CHALLENGES AND OPPORTUNITIES FOR AUSTRALIAN AUTOMOTIVE AND PROCESSED FOOD INDUSTRIES IN CHINA

By

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PREFACE

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ABBREVIATIONS

AAI	Australia Automotive Intelligence
AIP	automotive industry policy (China)
APEC	Asia Pacific Economic Cooperation
ASEAN	Association of Southeast Asian Nations
BIE	Bureau of Industry Economics
CKD	completed knocked down
EAAU	East Asia Analytic Unit
EIU	Economic Intelligence Unit
EU	European Union
FAW	First Automotive Works
FDI	foreign direct investment
FFE	foreign funded enterprise
GAMC	Guangzhou Automotive Manufacturing Corporation
GDP	gross domestic product
GM	General Motors
IC	Industry Commission
MNE	multinational enterprise
NAFTA	North American Free Trade Agreement
NIE	newly industrialized economies

R&D	research and development
RMB	Ren Ming Bi (Chinese yuan)
SAIC	Shanghai Automotive Industry Corporation
SCA	Suspension Component Australia
SEZ	special economic zone
SOE	state-owned enterprise
TAIC	Tianjin Automotive Industry Corporation
UN	United Nation
VECCI	Victorian Employers' Chamber of Commerce and Industry
VW	Volkswagen
WTO	World Trade Organization

Chapter One

Introduction

1.1 General Background

China's economy has undergone radical structural changes since the economic reform began in 1978. These changes have provided new economic frameworks and resulted in a substantial development of the economy in the last two decades. In a 1997 report *China 2020,* the World Bank projected that "by 2020 per capita income in China would be approaching those of Portugal today … would still be less than half of those in the United States today" (The World Bank, 1997: 21). Further, the report predicted that China's export at 2020 could be nearly 10% of the world total, ahead of Japan (The World Bank, 1997:92). Based on such a projection, Chinese economists have made calculations that China would surpass the U.S. in aggregate GDP from the year 2025 to 2050 (Hu, 1999).

China's fast economic development has upgraded economic relationship between Australia and China and has provided trade opportunities for Australian manufacturing industries. Since 1996 China has been Australia's fifth largest trading partner. According to the East Asia Analytical Unite, the bilateral merchandise trade has been increased by more than 15% annually since 1978, an increase which is considerably faster than the growth of Australia's trade with the rest of the world. China will become increasingly important for Australia's

economic and strategic future owing to its huge economic potential and rising incomes (EAAU, 1997: 153-154).

But the statistics of the trade between Australia and China on manufactured products suggest that the export of Australian manufactured products to China have been lagging behind the average rate of trade development between the two countries. During the last four years, the average growth rate of the export of Australian machinery and transport equipment to China was about 9%, a rate which is significantly lower than the import of machinery and transport equipment from China averaged 22.7% in the same period (see Table-1). In addition, while the machinery and transport equipment took more than 20% of the total Chinese goods exported to Australia, it only took 3-4% of the total of the Australian export to China. The majority of Australian goods exported to China were raw material and low value added commodities such as ore, coal, wool, metal, fishery, cereal, and gas (ABS 1996 - 2000).

Table 1: Machinery and transport equipment trade between Australia and China
(In A$ Million)

Machinery and transport equipment	12months ended Dec Qtr 1996	12months ended Dec Qtr1997	12months ended Dec Qtr 1998	12months ended Dec Qtr 1999
Australia's Export to China	143	157	149	183
Australia's import from China	859	1036	1320	1587

Source: Australia Bureau of Statistics, (1996 - 2000).

Such a situation is not new to Australia in the post war era. Australia has long been playing a role of supplying raw materials and commodities to countries, such as Japan and Korea,

which have experienced rapid economic development. However, due to the fluctuation and decline of the price on raw material and commodity in the world market, the excessive reliance of the Australian economy on the export of these products has caused various problems, such as the current account deficit and build-up of foreign debts.

Since the 1980s, the Australian government, industries and academic institutions have endeavored to identify factors that have prevented Australian manufacturing industries from international competitive. According to some influential reports, the weak demand conditions in Australia and remoteness of the Australian economy from major international economic centers make Australia not favorable for developing some types of manufacturing industries, which require large economies of scale and support from a range of related industries (AMC, 1990). As pointed by Bell (1993), for a long period the industry policies to combat such a situation by the Australian government in the post war era were to apply high tariffs to protect domestic manufacturing industries and lure foreign investments. However, this government policy is widely considered to be indiscriminate and inefficient (Chapman, 1991). It made Australian manufacturing industries to be domestic orientated and less competitive in the international market. Cole (1991), former chairman of the Industry Commission comments that the government promotion have led to the establishment of many types of manufacturing industries which might not be suitable to be developed in Australia, such as the Australian automotive industry.

Since the 1980s, the Australian governments have designed and implemented various microeconomic reforms aimed at improving the competitiveness of Australian industries.

The focal point of these microeconomic reforms has been to reduce tariff protection and enhance competition within Australia. This position is based on the belief that market competition is the best mechanism for an effective allocation of resources and thus to improve the competitiveness of Australian industries. However, economists and politicians who believe that the playing ground for international trade is not level have continuously challenged this position as narrow-minded (Chapman, 1991). In recent years, with the strong development of foreign direct investment (FDI) worldwide and the expansion of international trade carried out through networks dominated by multinational enterprises (UN, 1977), awareness has risen in Australia for taking notice of the policies deployed by governments in other countries in attracting FDI. It is argued that the incentives provided by these countries could divert foreign investments away from Australia and result in further imbalance between Australia and the newly industrialized economies (NIEs) in Asia Pacific region in terms of developing high value adding manufacturing industries (Mortimer *ed*, 1997).

Such concern involved China as well. Since 1978, opening the country to foreign investments has been the most essential and important policy deployed by the Chinese government for reforming the Chinese economy. The Chinese government had built four Specialized Economic Zones (SEZs) in the early 1980s to attract foreign investment, introduce market economic elements and seek export opportunities. With the success of these SEZs, the opening area soon escalated to 14 coastal cities including some biggest industrial cities such as Shanghai, Tianjing and Beijing. The opening of the Chinese economy has further stimulated the inward FDI to China, according to World Bank (1998)

China has become one of the most important destinations for FDI globally. The strong FDI made into China has significantly promoted the integration of the Chinese economy with the world economy. In 1980, the FFEs only accounted for 0.05% of the Chinese export; in 1995, the share had increased to 31.5% (Huang, 1998). It is found in this study that some of major projects invested by MNEs in the Chinese automotive industry have strong strategic implications not only in the Chinese market but also in Asia Pacific region. It has certainly affected the mutual economic relations between China and Australia.

Hence, this research aims to investigate the changes in economic relations between Australia and China from the perspective of how the FDI and MNE activities in China have produced opportunities and challenges to the Australian manufacturing industries. Basically, this research confines its aims to following aspects:

1. Introducing basic strategies employed by the Chinese government for economic reforms. Analyzing how these strategies have been implemented and what are the consequences in terms of the scale and quality of FDI in China and the development of the Chinese automotive and food processing industries. Examining how such developments have generated opportunities and challenges to Australian automotive and food processing industries.

2. By collecting and analyzing first hand data and secondary information about the performance of the Australian automotive and food processing companies in China, this research attempts to identify and assess the factors that have contributed to the

success or failure of Australian companies in China. Based on the findings, suggestions to the Australian government and industries are made on the adjustments needed to expand the market share of the two Australian industries in China, and on the necessary preparations needed to meet the challenges and opportunities generated from the development of globalization.

3. Theoretically this research aims to deliver new empirical evidences for enriching concepts about how FDI and MNE activities have affected the economic development between two FDI recipient nations of different development stages, namely, Australia and China.

1.2 Structure

This thesis is divided into seven chapters. Chapter one introduces the general background, aims, and research questions of the study. Chapter two covers the literature review which discusses the theories and concepts about imperfect competition, FDI, MNE activities, and changing of national competitiveness. Basically, the theories referred in this study are the comments on FDI initiated by Hymer; 'product life cycle hypothesis' developed by Vernon; "Japanese style FDI" raised by Kojima; "investment path theory" developed by Dunning, and the theory about changing of competitive advantages between nations developed by Porter.

Chapter three introduces the basic situation of the Chinese economy and basic approaches taken by the Chinese leadership for the reform, for instance, the opening policy, State Owned Enterprises (SOEs) reform and rural reform. Analysis is provided to cover how these strategies have been implemented and the consequent changes to the government administration, macroeconomic management, investment environment, and business operation in China.

Chapter four focuses on the discussion of the factors influencing the development of the Chinese automotive industry and the food processing industry. These factors include the function of the Chinese government, the rising importance of the Chinese market, and the involvement of MNEs in China.

Chapter five is about the development of the research questions for this study and the methodology required for fulfilling the investigation. The research questions are developed from theoretical reviews, analysis to the collected secondary information and contacts to the industries. The research questions are focused at how and why FDI are being made into China, and what are the consequent opportunities and challenges to the Australian automotive and food processing industries. In the methodology part, the rational for selecting the automotive and food processing industries for this research is provided. Also the procedures of questionnaire development and the approaches of conducting surveys are introduced.

Chapter six includes the survey reports to the Australian automotive and food processing industries in terms of their performance in direct investment and export to China. These reports are presented in a systematical way though which to introduce and analyze the result of questionnaire surveys and face to face interviews. It has found that the Australian automotive industry had a very limited presence in China while the market coverage of the Australian food processing industry had been mixed. The main contributing factors to the success of Australian companies in the Chinese market are technological advantage, commitment of the management in developing business in China, and the use of professionals with Chinese ethnic background. The main factors preventing Australian companies from entering the Chinese market are the high tariffs, restrictions from parent company, and unfamiliarity with the Chinese market.

Chapter seven summaries the findings of this research and the theoretical contribution of this study. Furthermore, policy suggestions are provided for the Australian government and enterprises to penetrate into the Chinese market and react to the development of globalization. Basically, this study confirms that under the influence of globalization, the government policies of other countries and global strategies of large MNEs are increasingly affecting the performance of Australian manufacturing industries. The rising importance to the developing counties due to their government policy, market potential and cheap labor and production cost may induce significant inflow of capital and technology into those countries. This development overshadows the technological advantage held by Australian companies over developing countries. It is even possible

that the affiliates of large MNEs in those developing countries replacing foreign subsidiaries based in Australia for making intermediate products.

Therefore, there are urgent needs for an improved coordination between the Australian government and industries, and within the industries to upgrade the competitiveness of Australian manufacturing industries. Such coordination should be considered as an important move to improve the value chain of Australian manufacturing industries and to build up industrial clusters in Australia.

Chapter Two

Theoretical Framework

It has been long argued and advocated from Adam Smith and David Ricardo to contemporary neoclassic economists such as Heckscher and Ohlin, that the nations of the world can benefit from a free trade regime based on specialization of production in accordance with their comparative advantages. This argument is based on the rationale that economic resources are unevenly distributed among nations of the world in terms of endowment of natural resources, location, population and market sizes. Furthermore the efficiency of utilizing resources between nations is also significantly different due to the variation of economic management systems and accumulation of technology. Numerous examples have been raised in articles and textbooks to verify that total output will be greatest when each good is produced by a nation which has lower opportunity cost. Specialized production in accordance with the principle of comparative advantage among nations allows the world to get more output from given amount of resources (Jackson & McConnell, 1988: 564). Free trade internationally on such conditions will generate maximum welfare worldwide.

However, "no matter how compelling the logic of the case for the free trade, it is the protectionism that often prevail in the practice" (Jackson & McConnell, 1988: 565). Nations are taking broad considerations in determining their trade and industry policies. It is very common for government of different countries to use tariff and non-tariff barriers to protect

the domestic industries that have important implication to national security, employment, and political stabilization from the competition imposed by foreign companies.

Since the 1960s, with the rapid development of technology and growing trend towards globalization, FDI and MNE activities are increasingly playing an important role in world economic development. Even though traditional international trade conducted on an arm's length basis remains a vital part, the international production and sales by multinational corporations are increasingly becoming the dominant force. The value of FDI in 1970 was US$40 billion, this figure increased to US$170 billion in 1980, US$232 billion in 1989 and US$ 349 billion in 1996 (UN, 1998). Currently, the value of intra-firm trade cross border among MNEs' worldwide affiliates has accounted for one third of the total world merchandise trade; and MNEs carried out 70% of the world FDI (UN, 1998).

These phenomena raise important issues such as to what degree are the conventional explanations valid in explaining why nations trade and who gains or loses from international trade. New frameworks are needed to better describe the factors influencing international trade. Since the 1960s, numerous theories have been developed to explain the impact on the world economy due to the development of FDI worldwide, MNE activities, and economic globalization.

2.1 FDI in an environment of imperfect market competition

To the advocates of the strategic trade theory such as Krugman (1986: 7), international trade is to be carried out in an imperfect market condition. Such an imperfect condition is mainly formed due to the difference between nations in accumulation of capabilities and resources for innovation. As the result of rapid technological development in the post war era, factors such as economies of scale, high quality and quantity of human resource, well established economic management system, availability of capital, and diffusion of technology are increasingly playing important role in economic competition between different nations. Government trade and industry policies can provide conditions influencing the behavior and performance of domestic firms in international competition. Tariff protection, government subsidies targeting strategic industries, and government supported coordination between domestic industries can create so called economic "rent" to domestic firms facilitating their innovation, cost reduction and sharing of technology and know how each other. For example, without the support of the governments of Western European nations, it would have been impossible for Airbus to be able to compete against American giants such as Boeing, as the development of aviation industry needs large economies of scale, huge investment and a protected market.

Krugman and other economists who develop strategic trade theories argue that the example of Airbus shows that government protective policy and subsidies can help domestic firms establish themselves in strategic industries or prevent the potential entrants of other nationalities from entering the industry or market. Carefully targeted

government subsidies generate benefits not only to the targeted industries but also to the domestic economy as a whole through knowledge diffusion and stimulating domestic innovation. This will lead to the establishment of monopoly power of domestic firms in a segment of market internationally or enable them to earn a higher rate of profit at the cost of contraction of rival foreign companies. In particular, protective policies and government roles are considered important and necessary for developing countries to build up infant domestic industries in the face of strong international competition imposed by powerful MNEs.

In the recognition of the fact that international trade and investment is carried out in an imperfect competition environment, Hymer, Vernon, Dunning and others have been endeavoring to define the motivation, function, effects and implication of FDI to world economic development. Hymer (1974) argues that due to significant barriers existing in the conventional international trade, FDI becomes an efficient way to penetrate into foreign markets as it brings in capital, technology and employment opportunities to host nations. However, Hymer considers that the basic character of FDI is that it ensures investing company possessing the property right over the facilities invested overseas. Based on such a property right investing companies can establish themselves in a foreign market, and further access to local advantages such as cheap labor, growing market and other local resources. In many cases, investing companies could take advantage of protective policies adopted by host countries to deter its competitors from entering the market. Therefore, the success of a firm to establish market share in a foreign country earlier than its competitors could mean win the market shares in that country. In order to maximize market share globally, MNEs

are very active in vertical and horizontal expansion by shifting part of the value chain to foreign country where new market demand is emerging. In this way, MNEs set up networks worldwide to excise their control over foreign markets at the regional and global base (Hymer, 1974:3).

FDI is a very complicated phenomenon, its implications to the international investment and trade are profound. Kojima (1978) considers that FDI can be divided into two categories, which are anti-international trade and pro-international trade. Kojima comments that the American style of FDI is anti-international trade. In order to occupy foreign market and deter competitors, American firms tend to build plants abroad with their best technology and start from the industries that have the strongest competitive advantage at home. According to Kojima, the technology of these investments is often so advanced that local firms in host countries are enable to play a active role in the development. The intention of these investments is simply to gain the control over foreign markets and to further exploit their monopolistic advantages.

The style advocated by Kojima is the Japanese FDI, to which he considers to be free trade orientated and can facilitate trade between home and host nations through division of labor based on the difference in comparative advantages. Kojima (1978: 15) argues that FDI should be used to facilitate free international trade. "Direct foreign investment that is released from a comparatively disadvantageous industry in the investing country and finds its way into the industry with overt or potential comparative advantage in the host country will harmoniously promote an upgrading of industrial structure on both sides and thus speed

up the expansion of trade between the two countries". According to the Japanese style FDI, Japanese firms undertake FDI in an industry becoming comparatively disadvantageous in Japan which at the same time has the potential of becoming comparatively advantageous in a foreign country. In this way, Japan can allocate resources to enlarge the industry that it has comparative advantage and increase the trade with countries that receive the industries transferred from Japan. As a result, the Japanese style FDI can promote diversification and upgrading of industrial structures both to home and host countries, and promote trade between these nations based on division of labor in accordance with labor cost and other comparative advantages between Japan and the countries.

Although, the Japanese FDI may promote trade among Japanese MNEs and subsidiaries and subcontractors in host nations, some economists still see the purpose of the Japanese FDI is to pursue the dominance or control in the host countries. Machado (1991) considers that one of the reasons that Japanese MNEs favor transferring some component industries and assembling industries abroad is that it permits the control of Japanese companies over the intra-firm trade and promoting a regional integration in which Japanese MNEs take control. For example, by transferring technology and establishing subsidiaries or affiliates for making different automotive components in different South East Asia nations, Japanese automotive multinationals have dominated 90% of the market share in South East Asia countries (EIU, 1994).

