

CHINA IN 2003

OUTLINE

- THANKS. THIRD PRESENTATION SINCE SEPTEMBER 2001. UNDERSTAND NOT DUE TO QUALITY OF THE SPEAKER BUT IMPORTANCE OF THE SUBJECT.

- TODAY, I WILL ADDRESS A NUMBER OF TOPICS:
 - THE MACRO ECONOMIC SITUATION
 - CHINA'S IMPORT PROFILE AND WHERE CANADA FITS
 - WTO IMPLEMENTATION UPDATE
 - MICRO/MACRO POLICY DIRECTIONS AND THE NEW LEADERSHIP.

- THE BASIC NUMBERS THAT INFORM MY PRESENTATION ARE BEING PROVIDED TO YOU FOR YOUR CONVENIENCE.

- MY PRIMARY OBJECTIVE IS TO PROVIDE YOU WITH INFORMATION AND VIEWS THAT WILL BE USEFUL FOR YOUR BUSINESS AND YOUR UNDERSTANDING OF CANADA'S RELATIONS WITH THE PRC.

- THERE ARE A NUMBER OF DIFFICULTIES THAT YOU HAVE TO OVERCOME IN TRYING TO UNDERSTAND CHINA TODAY FROM A BUSINESS PERSPECTIVE. LET ME JUST FLAG THREE .
- FIRSTLY, YOU MUST TRY TO UNDERSTAND THE IMPACT AND IMPLICATIONS OF ECONOMIC GROWTH. CHINA'S GDP WAS US \$1.3T IN 2002 AND WILL BE \$1.4T THIS YEAR. THIS ADDITIONAL \$100B IS THE ENGINE THAT CONTINUES THE PROCESS OF TRANSFORMING THE STRUCTURE OF THE CHINESE ECONOMY.
- WHEN CHINA'S GDP WAS \$1.2T, IN 2000, THE AGRICULTURAL COMPONENT WAS 15.9%. TODAY, IT IS 14.8%, NOT MUCH RELATIVE CHANGE. BUT IN FACT, SINCE 2000, CHINA HAS ADDED \$180B IN AGRICULTURAL PRODUCTION, \$633B IN INDUSTRIAL PRODUCTION AND \$420B IN SERVICES ACTIVITY.
- WHAT THIS SAYS IS THAT THE SECONDARY INDUSTRIAL SECTOR IS TAKING THE LEAD ON PRODUCTION AND EMPLOYMENT IN CHINA; THAT MORE CHINESE ARE NOW PART OF THAT SECTOR, AND LIVING IN CITIES; THAT THEY ARE DEVELOPING URBAN CONSUMPTION HABITS; THAT THIS IS FURTHER CONTRIBUTING TO THE EXPANSION OF THE TERTIARY SECTOR.
- THESE DEVELOPMENTS ARE CREATING NEW OPPORTUNITIES FOR BUSINESS, FOR EXAMPLE CLOTHING FROM PORTS INTERNATIONAL OR FOODSTUFFS FROM MAPLE LEAF FOODS OR LIFE AND ACCIDENT INSURANCE FROM SUN LIFE AND

MANULIFE. THEREFORE, MAKING SENSE OF CHANGE AND HAVING IT WORK TO YOUR ADVANTAGE IS THE FIRST CHALLENGE.

- THE SECOND PROBLEM INVOLVES DESCRIBING AND USING INSTITUTIONS IN TRANSITION. FOR EXAMPLE, THE LEGAL SECTOR IN CHINA IS VERY IMPORTANT FOR CANADIAN BUSINESSES. I BELIEVE THAT THE LEGAL ENVIRONMENT IN CHINA IS IMPROVING. THERE IS A SYSTEMATIC EFFORT BY THE STANDING COMMITTEE OF NATIONAL PEOPLE'S CONGRESS TO PREPARE AND STUDY DRAFT LEGISLATION, CONSIDER ITS IMPLICATIONS AND INTERNALLY DEBATE ITS IMPACT, THEN APPROVE AND PUBLISH THE RESULTS.
- IN COMMERCIAL LAW, FOREIGN INVESTED ENTERPRISES ARE BEGINNING TO WIN IMPORTANT CASES INVOLVING, AMONG OTHER PROBLEMS, THEFT OF ASSETS AND INTELLECTUAL PROPERTY PROTECTION.
- THERE ARE OVER 10,000 LAW FIRMS AND 100,000 LAWYERS, INCLUDING CANADIANS. EVERY LARGE BOOK STORE IN CHINA HAS AN IMPRESSIVE SECTION ON LAWS AND LEGISLATION. THIS INDICATES TO ME THAT THE CHINESE PUBLIC IS BEING INVOLVED IN THE PROCESS OF MOVING TOWARDS RULE BY LAW, IF NOT YET RULE OF LAW.

