

## The Value of the Chinese Connection [and Comments]

Roger Sullivan

Michael Y.M. Kau

James C. Hsiung

Jan S. Prybyla

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## CHAPTER V.

### THE VALUE OF THE CHINESE CONNECTION

*Roger Sullivan\**

Americans find it very difficult to be dispassionate on the subject of China. When people ask me, as you have in my informal remarks to this Workshop, to specify what benefits or what value there is to the United States-China relationship, if any, I always hesitate to answer. This is not just because there are no simple answers, but also because the answers to the questions depend on one's interests, expectations and perhaps, one's prejudices.

In July, 1971, President Nixon said that there can be no stable or enduring peace without the participation of the People's Republic of China (P.R.C.) and its 800 million people. While we believe that this statement is generally still true, we can be a lot more specific about the value of the so-called "Chinese Connection" today than we could in 1971. The United States' establishment of closer ties with China, culminating in the establishment of diplomatic relations, has made possible extensive exchanges on both global and regional issues. We have been able to explore common interests and to develop shared perspectives with a much greater openness and trust than was possible in the past. Before the establishment of diplomatic relations, our discussion of problems was, more or less, limited to an arm's length exchange of positions. Now, there is much more give and take; a real desire, not just to exchange views, but to resolve problems. There is a degree of cooperativeness to the relationship that few had dreamed possible in the early stages of normalization.

This very dramatic change in our relationship with China is a direct result of normalization. There has been a reduction of tension between China and the United States on several issues (Taiwan is a dramatic example of that; Korea to a lesser, but still real degree). We have also reaped an important side benefit, with the possibility of much closer relations with Japan as a consequence of the good relations between China and the United States. For the first time in this century, both Japan and the United States are in a position of not having to choose between having good relations with each other and having good relations with China. From the period after the war until, at least, 1971-72, there was not only concern about the "Chinese threat," but there was also the problem that American hostility towards China was an obstacle to a closer Japanese-American relationship. It

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\* Deputy Assistant Secretary of State for East Asian and Pacific Affairs.

certainly was the major cause of opposition in Japan to the U.S.-Japan security relationship.

In the Southeast Asian countries, there is not only a reduction in fear of China (in fact, fear has changed to a great interest in cooperating with China as a means of containing Vietnam), but also a diminution of fears about a withdrawal from the area on the part of the United States. The United States is redefining its relationship towards Asia, demonstrating by its normalization of relations with China that, far from losing interest in the area, the United States is becoming more deeply involved, although in a different way from the past.

This new political relationship has also opened up new economic possibilities. Here, the China euphoria has been mislaid. It is very easy to exaggerate the benefits that can flow to the United States, in terms of trade and economic relations, from normalization. Those who like to dismiss that relationship have emphasized China's poverty and the relative unimportance of China as a trading nation. Both of these factors are very true. There are, however, opportunities for the United States. We have resolved most of the obstacles to an economic relationship with China. In particular, we have solved the claims and assets problem; we have disposed of, though we have not exactly solved the textile problem; we have also paved the way for the signing of the trade agreement which was initialled by Juanita Kreps on her visit to China.<sup>1</sup> This trade agreement — which I am confident will meet with support in Congress — will extend to China "most-favored nation" status and provide not only greater opportunities for China to export to the United States, but will improve the climate in China for American exports and American cooperative ventures, particularly in energy-related areas. We have already had some extensive negotiations between American oil companies and the Chinese on the exploration of China's offshore oil resources.

Questions always arise about all these stories we hear that China is backing away from modernization and economic relationships with the outside world. This is simply not the case. What we have seen in the last few months is a reassessment on the part of the Chinese of the commitments or semi-commitments they have already made; they wanted to make sure that the decisions they were making were in line with their priorities. By no means were the Chinese backing away from the basic policy of modernization or their basic modernization program. In fact, in the month of May, the Chinese have signed loan agreements with foreign governments and banks totalling \$21 billion. This is \$21 billion of a total \$26 billion to which the Chinese have gained access. Negotiations are underway which could bring

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1. See the text of William W. Clarke's speech, p. 92 *infra*.

that total up to \$30 billion. We now expect the Chinese to resume their program of major capital purchases as they complete their reassessment.

These loan agreements should enable the Chinese to spend something on the order of \$50–60 billion on imports of capital goods and technology over the next five years. Our exports to China this year should be well over one billion dollars. By 1985 they should easily be in the range of about \$5 billion each year. This is certainly not going to solve America's economic problems, but it is significant.

It is important that we take a long range view, keeping in mind that what we do with China today is going to continue to affect events and attitudes for the next twenty-five or thirty years or more. I would hate to see us put ourselves in the position where, in the year 2000, we look back with regret over some of the decisions we made or decisions we did not make in 1979–80. I do not know how many people realize the price we have paid over the years for such a simple thing as John Foster Dulles' refusal to shake hands with Chou En-Lai in 1954.

