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Why Is China Growing So Fast?

ZULIU F. HU and MOHSIN S. KHAN*

China has been growing at a spectacular rate in recent years, enabling per capita incomes to almost quadruple in only the last decade and a half. This paper identifies the sources of economic growth in China from 1952 to 1994. While capital accumulation played an important role in China's economic growth throughout the period, it is basically the sharp and sustained increase in total factor productivity that accounts for the unprecedented economic growth observed during the reform period. The productivity gains largely reflect market-oriented reforms, especially the expansion of the nonstate sector, as well as China's "open-door" policy, which brought about a dramatic expansion in foreign trade and foreign direct investment. [JEL O4, O5]

Capital accumulation played a dominant role in China's economic growth during the central planning era of 1952–78 (Perkins, 1988 and 1989; and Chow, 1993) because of the ability of the government to mobilize saving and undertake large-scale investments in physical and human capital to support its policy of rapid industrialization. Growth rates, while impressive, were substantially below those that have been witnessed in more recent years. Since market-oriented economic reforms were launched in 1978, China has achieved quite phenomenal rates of growth, with real GNP growing on average by nearly 10 percent a year. What are the principal sources of China's postreform economic growth? In particular, what has been the role in China's recent growth performance of the improvements in productive efficiency that typically are expected to accompany structural reforms? These are the main questions addressed in this paper.

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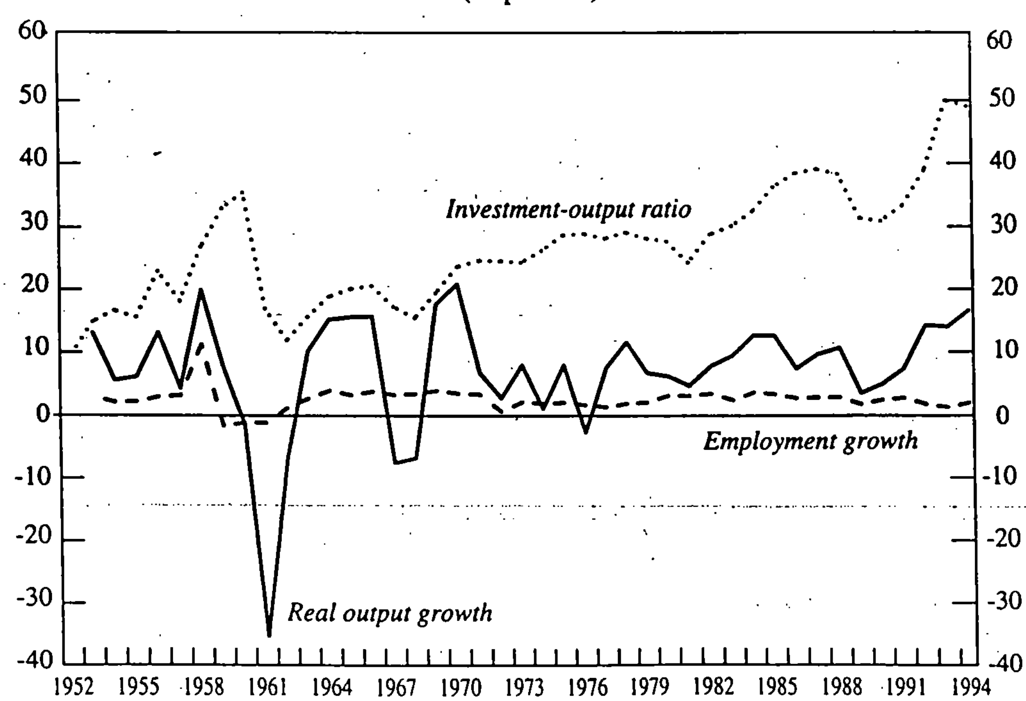
It is useful first to consider some stylized facts to obtain an overview of the issue under consideration. Figure 1 depicts the behavior of the investment-output ratio, employment growth, and output growth in the 1952–94 period. Real national income expanded by an average of 7.2 percent annually in the past four decades. The average investment-output ratio was above 27 percent throughout the period, and in fact rose to over 40 percent toward the final years of the period. By contrast, employment growth was fairly steady, averaging 2.6 percent, although the educational attainment of the labor force, and thus its quality, increased significantly over this period.

This study examines the contributions of capital and labor inputs, and particularly productivity, to economic growth in China within the standard neoclassical growth framework. To undertake this exercise, a comprehensive data set based largely on official Chinese-language sources was constructed. This data set contains consistent time series on the relevant variables for a longer period than hitherto available. The results of the decomposition of growth highlight the relative importance of each factor in explaining the growth of output and thus provide important insights about the underlying causes of economic growth in China.

The central finding that emerges from this study is that, while physical investment continued to play a dominant role in China's economic

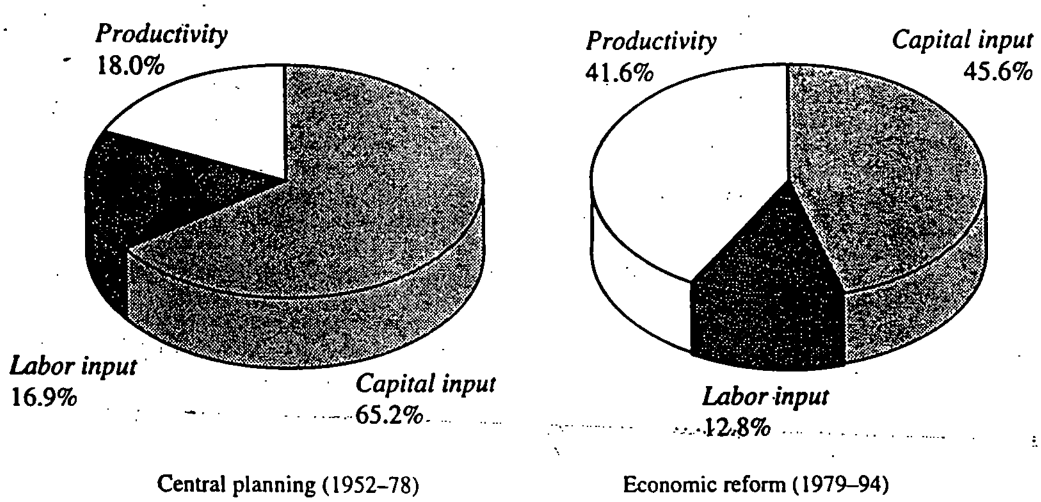
Figure 1. *Factor Supply and Output Growth*
(In percent)



growth, its importance diminished over time, particularly during the reform period 1979–94. Since economic reforms were initiated, productivity growth has become the more significant force in driving the Chinese economy. Figure 2 shows the relative importance of capital, labor, and productivity in China's economic growth before and after the reforms. Capital formation contributed over 65 percent of the output growth in the central planning era of 1952–78, while productivity growth contributed only 18 percent. However, a new pattern emerged following China's economic reforms. In the 1979–94 period, productivity growth became substantially more important and accounted for about 42 percent of China's aggregate growth.

This study adds to a growing literature examining China's recent growth experience, including McMillan, Whalley, and Zhu (1989), Li and others (1993), Woo (1995), Borensztein and Ostry (1996), and Sachs and Woo (1997). Since these studies are all motivated by a set of closely related issues concerning China's growth, some of the differences between the findings here and the results obtained in these other studies will be briefly outlined. Comparisons of the results for China in the paper are also made with available estimates for industrialized countries, some Latin American countries, and four East Asian newly industrialized economies.

Figure 2. *Sources of Economic Growth, 1952–94*



Source: Authors' estimates.

The remainder of this paper proceeds as follows. Section I briefly outlines the methodology used in this study. Section II describes how the data set was constructed. Section III presents the main findings of the analysis. Section IV extends the results in a number of directions and compares the findings for China with those obtained in other studies. The final section contains some concluding remarks.

I. Methodology

The methodology utilized in the analysis of this paper is the familiar one based on the notion of an aggregate production function for the economy. As is well-known from the large body of growth-accounting literature, this aggregate production function approach is an analytical simplification that makes it possible to summarize detailed information about the complex process of economic growth within a simple, unified framework.[1]

The neoclassical growth framework takes as its starting point an aggregate production function, F, which relates a national output measure to capital and labor inputs and time:

$$Y = F(K, L, T), \tag{1}$$

where Y is output, K and L are capital and labor inputs, and T is time. The specific form for the production function selected here is the translog production function:[2]

$$Y = \exp[\alpha_0 + \alpha_k \ln K + \alpha_l \ln L + \alpha_t T + \frac{1}{2}\beta_{kk}(\ln K)^2 + \beta_{kl}\ln K \ln L + \beta_{kt} T \ln K + \frac{1}{2}\beta_{ll}(\ln L)^2 + \beta_{lt} T \ln L + \frac{1}{2}\beta_{tt} T^2]. \tag{2}$$

The translog production function represents constant returns to scale technology if and only if the parameters satisfy the following conditions:

$$\alpha_k + \alpha_l = 1, \quad \beta_{kk} + \beta_{kl} = 0, \quad \beta_{kl} + \beta_{ll} = 0, \quad \beta_{kt} + \beta_{lt} = 0. \tag{3}$$

The shares of primary inputs in output can be defined as

$$v_k = \frac{P_k K}{Q_y Y}, \quad v_l = \frac{P_l L}{Q_y Y}, \tag{4}$$

[1]See Solow (1957), Denison (1962), Jorgenson, Gallop, and Fraumeni (1987), and, more recently, Young (1995), among numerous others.

[2]See Christensen, Jorgenson, and Lau (1971 and 1973).

III. Sources of Economic Growth in China

Aggregate Productivity Growth

As shown in Table 1, China's real national income (the derived net output measure) grew by 7.2 percent a year on average over the four decades to 1994. At the same time, there was extraordinary input growth. With investment averaging 27 percent of national income, China's real capital stock expanded by 6.8 percent a year for the period (Table 2). Surprisingly, the capital-output ratio remained roughly constant at about 2.6. The absence of pronounced "capital deepening" in the Chinese economy suggests that capital accumulation is only a part of the story behind China's economic growth.

Output growth in China for 1953–94 and the various subperiods was decomposed along the lines indicated by equation (9) in Section I. From this decomposition, it is possible to obtain estimates of the rate of growth in TFP, that is, the growth of output with respect to time, holding capital and labor inputs constant. The results are shown in Table 4.

Table 4. *Aggregate Productivity Growth in Selected Periods*
(Average annual percent change)

	1953–94	1953–78	1979–94
Output	7.2	5.8	9.3
Capital stock	6.8	6.2	7.7
Employment	2.6	2.5	2.7
Total factor productivity (TFP)	2.1	1.1	3.9

Sources: State Statistical Bureau, People's Republic of China, and various ministries; and authors' estimates.

As can be seen from Table 4, capital grew for the 1953–94 period as a whole at 6.8 percent, and labor grew at 2.6 percent. By comparison, TFP growth was 2.1 percent. However, productivity performance improved dramatically during the reform period. While the average TFP growth rate amounted to about 1.1 percent during 1953–78, it rose sharply to 3.9 percent during 1979–94 when China was implementing market-oriented economic reforms.[12] It is interesting to note that Chow (1993) finds no technological progress prior to 1978 in the Chinese economy. The results presented here

[12] For a more-detailed description of the Chinese economic reforms, see Bell, Khor, and Kochhar (1993) and Perkins (1988 and 1989).

indicate that, although productivity performance differed sharply before and after 1978, it was positive in the prereform era. The opening up to foreign trade and investment, the gradual price decontrol, the rise of rural township and village enterprises (TVEs), and the expansion of new private businesses brought competitive forces into the Chinese economy and helped make the economy more efficient during the reform period.

Sources of Economic Growth

Table 5 shows the relative contributions of capital, labor, and productivity to aggregate output growth in 1953–94 and various subperiods. The percentage contributions of capital and labor are obtained by weighting the corresponding growth rates by their respective income shares. For the period 1953–94 as a whole, capital is clearly the most important source of growth in China. During the central planning period 1953–78, capital input alone accounted for 65 percent of the output growth. The relative importance of capital has diminished over time, however. For the reform period 1979–94, capital contributed less than half of the output growth; for the last five years of the sample period, capital accounted for only about 30 percent of the output growth. Labor is the least important source of growth. For the period 1953–94 as a whole, labor accounted for 15 percent of the output growth. Labor was responsible for 17 percent of the growth for the central planning period 1953–78, but its contribution dropped to less than 13 percent during the reform period.

While the Chinese economy experienced low productivity growth in the central planning era, productivity growth has clearly become a significant

Table 5. *Sources of Economic Growth*
(In percent)

Variables	1953–94	1953–78	1979–94
Output growth	7.2	5.8	9.3
Capital input growth	6.8	6.2	7.7
Labor input growth	2.6	2.5	2.7
Total factor productivity (TFP)	2.1	1.1	3.9
Contribution of capital[a]	55.6	65.2	45.6
Contribution of labor[a]	14.9	16.8	12.8
Contribution of productivity growth[b]	29.5	18.0	41.6

Sources: State Statistical Bureau, People's Republic of China, and various ministries; and authors' estimates.

[a] Ratio of input growth, weighted by the corresponding factor income share, to output growth.

[b] Ratio of TFP growth to output growth.

source of economic growth since the beginning of economic reforms. Productivity growth contributed 42 percent of the output growth in the reform period 1979–94, rivaling the percentage contribution of capital.

In sum, China's rate of output growth increased by more than 3 percentage points in the reform period compared with the central planning period. Although growth rates in both capital and labor inputs rose significantly in 1979–94, the productivity growth differential appears to explain the bulk of the difference in output growth between prereform and reform periods.

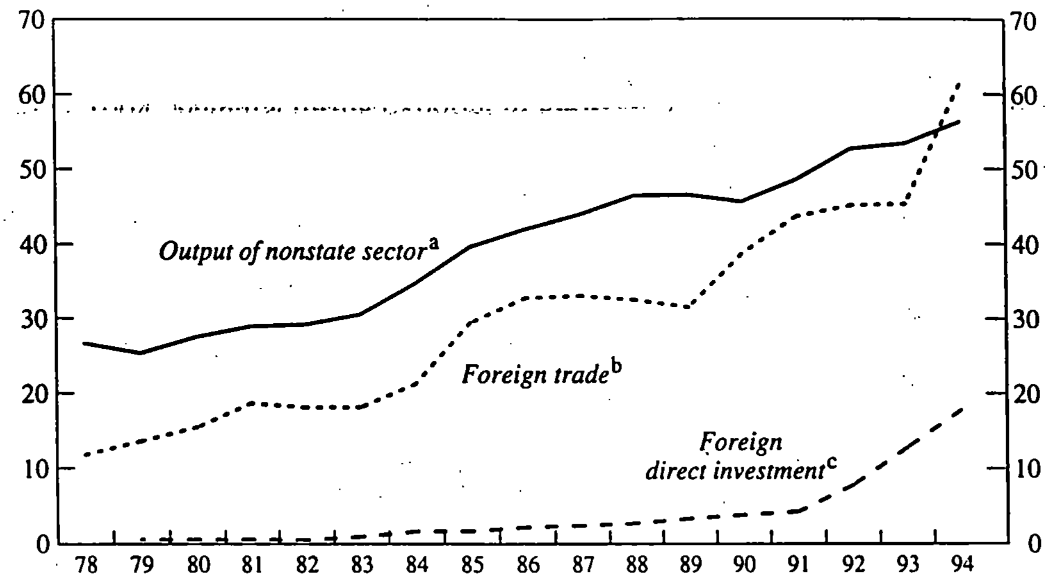
Causes of Productivity Growth

A variety of market-oriented reforms and increased integration into the global economy are the most likely explanations for the rapid productivity growth observed in China in recent years. Specifically, several factors are directly related to productivity growth in the reform period.

First, there has been a significant reallocation of labor from agriculture to the industry and services sectors. Agricultural employment as a share of labor force fell from more than 70 percent in 1978 to 54 percent by 1994. The process of labor reallocation into activities with higher value added, such as manufacturing, has been an important source of aggregate productivity growth for the economy as a whole, as noted by Woo (1995), Borensztein and Ostry (1996), and Sachs and Woo (1997), all of whom attribute a large part of aggregate TFP growth to the effects of labor reallocation.

