The Collaboration with Neighboring Northeast Asian Countries Aspired to in China's Northeast Development Strategy (Summary)

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1. Background

The three northeastern provinces of China assumed a weighty responsibility within the national economy during the era of the planned economy, functioning as traditional bases for heavy and chemical industry. However, in contrast to the Pearl River delta and the Yangtze River delta, which have experienced remarkable development since the policy of reform and opening up, with foreign capital inflows as the driving force, the three northeastern provinces are lagging behind in terms of both the transition to a market economy and the introduction of foreign capital, and factors such as the large share of state-owned businesses have hindered economic development. The Chinese government, which took the situation seriously, formulated a new national strategy entitled the Strategy for Developing Old Industrial Bases in Northeastern China (hereafter referred to as the Northeastern Development Strategy) in the autumn of 2003, and has devised numerous policies, including preferential fiscal and financial measures.

This paper first of all provides an overview of economic problems affecting the three northeastern provinces and economic relations with neighboring Northeast Asian countries. It then introduces the development of the Northeastern Development Strategy and the policy of opening up to the outside world. Finally, it discusses the expectations of Northeast Asian countries with regard to the Northeastern Development Strategy, above all the potential for progress in collaboration with Japan.

2. What Economic Problems Do the Three Northeastern Provinces Face?

(1) Dominance of state-owned businesses

One of the problems relating to the economic structure of the three northeastern provinces that led to the formulation of the Northeastern Development Strategy was the high level of dominance on the part of state-owned businesses. The share of state-owned businesses in industrial production is declining nationwide. Looking at the situation since 1998, we can see that the share of state-owned businesses has fallen from 49.6% — almost half — in 1998 to 35.2% in 2004. This indicates that there has been an influx of foreign capital, as well as the development of domestic private sector companies.

However, the share of state-owned businesses in the three northeastern provinces is still high. The share of industrial production accounted for state-owned businesses in 2003 was as high as 79.5% in Heilongjiang Province, 75.8% in Jilin Province and 58.1% in Liaoning Province. These figures fell slightly in 2004, to 79.1% in Heilongjiang Province and 73.5% in Jilin Province, but they are still high. Incidentally, the share of industrial production accounted for by state-owned businesses was low in regions where the policy of reform and opening up is at an advanced stage of development, standing at 18.4% in Guangdong Province, 13.1% in Zhejiang Province, and 19.0% in Jiangsu Province.

It has been pointed out that management problems faced by state-owned businesses include additional costs arising from their provision of welfare services, such as schools and hospitals, and a lack of corporate governance resulting from the failure to separate businesses from the state.

(2) Lagging behind in investment and the introduction of technology

The second problem in Northeastern China is the decrepit technology and equipment owned by most state-owned businesses. If we look at the investment rate (value of fixed capital investment / GDP) as an indicator of the renewal of technology and equipment, we can see that the investment rate in the three northeastern provinces has consistently been lower than the national average since 1992. While the national average investment rate over the five years from 2000 to 2004 was 43.2%, there was a significant gap between this figure and the averages for Liaoning Province (31.2%), Jilin Province (35.8%) and Heilongjiang Province (27.3%). As investment in equipment in the three northeastern provinces was poor for many years, one can imagine that this region has been lagging behind in terms of the introduction of modern capital equipment.

⑶ Lagging behind in terms of internationalization

With regard to the value of trade for each province in 2004, trade totaled $34.4 billion in Liaoning Province (exports $18.9 billion, imports $15.5 billion), $6.8 billion in Jilin Province (exports $1.7 billion, imports $5.1 billion) and $6.8 billion in Heilongjiang Province (exports $3.7 billion, imports $3.1 billion). The total for the three provinces is $48 billion, accounting for 4.2% of trade in China as a whole.

The main items exported from Liaoning Province are industrial goods, such as machinery, and these also make up the bulk of imports.

The main items exported from Jilin Province in 2004 were corn (11%), clothing (14%) and chicken (4%). Industrial goods form the bulk of imports into Jilin Province, with automobile components alone accounting for 34%.

Heilongjiang Province’s main export items were light industrial goods, such as clothing (31%), footwear (13%) and spun goods (8%), as well as machinery and electrical equipment (13%), while major imports included machinery and electrical equipment (28%), logs (20%), crude oil (8%) and pulp (6%) (2004).