- BUT IT IS ALSO STILL TRUE THAT JUDGES HAVE LITTLE POWER TO ENFORCE COURT ORDERS. NOTIONS OF CONTEMPT OF COURT OPERATE VERY DIFFERENTLY IN CHINA THAN IN CANADA, AND NOT ALWAYS TO THE ADVANTAGE OF SUCCESSFUL LITIGANTS.
- FURTHERMORE, JUDGEMENTS ARE VETTED BY THE POLITICAL SCIENCE AND LAW COMMISSION (THE ZHENGFA WEIYUANHUI) OF THE LOCAL COMMUNIST PARTY BRANCH, TO ENSURE THAT JUDGEMENTS REMAIN UNDER THE PARTY'S PURVIEW AND RESPONSIVE TO THE PARTY'S, AND MORE OFTEN, ITS MEMBERS INTERESTS.
- ANOTHER EXAMPLE IS FROM THE REGULATORY SECTOR OF GOVERNMENT. CHINA HAS CREATED INSTITUTIONS SUCH AS THE INSURANCE REGULATORY COMMISSION, THE SECURITIES REGULATORY COMMISSION, A NEW BANKING COMMISSION AND SO FORTH. THESE ARE LEAD BY RELATIVELY BRIGHT, SHARP AND KNOWLEDGEABLE MINISTERS AND STAFFED BY YOUNG PROFESSIONALS WITH DEGREES FROM THE BEST DOMESTIC AND FOREIGN UNIVERSITIES. THEY EMBRACE THE WTO COMMITMENTS FOR ADVANCE PUBLICATION OF DRAFT REGULATIONS, TRANSPARENT APPLICATION PROCEDURES AND TIME LIMITS BY WHICH THEY MUST ANNOUNCE THEIR DECISIONS.
- THAT SAID, TIME ALLOWED FOR COMMENTARY IS OFTEN TOO

BRIEF TO BE MEANINGFUL. THE PUBLISHED DEADLINES FOR DECISION MAKING MAY BE IGNORED. THE RATIONALE FOR DECISIONS CAN BE OPAQUE.

- THESE “GLASS HALF FULL, GLASS HALF EMPTY” REALITIES MAKE MANY TYPES OF BUSINESS DECISIONS DIFFICULT. THE DECISION ON WHETHER TO PURSUE DISPUTES THROUGH THE LEGAL PROCESS, OR HOW MUCH TO INVEST IN MARKET ENTRY CAN BE DIFFICULT TO MAKE.
- THIRDLY, WE MUST AVOID MAKING ASSUMPTIONS ABOUT BUSINESS REALITIES BASED ON WESTERN CONCEPTS.
- CHINA HAS STOCK EXCHANGES IN SHANGHAI AND SHENZHEN. VERY LARGE COMPANIES ARE LISTED ON THEM. IT ALMOST LOOKS LIKE A MARKET. HOWEVER, ALL BUT A DOZEN OF THE 1187 FIRMS ON THE SHANGHAI EXCHANGE ARE OWNED OR CONTROLLED BY GOVERNMENT ENTITIES, INCLUDING THE LARGEST FIRMS. FURTHERMORE, TWO THIRDS OF THE MARKET CAPITALIZATION OF THE SHANGHAI STOCK EXCHANGE CONSISTS OF GOVERNMENT CONTROLLED NON-TRADED SHARES.
- IT IS NOT POSSIBLE TO EFFECT A TAKE-OVER THROUGH PURCHASING A SUBSTANTIAL PERCENTAGE OF SHARES OF A FIRM. NOR IS THERE MARKET FOR SMALL CAP COMPANIES OR NEW VENTURES TO OBTAIN START-UP MONEY.

- SHAREHOLDERS WHO CARE TO, CAN OBTAIN LARGE AMOUNTS OF INFORMATION AND OPINION ON THEIR CANADIAN OR US STOCKS, COMPARED TO THE QUANTITY AND THE TRUTHFULNESS OF INFORMATION AVAILABLE ON CHINESE COMPANIES. AND SO FORTH.
- ANOTHER EXAMPLE. TELECOMMUNICATIONS IS A RELATIVELY OPEN BUSINESS IN CHINA. THERE ARE MANY LARGE AND SUCCESSFUL FOREIGN EQUIPMENT SUPPLIERS SUCH AS NORTEL, AND VERY LARGE SERVICE PROVIDERS SUCH AS CHINA TELECOMS. CHINA TELECOMS IS A \$__ FIRM. IT HAS A LARGE HEADQUARTERS BUILDING IN BEIJING AND BRANCHES THROUGHOUT THE COUNTRY. YOU WOULD THINK THAT DEALING WITH SUCH A GIANT SHOULD BE STRAIGHT FORWARD. AN INFORMED AND WELL FINANCED SALES PLAN SHOULD BE ENOUGH TO, AT LEAST, GET YOU THROUGH THE DOOR.
- IN FACT, CHINA TELECOMS HEAD OFFICE, BEYOND CERTIFYING EQUIPMENT SUPPLIERS, HAS VIRTUALLY NO POWER TO INFLUENCE THE PURCHASING DECISIONS OF THE PROVINCIAL CHINA TELECOMS PURCHASING DEPARTMENTS. THAT'S WHERE DECISIONS ARE MADE. YOU THINK YOU ARE DEALING WITH ONE COMPANY, BUT YOU ARE IN FACT DEALING WITH OVER 30, AND YOU THUS NEED 30 MARKETING PLANS, NOT ONE. IN THIS EXAMPLE, CHINA TELECOMS REFLECTS THE TRADITIONAL CHINESE TENSION BETWEEN THE NOMINALLY GOVERNING

CENTER AND THE REALITY OF POWER IN THE PROVINCES.