Second, as can be seen from Figure 3, output of the nonstate sector—broadly defined to include the urban collective sector, rural industry, agriculture, and private and foreign businesses—has risen dramatically over the past one-and-a-half decades. Even if agriculture, which had already been liberalized from the collective commune system by the early 1980s, is excluded, the share of the nonstate sector in China's nonagricultural economy, which was once dominated by the state sector, rose from 25 percent of output in the late 1970s to 56 percent by 1994. A growing literature has explored the nature and operations of China's nonstate enterprises, especially the rural TVEs. Several features that distinguish TVEs from SOEs are important in explaining why nonstate businesses may outperform SOEs. First, TVEs have strong profit incentives and sharply focus on their financial bottom lines, whereas SOEs often have a variety of nonfinancial objectives, including the provision of social services (Byrd and Gelb, 1990; and Hu 1994). Second, unlike their counterparts in the state sector, TVEs face hard budget constraints, with high bankruptcy rates, while loss-making SOEs can obtain budgetary and credit subsidies (Qian and Xu, 1993). Third, TVEs enjoy more operational autonomy and, in particular, are relatively free of interference from the central and local bureaucracy in their

Figure 3. *Foreign Direct Investment*
(In percent)



Sources: Chinese authorities and authors' estimates.
[a]The share of the nonstate sector output in total nonagricultural output.
[b]The share of the total foreign trade in national income.
[c]The share of foreign direct investment in total fixed investment.

labor hiring and firing and wage-setting practices, allowing for far greater labor market flexibility (Hu, 1994). The rapid growth in the rural TVEs played an especially important role by drawing tens of millions of workers from agriculture into the higher-value-added manufacturing industry. The expansion of the nonstate sector relative to the state sector clearly helped raise overall production efficiency in the Chinese economy. Jefferson and Rawski (1994) provide estimates for sectoral productivity growth in Chinese industry, classified by ownership. They find that productivity in China's nonstate sector grew more than twice as fast as in the state sector between 1980 and 1992. During the subperiod 1984–88, for example, productivity grew by 3.0 percent in the state sector, 5.9 percent in the urban collective sector, and 6.6 percent in the township and village sector. The sectoral evidence underscores the role of the nonstate sector in the surge of China's aggregate productivity in the reform period.

Third, China's open-door policy and "special economic zones" helped attract massive foreign direct investment. Foreign direct investment into China was negligible prior to 1979. By 1994, however, cumulative foreign direct investment had reached US$95.6 billion. Annual inflows increased from about 0.5 percent of total fixed investment in 1979 to 18 percent in 1994. Significant spillover in technology and managerial know-how was likely through the numerous joint ventures and wholly owned foreign enterprises that have sprung up along China's coastal provinces in the last decade.

Finally, China emerged as an export powerhouse over the last decade. Total exports as a share of national income rose from less than 6 percent in 1978 to over 30 percent in 1994. Manufacturing exports, in particular, were expanding in U.S. dollar terms at a rate of 19 percent a year in the 1981–94 period. The ratio of trade to national output increased from a little over 10 percent in 1978 to over 60 percent by 1994. The evidence from a large number of cross-country studies suggests that export growth has a strong positive correlation with productivity growth in domestic industries. The competition in world markets apparently exerted strong pressure on Chinese industry to adopt the best manufacturing practices and improve efficiency.

International Comparisons

A recent study by Young (1995) documenting the East Asian growth experience has stirred a heated debate. Noting Young's findings that East Asian economies had rather unspectacular TFP growth rates, Krugman (1994) dismisses the East Asian economic miracle as a myth and goes so far as to put Singapore and the former Soviet Union in the same category of economic inefficiency! As it is widely suggested that China is well on its way, following the examples of its East Asian neighbors, to achieving an economic miracle of a far bigger proportion (for example, Perkins, 1989), it is interesting to compare China's growth experience with those of other countries.

Table 6 tabulates estimates from previous studies for the Group of Seven industrialized countries (Dougherty, 1991), several Latin American developing countries (Elias, 1992), and four newly industrialized East Asian economies (Young, 1995). While China's TFP growth in the prereform period was lackluster in comparison with productivity in other economies, its TFP growth rate in the postreform years was notably higher than those experienced by other countries in the periods shown in the table. China's high TFP growth indicates that it is rapidly catching up with international productivity levels, particularly those in the advanced industrialized countries.

IV. Further Explorations and Sensitivity Analysis

Although extremely useful, growth accounting is nevertheless a very delicate exercise. The question is whether the results reported in this paper constitute firm evidence that the Chinese economy has truly moved since

Table 6. *Productivity Performance in China and Selected Countries*
(Average annual percent change)

Country	Period	Total factor productivity (TFP) growth
G-7 industrial countries[a]		
Canada	1960–89	0.5
France	1960–89	1.5
Germany	1960–89	1.6
Italy	1960–89	2.0
Japan	1960–89	2.0
United Kingdom	1960–89	1.3
United States	1960–89	0.4
Latin America[b]		
Brazil	1950–85	1.6
Chile	1940–85	0.8
Mexico	1940–85	1.2
Venezuela (manufacturing)	1950–70	2.6
East Asia[c]		
Hong Kong	1966–91	2.3
Indonesia	1979–96	0.9
Malaysia	1979–96	2.0
Singapore	1966–90	0.2
	1979–96	2.5
Korea[d]	1966–90	1.7
Taiwan Province of China[d]	1966–90	2.1
China	1953–94	2.1
	1953–78	1.1
	1979–94	3.9

Sources: Authors' estimates and references cited in the footnotes.
[a] See Dougherty (1991).
[b] See Elias (1992).
[c] The estimates of TFP growth for earlier periods (1966–91) are from Young (1995) for Hong Kong, Singapore, Korea, and Taiwan Province of China; estimates for more recent period (1979–96) are taken from Sarel (1996).
[d] Excluding agriculture.

the reforms onto a sustainable long-term path of high productivity growth. To check the robustness of the findings, the analysis was redone using alternative data and methodologies suggested by other studies.

Impact of Political Disruptions

Comparisons of China's efficiency and growth performance in the central planning and economic reform periods may be affected by the major political disruptions that occurred before the country's opening up to the outside world in 1979. During the central planning period 1952–78, China experienced periodic political upheavals, highlighted by the 1966–69 Cultural Revolution. It is well-known that in those politically chaotic years China subordinated the national priorities of economic development to political objectives, and that the ideological struggles greatly disrupted economic activity. As noted by a number of studies, including Chow (1993) and Borensztein and Ostry (1996), it is important to separate out the influence of political disruptions on China's growth performance. Borensztein and Ostry (1996) find that, once the political turbulence of prereform China is taken into consideration, the difference in the growth rates of GDP per worker between the prereform and postreform periods becomes less dramatic. Their results point to the possibility that, excluding political influences, the true improvement in China's productivity growth in the reform period may be smaller than suggested by the unadjusted official data.

We also find that failure to take out the impact of political disruptions would lead to underestimation of output growth in prereform China. When the politically disruptive years from 1958 to 1970 were excluded, the growth rate in output per employee was 4.5 percent in the prereform period, rather than 3.8 percent, as estimated from the unadjusted data (Table 7). Nevertheless, the TFP growth rate in the prereform period, excluding the politically disruptive years, amounted to 1.6 percent, only marginally higher than the TFP growth for the entire prereform period, mainly because higher output growth in the politically stable years was also accompanied by higher investment growth. It thus seems that political events alone cannot completely explain the lower productive efficiency in China's central planning period. Even after excluding the politically most disruptive years from 1958 to 1970, the difference in estimated TFP growth rates between the central planning and reform periods remains substantial.

Table 7. *Impact of Political Disruptions on Efficiency and Growth* (Average annual percent change)

	1953–78	1953–78[a]
Output	5.8	6.6
Output per capita	4.5	4.7
Output per employee	3.8	4.5
Real capital stock	6.2	6.5
Employment	2.5	2.2
Total factor productivity (TFP)	1.1	1.6

Sources: State Statistical Bureau, People's Republic of China, and various ministries; and authors' estimates.

[a] Excluding the politically disruptive years from 1958 to 1970.

Table 8. *Efficiency and Growth in the Nonagricultural Economy*
(Average annual percent change)

	1953–94	1953–78[a]	1979–94
Output	8.5	9.3	10.0
Capital input	10.1	12.1	9.3
Labor input	5.0	6.5	5.4
Total factor productivity (TFP)	0.9	–0.8	3.1

Sources: State Statistical Bureau, People's Republic of China, and various ministries; and authors' estimates.
[a] Excluding the politically disruptive years from 1958 to 1970.

Efficiency of China's Nonagricultural Economy

In the 1952–78 period, Chinese central planners favored the urban industrial sector over agriculture, allocating the predominant share of national savings as capital investment to industry while forcing the rural population to stay in agriculture by strictly controlling migration to the cities. In the reform period 1979–94, Chinese industry continued to receive a dominant share of capital, but the government also adopted a more flexible labor market policy that permitted rural surplus labor to move out of agriculture into rural industry or the urban services sector. At the same time, agriculture shrank from 40 percent of the national income in the early 1980s to about 25 percent by 1994.[13]

With the continuing reduction in the shares of agricultural output and agricultural labor force, and with more capital and labor resources drawn into the nonagricultural economy than ever before, an important question arises: How have such sectoral shifts in output and reallocation of labor affected the efficiency of China's nonagricultural economy?

As can be seen from Table 4 and Table 8, growth in nonagricultural output outpaced output growth for the economy as a whole, but growth in inputs for the nonagricultural economy was considerably higher than growth in inputs for the aggregate economy. The capital stock expanded by 10 percent a year for the nonagricultural economy, compared with 6.8 percent for the aggregate economy, while growth in labor inputs averaged 5 percent in China's nonagricultural economy, as opposed to 2.6 percent for the economy as a whole. Excluding agriculture, TFP growth turned out to be negative (minus

[13] In the 1950s, the Chinese economy was predominantly agricultural: the share of agricultural output in national income was 58 percent in 1952. Indeed, if the forced concentration of population in the rural areas is not taken into account, one could argue that China's official development policies favoring industrialization over agriculture through much of the period were largely successful.

0.8 percent) in 1953–78 and 3.1 percent in 1979–94.[14] While TFP growth for the nonagricultural economy was a little lower than the 3.9 percent for the overall economy (including agriculture) in the 1979–94 period, the contrast in productivity performances of the nonagricultural economy between the central planning era and the reform period is remarkable.

Can China's TFP Growth Be Sustained?

Looking at the reform period alone, the question arises, How sustainable is China's productivity growth?[15] If the dramatic productivity improvement in the 1979–94 period mainly reflected the onetime gains induced by the earlier reforms, such as the dismantling of collective agriculture (including the people's communes) and the restoration of family farming in the rural areas, one might have observed a subsequent slowdown in aggregate productivity growth as the potential for efficiency gains was exhausted over time. In the first six years until 1984, Chinese reforms were concentrated in the rural sector and were largely successful. As shown by McMillan, Whalley, and Zhu (1989) and by Khan and Khan (1995), productivity growth in Chinese agriculture during this period was impressive, partly owing to increases in agricultural prices and—more important—to positive incentives to farmers induced by institutional changes. These changes included the introduction of the household responsibility system and the increased labor market flexibility that permitted rural surplus labor to move into industrial and urban tertiary sectors. As shown in Table 9, the estimated TFP growth for the aggregate economy over the initial period of reforms (1979–84) was 2.5 percent, a full percentage point higher than in the prereform period.

Beginning in 1984, China shifted its reform priorities to the urban, state-owned industrial sector. These reforms proved far more complex and challenging than the earlier rural reforms (Perkins, 1988; and Bell, Khor, and Kochhar, 1993). It was possible that the continued problems with the state industry would limit the scope for sustained further productivity gains in the Chinese economy. Nevertheless, mainly because of increased autonomy and strengthened working incentives associated with a number of reform measures, even the Chinese SOEs registered higher productivity growth (Groves and others, 1994). Indeed, as shown in Table 9, TFP for the aggregate economy grew by 2.7 percent between 1985 and 1989. In the last

[14] Focusing on the nonagricultural economy is likely to produce more accurate TFP estimates because land is not included as a separate productive factor for the aggregate economy.

[15] The sustainability of productivity growth in China has recently been questioned by Woo (1995).

Table 9. *Productivity Growth in the Reform Period*
(Average annual percent change)

	Rural reform 1979–84	Extension of reform to urban, state-owned sector 1985–89	Accelerated reform 1990–94
Output	8.0	8.8	11.5
Capital input	7.1	8.6	7.5
Labor input	3.0	2.8	2.1
Total factor productivity (TFP)	2.5	2.7	5.8

Sources: State Statistical Bureau, People's Republic of China, and various ministries; and authors' estimates.

several years of the sample period (1990–94), TFP growth reached an astonishing 5.8 percent, and productivity changes for the first time overtook capital as the predominant source of China's economic growth. Instead of slowing down (as one might have expected), productivity growth reached stunning new highs as China moved forward on the reform path, albeit at an uneven pace.

Therefore, the evidence from this study points to a somewhat different conclusion from that reached by Sachs and Woo (1997). Even though the efficiency gains brought about by earlier agricultural reforms may have dissipated, the sharp growth in rural industry, the surge in foreign direct investment, the export boom, the further dismantling of the central planning system, and the increasing market orientation in the state-owned sector have combined to boost aggregate productivity growth in the 1985–94 period, and even more so during 1990–94.

Adjusting Capital Stock Growth

During the central planning period, much of the fixed investment was allocated to new machinery and equipment to increase the country's industrial capacity, while infrastructure and residential investment was neglected. In the reform period, outlays in new housing by state and nonstate entities increased sharply, taking a larger share of gross fixed investment. Since the Chinese NI series excludes the imputed value of residential housing services, a corresponding adjustment for the capital stock was made by deducting residential investment from gross fixed investment. As can be seen from Table 10, such an adjustment has no impact on the TFP growth estimates for the central planning period 1953–78 but raises the estimated TFP growth for the 1979–94 reform period to 4.4 percent from 3.9 percent.

Table 10. *Sensitivity Analysis of Total Factor Productivity (TFP) Growth Estimates*
(Average annual percent change)

	Central planning period 1953–78	Economic reform period 1979–94
Alternative TFP growth estimates		
Li and others (1993)[a]	–0.8	2.5
Borensztein and Ostry (1996)	–0.7	3.8
Sachs and Woo (1997)[b]	—	1.7
Alternative measures of capital input[c]		
Excluding residential investment	1.1	4.4
Reducing initial capital stock[d]	–0.9	3.7
Assumed values of labor shares[e]		
$\alpha = 0.3$	0.7	3.2
$\alpha = 0.5$	1.1	3.7
$\alpha = 0.6$	1.8	4.6

Sources: Li and others (1993), Borensztein and Ostry (1996), and Sachs and Woo (1997); and authors' estimates.

[a] The economic reform period covered is 1979–90.

[b] The economic reform period covered is 1978–93. Sachs and Woo (1997) also report TFP growth estimates of 3.3 percent and 0.8 percent for subperiods 1978–84 and 1985–93, respectively.

[c] Using authors' own estimates of output growth, input growth, and factor shares.

[d] Setting initial capital stock at Y58.9 billion in 1952, which reduces the initial capital-output ratio from 2.5 to 1 in 1952.

[e] Using authors' own estimates of output and input growth.

TFP growth estimates can also be sensitive to the initial values of capital stock. To assess this possibility, the value of initial capital stock was set at Y58.9 billion (1952 prices),[16] which reduces the starting capital-output ratio from 2.5 (derived from Chow's (1993) estimate) to 1. This adjustment increased real capital stock growth rates, particularly in the earlier central planning period. As a result, estimated TFP growth turned negative (minus 0.9 percent) for 1953–78, but it was only slightly lower for the reform period 1979–94 (3.7 percent) than when Chow's (1993) estimate of the initial capital stock was used.

Measurement Errors in Output and Input Data

The potential measurement errors in the official Chinese data warrant considerable caution in interpreting the results presented in this paper and elsewhere. Woo (1995) and Sachs and Woo (1997) assert that the Chinese

[16] Recall that Chow (1993) uses a value of Y175 billion (at 1952 prices).

official output data overstated output growth by as much as 0.5–1.0 percentage points in the postreform period. If correct, their output adjustment would reduce the TFP growth estimates in this paper by 0.5–1.0 percentage points, holding inputs and factor shares at the same levels.

