

SOUTH-WESTERN CHINA OVERVIEW

A major shift in Chinese infrastructure expenditures is driving major regional projects in the transport, IT, energy, environment, and education sectors, where Canada is globally competitive. South West China's share of the national economy is expected to jump from 10 % to 15 % in the next decade, substantially expanding real markets for Canadian products and services positioned to exploit growth in this resurgent region.

Canada's initiative to open the Chongqing Consulate five years ago anticipated substantial new market opportunities, but it is only in the past year that the West's growth has outpaced the coastal regions. Since January this year, 55 to 60 % of all central government infrastructure expenditures have been directed to China's west, fuelling a building and housing boom and major infrastructure projects that has lifted regional growth well above 9 % in the main urban centres. Average growth figures now mask substantial divergences, as one emerging economic corridor (Chengdu-Chongqing) and two urban centres (Kunming, Guiyang) present elevated standards of living matching the coastal regions, while very large central and provincial government's expenditures are driving substantial market opportunities in sectors where Canada had a recognised comparative advantage. Over 20 million urbanizing residents in the Chongqing-Chengdu corridor represent the largest growth of any province over the next five years. Considered in addition to the existing 26 million urban dwellers in the Sichuan basin and Chongqing corridor with average incomes 40 % above the national average – these emerging Chuppies and urbanizing aspirants will develop into an influential market force in the next five years, even more so if WDS flows are maintained.

China's South West offers a large and growing market to producers of a wide range of goods and services for industrial use and retail consumption. The SW region's population of 180 million provides a US dollar market that when measured in terms of purchasing power parity is 2.75 times greater than the Viet Nam market, double the size of the Malaysian market, nearly 30 % larger than the Philippine market, and about 10% larger than the Thailand market. Moreover, the SW region's current GDP comes to about 74% of the GDP of Indonesia.

South-Western provincial markets already compare favourably with the national markets in many Asian countries. Sichuan's GDP is about equal to that of Malaysia; Yunnan comes to about two-thirds of the Vietnamese GDP, and even Guizhou, one of China's smallest and least prosperous provincial economies, has a GDP one-third of the Viet Nam figure. While standards of living are of course still quite low in the Southwest, the region's GDP/capita, was almost 10 % above the Viet Nam average, was within 10% of the India average – this amounts to about one-half of the Philippines average and over one fifth of the Indonesian average. A quick review of China's overall economic growth data fails to single out the significant specific opportunities emerging under WDS-led infrastructure expansion. There are parts of the Southwest China market that compare favourably now with markets in the more highly developed PRC provinces. Kunming, the capital of Yunnan, is a modern, prosperous, rapidly growing city that offers an urban market of 2.1 million people who enjoy a standard of living that is nearly four times higher than the national average. In Sichuan and Chongqing, an urban corridor is starting to emerge that begins at Mianyang north of Chengdu, runs through Chengdu and ends in Chongqing. This is one of the most industrialised and densely populated parts of China. The 26 million urban residents who live along this corridor, constitute 23% of the total combined population of the two provinces, and have GDP/capita that on average is 42% above the national standard. In the case of the 7.3

million urban residents in the city of Chengdu and the surrounding area, GDP/capita is more than double the national average. In short, there are many areas of relative prosperity and quite high growth in the Southwest Region, which on average is below the national norm in a wide range of socio-economic indicators.

The recent World Bank futures study of the Yangtze Valley (half of China's GDP) used a relatively conservative base-growth scenario that GDP in the Southwest would expand at the annual average rate of 6.3% from 2000 to 2010; then by an average of 5.6 % from 2010 to 2020. GDP/capita in the Southwest would expand by 6.0 % per year from 2000 to 2010, compared to the national rate of increase of 6.2 %, and by 5.3 % per year from 2010 to 2020, when the national growth rate is estimated to be 5.5 %. Measured in terms of US dollars and purchasing power parity (Table I above), Southwest Region GDP in 2010 would be \$US 763.2 billion and in 2020 it would be \$ 1,311 billion. These are conservative figures - should WDS flows maintain current growth levels, incremental growth will be 50 % higher (9 % vrs 6 %). A visit to the region would underline that the South-west is booming, with a real growth rates pushing 9 %, thus sopping up much of the displaced Three Gorges settlers, and disadvantaged rural unemployed now streaming into Chongqing and Chengdu. In terms of market size, the Southwest region in 2020 would be comparable to the current markets provided by Brazil, France, Italy, and the United Kingdom, and would be 80 % larger than Canada's GDP in 1999. Standards of living and consumer purchasing power in the Southwest will also move much higher. GDP/capita in purchasing power parity terms would be \$US 3,822 in 2010 and \$6,410 in 2020. The 2020 figure would move Sichuan into the ranks of the current middle income countries such as Brazil, Columbia, Croatia, Venezuela and Thailand. Competitive Moves: In response, Canada's competitors are ramping up their presence and support capabilities to capture their fair share of the real market opportunities emerging under the Western Development Strategy (WDS).