But when I say we should think strategically, I am not talking about entering a military relationship with China. We are not trying to use China as a counterweight to the Soviet Union. It would be a mistake to think in those terms. We have said many times that we are not improving relations for short term reasons. We are not playing the China card or any other dangerous games with our relationship. Our goal, and what should continue to be our goal, is a strong and secure China. By that we mean a China that can provide the necessities to its own people and protect the capability to maintain an independent foreign policy. A China like that could then play the kind of a role that China must play if global and regional peace is to be maintained.

Our opinion about China and the current Soviet paranoia have really turned reality on its head. The danger to China has never come from its strength, but from its weakness. China is now acknowledging that weakness for the first time and is starting to do something about it. I saw the beginnings of this in July last year when I went to China with Dr. Frank Press, the President's Science Advisor. It was a very dramatic time when it became apparent that China had made up its mind to open itself up to the United States economically and technologically, as well as diplomatically. It was absolutely clear on that visit that progress in our relations would come very quickly. Deng Xiaoping left no doubt in our minds that he had made up his mind that China had to move ahead and had to move very quickly if it was going to rebuild its economy and its society from the bottom up. The school system had been destroyed and the economy was barely functioning. We could almost detect a note of desperation. It was clear that everyone we

talked to knew that they had to do something, that they had to do it quickly, and had to do it correctly or face collapse.

It was this realization and not any short-run considerations that prompted the Chinese to move ahead with the United States. China needs a long-term relationship, not just with the United States, but with Japan and Europe in order to get the technology, the capital and the trade that it has to have if it is going to modernize. At the same time, it is clear that they also see this new relationship as a means of providing themselves with a breathing space (a sort of political deterrence) from Soviet pressure.

I believe that it is crucial to regional and global peace that China not fail in this modernization effort, that it succeed, at least to the extent of being able to maintain its independence and play a constructive role in the region. A China like that would not be a threat to anyone. Rather, a China which found itself rejected by the outside world, unable to get the technology and capital it needed, failing in its effort of modernization, embittered and impoverished, and forced to come to terms, perhaps, with its hostile neighbors, would be a threat to all of us.

Asia is and will continue to be of increasing importance to the United States. Anything that happens in Asia will in one way or another affect or be affected by China and the U.S.-China relationship. It took us thirty years, two wars, many lives and billions of dollars to learn that lesson. I hope we will not forget it.

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## COMMENTS

*Michael Y. M. Kau\**

In recent months, the Carter administration has been using various public forums to defend its policy and methods of normalizing relations with the People's Republic of China (P.R.C.). It is natural for administration officials to explain policies of major significance to the nation on behalf of the President in order to create public support and consensus. The presentation of their arguments has, however, been less than candid. While stressing enthusiastically the positive value of normalization and the Chinese connection, they fail to inform the public of all the possible flaws and risks involved. They assert that Washington had obtained the best possible terms from

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\* Professor of Political Science, Brown University; Specialist on Chinese political developments.

Peking; Taiwan has become even more secure as a result of normalization; and the Chinese connection shall be beneficial to peace and stability in Asia. Serious questions can be raised with respect to these assertions.

The alleged benefits of our new policy are simply optimistic assumptions on our part, clearly not proven facts. Such benefits may or may not be forthcoming. Even if they can be achieved, the question remains as to what risks and pitfalls we will have to face in the years ahead. Beyond the problem of policy objectives, the method and process of normalization should also be scrutinized. How an issue and its negotiations are handled is often just as important as the ultimate outcome itself.

Before discussing these various questions, it is important to mention a few facts about Taiwan, the party which our China deal affects most directly. Taiwan has too often been treated as an abstract, dispensable pawn in the superpower game between the United States and the P.R.C. In comparison with a huge China, Taiwan may indeed appear quite small and insignificant. It should be remembered, however, that Taiwan's population of over 17 million is four times larger than that of Israel and is larger than the population of over 100 countries in the United Nations. Taiwan's current \$26 billion two-way trade ranks twentieth in the world, and at present, Taiwan is the eighth largest trading partner of the United States. With our explicit initiatives and encouragements, the Republic of China (R.O.C.) on Taiwan has been our faithful ally and friend for the last three decades. The island and its people served well our strategic and political interests in Asia in the era of the Cold War against Communist expansion and during the years of the Vietnam War. Taiwan's prosperous economy has become the "success story" of American foreign aid. Yet in the process of our involvements, we have also helped create a peculiar international status for the island, to which we have incurred a moral and political obligation for its security and well-being. Hence, no discussion of our normalization policy can be meaningful without taking into consideration the issue of Taiwan.