According to these recent studies, the errors in the official output data stem mainly from two sources: overreporting of nominal industrial output and underdeflating of nominal industrial output by Chinese collective enterprises, especially TVEs. It is puzzling that China's nonstate enterprises should in the reform period overreport their nominal output to the authorities. These enterprises have strong profit incentives and would like to avoid taxes if possible. One possibility is that overzealous local officials overstated the total output in their jurisdictions to justify their job performances to their superiors. However, such bureaucratic incentives are presumably far weaker in the postreform era of decentralization and increased local autonomy than they were in the central planning period. In fact, plenty of evidence suggests that China's informal sector expanded substantially since the economic reforms, which had a growth effect as well as a level effect on output. As such, it is doubtful that correcting a bias resulting from the overstating of output could reduce the sharp differences in China's output growth before and after reforms.

The underdeflating of nominal output could be a more important source of bias. Recent work by Woo (1995), Borensztein and Ostry (1996), and Sachs and Woo (1997) attributes much of the upward bias in official output growth estimates to the improper deflating of industrial output, especially in the collective sector. However, they fail to make the symmetric adjustment to the official investment series, which could be similarly underdeflated as industrial prices determine to a large degree investment goods prices. Thus the net impact of the Sachs-Woo adjustment on the true TFP growth estimates is not clear. One should also bear in mind that official output statistics in the central planning period are not free of the "improper deflating" problem. Selecting an appropriate deflator for that period is a delicate matter because of the severe repressed inflation. The chronic shortages, queues, and excess demand for capital investment indicate that, in the absence of price control, open inflation would have been much higher. Thus, while underdeflating the output series poses a serious problem for the estimated values of TFP growth, it does not change the basic conclusion that efficiency has improved substantially in the reform period.

Essentially, the biggest problem with the official statistics lies with the capital stock data. As noted in the discussion of data construction in Section II, the official asset surveys do not produce stock estimates consistent with the investment flow data from the national accounts. The differences between the official estimate of the capital stock and the estimate obtained by applying the perpetual inventory method to the disaggregated investment flow data, with proper deflating, are substantial. Woo (1995), Borensztein and Ostry (1996), and Sachs and Woo (1997) all use a series of capital stock estimated earlier by Li and others (1993). As discussed in great detail in Hu (1996), this capital stock series, although representing a significant improvement over the official series, seriously overestimates China's real capital stock growth in certain time periods.

Table 10 shows how TFP growth estimates vary if different measures of output, capital input, and factor shares are used. Li and others (1993) estimate TFP growth rates to be minus 0.8 percent for 1953–78, and 2.5 percent for 1979–90. Woo (1995) and Sachs and Woo (1997) estimate TFP for China's aggregate economy to be 1.7 percent for 1978–93.[17] Borensztein and Ostry (1996) estimate TFP growth to be 3.8 percent for the reform period 1979–94. These estimates do not differ substantially from the TFP growth estimate of 3.9 percent for 1979–94 reported in this paper, considering their use of alternative output and input data. Li and others' (1993) results imply a net increase of 3.3 percentage points in TFP growth, for instance, as compared to the 2.8 percentage point increase from the central planning to the reform period estimated here. Using alternative values for factor shares, as for example done by Borensztein and Ostry (1996), also does not change the results significantly (Table 10). In particular, the differential in TFP growth between the prereform and reform periods remains large, irrespective of the value chosen or the labor share (α). By and large, the available evidence from these studies confirms that productivity improvements are a significant source of economic growth in China during the reform period, and the basic conclusion remains unchanged when alternative measures of capital input and values of labor income share are used.

V. Conclusions

The central finding of this paper is that, although capital accumulation was a dominant factor in China's economic growth, productivity improvements have assumed an increasingly important role. Because of China's high savings rates and abundance of labor, the significance of factor inputs in China's economic growth is well understood; however, it is interesting to find that China has continued to achieve an impressive record of productivity growth in recent years.

The evidence is clear that China has reaped considerable gains from its market-oriented economic reforms in the past two decades. The TFP growth rate in the Chinese economy was fairly low for the period 1953–78 because

[17] Their TFP growth estimates are 3.3 percent and 0.8 percent for subperiods 1978–84 and 1984–93, respectively.

the system of central planning stifled economic incentives, prevented competition, and distorted resource allocation. By contrast, China achieved spectacular productivity growth in the reform period, with the increase in TFP approaching 4 percent a year. Productivity growth contributed more than 40 percent of China's aggregate economic growth during the reform period and rapidly replaced capital input as the predominant source of economic growth in China. In the absence of an identified surge in research and development efforts, the observed productivity gains can be mainly attributed to improved allocative efficiency under market-oriented reforms, such as the emergence of family farming and the rise of rural industry, as well as to China's decade-long open-door policy, which brought about an expansion in foreign trade and foreign direct investment. While at this stage it is not possible to pinpoint the exact sources of productivity growth in China, there are good theoretical and empirical reasons to believe that the reform process that was initiated in 1978 has had, and apparently continues to have, an important effect on the rapid productivity growth observed over the past decade.

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China's Economy to 2010: Views of Leadership on Prospects and Problems of Fifteen Year Plan

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SUMMARY

Economic growth and transition to an efficient market system in the global economy is a centerpiece of Chinese policy. High, if not first priority is given to improvement in the rural agricultural economy assuring supply of basic products to all citizens and raising the living standards by improved quality and availability of products to consumers. Massive underemployment, i.e., 120 million redundant rural work force, and limits of credit, shrinking arable land and undeveloped ability to absorb and convert to productive use advanced technology are both daunting problems and factors of potential growth.

From China's perspective large scale loss making industrial enterprises must be made profitable and competitive but within the context of assuring the adequacy of social safety nets (pensions, health, education) and employment opportunities. Improved production through the market creative destruction has to be weighed against social unrest and inequity of benefits.

Integration into the global economy and domestic economic production and growth are closely tied. The benefits of market access, advanced country technology and financial support from the global system are clear but the necessity to open the domestic enterprises to competition is not, and the inclination to control and limit foreign enterprises integrating with the Chinese economy is apparent.

Finally, the need to reduce economic risks, increase predictability and reduce crime and corruption that hobble healthy growth are evident to Chinese interlocutors. The utility of a Chinese form of economic and commercial law of the market place including an independent central bank and efficient commercial banking system, a federative, fair and equitable tax code and system, mechanisms to restrict monopolies and assure free entry are less clear. In short, the use of advanced technology of the Western industrial economies and the efficiency of the market are more clear than the self interest of China in

adhering to the rules of the game in the international market and the institutionalization of a fair and robust Chinese market.

China may triple its total and per capita Gross Domestic Product (GDP) by the Year 2010 as projected but only if the proper choices and tradeoffs are made in coping with the above priority problems. Such changes, if made, would also contribute to China's becoming a pluralistic market system under a rule of law

BACKGROUND

Discussions with the author on the future of China's economic prospects and problems were held in Beijing during May 20-24, 1996, and were organized to include Chinese professional economists who are advisors to top leaders, and culminated in a meeting with Vice-Premier Jiang Chunyun.[1] The objectives of the 15-Year Program in the context of the current Ninth Five-Year Plan are to continue the transition toward an efficient market economy, accompanied by high rates of growth, with increased integration into the global market.[2] The agenda for each of the meetings was set by the author, reports from earlier meetings were sent forward to the final meeting with the Vice Premier; the agenda was repeated with specialists on China in the Japanese government; similar discussions were held with Chinese specialists in the Ministry of Foreign Affairs, Japanese External Trade Organization (JETRO) and Ministry of International Trade and Industry (MITI) in the week of May 27-31 in Tokyo.

The four areas of prospects and problems discussed were: (1) agricultural and rural economic development, (2) industrial growth and competitiveness, (3) interdependence of the emerging market economy with the global market, and (4) market-friendly institutions to include adoption of rule-of-law in economic relations. The four areas of priority were accepted by the Chinese in each case as a basis for discussion.

FUTURE OBJECTIVES FOR CHINA'S ECONOMY IN THE YEAR 2010

The progress in establishing a rudimentary market system in the two decades of modernization (1978-1996) is being followed by a second stage of development, that of an emerging market economy with a substantial improvement in living conditions, quality of life, competitiveness in the global

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[1] A full list of interlocutors and description of the exchange is available as a Memorandum of Dialogue on Chinese Fifteen Year Plan to 2010 to China Watchers. The dialogue was designed to provide background for the Joint Economic Committee study, *China's Economic Future: Challenges for U.S. Policy*, expected to be released in the summer of 1996. The pattern of the exchanges was similar to that by the same author in May 1992 that culminated with a meeting with Vice-Premier Zou Jiahua. CRS Report 92-6006, *China's Transition to the Market*, July 30, 1992. 6 p.

[2] Li Peng, Premier of State Council, *Report on the Outline of the Ninth Five-Year Plan for National Economic and Social Development and Long Range Objectives to the Year 2010*. Cf. Virendra Singh and Narendra Singh, *China: Economic Prospects to 2010*. Wharton Economic Forecasting Group in forthcoming JEC volume, op.cit.

economy and stability at home and abroad. This is part of a longer-term process of development that may put China on a course toward joining the Western industrialized countries as a major force in the global trading, financial and monetary markets, and international institutions potentially enroute to becoming an economic superpower.

The multiple implied objectives for China's future are to maximize output, provide full employment for their urban and rural labor force, maintain price stability, and attain a share of the global market appropriate to their increasing economic capabilities. These objectives are both synergistic and competitive. They are also similar to objectives and trade-offs in Western market economies as indicated by the Employment Act of 1946 in the United States. The opportunities and constraints of China's future economic performance present somewhat similar dilemmas for their economic policymakers as those faced in the advanced industrialized economies.

The following commentary deals with the opportunities for the projected future economic development and some problems or constraints on attaining these new levels of performance:

I. Agricultural and Rural Economic Development. Increased yields in grain crops and delivery systems will be needed to stabilize food availability throughout China. Improved living standards will come from expanded quality food outputs in meats, fruits, vegetables and processed food. Limited arable land area will be further constrained by non-productive land use, albeit countered by some expansion in cultivated land through irrigation. Productivity increases from the intensity of land use will feature the application of modern mechanical and chemical inputs, better seeds and veterinary medicine. Weak rural infrastructure in roads, storage and processing will restrict the increased value of output. Continued subsidized basic crops will deter productivity and require transfer payments from richer to poorer urban and rural provinces. Expanded use of leases and cooperative land tenure may facilitate the expanded production on the limited arable land. Local initiatives and broad-scale educational efforts will be required to effectively bring appropriate technology to the productive rural sectors. Bilateral Japanese assistance focusses on bottlenecks such as the water supply through irrigation. The 120 million workers in the rural economy considered redundant by Chinese estimates must be employed in productive activities to ensure projected growth. Rural industrial development has been a key employment generator in the past but a much broader approach to infrastructure, environmental quality, and local industrial development is probably needed but not sufficiently projected for expected performance.

II. Industrial Growth and Competitiveness. Growth and competitiveness in the past have been in small- and medium-sized industrial and service sectors. Reportedly some 14,000 large-scale state enterprises are unprofitable, non-competitive, and place a heavy subsidy burden on the state budget. Some 20%-30% of the staff of the State-Owned Enterprises (SOE) are redundant workers that would need employment if these enterprises were restructured, especially through bankruptcy. The social safety net responsibility involving health, education, employee training, retirement programs and pensions would all have to be shifted to localities, other government facilities or funded in some other fashion such as private funding. Future political stability is endangered by the expectations of problems from restructuring the large SOEs.

Progress in restructuring SOEs has been very limited. Some 80 enterprises were said to be identified for bankruptcy in 1995, but none were restructured according to a Japanese report. Several enterprises were restructured as joint ventures and sold to overseas Chinese investors but have not proven to be useful models. In a study released at the time of these discussions, the World Bank was pushing China for rapid action, but social problems have yet to be addressed or resolved by the Chinese.[8] Indeed, a number of programs have been withdrawn because they resulted in demonstrations in some cases, even strikes, in the localities of projected SOE restructuring, based on Japanese sources.

III. Interaction of the Emerging Market Economy with the Global Market. If growth in rural agriculture and urban industry is to be successful, openness to the global economy will be important: imports of technology, management culture and financial support from both foreign direct and portfolio investment will be important to increase the profitability and access to foreign markets, especially access to the American, Japanese and European markets. The importance of ensuring access to major markets such as that of the United States to Chinese growth did not seem to be clear to the Chinese in discussing their country's future performance to the year 2010.

Foreign openness requires the acceptance of reciprocal market rules by China in trade, technology transfer, intellectual property and financial institutions within the Chinese economy. A continued special relationship between the market economies in Asia that have large indigenous Chinese population will be especially relevant for increasing interaction. The maintenance of productive interdependence during a process of accession of Hong Kong and continual productive engagement with Taiwan would continue to be positive contributors to growth, while controversy and confrontation would be counterproductive to effective integration into the broader market economies. This point when made was not responded to by the Chinese. A Japanese view drew attention to the dilemma in China policy over the issue of sovereignty and the maintenance of the one-China policy on the one hand, and the relationship between interdependence and openness to the global market on the other. This dilemma between international security and economic integration policies helped explain the ambivalence in Chinese policy during the recent Taiwan Straits crisis.

IV. Market Friendly Institutions with of Rule-of-Law in Economic Relations. Basic market institutions that provide a legal and regulatory framework include: a modern tax code and revenue system; an independent

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[8] *The Chinese Economy; Fighting Inflation, Deepening Reforms*. World Bank, May, 1996.

central bank with supervisory authority over efficient private commercial banks, a civil code establishing property rights and judicial procedures for establishing rights and obligations of contracts; and a commercial code providing for effective operation in the global market economies. Participation in global economic institutions, especially the Bretton Woods institutions (IMF, World Bank, World Trade Organization (WTO), are essential for China and require progress in adherence to the rule-of-law in its economic relations with other countries. These points were also raised in the context of inequality and lack of equity in China as between regions and among citizens. The international institutional integration discussion was in the framework of ensuring fair and equitable commerce. Neither of the two links seemed clear to the Chinese interlocutors.

Certain institutional developments at home and abroad would markedly improve the fairness and competitiveness of China's system through anti-monopoly action; revenue sharing for equity; legislative and judicial actions to reduce crime and corruption; and fairness to reduce disparity of economic benefits between city and countryside, coastal and interior regions, entrepreneurs and workers, etc. Addressing the problem of social unrest, which may derive from a sense of unfairness, or achievement of a social consensus that economic performance validates the legitimacy of the regime, seem important and are recognized by the Chinese. Many suggest that Chinese or Asian culture dictates a process of family or group interaction that appears to be corrupt by American standards. Whatever the ultimate differences in culture, it appears that Chinese do not feel their current transitional system of benefits and cost distribution is fair or equitable. Chinese officials agree the Gini income distribution index for China shows too much inequality.

Strengthening and rationalization of the emerging market system involving sharing of power between the executive and the parliament in Beijing and the center and the localities would politically be supplemented by the federative nature of a more efficient and equitable revenue system. In this developing separation of powers it may be increasingly relevant for the U.S. Congress to deal directly with their Chinese parliamentary counterpart as well as the Chinese executive branch. Indeed, several Chinese suggested more parliamentary exchanges.

CONCLUSIONS AND OBSERVATIONS

In their preparation of the future plans, the Chinese leadership is giving priority to appropriate sectors and problems in projecting future performance in agriculture and industry. This leadership is concerned about integration into the global economy but give less emphasis to the trade-offs and dilemmas they appear to face. Their concerns regarding political stability, crime and corruption are ever-present in discussions, yet the relationship of these problems to development of market-friendly and pluralistic institutions under a rule-of-law is less evident.

The reciprocal nature of interdependence was least clear with the Chinese interlocutors. That openness in commerce and participation as well as membership in the global economic system and institutions have both privileges and benefits, responsibilities and obligations did not appear to be clear. Further dialogue with the Chinese and demonstrations of the two-way street nature of economic interdependence and integration seems in order.

Although the format of the discussion was similar in 1996 to my 1992 discussion several differences were noteworthy:

(1) The professional economists directly involved in preparing assessments for the top leadership were more knowledgeable in Western economic theory and analysis than four years earlier (two had Western Ph.D's in economics).

(2) The knowledgeable, mainly young, Chinese economists were extremely interested in an indepth dialogue. The 5-hour seminar in the first day was taped in full; one economist was tasked to prepare a memo for the Vice-Premier; most of the dialogue before and after lunch was an exchange generated by their questions.