Product life cycle hypothesis circulated by Vernon has special contribution in analyzing the nature of FDI. Vernon (1996) argues that the development of FDI is the last part of a

process through which products are being innovated, exported in home country and than produced overseas. The product life cycle hypothesis begins with the assumption that home market, typically the U.S. market in 1950s-70s provided the demand conditions and economies of scale to stimulate the innovation of new products. Once the innovator has set up its first production facility in the home market, any demand that may develop in a foreign market would ordinarily be served from the existing production facility or by licensing agreement. When foreign markets develop an increased demand for products that had previously been generated in America, the marginal costs of producing for export in the home country plus international transport cost and tariffs are being compared with the full cost of producing the required amount in a foreign subsidiary. Due to the difference in labor costs between America and other countries, and the fear that the innovator is threatened by losing monopoly positions due to the entry of competitors into the potential markets, US firms are eventually moving abroad to establish producing subsidiaries.

Recently Vernon (1996: 255) acknowledged that the product life cycle hypothesis has a diminished application to the current international trade and FDI due mainly to two facts: first, the convergence of living standard and demand conditions in advanced industrialized nations, and second, the geographical reach globally of MNEs that are involved in new product development.

But Vernon (1996: 265) considers that some principles of the theory are still validated. "The assumptions of the product cycle hypothesis may still apply to smaller firms that have not yet acquired a capacity for global scanning through a network of foreign manufacturing

subsidiaries". That is, firms in these countries are still following the pattern of product life cycle in conducting foreign direct investment, which goes through stages of innovation, maturing and export, and overseas production. Further, Vernon argues that gaps still separate countries of different development levels. Firms in developing nations, including foreign subsidiaries are not to acquire all of the products that produced in richer and larger markets. According to Vernon (1996: 265) "Most of the developing countries are still in process of absorbing the innovations of other countries introduced earlier, according to patterns that remain reasonably consistent with product cycle expectations".

2.2 Relation between FDI and national competitiveness

The theories reviewed in the previous section have shown the extreme complex nature of FDI. The theories have covered a wide range of issues ranging form the control over foreign market through FDI, comparative and competitive advantages of a nation and their relationship with international investment, and to the technology transfer, international division of labor and changing of pattern in international trade associated with FDI. Due to these developments, complicated questions are being raised such as on what condition do nations compete with each other for attracting FDI? What can be expected from the outward and inward FDI to the economic development of a country? What are the roles that government can play for attracting FDI?

Dunning has been trying to answer these questions. He reasons that the outward and inward direct investment position of a country is systematically related to its economic

development relative to the rest of the world (Dunning & Narula, 1996:1). Dunning argues that the ownership specific advantages of firms and locational advantages of the nation where the firms are located are the basic factors that determine the nature of FDI. Dunning defined the ownership specific advantage as the possession by firms of particular assets including both tangible assets such as natural endowments, human resources and capital and intangible assets such as patent, know how and managerial expertise, relative to those of firms of other nations. Particularly, the intangible assets are recognized to be unique to firms of a particular nationality of ownership. Dunning (1996) refers the location-specific advantage as the public assets available to all firms specific to a particular location. These assets are natural endowments, cultural, legal and political frameworks, market structure and government legislation and policies. These resources are local–bound to a specific country relative to those of other nations.

Further, Dunning and Narula (1996: 1-12) explain that nations tend to go through five stages in terms of change of propensity in outward and inward FDI due to the change of ownership advantages and location specific advantage. According to this "investment development path theory", countries in stage one are unlikely to receive inbound FDI due to lack of local-bound specific advantages and ownership specific advantages.

In stage two, as nations improve local-bound advantages, inward FDI starts to rise. Governments of host nations in this stage tend to impose policies to protect the growth of domestic manufacturing industries that can produce products substituting with the imports.

The inward FDI in this stage are normally focused at seeking natural resources or cheap labor of the host country.

In stage three, as countries in this stage have upgraded their local-bound advantages and firms in these nations have improved their ownership advantages, the nature of inward and outward FDI related to these nations are changing. The growth rate of inward FDI to the countries in this stage is gradually slowing down while the outward FDI increases. The inward FDI is moving away from import substitution to taking advantages of improved human resources and intangible assets offered by the firms in host nations. Countries in this stage will increase their outward FDI to stage one and stage two countries so as to seek export markets.

Stage four is reached when a country's outward direct investment exceeds or equals the inward investment, and the rate of growth of outward FDI is rising faster than that of the inward FDI. Inward FDI is increasingly for seeking efficiency and strategic assets carried out by firms from other stage four countries. Outward direct investment will continue to grow as firms moving operations, which are losing their competitiveness to offshore locations due to increase of labor and production cost in home country. The intra-industry trade will become more important than exports, as firms are shifting operations abroad to expand their market share and competing in an oligopoly environment.

Both inward and outward FDI are likely to grow for countries in stage five as the structure of location-bound assets between these countries are converging due to close of gaps

between advanced industrialized nations in living standard and demand conditions. In order to access ownership and location-bound advantages in other advanced nations, mergers and acquisitions between powerful MNEs have become common. The strategic FDI made by these MNEs are carried out in a large extent between the nations of same level, as the motivation of these FDI is changing from primarily exploiting existing ownership advantages to the acquisition of new ownership advantages. This reinforces the tendency of intentional trade to be carried out through a network created by multinationals instead of markets. Thus international trade gradually shift away from arm's length trade between nations producing very different goods and services to trade within hierarchies or cooperative ventures between countries producing very similar products (Dunning 1997).

2.3 Summary

The theories reviewed so far have come up with different explanations and mentioned different aspects of FDI. Hymer's approach is to verify that the centerpiece of FDI is to seek the control over foreign market by investing companies, as FDI facilitate investing companies controlling the property rights on facilities invested in host countries. The activities of FDI conducted by MNEs have been growing very strong since the 1960s through which they are building vertical and horizontal integrated networks to expand their market share worldwide.

Kojima is critical to this American style of FDI and advocates the Japanese style which basically is to set up an international division of labor through FDI. Such a division of labor

is based on the difference between countries in comparative and competitive advantages. Basically, MNEs in advanced country strategically place central level of administration, finance and R&D in home country while distribute labor intensive industries to countries of lower development stages. As a result, complementary economic relations could be formed between home and host countries involved with the FDI. However some economists still believe the heart of Japanese style of FDI is to control foreign markets. Nevertheless, FDI conducted on such a basis still associates with substantial technology and capital transfer, and trade opportunities between the home and host countries.

Vernon sees FDI as a part of the process through which technology and production are transferred from firms in advanced countries to developing countries as a result of change of the cost, market demand conditions and technology level between these countries. One important event emphasized by Vernon is that under the process of globalization, the 'global scanning power' of MNEs is increasingly having a dominant influence upon firms from countries of lower development stages.

Dunning suggested that the content of FDI is systemically related to the level of locational specific advantage of the country and ownership advantages of the firms involved with the FDI. Given the process of globalization, the relations between countries are increasingly integrated and interdependent. As pointed by Porter (1990: 545) "Widespread global competition has made the portion of leading economies subject to international competition more and more decisive to national economic prosperity."

As mentioned in the introduction chapter, this research is aimed to investigate the changing of economic relationship between Australia and China from a perspective of how FDI and MNEs activities in China have produced opportunities and challenges to the Australian manufacturing industries. In order to fulfil this aim, it is necessary to study how the Chinese government policies in combination with the factor conditions in China have functioned to attract FDI into China. Hence, Chapter three introduces the basic situation of the Chinese economy and basic approaches taken by the Chinese leadership for the reform. Chapter four discusses the factors, in particular the FDI, in influencing the development of the Chinese automotive and food processing industries.

Chapter Three

Opening Policy - Basic Strategy of China's Reform

Before 1978, the comprehensive state ownership of production assets in China laid a foundation of the social structure of the country. Almost all the manufacturing, retailing, wholesale, transportation and communication infrastructures in the urban sector belonged to the State. Land, major machines and large cattle in rural sector belonged to People's Commune, a type of organization collectively owned but actually created by the authority for controlling all kinds of activities in the rural area.

One of the most outstanding characteristics of this comprehensive state ownership was that it combined the administrative and political functions of the government and economic activities of the enterprises together. A huge and complicated hierarchical system including central, provincial and local governments were created for running the economy and controlling the society. Under such a system, transactions between SOEs were conducted through State distribution and retailing system with the price set by the government. State took profit from factories or provided subsidies if enterprises ran at loss. SOEs were not separate legal entities but only production units. They had no right to hire people, set price or decide what to produce. Employment of workers was assigned by government agencies and wages were standardized. Every one belonged to an organization in which not only did they get paid but also supplied with cheap rental, health care, retirement and even education benefits. People were made to be the dependants of their organization. In this way, the

government turned the factories and People's Communes into basic elements of the entire political and economic control system.

Although this system functioned in the 1950s and the early 1960s when China was recovering from long periods of different wars, it had revealed its problems in long run. This system failed to deliver incentives for workers and their work organizations. The highly centralized economic planning system were incapable of running the economy efficiently when the economies of scale grow large and complexity of making economic decisions rise.

3.1 Reform strategies 1978 to 1994

Deng Xiaoping was the late Chinese paramount leader who had promoted China into reforms started in 1978. Deng believed that the mechanisms of market economy could be adapted and integrated with the existing political system in China. Such integration would make China to be a destination receiving labor intensive industries that had transferred from advanced economies nearby, This would facilitate China to conduct an export-led economic development as other NIEs had achieved, such as Korea and Taiwan. To the Chinese political leaders and some scholars, the establishment of market economy in East Asia is different from that of the West. They argue that the development of market economy in East Asia is primarily the consequence of independence of the nation. Government in these nations has played a major role in the development of modern industries and legal and other social frameworks necessary for the operation of a market economy (Lou, 1995).

However, a major difference between China and the East Asian NIEs is that China has a huge state owned economy. With most of the urban population dependent upon the state economic sector, any radical reform policies of 'big bang" style such as instant slashing of subsidies to loss-making SOEs, freeing prices in the market, and privatizing state assets, is likely to create problems such as massive unemployment, enormous loss of state assets, high inflation and social instability.

The harsh conditions determined that the reform should only be carried out in a soft approach. It should not only create a system that would benefit the nation in the future but also an instant improvement of the standard of living of the people. The basic approach taken by the Chinese leadership in dealing with such a difficult task is not to take radical changes in a short time, but to carry out reforms in a controlled pace, the so called "gradualist reform". During the period between 1978 to 1994, while the basic political, legal and financial frameworks of the country were kept unchanged to maintain social stability, reforms were carried out mainly in three fronts: opening the country to foreign investment, reforming the rural sector, and the reform of state owned enterprise.

3.1.1 Open-door policy

The centerpiece of the Open-door Policy during the 1980s and the early 1990s was to set up Special Economic Zone (SEZ) and open selected cities for attracting FDI. Favorable conditions, such as tax and tariff reduction, free labor market and high autonomy in conducting international trade were provided to foreign funded enterprises (FFEs) operating

in the SEZs and Opening Cities. Because of the incentives and the potential of the Chinese economy, foreign direct investment (FDI) made into these SEZs grew fast. The combination of the advanced technology, managerial skill, capital, and connections to the world market brought in by foreign investors with cheap Chinese labor and subsidies provided by the Chinese government made economy of SEZs very competitive both in international and domestic markets. (Wu, 1999: 346)

At the early stage, the FDI was highly concentrated in labor intensive industries such as clothing, footwear and toy industries. China soon became a major exporter in these industries. The strong export stimulates the import of foreign machinery and material. In 1994, the total value of the goods imported and exported accounted for 45.4% of the Chinese GDP (Wu, 1999: 340). Millions of workers are working for the overseas market. China has become the highest recipient of FDI among developing nations.

3.1.2 Rural reform

The main policy of China's rural reform in the 1980s was the termination of People's Commune and implementation of the "family production responsibility system", which allowed farmers to lease land and other major production assets for a period of thirty years. Except for an obligation to supply a quota of products to the state at the price set by the government, farmers can use the land and other production assets at their will.

This system has provided incentives to farmers to run family production and develop private businesses. It had particular success in the 1980s with output of agricultural products in China expanding to new levels.

The strong economic development and the demolishing of the People' Commune System have made it possible for millions of farmers to move into processing and manufacturing industries that become available in areas abject to SEZs and Opening cities. Since the enterprises are located in towns in the rural area, they are called "township enterprises", which are mainly collective owned or private businesses. Thanks to the development of township enterprises, between 1978 to1996, the labor force in rural areas involved with agricultural production reduced from 92.8% to 71.8%. Within the GDP value produced by the Chinese agricultural sector, the rural manufacturing industries increased its share from 15.8% to 58.4% in the same period (Gou, 1998). Township industry has erupted as a major force in national economic development. Its output value increased 11.9 times during the 1980s; it shared 44% of the total added value of the Chinese manufacturing industries in 1995 and a quarter of China's GDP in the same year (China Ministry of Agriculture, 1997).

3.1.3 Reform of state owned enterprise

The main policy for reforming SOE in this period was to link the profit retention and staff income to SOE's performance. By signing a contract between government and SOE management, an enterprise can retain the profit after a contracted amount of profit has been

taxed. In order to implement the contract, the standard wage system and government controlled employment system were abolished. The government loosened its control on the setting of prices of goods, and SOE managers were given the power to run enterprise. They can make decisions on issues such as wage, bonus, price, production, sales, and personnel management.

Despite these efforts, SOE reform has not achieved a favorable outcome. In fact, the performance of the sector has deteriorated in the last twenty years. The output value of SOEs dropped from 78.5% in 1979 to 35% in 1995. Currently, more than 75% of SOEs are making losses (State Council Development Research Center, 1997).

It is believed that the most significant reason for the inefficiency of SOE is the ambiguous definition of the property right. Although SOEs are owned by the government or 'whole of the people', there is no personalized owner, or group of owners, with interest in defending the value of the capital invested in SOE, or actively demanding a good return on that investment. This leads to a weak supervision to the SOE management and poor selection of SOE managers. Besides, SOE are still bearing huge social burdens. The World Bank estimates that the social service payments of SOE, in terms of pension, housing and health care, are approximately equal to their losses (The World Bank, 1996a: 17). Furthermore, the redundancy of the workforce in SOE is very high, which is believed to be around 30% of the total workforce, or 20 million workers. Many rotten SOE are running to avoid high unemployment rate and other social and political problems.

3.2 Unbalanced development

Basically, the policies chosen by the Chinese leadership in reforming SOEs, energizing the agricultural sector and establishing SEZs in the period between 1978-1994 was to gradually deregulate the rigid planning economic management system and shift power and resources to different sectors to pursue a high economic growth. Such a high economic growth is considered vital to absorb the shocks generated from the change of social structure and winning political support for the further reform.

With the continuous deregulation and implementation of reform policies, the portion of the Chinese economy that composed of foreign investment and private business is growing much faster than the state owned economic sector. Due to the sluggish of SOE reform, the state owned economic sector has been declining in terms of value of production and profitability. The Chinese economy is increasingly becoming two blocks running side by side. In order to coordinate the operation of these two economic blocks, in the 1980s and early 1990s, the Chinese government endorsed a "dual-track price system" which involved two prices and two standards existing side by side for the same product or business activities. The application of one of the two prices was in accordance with the system in which the transactions were conducted. For example, the interest rate of loans issued by state banks to SOEs could be as low as 3%, but the interest rate on same amount of loan at the market could be as high as 15% (Shi, 1994). Government departments run this dual price system. Government officials played key role in establishing boundaries between the two sectors and in distributing and balancing resources accordingly.

With the rapid development of the economies in SEZs and Opening Cities, the importance of the role played by the provincial and local governments is growing. In order to recognize the function of local governments in managing regional economy, a financial management system was established gradually throughout the 1980s. The system allowed provincial government to retain any surplus of revenue after submitting a fixed tax to the central government. Compared with the old taxation system which involved almost a total submission to the central government, this policy provided great incentives for local government to expand the local economy. The more revenue local government had, the more it could expend and vice versa. As a result, a localized and multiple centered economic structure have gradually replaced the centralized economic planning system (Wu, 1999: 308).

According to Wu Jinglian, one of the most influential economists in China, the continuous shifting of power from the central government to various sectors and the establishment of a multi-centered economic pattern has contributed to the erosion of the unity of the planned economy. Economic relations between different locations and enterprises have changed from government allocation to sales and purchases. The shift of economic power and interests has functioned to stimulate SOEs and local governments to imitate private business to compete in a market economic environment. In this way, market economic elements have developed gradually between localities and factories. However this multiple centered economy is not a real or complete market economy. It is a combination of different economies cultivated, coordinated, and managed by central and local administrations while influenced by market forces (Wu, 1999).

China's reforms between 1978 and 1994 had achieved remarkable success in terms of promoting a high economic growth and the introduction of market economic elements into the country. In this period, China remained as the fastest growing economy in the world. The industry output value covered by the planning economic system decreased from 70% in 1979 to only 5% in 1995. According to EAAU (1997: 75), in 1995, over 90% of retail prices and over 80% of agricultural and raw materials prices now were set by the market. Non-state economic sectors surpassed state owned economic sector in the share of the GDP value and contributed half of the national export value.