- I SAY ALL OF THIS TO MAKE TWO POINTS: CHANGE IN CHINA IS NOT ONLY ON THE SURFACE BUT IS FUNDAMENTAL, AND UNDERSTANDING CHANGE TO ONE'S BENEFIT AND PROFIT IS NOT AN EASY TASK.
- SECONDLY, I ALSO MAKE THE APPARENTLY OPPOSITE POINT THAT OUTWARD APPEARANCES - THE ESTABLISHMENT OF MODERN INSTITUTIONS SUCH AS STOCK MARKETS AND LARGE, LISTED CORPORATIONS THAT APPEAR SIMILAR IN FORM TO WHAT EXISTS IN CANADA - CAN IN FACT OBSCURE A VERY DIFFERENT REALITY.
- CHINA IS A WORK IN PROGRESS.

THE NUMBERS

- NOW, LET'S LOOK AT THE NUMBERS.
- 1. FIRST, MACRO-ECONOMIC. THE OVERALL GDP GROWTH RATE THIS YEAR WILL AGAIN WELL SURPASS 7%, PROBABLY REACHING 8% OVERALL, AFTER A VERY HOT, PERHAPS TOO HOT FIRST HALF.
- CHINA MUST GROW IN ORDER: TO KEEP A MANUFACTURING POPULATION OF 163MM EMPLOYED AND TO MEET THEIR RISING MIDDLE CLASS EXPECTATION; SUSTAIN EMPLOYMENT FOR A

POTENTIALLY DESTABILIZING FLOATING POPULATION OF 100mm WHO HAVE LEFT THEIR RURAL COMMUNITIES WITH THE PRIVATIZATION OF AGRICULTURAL PRODUCTION; ABSORB AN ADDITIONAL 175MM RURAL WORKERS WHO ARE BEING DISPLACED BECAUSE OF CONTINUING RATIONALIZATION OF THE AGRICULTURAL SECTOR, AS FARMERS ARE ALLOWED MORE CHOICE OF WHAT THEY GROW, FACE GREATER DOMESTIC AND INTERNATIONAL COMPETITION, AS WELL AS FEWER RESTRICTIONS ON LEAVING THE OVERCROWDED COUNTRYSIDE; NOT TO SPEAK OF THE ADDITIONAL 9MM WHO ENTER THE LABOUR FORCE EVERY YEAR, SPURRED BY A POPULATION GROWTH RATE OF OVER 1mm NEW MOUTHS TO FEED EVERY MONTH.

- 2.THE NEED IS TO GROW THE DOMESTIC SECTOR OF THE ECONOMY, WHERE MANY JOBS WILL COME. THIS YEAR, BOTH EXPORTS AND IMPORTS ARE ON A ROLL, LEAD BY FIEs WHICH CURRENTLY ACCOUNT FOR 52% OF EXPORTS AND 48% OF IMPORTS, MAKING CHINA THE WORLD'S 4TH LARGEST EXPORTER AND 4TH LARGEST IMPORTER...
- 3....AS WELL AS THE 4TH ECONOMY IN THE WORLD.
- 4...AND WITH LOTS OF ROOM TO GROW, GIVEN A PER CAPITA INCOME OF OVER US\$1,000 THIS YEAR. ON A STRAIGHT DOLLAR BASIS, CHINA IS STILL ONLY THE 109TH ECONOMY ON THE GLOBE. MALAYSIA IS THE 53RD ECONOMY TODAY, WITH A PER

CAPITA INCOME OF \$3,600. AT A 7% GROWTH RATE PER YEAR, CHINA STILL NEEDS 23 YEARS TO REACH MALAYSIA'S CURRENT LEVEL. IN ORDER FOR HALF OF CHINA'S POPULATION TO REACH MALAYSIA'S CURRENT LEVEL WILL REQUIRE ANOTHER 15 YEARS OF 7% GROWTH.