Turning to the substantive questions concerning the value of normalization and the Chinese connection, first, the Administration argues that normalizing our relations with the P.R.C. is a matter of "recognizing simple reality." At issue here is not whether we should have recognized the P.R.C., but rather on what terms should recognition have taken place. By totally accepting Peking's demands to withdraw recognition from the R.O.C. and to terminate our 1954 Mutual Defense Treaty with Taiwan,<sup>1</sup> we have clearly "abnormalized" our relations with Taiwan. The end result is that Taiwan is reduced to a "non-entity," we "acknowledge" Peking's claim over the island, and allow the future of its 17 million people to drift in limbo at China's

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1. [1955] 6 U.S.T. 433, T.I.A.S. No. 3178.

mercy. Since the initiation of the Nixon-Kissinger negotiations with the Chinese in 1972, the issue has been the crucial question of Taiwan's external security vis-à-vis China. Peking leaders have threatened repeatedly to liberate Taiwan by force, if necessary. It is absolutely incredible that the Carter administration did not even ask the Chinese leaders for a pledge not to use force to settle the Taiwan issue.

The weak negotiating position that the Administration took is indeed hard to comprehend, especially when there is a clear consensus that under the current Chinese domestic and external situation, the Chinese need us more than we need them; we were in a position to negotiate from strength. This same meek attitude of the Administration was clearly revealed again in the original version of the Taiwan Omnibus Bill submitted by the President to the Congress. The bill said nothing about our continued commitments to Taiwan's military and economic security against external threat. Fortunately, Congress had the wisdom and courage to write into the final version of the Taiwan Relations Act<sup>2</sup> what the Administration was, under pressure from Peking, afraid to say.

Second, Administration officials argue that the P.R.C. has neither the intention nor the capability to take over Taiwan. Of course, it may be true that China would not and could not invade Taiwan immediately, but nobody can tell what will happen in the long run. The Administration did not remind us that Peking signed a peace pact with Tibet in 1951, only to use force to crush the Tibetans in 1959. In 1962, China mobilized its forces to teach India a bloody lesson. If this history is too remote to recall, China's invasion of Vietnam last February ought to be still fresh in our minds. In spite of serious warnings from the Soviet Union, China did not hesitate to use force to try to achieve its foreign policy objectives in India. If Peking can justify its action in Vietnam, it has even greater justification to use force on Taiwan. Besides, one should remember that Peking has never renounced officially the use of force to settle the Taiwan problem.

While the armed forces in Taiwan are well-trained and equipped, one should not fail to recognize the simple fact that when the chips are down, in a military confrontation between China and Taiwan, it will involve a contest between a giant of 900 million people against a dwarf of 17 million. It would surely be a very different contest from that between East and West Germany or that between North and South Korea. According to most military experts, there is absolutely no way Taiwan can sustain prolonged attack from across the Taiwan Strait by the world's third largest Navy (ninety submarines) and

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2. Pub. L. No. 96-8, 93 Stat. 14 (1979). See Appendix-Selected Documents p. 114 *infra*.

Air Force (5,000 jet fighters), despite its edge of qualitative superiority and its control of the Strait.

In fact, Peking's calculus of liberating Taiwan may not be a military one. It is likely to involve a mixture of psychological, economic and political warfare, which is a low-cost and low-profile approach that can be ever more effective. A well-orchestrated military harassment or threat of harassment to Taiwan's trade can cause serious disruptions to the steady flow of raw material, technology and capital which constitute the lifeline of Taiwan's heavily trade-oriented economy. Once this lifeline is shaken, Taiwan could not maintain political morale and social stability and the island could be brought to its knees in a relatively short period of time.

Finally, the Carter administration argues that normalizing our relations with China can enhance peace and stability in Asia. Administration officials are quick to point out the unusual achievement that for the first time in this century we have both Japan and China on our side, and that we expect China to play a major role in the world arena. Thus, the Administration proclaims that "a secure and strong China" is in the interest of the United States and the world. Despite repeated official statements that we are pursuing an "even-handed" policy with China and the Soviet Union, the Soviets are clearly looking at our new policy posture with great concern and suspicion. Our willingness to give China most-favored nation treatment. Eximbank loans and sophisticated advanced technology is naturally causing the Soviets great alarm. As long as Moscow perceives that we are "tilting" towards Peking in the delicate balance of superpower politics and that we are playing the "China Card" against their global strategic interests, we will have to face whatever consequences may ensue.