However, the strong economic growth does not indicate that China's reform has achieved a decisive success. The reform strategy in the period was intentionally bypassing sensitive reforms such as the political reform, redefinition of the property right on state assets, and the establishment of independent national financial system and legal system. Basically, by relying on the existing authority, the Chinese government has acted as an initiator promoting reforms as well as a controller balancing the society. The hardest challenge to this approach is that as the reform goes deep, it requires the government to change its role accordingly. But, for fear that the political reform and other fundamental changes would undermine the authority of the existing government and threaten the stability of the country, the Chinese leadership has avoided to tackle these fundamental issues directly. Under such a circumstance, the control of the government is inevitably weak, changeable, controversial and sometimes contradicting. The continuous shift of power from the central government to various social sectors has weakened the power base of the central government itself. For example, the proportion of the central government tax revenue in national income had

dropped from 31.2% in 1987 to 14.7% in 1992 (Hu & Wang, 1995). The power of government officials and SOE managers over economic resources is expanding significantly. As China lacks a monitoring system to counterbalance the increasing power of government officials and SOE managers, corruption has become widespread and the society is increasingly becoming unbalanced and separated.

Due to the lack of efficient macro control, the quality of the economic growth in China is low. It is common for local governments, SOEs and township enterprises to make excessive investments into profitable industries that lead to a severe oversupply and excessive competition. In order to protect the regional economy, provincial governments are building barriers between provinces. This has impeded the Chinese manufacturing industries from reaching large economies of scale. In addition, many regional projects are unable to develop undifferentiated products due to lack of technology and management skill. Many of these projects never reached break-even returns. A great deal of these poor managed investments is carried out by SOEs. This has put on heavy pressure on state banks. International media reported that the estimated bad debts of state commercial banks are about 25% of their total loans (*The Chinese Business Review,* November, 1999). The potential of financial turmoil in the country is high.

During the 1980s and early 1990s, the industries that had fast development speed were mainly labor-intensive transferred from nearby NIEs, and the assembling industries invested by MNEs. Geographically, only coastal regions benefited from these industries. Due to the technological, management and investment factors, the Chinese heavy industry, petrol-

chemical industry, electronic industry and machinery industry were unable to support the fast development of labor intensive and assembling industries (Lin, 1995). China's import of machinery, transportation equipment, industrial intermediates, components and raw material has been continuously growing since the opening of the country to foreign investment. Domestic companies troubled with sub-scale, tight working capital and limited R&D capability are unable to compete with MNEs. With the opening of the Chinese market, the domestic market is increasingly taken over by foreign products. This situation has brought attentions to the government, industries and academe. There are comments that if such a trend persists, the domestic industries would be taken over by MNEs, and ultimately, China will lose its capability to sustain the economic growth.

3.3 Adjustment after 1994

In the fact, in the period between 1978 to the early 1990s, it was the success of the opening policy that had supported the fast economic growth in China and cushioned society from the shocks generated from the reforms and changes. This particular success has provided valuable implications to the Chinese leadership. First, the biggest asset to China is its market potential, and it can only be utilized if the country has a stable political condition and a favorable investment environment. Second, by taking advantage of the market potential, cheap labor, and government provided incentives, Chinese industries can attract FDI and via these FDI to enter the international market. Third, in order to maintain an ideal investment environment, it is important for the government to establish market friendly legal and financial frameworks and conduct anti-corruption campaign. Currently, China

urgently needs a market orientated macro economic control system upon which the government could change its way of economic management from direct control to indirect control. In addition, the Chinese industrial structure needs to be rationalized and the effectiveness of the Chinese industries should be upgraded.

In addressing these issues, the Chinese leadership under President Jiang Zemin and Premier Zhu Rongji started a series of major adjustments and further reforms since 1994. In the economic front, The strategic tasks of the adjustment are mainly towards two directions.

3.3.1 Establishment of a modern macro economic control system

The main thrusts under this direction are the taxation reform and banking system reform. The basic policy of taxation reform is to divide tax items and split tax revenue between the central government and the local governments. It is designed that the division of tax revenue can ensure the central government with a secured share while incentives are still provided to localities that increasingly play a major role in the regional development. As the taxation reform is carried out within the hierarchy of the existing government, the authority is able to use its overwhelming political power to fulfil its goal. The tax revenue of central government has been rising significantly every year since 1993. China's tax revenue reached a record of 1.03 trillion yuan (US$ 124 Billion) in 1999, 13.4% more than in 1998 (*China Daily,* January 11, 2000).

The banking reform involved a separation of the national financial institutions into central bank and commercial banks. The People's Bank of China will function as a central bank to provide monetary policy and to control the stabilization of the currency. With the issue of Bank Law in 1995, theoretically, the People's Bank of China should have an independent statue and can carry out monetary policy without political influence from any level of the government. Other state-owned commercial banks are required to hold responsibility for their own profits and losses. Foreign banks are being permitted to carry out more kinds of businesses in more locations in China.

As the state banks are still owned by the government, and are still tools of the central government for achieving its macro objectives, the total independence of state banks will be a long way to go. However, with the implementation of the reform policies, responsibility of banks for their own profit and loss is on the increase. This makes loans from state banks increasingly based on calculations of creditworthiness, which inevitably slows down the flow of capital to loss-making SOEs.

3.3.2. SOE reform and industrial restructuring

Since the late 1993, the Chinese leadership has renewed reform programs to tackle the deterioration of the state economic sector. The basic strategy of the reform policies this time is "grasping the large and enlivening the small", which is to separate a large number of loss-making small-medium SOE from the sector so as to make resources available to the building of large corporations in strategic industries. According to a survey, 500 large scale

SOE only represent 0.22% of the total number of SOEs but account for 36% of the total state assets and produce 78% of the profit in the state owned economic sector (China State Council Development Research Center, 1997). Under the government plan, large number of small to medium SOEs should be converted into limited liability or joint stock entities, or purchased by FFEs operating in China. By separating loss-making SOE from the state economic sector the burden on the government will dramatically lighten. This will make it manageable for the government to concentrate resources into the development of Korean style conglomerates in strategic industries, including heavy machinery, chemical and petroleum, automotive, military industries, transportation, telecommunication, energy, major mining corporations and steel mills.

The government promotion of the strategic industries is also considered an important industry policy aimed at improving the structure and lifting the overall competitiveness of the Chinese manufacturing industry. One of the fundamental aspects of this policy is to seek the incorporation of Chinese large state owned corporations with major MNEs. The main incentive is to further open the domestic market to MNEs that are willing to transfer advanced technology, capital, export arrangement and managerial expertise to China. These MNEs are encouraged to set up joint venture with major Chinese corporations.

3.3.3 Impact of East Asia financial crisis

In 1997, after three years of adjustment China successfully achieved a soft landing cooling down the economy from double figure inflation. But soon after that, China encountered with the impact of East Asia financial turmoil.

China has avoided the type of impacts hit Korea, Indonesia, Thailand, Hong Kong and other East Asia countries. According to the Chinese and international analysis, a number of factors are relevant. First, the structure of China's foreign debt is favorable, most of them are long or medium term loans. Second, the capital account is still controlled by the Chinese government, which provides protection against speculation. Third, the economic adjustment since 1994 has functioned to stabilize the Chinese economy.

However, the impact of the East Asia financial crisis on China can not be underestimated. The trend of rising export and inward FDI has been reversed since 1997. The slowdown of the export and inward FDI in combination with the closure of large number of SOE sends China into deflation. The demand of domestic market is weak and unemployment rate is increasing.

The East Asia financial crisis has given lessons to China including the importance of a healthy, independent financial regulatory regime, and the potential danger of having huge bad loans on state banks. The pressure upon China to reform its state economic sector and restructuring its industrial structure is high. Eventually the time has come for China to end the approach of stimulating economic growth by shifting political power and economic resources to various sectors.

3.3.4 Admission to WTO

In order to carry out SOE reforms, China needs great sum of capital to purchase the shares converted from the assets and debts of SOEs. China needs more export opportunities to

create jobs for absorbing millions of laid-off workers due to the closure of SOEs and millions of farmers looking for job in cities. Under this situation, China is determined to further exploit the benefits of the open-door policy. Admission to WTO is a strategic move in this regard.

By joining WTO, China's trade potential will be much improved. According to Chinese government and the majority of Chinese scholars, in the long run, WTO membership will benefit China. It will enable China to take advantage of its competitiveness in labor intensive industries for expanding the export in this sector. It will stimulate FDI made into China which in return will facilitate the restructuring of the Chinese manufacturing industries. The entry of MNEs will provide China intra-industry trade opportunities through networks organized by MNEs. In this way, Chinese firms could further participate into the international division of labor and expand the export. A report prepared by the Research Center of China's State Planning & Developing Committee claimed that WTO membership could double China's export by 2005, double inward FDI in the next five years, increase an extra percentage point of economic growth for the next decade, and cut the unemployment rate to 5% (*The Economist* November 20, 1999). China's accession to WTO will induce great changes to the economic and politic systems in China. Institutional reforms will be prompted for the recognition of the roles played by private sectors and foreign investors. The Chinese market will be further opened up and the integration of the Chinese economy with world economy will be further developed.

In November 1999, China and the U.S. sealed the negotiation for China's accession to WTO. This deal paved the way for China's final admission to the WTO. According to the deal China's tariffs for wheat and maize will be cut to 14.5% by 2004 from the current 45%. Tariffs for cars will be cut from 80-100% to 25% in five years. Foreign companies can have 49% stakes in the Chinese Tele-communication and Internet companies, rising to 50% in two years. Foreign banks will be allowed to do local currency business with Chinese companies within two years of WTO accession and with Chinese individuals within five years. It is estimated that the business of foreign banks in China could have an annual increase of 40% up to 2010. By the time, foreign banks could have 8% of total loans in China (*Time,* May 22, 2000). MNEs will gain higher autonomy in importing and exporting products through their international networks. Foreign companies will be able to set up wholesale, retail, distribution and after-sale networks in China. New laws and regulations will be set in compliance with WTO rules.

This deal would bring China a great deal of short-term pains as many Chinese manufacturing industries and some sectors of agriculture are not competitive with international standard. The adjustment of these industries will raise unemployment level. It is estimated that millions of Chinese farmers will lose jobs due to the opening of domestic market to American agricultural products. Many Chinese automotive component factories will be closed, or rationalized through merge and sold out. However, these adjustment costs China will have to pay even without the admission to WTO. Without the export opportunities provided by WTO membership, such adjustments might be even more difficult.

3.4 Summary

From the above analysis it can be concluded that the most valuable comparative advantages that China possesses for attracting FDI are its great market potential and cheap but relatively efficient labor force. The Chinese government is fully aware of the significance of these advantages and has designed and implemented policies to take advantages of them. It is expected that the combination of the market potential, cheap labor and government subsidies could make China ideal for accommodating the transfer of the industries that become less competitive due to the rise of labor cost in advanced counties. In this way China could take part into the international division of labor and pursue an export led economic development.

The basic position taken by the Chinese government is that while high tariff and other non-tariff barriers are deployed to protect the domestic market, foreign investors willing to introduce capital, technology, management expertise, and connections to international market are encouraged to enter China. In the early stage of this opening process between the 1980s and early 1990s, business people from Hong Kong, Taiwan and overseas Chinese from other foreign countries carried out much of the FDI, as same cultural background made them easier to adapt to changes in China and seize business opportunities. The projects invested were mainly in labor-intensive industries in the period.

However, the development of labor intensive industries in China can not deliver a sufficient leverage to sustain the economic development. In recent years, China feels the pressure that many of its manufacturing industries are becoming obsolete (Qiou, 1998: 224). Besides, China still faces an unbalanced development due to the sluggish reforms to state owned economic sector, macroeconomic management systems, and political sector. The Chinese government has been trying to find a way that not only could facilitate the transformation of SOEs but also upgrade the structure and technological standard to the Chinese manufacturing industry. It has always been the intention of the central government to build strong manufacturing industries in China with the help of foreign capital, technology and management skill. Against such a background, recently the open door policy has been redirected towards the task of industrial restructuring and the development of large corporations in strategic industries. Specific policies have been developed for promoting the establishment of large joint venture between major SOEs and MNEs in strategic industries including the automotive, information and telecommunication industry, heavy machinery, and petrol-chemical industries. The local partners of these major joint ventures are normally the SOEs that are directly supported by the government and have wide scope in the domestic market. Some of them enjoy a monopolistic power in China. It is expected that these major corporations should upgrade the competitiveness of the Chinese manufacturing industries to meet international competition both in the domestic and international markets. Politically, such an approach is expected to generate a sustained economic growth that will absorb the shocks of the reforms and provide conditions for further adjustments.

Chapter Four

Development of the Chinese Passenger Car and Food Processing Industries

Divided into two parts, this chapter provides the introduction and analysis to the background and the basic factors functioned to the development of the Chinese automotive and food processing industries. The focal point is to link the Chinese government policies, especially the policy of attracting FDI and the entry of MNEs with the development of the two Chinese industries. The first part focuses on the automotive industry and the second part deals with the food processing industry.

4.1 Development of the Chinese passenger car industry

In general, the growth and decline of the three forces in China have shaped the outcome of the Chinese passenger car industry in the last 15 years. These forces are the changing of the role played by the central government in directing the economic development in China, the growing power of provincial and municipal governments in developing regional economies and the opening of the Chinese economy to international investment.

The Chinese government has been the dominating force in planning and building the automotive industry since it took over the power in China since 1949. Before the reform

started in 1978, the industry was built into two levels. First, the large corporations directly under the control of the central government, and secondly the smaller regional factories both controlled by the local governments and the central government. As the Chinese economy started to change from a planned economy to a market economy in 1978, the Chinese military industry and part of the aviation industry have entered the automotive sector as an attempt of the government to adapt these government owned military industries into a market economic environment.

Hence, the current Chinese automotive corporations are generally of three types of background. The first is the large corporations that used to be controlled directly by the central government, such as First Automotive Works (FAW) in northeast China, Dongfeng Automotive Works (the former Second Automotive Works) in central China and Heavy Track Corporation in east and north of China. The second group is the firm that used to be controlled mainly by municipal and provincial governments such as Shanghai Automotive Industrial Corporation (SAIC), Tianjing Automotive Industrial Corporation (TAIC) and similar state owned companies in Beijing, Guangzhou, Nanjing and other industrial cities. The third group is the corporation of military industry background mainly located in northwest and southwest China. There are also other types of companies making buses, pick-ups and agricultural vehicles all over the country. Apparently, the Chinese automotive companies, whether big or small, belong to different systems. Competition between these firms is fierce, but it is conducted not purely on market economic conditions. Both the central government and municipal and provincial governments play an important role in the performance of these companies.

4.1.1 Central government function

It has been the intention of the Chinese government to build the passenger car industry as a pillar industry through which to stimulate the development of related industries, reduce the import of cars and to export local made cars in the future. When China made such a decision in the early 1980s, there was a huge technical gap between the Chinese automotive industry and the international standard. In addition, large sums of capital and foreign currency were needed, but were scarce at the time. In the light of these difficulties, the basic approach of the government in developing the industry was to exchange the domestic market with MNEs for their technology and capital. Selected MNEs were allowed to set up joint ventures with Chinese automotive firms to produce passenger cars locally, as a condition, these multinationals were required to bring in advanced vehicle models and technology. Through localization of these technologies, domestic firms expected to be able to produce high standard vehicles and components.

Since the early part of the 1980s, the government assigned a few automotive corporations to contact foreign companies to set up car assembling joint ventures. The mission assigned to Shanghai was to build an annual 30,000-unit car plant with the emphasis on localizing car components. In October 1984, Shanghai Volkswagen Automotive was set up, an equal partnership joint venture between Volkswagen and Shanghai Automotive Industry Corporation (SAIC). The joint venture produces Santana; a 1.8-liter sedan introduced by Volkswagen with the design of 1978 and was the most advanced model of Volkswagen in this range at the time (Chen, 1998a).

The mission assigned to FAW was to assemble cars to stop the imports. In 1988, FAW struck a license agreement with Volkswagen to assemble Audi 100 with a capacity of 30,000 per annum. Later, this project was escalated into a joint venture between FAW and Volkswagen in 1992.

The major project was assigned to Second Automotive Works Corporation (Dongfeng Motor Corporation) to build a modern car-manufacturing base. The Chinese authorities set up a few conditions for this project. The model should be advanced in technology, the output of this plant should be large enough to meet the requirement of economies of scale and that 2/3 of its output should be exported. After a revision of these conditions especially the export requirement, the Second Auto Works Corporation signing an agreement with Citroen in 1989. A joint venture, Dongfeng Citroen Automobile was established in 1992. Citroen introduced ZX, a 1.36-liter hatchback to the joint venture, the only model being built in China with a design of the 1990s at the time (Chen, 1997b).

The above three joint ventures are so called the 'Big Three' in the passenger car sector in the Chinese automotive industry. There are also some smaller corporations which also have national influence. Tianjin Automotive Industry Corporation (TIAC), Beijing Automotive Industry Group, and Guangzhou Automotive Manufacturing Corporation (GAMC) are the so called "little Three'.

Beijing Automotive Industry Group Corporation and America Motor Corporation (AMC) started their joint venture - Beijing Jeep Corporation in January 1984, the earliest in China.

In 1987, Chrysler took over AMC and so the stake in Beijing Jeep Corporation. The joint venture produces Cherokee jeep. In 1984 and 1986, TAIC had two technology transfer agreements with Daihatsu to produce Charade passenger car. In 1985, GAMC and Peugeot established a joint venture to produce Peugeot 505 and 504 (Xing, 1997). Due to the high cost and inferior quality of the cars made by Guangzhou Peugeot, the joint venture officially ceased in 1997. Later in 1999, GAMC teamed up with Honda for a new joint venture making Accord in the previous factory.

The central government controls the entry into the industry. Establishment of joint ventures between foreign and Chinese companies in assembling vehicles and making components in large scale has to be approved by the central government and foreign partners are not allowed to have majority equity in the joint venture.