· 5.BUT THE FACT OF THE MATTER IS THAT THE CHINESE THEMSELVES AND THE WORLD ECONOMY NEED CHINA'S GROWTH. CHINA IS ALREADY A MAJOR IMPORTER, \$339B IN GOODS AND SERVICES IN 2002, 77% OF JAPAN LEVEL, 24% OF USA AND 21% OF THE EU. THESE SHARES ARE EVEN GREATER IF YOU INCLUDE HONG KONG'S \$50B IN IMPORTS. CHINA IS MOVING SO RAPIDLY TOWARDS GLOBAL ECONOMIC INTEGRATION THAT, FOR EXAMPLE, THE PEARL RIVER'S CONTAINER TRAFFIC IS NOW ALMOST EQUIVALENT TO THAT OF ALL OF THE USA. CHINA IS NOW THE WORLD'S BIGGEST IMPORTER OF INTEGRATED CIRCUITS, SULPHUR AND POTASH. FREIGHT RATES TODAY, FOR BOTH BULK (\$25Kpd) AND CONTAINER (\$30Kpd) TRAFFIC, ARE THREE TIMES WHAT THEY WERE JUST 2 YEARS AGO, THANKS TO CHINESE DEMAND. THE DEBATE OVER THE RENMINBI RE-VALUATION IS ALL ABOUT THE IMPACT OF CHINA'S EXPORTS ON THE USA, JAPANESE AND EUROPEAN MARKETS AND THIS AT A TIME WHEN CHINA'S GLOBAL BALANCE OF TRADE MAY SOON BE ZERO, WITH \$100B IN SURPLUSES WITH THE U.S. BEING USED TO IMPORT FROM JUST ABOUT EVERYWHERE ELSE.

· 6.MERCHANDISE IMPORT GROWTH RATES ARE WELL ABOVE THE

OVERALL ECONOMIC GROWTH RATE...

- 7. AS IS THAT OF SERVICES.

- 8. NOTE THAT 47% OF CHINA IMPORTS LAST YEAR WERE ELECTRICAL AND OTHER MACHINERY, A GOOD PART OF WHICH - 50% OR SO IF WE ASSUME THAT HALF GOES INTO FIEs - GOES INTO INCREASING ITS MANUFACTURING CAPACITY AND PRODUCTIVITY. THIS IS OF GREAT INTEREST TO CANADA'S EXPORTERS, AS ARE CHINA'S IMPORTS OF MINERAL PRODUCTS, TRANSPORTATION EQUIPMENT AND AGRICULTURAL GOODS AND FOODSTUFFS.

- 9. NOT SURPRISINGLY, IMPORTS ARE SOURCED IN THE MAJOR ECONOMIES OF JAPAN, THE EU AND THE USA, AS WELL AS THE GREATER CHINA AREAS OF TAIWAN AND HONG KONG. CANADIAN COMPANIES PROVIDE ABOUT 1.5% OF CHINA'S MERCHANDISE IMPORTS. THIS MAKES US 13TH AMONG CHINA'S TRADE PARTNERS.

- 10. THE BASIS OF GROWTH IN IMPORTS IN THE LAST TWO YEARS OR SO IS EVIDENT: OVER 50% INCREASES IN INTEGRATED CIRCUITS, SEMICONDUCTOR DEVICES AND SO FORTH, A DOUBLING OF AUTO INDUSTRY IMPORTS AND SO FORTH. THAT IS HOW ONE GETS A 21% INCREASE IN IMPORTS OVERALL.

- 11. SERVICE SECTOR IMPORTS WERE ALMOST \$50B LAST YEAR. AIR CANADA, THE PORT OF VANCOUVER, CANADIAN LAW

FIRMS, ARCHITECTURAL FIRMS, ENGINEERING COMPANIES, CANADIAN INSURERS AND BANKERS ARE A VISIBLE PART OF THIS BUSINESS.

- 12. CHINA IS THE WORLD'S FORTH LARGEST EXPORTER AS I HAVE SAID. HALF OF CHINA'S EXPORTS GO TO THE USA, JAPAN AND THE EU, AND ANOTHER 25% GOES THROUGH HONG KONG.
- 13. ABOUT HALF ARE GENERAL CONSUMER GOODS. THE VAST MAJORITY DO NOT CARRY RECOGNIZED BRANDS. THEY ARE MANUFACTURED FOR CANADIAN TIRE, WALMART AND OTHER RETAILERS. FOR EXAMPLE, CANADIAN TIRE HAS A VERY LARGE SOURCING OPERATION BASED IN HONG KONG. BUT THIS WILL CHANGE. ALREADY, CHINESE COMPANIES SUCH AS HAIER FOR WHITE GOODS, LEGEND FOR COMPUTERS ARE LAYING OUT NORTH AMERICAN, JAPANESE, EUROPEAN AND SOUTHEAST ASIAN MARKETING STRATEGIES.
- 14. CHINA'S GLOBAL EXPORTS ARE LARGELY TRACKED IN THEIR EXPORTS TO CANADA, A TOTAL OF SOME CDN\$16B WORTH OF GOODS AND...
- 15. ...CDN600mm OF SERVICES LAST YEAR.
- THESE TWO LAST TABLES ARE AMONG THE MOST IMPORTANT PIECES OF INFORMATION THAT I CAN PROVIDE TO YOU. THESE AND OTHER SECTORS ARE WHERE CHINA'S GLOBAL

COMPETITIVE IMPACT IS AND WHERE IT IS HEADED IN THE YEARS TO COME. I OFTEN SAY, AND I WILL REPEAT HERE TODAY, THAT EVERY FIRM MUST HAVE A CHINA STRATEGY, EITHER TO MAKE MONEY FROM CHINA'S GROWING MARKET, OR TO ENSURE THAT YOU HAVE A GRASP OF A NEW, EMERGING COMPETITIVE ENVIRONMENT. YOU MAY NOT BE IN CHINA BUT CHINESE FIRMS AND FOREIGN INVESTORS ARE, AND THEY ARE NOW OR IN THE FUTURE EYEING YOU AS A COMPETITOR.

