

Reese, K.

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### Mainland China and Western Trade Credits

Dr K. Reese, Johannesburg \*

**The author discusses the question whether autarky will remain a central national policy goal in Peking after the present ruling group relinquishes power. He comes to the conclusion that, although China's foreign trade particularly with the Western world will expand rapidly, Peking will continue its abstinence from foreign trade credits.**

Mainland China is the only socialist country virtually free from foreign debt, its currency ranks among the most stable in the world and Peking displays a definite aversion to Western trade credits. This is a most unusual mix for a country the size of Mainland China and with its comparatively underdeveloped industrial structure.<sup>1</sup> This attitude is all the more surprising because Western trade credits are readily available to Peking, at conditions which would make less creditworthy borrowers, like Uganda, cringe with envy. As an official of the National Westminster Bank put it: "Our experience has shown that the Chinese are non-committal on the subject of medium and long-term credit — as a country they prefer to deal on a cash basis."<sup>2</sup>

Even though rumours persist among optimists that Western trade credits will become more acceptable to Peking the evidence contradicts such rumours. Just a few months ago China imported a cold-rolling mill from Germany at a price of DM 650 mn. This was a major import contract but again the Chinese have kept to their principle of not entering into debt with foreign countries and the plant is being paid for on delivery.<sup>3</sup> This principle of not getting into debt with foreign countries is undoubtedly an intriguing one and merits closer analysis. Recent pictures of Chairman Mao show biology at work, as the Economist euphemistically put it, and it is widely believed that major changes

in the foreign policy of China might be imminent when he dies.<sup>4</sup> This paper therefore in particular is trying to establish whether or not the above principle of abstinence from readily available trade credits has roots other than Chairman Mao's known xenophobia to any dependence on outside interests. Phrased differently the question is whether autarky will remain a central national policy goal in Peking after the present ruling group of men relinquish power.

#### Autarky

It may be wise to note carefully the assessment of the American Deputy Assistant Secretary for the Far East, M. Green, that the outside world has little leverage on the course of development in China because it is tightly controlled by a small group of men singularly impervious to ideas from abroad. Most vital to note is Green's description of the common bond that welds the seventy or so top Chinese leaders together. Green pertinently stresses that these Chinese leaders have together "gone through the cruel and annealing experience of the long march, the Yunan Caves, and the struggle against the Japanese, the Chinese Nationalists and the United Nations in Korea. These are men who have grown tough and hard and intransigent in the course of this long struggle. They are men who are dedicated Maoists, who are Sinocentric in their outlook, and whose suspicions and inherent xenophobia have been fed by deep resentment of the indignities which China suffered at the hands of the West in the 19th century. In the course of this long common struggle the leaders of Communist China have experienced what in their eyes has been a triumphant success,

\* Senior Lecturer in the Department of Business Economics at the University of the Witwatersrand.

<sup>1</sup> W. W. Whitson (ed.), *Doing Business with China*, Praeger Publishers, New York 1974, p. 392.

<sup>2</sup> A. Rowley, *Reluctance to buy on credit may soon dissolve*, in: *The Times*, March 21, 1973, Special Report on China Trade, p. III.

<sup>3</sup> *The Month in Brief, China*, in: *Asia Research Bulletin*, June 30, 1975, p. 94.

<sup>4</sup> *When old faces go*, in: *The Economist*, October 8, 1975, p. 9.

and this flush of success has contributed to the absolute certainty they feel that the course on which they are embarked is the only one for China. They have a monumental conviction as to the rectitude of their position."<sup>5</sup>

In the museum in Yunan the box of writing ink used by Chairman Mao in 1937 is preserved and on this box he inscribed "strive for autarky"; a policy position of seeming unaltered validity in Peking today. Pundits on China assert that Mao genuinely believes that he can virtually remould the whole nation in his own image, that he can transform the Chinese people into 700 mn mini-Maos.<sup>6</sup> Should the Chairman indeed succeed in this rather herculean undertaking, then autarky would truly remain an unalterable tenet of Chinese foreign policy for ever after. If Mao, however, fails in his transformation efforts, then the new leader who succeeds him might adopt a more relaxed attitude on foreign trade credits — if there are no considerations other than Mao's personal message not to strike a bargain with the West.