(3) More interest than in 1992 but little detailed knowledge, was evident on the experience of other economies in transition, e.g., Central and East Europe. A considerable part of the first day seminar was on comparative developments.[4]

The degree of economic-professionalism required and utilized in preparing leadership assessments has been markedly improved. The access of young market-oriented economists to top leadership deliberations was substantially more than in 1992. The interchange at all levels were cordial, reciprocal, and informative.

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[4] In the discussions with the Chinese, many references were made by the author of this report to material on the then-forthcoming World Bank document, *World Development Report 1996*, released June 27, 1996.

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Intellectual Property Protection in China

Information Office State Council
Of the People's Republic of China
June 1994, Beijing

Contents

Foreword

Chinese civilization has a long history. The Chinese nation has a vast reservoir of creativity. The brilliant culture created by the Chinese people has exerted a deepgoing influence on the progress of human civilization. Over the past several thousand years, vast numbers of outstanding Chinese scientists, inventors, writers and artists have given the glorious fruits of their mental labour to the development of humanity's common civilization, making enormous contributions.

The intellectual property protection system emerged as a product of the development of human civilization and commodity economy and, in various countries, it has increasingly become an effective legal tool for protecting the interests of the owner of intellectual products, promoting the development of science, technology and the social economy, and allowing international competition. As a whole, China, however, for a variety of historical reasons, began work on its intellectual property rights protection system at a comparatively late date. After China started reform and opening to the outside world, it accelerated the process of establishing an intellectual property rights protection system in order to rapidly develop social productive forces, promote overall social progress, meet the needs of developing a socialist market economy and expedite China's entry into the world economy. Since the end of the 1970s, China has done a tremendous amount of effective work in this field, covering in a little more than a dozen years a distance which took other developed countries scores of years, even a hundred years, establishing a relatively comprehensive legal system for the protection of intellectual property rights, thereby attracting worldwide attention for its achievements not only in establishing the system but also in enforcement.

Today, intellectual property protection is an issue of universal concern in the international political, economic, scientific, technological and cultural exchanges. International bilateral and multilateral negotiations on this topic, especially the reaching of the Agreement on Trade-related Aspects of Intellectual Property Rights in the General Agreement on Tariffs and Trade (GATT), have raised worldwide intellectual property protection to a new level.

In today's world, great importance is attached to intellectual property protection. What is China's specific position regarding this question? What is China's current legislation on intellectual property rights and how is it enforced? What measures has China taken to ensure its international commitment to intellectual property protection? A brief introduction to these issues will prove useful.

I. China's Basic Position Regarding the Protection of Intellectual Property Rights

It is the Chinese government's view that the intellectual property protection system plays a significant role in promoting progress in science and technology, enriching culture and developing the economy. It functions both as an important institution ensuring the normal running of the socialist market economy and as one of the basic environments and conditions for conducting international exchange and cooperation in science, technology, economy and culture. China considers the protection of intellectual property an important part of its policy of reform and opening to the outside world and of the building of its socialist legal system. Beginning in the late 1970s, China has been formulating laws and regulations for intellectual property rights protection, and has been participating in activities organized by the relevant international organizations aimed at strengthening international exchange and cooperation in the field of intellectual property rights. From its inception China's intellectual property rights protection system was directed towards the world and geared to high international standards. Spurred on by its reform and opening up, China has carried on its intellectual property protection legislation at a speed never before known.

On March 3, 1980, the Chinese government submitted its application for admission to the World Intellectual Property Organization, and became a member state as of June 3, 1980.

The Trademark Law of the People's Republic of China was adopted at the 24th meeting of the Standing Committee of the Fifth National People's Congress on August 23, 1982, effective March 1, 1983, significantly marking the beginning of the systematic establishment of China's modern legal system for the protection of intellectual property rights.

On March 12, 1984 the fourth meeting of the Standing Committee of the Sixth National People's Congress adopted the Patent Law of the People's Republic of China, effective April 1, 1985.

On December 19, 1984, the Chinese government submitted its instrument of accession to the Paris Convention for the Protection of Industrial Property to the World Intellectual Property Organization and became a member state as of March 19, 1985.

The General Principles of the Civil Law of the People's Republic of China were adopted at the fourth session of the Sixth National People's Congress on April 12, 1986, effective January 1, 1987. In this legislation, intellectual property rights as a whole were clearly defined in China's basic civil law for the first time as the civil rights of citizens and legal persons. This law for the first time affirmed citizens' and legal persons' right of authorship (copyright).

The Chinese government has also worked hard in helping to build up an international environment wherein intellectual property rights in integrated circuits are protected. The World Intellectual Property Organization adopted the Treaty on Intellectual Property in Respect of Integrated Circuit at a diplomatic conference held in Washington D.C. in 1989; China was among the first signatory states.

The Chinese government presented its instrument of accession to the Madrid Agreement for the International Registration of Trademarks to the World Intellectual Property Organization on July 4, 1989, and became a member state as of October 4, 1989.

The Copyright Law of the People's Republic of China was adopted by the 15th meeting of the Seventh National People's Congress Standing Committee on September 7, 1990, effective June 1, 1991.

On July 10, 1992, the Chinese government presented its instrument of accession to the Berne Convention for the Protection of Literary and Artistic Works to the World Intellectual Property Organization and on July 30, 1992 its instrument of accession to the Universal Copyright Convention to UNESCO, becoming a member state of both conventions as of October 15 and October 30, 1992 respectively.

On January 4, 1993, the Chinese government presented its instrument of accession to the Convention for the Protection of Producers of Phonograms Against Unauthorized Duplication of Their Phonograms to the World Intellectual Property Organization, and became a member state as of April 30, 1993.

The Law of the People's Republic of China on Combating Unfair Competition was adopted by the third meeting of the Standing Committee of the Eighth National People's Congress on September 2, 1993, and became effective on December 1 of the same year.

On September 15, 1993, the Chinese government submitted its instrument of accession to the Patent Cooperation Treaty to the World Intellectual Property Organization, becoming a member state as of January 1, 1994. The Patent Office of China is China's agency dealing with cases involving the Patent Cooperation Treaty, performing international patent searches and preliminary examinations.

The above are only part of the records of China's intellectual property legislation and its participation in the activities organized by related international organizations, demonstrating the importance China has attached to intellectual property protection.

The basic framework for China's intellectual property rights protection legal system was completed for the most part in the 1980s. In the 1990s, international economic relations and the international economic environment have already undergone great changes. In November, 1990, multilateral trade negotiations in GATT's Uruguay Round produced a draft Agreement on Trade-related Aspects of Intellectual Property Rights. This signaled that a new international standard of intellectual property rights protection was taking form. The Chinese government actively participated in the negotiations and made unremitting efforts towards their final success. In order to meet the needs of the ever-wider opening up, China has consciously sought to fulfil its international obligations in intellectual property rights protection, endeavouring to bring its intellectual property protection level near the new international standards, and has taken many major measures to further raise its current level of intellectual property rights protection.

The Chinese government's sincerity in its efforts to scrupulously abide by international conventions and bilateral agreements regarding the protection of intellectual property rights, and its capacity to fully implement its international obligations have been appreciated and supported by world opinion. When reviewing the World Intellectual Property Organization's past 20 years of cooperation with China, Dr. Arpad Bogsch, Director-General of the Organization, pointed out that "China had accomplished all this at a speed unmatched in the history of intellectual property protection."

China adheres to the principle in legal system that "there shall be laws to abide by, everyone should abide by the law, the law must be enforced strictly, and those who violate the law must be dealt with." Still, the intellectual property rights protection system has only comparatively recently been introduced in China, and some portion of the population has a rather incomplete understanding of intellectual property rights. In order to better implement this principle, while improving its legal system, enforcing the laws earnestly and striking relentless blows at infringements and other unlawful practices, China has spared no efforts in publicizing and providing education about the intellectual property protection legal system and in accelerating the training of professional personnel in this field. In China the promulgation of every intellectual property law was followed by widespread publicity through the media and distribution of large quantities of educational video-tapes and seperate editions of the law. Mean-while, governments at all levels ran legal knowledge forums and training classes so as to promptly make the relevant law known to all the people. After the revision of the Patent Law, for instance, millions of people throughout China attended such classes, the attendance in Hunan Province alone reaching 600,000 people. The fact that there has been an increasing number of cases involving intellectual property rights in recent years and that these cases have been remedied through recourse to law reflects the people's heightened awareness and the wide spread of intellectual property rights knowledge throughout society. In order to speed up the training of personnel in this field, the Chinese government has, in close cooperation with related international organizations, sent people abroad to study or to attend training classes and seminars. Together with the World Intellectual Property Organization, China has held more than 30 training classes and seminars, with the attendance of over 3,000 people. Programmes in intellectual property rights education and research have also been initiated at over 70 institutions of higher learning throughout the country. In 1986, a teaching and research centre for intellectual property rights was established at the People's University of China, enrolling non-law majors to study for a second degree in intellectual property rights; Beijing University's School of Intellectual Property Rights was founded in 1993 on the basis of the achievements it had attained in teaching and research in this regard. An education system for training professional personnel in this field for their second, Master's or Doctor's degrees has gradually taken form in China, providing the nation with batch after batch of qualified personnel in intellectual property rights protection.

II. China Has a High-Grade Legal System for Intellectual Property Protection

Along with its progress in reform and opening up, China has made big strides in intellectual property protection. In accordance with its national conditions and current tendencies in international development, China has formulated and finetuned various laws and regulations on intellectual property protection, thereby constructing a socialist legal system for intellectual property protection with Chinese characteristics. The scope of the intellectual property rights protected in China and the degree of protection afforded have gradually conformed with international practices and the high degree of legal protection for intellectual property rights has been realized.

Effective as of March 1983, the Trademark Law of the People's Republic of China and the rules for its implementation set forth the principles of application, examination and registration in trademark registration procedures which are entirely identical with common international principles. In order to meet the requirements of the reform and opening up and of economic development, to more effectively crack down on trademark counterfeiting and stop acts of infringement, and to conscientiously protect the right to exclusive use of a registered trademark, in 1993 China revised both its Trademark Law and the rules for its implementation to expand the range of trademarks protected. Regulations on commodity trademarks were joined by regulations on the registration and management of service trademarks; in examination as to form, a revision procedure was added, and in examination as to substance, a written comment system was established to provide convenience for registered trademark applicants. All these regulations coincide completely with the requirements of GATT's Agreement on Trade-related Aspects of Intellectual Property Rights. In addition, the State Administration for Industry and Commerce has issued a series of regulations including the Regulations on the Administration of the Printing of Trademarks and the Procedures for Filing License Contracts for the Use of Trademarks. In February 1993, the National People's Congress Standing Committee adopted the Supplementary Regulations on Punishing Criminal Counterfeiting of Registered Trademarks to further intensify punishment for such counterfeiting and other infringements. These laws and regulations fully and effectively guarantee the right to the exclusive use of Chinese and foreign registered trademarks.

The Patent Law of the People's Republic of China and the rules for its implementation came into effect in April 1985, expanding the scope of intellectual property protection in China to include inventions and other new creations. In order to bring the level of China's patent protection closer to international standards, the Standing Committee of the National People's Congress adopted an amendment to the Patent Law on September 4, 1992, which included important revisions. Proceeding from the needs of expanding the opening up and accelerating scientific, technological and economic development, first, the revised Patent Law expands the scope of patent protection: patents may be granted to all types of technological inventions, whether new products or new techniques, including pharmaceutical products and substances obtained by means of a chemical process, foods, beverages and flavourings. Second, an invention patent's duration has been extended from 15 years from the date of application to 20 years; the duration of utility model patents and of exterior design patents has been extended from 5 years from the date of application to 10 years. Third, the protection of patent rights has been further strengthened. In addition to extending the protection of a patented process to include products directly produced by that process, the law clearly stipulates that the importation of patented products requires the permission of the patent holder, thereby giving more effective protection to the rights and interests of patentees. Fourth, conditions for imposing compulsory patent license were re-stipulated. These measures mark the reaching of a new level of patent protection in China. In this way, the Patent Law of China has essentially been brought in line with the GATT Agreement on Trade-related Aspects of Intellectual Property Rights.

The Copyright Law of the People's Republic of China and the rules for its implementation explicitly protect the copyright and other legitimate rights and interests of the authors of literary, artistic and scientific works. The law provides that in addition to protecting the copyright of written works, oral works, music, operas, *quyi* (folk art forms including ballad singing, story telling, comic dialogues, clapper talks, cross talks, etc), choreography, works of fine arts, photographs, films, TV programmes, video tapes, engineering designs, product designs and their descriptions, maps, sketch maps and other graphic works, China also protects computer software. China is among a select group of countries that have explicitly listed computer software as the object of protection by copyright laws. The State Council has, moreover, promulgated the Regulations on the Protection of Computer Software, providing the specifics whereby the laws protecting computer software will be implemented. These regulations, a necessary adjunct to the Copyright Law, came into effect in October 1991. On September 25, 1992 the State Council promulgated the Regulations on the Implementation of the International Copyright Treaty, providing specific regulations on protecting foreign authors' copyrights in accordance with the international treaty.

These laws and regulations have been joined by the Technological Contract Law of the People's Republic of China and the Law on Scientific and Technological Progress of the People's Republic of China as formulated by the Standing Committee of the National People's Congress, as well as a series of administrative regulations concerning intellectual property protection worked out by the State Council, together further optimizing the nation's legal system for the protection of intellectual property rights, in the whole bringing the system close to and in coordination with international levels of protection.

China has a complete legal system for the protection of intellectual property rights. China's intellectual property law stipulates the legal responsibilities to be borne by anyone who violates the law, including civil liability, criminal liability and exposure to administrative sanctions.

China's Patent Law provides that in the case of infringement arising from the exploitation of a patent without authorization of the patentee, the patentee or other affected parties may request the patent administrative authorities to deal with the matter or may directly file suit in a people's court. In investigating and dealing with the matter, the patent administrative authorities are empowered to order the infringer to stop all acts of infringement and compensate for any losses. Whoever counterfeits a patented product or wrongly appropriates a patented technique will be ordered by the patent administrative authorities to cease all acts of counterfeiting, to provide the public with notification of his or her violation, and to pay a fine. In the case of serious violations, the criminal liability of the person directly responsible shall be investigated through application of relevant articles of the Criminal Law, and if found guilty, the person directly responsible shall be sentenced to fixed-term imprisonment of not more than three years, criminal detention or a fine.

China's trademark laws and regulations stipulate that in the event of infringement on the right to exclusive use of a registered trademark, the administrative department for industry and commerce can, in line with its functions and powers or on the basis of a consumer complaint, examine and deal with the violation on its own initiative. The party whose right has been infringed may also, at the place where the infringer lives or where the act of infringement took place, request an administrative department for industry and commerce at or above the county level to handle the matter. The relevant administrative department for industry and commerce has the right to order the infringer to immediately cease infringement and to compensate the party whose right has been infringed for its losses. If the act of infringement on the right to exclusive use of a registered trademark does not constitute a crime, the administrative department for industry and commerce may still impose a fine on the infringer. If the party concerned wishes to challenge the decision of the administrative department for industry and commerce, it may bring suit in a people's court within a fixed time and the court will render judgement on the case. These regulations provide convenience to the litigants, and, moreover, ensure consistency, impartiality and seriousness in administrative law enforcement and judicial adjudication. In the event of an infringement on the right to exclusive use of a registered trademark, the party whose right has been infringed may also directly bring suit in a people's court. If the counterfeiting of registered trademarks constitutes a crime, the person who committed the act shall be ordered to compensate the party whose right has been infringed for losses suffered and his criminal responsibility shall be investigated and dealt with in accordance with the law. In accordance with the Supplementary Regulations on Punishing Criminal Counterfeiting of Registered Trademarks, in cases where the illegal gains are relatively large or other serious circumstances are involved the counterfeiter of a registered trademark will be sentenced to fixed-term imprisonment of not more than three years or criminal detention, and/or fined; if the illegal gains are very large the counterfeiter shall be sentenced to fixed-term imprisonment of not less than three years and not more than seven years and be fined. If an enterprise or institution is guilty of criminally counterfeiting a registered trademark, the unit will be fined and the criminal liability of the person in charge and other people directly responsible for the counterfeiting shall be investigated and dealt with in accordance with the law. If a government employee knowingly covers up the criminal counterfeiting of a registered trademark or if a person charged with enforcing the law compromises the law for personal gain, his or her criminal malfeasance will be determined by law.

