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The first American ship to trade with China, the Empress of China, arrived in Canton on August 28, 1784. Captain John Green sold all the goods carried on his ship and proceeded to buy Chinese products for the American market.

Americans have long viewed China as a market of vast potential. Today, 200 years after the visit of the Empress of China, this market of 1.1 billion people continues to beckon American business people attracted by China's open door policy of encouraging foreign business to invest and joint venture in China. While the People's Republic of China (China) has taken other steps to this end, one of its most positive efforts to expand its commercial ties with the West has been the establishment of the new Special Economic Zones (SEZs). Since 1979 China has established four SEZs to attract Western capital and technology.

Three of China's SEZs are located in the Guangdong Province adjacent to Hong Kong: the Zhuhai SEZ is near the Portugese trading port of Macao; the Shenzhen SEZ is across the border from Hong Kong; and the Shantou SEZ is 160 miles north of Hong Kong. The fourth SEZ, Xiamen, is located in Fujian Province, north of Guangdong Province.

These SEZs were established when the People's Republic of China Government in Beijing adopted its new "open door strategy" to expand

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its economic ties with the West. The SEZs are primarily experimental models whereby the Chinese test various methodologies of doing business. If successful, they can apply these methods to the general laws governing the conduct of Chinese business relations. The best investment opportunities to date in China are through the SEZs.

Chinese leaders and scholars have identified the objectives to be achieved through four SEZs as follows:

(A) To obtain more direct overseas investment along with an influx of sophisticated technology and basic equipment;

(B) To improve Chinese managerial skill in the course of acquiring essential experience in the conduct of international business;

(C) To use the SEZs as experimental models from which the Government can take guidance in the reformation of China's economic institutions;

(D) To expand China's foreign trade, increase the country's foreign exchange earnings, strengthen China's position in the world market, provide more consumer goods, and meet domestic needs while developing an advanced technology;

(E) To train and employ Chinese workers;

(F) To influence Taiwan and Hong Kong both politically and psychologically.

In contrast, foreign investors' objectives for operating in SEZs are as follows:

(A) To obtain lower production costs than in other Asian countries and elsewhere;

(B) To operate in a developed infrastructure—including transportation, communications facilities, electric power, water supply, and factory buildings—those elements necessary to support the development of middle and large industrial projects;

(C) To deal with more flexible economic institutions based on a market mechanism;

(D) To penetrate China's vast domestic markets;

(E) To obtain the SEZs' relatively lower tax rates and easier customs duties than are found in other countries and elsewhere in China;

(F) To operate in an environment of relative political stability and reliable legal procedures.

Generally, the SEZs have satisfied these objectives. For example, in 1985, 1,300 Sino-foreign joint ventures were created—the equivalent of the number established in the previous five years. Additionally, China's four Special Economic Zones have attracted $1.2 billion in direct foreign investment over the last five years—about one-fifth of the foreign investment in all of China. Finally, 900 new factories with new technologies and equipment have been built. These factories are producing a total industrial output equal to $4.8 billion yuan, five times the industrial output in 1979.

The SEZs provide many incentives and advantages. First, the zones depend heavily on foreign investment for development, whereas other parts of China rely on budget appropriations from the State. As a result, investors in the zones have greater freedom, and their economic development is largely guided by market demand rather than central planning.

The SEZs also represent an important advance in the decentralization of China's decision-making system. The basic mechanism in the SEZs is no longer planning, but rather a market mechanism directly related to the international market. The SEZs can be viewed as a part of the world economy rather than as a part of the Chinese economy. This is because their ties with the international market are more important than their contacts with other parts of China. In addition, there is very little Communist Party control of enterprises within the SEZs.

There are other incentives as well. Sino-foreign joint ventures and foreign businesses in the zones are exempt from import duties when they buy foreign equipment, raw materials, vehicles, and spare parts for their production. Their products, when sold abroad, are exempt from export duties.

Businesses in the zones enjoy the lowest income tax rates in the country. They pay fifteen percent, compared to thirty-three percent elsewhere. In addition, industrial, agricultural, and transport companies, with the approval of the local SEZ governments, are not required to pay any income tax until the third year after they begin to make profits.

Sino-foreign joint ventures may be undertaken for as long as fifty years in the zones compared to thirty years in most other parts of the country. Factories in the zones also pay a lower fee for land use, from ten to one hundred yuan per square meter.

Foreign currency exchange management in the zones is also different. Businesses utilizing foreign investment may keep hard currency earnings for reinvestment rather than hand over the bulk of these earnings to the state.

Factories in the zones, with approval of the local governments, may also buy and sell directly overseas without going through designated trading companies. Although factories in the zones are encouraged to expand overseas markets, the state does allow some domestic sales of advanced technology products.

The four zones have drafted business regulations to guide local economic development. Land has been prepared for industrial development and large numbers of factories, office buildings, residential areas, and transport connections have been built.