Whatever the decision of Mao's successors, it must be mentioned that autarky is a viable policy for Mainland China because all essentials to keep the country going can be produced by one of the diverse provinces of this continental-scale country.<sup>7</sup> Foreign trade is not, nor will it ever be, a matter of grave economic significance for Peking — quite different from, say, Germany with its extremely high degree of dependence on international trade. Peking's interest in foreign trade extends in principle only to procuring advanced technology that is not available from within its borders, but nevertheless essential to fulfil the national economic plans. Foreign trade, if valued in Yuan at the exchange rate quoted by Peking, accounts for a meagre 5–6 p.c. of Mainland China's gross national product. If one takes the US dollar as the basis for these computations, then Peking's foreign trade accounts for 2 p.c. of its GNP only. Peking can quite legitimately regard itself as truly self-sufficient.<sup>8</sup> Furthermore, as in other socialist countries, Peking can easily control its foreign trade because only state-owned trading houses are licensed to deal with foreigners. The eight specialized state trading houses are kept on a very short leash by Peking.<sup>9</sup> As foreign trade also involves hard currencies, which can be obtained from Peking only, the net of con-

trols is quite literally tight.<sup>10</sup> The instruments to maintain autarky as a national policy goal are thus there. It remains therefore now to enquire whether there are other reasons than Chairman Mao's message for autarky that might keep future Chinese leaders on the same track. The most vital of such other reasons that must now be considered is certainly China's relationship with Russia.

### Relationship with Russia

During the 1950s Russia granted medium-term trade credits to China and also gave military loans while China was involved in the Korean War. The Russians supplied complete sets of factories to assist in building up a heavy industry in China.<sup>11</sup> When the two countries fell out over the question of Marxist purity in 1960 this brotherly help from Russia came to an abrupt end. All Russian technicians left immediately and no further know-how was provided.<sup>12</sup> The Russians even cut back the gasoline shipments on which the Chinese at that time were sorely relying. Peking had little option but to go all out for a deliberate and far-reaching reorientation of its foreign trade. While only 30 p.c. of Peking's trade was with the West in 1960 and 70 p.c. with communist countries, this ratio has since then been entirely reversed.<sup>13</sup> In the early 1960s Peking concentrated all its energies on increasing the trade surplus with the West and has cut back on imports, despite the hick-ups caused by the desertion of the Russian technicians, to repay all its debt to Russia in record time. In 1963 this aim had already been achieved and China started to import complete factories again; this time from the West. The time when the communist countries were the most important trading partners for Peking has irreversibly gone by.<sup>14</sup>

The split with Russia is a key to understanding Peking's attitude to foreign trade credits. As G. Hawtin very aptly formulated: "China learnt what it considers a hard lesson in the late 1950s — that one should not build too great a reliance on any one nation as a trading partner. This lesson seems to have coloured its home and foreign economic policy ever since. Self-reliance at home has resulted in a surprisingly small volume of external trade for such a large and populous country. It has also bred a healthy suspicion of credit.

<sup>5</sup> M. Green, *Communist China: A Problem in US Policymaking*, in: *Foreign Affairs Outline*, Department of State, No. 11, May 1965, p. 1 and 2.

<sup>6</sup> E. MacFarquhar, *China, Mao's Last Leap*, in: *The Economist*, Brief 6, 1968, p. 2.

<sup>7</sup> Green, *op.cit.*, p. 1.

<sup>8</sup> M. Menguy, *L'Economie de la Chine Populaire*, in: *Presses Universitaires des France*, Paris 1965, pp. 119-120.

<sup>9</sup> Whitson, *op.cit.*, p. 398.

<sup>10</sup> T. Miyashita, *The Currency and Financial System of Mainland China*, The Institute of Asian Economic Affairs, Tokyo 1966, pp. 79-80.

<sup>11</sup> Background Notes, *Communist China*, in: US Department of State Publication 7751, August 1966, p. 4.

<sup>12</sup> S. Klein, *Politics versus Economics, The Foreign Trade and Aid Policies of China*, International Studies Group, Hong-kong 1968, pp. 203-204.

<sup>13</sup> Background Notes, *op. cit.*

<sup>14</sup> Menguy, *op. cit.*

Abroad, China has pursued a trade policy of buying only as much as it sells and, as far as possible, not allowing one supplier nation to gain overwhelming dominance." The result is that Western traders are falling over one another to offer Peking credit facilities which it serenely rejects. As Hawtin puts it: "One of the hardest nuts for exporters to crack has been China's approach to credit." Hawtin felt that as of late this rigidity might be "softening" but is quick to add that "softening" in this context only means that China will consider deals allowing the normal short-term credit, such as 90 to 180 days that are standard practice for most of the world trade.<sup>15</sup> Credit purchases in the real sense of the word are out for Peking and even after Mao's death the key experience with Russia is going to be remembered well by his successors. It fits logically into this political landscape that Peking should be very interested in good relations with the nine members of the EC.