- SO WATCH THIS SPACE....

- 16. ...AS CHINA'S GDP REACHES \$1.6T, AND IMPORTS AND EXPORTS BOTH CONTINUE TO RISE.

- CAN ANYTHING STOP OR SLOW CHINESE GROWTH? I'LL COME TO THAT IN A MOMENT.

- 17. WHERE DO WE FIT AS A SUPPLIER OF GOODS AND SERVICES TO CHINA? LAST YEAR, CANADIAN EXPORTS WERE VALUED AT JUST OVER CDN\$4B, WITH POTASH FROM CANPOTEX, TRANSPORTATION EQUIPMENT FROM BOMBARDIER AND CAE, ELECTRICAL EQUIPMENT AND MACHINERY FROM COMPANIES SUCH AS NORTEL, PULP FROM TEMBEC AND NICKEL FROM INCO, AND SEAFOOD FROM FISHERY PRODUCTS INTERNATIONAL, MEAT FROM MAPLE LEAF FOODS, CANOLA FROM J.R. RICHARDSON, ETC. THESE NUMBERS HOWEVER DO NOT MAKE CLEAR THE INVOLVEMENT OF HUNDREDS OF SMALL AND MEDIUM SIZED CANADIAN COMPANIES WHO ARE ALSO

GETTING A PIECE OF THE MARKET, INCLUDING OF COURSE COMPANIES FROM QUÉBEC AND ONTARIO, B.C. AND ALBERTA.

- 18. IN 2001, OUR SERVICE EXPORTS - AS I SAID EARLIER, FROM TRANSPORTATION TO INSURANCE AND TOURISM - REACHED THREE QUARTERS OF A BILLION TWO YEARS AGO.

- 19. THE MAKEUP OF OUR MERCHANDISE TRADE HOWEVER IS ALSO HIGHLY VOLATILE. SO FOR THAT MATTER ARE SERVICES, WHEN YOU FACTOR IN THE LOSS OF TRANS-PACIFIC TRAFFIC AND TOURISM DUE TO SARS. LAST YEAR, INCO ENJOYED A MAJOR INCREASE IN NICKEL SALES, NORTEL AND EXFO SAW INCREASES IN THEIR SUPPLY OF TELECOMS EQUIPMENT. ON THE OTHER HAND, LACK OF SUPPLY KEPT MOST CANADIAN CANOLA OUT OF THE MARKET. IN 1988, WHEAT AND BARLEY MADE UP 64% OF CANADA'S EXPORTS TO CHINA. IN 2001, THEY WERE 8%, CDN\$302mm, VS. OVER \$1B FIVE YEARS EARLIER. SO FAR THIS YEAR, POTASH, ELECTRICAL AND ELECTRONIC PARTS, NICKEL AND AUTO PARTS ARE UP, WHILE SOME KINDS OF PULP IS DOWN. WE EXPECT AN OVERALL RISE FOR THE YEAR, HOWEVER.

- 20. ...AND, GIVEN THE STRUCTURE OF OUR EXPORT SECTOR, WE ARE OPTIMISTIC FOR THE FUTURE. IF WE CAN KEEP OUR MARKET SHARE, WE CAN REACH CDN\$7B IN GOODS IN THE NEXT HALF DECADE...

- 21. ...AND CLOSE TO A BILLION IN SERVICES AS WELL BY 2007.

- THIS IS POSSIBLE FOR A NUMBER OF REASONS. WTO ACCESSION IS ALREADY HAVING AN IMPACT BECAUSE CHINA HAS IMPLEMENTED THE HAS IMPLEMENTED THE SCHEDULED TARIFF REDUCTIONS. IN SOME SECTORS, IT HAS IMPROVED UPON ITS COMMITMENTS.

- 22. THE LIST OF COMMITMENTS OF INTEREST TO CANADA INCLUDE AUTO PARTS, LINE TELEPHONE EQUIPMENT, SHRIMP ETC. THESE PRODUCTS ARE INDEED INCREASING THEIR PENETRATION OF THE CHINESE MARKET.

- 23. WHEN ALL TARIFFS OF ITS TARIFF REDUCTION COMMITMENTS ARE IN PLACE, CHINA WILL HAVE RATES CONSIDERABLY LOWER THAN THE OECD AVERAGE.

- 24. A LARGE NUMBER OF REGULATORY CHANGES ARE ALSO IN THE OFFING, OF INTEREST TO ALL COMPANIES INVOLVED IN IMPORT/EXPORT BUSINESSES, CANOLA SUPPLIERS, BANKS AND INSURANCE COMPANIES.

- 25. ALL THAT SAID, THERE ARE AND WILL CONTINUE TO BE BARRIERS TO ENTRY, OR AT LEAST LOW COST ENTRY.