The Copyright Law of China provides that the following acts shall be regarded as infringement: publication of a copyright owner's work without his or her permission, and the unauthorized publication of a cooperative work as the work of a single author; claiming authorship of another person's work without taking part in its creation with the intention of gaining fame or profit; distortion or alteration of another person's works; exploitation of an author's work in any manner without prior permission; the use of another's work without providing the legally stipulated payment; and live broadcast of a performance without the performer's prior permission. In such cases, the infringer shall bear civil responsibility for the cessation of the infringement, for the elimination of any negative effects caused by his actions, for offering a public apology, and for compensation for any losses. Those who plagiarize other people's works, or reproduce and distribute another person's works for their personal benefit without the copyright holder's permission, those who publish a book without the permission of the owner of the publishing right, and those who duplicate and distribute video and audio tapes without getting the permission of the tape manufacturers bear civil responsibility for their actions. The copyright administrative authorities may confiscate their illegal income or impose a fine on them. In the case of a copyright infringement or of violation of other related interests, the party whose rights have been infringed may also directly bring suit in a people's court. With regard to illegal activities that gravely jeopardize the social order or seriously infringe on the legitimate rights and interests of a copyright holder or the holder of other intellectual property rights, in cases where such violations constitute a crime the criminal liability of the infringer shall be investigated and dealt with in accordance with the relevant laws.

With the implementation of intellectual property laws, intellectual property rights are effectively protected in China. These laws are also actively encouraging invention and other forms of creation and fair competition. For instance, the protection of the right to the exclusive use of registered trademarks has resulted in the rapid growth of the number of trademarks registered by Chinese and foreign businessmen in China. By the end of 1993, the number of effective registered trademarks had exceeded 410,000. Of these, 350,000 were domestic, with the remaining 60,000 coming from 67 countries and regions. Companies from the United States, for example, had only 122 trademarks registered in China before 1979; by 1993 that number had soared to 16,221, more than a hundred times the earlier figure. In 1993, there were 170,000 applications for trademark registration annually in China, including more than 130,000 applications for new trademarks registration, among the highest number in the world. In addition, the Patent Law of China has greatly encouraged inventions and other creations in China, and has proved a magnet to patent applications from other countries and regions. On April 1, 1985, the first day the Patent Law came into effect, 3,455 applications for patent rights were submitted. By the end of 1993, the Patent Office of China had handled over 360,000 applications for patent rights. Of those, 27.5 percent were for inventions, 62.8 percent for utility models, and 9.7 percent for exterior designs; domestic applications accounted for 86.4 percent, while 13.6 percent were applications from 70 countries and regions. By the end of 1993, 175,000 patents had been approved, including more than

20,000 invention patents, more than 130,000 utility model patents and over 20,000 exterior design patents.

III. China Has a Complete Law Enforcement System for Intellectual Property Protection

China has formulated comprehensive intellectual property rights laws and regulations. Today, it is earnest and fair in executing these laws, and much has been accomplished in this regard.

These great achievements in the execution of the intellectual property rights protection laws and regulations are above all the product of comprehensive judicature and administration provided for in these same laws and regulations.

1. China's judicial institutions for intellectual property protection.

In China, any citizen, legal person or organization entitled to intellectual property rights whose rights and interests have been infringed may bring a lawsuit to the people's court in accordance with the law and receive practical and effective judicial protection.

The people's courts exercise judicial power independently according to law, are subordinate only to the law itself, and are not subject to interference by any administrative organ, public organization or individual.

Earnest execution of the law is the core of the administration of justice. The judicial activities of a people's court are carried out on the basis of facts, and with the law providing the criterion. Cases are tried strictly in accordance with substantive and procedural laws. Cases are heard in an open court, and a collegial system, a challenge system, a system whereby the court of second instance is the court of last instance, and a trial supervision system are practised. Judicial work, in accordance with the law, is also subject to supervision by people's congresses and people's procuratorates at all levels and by the masses, so as to ensure openness, impartiality, and seriousness.

The establishment and fortification of the judicial organs for trying intellectual property rights cases and the optimization of the judicial system are important guarantees for the people's courts correctly to handle such cases and conscientiously to protect intellectual property rights according to law. In recognition of the specialized nature of intellectual property rights cases and the advanced nature of the technology often involved, the higher people's courts in several provinces and municipalities directly under the central government such as Beijing, Shanghai, Guangdong, Fujian and Hainan have since 1992 established such intellectual property rights courts as their actual needs demand. The intermediate people's courts in all the special economic zones as well as Beijing and Shanghai have also established intellectual property rights courts. Intermediate people's courts in the capital cities of other provinces, municipalities and autonomous regions have set up collegial panels specializing in cases involving intellectual property rights protection. In this manner the hearing of intellectual property rights cases is centralized with the advantageous results that unity in executing the law is ensured, experience in dealing with the law is amassed, and the quality of judicature in intellectual property rights cases is strengthened.

With the implementation of China's law on intellectual property protection and the increasing improvement of the judiciary's protective power, people's courts at various levels in China have accepted and decided a large number of civil disputes concerning intellectual property rights. A total of 3,505 cases concerning intellectual property rights disputes were accepted and handled by people's courts throughout the country from 1986 to the end of 1993, 1,168 of which concerned copyrights, 1,783 patents, and 554 trademark rights. The people's courts in accordance with the law defend the legitimate rights and interests of the foreign and domestic intellectual property rights holders through trying cases concerning intellectual property rights disputes. For example, the inventor of a new "technique for sinking piling using drill holes," brought a suit against the Beijing Subway Foundation Engineering

Company to determine ownership of the patent on the invention. After trying the case, the Beijing Higher People's Court held that this invention was not a service invention as described by the Patent Law, so the patent right belonged to the inventor and not to his employer. In another example, Hong Kong's Sendon International Co., Ltd. brought suit against Shenzhen's Huada Electronics Co., Ltd. for trademark infringement. After hearing the case, the Shenzhen Intermediate People's Court ruled that the trademark "SENDON" was registered in China mainland by the plaintiff and should be protected by law. The defendant's use of the trademark "SENDON" on the same commodity sold by the plaintiff under that name constituted infringement.on the rights to exclusive use of a registered trademark. The court decided that the defendant should pay the plaintiff 468,314.4 yuan in compensation.

Intellectual property rights are important civil rights. In civil infringement cases, the people's court is empowered to order the infringer to bear civil responsibility for the cessation of the infringement, for the elimination of any negative effects caused by his actions, for offering apologies, and for compensation for any losses in accordance with the law. Furthermore, it is empowered to confiscate the infringer's illegal gains and/ or adjudge the infringer to criminal detention or a fine.

If the infringement of intellectual property rights is so serious that it has disrupted the economic order and constitutes a crime, the infringer's criminal responsibility is investigated and dealt with according to law. When a people's procuratorate institutes prosecution for a criminal act of infringement, if the evidence is sufficient to prove that the defendant has counterfeited another's trademark or patent right and the case is so serious as to constitute a crime, the people's court shall promptly and precisely impose punishment in strict accordance with the law. Between 1992 and 1993, people's courts accepted 743 criminal cases for counterfeiting trademarks, of which 731 have been tried with 566 people being sentenced to fixed terms of imprisonment, criminal detention or other punishments. The People's Court of Zhongshan City in Guangdong Province in separate cases imposed fines on five persons directly responsible for counterfeiting the American Mobil Oil Corporation's trademark "MOBIL," further sentencing the defendants to fixed terms of imprisonment from one year to two and a half years. This amply demonstrates that the people's courts of China are resolute in their stand towards punishing criminals and safeguarding intellectual property rights.

According to China's Administrative Procedure Law, if a citizen, legal person or organization wishes to contest a judgement or order of an administrative department for intellectual property protection in a dispute concerning intellectual property rights and to initiate administrative procedure litigation, the people's court shall try the case and shall, in accordance with the law, make a decision to maintain, rescind, or alter it.

When a people's court tries a case arising from intellectual property rights involving foreign nationals, it acts in accordance with Chinese laws and relevant international conventions to which China is a party, adhering to the principle of equity and reciprocity. In this way, the court provides the solid legal guarantees necessary for expanding international economic, technological and cultural exchange and cooperation. The Shenzhen Intermediate People's Court accepted the American E.F. Houghton Company's suit against the Shenzhen Hailian Chemical Co., Ltd. for the latter's trademark violations. Investigation proved the defendant's infringement and held it responsible. The two parties negotiated a settlement through mediation. The defendant promptly stopped its acts of infringement, offered public apology to the plaintiff, and handed over 130,000 yuan as a compensation for the plaintiff's economic loss. The court, in addition, adjudged the defendant a civil sanction fine. Ten days passed from the court's acceptance of the case to its resolution, expeditious remedy much appreciated by the American plaintiff. In acknowledgement of this, the E. F. Houghton Company presented the court with a silk banner reading: "Chinese law is just; judges try cases expeditiously."

Over the past few years, in an effort to raise the level of the administration of justice, the people's courts have adopted a series of potent measures to improve their quality and efficiency in handling cases. In order to amplify their impact, the people's courts have selected typical cases and tried them publicly, conducting information campaigns through the various public media. Undeniable social effects have been achieved through the use of specific cases in the popularization of legal education and the dignity of the socialist legal system has been maintained.

2. Administrative channels for intellectual property protection in China.

n addition to judicature in accordance with international practices, China's system for the protection of intellectual property rights comprises the Patent Law, the Trademark Law, and the Copyright Law and other administrative channels designated in intellectual property laws, all proceeding from China's actual conditions.

Under the Patent Law, the competent authorities in the State Council and local people's governments have the right to establish patent offices. Today, China has more than 50 patent offices established by local governments and more than 20 patent offices established by various ministries and departments under the State Council. The State Copyright Administration and local copyright administrative organs have been established in accordance with the Copyright Law. Trademark administration calls for unified registration of trademarks by the central government and level-by-level administration by the various local governments. Trademark administrative departments under the administrative bureaus for industry and commerce have been established at the central, provincial, city, prefectural and county levels; below the county level, there are administrative offices for industry and commerce. Today, there are well over 7,000 full-time trademark administration personnel throughout China, in addition to 300,000 part-time personnel.

Chinese intellectual property rights administrative departments exercise their legally stipulated powers and functions to safeguard law and order within the field of intellectual property, encourage fair competition, mediate disputes, settle cases involving violations of intellectual property rights, and protect the interests of the broad masses of the people by maintaining a good social and economic environment.

In China the administrative procedures for solving disputes concerning intellectual property rights are simple and convenient. Cases can be quickly filed for official examination and possible prosecution, investigation follows promptly, and efficiency in handling the case is high. This is advantageous to the owners of the rights. The patent administrative organs in China always treat patent violation claims seriously and deal with them without delay in accordance with the law.

Since the Copyright Law was put into force, local administrative organs responsible for copyright affairs investigated and dealt with more than 150 cases involving pirated books and video products from June 1991 to the end of 1993. They have confiscated and destroyed the pirated goods and levied administrative sanctions on the infringers. In 1994, the Chinese government has organized the departments concerned to launch an assault, investigating and dealing with the illegal duplication of laser discs and illegal reproduction of books. In April 1994 in Guangdong Province, the administrative departments in charge of copyrights, cultural affairs, broadcast, film and video-tapes, the administrative departments for industry and commerce, and public security departments took joint action to deal with the illegal duplication of laser discs. Subsequently, Shanghai, Jiangsu and Hunan also took actions to deal with these problems. These measures dealt a heavy blow to the production and selling of pirated products. Over this same period, relevant departments of the Chinese government took steps to strengthen administration over the establishment of enterprises manufacturing compact discs and supervision over their production in accordance with the law.

The Trademark Law of China has been in effect for more than ten years. During this time, the administrative departments for industry and commerce have dealt with 130,000 cases of trademark violation and counterfeiting, including a number of particularly serious cases, e.g. trademark violations or counterfeited trademarks for "Zhonghua" cigarettes, for "Forever," "Phoenix" and "Flying Pigeon" bicycles, for "Guizhou Maotai" wine, and for "Xingkaihe" ginseng. Effective protection was thus given to the lawful rights and interests of the registered trademark owners.

China's intellectual property rights administrative organs, in accordance with Chinese laws and relevant international treaties to which China is a party, adhering to the principle of equal treatment for nationals and non-nationals and reciprocity, give protection to foreigners' intellectual property rights in accordance with the law. For instance, the Zhejiang Provincial Patent Administration Office recently reached a just settlement in a complaint brought by a foreign plaintiff concerning unlicensed production of a cigarette lighter to which he held patent. The competent authorities ordered the factory concerned to cease all acts of infringement and compensate the foreigner for his losses. The State Copyright

Administration investigated and then dealt with a series of cases in which a dozen odd arts and crafts factories in Fujian and Guangdong had manufactured pirated toys copying several foreign companies' toy designs, and a case in which an electronics enterprise in Jiangsu was illegally producing compact discs. Administrative departments for industry and commerce have investigated and dealt with 3,000 cases involving the counterfeiting and other violations of such foreign trademarks as TDK, Toshiba, Sony, IBM, 3M, ESSO, P&G, Head & Shoulders, Xiaotiancai, and Philips.

A large proportion of the cases concerning violations of foreigners' intellectual property rights were investigated and dealt with by China's intellectual property protection administrative offices on their own initiative, acting in accordance with their prescribed functions and powers.

China's administrative departments for industry and commerce have undertaken the responsibility of maintaining economic order and can make market investigations on their own initiative so as to effectively protect the rights of the registered trademark owners. Since 1988, administrative organs for industry and commerce at various levels in Guangdong Province have investigated and dealt with 301 cases concerning the violation of US-owned trademarks. Out of these 301 cases, one third were filed by the American trademark owners, with the remaining cases being the product of market investigations by the administrative organs for industry and commerce or consumer complaints. China's intellectual property rights administrative offices are impartial, and firmly safeguard the lawful rights and interests of those who hold such rights. This has earned them praises from many foreign enterprises and joint ventures. Some of these companies presented the administrative departments for industry and commerce silk banners or gilt boards, bearing words of praise such as "Upright and honest, firm as a rock in administering justice," "Impartiality in enforcing the law, support right, eliminate wrong," "Just settlement, protection of commerce," "Strict and impartial justice, conquerer of fakes and frauds," and "Strict and impartial in executing the law, consummate impartiality." They praised the personnel handling the cases as "conscientious in work and resolute in action," "Such speed in handling a case is seldom encountered anywhere in the world," etc.

Concluding Remarks

As China implements its reform and opening to the outside world, it is changing with each passing day. Today more than a few international observers have come to the conclusion that in terms of intellectual property protection China has reached international advanced levels. China's backwardness in its intellectual property system is now a thing of the past.

However, there remain some naysayers in the world seemingly willfully blind to China's development and transformation who incognizant of present realities pass improper judgements on the nation's current situation regarding intellectual property protection. They allege that China has not yet established a "full and effective intellectual property system," and that China "lacks the ability to undertake international obligations." Such unfounded opinions do not bear argument; the truth speaks for itself.

Nonetheless, China cannot remain satisfied with the achievements it has already made. China is a developing country and still has much work towards optimizing its intellectual property system. This system in its modern form was established only a short time ago, and as a result, awareness of intellectual property rights remains underdeveloped in society at large. In some regions and in some governmental departments there is insufficient appreciation of the importance of intellectual property protection. Some serious acts of infringement have violated not only the legitimate rights and interests of the holder of the intellectual property right, but also the dignity of the law. Accordingly, even as the nation continues to otherwise improve the intellectual property legal system, the State Council has drawn up Decisions on Further Strengthening the Protection of Intellectual Property. China is confident that the implementation of all the important measures contained in the Decisions will mark a great new step forward in the nation's efforts to ensure the protection of intellectual property rights.

China will continue actively to promote international cooperation in the field of intellectual property. China itself has received active assistance from the World Intellectual Property Organization and from others working in the field in establishing and fine-tuning its intellectual property rights protection system. The nation will, as in the past, actively join in the activities of relevant international organizations and fulfil the obligations described in the international intellectual property treaties and agreements. Operating on the basis of the Five Principles of Peaceful Coexistence and in accordance with the principle of equality and mutual benefit, China will continue to cooperate with the rest of the world's nations, working and making positive contributions towards the development and optimization of the international intellectual property system.

19. OVERVIEW: SHANGHAI

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20. OVERVIEW: HONG KONG

Current Economic Statistics - Hong Kong

Hong Kong

The Really Useful Guide: Hong Kong

Hong Kong at a Glance

~~CNF~~ Currency Boards: Straitjackets for Monetary Policy?