125 out of the Fortune 500 giants have already invested in this region (Sichuan, 70, Chongqing: 35, Yunnan, 15, Guizhou 5), such as Motorola, BP Amoco, Toyota, Ford, Siemens, Alcatel, Lafarge, P&G, N-Mart, Metro, Carrefour and Wal-mart. There are more than 140 Canadian or Canadian invested companies, JVs and Canadian corporate representative offices in the Consulate's territory (mostly in Sichuan 105), such as Nortel, Nordx/CDT, MRF, Cell-Loc, InterLandBank, ISPAT, Sunlife, Scotia Bank and Davey International.

CHONGQING

Chongqing Municipality covers 40 administrative districts and counties (cities). Chongqing has a total population of over 30m, around 6m (20%) of whom are urban residents. Chongqing was the home to Canada's first Embassy in China when the city served as China's Wartime Capital during the Second World War. Chongqing is twinned with Toronto.

Chongqing, which was once the second city in Sichuan province, rates as the chief industrial city of SW China, while the provincial capital of Sichuan, Chengdu, serves as the retail and financial centre. In 1997, Chongqing was granted the status of provincial level municipality directly under the Chinese Central Government. It is one of four such municipalities in China, and the only one in Western China. The patronage of former premier Li Peng (the driving force behind the Three Gorges dam project on the Yangtze) and Deng Xiaoping (a native of the Chongqing area) are said to have been key to this elevation. The central government is

now promoting Chongqing as one of the major hubs for economic growth and reform under the Western Development strategy.

The municipal authorities undoubtedly face a major challenge in realising the city's appointed role as a spur for economic growth in SW China. There is an ageing loss-making heavy industrial base - the main industries are automotive and iron/steel - and considerable difficulties to overcome luring foreign investors, especially those in export - oriented fields, away from established coastal investment destinations. They also have to factor in the needs and problems of a predominantly rural population. There has been some progress. Expanding the private sector was made a top priority for Chongqing and this sector now employs more people than the state sector, although most workers are in mini-enterprises. Restructuring inefficient state-owned enterprises and shedding a surfeit of employees has also greatly contributed to growth in the private sector. Private enterprise contributed 36% to overall GDP in 2000, and the forecast is that this will reach 55% by 2005.

GDP growth in 2002 was 9%, fuelled in no small part by expenditure funded by state bonds for capital and infrastructure development. Fixed asset investment reached RMB 51bn (+18.5%). This year's GDP growth target is 8.5%, and the forecast for fixed asset investment is an ambitious 20%. The average urban income in Chongqing last year was RMB 6,200, up 5% to about one quarter of the level in Shanghai; rural incomes are less than a third of that. Utilisation of foreign capital is forecast to almost double to US\$500m in 2001. Foreign-funded enterprises now account for 18% of the city's total tax revenue, and employ over 100,000 people.

According to a recent survey by "Fortune" magazine, Chongqing came fourth among investment destinations in China after Shanghai, Beijing and Shenzhen. Some local investment incentives are offered to negate, or compensate for, comparative disadvantages. Chongqing has two development zones, the Chongqing Economic and Technological Development Zone; and the Chongqing High-Tech Development Zone. Over 230 overseas enterprises are established in the first of these, with total investment of over US\$1bn; but there is no Western company to date. According to a recent Business Week article, the Chinese Government is planning to pump US\$ 200 bln into this municipality over the next decade to further turbocharge the growth of its economy.

When the Three Gorges dam is completed in 2008, the government hopes that the dam will stimulate growth in the Yangtze Economic Region which stretches over 9 provinces and has a population of over 200m. Chongqing will directly benefit by being located on a major artificial lake, which will allow much larger, ocean-going, vessels to unload at its docks. The dam will make Chongqing a deep water port - navigable by ocean vessels up the Yangtze River all the way from Shanghai. This will offer great opportunities for future economic development and Canadian investment and make the location much more attractive.

There are around 25 Canadian companies with investment or commercial interests in Chongqing, mainly in the sectors of IT, telecommunications, real estate development, forestry, Education as well as transportation. Major Canadian players in Chongqing include Nortel, Harris, Cell-Loc, Nordx/CDT, SNC-Lavalin, Alcatel Canada Transport, Bombardier Transport, Cummins Westport, UBC, University of Waterloo, Quebec Government, as well as a number of Canadian SMEs.