- EVERYTHING DEPENDS ON YOUR FIELD OF BUSINESS. SPECIFIC

ONGOING ISSUES THAT MAKE ACCESS DIFFICULT. I CAN GO INTO SOME DETAIL DURING THE Q&A SESSION, BUT THESE INCLUDE UNFAVOURABLE REGULATORY CONDITIONS OR TERMS OF TRADE AFFECTING REGIONAL AIRCRAFT, INDUSTRIAL OFFSETS, BANKING AND INSURANCE, COSMETICS, SPS, TRQs ETC.

- 26. ALL OF CHINA'S OTHER MAJOR TRADING PARTNERS HAVE SEEN RAPID INCREASES IN THEIR EXPORTS TO CHINA AND THEIR IMPORTS FROM CHINA.
- FOR EXPORTS TO CHINA, GROWTH IS MOST EVIDENT AMONG THOSE WHO HAVE INVESTED IN MANUFACTURING IN CHINA. MOST SUCH INVESTMENTS REPRESENT SHIFTING PRODUCTION OF CONSUMER PRODUCTS FROM OTHER DEVELOPING COUNTRIES OR SHIFTING PRODUCTION OF LABOUR INTENSIVE PORTIONS OF PRODUCTION OF SUCH GOODS TO CHINA. THE KEY TO REMEMBER IS THAT ABOUT HALF OF CHINA IMPORTS AND HALF OF CHINA'S EXPORTS ARE CARRIED OUT BY FOREIGN INVESTED COMPANIES.
- FOR IMPORTS FROM CHINA, GROWTH HAS BEEN RAPID ALMOST EVERYWHERE AS CHINESE PRODUCTION DISPLACES PRODUCTION ELSEWHERE OF CONSUMER GOODS AND OTHER LABOUR INTENSIVE MANUFACTURES.
- THIS RAISES THE ISSUE OF INVESTMENT. THE CHINESE GOVERNMENT ANNOUNCED ON SEPTEMBER 8 THAT CHINA

EXPECTS TOTAL FDI TO REACH US\$57B THIS YEAR, \$4.3B MORE THAN LAST YEAR. 400 OF THE WORLD'S 500 LARGEST FIRMS HAVE LAUNCHED OPERATIONS IN CHINA, ACCORDING TO CHINESE SOURCES. FDI REGULARLY CONTRIBUTES OVER 10% OF CHINA'S GROSS FIXED CAPITAL FORMATION, WITH SIGNIFICANT SPIN-OFF BENEFITS INCLUDING PRODUCTIVITY GAINS.

- FURTHERMORE, AS OF JULY THIS YEAR, OVER 7,200 CHINESE FIRMS HAVE ESTABLISHED OPERATIONS OF ONE SORT OR ANOTHER ABROAD, OPERATING IN OVER 160 COUNTRIES, WITH A TOTAL INVESTMENT OF \$10B.
- ALL OF THESE DEVELOPMENTS, THE INCREASING GDP, THE RISE IN IMPORTS AND EXPORTS, FDI IN CHINA, AND THE STIRRINGS OF CHINESE INVESTMENT ABROAD, ARE WELCOME DEVELOPMENTS. IF YOU BELIEVE THAT A GLOBALIZED, INTERDEPENDENT WORLD CONTRIBUTES TO RISING STANDARDS OF LIVING AND STRONGER UNDERPINNINGS IN SUPPORT OF GLOBAL PEACE AND SECURITY, THEN CHINA'S REMARKABLE ACHIEVEMENTS OVER THE LAST TWO DECADES SHOULD BE WELCOMED, NOT FEARED.
- LAST YEAR, OVER ONE THOUSAND CANADIAN COMPANIES WERE INVOLVED IN EXPORTS TO CHINA AND IMPORTS FROM CHINA. OVER 500 CANADIAN FIRMS NOW HAVE REGISTERED OPERATIONS IN CHINA, DOUBLE THE NUMBER ONLY SIX YEARS AGO. LARGE COMPANIES SUCH AS BOMBARDIER, NORTEL,

MANULIFE, SUNLIFE, THE CANADIAN WHEAT BOARD, AS WELL AS HUNDREDS OF SMALL AND MEDIUM ENTERPRISES HAVE DEVELOPED THEIR NICHEs IN CHINA AND ARE GROWING WITH IT.