An exemption from or reduction of import duties on importation of machinery and equipment, spare parts, raw materials, and transportation equipment needed for production is available. A reduction of or exemption from tax on the portion of profits reinvested in the SEZs in projects which exceed five years is also available.

If the investment in the SEZ is involved in educational, cultural, scientific, medical, and social services, preferential treatment is given to the land-usage fee charged. If such services are non-profit, exemption may be granted on the land-usage fee.

The cost of raw materials, machinery, and equipment, or other products manufactured in China and used by enterprises in the SEZs can be charged to them based on preferential treatment in relation to the export price.

Special travel permits can be issued to foreign visitors and overseas Chinese if they invest in the SEZs or if they purchase a residence in the SEZs. Transportation vehicles can be given exit permits if they travel between the SEZ and Hong Kong or Macao.

In response to a request from the Shantou SEZ, the U.S. China Shantou Technology Trade Investment Resource, Ltd. (USCS) was established in an attempt to expand Shantou's business. The Shantou SEZ has asked for assistance in identifying and aiding American and Canadian businesses which might be interested in and have the potential to invest in, joint venture with, or transfer high technology to the Shantou SEZ. USCS does not provide legal services, but rather facilitates trade and investment in China by helping the businessperson with the practical aspects of dealing with the zone. USCS assists in getting foreign businesses into China and helping them finalize a contract with the Chinese. USCS is a joint venture undertaken with financial assistance from the Shantou SEZ to accomplish these tasks. The services USCS offers companies are offered at no expense to those American or Canadian companies which might wish to use its services. USCS has offices in San Francisco; New York City; Washington, D.C.; Charlotte, North Carolina; Los Angeles; St. Petersburg, Florida; and Hong Kong.

As the exclusive representative of the SEZs in the United States and

Canada, USCS serves as a bridge to and from the SEZs. USCS works to educate both Chinese and foreign businesses and provides basic background information on the SEZs to foreign businesses.

USCS provides translation and telex services to facilitate direct communication. It coordinates and advises businesses regarding contract negotiations with the Chinese. To expedite planning and programming visitations to and person-to-person discussions in the SEZ, USCS has a special visa which allows it to bring in ten people on one visa. Thus, USCS can get the businessperson into China within two or three days after the decision is made to visit the zone.

Relatively speaking, the United States has done poorly in comparison to European nations in dealing with the Chinese. It has probably done less trading over the last several years than all other major foreign countries with a trading history with China. It is helpful to think about a Chinese contract as a structure for how a relationship and business deal ought to work. The importance of the contract is not the words on the paper; it is the spirit in which that contract is developed and the relationship between the parties. It is important to establish a trusting relationship when dealing with the Chinese.

In developing this trust, the most important element for a business attempting to establish business ties with China is to send someone to China who has the authority to make the deal. The first thing the Chinese will ask the representative is whether he or she can negotiate for the company and has the authority to sign the contract. When a company sends a representative to China who does not have authority to make a decision, the negotiation often ends in frustration.

A foreign investor should request information and discuss preliminaries before going to China for the actual contract negotiations. All basic questions can be answered before arrival to ensure that the time in China actually will be spent negotiating.

There are five basic forms of direct overseas investment in the SEZs: joint venture, coproduction (joint management), compensation trade, processing, and one hundred percent direct foreign investment. In joint ventures, the Chinese Government and foreign corporations share an investment. Usually the Chinese have fifty-one percent and the foreign party forty-nine percent. The Chinese assume most of the responsibility for planning and managing the enterprise. Distribution of profits is made in accordance with the investment share.

Coproduction is more flexible because all business between the two parties can be negotiated. Under this type of agreement, the sharing of investment is determined by discussion. Foreign corporations usually provide the major portion, if not all, of the capital investment and equipment. The Chinese provide labor, land, raw materials, energy, and sometimes the physical facilities.

In compensation trade, foreign businesses are expected to provide free equipment to the Chinese partner in return for later payment in the form of products. The foreign partner maintains control of marketing until the end of the contract period.

In processing, the foreign business provides materials, parts, tooling, and usually equipment, although in some instances the Chinese supplement equipment. The foreign partner gives technical advice while assuming responsibility for the sale of products in the international market. The Chinese receive a fee for processing and the foreign investors get the profits.

Finally, with the one hundred percent direct foreign investment, overseas corporations control not only the entire enterprise but also the marketing of goods; the Chinese provide labor. This form of investment is, however, rather rare.

The Chinese never envisioned some of the political problems they have had in promoting the open door policy. It is a relationship in flux, and the Chinese are working to improve it.

The best types of investments for smaller companies are low-level, labor-intensive technologies. Those companies that enter China now, although they may not make a profit in the short term, are most likely the companies that will be more successful in the long term. The sooner a company arrives and learns how to do business in China by developing and nurturing a long-term relationship with the Chinese, the sooner its investment in that friendship will result in success.