In order to take advantage of an early production, even export and a gradual improvement of the capability by learning from doing, the Completely Knocked Down kits (CKD) model was chosen to assemble cars in the joint ventures. At the beginning, imported components assembled on the vehicles were close to 100%. Therefore, the local supply of component is critical to the profitability of the joint ventures. The central government has been using component localization requirement as a lever to urge auto joint ventures to raise local content level. Stipulated by the Chinese government in its "Automotive Industry Policy" issued in 1994, automobile assembling joint venture must start production with 40% local content to qualify for 37.5% import duties on parts. Car making joint venture that reach local content level of 60-80% may import parts at a rate of 20-30% (Zhang, 1995).

4.1.2 Fragment of the industry

However, the development of the Chinese automotive industry is not fully in line with the desire of the central government. Because of high tariff protection and growing demand, the passenger car industry has become an attractive business in China. Many municipal and provincial governments are eager to develop passenger car industries in their region. Such a development is considered to be important in reducing regional unemployment level and increasing local government revenue. For instance, in 1995, Tianjin Automotive Industry Corporation contributed 3/4 of the total profit of the entire manufacturing sector of the Tianjing City, which is the third largest in China after Shanghai and Beijing (China Economic News, August 12, 1996). Many localities including Shanghai, Jiling province, Tianjing, Hubei province, Jiangsu province, Shishuan provinces, Guangzhou City and others hold the automotive industry as a pillar industry.

As a result of the strong involvement of local governments in developing the automotive industry, it became highly fragmented. Local governments often impose restrictions on products produced in other regions to be sold or used in their own region. Shanghai Governments prohibited Taijing Charade to be used as taxi in Shanghai. Hubei province and Shanghai levied 10,000-yuen registration fee each other on cars built by opposite factories. In order to meet the local governments' requirement, Volkswagen had to build two engine plants both with SAIC and FAW and Pilkington set up at least three joint ventures with different groups in China.

The excessive investment promoted or supported by local governments in the passenger car sector has pushed the aggregate supply far beyond the domestic demand and the Chinese automotive industry has become the most fragmented in the world. In 1995, with an annual output of 1.8 million (50,000-passenger cars) in China, there were more than 100 auto assemblers and 3000 component manufacturers in operation. Excessive competition and regional protection impede the industry from reaching optimum scale. Though it is claimed by major corporations, including FAW Volkswagen, DongFeng Citroen, TAIC, Beijing Jeep that they are capable of producing 100,000 - 150,000 passenger cars annually, the actual output of these companies, except Shanghai Volkswagen is only about 50% or less of their designed capacity, which ranges from 20,000–50,000 units annually (Shen *ed*, 1998: 352).

The local protection ultimately stifle competition, limit effective market size, duplicate low level projects and cause high cost of auto parts and vehicles. This has made major auto manufacturers difficult to digest the heavy investment for improving the local content level and leads to high cost of making cars in China. As introduced by local managers in the interviews, the cost of Santana, produced by Shanghai Volkswagen, the most efficient car manufacturer in China, is higher than the similar car produced in Brazil. The poor economy of scale in making component is to be blamed for the high cost.

4.1.3 Function of FDI

So far, almost all the major automotive manufacturers in the world have taken part in large or small projects in the Chinese automotive industry. Complicated factors have functioned

to influence the behavior of FDI to the Chinese automotive industry. The most influential factors are the great potential of the Chinese market, and the possibility of the production facilities in China becoming major export bases in the next century. According to Economist Intelligence Unit (November 11, 1996), Volkswagen, General Motor and other European and American MNEs see the entry into China as a strategic step for expanding the market share not only in China but also the whole East Asia region. This is considered a strategic move challenging the dominance of Japanese companies in the region. To Volkswagen, its strategy is for China to become a big export base for the whole of Southeast Asia. " In the year 2003, I want to be able to go to Japan with German-engineered cars produced in China", commented Mr. Posch, the vice president of VW in charge of China projects (EIU, October 3, 1994).

To GM, the issue is how to take the strategic initiative in China away from the European companies, such as Volkswagen and Citroen and keep the Japanese firms at bay. In 1995, through a tough competition with Ford, General Motors won a 50% stake in a US$ 1.57 billion joint venture with SAIC to make a 3-litre variant of its Buick sedan.

Recently, as the importance of the Chinese market grows, Japanese automotive multinationals have also increased their investment in China. Toyota and Honda are vigorously competing with Volkswagen and General Motors to have a decent market share in China.

The commitment of the Chinese government in developing the passenger car industry is another significant factor influencing the FDI placed into the Chinese automotive industry. In interviews with Australian managers managing joint ventures in China, they all expressed that they are impressed with the Chinese government policies for building up a strong automotive industry. These policies include substantial tax and tariff reduction to foreign investors, coordination between the government and industries and the government spending. The Chinese government policy in combination with the potential of the Chinese market made the Australian companies believe that automotive industry in China will grow further. This is one of the major factors that promote the Australian companies investing in China.

The competition between MNEs in the Chinese market has provided chances for the Chinese government to ask for better terms in the negotiations with MNEs for setting up passenger car and component joint ventures. For example, in the negotiation between SAIC and GM, the American giant offered that it would license a broad range of component technologies to Chinese firms. Export targets were attached to these deals. In addition, GM had pledged US$ 40 million for five technology training institutions, with promises of significant technology transfers. A large part of the design work for the Shanghai Buick is to take place in China. According to GM"s president of China operations, Rudolph Schlaus, "through our joint venture, China is going to learn how to design and build a car" (EIU, August 19, 1996). It is commented that GM offered more than any other foreign automotive firm ever has and it has raised China's expectations of what can demand from foreign companies (EIU, August 19, 1996).

In response to the local content requirement raised by the Chinese government, MNEs are not only building their own facilities in China but are keen in introducing their first tier component suppliers into China. This move is very welcomed on the Chinese side. In fact, among 200 component suppliers of SAIC, more than 100 are joint ventures between foreign investors and Chinese companies. There are many German companies participating joint ventures in China owing to the establishment of the two largest passenger car joint ventures in China, namely the Shanghai Volkswagen and FAW Volkswagen. The representative of Volkswagen in Beijing claims that VW has contributed a great deal in mobilizing European component manufacturers to set up operations in China (He, 1999).

But as the Chinese market is still highly controlled by the government and the automotive industry is fragmented, foreign investors face serious challenges. For example, foreign companies feel constrained in doing business with a particular group or a limited market. It is difficult for foreign companies to extend their business to other regions unless they are willing to set up a branch or another operations with a different partner. In many cases, such movements are of high risks due to the insufficient demand in the region and incapacity of local partners for the new joint venture.

Currently, MNEs that have high market share and influence in China are Volkswagen, General Motors, Toyota, Citroen, and Honda. Volkswagen has teamed up with both SAIC and FAW in the two largest car assembling joint ventures in China occupying nearly 60% of the Chinese passenger car market (He, 1999). In response to the competition and the Chinese government Automotive Industry Policy, Volkswagen has accelerated its process

of introducing new models. By the end of 1999 the production of Passat B5 has began in Shanghai Volkswagen and Audi A6 will soon be produced in FAW Volkswagen in Jiling province.

Only after 12-month erection, the plant of Shanghai GM produced first car in 1999 with 40% local contents. The project is praised as the most efficient of this kind in GM all over the world (McCarthy, 2000).

After the completion of US$ 1.25 billion first phrase investment, Dongfeng Citroen has reached a capacity of producing 150,000 ZX Fukang (local name) and 200,000 engines annually. The facility is one of the most advanced automobile plants in China. The local content level of the car has reached 65% in 1997 and a 1.6-liter Electronic Fuel Injected Fukang has been developed on the original RG model. The sale of ZX Fukang has been continuously strong in recent years, owing to the advanced features and good performance of the car, which is superior to Volkswagen's Santana and Jetta whose designs are of the 1970s and the1980s (Chen, 1998c).

In September 1995, Toyota doubled its stake in Daihatsu from 17% to 33%. This move provided Toyota with means to join the license agreement between TIAC and Daihatsu. Recently, Toyota has submitted a proposal for establishing a joint ventures with TAIC for producing 1.3 liter small car and engine, with the capacity of 150,000 units annually. Because of these investments, TAIC has consolidated its position in the Chinese automotive industry (Qin, 1999).

In May 1999, Guangzhou Automobile Group and Honda signed a contract to form a 50/50 percent joint venture on the site of former Guangzhou Peugeot Automobile Corporation. The venture will be able to produce 30,000 newly developed Accord sedan annually in its first stage of operation. Now the plant is in operation and Accord is built with 40% local made components. Honda promised that it would transfer its advanced technology to the project.

Ford, Chrysler, Hyundai, Fiat, Nissan, Daimler Benz, Volvo and others are all involved in passenger motor vehicle assembling projects in China. The Chinese automotive firms with military industry background have established several license agreements with Japanese companies such as Suzuki, Mitsubishi, and Fuji Heavy Industry for making mini cars.

The critical mass of foreign automotive multinationals in China has lured the world's leading auto-parts companies to set up operations in the country. AlliedSignal Inc, Rebert Bosch, Cooper Dana Corp, Delphi Automotive Systems, GKN, ITT, Rockwell, Siemens, TRW Inc, Tenneco Inc, United Technologies Corp, Valeo, as well as leading Japanese and Korean component manufacturers have all invested in parts and components joint ventures in China. In 1996 alone, 74 automotive joint ventures were set up. By the end of 1996 the total number of automotive cooperative projects, joint ventures and wholly foreign-owned ventures reached 455, with an estimated US$ 2.5 billion in foreign capital. Asian Strategic Investment Corporation (ASIMCO), an America based overseas investment company invested nearly US$5.5 million in 17 joint ventures located in ten of China's provinces. These factories manufacture fuel systems, engine and brake parts and a wide range of

castings. According to the CEO of ASIMCO, the company "is well on the way to becoming the leading components group in China and also a global attractive company in the coming years." In 1997, the company exported US$15 million worth of auto parts, mainly to the United States (*China Daily,* July 4, 1998).

4.1.4. Future concentration

The Chinese government is always interested in building large conglomerates that can take on MNEs both in domestic and international markets. The keynote of the Automotive Industry Policy (AIP) issued in 1994 was to consolidate the industry that would lead to the evolution of 3-4 large automotive conglomerates, which include 6-7 key vehicle manufacturers. It is planned that by 2000-2010, the government would support the formation of 3-4 internationally competitive automotive conglomerates and 5-10 internationally competitive components groups (Xing, 1997).

Currently the central government still controls the entry of foreign companies into the automotive industry, and the government is purposely to use this power for encouraging the concentration of the industry. For example, the Chinese government has arranged ten major Chinese companies including SAIC to form a consortium named as China United Auto Electronics to set up a 50-50 joint venture with Robert Bosch. The total investment of this project is 2.67 billion yuan (equivalent to A$460 million). The joint venture enjoys monopoly power in China in making Electronic Engine Management Systems with a guaranteed domestic market. In an interview with the author, the senior manager of the joint

venture claimed that the technology of the product is more advanced than the Electronic Fuel Injection Systems made by Bosch Australia. The joint venture has already started exporting to Citroen in France. Negotiations for export to Volkswagen, GM and other large carmakers are on the way.

The development of the Chinese automotive industry in recent years is increasingly a result of the combination of forces between the Chinese central government, local government, and capability of Chinese firms and foreign MNEs. The availability of location-advantage and ownership advantage is becoming a most important determinant for the success of the investment. For example, even though the project assigned to Shanghai by the central government in the 1980s was limited in comparison with the project assigned to Dongfeng group, Shanghai soon won the competition and SAIC became the largest and the most efficient passenger car producer in China. As a traditional industrial center, the political, economic, human resources and supporting industries are far better in Shanghai than other regions in China. The relatively low technical standard of the Santana also helped Shanghai Volkswagen to achieve a high rate of localization ahead of its competitors. This enables Shanghai Volkswagen to reduce cost, expand the market share, and make further investment. For a very long period, Shanghai Volkswagen has occupied more than 40% of the market share in China's passenger car market. Protected by the tariff which was between 100-150% in last 10 years, Shanghai Volkswagen enjoyed an abnormal profit. In 1996, the total profit of the Chinese automotive industry was RMB 6.6 billion (A$1.15 billion) of which Shanghai Volkswagen took RMB 6 billion, a share of 90.9%. The joint venture has reached the capacity of producing 300,000 cars annually in 1997 with more than 90% local

contents on the oldest model. The sales were 230,000 units in 1997, and 215,427 in 1998 (Chen, 1998a). SAIC's outstanding competitiveness helped its effort of seizing opportunities with General Motor for establishing a joint venture in making 3-liter Buick in 1995. This deal reinforces the leading position of SAIC in car making in China. SAIC is solely responsible for the capital investment without funding from the central government is a very important factor for winning the support of the central government for this project, as other local car making groups and provincial governments were also competing for this project.

In November1999, China and the U.S. sealed the negotiation for China's admission to WTO. In the deal China will cut tariff for cars from its current 80-100% level to 25% in 2006 (*Time* May 22, 2000). Further, restrictions imposed on foreign companies investing in China will be eliminated. These restrictions are normally required on export, local content level, and technology transfer attached to the joint venture agreement. China has recently announced to change its law for foreign investment so as to comply with the WTO rules.

It is expected that China's admission to WTO will enable car making joint venture in China to increase the import of components. Shanghai GM has already adopted a policy of global selection of components. MNEs can more freely select local partners and promote their products in China. These expected changes would put great pressure on domestic automotive industry and alter the way in which the government intervenes with the industry. It is anticipated that a large number of domestic component manufacturers will be

forced out of the industry through mergers and acquisitions. The reduction of protection will help the Chinese automotive industry toward concentration.

4.2 Development of the Chinese food processing industry

Basically, the development of the Chinese food processing industry in the last twenty years is a process in which SOEs are struggling to adopt themselves into an environment in which the old planning economic management system is being gradually replaced by market economic system while foreign and other non-state owned companies compete swiftly to take over the dominance away from SOEs in the market.

4.2.1 Food-processing SOEs in the reform period

China's food processing industry used to be mainly in cities and owned by the government. These SOEs were organized into a huge hierarchy, which are controlled by government departments at the central and local level. For example, Shanghai Food Processing Industrial Corporation used to be the government body managing state owned food manufacturers in Shanghai. The corporation reported to both Bureau of Light Industry under Shanghai Municipal Government, and Ministry of Light Industry in Beijing under the State Council of the central government.

Since the reform started in 1978, the policies of reforming state owned economic sector have been concentrated at shifting political power and economic interests from the central government to local governments and SOEs. The main policy of SOE reform is to grant

administrative power to enterprise management and link staff income to the enterprise performance. It is widely believed that even though the policy has provided incentives for SOEs to compete in an environment in which market forces are growing, it failed to address the fundamental reason causing the inefficiency of SOEs, which is the ambiguous definition of the propriety right of SOEs. Without personalized owner to look after the enterprise, SOEs still belong to the government but not as a real separated entity responsible for its own profit and loss.

However, the continuous shift of economic power from the central government to local governments and SOEs has changed the relationship between state owned food-processing manufacturers and the government. While the influence of the central government is declining, the connection between food processing enterprises and regional governments becomes stronger. Most of the provincial and local governments in China take great importance on the development of food processing industry, as many regions in China are rich in raw materials for developing food-processing industry. In addition, investment scale and technological requirement for food processing can be flexible while the local market can be reserved to local firms if protective measures are under taken.

In view of this, the investment on the food-processing industry made by SOEs subsidized by local governments as well as the central government has been on the rise since 1978. Between 1992 and 1996, the investment on fixed asset to the food processing industry totaled 144.2 billion yuan (about A$25 billion) and from 1979 to 1997 the Chinese food

processing industry has utilized more than 10% of the total FDI made into China (Wang, Jan.3, 1999).

However, as commented by Yu Zhen, head of the Chinese Light Industrial Association, one of the significant shortcomings associated with these investments is that they are divided into hundreds of projects in different locations with low technical contents (Yu, 1998). In addition, as the main investors of these investments are SOEs and government agencies that are struggling to adopt themselves into a changed economic environment, their management expertise, human resources, and R&D capacity are insufficient to run these projects efficiently. Therefore, these investments have not upgraded the competitiveness of the state owned food-processing industry as expected. There are no powerful domestic companies covering the market share at national level. The industry became highly fragmented. Excessive capacities are built in different locations for making undifferentiated products. Therefore, SOEs are not able to compete with the MNEs and other foreign companies that have invested in the Chinese market.

As an effort of the Chinese government to break down the direct connection between the government and SOEs, reforms have been reinforced since 1994 for downsizing the government agencies that control SOEs directly. For example, now the Shanghai Light Industry Bureau has become a state equity holding company and the Shanghai Food Processing Industry Corporation has been abandoned. The Light Industry Ministry in Beijing has been downsized to an Association of Light Industry. Food manufacturers that

used to be under Shanghai Food Processing Industry Corporation formed two corporation groups, namely, Mailing Aquarius Group and Guan-Sheng-Yuan Group.

In a number of interviews conducted by the author in the field study in Shanghai, some senior executives, factory directors and managers from these two groups, considered that major changes had taken place in the industry. First, the oversupply in the market has left little chance for SOEs to have a major market share and decent profit. Due to too many employees left from the old time, wage expenses has been the highest cost in the total operation. Though the autonomy of factory management in daily operation is much stronger than before, the excessive government intervention still prevents them from reacting swiftly in market competition, particularly in the areas of selling assets, acquisition and merger. Due to the deepening of the banking system reform, it is increasingly difficult for SOEs to access subsidies and loans from government and state banks. Most of the factories are short of cash. SOEs are generally having a very limited spending on R&D. Shanghai Guan-Sheng-Yuan Group can only spend 0.5% of its limited sales on R&D; Shanghai Mailing Aquarius Group is even less than that.