CURRENT ECONOMIC STATISTICS–HONG KONG

Economic Performance

Strong growth in **real GDP** during the first half of 1997 evened out the poor final quarter, yielding a 5.3% growth rate for the year. This was an increase from 4.9% growth in 1996 and 3.9% in 1995. The increase in growth is notable in the presence of the growing government budget surplus in addition to the impact of the Asian crisis on the stock market and the deteriorating trade balance in goods and services. The government has forecast 3.5 percent growth for 1998, while the predictions of many analysts are lower, around 2.0 percent.

Unemployment is rising, from 2.4% in 1997 to 3.5% in the first three months of 1998.

Inflation improved somewhat in 1997, as consumer prices (as measured by the composite CPI) declined from 6.3% in 1996, to 5.8% in 1997. In 1994-95, inflation was more than 8%. The decline in inflation can be attributed to the strong Hong Kong dollar and weak domestic demand. In February, the CPI had risen 4.5% over the previous 12 months. The government forecasts 5.0% inflation in 1998.

Fiscal and Monetary Policy

Hong Kong has had a **government surplus** in three of the past four years. In 1997, the budget surplus rose to 3.8% of GDP in 1997, from 2.2% in 1996 (there was a 0.3% deficit in 1995). Government expenditure has been relatively stable at about 16-17% of GDP. This year's budget included a number of modest tax cuts and other measures designed to ease economic adjustment and recovery.

Despite the regional currency troubles and stock market volatility, **monetary figures** show no signs of capital flight or panic. 12 month growth in M3 fell to 4.0% in February 1998, from an earlier rate of 6%. In 1996, M3 growth was 10.6% and in 1995 it was 13.6%. Although Hong Kong's prime interest rate has been raised twice in the past year, Hong Kong dollar short-term interest rates have dropped to their lowest levels since the October attack on the currency, now sitting in the low-7 percent range after hitting the mid-16 percent rage in January.

The Hong Kong dollar, which is pegged to the U.S. dollar through a **currency board** system, has been steady at around 7.74 ($HK/$US). The Hong Kong Monetary Authority (HKMA) is confident it can effectively defend the peg, and has demonstrated its ability and willingness to do more than once in the past year. (See *Hong Kong and the Asian Crisis*).

Internal Structure

Because of the exchange rate peg, Hong Kong's adjustment to the competitive devaluations occurring in the region has had to come as a decline in asset prices. This has materialized both in the real estate and stock markets. Painful as this decline in prices has been, it is generally viewed as contributing to Hong Kong's competitiveness.

Hong Kong's **property market** is an important sector of the economy, comprising 40-50 percent of the investment market either directly or indirectly. Generally speaking, housing supply has not kept pace with demand, and appears unlikely to do so for some time to come. In both 1996 and 1997, residential property prices increased 20% to 40% for mass housing, and almost 50% for luxury properties, with some choice properties almost doubling in price. As the region's economic downturn progressed, high interest rates put pressure on mortgages and property demand. Residential property prices began to retreat and analysts believe prices are off 25% to 30% from their summer 1997 highs. Further declines of 10% to 15% are expected before the market hits bottom. Commercial property prices were already soft, and with substantial additional capacity arising in 1998, prices and rents are expected to decline perhaps 10% to 15% as well.

Hong Kong's **stock exchange** (as measured by the Hang Seng index) achieved its record high of 16,820 in August 1997, up 20 percent compared to year-end 1996. Optimism about the performance of Chinese-owned firms based in Hong Kong after reversion and record oversubscriptions to new stock offerings boosted investor confidence levels. The market retreated some as worries over regional financial turmoil increased, to around the 14,000s through the early autumn. On October 23, the Hang Seng index fell 10.4% when the overnight interbank rate shot up to a historic high (280%), as Hong Kong fended off speculative attacks. The index tumbled again on October 28 to 8,776, its lowest level in two and a half years and down 48% from its all time high in August. The market bounced back to end the year at 10, 723. Further volatility and the worsening crisis led to another downturn on January 12 when the market reached 7,909, its lowest point in three years. The market has since recovered a bit and is currently around 11,000.

External Sector

Hong Kong's economy depends on international trade and investment. It is the world's eighth largest trading economy, the 12th largest export market of the U.S., and the source of more than half of direct foreign investment into China. Almost one-half of China's trade is conducted via Hong Kong.

Hong Kong ran a modest **trade deficit** in 1997 of $6.7 billion, up from $2.5 billion in 1996, with total imports of $232 billion exceeding $225 billion in exports. Of the $188 billion in merchandise exports in 1997, domestic exports (15 percent of total) were off 0.5 percent, while re-exports (85 percent of total, and mostly to and from China) rose 4.6 percent. Merchandise imports rose 4.8 percent to $209 billion, of which $48.4 billion were for use in Hong Kong. As in previous years, Hong Kong's services balance ($14.5 billion) served to offset much of its merchandise trade deficit.

Foreign exchange reserves were $92.8 billion in February 1998, the third largest in the world. This is slightly below $96.9 billion reported last November, but well above levels held in earlier years.

Future Challenges

Despite Hong Kong's relative success in weathering the **financial storm** that has sunk neighboring economies, many concerns remain. Some bankers continue to fear speculative attacks against the Hong Kong dollar, despite its relative strength and stability. Others worry the pressures and long-term effects of maintaining high interest rates to defend the peg. Another fear is that a stock market correction in the U.S. might trigger another downturn in the region and especially Hong Kong, given its close linkages to the U.S. economy. Others are concerned that China's economic growth might falter and investments drop off.

Hong Kong must also absorb the decline in asset prices and cope with growing unemployment. And Hong Kong is not immune to shocks within the region; Indonesia's economic woes are weighing on the minds of local bankers and investors. Efforts to deepen Hong Kong's debt market are continuing apace, as the newly-created Hong Kong mortgage corporation expands its operations, and Hong Kong plans to being operation of its mandatory provident fund starting in early 1999.

HONG KONG
Summary Statistics

Population: 6.5 million (1997)
Per Capita Income (1996): US$ 24,500

Population Growth Rate: 1.0%
Fiscal Year: April 1 - March 31

GROSS DOMESTIC PRODUCT	**1994**	**1995**	**1996**	**1997e**	**1998e**
GDP ($ bn)	131.9	146.5	160.8	180.8	190.0
Real GDP Growth	5.4%	3.9%	4.9%	5.3	3.8
Gross Domestic Investment (% of GDP)	31.9%	34.8%	32.3%	33.6%	33.1%
Gross Domestic Savings (% of GDP)	33.1%	30.4%	30.6%	31.1%	31.4%
Unemployment Rate	1.9%	3.2%	2.8%	2.4%	n.a.
GOVERNMENT BUDGET (% of GDP)					
Expenditure	16.0%	17.0%	15.3%	15.9%	17.1%
Government Surplus	1.3%	-0.3%	2.2%	3.8%	2.0%
INFLATION/MONEY					
Consumer Prices	8.1%	8.7%	6.0%	6.0%	5.0%
Money Supply Growth (M3)	13.6%	13.6%	10.6%	n.a.	n.a.
EXCHANGE RATE (HK$/US$)					
Nominal	7.728	7.726	7.734	7.745	7.745
Real Effective (Index 1990=100)	114.5	112.9	120.9	131.6	n.a.
BALANCE OF PAYMENTS ($ bn)*					
Exports	151.2	174.0	180.1	191.3	203.0
(% Change)	ERR	15.1%	3.5%	6.2%	6.1%
Of Which: Re-exports	122.5	144.0	152.0	164.6	n.a.
Imports	161.7	193.6	198.6	211.7	224.8
(% Change)	ERR	19.7%	2.6%	6.6%	6.2%
Trade Balance	-10.5	-19.6	-18.5	-20.4	-21.8
Net Balance on Goods and NFS	1.6	-6.0	-2.6	-4.3	-3.2
(% of GDP)	1.2%	-4.1%	-1.6%	-2.4%	-1.7%
				November	
INTERNATIONAL RESERVES ($ bn)*	49.3	57.2	63.8	96.9	n.a.
Months of Imports	3.7	3.5	4.0	5.5	n.a.
CREDIT RATING					January
Standard & Poor's					A+
Moody's					A3
IBCA					A+

Sources: IMF, HKMA and Treasury Department Data; Consensus Forecasts

January 7, 199

* Hong Kong does not report complete current account or capital account data.
* 1997 Reserves include forwards and foreign currency assets of land fund.

HONG KONG

After more than a century and a half of British colonial rule, Hong Kong became a Special Administrative Region of the People's Republic of China on July 1, 1997. The 1984 Sino-British Joint Declaration (JD) defines Hong Kong's post-reversion status and establishes the "one country, two systems" model, under which Hong Kong will remain autonomous in social, economic, and cultural affairs for at least fifty years. Hong Kong's pre-reversion court system and government remain intact, responsibility for defense and foreign affairs has shifted from the UK to China. Thus far, the transition has been smooth. China has lived up to its Joint Declaration obligations.

The United States has a strong interest in a continuing successful transition. U.S. trade, investment, and business with Hong Kong flourish in a virtually barrier-free environment. Our exports to Hong Kong, many of which are re-exported to China, total over $14 billion; our two-way trade is over $24 billion. U.S. companies have about $16 billion of investment in Hong Kong, and some 1100 U.S. firms maintain offices there. About 50,000 American citizens live and work in Hong Kong. U.S. Navy ships make 60-80 port calls per year there, and those visits continue. Cooperation between Hong Kong and U.S. law enforcement agencies makes a real difference in efforts to combat drug trafficking, alien smuggling, organized crime, and counterfeiting. The U.S. has an extradition treaty with Hong Kong.

Our policy toward Hong Kong is grounded in a determination to help preserve Hong Kong's prosperity and way of life. We strongly support the Joint Declaration. It provides a sound basis for a smooth transfer of sovereignty and a rational framework for continued stability and prosperity. Although specific transition arrangements have been matters for the UK and China, we play a strong supportive role in order to preserve Hong Kong's autonomy and protect our interests. While recognizing that Hong Kong is now part of China, the 1992 U.S.-Hong Kong Policy Act created domestic legal authority to treat Hong Kong as a distinct non-sovereign entity within the PRC. This accepts and reinforces the Joint Declaration concept of "one country, two systems."

Hong Kong's next major political test will be the first post-colonial legislative elections, which are scheduled for May 1998. Controversial legislation passed after reversion established rules for the election. The U.S. government criticized the law because it diminished voter participation for some of the indirectly-elected seats, particularly in the "functional constituencies," and it seemed designed to reduce the number of seats held by activist Martin Lee's Democratic Party. Now that the bill is law, however, parties and candidates are making election preparations. Some activists have proposed international election monitoring. Hong Kong authorities have rejected such oversight, however, and the British have publicly stated that it is unnecessary. Hong Kong authorities have imposed no restrictions on potential candidates or parties, and there is little doubt that polling will be free and fair. The government has stated its intention to propose a new treason and sedition law, as it must under the governing Basic Law, soon after the election. That legislation promises to be controversial because some fear that its provisions might undermine fundamental freedoms.

At present, the Asian economic crisis is the most serious problem facing Hong Kong. The U.S. government has consulted closely with Hong Kong throughout the crisis and Hong Kong has played a helpful role. Hong Kong has weathered attacks on its currency and has the capacity and determination to maintain the U.S. dollar link. Hong Kong's banking sector is strong and its regulatory regime and financial officials are among the best in Asia. Monetary figures show no sign of capital flight or panic. The highly-publicized collapse of Peregrine Holdings has been absorbed. Still, economic growth will slow substantially this year due to high interest rates (necessary to defend the peg), reduced exports, and drops in the stock and property markets. Hong Kong will also remain vulnerable to regional developments. Hong Kong maintains a separate currency and monetary policy from the PRC.

The Really Useful Guide

If Hong Kong seems like an unintelligible vortex of commercial madness, read this

By Jim Erickson

Who lives there?

Don't let the English street signs mislead you. Hong Kong's 6.3 million people are 95% Chinese, the majority speakers of the Cantonese dialect. Nearly 60% were locally born. The rest tend to be immigrants or refugees from China. The jot of non-Chinese come from all over the world: Filipinos mainly, plus Americans, Britons, Canadians, Indonesians, Thais, Indians, Japanese, Australians and Malaysians. Nearly 20% of the population is less than 15 years old, and they'll be hanging around for a while. Average life expectancy is 79 years, a longevity rate topped in Asia only by Japan.

Who runs the place?

Since 1841, the year China ceded Hong Kong to Britain, ultimate authority has been vested in an appointed British Governor acting for the Crown. The overseers usually ruled their possession with a light hand, leaving local government to appointed plutocrats and civil servants. Chinese, at least the wealthy and well-connected, have always had some say (the first was named to the Legislative Council, which controls the territory's purse strings, in 1880). In recent decades, the power of Hong Kong (and increasingly mainland) Chinese tycoons has been growing at the expense of the British taipans. The first direct democratic elections did not occur until 1991. With the handover clock ticking loudly, Britain two years ago instituted reforms allowing the direct or indirect election of all 60 legislators.

How does the economy stack up globally?

Let the numbers speak: Hong Kong is the world's eighth-largest trading economy, with 1996 exports of $180.6 billion and imports of $198 billion (China, the U.S. and Japan are the territory's largest trading partners). Hong Kong is a powerhouse financial center, host to more than 182 licensed banks. The world's largest container port is located there. Per capita gross national product ($24,455) is greater than in Britain, Canada or Australia. At a growth rate of about 7.5% a year for the past 20 years, Hong Kong's economy has been ballooning twice as fast as the world's average.

Why has Hong Kong flourished?

It hasn't always. The colony got its start as a nearly uninhabited pestilential appendix to the mainland, and has been written off several times as other Asian cities threatened to eclipse it as the leading entrepot for China and the region. But its residents are nothing if not resilient. After surviving Japanese occupation during World War II, Hong Kong became by one reckoning the fastest-growing city in the world over the past 30 years. Credit goes to: 1) proximity to southern China and economically booming Southeast Asia; 2) one of the world's least-restricted and ardently capitalist economies; 3) a first-rate deepwater port; 4) adherence to the "rule of law" and an independent, British-based legal system that provides for impartial administration and regard for property rights; 5) and, most important, perhaps the most ambitious, acquisitive, industrious workforce on Earth.

The place looks like a termite colony. Why all the tall buildings?

For political, fiscal and environmental reasons, the government releases land for development very slowly, which sends property prices sky high. Another factor is that adequate sites for construction are limited by the territory's hilly terrain. Much of the Hong Kong waterfront is land reclaimed from the sea, but reclamation can't keep up with population. Developers have no choice but to build to the sky, buttressed by the omnipresent bamboo scaffolding. The upside: the most breathtaking skyline in the world (yes, it's better than lower Manhattan). The downside: Hong Kong is, like few cities, continuously rebuilding itself, and streets are under constant siege from deafening jackhammers and pile drivers.

What is that horrid smell? And what exactly is hanging from that meat hook?

A casual stroll down almost any promenade presents many arresting sensory experiences. Among them: rotting vegetables; open-air butchery; honking horns; sewer gas; rancid cooking oil; auto-parts solvent; typically loud Cantonese; caged barnyard animals; free-range cockroaches; dead sea-things; live sea-things; organs of sea-things.

Are German luxury cars given away free?

So it seems. But in truth, the territory sports more billionaires per capita than anywhere else in the world -- which means many can afford flamboyant transportation. A few years back, one out of every eight private vehicles on Hong Kong roads was a Mercedes-Benz. You almost have to be well-off to drive at all. New cars are subject to a stiff tax ranging from 40% to 60% of the base price, a surcharge imposed by the local government to discourage road-system gridlock.

Is it just me, or does everyone have a cellular phone?

You are not far off. Personal communications devices lend themselves well to the go-go consumeristic and commerce-centric lifestyle. Hong Kongers are among the world's most avid faxers and pagers; there's more than one pager for every five people. Sometimes it seems like the damn things are bleeping all at once, particularly during a meal at an elegant restaurant or just as you are being transported by a scene in a darkened movie theater.

What gods are worshiped here?