Looking at the per capita value of trade in 2004, we can see that whereas the national average was $888, Liaoning Province recorded a level of $816, Jilin Province $251 and Heilongjiang Province $178; the low levels in the latter two provinces are particularly striking. With regard to other coastal areas, the level is higher in areas where reform and opening up have progressed further, reaching $9,185 in Shanghai, $6,335 in Beijing and $4,300 in Guangdong Province.

If we look at the receipt of foreign investment, an even more pronounced disparity emerges. With regard to the use of foreign capital in the three northeastern provinces, while it is growing in Liaoning Province, it remains at a low level in Jilin and Heilongjiang provinces. Looking at per capita receipt of foreign capital (2004, in real terms), whereas the national average is $49, the figure for Liaoning Province is high, at $128, but the figures for Jilin and Heilongjiang are very low, at $7 and $9 respectively. With regard to other coastal areas, Shanghai recorded a figure of $362, Guangdong Province $121, Jiangsu Province $94 and Beijing $171. Among the three northeastern provinces, the backwardness of Jilin and Heilongjiang provinces in attracting foreign capital is irrefutable.

The image of the three northeastern provinces that we can perceive from these data, particularly the characteristics of Heilongjiang and Jilin provinces, is that old-established state-owned companies have been preserved, but these have missed the wave of modernization; they do not conduct much external trade, nor do they receive foreign investment, so they are in a semi-isolated state. However, exceptionally, internationalization is progressing in Liaoning Province, particularly in Dalian.

The direction to be pursued in seeking solutions to such problems affecting the economies of the three northeastern provinces is clear. In order to reduce the share accounted for by state-owned companies, while increasing the share of non-state-owned companies, it is necessary to privatize state-owned companies, nurture private sector companies and introduce foreign capital. As will be described later, the penetration of foreign capital is greatly welcomed within the Northeastern Development Strategy; in particular, it is hoped that equity participation in state-owned companies will take place, by means of mergers and acquisitions. The penetration of foreign capital will undoubtedly contribute significantly in terms of jump-starting trade and investment, which were lagging behind markedly in the three northeastern provinces. Investment is a structure that begets trade; for example, in Jilin Province, where Volkswagen (VW) of Germany has built a plant, automobile components account for 33.8% of imports, making Germany Jilin’s largest trading partner in terms of imports (54.7%) (2004). Due to the fact that Toyota has also built a plant in Changchun, which has begun operations, it is thought that imports from Japan will increase in the 2005 statistics. New investment projects, such as those implemented by VW and Toyota, are also vital in terms of the import of technology. New investment is combined with new technology, increasing productivity, and through collaborative efforts, China can obtain advanced technology and business management know-how.

3. Economic Linkages with Northeast Asian Countries

Trade focused on the Northeast Asian region has continued to demonstrate remarkable growth in recent years. According to the statistics for 2004, trade between Japan and China totaled $167.9 billion (up 25.7% on the previous year), that between China and the ROK $90 billion (up 42.5% on the previous year) and that between Japan and the ROK $66 billion (up 26.1% on the previous year). Furthermore, trade with Russia is also growing rapidly, with trade between Japan and Russia totaling $9.9 billion (up 66.3% on the previous year) and that between China and Russia $21.2 billion (up 34.7% on the previous year). In addition, according to preliminary figures for 2005, trade between Japan and China seems to have totaled $184.5 billion, while that between China and the ROK apparently amounted to $100.6 billion.

A number of features can be seen in Northeast Asian trade, focusing on China and its three northeastern provinces.

Firstly, the countries of Northeast Asia are important trading partners for China. Looking at the trading partners of China as a whole, we can see that the total for the five countries of Northeast Asia (Japan, the ROK, the DPRK, Russia and Mongolia) is $281.3 billion, accounting for 24.4% of the total ($1,154.8 billion). Of the Northeast Asian countries, Japan is China’s largest trading partner, accounting for 14.5% of the total, with the ROK accounting for 7.8%.