**Relationship with the EC**

While all Western countries qualify as friends under the old Chinese approach of making the enemies of one's arch enemy one's friends, there are some of Russia's enemies that are more palatable to Peking than others — the EC for one. Ideally Peking "would like to see a self-reliant Western Europe based on a self-defence community independent of the United States and able to stand up to Soviet pressure. At the same time such a Europe should also identify its common interests with the Third World and consequently seek to cooperate in the construction of a new international economic order."<sup>16</sup> Europeans indeed found to their bemusement that Peking was "plus Européens que les Européens".<sup>17</sup>

<sup>15</sup> G. Hawtin, Traders look to steady rise after boom year — especially in higher technology, in: *The Times*, op. cit., p. III.

<sup>16</sup> M. B. Yahuda, Chinese foreign policy after the victories in Indochina, in: *The World Today*, Vol. 31, No. 7, July 1975, p. 296.

**Table 1**  
**Trade between the EC and Mainland China**

EC Countries	Volume of Trade (in US \$ mn)			China's Surplus or Deficit Trade (in US \$ mn)		
	1970	1971	1972	1970	1971	1972
Belgium/ Luxembourg	33	25	35	— 12	+ 10	+ 12
Denmark	14	14	18	+ 7	+ 9	+ 1
France	151	183	162	— 11	— 41	+ 45
Ireland	2	4	3	+ 2	+ 1	+ 3
Italy	121	127	163	+ 5	+ 2	+ 6
Netherlands	49	53	55	+ 5	+ 18	+ 35
United Kingdom	187	144	167	— 26	+ 8	+ 11
West Germany	252	232	271	— 83	— 41	— 59
<b>Total EC Nine</b>	<b>809</b>	<b>782</b>	<b>874</b>	<b>— 113</b>	<b>— 34</b>	<b>+ 54</b>
<b>World</b>	<b>4246</b>	<b>4611</b>	<b>5706</b>	<b>+ 120</b>	<b>+ 117</b>	<b>+ 152</b>
EC Nine as per- centage of World	19	17	15			

The Common Market is of interest to Peking also on purely trade grounds because the EC is "China's second largest trading partner after Japan. It is the third biggest export market for China after Japan and Hongkong and the second biggest import supplier to China after Japan. Perhaps more important than the totals of imports and exports is the fact that China . . . successfully converted a trade deficit with the EC Nine into a substantial surplus." Peking furthermore appreciates that the EC provides a well diversified market and that the commercial interchange is not therefore uncomfortably intertwined with the ups and downs of any particular European industry. In fact, "China sells a wide variety of traditional raw materials and modern manufactures to Europe, of which textiles, canned and preserved foodstuffs, raisins, ceramics, bristles, feathers, tungsten and handicraft are among the most important. In return the Chinese buy chiefly machinery and transport equipment, special steel products, non-ferrous metals and diamonds, grain, chemicals and

<sup>17</sup> D. Wilson, China and the European Community, in: *The China Quarterly*, No. 56, October/December 1973, p. 649.

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scientific instruments."<sup>18</sup> Despite all these rather satisfactory sounding statements one must not lose sight of the fact that the EC Nine account for about 15–20 p.c. of China's global trade only. Table 1 will help to put the matter in perspective<sup>19</sup>.

The trade between the EC and Mainland China has, however, various factors in its favour which make it likely that this trade will slowly expand in future. For one, "the progressive liberalization of discriminatory quotas on imports from communist states which has been gradually pursued in recent years by the EC Nine individually and by the Six collectively will continue to remove obstacles to Chinese sales. The EC Commission's Regulation No. 109 of 1970 sets out the basic rules governing this process; and the lists of products freed wholly or partially from restrictions are from time to time added to. China is specifically mentioned, along with North Korea, North Vietnam and Mongolia, in one of these, viz. Regulation No. 2406 of 1971 and the aim of the EC Commission is eventually to lift almost all remaining restrictions." This process of liberalization is eagerly watched by its European promoters, the Peking lobby, viz. those firms which are selling — or hope to sell — equipment and technology to China. As it is well known that China seeks, as far as possible, to balance its trade with each foreign partner an additional incentive exists for the lobby to keep urging the EC Commission along the road of trade liberalization. The fact that Peking's foreign exchange reserves of about \$ 750–1000 mn give China substantial flexibility in multilateral trading is, inexplicably, almost never discussed<sup>20</sup>. To assess the trading potential of Mainland China in a balanced way it is necessary to take a close look at China's global trade data.