Religious and ethical beliefs are approached in much the same way as dim sum, with samplings from Confucianism, Buddhism and Taoism. There is a polyglot of deities, holdovers from ancient rural animism, including earth gods, sea gods, kitchen gods and hundreds of patron saints. The god of money is also assiduously honored. Ancestor worship, as well as respect for one's living extended family, is a foundation of Chinese culture and society. Homes and shops often contain a small ancestral altar where candles, incense or red electric bulbs are used to honor the departed. Hong Kongers are also a superstitious lot obsessed with lucky numbers. In 1994, a resident paid $1.7 million for a personal license plate bearing the number "9," which sounds like the Cantonese word for longevity.

Is there a local ordinance requiring public churlishness?

If Chicago is the city of the broad shoulders, Hong Kong is the city of the pointy elbows. Public touching by tradition is frowned upon, but this prohibition is relaxed in the rugby scrums that form in crowded buses, trains and department stores. Store clerks and restaurant staff can be surly and have the capacity for stunning rudeness should they decide a customer is behaving densely. Don't take it personally. In a bountiful society, there are harsh words enough for all.

Can I still find bargains in consumer electronics and clothing?

Sorry, all sold out. It's true that Hong Kong's back streets and bazaars are loaded with cheap merchandise, but most of it is counterfeit or copycat products of suspicious origin and questionable quality. The territory's light manufacturing industry, which once filled local shops with reasonably priced products, has decamped. Today, three out of four residents are employed in the service industry. Anyone need a good consultant? Or a $6 ice coffee?

If goods are so expensive, how do the poor manage?

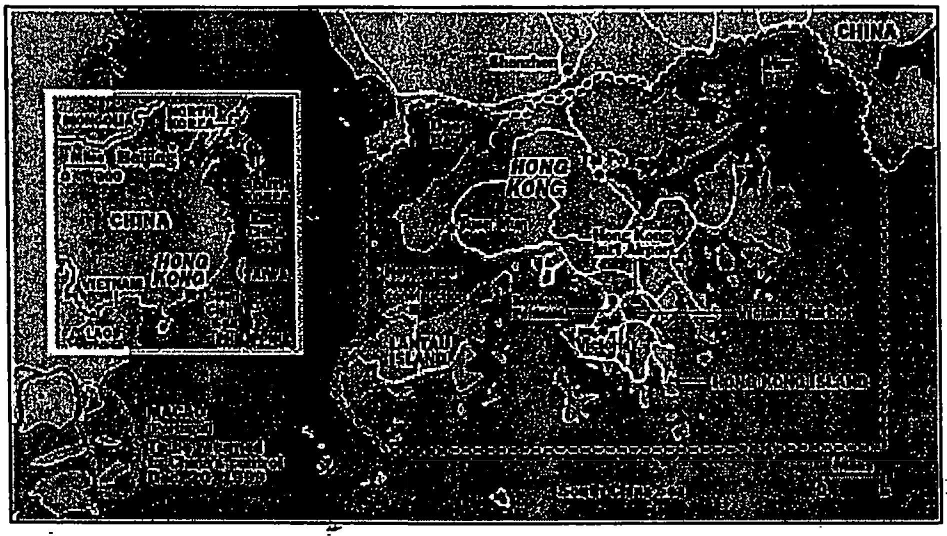
The plight of the truly destitute is a desperate one. This is not a welfare society, and the gulf between rich and poor is wide. In 1996, the government spent 7% of its budget on social welfare. The lack of a safety net encourages everybody to work, and the employed get to keep most of what they earn due to low tax rates -- more than half of wage earners pay no tax at all. And the government does help some cope with astronomically high home prices and apartment rents. More than half the population lives in public housing, and many have purchased homes thanks to subsidized mortgages and other assistance.

Shop, shop, shop. Can't I see a play or something?

Culture used to play a poor court jester in a territory where commerce is king and venal is vogue. But Hong Kong has largely shed its image as an artistic wasteland, and today cultural diversions are myriad. The territory hosts several regional arts festivals, the Philharmonic and the Hong Kong Chinese Orchestra, and a boisterous Cantonese theater scene. Religious festivals abound. Hong Kong is also a pop-culture hothouse. It's home to the world's third-largest film industry and serves as a breeding ground for Canto-pop, a treacly transmogrification of Western pop-rock that can leave the listener feeling rather like a glazed donut -- coated in sugar but with a big hole in the middle.

The New York Times
HONG KONG

Hong Kong at a Glance



POPULATION: 6.3 million in 1996, of which 95 percent are Chinese. Only 0.4 percent, or 25,500, are British.

		Hong Kong	Britain	China	U.S.
Per Capita GDP	**In 1995**	**$23,500**	**$18,700**	**$581**	**$26,434**
Life Expectancy	**Men**	**76**	**74**	**68**	**73**
	Women	**82**	**79**	**72**	**79**
Infant Mortality	**Per 1000 Live Births**	**4.1**	**6.2**	**31.0**	**7.3**

What's changing in the handover...

Government titles, uniforms and stationery lose references to the British Crown.
Some public holidays: Queen's Birthday is out, Chinese National Day is in.
National anthem: "God Save the Queen" yields to China's "March of the Volunteers."
New flag features the Bauhinia flower.

...What's not

Hong Kong - From Opium War to 1997 and Beyond

By 1836, 8 million lbs of Opium were illegally smuggled into China. Opium had become the British economic panacea. In the opposite, China had become the largest worst drug case in Human History. Following is a summary of information from various sources.

Hong Kong, Britain's last important colony with population 6.5 million squeezed into a land of only 1,080 square km

In early 18th centry, foreign traders came to China to purchase tea, silk, rhubarb, and other articles. but they paid in gold and silver, the Chinese found little need for the industrial products of the West. The British East India Company's shipments to China were 90 % of gold, and only 10 percent commodities. Slowly the balance began to slip the other way - by Opium.

In 1773, the British illegally smuggled 70,000 kg of Opium through its East Indian Company. Since then the number of Chinese addicts grew exponentially. Other foreign countries, e.g. American and French traders followed immediately to grab their share of fortune.

By 1836, 8 million lbs of Opium were illegally smuggled into China. In that same year, British sold 18 million worth of Opium in China as against the 17 millium worth of Chinese tea and silk which they bought. **Opium had become the British economic panacea. In the opposite, China had become the largest worst drug case in Human History**. In 1838, 9 out of 10 people in Kwangtung and Fukien provinces were addicts.

Writing home, a Yankee named Warren Delano said he could not pretend to justify the Opium trade on moral grounds, "but as a merchant I insist it has been ..... fair, honorable and legitimate".

As a result, both the Chinese central and local government officials were completely corrupted by this addictive drug. The drug traffic caused a disastrous outflow of wealth. Alarmed at the rapid drain of gold and silver, the Emperor appointed Lin Tse-Hsu to be the imperial commissioiner charging him with suppression of the Opium traffic.

Twice Lin wrote to Queen Victoria to seek her intercession. In his first letter, Lin urged the Queen to stop poppy cultivation and manufacture. In his second well known letter, he stated in part :

*The wealth of China is used to profit the barbarians ..... By what right do they in return use the poisonous drug to injure the Chinese people ? ....***Let me ask, where is their conscience ? I have heard that the smoking of Opium is very strictly forbidden by your country ..... Why do you let it be passed on to the harm of other countries ?** *Suppose there were people from another country who carried Opium for sale to England and seduced your people into buying and smoking it; certainly your honorable ruler would deeply hate it and be bitterly aroused ..... Naturally you would not wish to give* *unto others what you yourself do not want .... May you, O Queen, check your wicked and sift your vicious people before they came to China, in order to guarantee the peace of your nation, to show further the sincerity of your politeness and submissiveness.*

On March 18, 1839 Lin ordered all foreign Opium traders, Jardine, Innes, Dent, and others to surrender their Opium. He also severely punished corrupt Chinese officers who connived with the smugglers. In response, British sent its expeditionary warships and took control of Hong Kong in 1841 following the infamous **First Opium War**. Defeated by the British, China was forced to accept the humiliating **Treaty of Nanking** in 1842. China had to pay a huge **indemnity : 21 million taels of silver, Hong Kong was ceded to the British in perpetuity etc ..... The most ironic point was that Opium, the immediate cause of the war, was not even mentioned.** The Opium traffic got much worse than before.

The phenomenal huge trade profit soon tempted the British and French to seek an excuse to renew their hostilities in order to extend their trades in China. In October 1856, some Chinese officials boarded a British-registered ship but owned by a Chinese resident in Hong Kong, the Arrow, charged its crew with smuggling and lowered the British flag which became British's excuse for another war.

The French, using the murder of a French missionary in the interior of China as their excuse, joined the British military operations - the infamous **Second Opium War**, also known as **The Arrow War.** Defeated again by the British and French, China was force to accepts the humiliating **Treaties of Tientsin** and had to pay 6 million taels of silver indemnity etc ..... In the further negotiation in Shanghai, **the importation of Opium was even legalized.**

The Chinese, however, refused to ratify the treaties, and the allies resumed their hostilities, captured Peking (Beijing). Immediately, **British and French looted all the precious Chinese national treasures, ancient artifacts they could find in the Beijing city and then burned the famous Summer Palace.**

In 1860, China was forced to sign the **Peking Convention**, in which China was forced to observe the Treaties of Tientsin. China also had to pay an increased **indemnity - 16 million taels of silver and Kowloon and Stonecutters Island were ceded to British etc .....** Foreign countries had now gained unrestrict right to legally import the Opium drug to China. China had became the **"Sickman of the East"**.

In **1898**, British obtained the **New Territories under a 99-year lease, rent free.**

After losing the 2 infamous Opium War, China started to disintegrate. Close on the heels of the British came the French, American, Russian, Germany, other European countries and then came the Japan ....

Foreign powers introduced a whole century of humiliation and many other humiliating unequal treaties (more than 1,100 treaties) onto China. China had become a semi-colony country. China was not freed from this Unequal Treaty System and the addictive Opium drug until 1943.

Finally, the Ching dynasty was overthrown ...... Then, after 14 long years of **WWII with Japanese**, then resumed the interruped **Civil War** for another 4 years un-ended with Communist took over mainland and Nationlist forces retreated to **Taiwan**, then suffered another 30 long years of various irrational political chaos, China has now slowly regained her strength.

At the same time, Hong Kong underwent its own economic and social miracle :

Hong Kong grew rapidly in part because the unsettled conditions in China. In the 1850s, the Taiping rebellion erupted in south China, sending tens of thousands of refugees to Hong Kong. Similar waves of refugees repeated many times - the Warlord era, the Japanese Invasion, the Nationalist-Communist Civil War, cutting down of the intellectual Hundred Flowers movement, the unscientific Great Leap Forward, and the destructive Cultural Revolution. **These millions of refugees from the mainland China provided the needed labour force for the economic miracle.**

HK has no natural resources. But its people prepared to work very hard for very little. In the 50s, majority of HK people were desperately poor. They huddled in the tenement blocks, several families to a unit. They built squatter huts on rooftops or hillsides. Often a family of 8 shared only one bed. Life in 50s and 60s was really harsh.

Starting with textiles, Hong Kong factories branched quickly into garments, plastics, electronics, other light industrial products, and later the economy began to diversify from manufacturing into finance. In 1970s, Hong Kong strived and became one of the most industrialized societies in the world.

The Heritage Foundation, one of the America's leading "thinktanks", has rated HK as the most free economy in the world. **For the 3rd year since 1995,** the Geneva-based World Economic Forum, Davos, and the Switzerland's International Institute for Management Development, Lausanne, placed HK in the top three of the world's most competitive economies in their annual reprots - with the United States and Singapore.

HK is now one of the wealthiest economies in the world and second only to Japan in Asia. It is the 8th largest trading place in the world. Its container port is the busiest in the world. Its international airport handles more international air cargo than any in the world except Tokyo's. With China's economic opening, HK's economy has been transformed. Hong Kong-funded factories employ over 4 million workers in China. As a result, Hong Kong has undergone a dramatic transformation from a manufacturing to a services economy.

Today, it is Asia's principal hub for the regional headquarter operations of multinational companies, Asia's leading capital market outside Japan, and plays a key role in rasing funds for emerging Chinese enterprises. It is one of the epicenter of the dramatic developements of massive infrastructure-building drive occurring across the Asia-Pacific region.

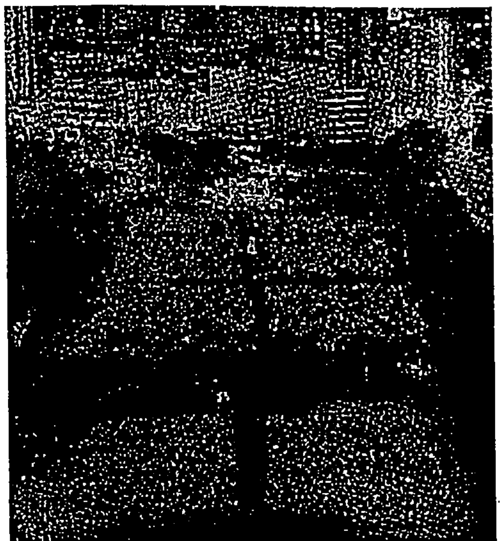
Hong Kong is ranked as the U.S. 13th largest trading partner. It is estimated that 60 % of all the new investment in China are provided by HK. **With less than 1 % of China's population, HK produced 1/5 of the mainland's wealth.**

Hong Kong is now being a British colony for 156 years.

The 99 years lease of the New territories will soon be due in the year 1997 June 30.

Once again, the negotiation between China and British resumed after the 2 infamous Opium War. In 1984, China and British signed a Joint Declaration that Hong Kong will be returned to China but will remain as an autonomous Special Administrative Region with its own government and legal system for another 50 years. Under the formula of "One Country, Two Systems", Hong Kong will continue as a captalist economy and international business center, operating under the rule of law, with its cosmopolitan way of life unchanged for 50 years beyond 1997. This is an internatinal agreement registered at the United Nations - and the future Basic Law of Hong Kong, which was adopted by China's National People's Congress in 1990 as part of China's constitution.

After Hong Kong is returned to China in 1997, another neighbouring **colony Macao will also be returned to China by the Portuguese on December 20, 1999.**



Approx. 40,000 candle lights on June 4th night 1996 in the Victoria Park, Hong Kong.
Approx. 50,000 Hong Kong people turned out on June 4th night 1997.

Holding flickering candles high against the night and singing freedom songs, about 50,000 people in Hong Kong defied China's threat to democracy there. They all joined at June 4 night to honor the victims of the 1989 Tiananmen Square Massacre and call for democracy, freedom and protection for basic hunan rights. Each demand is, by Beijing's definition, a subversive thought which China's leaders have ruthlessly tried to banish from the minds of its own 1.2 billion people in the People's Republic.

The crowd clapped and cheered when speakers from the multi-party organizing committee, the Hong Kong Alliance in Support of the Patriotic Democratic Movement in China, called for continued pressure for reform in China and Hong Kong after 1997. **"It is the time for our test"** Cheung Man Kwong, a spokesperson told the crowd. **"The night is long and so is the road.** However, the candle in our hands demonstrates the children of the Chinese race have a strong heart for the democratic fight." Cheung insisted the movement will continue to work peacefully. "We'll not accept that we are a subversive organization and the Hong Kong people will not accept it either," he said. At least **one million people marched through the streets of Hong Kong after the massacre in Beijing 8 years ago,** and the crowds dropped sharply in the following years. But this year's crowd appeared larger than the one in 1996 and showed average people aren't giving up despite their worries about what 1997 may bring.

The few hours dignified candle light ceremony, which moved many to tears, was given added poignancy with the knowledge that this could be the last such tribute to take place before China takes over the rule of Hong Kong in July 1st, 1997.

Until Tiananmen, Britain's only objective had been to protect its own lucrative relationship with Hong Kong; it had certainly never, in the hundred years of its presence there, considered the establishment of meaningful democratic institutions. **The tremendous impact of Tiananmen Massacre forced the British government, for the first time, to consider the future from the point of view of the people of Hong Kong, and not just from the perspective of British trade.**

Something had to be done. Christopher Patten, the last governor, whose mandate became to enhance what political freedoms could be institutionalized before the handover. Working within the agreements signed earlier by Britain and China, he had little room to manoeuvre; but he did manage to establish a democratically elected legislative concil, albeit one with a complex and partly indirect voting structure.

Beijing reacted angrily to all his moves and called him the serpent, whore, and "sinner for a thousand years".