Secondly, the importance of Northeast Asian countries is even more pronounced as far as the three northeastern provinces are concerned. Looking at the trading partners of the three northeastern provinces, we can see that the five countries of Northeast Asia account for 44.9% of total trade. Of these countries, Japan is the biggest trading partner, accounting for 23.9%, followed by the ROK, which accounts for 10.8%. Moreover, looking at the situation on the basis of partner countries, 77.2% of trade between China and the DPRK takes place via Liaoning and Jilin provinces, while 18.0% of trade between China and Russia takes place via Heilongjiang Province, demonstrating the strength of economic links between regions that neighbor each other across national borders.

Thirdly, the three northeastern provinces each have their own characteristic trading partners, with the countries of Northeast Asia occupying important positions *vis-á-vis* each province.

Japan is the biggest export partner for Liaoning Province, accounting for 28.9% of total exports in 2004, followed by the US with 15.8% and the ROK with 12.2%, and the shares of these two countries are growing. In addition, the share of Liaoning's exports accounted for by Japan, the ROK and the DPRK reached 43.3% in 2004.

Japan is also Liaoning Province's largest import partner, accounting for 26.8% of imports in 2004, with the ROK in second place, accounting for 12.7%. In 2004, the share of imports accounted for by Japan, the ROK and the DPRK was 41.3%.

With regard to Jilin Province's major export partners, Japan is in first place (21.2%), followed by the ROK (20.3%), the US (8.3%) and the DPRK (7.6%) (2004). The share of exports accounted for by Japan, the ROK and the DPRK was 49.1%.

As far as Jilin's import partners (2004) are concerned, Germany accounts for the majority (54.7%), followed by Japan (20.7%), which is increasing its share rapidly. Most of the imports from Germany are parts imported in order to assemble cars at Volkswagen's Changchun Plant. The share of imports accounted for by Japan, the ROK and the DPRK was 26.2%.

Historically, economic links between Heilongjiang Province and Russia have been strong. With regard to major trading partners in 2004, Russia accounted for more than half of all exports (58.5%) and imports (53.7%). Consumer goods, fruit and vegetables are exported to Russia from Heilongjiang, while timber and oil are imported overland from Russia. Other export partners include Japan (7.1%) and the ROK (5.9%), while import partners include the US (8.8%), the ROK (7.0%) and Japan (5.7%). In addition, the share accounted for by Russia, Japan and the ROK was 71.5% in the case of exports and 66.4% in the case of imports.

4. The Progress of the Northeastern Development Strategy: Results and Issues Over Two Years

Over the two years or so since the plan was announced, the Northeastern Development Strategy has undoubtedly begun to get underway. Domestic policies include i) promoting the reform of state-owned companies; ii) providing financial support; iii) instituting preferential tax measures; iv) establishing a social security system; and v) regenerating resource-focused cities. Furthermore, measures devised in order to promote opening up to the outside world include measures aimed at promoting use of foreign capital and collaboration with neighboring Northeast Asian countries.

⑴ Domestic policy measures and their outcomes

The reforms of state-owned companies are multifaceted. The restructuring of mainly poorly performing state-owned companies by means of mergers and acquisitions is gaining momentum. More specifically, large-scale mergers have taken place in such fields as coal mining, iron and steel, special steel and machinery manufacturing. Moreover, institutional reforms of small and medium-sized state-owned companies under the control of the governments of each province are taking place, with the diversification of rights in 100% state-owned companies being put into practice by means of such methods as stock transfers and transformation into joint stock companies. Furthermore, policy support for the closure or bankruptcy of state-owned companies that would find it hard to achieve recovery is being implemented. In particular, the policy of closing coalfields and mines where resources have been depleted and redeploying employees has been taken. With regard to state-owned companies where management is deteriorating, relief measures have been implemented, including exempting them from interest on loans, and the disposal of bad loans is also taking place. One of the factors putting pressure on the management of state-owned companies is the fact that they incorporate administrative divisions and welfare facilities, such as schools, hospitals and police, but schools and hospitals have been transferred to the government and work is taking place aimed at separating divisions that are auxiliary to production.

The central government has reinforced its provision of financial support for structural adjustments and priority projects, in such forms as government bond projects. Moreover, the China Development Bank is providing additional funding for infrastructure projects.

As a preferential tax measure, waivers of agricultural taxes were applied from 2004 in both Heilongjiang and Jilin provinces, which led to an expansion in agricultural production. Moreover, there were widespread reductions in value-added tax and the depreciation period was also reduced.