4.2.2 Development of food-processing township enterprises

The development of township enterprise has a direct impact on the Chinese food processing industry, as 43% of the food and beverage processors in China are township enterprises (*Economic Daily*, January 12, 1998). Township enterprise has been proved to

be an effective form in adding value to agricultural raw material. According to some successful examples, township agribusiness can be very competitive owing to obtaining large economies of scale by collecting large numbers of small or family businesses around core processing plants. These families and small businesses are extremely flexible. They can supply very fresh and cheap agricultural products to be processed. The high concentration of growers and processors together has reduced transportation costs and formed a large pool of capital, information and human resources. By entering into a contract to supply raw materials to the processor, farmers benefit from a guaranteed purchase of raw material and improved sales margin (*China Food Newspaper*, May 11, 1998).

Township enterprises involved in food processing industry have a high percentage in the livestock industry, meat processing industry, fruit and vegetable processing industry, soft drink industry and dairy industry. The development of these industries, among with other factors have contributed to a significant improvement of the food consumption per capita in China. Since 1978, the annual consumption of meat has increased from 20 kg to 48.3 kg, egg from 5.4 kg to 16 kg, milk from 3.5 kg to 6 kg, fruit from 15.3 kg to 38 kg and aquatic products from 8.7 kg to 27 kg (Gao, 1998).

But there are weaknesses associated with the development of these township enterprises involved with food processing. A Chinese survey revealed that there is an astonishing similarity of the product structure and technological conditions among township enterprises

all over the country, which are basically producing undifferentiated products. Most of these township enterprises are developed from collective entities and private businesses in rural areas and backed up by local governments. These firms are usually small and limited with financial, human resources and information resources. Normally they can only apply primitive technology. Before 1994 and 1995, many of these enterprises were able to grow because the market then was short of supply. Such a situation has been changed in recent years as the market has gradually been saturated with undifferentiated products (Zhang, 1998).

The number of township enterprises peaked in 1994, but began to decline in number since then. By the end of 1997, the stockpile of township enterprises reached RMB 400 billion (A$ 80 billion). Among the township enterprises 15 % are making losses with a total value of RMB 60 billions (Wang, 1998). Due to the sluggish demand and excessive supply the price of agricultural products, including rice, wheat, meat, vegetable and fruit is falling, The news of farmers slaughtering cows, chicken, pigs, and destroying fruit trees became common.

4.2.3 Entry of FDI and growing dominance of MNEs

In China, the establishment of joint venture between SOEs and foreign companies has been widely regarded as a solution to energize SOEs and thus promoted China's economic growth. The central government is generally in favor of approving more joint ventures, in

particular to the food processing industry which is not considered to be a 'strategic industry'. To many local governments, increase in joint ventures in the region can strengthen regional economy, reduce regional unemployment rate and increase local tax revenue. Therefore, local governments are normally more enthusiastic than the central government in attracting foreign investment into their region. Developing regional food processing industry with the help of foreign investment is a priority for many agricultural provinces in China. As to SOEs, they are generally keen to incorporate with foreign investors. By setting up joint ventures SOEs not only can access foreign technology and capital but also can be eligible for tax concessions and cheap loans from the government.

The above factors, in combination with the importance given by international companies to the Chinese market, have facilitated a significant amount of FDI being put into the Chinese processed food sector since China opened its door in the late 1970s. Substantial investment from Hong Kong, Taiwan, Japan, America, Singapore, Korea and European nations has been invested in the soft drink, dairy products, confectionery, biscuits, instant noodle, seafood, meat, poultry and other food processing industries.

As SOEs are struggling in the process of transition, and township enterprises are troubled with limited scale and inferior technological standards, domestic companies are not able to meet the challenge imposed by MNEs in the Chinese market. Taking the confectionery business as an example, import of chocolate confectionery into China more than tripled, from 600 tones to 2100 tones between 1988 to 1993. More than 60% of Chinese

confectionery businesses have been forced to close since 1988 (EIU, September 30, 1996). Nowadays, mergers and acquisitions are frequently happening in the Chinese food processing industry.

Since 1992, FDI into China has significantly increased from the previous level. Major food processing MNEs are entering the Chinese market. In the face of strong challenges imposed from foreign companies, the number of SOEs, particularly large SOEs, seeking establishment of joint venture with MNEs are increasing. Furthermore, as the endorsement of the Chinese government for turning SOEs into joint stock companies recently, MNEs have increasingly used acquisition of shares in a Chinese company to expand their size in China. In recent years, some influential acquisitions of major SOEs conducted by MNEs have significantly changed the landscape of the Chinese food processing industry. Among the eight biggest local beverage companies located strategically in different regions, MNEs bought seven. More than 90% of the major local breweries teamed up with foreign breweries. The most significant motivation of Chinese companies to sell their equity is to access capital for survival (Wu & Zhang *eds.,* 1997). Currently, there is an ongoing concentration of foreign brands in the Chinese market. Many of these foreign branded products are produced locally by joint ventures between MNEs and Chinese firms. Nescafe has occupied 50% of the Chinese instant coffee market. Coca-Cola shared 30% of the carbonated drinks market. United Biscuits of England, Danone of France, Nabisco of the U.S.A. dominate the biscuits market in Guangdong, Shanghai, and Beijing respectively. The leading manufacturers of Chocolate in China are Mars, Cadbury and Nestle. More than 60% of the market share of ice cream in Shanghai is taken by foreign brands (Bowles,

1997). Many MNEs have entered a stage with a main objective of securing a dominant share in the Chinese market. These MNEs are focused on issues such as how to effectively managing key local partners, including establishing relationships with the decision-making authorities, such as the industry associations, government bureaus and ministries.

It is apparent that a strong FDI leads to a rapid concentration of foreign products in the Chinese market, but this does not mean that the Chinese market is ideal for all kinds of foreign investors. The fragmentation of the market and the oversupply of materials and processed food are also influencing FDI in the Chinese food processing industry. According to a 1996 EIU (December 9, 1996) report more than half of the foreign companies invested in China had overstated the Chinese market. China's retail food market remains relatively small, an estimated sales volume in 1995 was roughly US$ 126 billion, which was equivalent to that of Britain (Bowles, 1997). In reality, the market could be even smaller as barriers exist between different provinces in China. There is stiff competition between foreign investors. Presently, approximately 40 major international breweries have set up joint ventures in China. In 1998, each of China's leading brewers of foreign premium brands was likely to be operating at less than 50% capacity (Wu & Zhang, 1997).

Furthermore, FFEs are confronted with a chaotic distribution system. The distribution system in China used to be controlled by the government. Reforms may have broken the centralized distribution system at the national level, but local governments are still holding strong influence on local distribution system. It is common for local governments and SOEs

to take advantage of such a position to prevent products made in other regions from entering into their market.

The Chinese market has been very unique and challenging for foreign investors. "A 1999 survey by AT Kearney found that 60% of all foreign companies were unprofitable in China" (McCarthy, 2000). Though there are some examples of foreign small to medium companies taking niche markets in China, it seems that only large MNEs are able to establish a dominant position at the national level. MNEs are normally transferring mature products with high sales volumes to China and concentrate on manufacturing and market promotion. This approach reflects that the investment of MNEs is mainly for market expansion. Setting up plants in China has provided a way for these MNEs by passing the tariff barriers and building up connections and experiences for doing business in China.

The capacity of MNEs in market promotion is much stronger than that of most SOEs, township enterprises and small-medium foreign companies. This factor has directly contributed to the winning of market share of MNEs from SOEs in China. In interviews with the author, SOEs' managers complained that the MNEs in China even promote their products with a deficit in their balance sheet. They argued that these MNEs aim at pushing SOEs and other competitors out of the market so as to establish a monopoly in the future.

MNEs are often concentrated to one or two plants initially and expand to other regions after gaining experience in doing business in China. In this way they overcome the problem of

high fragmentation of the Chinese market. MNEs that have high market share in China are normally having multiple production and representative facilities in different regions. Nestle has 11 plants in China, Coca-Cola has 20 bottling plants with some more being built, and Pepsi has 12 plants. MNEs endeavor to obtain majority of equity in joint venture that can enable them to control the distribution. Today, Coca-Cola operates a hybrid distribution system that relies on both direct distribution and third-party wholesalers. Roughly 30% of the company's nationwide distribution is handed in house. In its newest plants, such salespeople account for 40-50% of all employees (EIU, February 19, 1996).

4.2.4 Further development

It is estimated that the current surplus of labor force in the rural sector in China is about 150-200 million (Gou, 1998). One of the basic solutions to absorb so large a labor force in the Chinese rural sector is to link the agriculture with food processing industry. This is of strategic importance to China as it will increase income of farmers and thus cultivate a growing demand for manufactured products.

In view of this, the development of township enterprise is being highlighted as a direction for the future rural economic development. In particular, the government called on farmers, township enterprises, and local governments to develop agricultural business specializing in adding value to agricultural raw materials. According to the Chinese statistics, only 40% of the agricultural raw material in China have been processed into manufactured food

products. This ratio is much lower than the level of 100% to 300% in developed nations. In other words, there is a huge room in China to develop food-processing industry in rural areas (Wang, 1999).

As pointed out by the Chinese Ministry of Agriculture (1997), the future success of the township enterprises in agricultural business will depend on the avoidance of duplication of small and poorly equipped projects. The key is to build large-scale enterprise that integrates and completes the value chain from agricultural production, food processing, to wholesale and retailing. These large enterprises are able to attract foreign investment, deploy advanced technology, improve value chain of production and link rural communities with both urban and export markets.

In line with these new policies, there are some large agricultural businesses being built around the suburbs of major cities. These large agricultural businesses are normally transferred from the former state farmers. For example, in 1995, the Shanghai Agricultural Commission turned into Shanghai Agriculture, Industry & Commerce General Group Corporation, an equity holding company owned 4600 factories, 230 joint ventures, and 52000 hectares of land. It integrates production, processing and marketing of agricultural commodities. Its products include beef, pork, aquatic products, milk and dairy products, fruits and vegetables, high quality grain, flowers and turf. These large agricultural businesses have provided a channel to absorb foreign investment. For example, Beijing Agriculture, Industry & Commerce General Group Corporation is the local partner of the

joint venture with Cadbury Australia in Beijing. So far, 6000 FFEs have been established in the agricultural sector utilizing more than US$10.2 billion. Under the Ninth Five-year Plan (1996-2000), the Ministry of Agriculture hopes to attract US$ 7 billion in agriculture, and US$14 billion in wider agribusiness sector which includes related light industrial processing and agrochemical industries (Helsell, 1997).

The above position of the Chinese government is again reinforced by the deal signed between the U.S. and China for China's accession into WTO in November 1999. Currently, as too many people involved with agricultural production in China, the cost of producing wheat, corn, soybean is already above the international standard (Ye, 1996). In the deal with the U.S. government, China has agreed to reduce tariff for agricultural products from current 45% to 15 % in 2005. As a balancing adjustment to such a commitment, China will concentrate on developing the agricultural sector requiring large labor force, such as growing and processing fruits, vegetable, livestock and aquatics. As reported in *Jiafong Daily* (May 20, 2000), the official newspaper of Shanghai government, the foreign and local investments made into high-tech agricultural projects around suburbs of Shanghai have increased to A$600 million. Foreign investors from Holland, Israel, Japan, New Zealand and others have brought in advanced technology for growing high quality vegetables, flowers and other types of agri-food products.

As agriculture and livestock is the first link of the chain for food processing, such a change will have a profound impact on the Chinese food processing industry. It is expected that

imported raw materials such as wheat, flour, milk powder and sugar will increase. With the decrease in tariff, prices for imported manufactured food products will also be cheaper. This will further eliminate inefficient producers in the Chinese market and encourage the concentration of foreign brands in the Chinese market in sectors such as confectionery, bakery, health food and dairy products. MNEs will take advantage of their strong international networks to import or produce products locally for the Chinese market in a most cost efficient way.

The Chinese government will further encourage township enterprises engaging in productions adding value to agricultural products. Township enterprises will play an increasing important role in agri-food industries such as livestock and fish growing, meat processing, fruit processing and other sectors that need significant labor input. The exports of these products from China will further increase from the current base. In order to develop these industries, China needs to introduce more advanced technical expertise, special machinery and management skill. Foreign investment on these sectors will need to be increased.

Chapter 5

Research questions and Methodology

5.1 Research questions

It can be concluded from the theories reviewed previously that in an imperfect market competition environment, FDI becomes an important tool for countries and companies of different backgrounds to achieve strategic objectives. According to UN report (1998), the international FDI can be generally classified into two kinds. The fist kind, which is also the most common type of FDI currently, is the investment made by firms between industrialized nations. As indicated by Dunning (1996), the motivation of this kind of FDI is basically for accessing differentiated ownership and locational advantages in other developed countries. A cross investment between firms of industrialized countries can benefit companies involved from sharing high quality human resources and infrastructures, improving R&D capacity, enlarging economies of scale, and reducing cost. Recently the merges between some world largest automotive companies and banks, such as Mercedes Benz and Chrysler, General Motors and Fiat can be considered as perfect examples of this type of FDI.

The FDI made by companies in industrialized countries to developing countries is another major type of FDI internationally (UN, 1998). According to Investment Path theory

(Dunning 1996), this type of FDI is mainly aimed to access locational advantages in developing countries such as cheap labor and emerging markets. Such kind investment is very important to MNEs, as it is a critical part of the strategy developed by MNEs in response to international competition. On the developing country side, as FDI can benefit host country in terms of substantial capital investment, technology transfer, employment and export opportunities, developing countries are generally in favor of attracting FDI as much as possible.

Attraction of FDI has been one of the basic strategies deployed by the Chinese leadership for implementing the reforms and pursuing a fast economic growth. With the deepening of the reforms and gradual opening of the Chinese economy, the inflow of FDI has been growing continuously. These developments have rapidly improved the living standard in China and the strategic importance of the Chinese economy. Since 1992, strategic investment made by MNEs aimed at conquering a position in the Chinese market has been expanding rapidly. In order to exploit the market potential, meet the competition between international companies in the Chinese market and satisfy the Chinese government requirements, many of the automotive and food processing projects invested in China by MNEs are of large scale and with substantial technology transfer. Volkswagen, General Motors, Coca-Cola and others hope that their affiliates in China could become major production or export bases in the 21st century.

In the face of a rapid growth of FDI made into China, the implications to the Australian manufacturing industries in terms of entering the Chinese market are profound. First, the

factors influencing the entry of Australian companies to China should be broadened to international area. Vernon (1996) suggests that the capability of smaller companies in access to foreign markets might be limited or weakened by the strong 'scanning power' of multinationals. This point might be of great importance to the performance of Australian industries in China. Though Australian companies may have the technological advantage over their Chinese counterpart, the massive transfer of technology of MNEs to their Chinese affiliates may overshadow the marketing of these Australian technoiogies to China. Also, the export of Australian manufactured products to China might be undermined due to the strong promotion of MNEs for their products in China. Small to medium Australian companies that have limited financial and human resource might be particularly disadvantaged in exporting or investing in China due to the dominance of MNEs in the country.

Kojima (1978) considers that FDI can promote mutual trade and industrial restructuring both in home and host countries. This judgement is again verified in China, as various reports indicate that FDI has significantly contributed to the Chinese international trade, and the restructuring of the Chinese manufacturing industries. EAAU (1996) comments that the share of FFEs in China's total export increased from 12.58 % in 1990 to 40.91 % in 1996, and the share of FFEs in the total import raised from 23.07% in 1990 to 52.42% in 1996. A great amount of China's exports is based on the reprocessing of materials, semi products and components imported. The increasing influence of MNEs to the Chinese international trade generates even more and complicated implications to the Australian food processing and automotive industries that both has a high percentage of foreign ownership.

According to Dunning (1996), the contents of FDI, in terms of motivation, destination, forms, investment scale, technology transfer, and trade opportunities are closely related to the overall competitiveness of the home and host countries involved. By referring to Porter's 'diamond model', Dunning argues countries that have skilled work force, strong R&D capability, large and demanding market, and high standard infrastructures are most likely to conduct or receive the FDI associated with high value adding activities. Increasingly MNEs invest in countries where they can access strategic assets contributing to innovation, cost reduction or market expansion. The decision to invest in a particular country rests on the comparison of the competitive advantage of the firms and countries concerned relative to those of firms of other countries. Furthermore, Dunning (1996) comments that FDI to a host country will have two-side effects. On one hand, it brings in capital, technology and international trade opportunities, on the other, it takes away the payment from host nations. The payment is not only as profits, dividends and managerial fees but also the control imposed by investing companies to the domestic firms.

Given the fact that comparative and competitive advantages between nations have played a vital role in the flow of FDI internationally, when MNEs assess their investment plan in Asia Pacific region, the comparative and competitive advantage that Australia can offer is increasingly being compared with what other countries in the region have offered. MNEs will allocate different roles to their affiliates in Australia and other countries in accordance with the difference in national comparative and competitive advantages. This process might provide particular answers to the performance of the Australian based foreign subsidiaries

in the Chinese market. Some subsidiaries might actively participate their parent company in projects in China while others might be restrained due to their various limitations.