Recent escalations of political and military crises in Indochina are clearly a case in point. Arguably, the way we handled (or mishandled) the process of normalization and the Chinese connection late last year apparently had direct bearing on the stepped-up interventions in Kampuchea (Cambodia) and Laos by the Vietnamese under Soviet support. Moreover, the Chinese invasion of Vietnam last February, which was viewed to have tacit approval from Washington, has clearly sped up Soviet build-up in Vietnam in recent months. We should be fully cognizant that the Soviet Union is the only adversary which has the capacity to threaten our national security, to engage in an arms race with us and to challenge our influence on a global scale. Furthermore, it should be remembered that the military capability that China is acquiring has no strings attached. The same weapons that China acquires from us today could be used against our allies tomorrow. In the same vein, neither can anyone guarantee that the feud between China and the Soviet Union will never come to an end and that the two powers will not once more resume their alliance of the 1950s. In this world of uncertainties, our



foreign policy should be based squarely on our own strength and leadership, and not on some naive and well-intended assumptions.

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## COMMENTS

*James C. Hsiung\**

Since our China policy is only as sound as the conceptual foundation on which it is based, I propose to take a critical look at that foundation. But first let me suggest a distinction between "normalization" and a sensible United States-China policy. I am not questioning the wisdom of the former but merely questioning whether the China policy pursued by Washington, quite outside the "normalization" question, is a sensible one.

### NORMALIZATION IN THE ERA OF MULTIPLE DETERRENCE

The normalization of relations between the United States and the People's Republic of China (P.R.C.) took place within the new era of multiple deterrence, in which the P.R.C. has joined the two super-powers in the coveted nuclear club. In fact the new era logically compels the termination of the non-recognition policy of the United States. That logic is inherent in the drastic transformation of the "rules of the game," as certain fundamental assumptions underpinning the strategy of conflict developed during the erstwhile dyadic deterrence period have been rendered invalid or called into question. While this is a very complex topic, I shall merely focus on one aspect — with the existence of a third adversary, there can be no winner in any nuclear conflict. Even assuming the United States wins in a hypothetical nuclear exchange with the Soviet Union, it would have lost in comparison to China, the bystander whose nuclear capability would remain intact and who, by default, would emerge as the strongest among the three adversaries.

A few new rules have been called into being as a result of the transformation of the international system into a "no win" era. In the first place, the concept of "massive retaliation" that was for so long the central pillar of nuclear strategy during the previous period is no longer adequate. It has to be augmented by the concept of "reward," as it is incumbent upon all the nuclear adversaries to reward one another for not rocking the nuclear

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\* Professor of Political Science, New York University; Specialist on the foreign policy of the People's Republic of China.

boat. Normalization, therefore, is consistent with the logic of mutual reward in the new era. In order to make the reward structure (*i.e.*, *détente*) work, a few other rules must be observed, including "no first use" of nuclear weaponry, and a commitment not to "gang up" with one against the other adversary. Stability in the system would be greatly compromised if either of these two rules should be violated.

#### THE KISSINGERIAN PREMISES AND THE OPENING TO CHINA

The opening to China and the modality set for it in the Shanghai Communiqué signed by President Nixon in February, 1972<sup>1</sup> followed certain premises, or basic assumptions, which can be identified with Henry A. Kissinger, the architect of Nixon's foreign policy.

The first premise was that the Sino-Soviet split was irreversible. A corollary to this was that the United States could take advantage of the Sino-Soviet split by alternately "tilting" to one end and then the other of the two Communist giants.

The Kissingerian "tilting" strategy ran afoul of one of the maxims (or "rules of the game") of *détente*, namely that none of the three principal adversaries should manipulate either of the other two against the third (*i.e.*, no "ganging-up"). In reality, the tilting did not work for the United States, but alternately alienated the Soviets (hence, the SALT II impasse for a few years) and the Chinese (resulting in reductions in Sino-U.S. trade in 1975-76 and a temporary return to militant rhetoric in 1976).

The second Kissingerian premise was that China was strong enough to be a counterweight to the Soviet Union, but not strong enough to threaten the United States. The obvious fallacy in this premise is its total neglect of the time element. What if at a given time China is strong enough to threaten both the Soviet Union and the United States? A statesman should anticipate such eventualities and make preparations accordingly.

The third premise was that if China was to be encouraged to direct its undivided attention northward to deal with the Soviets, all her "southern" problems — *i.e.*, the Vietnam war and the Taiwan question — must be resolved for her. I would say that the assumption here that decision-makers can deal with only one issue at a time — that China could not simultaneously deal with her colossal North and her "southern" problems — is alarming.

#### THE BRZEZINSKI PREMISES AND NORMALIZATION

The Carter administration's China policy, extending beyond the normalization of relations with Peking, is based on a set of premises mostly

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1. 66 DEP'T STATE BULL. (No. 1708) 435-38 (1972).

formulated by the National Security Council staff headed by Zbigniew Brzezinski and assisted by China specialist Michel Oksenberg.