#### Global Trade Data

In comparison to the wealth of statistical information that is available in the West on the economies of the East European countries there are preciously few data available on China; indeed there also appears to be little available in Peking itself.<sup>21</sup> In the 1960s Peking furthermore imposed a statistical black-out and estimates by various foreign government and academic economists had to be relied upon. Fortunately, however, this ban on official data has been eased and Peking again publishes information on its foreign trade<sup>22</sup>. On the basis of such recently published trade data Table 2 was constructed which gives a

bird's eye view of the essentials that are of interest in the context of this paper.

**Table 2**  
**Global Trade of Mainland China – Selected Years**  
(1975 US \$ in bn)

Years	Exports f.o.b.	Imports c.i.f.	Surplus/Deficit
1952	0.88	1.01	— 0.13
1957	1.62	1.44	+ 0.18
1958	1.94	1.82	+ 0.12
1959	2.23	2.06	+ 0.17
1960	1.96	2.03	— 0.07
1961	1.53	1.49	+ 0.04
1962	1.53	1.15	+ 0.38
1963	1.57	1.20	+ 0.37
1964	1.75	1.47	+ 0.28
1965	2.04	1.84	+ 0.20
1966	2.21	2.03	+ 0.18
1967	1.95	1.95	± 0
1968	1.94	1.82	+ 0.12
1969	2.03	1.83	+ 0.20
1970	2.05	2.24	— 0.19
1971	2.41	2.31	+ 0.10
1972	3.08	2.84	+ 0.24
1973	4.90	4.98	— 0.08
1974	5.90	6.70	— 0.80

Table 2 illustrates that, on average, Mainland China ran a trade surplus and was able to build up a sizeable cushion of foreign exchange<sup>23</sup>, referred to above. The main sources of this foreign exchange surplus must now be identified and commented upon.

#### The Main Sources of Foreign Exchange

Most of Mainland China's foreign trade contracts are negotiated at the Chinese Export Commodities Fair which is held twice a year. Businessmen of over 90 countries attended — strictly by invitation only.<sup>24</sup> In these foreign trade contracts the Chinese, however, attempt to balance their exports and imports as far as feasible with each country concerned, as outlined above. Table 2 shows, nevertheless, that on average Peking ran a positive global trade balance and almost all this surplus can be attributed to one source, Hongkong. Hongkong provides between 30 and 40 p.c. of China's foreign exchange earnings.<sup>25</sup> Apart from Hongkong it is Singapore on a much lesser scale and Malaysia to an even lesser extent that provide Peking with its hard currency surplus. Hongkong, however, is the undisputed kingpin among the hard currency providers of Peking and because of its geographical position is virtually a captive market.<sup>26</sup>

<sup>18</sup> *Ibid.*, p. 655.

<sup>19</sup> *Ibid.*, p. 656; adapted from Table on China's Trade with the EC.

<sup>20</sup> *Ibid.*, pp. 659–660

<sup>21</sup> G. H a w t i n, £ 50,000 a year now available to give advice and encouragement to the Businessman, in: *The Times*, op. cit., p. IV.

<sup>22</sup> T. G. R a w s k i, *Recent Trends in the Chinese Economy*, in: *The China Quarterly*, No. 53, January/March 1975, p. 1.

<sup>23</sup> Adapted from *Economic Indicators for China 1975*, in: *Asia Research Bulletin*, June 30, 1975, p. 95.

<sup>24</sup> People's Republic of China, *Barclays Economic Intelligence Department*, London, May 19, 1972.

<sup>25</sup> *Offshore — A survey of Hongkong*, in: *The Economist*, July 19, 1975, p. 9.

<sup>26</sup> C. M a c D o u g a l l, *Chinese trade since the Cultural Revolution*, in: *The World Today*, Vol. 28, January–December 1972, pp. 27–28.