With regard to the social security system, companies bore the entire financial burden hitherto, but since 2002, an initiative has been being tested in Liaoning Province, under which the central government, the provincial government and the company each bear one-third of the burden. This scheme has since been being tested in Jilin and Heilongjiang provinces as well.

⑵ Measures promoting opening up to the outside world

One of the aims contained in the Northeastern Development Strategy is expanding the opening up of the northeastern region to the outside world and intensifying trade and investment. Furthermore, there are high hopes that foreign capital can be used to promote the restructuring of state-owned companies. On 30th June 2005, the Chinese government promulgated its "Opinion on Further Expanding Opening up to the Outside World in Promoting the Development of Former Industrial Bases in the Northeastern Region" (Information Office of the State Council, No.36, 2005). This is frequently cited as Document No.36 and is considered by parties within the governments of the three northeastern provinces who are involved in the formulation and implementation of development strategies for the development of former industrial bases to be a sort of bible for this policy. Its key points are listed below.

i) Promoting foreign capital in such a way as to contribute to the restructuring of state-owned companies, and accelerating systemic and structural reforms: The government will encourage mergers with, acquisitions of and equity participation in state-owned companies by means of foreign capital, upgrade the normative environment required in order to do so, and provide preferential measures for foreign capital. For example, if foreign capital is used to acquire a state-owned company, the government will provide such benefits as waiving the state-owned company's past unpaid taxes.

ii) Supporting investment by foreign companies in firms in priority business fields: Priority business fields include modern agriculture, processing of agricultural produce, equipment manufacturing, chemical industry and hi-tech industry. Foreign investment projects in fields being promoted can benefit from beneficial import tax revenue policies. Moreover, investment by foreign companies in research and development centers, as well as in succeeding and alternative industries in cities where resources have been depleted, will be promoted.

iii) Opening up to the outside world will be expanded to service industries: Limits on the percentage of stock that can be held by foreign interests will be eased. The policy of opening up to the outside world will be extended to such industries as the financial services industry, the transport industry and the distribution service industry.

iv) The geographical advantage of the northeastern region will be utilized and the sound development of the regional economy promoted: Economic exchange with neighboring countries will be promoted and cooperation deepened in such fields as trade and investment, science and technology, and tourism. Moreover, international cooperation in the Tumen River area will be expanded, with the construction of border economic cooperation zones and export processing zones being accelerated in such places as Heihe, Suifenhe, Hunchun and Dandong. Furthermore, the development of the Dalian Northeast Asia International Marine Transport Center will be speeded up.

v) Promoting environmental improvements in order to achieve development and opening up to the outside world: Conditions and environments beneficial to the operation of foreign-invested companies will be extended. Existing development zones will be used in order to welcome partners from advanced countries. Infrastructure construction, such as the East Northeastern Region Railway, will be promoted, as will human resource development and the introduction of foreign capital to small and medium-sized companies.

In response to the central government's policy of promoting the opening up of the northeastern region to the outside world, various preferential measures concerning the introduction of foreign capital have also been prepared at the provincial level. Consequently, a three-tier system of preferential measures for foreign capital will be provided, consisting of measures provided for China as a whole, measures provided under the Northeastern Development Strategy and measures provided at the provincial level. Incidentally, no time limit has been set for the preferential measures for foreign capital.

(3) Questions concerning the restructuring of state-owned businesses

Two years since the Northeastern Development Strategy got underway, one could say that the policy measures implemented by the central government and the governments of the three northeastern provinces are at the trial and error stage. Questions concerning the reorganization of state-owned businesses at the current stage include i) Will the reorganization of large state-owned businesses under the control of the central government progress?; ii) Will the systemic reforms of state-owned businesses being promoted be effective in enhancing competitiveness?; iii) Will foreign capital investors cooperate in the reorganization of state-owned companies?; and iv) Will it be possible to eliminate the deep-seated resistance to privatization?

5. Can Northeast Asian Countries, Including Japan, Live Up to Northeastern China's Expectations?

(1) Attracting foreign investment and cooperation in the restructuring of state-owned businesses

What I have felt when visiting various parts of Northeastern China is the fact that the attraction of foreign capital has become the focus of attention solely from the perspective of promoting the region's opening up to the outside world. Furthermore, hopes are high that foreign investors will assist in the reorganization of state-owned businesses.