- JUST OVER THE LAST FIVE YEARS, CANADIAN FIRMS HAVE SOLD CDN\$__ WORTH OF GOODS AND SERVICES TO CHINA, AND CANADIANS HAVE BENEFITED FROM SOURCING \$__ OF CHINESE IMPORTS. LITTLE OF THIS TRADE AND ECONOMIC ACTIVITY EXISTED 10 YEARS AGO.
- SO WE WELCOME THIS VERY SIGNIFICANT ADDITION TO THE WORLD OF TRADE AND ECONOMICS. WE THUS ALSO HAVE A STAKE IN CHINA'S SUCCESS.
- STRAIGHT LINE PROJECTIONS OF ANY KIND SHOULD BE AVOIDED HOWEVER, PARTICULARLY WHEN THEY POINT UPWARD. EVERYONE SHOULD BE EQUALLY AWARE OF THE LIST OF IMPEDIMENTS THAT COULD LIMIT OR EVEN REVERSE CHINA'S ECONOMIC GROWTH.
- CONFLICT ON THE KOREAN PENINSULA OR ACROSS THE TAIWAN STRAITS WOULD SEVERELY IMPAIR TRADE IN GOODS AND SERVICES, THE CONFIDENCE OF FOREIGN INVESTORS, ACCESS TO THE USA AND JAPANESE MARKETS, AND POSSIBLY A MELT-DOWN OF THE POLITICAL AND ECONOMIC CONSENSUS THAT HAS UPHELD THE WESTERN PACIFIC PEACE AND

STABILITY FOR THE LAST 60 YEARS.

- SERIOUS ECONOMIC DIFFICULTIES IN ONE OR MORE OF CHINA'S MAIN ECONOMIC PARTNERS - THE EU, USA, JAPAN, HONG KONG AND TAIWAN, WOULD CONSTRAIN OPPORTUNITIES FOR GROWTH AND COULD CONCEIVABLY RESULT IN DECLINES WHERE WE HAVE ONLY SEEN INCREASES.
- SERIOUS AND HIGHLY VISIBLE SOCIAL INSTABILITY IN CHINA, ARISING FROM THE GROWING DISPARITIES IN WEALTH AND OPPORTUNITY WOULD SHAKE THE CONFIDENCE OF INVESTORS.
- SERIOUS, SUSTAINED AND PUBLIC POLICY DISAGREEMENTS AMONG THE TOP ECHELONS OF THE COMMUNIST PARTY OF CHINA WOULD FREEZE THE DECISION MAKING PROCESS IN ITS TRACKS, AND SEND GOVERNMENT OFFICIALS AND LOWER LEVEL BUREAUCRATS RUNNING FOR COVER TO AWAIT SIGNS THAT WOULD TELL THEM IN WHICH DIRECTION THE WIND IS BLOWING.
- OR SOMETHING TOTALLY UNEXPECTED - A NEW, EVEN MORE VIRULENT STRAIN OF SARS; A POLICY DECISION ON PROPPING UP THE FINANCIAL SYSTEM THAT GOES TERRIBLY BADLY; THE TAKEOVER OF THE COMMUNIST PARTY APPARATUS BY A CONSERVATIVE FACTION THAT TRIES TO REVERSE 20 YEARS OF REFORM AND OPENING - NOTHING SHOULD BE EXCLUDED.

- STRAIGHT LINE PROJECTIONS ARE NEVER CORRECT, BUT YOU HAVE TO PLAY THE ODDS. THESE ODDS REMAIN FAVOURABLE TO A CONTINUATION OF THE CHINESE ECONOMIC POLICY FRAMEWORK THAT HAS DONE SO MUCH TO BUILD CHINA INTO THE ECONOMIC POWER THAT IT HAS BECOME. HOPEFULLY, THE INTERNATIONAL ENVIRONMENT WILL ALSO REMAIN STABLE.
- WENDING YADAO YIQIE - STABILITY OVER EVERYTHING. THAT WAS DENG XIAOPING'S PRIORITY AND IT IS THAT OF THE COMMUNIST PARTY LEAD GOVERNMENT OF PRESIDENT HU JINTAO AND PREMIER WEN JIABAO AS WELL.
- THE COMMUNIST PARTY LARGELY COMPLETED ITS LEADERSHIP TRANSITION IN OCTOBER 2002. IN MARCH 2003 A NUMBER OF STATE COUNCIL POSTS WERE RE-ASSIGNED AND SOME GOVERNMENT MINISTRIES WERE RESTRUCTURED. THE FUNDAMENTAL ECONOMIC POLICY OF THE GOVERNMENT REMAINED UNCHANGED -- ENSURE CONTINUED, UNINTERRUPTED HIGH LEVELS OF ECONOMIC GROWTH AND USE FOREIGN TRADE AND INVESTMENT AS A TOOL TO MAKE THIS HAPPEN. ALL IMPORTANT GOVERNMENT POSTS REMAINED INTERTWINED WITH IMPORTANT COMMUNIST PARTY POSITIONS.

WE HAVE SEEN STRUCTURAL CHANGES THIS YEAR:

- THE TRADE MINISTRY HAS GAINED ADDITIONAL

RESPONSIBILITIES AND NOW REGULATES DOMESTIC COMMERCE (E.G. ISSUES THE REGULATIONS THAT GOVERN WALMART AND THE NEWLY EMERGING CHINESE NATIONAL RETAIL CHAINS) AND HAS A FIRMER HOLD ON TRADE REGULATION (E.G. WITH FULL RESPONSIBILITY FOR ANTI-DUMPING MEASURES).