That Hongkong is effectively captive to Mainland China cannot be disputed. "Supporting about four million people in a territory roughly the size of Cornwall, Hongkong is unable to meet its own food requirements. Food must be imported and China is by far the most important source. Pigs, chicken, fruit, vegetables and fish have to be imported. Hongkong cannot pay for them by means of exports since it produces little of what China needs . . . There is a massive trade imbalance between the British Colony and China. In 1971, for instance, Hongkong imports from China were worth US\$ 550 mn whereas its exports to China were worth no more than US\$ 10 mn. The difference is made good by a cash payment by Hongkong to China in hard currency."<sup>27</sup> With foreign exchange thus available trade seems set to expand with the West unless a certain commercial malpractice of the Chinese develops into a stumbling block, viz. their once only purchasing practice.

#### Once only Purchasing Practice

This malpractice — at least in the eyes of Western industrialists — cannot simply be seen as an aggressive policy to nurture indigenous design and engineering capabilities, but runs much deeper.<sup>28</sup> The following self-explanatory description of what is going on was given in a recent Asia Research Bulletin, where it was stressed that "China has always adopted a policy of a 'once only' purchase from which other similar plants can be 'home grown' as part of China's policy of self-reliance and self-sufficiency. Good examples of China's technique are two steel mills, one hot and one cold, sold to China a year ago by Japan and West Germany, respectively, at a cost of about US\$ 200 mn each. No-one is ever likely to sell another steel mill to China, although these two mills represent only a fraction of China's ultimate requirements, but it can be confidently asserted that subsequent mills will be 'home grown'. It has become an established Chinese practice to prolong negotiations with foreign industrialists in order to acquire Western and Japanese technology, until all the necessary technical data have been harnessed to ensure that the technology is of the highest standard, and that it is capable of adaptation to Chinese conditions. A deal can only move towards a successful conclusion if all the necessary technology is transferred to the Chinese purchasers during the course of negotiations, or guaranteed during plant construction. The level of technology and the quality of the plant are usually of greater concern

<sup>27</sup> A. Rowley, Hongkong, provider of hard currency, in: *The Times*, op. cit., p. VI.

<sup>28</sup> J. Baranson, Technological improvement in developing countries, in: *Finance and Development*, Vol. 11, No. 2, June 1974, p. 3.

to the Chinese than the final price. The overriding concern is to secure the technology behind the equipment and thus ensure the means of replication. The 400 or so Chinese technicians about to be trained in West Germany and Japan will assuredly master every detail, every nuance of modern steel making."<sup>29</sup> This malpractice of replication will have to be discussed with Peking before truly long-term improvements in foreign trade relations can become a reality; an improvement the EC Commission seems set to try for.

#### Epilogue

Foreign trade with Mainland China looks all set for slow but steady expansion; with Hongkong ready to provide the base for credit deals if trade credits ever become acceptable to Peking — the Bank of China in Hongkong in any case has all the required facilities ready to go ahead.<sup>30</sup> More likely, however, Peking will continue its abstinence from foreign trade credits which are seen by Mao and his probable successors as a first and fatal step to renewed dependence on outsiders who may abrogate their commitments in the same rude manner the Russians did in 1960. The foreign trade of Mainland China is bound to continue to be treated as an appendix to the national economy only and autarky can be expected to remain the key word in Peking in the foreseeable future.<sup>31</sup>

All those who work themselves into euphoria about the "potential" of Mainland China as a market for their products — and there are quite a number of such optimists around — should take careful note of the most pertinent warning by D. Bonavia that "the idea that China is the largest consumer market in the world is misleading for the purpose of foreign trade. China regards herself as an underdeveloped country. She does not intend to spend substantial amounts of foreign exchange on importing consumer goods, since her own light industries are capable of making most things she considers necessary."<sup>32</sup> As a closing thought one should mention that Mainland China is believed to have significant potential as an oil producer — with oil-hungry Japan as a secure market right at its doorstep. Should this oil bet come off, then all the aforesaid might have to be radically reassessed; irrespective of who follows Chairman Mao. Oil has changed many things in the world and it may just do the same for Mainland China.

<sup>29</sup> China's Industrial Self-Sufficiency Policy, in: *Asia Research Bulletin*, May 31, 1975, p. 85.

<sup>30</sup> *Offshore* — A survey of Hongkong, op. cit.

<sup>31</sup> Klein, op. cit., p. 2.

<sup>32</sup> D. Bonavia, Promising future for firmer commercial links, in: *The Times*, op. cit., p. I.