In the first place, the Brzezinski-Oksenberg team has inherited the three Kissingerian premises above, but has carried the Sino-U.S. triangularity to a fixation in the sense that every aspect of U.S. foreign policy has become a function of an overriding animosity toward the Soviet Union. Whereas Kissinger merely played a "tilting" game, the Brzezinski-Oksenberg team has entrenched the United States in a game of card playing, *i.e.*, playing the "China card" against Moscow. The danger of this card playing lies in its assumption about the *permanence* of the Sino-Soviet split. It neglects the fact that the Sino-Soviet alliance of the 1950s was not the result of a temporary ideological affinity, but of convergent national interests. It was preceded by a secret alliance in the nineteenth century signed by Li Hung-chang and Count Witte in 1896, dictated by a common interest against Japan. Common national interests may again unite the two countries in the future.

Furthermore, the U.S. acceptance, at the Chinese insistence, of the anti-hegemony clause in the final communiqué signed by President Carter and Vice Premier Deng on February 1, 1979, violated the "no ganging-up" prerequisite for *détente* noted above.<sup>2</sup>

The most important Brzezinski-Oksenberg addendum to the Kissingerian legacy is the premise that it is to the U.S. interest to make China a "responsible" actor. There is a twisted logic in this reasoning which runs like this: One, if there is instability in the international political supergame, it is because China has not been acting responsibly. Two, if China has not acted responsibly, it is because she is not strong enough; so let us make her stronger. Three, if there is still no stability, then it is because we have not done enough to make China strong enough to act responsibly; so let us do more to make her even stronger. The implicit assumption here is that once made sufficiently strong, reaching a parity with the Soviet Union, China would be a "responsible" counterweight shielding the United States from the brunt of the Soviet threat. This goes back to the assumption about the *permanence* of the Sino-Soviet rift noted earlier.

The fallacy in the reasoning is its total neglect of the history of U.S.-Soviet relations. The *détente* between the two superpowers became possible only *after* the Soviets had reached a position of nuclear parity with the United States, not before. There is every reason to anticipate a parallel development in Sino-Soviet relations once China has reached parity. At least our policy-makers should not leave out that possibility in their planning for the future.

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2. 79 DEP'T STATE BULL. (No. 2024) 11-12 (1979).

Furthermore, what assurance do we have that the Chinese conception of being a "responsible" actor coincides with our expectations? So far as can be ascertained, a military invasion of Taiwan, considered a province of China, would not be an irresponsible act, since it is, as Peking claims, an "internal affair." A China made sufficiently strong by the United States, with the expectation that she would turn her newly gained strength against Moscow, cannot be contained on a collision course over Taiwan, unless the United States is prepared to abandon the island completely.

The morals from the above are simple and evident: our expectations about the value of the China connection are only as sound as their conceptual bases. Most of the premises crucial to our China policy are either faultily conceived or are not coherent among themselves. Far from having all the obstacles removed in Sino-U.S. relations, normalization has left behind a volcano in the Taiwan Strait, the eruption of which depends on Peking's whims and willful manipulation in the future.

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## COMMENTS

*Jan S. Prybyla\**

My comments relate primarily to the luncheon presentation by Roger Sullivan on the "Value of the Connection." While I find myself in agreement with much that Mr. Sullivan has said, there remain aspects of the presentation which should, I think, be spelled out more clearly than they have been, and there are some areas where we disagree. My comments fall into three categories — facts, ability to pay and ability to absorb.

### FACTS

Sullivan rightly warns against euphoria in the matter of the China economic connection. Some of this extraordinary excitement on our side is generated, no doubt, by the simple, but also illusory, numerical importance attributed to the China market: 1 billion toothbrushes and 2 billion arm-pits. Peking has reinforced this notion with the impression of "no nonsense

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\* Professor of Economics, Pennsylvania State University; Specialist on the economy of the People's Republic of China.

1. For the text of Mr. Sullivan's speech, *see supra* p. 35.

pragmatism" since the arrest of the Gang of Four and the return of Deng Xiaoping to somewhere near the top of China's power pyramid. Arguably, the new leadership is bent on modernizing the country at rapid rates (*vide* the targets of the ten year modernization plan), a process which calls for the acquisition from abroad of huge amounts of very elaborate and very expensive equipment and technological know-how. Presumably, there is room for many sellers — not just for the Japanese who got there first — so that, provided we get in on the deal fast, there will be many benefits accruing to certain American industries and sectors (and also presumably problems for some other industries and sectors such as textiles). Trade with the United States, which now runs at around \$1 billion, is expected to rise to roughly \$5 billion within the next few years.

In pursuing this line of argument, it is useful to bear in mind the distinction between present reality and future potential. The reality is that:

1. the per capita gross national product of China is on the order of \$400–450 but very likely less;
2. the average yearly industrial wage (modern industry) is approximately \$360;
3. the bulk of the peasantry makes about 20¢ per person per day from collective endeavor;
4. the Chinese authorities admit that ten percent of the population (100 million people) do not have enough to eat (other reports speak of 200 million peasants being in a condition of acute privation);
5. per capita grain production today is the same as it was twenty years ago;
6. annual foreign trade turnover is less than \$20 a head; and
7. the \$1 billion current trade with the United States represents one-third of one percent of total U.S. trade.

