, 21/8/88). Discord among high level leaders regarding the price reform suspended the central political committee to meet at Beidai River (NYSP, 3/8/88). However, the meeting resumed one month later. Unfortunately, the price reforms precipitated panic buying and runs on the banks and were shelved in September of the same year (Sung 1995: 21).

Popular dissatisfaction over inflation and corruption led to social unrest and the outbreak of the pro-democracy movement in the spring of 1989. Zhao Ziyang was ousted for his sympathy towards the movement. The "Tiananmen Incident" dealt a severe blow to economic reforms and the open-door policy, as a result of which China entered a period of retrenchment. Foreign investment stagnated for almost two years.

It is worth noticing that Malaysian Trade and Industry Minister Datuk Rafidah Aziz still visited China as planned after the "Tiananmen Incident" (SCJP, 23/7/89) and that Malaysian billionaire Robert Kuok, still continued his projects in Beijing despite the incident (Forbes 28/7/97: 96). The economic relations between two countries seemed uninterrupted and the Vice Premier of China, Yao Yilin thanked Malaysia for "not intervening in China's domestic affair" and praised Malaysia for being "a friend in adversity" (NYSP, 27/7/89).

In an effort to lure foreign investment, PRC amended the Joint Ventures Law in March 1990. It stipulated that the state shall not nationalize any investment made by foreign investors and that foreign businessmen can assume the position of Chairman of the Board of Directors. In addition, foreign investors were also allowed to transfer to others the right of the use of land. The central government opened and developed Pudong New Area in Shanghai, which implemented the preferential policies of SEZs.

Shortly after 14 border cities and towns in the north were opened in 1992, five cities along the Changjiang (Yangtze) River, seven capitals of border provinces and autonomous regions, and 11 provincial capitals in the interior were also opened. All these cities implemented the policies of the coastal open cities and offered preferential treatment to foreign investors. As a result, the FDI rebounded remarkably, recording an increase of 152% over 1991 (Table 2.9).

TABLE 2.9 FDI In China By General Situation (US\$ Million)

Year	Contracted FDI	Utilized FDI
1979—1992	110462	34355
1979—1983	7742	1802
1984	2651	1258
1985	5932	1661
1986	2834	1874
1987	3709	2314
1988	5297	3194
1989	5600	3392
1990	6596	3487
1991	11977	4366
1992	58124	11007

Source: Statistical yearbook of China (1993), in Qing 1996: 93.

In the early stages of liberalization, China's comparative advantage was in labour-intensive industries instead of capital-intensive or skill-intensive ones. The first batch of foreign investors from Hong Kong had concentrated in labour-intensive manufacturing industries (Ash 1995: 85). The Taiwanese investors were pioneers in the footwear manufacturing industry of China (Liu Jian Lin 2/1993: 33). Later, many multinational companies and Overseas Chinese tested the Chinese investment environment through their subsidiaries in Hong Kong. Moreover, even Chinese companies invested in China through their Hong Kong subsidiaries in order to take advantage of the preferential treatment given to foreign investors (Sung 1995: 68). South China became a major production base for Hong Kong's traditional labour-intensive products. It was estimated that there were almost 25 000 Hong Kong manufacturing enterprises with employment of about four million workers operating in South China, which concentrated on textiles and clothing, toys and consumer

electronic in 1995 (Qing 1996: 94). This constituted a labour force about six times greater than the colony's own manufacturing workforce. From southern coastal areas, especially Guangdong and Fujian provinces, investors gradually surged to the eastern coastal areas. Between 1979 and 1991, Guangdong accounted for 43.4% of total foreign pledged investment, followed by Fujian which accounted for 9.2% (Guo 10/96: 62).

In the early years of 1980's, although the Taiwan government implemented the "three no's policy" (no contact, no negotiation and no compromise) and banned businessmen from investing in China, some businessmen already secretly invested in China through a third country. Their investments were small and export oriented. Thanks to the preferential treatment of the PRC government, these farsighted businessmen gained substantial profits from their investment (Zhou 4/96: 30).

The large-scale influx of Taiwanese capital into the PRC did not start until 1988. In the late 1970's, the appreciation of New Taiwan Dollar coupled with the deterioration in the domestic investment environment forced many Taiwanese companies to relocate outside Taiwan. At first, the United States was their preferred destination, followed by the Southeast Asia (Ho 1993: 32). Later, the political relaxation, in particular, the removal of the ban on travel to mainland China in 1987, triggered a steady stream of investment to the PRC (Qi 1995: 98). Between 1979-1991, the major source of the People's Republic of China's FDI is Hong Kong and Macao, which accounts for about 64% of the total FDI (Table 2.10). However, in 1992 alone, Taiwanese capital accounted for 13.19% of total FDI projects in China and 9.54% of total foreign capital commitments (Qi 1995: 98).

Table 2.10 FDI In China By Source (Contracted Investment In \$ Million)

	1979-84	1985	1986	1987	1988	1989	1990	1991
National Total	10393	5932	2834	3709	5297	5600	6596	11977
Hong Kong	6495	4134	1449	2466	4033	3645	4258	7215
United States	1025	1152	541	361	383	646	366	548
Japan	1158	471	283	385	371	515	478	812
Taiwan	---	---	---	100	420	480	1000	---
Singapore	117	77	141	80	137	148	107	155
Canada	66	9	91	34	40	49	21	31
Australia	91	14	32	47	17	84	18	44
Korea	---	0.1	1.8	6	5.4	14.5	57	---
Germany	142	20	56	140	69	160	---	---
United Kingdom	334	44	52	29	56	33	---	---
France	213	50	12	74	33	18	---	---
Italy	113	25	92	19	23	63	---	---
Thailand	26	15	13	5	42	57	---	---
Philippines	6	41	4	31	16	5	---	---

Note: --- = not available

Source: Qing 1996: 94 with additions.

FDI has been a major factor in stimulating economic growth and development in the PRC. For instance, FDI's played an important role in creating employment opportunities for the civilian population. In 1996, 120 000 foreign funded enterprises directly employed a total of 17 million people (Xu Kang Ning 5/1997: 96). In the coastal and southern provinces where foreign participation is more active, economic growth and improvement in living standards outperform the rest of the country (Sung 1995: 8-9). Although after years of market competition, foreign enterprises' products gradually took over the market share of home products and this raised public concerns (NYSP, 14/5/97). However, the ability of FDIs in promoting economic development

is beyond dispute. In the case of China, besides serving as a source of capital, technology and managerial skills, the benefits of FDIs were a driving force that fostered economic growth through its mobilization of domestic resources. It was also an agent to explore export markets and as an accelerator of economic transformation and restructuring (Qing 1996: 98).