Based on the above implications which are derived from the theoretical reviews and the reference to the development of the Chinese automotive and food processing industries, the first direction of this research is to investigate how FDI made by MNEs in China will affect their operations in Australia. Specifically, the investigation will attempt to answer following questions:

- Are the investments made by MNEs in China strategically complementary or competitive to the subsidiaries in Australia?

- Have Australian subsidiaries been encouraged or discouraged by their parent companies in participating with projects in China?

- Do Australian subsidiaries and subcontracts export products to China through the network provided by MNE parent companies?

- What kind role do the Australian subsidiaries play for their parent companies in China and what are the determinants of their roles?

The second direction of this research is to investigate how Australian small to medium sized enterprises, particularly indigenous companies been affected by the strong FDI in

China and the on-going integration of the Chinese economy into the world economy. Some questions in this aspect are:

- Have small-medium sized Australian firms been pushed out of the Chinese market due to the strong presence of large MNEs in China?

- What are the common assessments of the risks in doing business in China and in particular the small and medium Australian companies?

- Are Australian companies able to take advantage of the network created by MNEs in exporting or investing in China?

The third direction is to identify the factor conditions in Australia that have influenced performance of the Australian food processing and automotive companies in the Chinese market. The range of these factor conditions should cover natural resources endowments, cost structure, R&D capability, economies of scale, government industry policy, knowledge of the Chinese market, function of the Chinese descendents in Australia, and the capacity of Australian companies in doing business internationally.

5.2 Methodology

5.2.1 Selection of the food processing and automotive industries

In order to fulfil the tasks of this research, the automotive and food processing industries are selected for the investigation. As the largest manufacturing industry in Australia, the food processing industry accounts for 21 percent of the manufacturing turn over, 18 percent of the sectors employment and 25% of the manufacturing sector's exports in 1993-94 (BIE, 1996). The Australian food processing industry presents a wide range of the comparative and competitive advantages that are unique to Australia. The industry is backed up by an efficient agricultural sector, which provides high quality raw material with a world competitive price. The industry has developed a relative large scale and a strong R&D capacity, which is considered to be one of the best in the Asia Pacific region (BIE, 1996). Furthermore, as the industry has a high foreign ownership and a strong tendency of export, the exposure of the industry to international competition is high. Also, there are various government programs specialized in promoting Australian food processing industries overseas.

In contrast to the food processing industry, the size of the Australian automotive industry is small which accounts for 6.9 percent of the Australian manufacturing turn over (IC, 1997). However, the industry has a unique position in the Australian economy. It generates the demand for high quality of R&D in Australia (IC, 1997). The industry is subjected to a high degree of international competition, as the majority of the companies in the Australian automotive industry is foreign owned. The impact of globalization on the industry is particularly high. Although the Australian automotive industry is limited in size, it has developed sophisticated technology and unique advantage in designing and producing small quantity and high standard components with short time span (IC, 1997).

In a summary, the Australian food processing and automotive industries are the most important manufacturing industries in Australia. These two industries have technological advantages over their counterparts in China and their expertise is much needed there. However, as there is a large percentage of foreign ownership in these two Australian industries, the impact of globalization to these two industries is great. MNEs activities in the Chinese market and the whole Asia Pacific region will influence the entry of these two Australian industries into the Chinese market. Therefore, all the conditions of the automotive and food processing industries in Australia and China provide useful contrasting case studies for exploring the theoretical and empirical issues posed by this research.

5.2.2 Research Methods

The research used a variety of research techniques to fulfil the aims. First, a comprehensive literature review has been conducted to collect concerned information as much as possible. The information should cover following range:

- The analysis and statistics provided by the Chinese and international institutions in relation to the Chinese government reform strategy, in particular the policies for attracting FDI. The information should also include the changing of the Chinese industry structure, market demand, pattern of international trade, technological transfer associated with FDI and the trend of future FDI development.

- The approaches taken by foreign investors in entering the Chinese market; the purpose of the FDI in China; the role playing by the affiliates OF MNEs in China; major factors contributing to the inflow of FDI and major impediments to the future foreign investment.

- The Australian economic policy and industry policy debate; analysis to the competitiveness of the Australian manufacturing industry; factors that influence the performance of the Australian food processing and automotive industries; and the effectiveness of the Australian government economic and industry policies.

- Successful examples of Australian companies in entering the Chinese market and conversely the failure of Australian companies in the Chinese market.

- The relationship between Australian based foreign subsidiaries and their parent companies in developing business in China.

The sources covering the information mentioned above are available both in English and Chinese. There are some reports prepared by the Australian government agencies are extremely valuable to this research. Examples of these reports are *The Automotive Industry* (IC, 1997); *Agri-Food Case study: Micro Reform - Impacts on Firms* (BIE, 1996); *Automotive Case Study: Micro Reforms – survey of Impact on Firms* (BIE, 1996); *Evaluation of the Agri-Food Strategy* (1996 BIE), and *Investment abroad by Australian companies* (BIE, 1995). Substantial information are also available in other publications

issued by academic, government and private institutions, such as Australia Bureau of Statistics, Business Victoria and other magazines, and newspapers.

The information about China's reform and the development of the Chinese automotive and food processing industries are available in libraries of universities in Melbourne. Furthermore, there are also large quantity of valuable information can be derived from Internet. A field study had been carried out in China, which allowed the investigator to access a large number of Chinese publications, statistics and government reports provided relevant, detailed, and more complete information. During the field study, the author had conducted qualitative interviews with key informants in the automotive and food industries through personal contacts in Shanghai, China where the largest passenger car manufacturing industry and a very strong food processing industry are situated.

The collection of the secondary information in combination with the theoretical review on FDI form the platform from which specific research questions and questionnaires are developed. In order to test if the research questions and questionnaires developed are relevant to key issues concerned by the two Australian industries in relation to the entry into the Chinese market, the author has taken a systematical approach to seek feedback from the Australian industries. Following paragraph is the introduction of this process.

Before finalizing the research questions and questionnaires, the author has prepared two papers about the development of the Chinese food processing and the automotive industries and its consequences to the Australian industries. The preparation of these

papers is served to arouse the interests of informants and ask them to provide comments and suggestions to the research questions and questionnaires. The papers were sent to major industrial associations, government agencies and selected companies in the industries. The reply was high. The author received letters from Business Victoria and EAAU, and various companies and institutions such as the Australian Automotive Intelligence (AAI), Victoria Employers' Chamber of Commerce and Industry (VECCI), Federation of Automotive Products Manufacturers, Austrade, and Australian Food Marketing Center Victoria University. Some of these institutions such as AAI, VECCI and Austrade offered comments on the preparation of the questionnaire, provided valuable data, and arranged interviews for the author to meet with important informants from Australian industries.

5.2.3 Questionnaire Survey

Collection of original data and information was a major procedure for this research which was to be guided by the implication developed from the literature review and analysis to the collected secondary information. The collection of original data was carried out through a mail out questionnaire survey and interviews in Australia and China.

Sample companies selected for the questionnaire survey to the Australian automotive industry were primarily chosen from the *Products Directory 1999, Australian Automotive Industry,* edited by the Federation of Automotive Products Manufactures Australia (FAPM). Except for some very small and service-orientated companies, out of the 120

companies listed in this directory, 105 manufacturing companies were selected for the survey. These companies cover different types of ownership and employment sizes. In addition, 5 Victoria based automotive companies exporting to China which were added to the list were selected from the database of *Kompass Australia, 1998.* The selected companies represent the Australia automotive industry, as the *Products Directory 1999; Australian Automotive Industry* is a comprehensive and authoritative directory of the industry. This is confirmed by similar contents publicized in the major business directories in Australia, such as the *Kompass Company Information*, and *Business Who Is Who in Australia.*

The questionnaire survey to the Australian food processing industry covers sample companies of 150 food manufacturers and a few trading companies. The selection of the companies was purposely to include different types of enterprises in terms of employment size, ownership, and connections with the Chinese market. The companies were primarily chosen from *Kompass Australia 1997* and *Kompass CD Rom 1998.*

Chapter Six

Export and Investment of the Australian Automotive and Food Processing Industries in China

The main contents of this chapter are the reports of the questionnaire surveys and the face to face interviews conducted by the author to the Australian automotive and food processing industries in the topic of export and direct investment in the Chinese market. The comments in terms of the performance of the Australian automotive industry in China made by the Chinese informants during the field study in China conducted by the author are also provided. The first part is for the automotive industry and the second is for the food processing industry.

6.1 Automotive industry

The total number of the questionnaires sent for the survey was 110, three were returned because of changing of recipients' addresses. Out of the 107 effective questionnaires, 23 were completed and returned. In addition, the investigator received 5 letters from different firms and organizations and conducted 8 interviews with senior Australian managers from the Australian automotive industry. Also the author interviewed 5 Chinese senior managers mainly from Shanghai Automotive Industry Corporation during

the field study. The total number of the Australian companies that replied is 28. Following are the major findings of this survey.

6.1.1 Factors preventing Australian automotive companies entering the Chinese market

The percentage of Australian automotive companies exporting or investing in China is low. Among the 28 companies that replied in this survey, only three indicated that they exported automotive components from Australia to China. Two of these three companies have established joint venture in China and ranked their export to China as fairly important and the another company considered that its export to China was potentially important. All of these three companies had a fluctuated export volume all the time.

On top of the questionnaire survey, the author has conducted further investigations by collecting secondary information from newspapers, magazines, and government documents published in Australia and China and on Internet to check the number of Australian automotive companies having invested or exported to China. It was found that only 7 Australian companies were involved in various direct investments in China. The very low level of involvement of Australian automotive companies in China coincided with the fact that among the 120 companies listed in the *Products Directory 1999, Australian Automotive Industry* only 7 claim exporting to China (FAPM, 1999).

Table 2: Factors prevent Australian companies from exporting or investing in China (A breakdown by company ownership)

Factors	Number of companies	Foreign subsidiary			Australian owned firm		
		Factor significance			Factor significance		
		Major	Moderate	Minor	Major	Moderate	Minor
Tariff & trading barrier in China is too high	9	1	2	No	1	1	4
The China market is taken by parent company or other companies within the group	14	13	1	No	No	No	No
International companies dominate the Chinese market	5	1	No	2	1	No	1
Joint ventures in China import Products via channels provided by their foreign partner	6	1	2	1	1	1	No
Our product is not compatible with local made vehicle	1	No	No	No	No	No	1
Price of our product is too high	10	No	2	2	2	3	1
Difficult to find a distributor in China	9	No	2	2	1	3	1
Too much investment will be required to enter China	11	1	No	3	2	2	3
Chinese market is unknown to us	12	2	1	2	3	1	3
Other markets are more important than China	11	2	3	No	3	2	1

Source: Author's questionnaire survey May-June, 1999.

These findings do not indicate that the Australian automotive industry is not interested in entering the Chinese market. The author has felt that Australian automotive companies are enthusiastic about this survey. The response rate to the investigation was higher than

that of the Australian food processing industry. Currently, though only a few companies are operating in China, many are willing to and some are actively preparing to enter the market. However, it is found in this survey that there are complicated factors affecting Australian companies from exploiting the Chinese market. Basically these factors can be divided into four aspects:

a. The competitive advantage of the Australian automotive industry is not fully in line with the Chinese government automotive industry policy

It has been emphasized frequently by Australian managers in the interviews that the most distinguished competitive advantage that Australian automotive component manufacturers possess is the capability in delivering high quality products with small quantity, low production cost and short time span. Such kind of technology is very unique and is significantly different from the methods of mass production adapted by many large international companies. But this particular competitive advantage offered by the Australian automotive industry is not fully in line with the Chinese government policy whose intention is promoting the concentration of the Chinese automotive industry by encouraging the incorporation of local automotive corporations with MNEs. Even though the Australian technology is highly needed in China as the majority of Chinese automotive companies are running at small production scale with high cost.

One of the guidelines acknowledged in the Chinese Automotive Industry Policy 1994 for the selection of foreign partner for the major automotive joint ventures is that foreign

companies should have sufficient management know how, strong R&D and product development capacity, independent distribution systems and adequate financing. Such criteria meant to attract large MNEs into China (Xing, 1997). In recent years, under the influence of this policy, the scale of foreign investment in projects of car assembling and component manufacturing in China has been rising. Next paragraph shows some incomplete statistics about the investment of MNEs in the Chinese automotive industry in recent years.

The investment of GM to China has reached US$ 2 billion, including an engine plant, several component-manufacturing factories, the Buick car project and a research center in Shanghai (*China Daily, Business Weekly* June.28-July.4, 1999). Until 1999, Toyota has invested 28 component manufacturers in China (Qin, 1999). Recently its submission for establishing a 50/50 joint venture valued at US$ 1 billion with TAIC for making 1.3-liter small car has been approved by the Chinese central government. Ford has invested nearly 300 million in China, including five component joint ventures, one engine joint venture and one vehicle assembly plant (*China Daily, Business Weekly* June.28-July.4, 1999). Delphi had set up 15 component manufacturers in China between 1995 to 1998, including 11 joint ventures and 4 wholly owned plants with total investment of US$ 350 million. In 1999, Eaton Corporation of the U.S. established a joint venture in East China with an estimated investment of up to US$80 million. In 1998, Teksid, a subsidiary of Fiat Group set up an equal equity joint venture of US$80 million with Chinese partners making engine block (*China Daily*, June 20, 19998).

In the face of such a strong investment by MNEs in the Chinese automotive industry, both Australian managers and the Chinese managers interviewed in this survey considered that Australian automotive companies are unlikely to compete with MNEs in this sector.

According to a senior manager from Australian Federation of Automotive Products Manufacture, Australian companies are competitive in developing low volume, low cost and fast to market components for niche markets. Such a special competitive advantage often leads to a supplementary role in foreign countries. It is not in line with the tradition and competitive advantage of the Australian automotive industry to compete with major MNEs for large projects in China.

When asking by the author about the opportunities for the Australian automotive industry in China, the Chinese managers from SAIC group considered that the size of the Australian automotive industry is too small for seizing major projects. Given the Chinese government policy promoting the set up of large corporations, major Chinese automotive corporations like SAIC basically are looking for partners among powerful international companies. On the other hand, the competition between MNEs for entering the Chinese market is likely to induce MNEs offering attractive packages for the incorporation. These packages such as substantial capital investment, technology transfer, and export deals are normally beyond the capability that the Australian automotive industry can offer.

b. Less encouragement from parent companies

It is confirmed in this survey that in response to the local component level requirement imposed by the Chinese government, MNEs invested in vehicle assembling projects in China have been actively promoting their component suppliers to set up joint ventures in China. This is very important to the profitability of these car assembling joint ventures as meeting the local component level can qualify them for tariff reduction. Many of the foreign component manufactures motivated by MNEs to invest in China are small to medium sized firms sharing same home base with the MNEs or have been suppliers to these MNEs for a long time.

For example, in an interview with the author, former Vice President of SAIC commented that the strong German team working at the Shanghai-Volkswagen project had provided effective matching services to the German component companies for establishing joint ventures with Chinese companies. This has been confirmed by the claim made by the chief representative of Volkswagen in Beijing that Volkswagen has promoted and facilitated many German and European component manufacture entering China.

This scenario can also be applied to the entry of many American, Japanese and European component manufacturers into the Chinese market. Along with the investment of Toyota in Tianjin City, north China, many affiliated component makers of the Toyota Group have signed joint venture deals with Chinese companies in and near the city. "Nippondenso plans to produce car starters and alternators. Toyoda Goset wants to make

brake hoses, Acro produce car seats and Aisin Seiki manufacture gearboxes. All the ventures are intended to supply parts to Tianjing Automotive" (EIU, April 29, 1996).

Citroen encourages its international suppliers to set up satellite joint ventures in the Wuhan enterprise zone where Dongfeng Citroen is located. Some examples of European companies lured by Citroen to Wuhan are British Bundy International, which makes fuel tubes, Pilkington, which makes windscreen, and French Hutchinson, which makes oil seats (EIU, May 27, 1996). One of the features of GM's entry into China is its strategy of establishing automotive component joint ventures ahead of major car assembling plant. Before the signing of the deal for making Buick car in Shanghai, GM's then subsidiary Delphi had already established more than 10 automotive component joint ventures in China (EIU, August 19, 1996).

In contrast to these American, European and Japanese automotive component companies, it is found in this survey that the Australian automotive industry has received very limited encouragement form their parent companies for entering the Chinese market.

According to an Austrade expert specialized in automotive component trade, the Australian automotive component industry is mainly composed of about 200 manufacturers, of which the top 30 companies account for 85% of the production value and 77% export sales. There is a high foreign ownership of these 200 manufacturers. International marketing of these Australia based foreign subsidiaries is closely related to

the global strategy of their parent companies. Many parent companies or foreign partners of these Australian subsidiaries have substantial investment in China.

In an interview with the author, the director of Australian Automotive Intelligence commented that the role played by foreign subsidiaries based in Australia differs significantly. The subsidiaries with an American home base tend to be limited in size and business activities in Australia. Many of these companies have a simpler manufacturing role but more trading orientated. Therefore it is unrealistic to expect this type of foreign subsidiaries to be active in developing business in China. Rather, there are examples that these Australian subsidiaries are importing components made from the joint ventures invested by their parent company in China. For example, Ford Headquarter arranges Ford Australia to import windscreen from a joint venture in China between Ford, Pilkington and a Chinese partner, even at the cost of reducing the production of windscreen in the subsidiary in Australia.