- THE CENTRAL BANK IS BEING RESHAPED TO FOCUS MORE ON MONETARY POLICY LEAVING ITS ORIGINS AS THE ONLY BANK IN CHINA (1950S UNTIL THE START OF THE 1980S) FURTHER BEHIND.
- A NEW BANKING REGULATORY COMMISSION HAS BEEN ESTABLISHED TO FOCUS SOLELY ON DEVELOPING A WORKING BANKING SYSTEM AND CLEANING UP THE NON-PERFORMING LOAN LEGACY OF DIRECTED LENDING.
- A NEW AGENCY HAS CENTRALIZED CONTROL OVER LARGE STATE OWNED ENTERPRISES IN ORDER TO EITHER RUN THEM MORE EFFICIENTLY OR PRIVATIZE THEM (DEPENDING ON THE SOE AND THE PREVAILING POLITICAL WINDS).
- THE STATE DEVELOPMENT AND PLANNING COMMISSION HAS BEEN RENAMED THE NATIONAL DEVELOPMENT AND REFORM COMMISSION AND IS BEING NUDGED AWAY FROM ITS ORIGINS AS THE CENTRAL CENTRAL PLANNING MINISTRY TOWARDS A MINISTRY THAT SETS BROAD INDUSTRIAL AND

MACROECONOMIC POLICIES.

NOW THAT THE NEW TEAM HAS BEEN IN PLACE FOR A FEW (POST-SARS) MONTHS, WE ARE STARTING TO SEE STEPS TO MODERNIZE THE WORKINGS OF THE ECONOMY:

- AN ADMINISTRATIVE PROCEDURE LAW IS BEING DEBATED AND COULD END UP GREATLY REDUCING RED TAPE (AND RESTRICTING THE NUMBER AND COMPLEXITY OF LICENSES THAT REGULATORS CAN REQUIRE IN THE FUTURE).
- WORK IS UNDERWAY ON SETTING OUT FRAMEWORK LEGISLATION ON PUBLIC CONSULTATION AND REGULATORY TRANSPARENCY (FOR ECONOMIC REGULATION).
- LONG SHELVED DRAFT COMPETITION POLICY AND BANKRUPTCY LAWS HAVE BEEN DUSTED OFF AND NOW BEING DISCUSSED SERIOUSLY AGAIN.

ABOVE ALL, WE ARE SEEING A GOVERNMENT DEDICATED MORE TO INCREASING THE PRODUCTIVITY OF THE ECONOMY AND THE EFFICIENCY OF REGULATION AND LESS TO IDEOLOGY THAN EVER. IT REMAINS TO BE SEEN WHETHER OR NOT EFFECTIVE TINKERING WILL BE SUFFICIENT TO ADDRESS:

- THE URBANIZATION CHALLENGE, WHEREBY MILLIONS OF PEOPLE WILL NEED TO BE FOUND JOBS IN THE CITIES AND BE

INTEGRATED INTO URBAN LIFE;

- THE CHALLENGE OF DISPARITIES, WHEREBY LARGE PARTS OF THE COUNTRY WILL NEED TO BE INTEGRATED INTO THE COASTAL, FDI/TRADE-DRIVEN SUCCESSES. FROM BEIJING TO GUIZHOU, THE PER CAPITA DIFFERENCE IS A FACTOR OF 9.
- THE CHALLENGE OF INCENTIVES, WHEREBY DOMESTIC FINANCIAL MARKETS WILL NEED TO BECOME MORE MEANINGFUL AND ACTUALLY CHANNEL FUNDS TO THOSE WHO PERFORM AND WHEREBY A REAL PRIVATE SECTOR WILL NEED TO BE ALLOWED TO FLOURISH.
- THIS IS THE STUFF OF GOVERNANCE IN TODAY'S CHINA. CHINA'S NEW LEADERS APPEAR TO WISH TO GIVE GREATER PROMINENCE TO SOCIAL ISSUES, PARTICULARLY POVERTY AND UNEMPLOYMENT; THERE HAVE BEEN A SERIES OF STATEMENTS ON REVIVING THE NORTHEAST OF CHINA, TO BALANCE POLICIES IN FAVOUR OF WESTERN DEVELOPMENT. THERE IS A VERY ACTIVE DIPLOMATIC AGENDA - WE ARE TOLD THAT BETWEEN THEM, PRESIDENT HU AND PREMIER WEN ARE MEETING WITH LEADERS OF 65 COUNTRIES IN THE LATTER HALF OF THIS YEAR.
- OTHER POLICY ISSUES THAT WERE MOOTED DURING THE JIANG ADMINISTRATION AND REMAIN UNRESOLVED - SOE REFORM, REFORM OF THE FINANCIAL SYSTEM, EVEN INTERNAL CHANGES TO COMMUNIST PARTY GOVERNANCE - ARE NOT

RECEIVING A LARGE DEGREE OF PUBLIC ATTENTION. ONLY TIME WILL TELL US IF THE RESIDENT HU'S LEADERSHIP WILL DIRECT CHINA TOWARDS ADDITIONAL - IF NOT DIFFERENT - GOALS.

THANK YOU