Although, amidst this situation, there are extremely great expectations with regard to Japanese companies, Japanese companies themselves seem to be cautious about cooperation with state-owned companies in Northeastern China. It is likely that there are several factors behind this.

Firstly, Japanese companies think, "We do not want to be directly involved in the reorganization of state-owned companies in China". The true feelings of Japanese companies can perhaps be summarized as follows: "We want China to implement reforms, and if, after these reforms, state-owned companies have attractive technologies and market power, and we judge them to be advantageous collaborative partners, we will cooperate with them."

Secondly, Japanese companies want to implement new investment (green field investment), rather than acquiring old companies.

Thirdly, there is a mismatch of business sectors.

Fourthly, the upgrading of the investment environment is crucial. One receives the impression that the inland area north of Dalian is inconveniently situated a long way away, so the development of an attractive investment environment is required, by such means as improving access and cultivating workers who can speak Japanese.

In order to attract Japanese companies, it would be practical for China to conduct such reforms as rationalizing the management of state-owned companies, separating off welfare-related divisions, and consolidating unprofitable divisions; then, once it has been regenerated as a company with abundant potential, it should seek possibilities for cooperation with Japanese-affiliated companies. With regard to the form of cooperation with foreign capital, not only equity participation — including mergers and acquisitions — in state-owned companies, but also the attraction of new investment (green field investment) should be prioritized. In addition, in the industrial sector, investment in a wide range of fields, including light industry and service industries, should be welcomed, rather than insisting on investment in existing heavy and chemical industry. Furthermore, the upgrading of the investment environment is essential in order to accelerate the attraction of Japanese companies to inland areas. If foreign capital advances into a range of fields in a variety of forms, the share accounted for by state-owned companies will decrease in relative terms as a result.

⑵ Cooperation within Northeast Asia

Russia is already Heilongjiang Province's largest trading partner, with timber exports in particular accounting for 20% of the total value of imports into Heilongjiang Province. Russia is now trying to market its energy resources and has plans to sell its electricity and natural gas to China. Pipelines and other transport infrastructure are required in order efficiently to conduct trade in energy.

The development of overland transport routes is being proposed, with a view to intensifying Sino-Russian trade. In Heilongjiang Province, the idea of constructing a bridge over the Amur River between Heihe and Blagoveshchensk has been raised, but problems still remain with regard to coordination with the Russian side.

The improvement of the corridor that runs from eastern Heilongjiang Province to the Japan Sea via ports in Russia's Primorsky Krai is also crucial. Devising soft measures to facilitate transit across the Sino-Russian border would be desirable, as would the expansion of the area within which trucks from each country are permitted to operate within the other country.

With regard to the upgrading of the corridor that runs from eastern Heilongjiang Province to the Japan Sea via ports in Russia and the DPRK in the lower reaches of the Tumen River area, the improvement of road and rail infrastructure within the DPRK is deemed to be imperative.

Within the three northeastern provinces, work aimed at modernizing the railway between Dalian and Harbin, and making transport along it faster, is progressing and there are plans to construct a high-speed railway line solely for the transport of passengers. Moreover, the completion of the East Northeastern Region Railway, linking the areas of the three northeastern provinces along the eastern border with the existing railway, is also anticipated.

There are plans to upgrade the railway line (the Gyungui Line) running from Liaoning Province to the ROK via the DPRK, and to operate services along it. If the Gyungui Line begins operating, transport times and costs will be reduced compared with marine transport, which is the transport route currently used between the ROK and China, and access from the ROK to the three northeastern provinces will be improved.

6. Conclusion

I would like to salute China's endeavors in undertaking the gargantuan task of dealing with the legacy of the planned economy. Moreover, Japan, as China's neighbor, should cooperate to the maximum degree possible, and this institute would like to be of assistance in such matters as making approaches to Japanese companies. Furthermore, we intend to continue to contribute to the strengthening of multilateral economic and technological cooperation within Northeast Asia.

China's Northeastern Development Strategy has got off to an excellent start, but it is still in its early stages and is likely to face a variety of difficulties in the future. I sincerely hope that the outcomes of this strategy will be talked about a few years hence in terms of many successful experiences.