It is also commented by the director that some European MNEs that have built a parallel structure internationally may encourage their Australian subsidiary to become a regional headquarter in Asia Pacific region. These subsidiaries have high autonomy and have developed business scale and technology for making differentiated products. This point has been confirmed in the *Automotive Industry* (Industry Commission, 1997: F8) that companies of European background such as Bobert Bosch Australia, Hella Australia have developed themselves as regional center, BTR Nylex, Britax Rainsford and ROH have

developed substantial expertise in a particular area that may not be replicated elsewhere in the group.

Even though these Australia based foreign subsidiaries have established their position within the group in the Asia Pacific region; most of them are still unable to actively participate into the project in China invested by their parent company. Following is the list based on the author's investigation showing that those large Australian automotive subsidiaries had very limited role or without substantial involvement in the China project invested by their parent company or foreign partner.

Table3: Foreign subsidiaries based in Australia have no substantial involvement in China

Holden	Ford	Toyota	Mitsubishi
Bosch	Delphi	Unidrive	BTR
VDO	Fujitsu Ten	Pilkington	Denso
Dana	Bundy Tubing	Johnson Control	

Authors survey, May-July, 1999.

Such a situation has also been confirmed by the questionnaire survey of this research. More than 90% of the Australia based foreign subsidiaries which participated in this survey indicated that the Chinese market taken by the parent company or other companies within the group was the most significant factor preventing them from entering into the Chinese market.

It is also found in this survey that the percentage of Australian indigenous companies involved in direct investment and export to China, or has tried to do so, is much higher than that of the foreign subsidiaries. For example, Air International, and Suspension Component Australia are the two most successful Australian automotive component companies investing in China, both of them are indigenous Australian companies. Among major Australia based foreign subsidiaries, only Hella Australia has set up a joint venture in China. The contrast in attitude and activities between foreign subsidiaries and Australian indigenous companies in developing business in China should be regarded as evidence showing the restrictions imposed on Australian subsidiaries by their parent companies in the entry into the Chinese market.

c. Unfamiliar with ways of doing business in China

Though the major foreign funded assemblers in China claim that the local content level has reached high level, many of these locally made components are still made with imported parts. During the field study in Shanghai, China, many Chinese managers and engineers emphasized that China needs to build its secondary and third tier automotive parts industry. These Chinese managers considered that opportunities were there for foreign automotive component companies to invest in this sector, and these opportunities are particularly suitable for small and independent foreign companies.

Many of the local companies involved in this segment are small firms and desperately in need of advanced technology. Given that the government is promoting concentration of

the industry and the Chinese automotive industry is increasingly subjected to international competition, a large number of these companies would eventually vanish. Currently, the competition between these companies in establishing a stable relationship with major automotive company for supplying components is fierce. For many of these firms ability to supply products to major automotive companies means survival. In order to secure the opportunities these firms are very keen to access advanced technology and willing to team up with foreign companies.

However, the risk for foreign companies incorporating with these firms is considered high. Many of local firms in this sector are small and collectively owned. They have weak connections with the government. Some of which might be troubled with redundant workers, high debts, poor management and poor infrastructure. But there are numerous examples of rapid expansion of business scale in this sector, provided that these firms can access to quality management and advanced technology. By setting up joint venture with this type of foreign company, it is possible to set up a relatively stable relationship for supplying components to local carmakers or major component makers.

One of the basic conditions for foreign investors to be successful in this segment is that they have to understand how to do business in China. Without the capability of collecting and analyzing the information concerned and without the knowledge and skill in handling projects in this sector, it will be very difficult for foreign investors to be successful in this sector. This is the reason why many successful projects in this sector are invested and managed by business people from Hong Kong and Taiwan.

Historically, Australian automotive industry has no substantial connections with the Chinese market and is unfamiliar with the Chinese political, economic and cultural environment. The protection of the Chinese market and the transition of the Chinese economy from a planned economy towards market economy have produced obstacles for Australian automotive companies to enter. The managers from Hella Australia and Suspension Component Australia who run the joint ventures in Shanghai commented in the interviews that after 20 years of the reform in Australia, there are many Australian automotive component manufacturers should be competitive enough to enter the Chinese market. But many of these prospective companies lack the experience and knowledge of doing business in China. These Australian managers commented that this is one of the most significant impediments preventing Australian automotive companies from entering the Chinese market.

This factor has also been confirmed in the survey of this study. Many of the Australian companies that participated in the survey considered the Chinese market as a difficult market to do business with. The reasons range from cultural difference, lack of transparency and clear-cut legal framework, poor infrastructure to inferior management. Because of the difficulties and risks associated in entering China, the majority of the Australian companies that replied in the questionnaire survey indicated the Chinese market was not a priority for them. They were still focusing at traditional markets in America, Europe, Japan and Southeast Asia.

6.1.2 Contributing factors to the successful companies

During the field study in China, the author had two interviews with the Australian managers working at the joint ventures invested by Suspension Component Australia and Hella Australia in Shanghai. Also the author had an interview with the Manager Director of Suspension Component Australia in Melbourne. In the questionnaire survey, another large Australian owned automotive component company indicated the factors contributing to its export to China.

Though the number of these companies that have successfully entered the Chinese market is limited, their experience still stands for the comparative and competitive advantages that enable Australian automotive companies to enter the Chinese market. Basically these Australian managers identified these advantages as:

First, the Australian automotive industry can offer advanced technology that is urgently needed in China. Suspension Component Australia (SCA) has a stabilizer bar manufacturing joint venture with SAIC in Shanghai, China. SCA designed the joint venture's state-of-the-art high volume manufacturing facility, which has won the acclaim of major international automotive representatives. The joint venture has already captured a major share of the Chinese market for its products. Hella Australia has established itself as headquarter for the group in Asia Pacific region and the company maintains its own research and development departments and laboratory. The capability of the company in

product development made it confident that it could benefit in the long run by investing in a joint venture in China even though the competition is tough.

Second, the management of these Australian companies has attached a great importance to the potential of the Chinese market. They are fully aware of the importance of being able to exploit foreign market. Before entering the Chinese market, the management of these companies has accumulated rich experience in doing business in Southeast Asian countries such as the Philippines and Thailand. These companies are able to take advantage of multicultural conditions in Australia and employ Chinese descendants or working with Hong Kong consulting firms to seize opportunities in China.

Third, timing is important. In the face of strong competition among international companies in the Chinese market, the earlier entry into the market can have a decisive influence upon the performance among foreign investors. The early entry can enable foreign companies to team up with major local corporations that have large market coverage and strong support from the government. The Managing Director of SCA said that the company was able to make decision ahead of large international companies. This helped them to set up a joint venture with the powerful local partner- the SAIC group. The combination of SCA technology with the scale and market coverage of SAIC has laid a foundation for the success of the project. Other contributing factors that were mentioned in the interview and questionnaire survey were the growing demand in China; the capability of putting adequate resources into the Chinese market; and the availability of professionals of Chinese descendants in Australia.

6.2 The export and investment of Australian food manufacturers in China

150 questionnaires were sent in this survey. Out of the 150 questionnaires, 15 were returned due to the change of address of companies. Within the 135 effective questionnaires, 23 were completed and returned. The ratio of response was 18%. Moreover, the author conducted three interviews with senior level managers of Australian food manufacturers who are in charge of the Chinese market. Following are the major findings.

6.2.1 General findings

The completed and returned questionnaires have shown a higher percentage of Australian food processing companies having invested or exported to China than the automotive industry. From the 23 companies replied, 15 were exporting to China. Out of these 15 companies, three have established wholly owned operations and another three have set up joint ventures in China. The following table and charts classify the activities of these 15 companies in China according to the criteria of export, direct investment, size, ownership and etc.

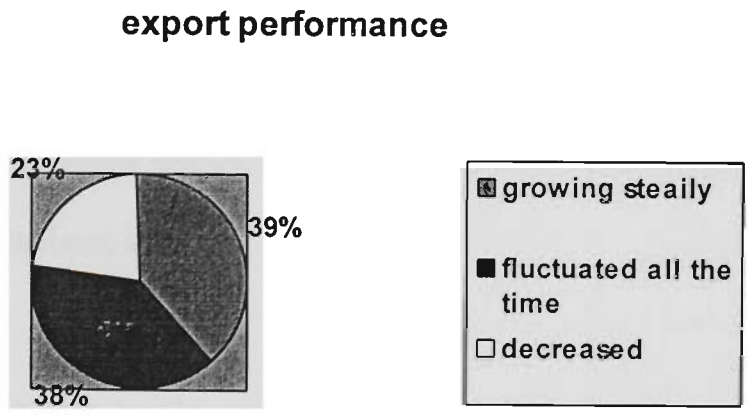
Table 4: The size and ownership of the Australian companies exporting to China

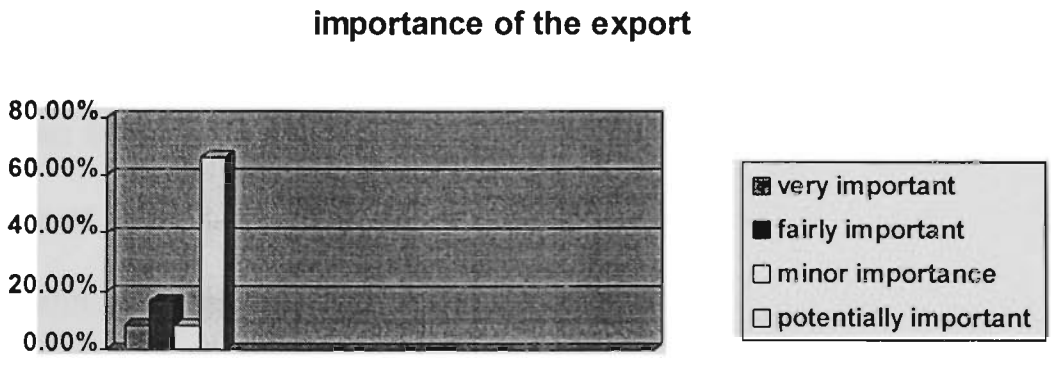
Activities	Number of companies	Company ownership and size							
		Australian owned				Foreign subsidiaries			
		Less 100	100-500	500-1000	1000 over	Less 100	100-500	500-1000	1000 over
Direct export to China from Australia	15	5	2	No	4	no	1	No	3
Trading company appointed for export	9	4	2	No	2	no	no	No	1
Set up production in China	5	no	no	No	2	no	1	No	2
Set up representative office in China	7	4	No	No	2	no	no	No	1

Source: author's survey, July-Aug, 1999.

Table 4 clearly indicates that the Australian indigenous companies are more active in exporting or investing in China than foreign subsidiaries based in Australia. It was also found that the majority of indigenous companies exported to China through trading companies, and had a tendency of setting up representative offices in China. The companies that had set up production facilities in China were mainly large companies except for a medium-size Australia based foreign subsidiary and a small indigenous company. Among the 13 companies exporting to China, 5 companies indicated that their export grew steadily; 5 had a fluctuated situation all the time, and 3 had a decreased export.

Charts 1-3: food export to China





Source: author's survey, July-August, 1999.

8 companies ranked their export to China as potentially important; one company indicated the export as very important; two companies considered it as fairly important; and one company suggested it of minor importance. Seven companies mainly exported highly transformed products to China; three companies exported semi processed products; one company mainly exported raw material; and three companies exported the mixture of the products listed above.

6.2.2 Contributing factors to the export and direct investment of Australian food processing companies in China

This survey has found that in comparison to the Australian automotive industry a fairly large number of companies are actively involved with various types of business activities in China, such as export, setting of representative office and direct investment. Basically the contributing factors to their entry into the Chinese market identified by these companies in the survey are as follow.

a. Competitive quality and price

Australia has favorable natural conditions for producing agricultural products. There are many kinds of agricultural products produced in Australia not only good in quality but also competitive in price in comparison to the Chinese agricultural products. These products include wheat, dairy products, sugar, meat, fruit and many types of seafood. In interviews with the author, Chinese managers from food manufacturers in Shanghai

revealed that the trend of importing milk powder from Australia and New Zealand for industrial use in China has been growing strongly in recent years. The demand for Australian seafood and fruits is high. During the field study in Shanghai, the author visited 10 supermarkets of different groups and sizes. It was found that Australian dairy products such as cheese and butter had dominated the market and Australian wine were sold side by side with French and Italian wines. According to an Australian manager working in China, if China reduces the tariff, it will be cheaper to import sugar from Australia than purchase locally. It was mentioned in the interviews by the Chinese managers that Chinese breweries import average 500 to 600 thousand tons of wheat from Australia for making beer in recent years. Table 5 indicates Australia's export of food products to China in recent years.

In the survey, among the 15 exporting companies to China, 7% export raw material, and another 20% companies export mixed products, including raw material. Three of these companies considered the competitive price of their products as a major factor underpinning their successful export to China, and another five companies indicate that this factor is of moderate significance to the entry into the Chinese market.

b. Large food manufacturers leading the export and investment in China

Thanks to the favorable conditions in Australia for developing agriculture and food-processing industries, the agri-food industry makes up the largest industry within the manufacturing sector in Australia. It contributes a fifth of total turnover in the Australian

manufacturing industries (BIE, 1996: 10). Between the period from 1988-89 to 1992-93, the industry was composed of 3300 establishments, of which 90% were small enterprises with less than 100 employees. Even though the industry is diverse in size, the concentration of the industry is high. In 1991-92, the 20 largest agri-food firms had 268 establishments in the industry accounted for just under half of the industry turnover (BIE, 1996: 12). The table prepared by DIST provides a list of top 20 Australian food processing companies with their turnover and ownership.

Table 5: Australian food and living animals export to China (A$ million)

Division	12 months ended Dec 1996	12 months ended Dec 1997	12 months ended Dec 1998	12 months ended Dec 1999
Live animals	4	2	11	11
Meat and meat preparation	26	30	33	32
Dairy products and birds eggs	10	11	13	22
Fishery	27	84	126	79
Cereals and cereal preparation	2	4	206	Figure not available
Vegetable and fruits	23	11	8	5
Sugar, sugar preparation and honey	102	25	2	10
Coffee, tea, cocoa, spices and manufactures thereof	4	4	2	2
Feeding stuff for animals	4	5	10	4
Miscellaneous	1	2	3	3
Total	204	177	414	169

Source: ABS. international merchandise trade 5422.0 Dec quarter 1997-March quarter 2000.

It was found in the survey that those large Australian companies whether foreign subsidiary or Australian owned have a higher tendency to invest and export to China. Among the 15 companies replied in this survey exporting to China, 7 are large companies having employees more than 1000. The contributing factors to their entry into the Chinese market were ranging from injecting adequate investment, technological advantage, experience in doing business in Asia Pacific region, to competitive price and high product quality.

These large Australian companies have close relations with MNEs, and are able to take part in the networks organized by MNEs for doing business in the Chinese market. In this survey, three of these large companies commented that the establishment of production facilities in China by their own company, or parent company, or major customers was the major significant factor contributing to their export to China. Another five companies considered this factor as moderate significance for their exporting to China. Also, four out of the seven companies that had set up production facilities in China indicated that international companies operating in China using their products was the major factor promoting them to set up a plant in China.

Table 6: Major food and beverage companies in Australia, 1994-95

Company	Australian Turnover A$ m	Export earnings A$ m	Ownership
Coca-Cola Amatil	2239	Nil	Australia (60%) and US(40%)
Goodman Fielder	2100	121	Australia (75%) and NZ (20%)
Nestle	1700	250	Switzerland
Carlton &United Breweries	1572	50	Australia
Lion Nathan Australia	1288	10	New Zealand
Pacific Brands Food Group	1064	Nil	Various
George Weston Foods	1038	15	UK (78%) and Australia (22%)
National Foods	1027	29	Australia
Bonlac Foods	991	427	Australia
Cadbury Schweppes	909	28	UK
Ingham's Enterprises	825	Nil	Australia
Murray Goulburn Co-operative Co.	805	485	Australia
Unifoods	700+	22	UK/Holland
Effem Foods	692	147	US
Australian Co-operative Foods	625	25	Australia
Kraft Foods	583	92	US
QUF industries	561	Nil	Australia
Arnotts Biscuits	546	23	US (61%) and Australia (29%)
CSR	425	600	Australia
Kellogg (Australia)	390	50	US

Source: DIST (1995b)

Some of the joint ventures invested by Australian large companies are of national influence in China, such as the chocolate plant invested by Cadbury in Beijing and Forster Brewery in Shanghai. In an interview with the author, a senior manager from Cadbury in charge of the confectionery joint venture in China commented that Cadbury Australia has taken full responsibility on behalf of the parent company in the Chinese market. It was emphasized by this manager that the position of Cadbury Australia as headquarter for the group in the Asia Pacific region, and its expertise in R&D, experience in doing business in Asia have contributed to a total control over the joint venture in China. The responsibilities undertaken include feasibility study, selection of local partner, plant management, technological support, machinery maintenance, product marketing, and business expansion in China.