First, China's hand-picked preparatory committee in Hong Kong **voted 149-1 to immediately abolish Hong Kong's first fully elected legislature** after this year's handover and replace it with appointed pro-China legislators and other loyalists. **The lone adviser was dismissed.**

Then more shocking when a senior Chinese officer indicated that Beijing will require proof of loyality from senior civil servants and a pledge that they will accept the authority of the rubber-stamp legislature. Any senior civil servants who do not make their loyality clear will lose their jobs. By undermining the elected legislature, China is violating key provisons of the joint declaration. And if those rights can be violated, what about others ?

Immediately, thousands lined up to apply for a British semi-passport, a travel document. The final count of the crush is more than 230,000. almost half of which came in the week before the deadline. The panic and desperateness alarmed Beijing. China answered the frenzied rush for the British travel semi-passport with the consoling words of an advertising campaign. Beijing immediately ran ads in both English and Chinese newspapers inviting Hong Kong's people to phone in with their obvious concerns. Rather than reverse its decisions, Beijing government offered only talk therapy.

Many pro-China supporters have also secretly prepared for the worst. Mr. Tsang Yok-sing, **once a street-fighting Maoist during the Hong Kong's Cultural Revolution riots, now head of Hong Kong's leading pro-China political party and a steadfast supporter of China for 30 years,** was waiting in line for medical examinations to clear him for emigration to Canada. He was part of his wife's family application. The story broke out in 1994 just before the election in 1994, causing Mr. Tsang and his party no end of embarrassment. This was **clearly NOT an endorsement of Hong Kong's future under Chinese sovereignty by the HK leading pro-China political party leader.** Due to public outcry, he had to give up his application.

The reason : Beijing may well opt to maintain Hong Kong's rule of law. But it can use its appointed legislature, which will replace the current elected body, to institute a "Rule of Repressive Laws".

Many people here said they came out not just to honor those slain in Beijing but to demand that Hong Kong's freedoms remain untouched. **"This is a test thermometer of human rights in Hong Kong after 1997," said Martin Lee. "If we cannot hold it in the future, then we can no longer see Hong Kong as "One Country, Two Systems", China's promise for its concept of autonomy for the territory which will also serve as a model for Taiwan.**

A committee of 150 people carefully picked by Beijing to oversee the transition to Chinese rule is set to name a 400 member electoral college. That group will then have to decide who will rule Hong Kong after 1997. However, none of the candidates for the chief executive has ever fought in any Hong Kong election. They will then remove all the elected lawmakers like Martin Lee who had won a landslide victory in the last election.

In October 1996, the Chinese foreign minister Qian Qi-shen told the Asian Wall Street journal that Hong Kong activists would not be able to mark the 1989 Tiananmen Square Massacre. He was responding to a question about whether China would permit commemorations to continue after the British colony is handed over to China. Qian's answer obviously implied that Beijing would not really treat Hong Kong as an autonomous special asministrative region.

This had immediately triggered series of protests from Hong Kong people. **"Of course we will continue commemoration."** said Cheung Man-kwong, a leader of the Hong Kong Alliance in Support of Patriot Democratic Movements in China, **~~"Commemoration is not illegal under Hong Kong's LAW. China~~ cannot just single out on the law book that the June 4 commemoration is illegal, while allowing patriotic activities to be held in Hong Kong, such as fund-rasing galas for victims of flood in southern China."**

Then, Chinese foreign ministry spokeman Shen Guofang explained that Mr. Qian's remarks had been **"wrongly extended"** and marked no shift in Chinese ploicy on posthandover Hong Kong. "Hong Kong people will have full freedom of expression, but all freedoms must be within the limits allowed by law," Shen said.

In October 1996, the Chinese government forced a group of Hong Kong politicians flying into China to return to Hong Kong before they could deliver a 60,000 signatures petition opposing Beijing's plans to scrap Hong Kong elected bodies and replace them with appointed councils.

In October 1996, Wang Dan who was a prominent student leader of the 1989 democracy movement and was later jailed for 3 and half years. He was again formaly charged after 17 months detention. Wang Dan was detained May 21, 1995 after signing a petition calling for reform in 1995. He was again sentenced to another 11 years for conspiring to subvert the government.

Chen Ziming, accused by the government as a "black hand behind the black hands" at Tiananmen Square, was originally sentenced to 13 years. He was paroled in May 1994 on medical grounds but was reimprisoned on June 25, 1995. Diagnosed with testicular cancer, he was "released" on medical parole on November 6, 1996 but effectively became a prisoner in his own home.

Many other activists on the mainland have also been recently sentenced to re-education through hard labour, forced to flee China, and charged with subversion.

Beijing affirms that no trial is needed because "re-education through labour for 3 years" is no judicial punishment. But, it also **tells us that the system is seriously flawed if the government may arbitrarily impose "few years of re-education through labour" on any Chinese citizen without any legal proceedings or charges.** Wang Dan and other's cases had caused great concerns and protest from Hong Kong.

Beijing also plans to garrison as many as 10,000 army soldiers in Hong Kong.

On December 11 1996, the hand-picked committee, as expected, had decided Tung Chee-hwa to be Hong Kong's first post-colonial chief executive. Tung's family company was on the verge of bankrupty during the oil crisis of 1980's. Part of the successful **rescue plan involved Beijing backing for the $120 million syndicate investment made by Henry Fok in return for 8 % of the shares in the trouble firm when Tung could not get any financial support from Taipei,** leaving many critics to speculate that Mr. Tung is on the hook to Beijing for the past financial support.

"We sincerely hope that Mr. Tung can now prove to the Hong Kong people and the world that he is better than the un-representative system that produced him. **What Hong Kong needs now is not a spokesman for China, but an uncompromising defender of the Hong Kong's freedoms and way of life.**" said Matin Lee.

On December 21 1996, the same China hand-picked committee that chose Mr. Tung had also chosen 60 members of a new provisional legislature that will replace the current elected assembly the moment British rule ends at midnight on July 30. China's decision to scrap the existing legislative council is on the ground that it was elected under unilateral democratic reforms pushed by governor Patten. New election will be called in the spring of year 1998 with new election rules. **both Bar Association and the Law Society have made clear that there is no legal basis for China's action** which has also been widely criticized by countries around the world.

Governer Patten has refused to extend any government assistance or recognition to the provisional legislature. As a result, all the meetings have to be held outside Hong Kong, in the swank state guest house of the Chinese border city of Shenzhen. "This body purports to be a legislature of Hong Kong. Why run away and meet in China ?" asked Martin Lee.

Big controversy was also caused by the recommendation of the legal sub-group of the Prepartory Committee. Among the recommendations are an **end to the legal supremacy of Hong Kong's bill of rights over other statutes, restoring the right of police to ban demonstrations and prohibiting political group from having ties with foreign organizations after July 1.** The irony is all the changes sought by China are designed to rollback to the old, outdated colonial status.

In the midst of escalating furor over these Beijing-backed proposals, Mr. Xi Yang, working for Hong Kong Ming Pao newspaper, was suddenly released on parole after serving 3 years of a 12 year prison sentence for allegedly stealing state secrets. He was arrested in 1993 after writing stories on China's interest rate policy and plans to sell gold on the international market. His release is seen by most observers as Beijing's effort to ease the current public furor.

On Feb. 1 1997, the Preparatory Committee (PC) adopted its legal subgroup's motion and asked the National People's Congress standing committee to declare when the Hong Kong SAR comes into being that the above mentioned 24 Hong Kong ordinances will in whole or in part cease to be in force. However, due to public pressure, the PC made it clear that it no longer insists on reinstating the repealed old colonial ordinances. It will be up to the future SAR to decide how to fill in the lacuna.

Almost all mainland provinces and cities have companies in Hong Kong. China-owned companies in the territory are estimated more than 15,000. Of them only about 1,000 have obtained the central government's permission to do business there. **If they practise "One Hong Kong, Two Systems" after July 1, then Hong Kong's social system and its spirit of the Rule of LAW will be jeopardised.**

In the early 1970s, Hong Kong's colonial administration created an independent agency to target the most hated corruption, extended its authority to business as well as the public sector. The Independent Commission Against Corruption **ICAC now is one of Hong Kong's most respected agencies. It has virtually demolished all syndicated corruption in Hong Kong.**

Anti-corruption was one of the key demands wanted by the students during the 1989 Democracy Movement at Tiananmen Square. 8 years after the massacre that shocked the world, corruption is now become one of the worst problems in China and is getting worse - Out of Control.

Hong Kong people is now really concerned about there might be **corruption spillover** into Hong Kong after July 1st. The authorities in neighboring Guangdong province have now turned increasingly to the ICAC for assistance in battling graft across the border to combat a **wave of corss-border crime.**

On April 9, 1997 in view of the extremely fruitful North America Fund Raising Tour made by Martin Lee who had successfully explained the importance of their party in HK to the overseas Chinese communities in North America, Hong Kong's future chief executive Tung Chee-Hwa immediately released his plans to curb Hong Kong's political freedom after July 1. **The plan would curtail demonstrations and foreign funding for political parties. Under the plans, societies and political parties would have to be registered and might be refused registration if they are known to have ties to or receive donations from foreign political groups or individuals.** A series of revisions by Tung's office in response to the outcry did little to mollify critics.

In May 1997, municipal officials had prohibited a sculpture called **Pilar of Shame** depicting about 50 painfully twisted bodies piled in a heap, from being exhibited during the summer in various Hong Kong parks because of the negative reaction from Beijing. The sculpture will be unveiled at the candlelight vigil on June 4 night.

Just barely one month before China could scrape the Hong Kong's elected legistlative council, the council officially passed **a historic motion to restore the justification of the student Democarcy Movement in 1989. The voting result : 29 to 1.** To avoid embarassment and not dare to face the judgement by the history and Chinese people in the future, there were **25 legislators absent in this historic voting.**

On June 1, 1997 approx. 5,000 Hong Kong residents took to the streets to remind their future rulers they have not forgotten the June 4 Tiananmen Massacre and demanded Beijing to reverse its verdict that the democracy movement was counter-revolutionary.

"No one really wanted June 4 to happen," Mr. Tung Chee-Hwa told reporter. "But over the past 8 years, some people have continued to persist on the issue of June 4. Perhaps they should look forward." "Why doesn't he ask the people of Hong Kong to forget the Opium War ?" said activist Hon Donfang, "That was also the past."

On June 4 night 1997, approx. **50,000 people turned out for the annual vigil. Of all the activities in Hong Kong, the biggest one is still the June 4 commemoration. It clearly reminds Beijing that**

Hong Kong people want more than merely a desire to make money.

The march and commemoration could be the last time in HK. After July 1, permission will be required. "In theory, the decision will be made by Tung Chee-Hwa. In reality, it will be up to Beijing." said Martin Lee.

A recent poll in June has indicated that more people were satisfied with the performance of the last colonial governor Pattern than Mr. Tung. As for the non-elected provisional legislature received a dismay rating of only 7 % which clearly underlines it has no legitimacy among HK people.

"If Beijing in the past 40 years had governed China better than Hong Kong, then no one in HK will oppose the handover." Lee Yee, the editor of Ninety magazine said.

July 1st, 1997 is definitely a historic **Happy Day** for all Chinese - the return of Sovereignty of Hong Kong to the motherland China. However, should the Chinese government **fail** to provide a better life to the HK people than the old British colonial government, then the same historic day, July 1, will also be remembered as a **Shameful Day** by all the Chinese as well.

At last, at midnight June 30 1997, for the 68th time this century, the Union Jack was slowly slided permanently down the colonial flagpole in HK. At one minute after the midnight on July 1st, China's flag rose in HK. President Jiang Zemin declared that a historic wrong has been righted and HK is coming home. The five-days celebration began. HK is now transformed from Britain's last major colony to a wealthiest, most advanced, free, democratic city in whole China.

Mr. Tung was surprisingly frank in his hallmark address, given the large number of high-ranking Communist leaders in the audience. "Democracy is the hallmark of a new era of HK," he declared. "The people of HK will continue to enjoy the freedoms of speech, assembly, association and the press". However, no one knows how well Beijing will respect the Rule of Law which is the very base of HK's prosperity.

On July 1st 1997, the first day after handover, with the china's top leaders still in town **about 3,000 HK people marched through HK demanding an end to one-party dictatorship in China.** This was the first peaceful demonstration after the handover. Police made no effort to halt the march. "It is a very positive sign that we could do today what we have done in the past," praised the organizer.

The deposed Democratic Party legislators have set themselves up as a "shadow opposition" to monitor the appointed pro-China legislature that replaced them. "What could be more unusual ? The elected legislators are sitting in the public gallery, and the appointed people are in their seats," said Martin Lee. 10 of the appointed legislators were defeated by Democratics in the 1995 elections.

An appeal court will hold a hearing on whether the legislature that China installed in HK after July 1 is legal. The court date was July 29. Due to its urgency, it is now moved earlier to July 22.

The result : Court of Appeal held that SAR courts, being regional courts, have no power to call into question any decision made by the National People's Congress (NPC) or any of its organs. On these lines, may SAR courts examine any of the laws adopted by the NPC ? If they may not, how can SAR courts safeguard "One country, Two systems" ? Imaginably, future legal actions will continue to arise.

On July 8, 1997 one week after the handover, the appointed HK government introduced proportional representation for the lone 20 out of 60 seats to be decided by universal suffrage. **The revised voting system is designed to reduce the Democracy party with the most popular support to a tiny minority in next year's legislature election.** Martin Lee called the amendments "a farcical distortion of the purpose of elections, which is to represent the public will."

Feb 9, 1998 selected by a small circle of 400 people, the 36 members of the National Peoples's Congress (NPC) in HK are about to attend the 9th NPC meeting in Beijing. With poor representativeness, HK people expect their NPC deputies to speak out for the 6.5 million HK people at the "highest organ of state power".

Feb 19, 1998 despite Asia's economic turmoil, HK massive cash store is swelling. Its reserves are expected to be a staggering sum of $98 billion by Mar. 1999. Government throughout southeast Asia are cutting heavily, HK tried to soften the blow with surprise tax breaks for homeowners, tourists and corporations to try to win back the confidence of investors.

Recently at the Chinese People's Political Counsultative Conference, HK leftist Xu Simin suggested Tung should tighten the RTHK radio station in HK so that it cannot criticize SAR's policies in HK. His comments immediately caused an outcry in HK. Jiang Zemin quickly pointed out in his speech that NPC deputies elected in HK only participate in running on behalf of their HK compatriots and ought not to interfere in the HK SAR govenment's business."

In March 1998 new cases have rocked HK and fuelled fears corruption is spreading under Chinese rule. Four officers in the ICAC were suspended on suspicion that they were feeding outsiders with confidential information. Two others were accused of illegally borrowing moneny from a colleague and other misconduct.

Xinhua New Angency used to be mainland's effective embassy and intelligence gathering base in HK before the handover. Emily Lau, a pro-democracy campaigner asked to see her Xinhau file under 1996 privacy law. The law gave Xinhau 40 days to respond to Lau's request but did not response for 10 months. After Lau complained to the privacy commissioner. Xinhua replied that it had no file on her. But the justice secretary decided not to prosecute Xinhua for violating HK's privacy statute.

Also, a senior Prosecutions Division official, having studied the ICAC's report, agreed that newspaper publisher Ms Aw and three executives of the Hong Kong Standard for conspiring with Ms Aw to defraud advertisers by inflating circulation figures, should be prosectued. The Director of Public Prosecutions concurred. However, the Secretary for Justice did not agree and had decided not to prosecute Ms Aw who sits on the National People's Congress and the Chinese Peoples's Political Consulative Conference. Public outcry have intensified and many worried that the law won't apply to people who have connection with Beijing.

In April 1998, HK government rushed through the Beijing-selected legislature before it is dismissed for May 24 1998 election, a bill that would replace the term "the Crown" from legal code with "the State". Sidney Jones, executive director of Human Rights Watch's said, "Once that principle is eroded, the protection of human rights is in grave jeopardy." Other legal experts said the bill would grant "sovereign immunity" to Beijing's representatives in HK, effectively putting them beyond the reach of the territory's Rule of Law. It is highly unlikely that this bill can be overturned, as the new electoral laws are designed to make it unlikely that members of pro-democracy parties will ever regain control of the legislature.

Whether Hong Kong, "The Pearl of the Orient", will continue to shine brilliantly solely depends on how wisely China will implement the interim "One Country, Two Systems".

Whether HK can finally be fully integrated into its motherland under "One Country, One System" solely depends how wisely China will implement its own long overdue **Fifth Modernization - Political Modernization.**

The amazing story of Hong Kong continues ....

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