SICHUAN PROVINCE

Sichuan province covers 5% of China's total territory, and is just a little smaller than France. The population is over 85 million, 7% of the national total, and around 80% are rural inhabitants. The province is land-locked and over 1600km away from any seaport. Sichuan is rich in natural resources. It has the largest exploitable water resources in China, and is among the foremost producers of coal, natural gas, chemical fertilisers, electricity and a wide variety of minerals. It is also one of the most fertile and productive agricultural areas in China, and is Western China's largest grain producer. Sichuan is home to 85% of the world's giant pandas and has other major tourist attractions. Chengdu is the political, economic and cultural hub of the province. It serves as the regional centre for services, science and high-tech industries. Chengdu has a total population of just over 10 million, many of whom live in the rural suburbs.

In the 1950s, heavy and defence-related industries were relocated from coastal areas to Sichuan for strategic, rather than economic, reasons. The aerospace and nuclear industries remain important, but many of these industries are now being restructured. There is a large pool of technically skilled workers available as a result, augmented annually by graduates from the province's large number of technical universities and institutes. The cities of Chengdu, Deyang and Mianyang are being developed into a high-tech corridor to take advantage of the skills pool.

Sichuan accounts for one third of the GDP of the entire western region of China. In 2000, Sichuan's GDP recovered from a sluggish 1999 and reached RMB 401bn, up 9%. The provincial economy is projected to grow by 8% in 2001. Average GDP for urban residents in the province in 2000 was RMB 5894, an increase of 7.5%. Chengdu continued to experience strong growth, with an increase in GDP of 10.8% over 1999, due largely to significant increases in fixed asset investment. The annual average urban income in Chengdu now stands at RMB11000 and not surprisingly, there are concerns of growing development gaps between Chengdu and the rest of the province.

Sichuan leads the field in bringing in FDI in Western China. This Province has attracted approximately US\$13bn and utilised US\$6.8bn in over 6,000 firms. A recent "Fortune" survey showed that Sichuan is rated sixth in China by foreign investors in terms of the investment environment. The major sources of foreign investment are Taiwan, Hong Kong and the US, and investment is mainly directed at the property, energy, manufacturing, building materials and electronics sectors. Foreign investment in mineral exploitation is being actively sought - the main deposits are around Panxi. To the end of 2000, Sichuan had approved a total of 48 British-invested enterprises, with contracted capital of US\$146m, and utilised capital of US\$59m.

To encourage foreign investment, the Sichuan government offers a package of preferential policies. In 2000, Sichuan saw significant increases in the total amount of foreign investment actually utilised (US\$960m, including US\$440m of foreign direct investment). 32 multi-national companies now have a direct investment in Sichuan.

Chengdu is a centre for electronics (the fourth largest in China), machinery, food processing, petrochemicals, textiles and aerospace. There are almost 3000 overseas funded enterprises in Chengdu. In 1999, contracted foreign investment reached US\$410m, and utilised foreign capital US\$230m (28% up on 1998). There are over 105 Canadian-invested establishments or Canadian representative offices in Sichuan. Chengdu is twinned with Winnipeg.

FOREIGN PRESENCE IN SOUTHWEST CHINA

Over the past 5 years, 12 national competitors have opened trade offices or Consulates in the South-West, particularly in Chengdu. UK, Japan, Singapore, Malaysia, Thailand, Korea, Australia, Italy, Netherlands, Britain, and France all have opened trade offices in Chengdu in the past 18 months. Both Germany and France have delivered subsidised loans over the past two years to build an increased presence from their construction, environment, energy and transport sectors. The Spaniards, Danes, Koreans and Australians have stated that they intend to open Consulates in Chongqing.

The UK Con Gen and British Council Office opened in Chongqing three years ago with a focus on public diplomacy, education and trade development (in order of priority). The UK Con Gen is staffed with a HOM and an Administrative/Commercial Consul as well as 9 commercial and support staff. The British Council Office is staffed with a British manager, an expatriate staff member and 17 locally engaged officers. They are about to open a visa office at some point in time in the first half of this year. According to LES sources, the UK ConGen has decided to refocus its resources on public diplomacy and education in order to use them as vehicles to significantly raise this region's awareness of UK's capabilities in the commercial sectors. It is noteworthy that the British Council initiative to make various scholarships widely available for local government decision makers and business leaders to study for a degree in UK has served the purpose well to shape and reinforce pro-UK attitudes amongst the local government and business community.

The Japanese ConGen established just prior to Canada, five years ago, has 6 Foreign Service Officers and 11 locally engaged staff, reinforced by major JIBC credits, and JETRO-supported local groups have 60 Japanese businesses in Chongqing and over 100 in Chengdu. The Japanese ConGen also operates a visa office in Chongqing. The Japanese ConGen concentrates on political and economic reporting and looking after the interests of Japan's already-established and prominent business presence in this area.

The Americans established a ConGen in Chengdu in the mid 80's, and now have 18 Foreign Service officers and 64 locally engaged staff (plus a contingent of marines) to support an American commercial presence of 117 firms and offices in Sichuan (the Chengdu American Chamber of Commerce has over 60 members). The US ConGen focuses on political and economic reporting and trade development program.