So, without in any way minimizing the usefulness of the China economic connection, it is good to remind ourselves that as of now we are dealing with 1 billion very poor customers. Moreover, these customers need our grain and technology more than we need their bristles and firecrackers. So, at the very least, we do not have to fall over ourselves in the scramble for a slice of the existing pie.

But what about the future? The Chinese are a prodigiously assiduous people, and the communist regime has shown itself capable of mobilizing the people's energies and channeling them into productive pursuits. The targets of the ten year modernization plan exemplify the determination of the regime to raise income by increasing the productivity of labor, capital and land through massive infusions of up-to-date technology.

I see two problems with these expectations. First, what we do know of the plan raises serious questions about its feasibility. The plan strikes me as a set of random, uncoordinated targets derived from the rule-of-thumb methodology "think of a number, then double it." A plan is a general equilibrium system, an internally consistent set of physical input-output relationships backed by a price structure which reflects fairly accurately the relative scarcities and utilities within the system. Given the state of Chinese economic science, which is still recovering from the severe damage inflicted by the Cultural Revolution, I doubt that anything even remotely resembling a plan in this sense exists in China today. Economists such as Sun Yeh-fang still reel from the beating they got during seven and more years in prison for having once dared to try and construct a socialist economic science applicable to China. Techniques of physical planning — *i.e.*, material balances, input-output tables and linear programming — have been allowed to fall into disuse and surely the price system must be in serious disrepair by now. (For example, the wage structure in industry has not been changed since 1956 despite far-reaching changes in the supply of, demand for and skill composition of labor.)

In this condition, it is curious to see so many business people from so many countries clamoring to get in on the presumed bonanza. I suspect that, in other cases, these very same businessmen and bankers would be more careful. Before extending credit, for example, or setting out on joint ventures, they would insist on more information and perhaps a feasibility study. Yet where China is concerned, one gets the impression that normally cautious and hard-headed entrepreneurs and capitalists succumb to the giddiness induced by target figures pulled out of nowhere by state and party bureaucrats who, but three years ago, were described by their opponents (then in power) as "the scum of the earth." I think it eminently reasonable for us to ask the Chinese authorities to at least let us see the ten year plan in its entirety, not just the spotty outline disseminated by the New China News Agency. A lot of people are likely to go broke if they hitch their fortunes to what looks like an unrealistic and conceptually primitive set of Chinese expectations.

The Chinese authorities are beginning to admit as much. The targets are being reappraised, rethought, retrenched, or whatever the euphemism is for pulling in the reins and taking a hard look at the whole thing. For example, the target of 400 million tons of grain by 1985 is said to be not feasible. The implied growth rate in grain production of four to five percent a year between 1978 and 1985 is quite out of reach. The same applies to the plan to turn out 60 million tons of steel by 1985. (I have heard that as much as half the steel output in China today is below minimum quality standards set by the state). The plans for agricultural mechanization have had to be stretched over a

significantly longer period of time. But as noted before, unrealistic targets are not the only or even the main issue. The basic issue is how the projected inputs and outputs mesh; and I suspect that they do not mesh at all because the Chinese planners have forgotten or do not know that they must mesh. Or they are quite simply too harassed by contrary political demands to do a proper job.

Second, there is almost certainly no agreement within the leadership about the plan. From the changes in direction, the trimming, inflating, equivocating and patching-up, one gets the unmistakable impression of internal discord. The disagreement seems to resolve less around technicalities than around the very conception of a great leap to modernity. Philosophical discord of this kind does not augur well for the future of the plan. Should the effort fail and the high aspirations raised at the dawn of the post-Mao leadership be disappointed, the possibility of a neo-Maoist xenophobic turning inward would, I think, be real. In any event, from the standpoint of the foreign investor and trader, China is not a nearly riskless society. While not lawless, it is still, by and large, without a law. While overall political stability has been demonstrated, there have also been very sharp policy swings. The present relative openness and outreach are not permanent fixtures on China's political firmament, nor are they reliable points to what the future may hold in store.

#### ABILITY TO PAY

China's ability to pay for all the things she proposes to import from Japan and the West hinges on the country's capacity to generate a sufficient volume of commodity and service exports. The repayment problem would be eased for a while if China could secure sizeable long-term credits from Western banks and governmental financial institutions. The major burden, however, falls on commodity exports.

There are three types of commodities which can be used for export in the next ten years: oil, materials from agriculture (*i.e.*, rice, processed foods) and manufactures.

Several problems arise in connection with oil exports. First, the quality of Daging oil leaves much to be desired; the oil has a heavy wax content and calls for the installation of rather expensive dewaxing facilities in the importing countries. Japanese refiners, for example, have done this with the help of sizeable government subsidies. Most of the currently exported oil comes from the Daging oil field, the output of which has probably peaked. Second, the bulk of China's projected exportable oil surplus through 1985 has been committed to Japan under the 1978 Sino-Japanese trade agreement. Of course, there is the possibility of increasing the surplus by drilling offshore.

To reach these deposits, a very large initial investment in exploration and production equipment is needed as well as "know-how." China will have to negotiate some combination of loans and joint ventures involving, perhaps, repayment in the product or even equity participation by foreigners in the joint undertaking. This will certainly add an acerbic edge to the ongoing leadership debate on the wisdom of the rapid and vast modernization drive. While there are no insuperable barriers, and the Chinese hope to use oil as an important means of paying the modernization bill, the oil export prospects over the next decade look less bright today than they did a few short years ago. Incidentally, the currently producing onshore fields are reportedly being used inefficiently and wastefully. Here, too, large investment in oilfield technology and equipment is needed if the resource is not to be squandered. One should also remember that despite China's determination to keep using coal as the principal energy source in the years ahead, modernization of the type and on the scale presently envisioned will inevitably lead to a substantial increase in China's domestic oil consumption. This, too, has to be factored in when estimating China's future oil exporting capacity. Should the most optimistic predictions materialize, China's oil will still be sold at OPEC-type prices.

The main obstacle to expanding exports of agricultural materials is likely to be the problem of raising farm output at rates substantially above the rates of natural population increase. In the past, agricultural output has grown at approximately two percent per year, just marginally above the growth rate of the population. Chinese agriculture has apparently run into diminishing returns to labor and almost the only way out of the quandry is to raise output through increases in factor productivity. This calls for a prior investment in land melioration, chemicalization, mechanization, improved transportation, storage and education, with the price tag in the tens of billions of dollars.

Exports of manufactures will have to negotiate a few major obstacles. First, over one-third of such exports consists of textiles which are import-sensitive in most Western countries and Japan; they compete directly with important domestic industries and evoke protectionist responses in no time at all. The United States has just slapped an import restriction on Chinese textiles. Second, there are problems of marketing Chinese products in highly sophisticated and fickle Western markets; both the quality of the goods and the quality of marketing techniques are at issue. Third, there is the competition from other low cost producers such as Taiwan, Hong Kong and Singapore.

It is not my intention to paint a gloomy picture of China's modernization and foreign trade prospects in the coming decade or so. I am merely trying to inject a dose of sobriety into the consideration of a problem which is complex



and, for the Chinese side, very arduous. I believe the record indicates that the Chinese will find it difficult to raise their hard currency commodity exports to heights consonant with the level of imports desired by them at this time.

Service income includes tourism and hard currency remittances from overseas Chinese. The latter fluctuate over time, roughly in line with China's policy toward the relatives in China of overseas Chinese. In recent times, such remittances came to about \$500 million a year. The new regime's policy on overseas Chinese and their families in China is benign. As long as this lasts, remittances are likely to continue at or exceed current levels. Before tourism amounts to very much, \$1.5 billion will have to be invested in 15,000 new hotel rooms. It is interesting to note that in recent months the People's Republic of China (P.R.C.) has increased her involvement in real estate speculation and hotel ownership in booming Hong Kong.

China's past loan repayment record has been exemplary and on the basis of this performance, the country has an excellent credit rating in the world financial community. In the past China pursued a very conservative foreign credit and balance of trade policy which, as much as anything else, explains the spotless credit history. The policy, now decried by the Chinese authorities, had been to shun joint ventures and long-term indebtedness to foreign banks and governments, and to avoid overall balance of trade deficits. If in any one year a sizeable deficit on the trading account developed, it would be reversed in subsequent years by the simple expedient of slashing imports. In general, until the fall of the Gang of Four, foreign trade was regarded by the Chinese authorities as a residual activity. China went out and bought what she could not make at home, paying with such exports as it could manage to push. Today, the picture is quite different. Foreign trade is taken to be the key link in the modernization process; it is to be actively promoted in the years to come; and a flexible attitude toward credit and other arrangements is to replace the rigidities of the past.

China's credit history is not necessarily a reliable indicator of China's future credit performance. This is not to suggest that the P.R.C. will massively default on her obligations or that she takes such obligations lightly. But China's present borrowing plans bear little relationship to past practice and must be examined on their own precise merits. This cannot be done unless the Chinese authorities release fuller information than they have done so far on their assets, liabilities, reserves and debt service ratios. If China wants to participate in the world economic community, she should be made to understand that continued obsessive secrecy regarding her economic performance constitutes unacceptable conduct. Are Chinese foreign exchange reserves \$2 billion (as reported by the *Christian Science Monitor* on March 28, 1979) or are they \$4 billion (as reported by the Bank for International

Settlements)? Both figures should be set against the tentative \$7 billion in equipment and technology import contracts signed by early 1979.

A whole profitable breed of consultants with allegedly "inside" information has been spawned lately in and around Washington and New York to help American China traders find their way in the dark. Estimates (they are usually referred to as "informed" estimates to lend them a degree of dignity and credibility) of Chinese import plans between 1978 and 1985 range from \$40 billion to \$200 billion — not a very informative range. In 1976, it was estimated that China had a debt service ratio (ratio of foreign repayment obligations to total hard currency earnings) of twenty-three percent, not far from the warning mark of twenty-five percent. A later U. S. government study predicted that the ratio between 1981 and 1985 would range from four to eleven percent and if downpayments are included, the upper limit would be as high as fifteen percent. Later, a figure of twenty-one percent was mentioned for the same period. *Statistics à la carte*; something to suit every taste.

The Chinese make up for the statistical confusion by being the world's most gracious hosts, when they decide to be so. But impeccable manners and hearty fellowship do not make up for the absence of good information flows. That is why I do not go along with the advice given by one U. S. executive (who has had twelve months' experience of dealing with the Chinese). He suggests to "shy away from legalese" and "laugh with them." If I am not mistaken, some such suggestions have also been floated at this Conference. Chinese culture, it is argued, is not our culture. The Chinese (at least on the mainland) dispense with all our "whereas'es" because things are just understood and taken for granted over there, and there is no need to spell them out. You might even offend the chaps by insisting too much on insurance claims when you lend them a billion dollars here and there.

#### ABILITY TO ABSORB

Absorption of advanced technology and equipment has four aspects: technical, institutional, political and cultural. The degree of absorption difficulty varies with the degree of technological sophistication, the size of the transfer and the time span allowed for digesting the new equipment and techniques. The more advanced the technology, the more massive the transfer; the shorter the time in which that transfer is to be accomplished, the greater the absorptive difficulty. Technically, there seems to be little point in importing high technology equipment when supporting services are lacking. It is useless to import a computer when you do not have computer operators or buy a tractor when you do not have tractor drivers, mechanics or repair facilities. Technology, like economic planning, is an integrated process,

not a series of random stabs. I believe that it is precisely in the area of the needed technological linkages that contemporary China is weak. The weakness can be overcome, but not in the time period assigned by the plan.

Institutionally, the question is whether the economy's arrangements are capable of supporting the vast modernization effort. I have discussed this problem elsewhere,<sup>2</sup> and will only mention three factors: poor planning, poor incentives to workers and poor management. The deficiencies of planning have already been noted.<sup>3</sup> Deficient incentives to workers (resulting in a loosening up of "labor discipline") are admitted by the present leadership. To properly motivate the workers — *i.e.*, spur them to use the new equipment and techniques in ways that will raise factor productivity calls for nothing short of a wholesale revision of the wage and rural incomes structures, both as regards the general level of earnings and income differentials. More consumer goods will have to be provided, without which increases in money incomes (already ordered) only make things worse. (Inflation is presently running at about ten percent a year in China.) Raising output by massive organizational means (mass mobilizations of labor) is losing its effectiveness, as are appeals to the workers' sense of moral responsibility, class consciousness and patriotism. The shabby spectacle at the top is not likely to invigorate the masses' flagging moral commitment to socialism. One of the most worrisome problems is sloppy enterprise management, not because of any particular lack of ability among the managerial cadres (although this, too, is a problem with the graduates of the Cultural Revolution), but because of chronic dialectical exercises and the consequent uncertainty of the political line at the top. Managers are paralyzed by fear that what they do today may be used against them tomorrow. There are solid historical grounds for this apprehension. The result is managerial inertia.

Politically, absorption hinges on whether the present modernizing regime will survive the plan it has set for the country. There are signs of rift within the leadership, and the possibility of a return to some of Mao's more obscurantist policies cannot be altogether excluded.

Finally, there is the question of whether China will be able to make the cultural adjustments necessary for the enormous leap into modernity. Massive transfers of advanced technology over brief periods of time have been known to unsettle some developing societies in various parts of the world. It is true that in the last thirty years China was subjected to great cultural transformations and huge value upheavals. Still, the magnitude of the proposed changes, their high technological content and the briefness of time

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2. Prybyla, *Changes in the Chinese Economy: An Interpretation*, ASIAN SURVEY 409-53 (May 1979).

3. See *supra* at 47-48.

allotted to the process will surely put much strain on the fabric of China's rural society.

All these considerations, diverse as they are, seem to be highly relevant to our gaining a balanced perspective of China's modernization, her foreign trade prospects and the value to the United States of the China economic connection.