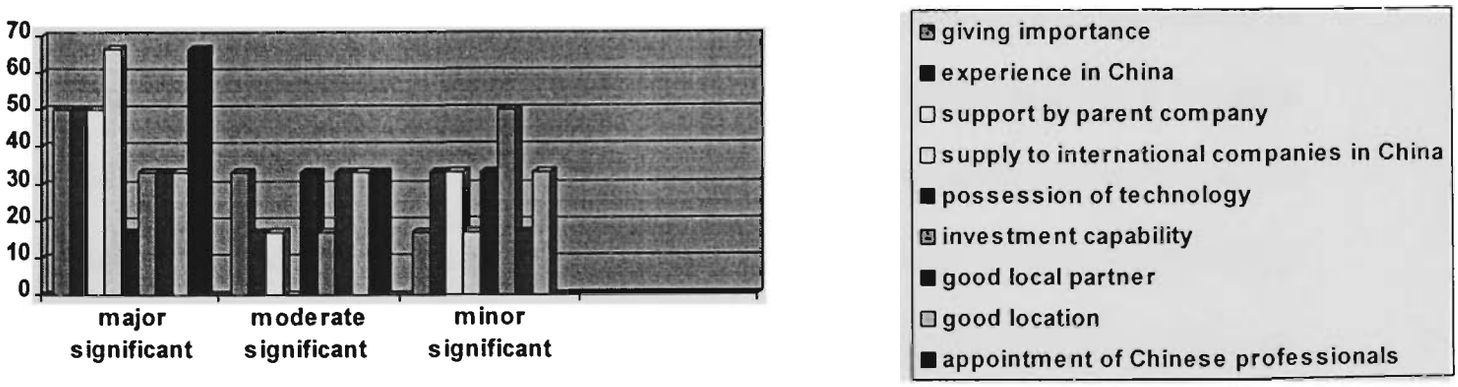
c. Other factors

Four of the companies investing in China suggested that their technical capability for developing products suitable to the Chinese market is one of the major reasons underpinning their direct investment in China.

The accumulation of experience in doing business in China has contributed significantly to the successful operation of the Australian companies in China. Multicultural environment in Australia and appointment of professionals with Chinese ethnic background are directly connected to this particular competitive advantage. In this survey, 30% of the companies exporting to China and two third of the companies

investing in China admitted that using Chinese ethnic professionals was a major factor contributing to their export and successful operation in China. Specifically this competitive advantage had helped Australian companies in selecting favorable local partners and locations for the investment. There are some trading companies based in Hong Kong and Australia having taken great role in the export of Australian food products to China. The number of the Australian companies exporting to China via trading companies is high, especially the small and medium companies. These trading companies are very experienced with the trade between Australia and China. Their services provide a solution to smaller Australian companies avoiding high marketing costs for exporting to China. In addition, more than 50% of the Australian companies in this survey considered that the growing demand in China was a moderate contributing factor to their export, while one company considered it as a major significant factor.

Chart 4. Contributing factors to direct investment in China



Source: authors' survey, July-August, 1999

6.2.3 Factors preventing Australian companies from entering the Chinese market.

a. The price and the tariff

Even though the standard of living in China has improved rapidly in the last two decades, the purchasing power of ordinary Chinese households is still low. It was commented in interviews with the experts from the Australian food processing industry that the price factor had been one of the major factors affecting the export of Australian processed food products to China. Several companies also indicated in the questionnaire survey that the high price of their products had prevented them from exporting to the Chinese market.

In the field study in Shanghai, China, the author collected the retailing prices of a variety of confectioneries and bakery products made by the joint ventures invested by MNEs based in China. Some of these products share same brand name, same packing with the products made or sold in Australia. After comparison it was found that the price difference was small. For example, an 80g Dove chocolate bar made by joint venture of Mars in Beijing was sold 10 yuan in Shanghai. Similar chocolate bar made in Australia sold A$1.40 in Melbourne. 120g chocolate sandwich cookies made by joint venture of Danone was sold 2.70 yuan in Shanghai. The similar Australian product 200g *TimTam* sold A$2.05 in Melbourne. According to the exchange rate that one Australian dollar was for 5.5 Chinese yuan at the time, the chocolate was sold cheaper in Melbourne while biscuits was cheaper in Shanghai. However, if these Australian products export to China,

the transportation cost and 30-50% tariff will make the retailing prices of these products too high to be acceptable to most of the Chinese consumers.

This reason explains why foreign companies are likely to establish production facilities inside China. FFEs normally produce products that are of high local demand and difficult to transport and store. Currently these products range from beverage, beer, confectionery, and bakery to some types of dairy products, such as milk powder and ice cream. The extensive FDI in these facilities makes the export of those manufactured food products from Australia to China even more difficult.

b. International competition in the Chinese market

FFEs involved in the Chinese food processing industry, especially those joint ventures invested by MNEs, have an advantageous position in supplying the Chinese market. By benefiting from tax reductions, avoiding tariff and transportation cost and using cheaper local labor, these joint ventures can offset the various cost involved with initiating production in China and maintain a competitive price for their locally made products. With the increase of efficiency and market coverage these joint ventures could expect even low cost in production in long run. Further, as being close to the consumer, these FFEs are able to take advantage of effective marketing means to promote their products locally. In addition, major MNEs are committed in establishing relationships with government departments and other authoritarian institutions, which are very important conditions for seeking the dominance in the Chinese market. All of these factors impose

challenges to the Australian food processing companies, particularly to small and medium sized companies when exporting products from Australia to the Chinese market.

Secondly, in the niche market sector, Australian products have to compete with sophisticated products provided by famous international suppliers from advanced industrialized countries. For example, Australian products with high value added sector have to compete with French and Italian wine, Swiss and Dutch baby formula, Swiss and Italian chocolate, and Danish and Dutch bakeries. Several companies in this survey indicated that international competition in the Chinese market had affected their export and investment in China.

Third, due to the massive FDI into the Chinese market, it is increasingly difficult for Australian companies especially small and medium firms to seek good partners in strategic locations in China. Also, the excessive investment both from overseas and domestic investors in the food processing industry in China has led to a severe oversupply. This makes the Chinese market more volatile and risky. This further reduces the chance of Australian companies entering the market through direct investment. For example, there are 6 companies in this survey indicated that they had tried to conduct direct investment in China but failed. Difficulty in finding a local partner was the most direct reason attributed to the failure. These Australian companies were not satisfied with Chinese counterparts who normally troubled with high debts, too many redundant employees, and poor infrastructures and management. The conditions raised by the Chinese firms for the cooperation were seen as unrealistic by the Australian companies,

which included major investment, re-employ redundant workers and introduction of the latest technology.

c. Some Australian companies are not used in doing business in China

As the Chinese economy is in the process of transition from a planned economy towards market economy, the Chinese market has been unique. As the Chinese manufacturing, distribution and retailing systems used to be controlled by the State, the Chinese governments, both at the central and local levels still have great power in influencing the operation and development of the Chinese food processing industry. It is often the case that Australian companies not only have to find a business partner but also have to seek permission from the government for developing business in China. The lack of a clear-cut legal framework, lack of transparency in the Chinese economy, lack of market orientated distribution system and fragmentation of the Chinese market has increased difficulties for the Australian companies to enter the market.

Under such a situation, as indicated by an Australian manager, a correct strategy for developing project in China would be the most important element to the success. This strategy should be based on a thorough understanding of the roles played by the foreign investor and local partner in the joint venture. Normally, foreign companies from industrialized nations investing in China should take the dominant position in production management, technology development, and marketing, as western companies normally possess rich expertise in these areas. The most important value that local company is

expected to input is the connection with various government departments and business organizations. The quality of the matching of the expertise and advantages between foreign and local partners often determines the future of the joint venture.

Finding business partners or business opportunities in China is a complicated process. It needs commitment, patience, resources and intensive research. Often Australian companies, especially small and medium companies are not prepared to be so patient and their resources are not sufficient enough to facilitate them to go through such a long and costly process. Therefore, indicated in the questionnaire survey the most common reason for companies not being able to enter the Chinese market was the difficulties in finding a good local partner.

For the Australian companies that have direct investment in China, the major factors that prevented them from further expansion are the inconsistency of the quality of local supplied material, division of the local market, chaotic local distribution system.

It was found that 70% of the companies in this survey considered that the government export-promoting schemes had had no effect on their export to China. Also it is of very low level of companies seeking advice from consultant institutions and government departments, such as Austrade.

Table7: Factors preventing the Australian companies from entering China

Indicated by the eight participated Australian companies that do not export or invest in China in this survey

Factors	Number of companies and factor significance		
	Major significance	Moderate significance	Minor significance
Business priority is not in China	5	2	1
Price is too high for the Chinese market	3	1	2
Not familiar with the Chinese market	4	2	2
Limitation in capital resources	2	2	4
Incompatible of the product to the Chinese market	2	2	4
International competition is too strong in the Chinese market	1	3	4
Tariff and other trading barrier are too high	1		7

Source: author survey, July-August, 1999

Table 8: Factors preventing the Australian companies from expanding in China

Indicated by the fifteen participated Australian companies that export or invest in China in this survey

Factors	Number of companies and factor significance		
	Major significance	Moderate significance	Minor significance
Tariff and other trade barrier are too high	6	3	6
Limited export volume does not justify further investment	4		11
Difficulty in collecting sales on credit	2	2	11
Lack of feedback from the market due to relying on trading company	2	4	9
International companies competing in the Chinese market		7	8
Difficult to find a good local partner	6	2	7
Uncertain about the future of the Chinese market	1	7	7

Source: author survey, July-August, 1999

Chapter Seven

Conclusion

Australian politicians, scholars and government departments often mention in articles and various occasions that Australia should and could take an active role in the economic development in East Asia. In addition, when the Chinese President Jiang Zemin and Premier Zhu Rongji visited Australia in recently, one of the keynotes of their official speeches made during the visit was to strengthen the economic relationship by taking advantage of a complementary economic conditions between Australia and China.

The intention and rationale for these judgements among governments and scholars in Australia and China might be different, but there are some common points in these judgements. To a large extent, these judgements (Garnaut, 1988 and EAAU, 1992) are based on the belief that the difference between Australia and China in terms of natural endowments and competitive advantages laid foundation for a complementary economic relationship. As a country rich in natural resources, Australia can supply commodities such as mining and agricultural products to China where the demand for these products increases as a result of expansion of the economy. Further, as a developed nation, Australia could export manufactured products and transfer technology to China as the standard of living in China improves and the country develops a demand condition similar to that of in Australia. In return, China can export labor-intensive products to

Australia such as clothing and footwear and manufactured products that are suitable for mass production.

There is no doubt that this type of trade between Australia and China has been growing strongly in the last twenty years. However, the development of the trade of manufactured products between Australia and China and the direct investment of Australian manufacturing companies in China in the same period reveals that factors influencing the economic relations between Australia and China are complicated. It was found in this survey that the rise of the Chinese economy internationally and the strategic adjustments made by MNEs for the Chinese market have functioned fundamentally to the formation of the economic relationships between the automotive and food processing industries in Australia and China.

7.1. The rising of a triangular relationship

The open-door policy and other reform policies deployed by the Chinese government in the last two decades have a clear intention to integrate the Chinese economy with the world economy. This strategic move by the Chinese government is based on the calculation that by opening the domestic market, China can access resources such as foreign capital, technology and international trade opportunities. These resources in combination with the market potential and cheap labor are expected to facilitate fast economic growth, strong export, and restructuring of the Chinese manufacturing industries. The Chinese government has intervened heavily in the implementation of the open-door policy. By providing incentives for inward FDI, keeping high tariffs and reserving central government approve

on strategic projects, the Chinese government has been aiming to attract more FDI into China and to ensure these FDI bring in advanced technology and export opportunities. Because of these policies, FDI has become a major channel through which foreign companies are able to get involved with the Chinese economic development actively and expand their local market shares (Huang, 1998).

According to UN publications (UN, 1998), FDI led predominately by MNEs from advanced industrialized nations has become a major medium for capital movement and an important tool of market expansion internationally after World War II. According to Dunning's (1996) "investment path theory", there are basically three types of FDI associated with countries in five development stages. The FDI conducted by MNEs from advanced industrialized nations are mainly for seeking 'strategic assets' and efficiency. As the reforms in China have upgraded the strategic importance of the Chinese economy and as the Chinese government encourages the inflow of FDI, great amount of FDI have been put into the Chinese economy.

The secondary information collected in this study has confirmed that the FDI conducted by the MNEs in China are more likely to meet the requirement raised by the Chinese government. Large MNEs often offer huge capital investment, substantial technology transfer, and export deals to Chinese partners. There are even examples of MNEs providing substantial assistance to their Chinese partners in R&D. The rationale for this type of investments made by MNEs in China is basically to establish the control over the Chinese market and cultivate the facilities in China becoming export base in the future.

The increase of MNE investment in China has induced profound impacts upon smaller international companies operating in China or willing to invest in China. In terms of the consequences to the Australian food processing and automotive industry, changes are happening in following areas:

First, because of the strategic importance of the Chinese market, the control over the investment in China by MNEs is likely to be excised from the headquarters of these MNEs in home country. This situation has not only diminished the function of Australia based foreign subsidiaries as a springboard for these MNES in accessing China but has also influenced the configuration of the strategies and structures of these MNEs in the Asia Pacific region. It was found in this study that in the automotive sector, the Chinese market is likely to be excluded from the Australian subsidiaries. The involvement of the Australia based food-processing foreign subsidiaries in the Chinese market is mixed.

Second, the investment made by MNEs in China has led to a direct competition between Australian firms with international companies in the Chinese market. As the Chinese government policy promotes MNEs incorporating with major local corporations, MNEs are given priority in selecting local partners. Consequently, the joint ventures of this type are likely to establish monopolistic position in the Chinese market. The trend of MNEs invested joint ventures dominating in the Chinese market has produced an exclusive effect upon smaller foreign investors. Primarily smaller foreign companies are restricted to access prospective local partners and major local markets. It is likely that these small foreign companies are constrained to only deal with local firms that have poor infrastructure and

inferior management. Furthermore, the massive technology transfer and capital investment made by MNEs has increased the expectations of Chinese firms from foreign companies. This has further disadvantaged smaller companies that normally have limited financial and technological conditions. Besides, smaller foreign companies have to cope with risks in doing business in China arising from the market division, excessive government intervention, and ambiguous legal framework.

Third, the inflow of FDI into China, in particular the investment of MNEs, has significantly affected the pattern of China's international trade. Nearly half of the Chinese foreign trade is carried out by FFEs based in China, which import and export significant amount of components, raw material, semi-processed products and machinery through networks centered by MNEs. The increase in the number of Chinese firms joining the intra-industry trade systems involved with MNEs has kept the Australian companies racing against the suppliers from other industrialized countries for trade with the Chinese firms. It was found in the survey that the Australian automotive industry is disadvantaged to these opportunities in comparison with the suppliers sharing same nationality with major MNEs that have substantial investment in China.

In summary, under the process of globalization, the integration of the Chinese economy with the world economy has changed the economic relation between Australia and China significantly. This integration has extended the economic relationship between Australia and China further into international arena. It has actually produced triangular relationships between Australia, China, and MNEs from advanced industrialized countries. These

relationships have a great influence upon the performance of Australian manufacturing industries in the Chinese market. It has been proven in this study that in many cases the entry of Australian companies into the Chinese market is interrupted due to the involvement of MNEs in China.

7.2 The implication of "product life cycle hypothesis"

The author considers that the "product life cycle hypothesis" developed by Vernon (1996) in the 1960s and the modification to this hypothesis he made in an article published in 1996, are both relevant in explaining the formation and changing of the triangular relationship between Australia, China, and MNEs.

The key elements of Vernon's "product life cycle hypothesis" developed in the 1960s are that the innovative products are firstly developed in advanced industrialized countries as demand condition and R&D capabilities in these countries are promising. Then, these products are further advanced and matured in these countries. By this time similar demand for the products will be developed in countries of lower development stages. In order to meet the demand, take advantage of the cheaper labor, and react to competitors, innovative companies from advanced industrialized nations are likely to take FDI in the prospective foreign countries.

In an article published in 1996, Vernon (1996) made modifications to the "product life cycle hypothesis". The main points of the modification are that due to the convergence of

demand conditions among industrialized countries, and the extensive deployment of FDI worldwide for market expansion, the "product life cycle hypothesis" has a diminishing role in explaining the current FDI and MNE activities. In this paper Vernon implicitly suggested that MNEs which are equipped with 'strong scanning power' would affect the technology transfer conducted by smaller companies. However, Vernon still considers the principles of the hypothesis still hold true for developing nations seeking technology from advanced countries.

This study has found that both of the concepts made by Vernon in the 1960s and 1996 are relevant to some extent to the explanation of the investment and trade of Australian automotive and food processing companies to China. First, as a developed nation, the Australian industries are more sophisticated in many ways than the Chinese automotive and food processing industries. Equipped with better technology and management expertise, Australian companies in these two industries should find direct investment or export opportunities in the Chinese market. It was confirmed in the survey that all the Australian companies which had already invested in China considered that their advanced technology formed a foundation for the investment. Similarly the companies had already exported to China considered that the technological advantage was one of the major factors contributing to the successful of entry into the Chinese market.

However, this study has found that the Australian automotive and food processing industries indeed have been disadvantaged due to the strong involvement of other MNEs in China. As discussed previously, in order to meet their strategic interests, MNEs

selectively exclude or include Australian subsidiaries with their investment in China. In addition, the substantial transfer of advanced technology from MNEs to the Chinese partners has reduced the technological gap between Australian and Chinese companies. Even though many Australian companies have the technology that is much needed in China, it is still difficult for these Australian companies to gain access to appropriate local partners. Such a situation justifies the 'strong scanning power' of MNEs to impose strong influence on smaller companies in investing in developing nations.

However, this study does not conclude that smaller Australian companies are being deprived of opportunities in exporting or investing in China. In the interviews, all the managers from successful Australian companies exporting or investing in China expressed strongly that there are still many opportunities available in China suitable for Australian small-medium companies. According to these managers, after nearly 20 years of various microeconomic reforms in Australia, the cost structure and R&D capability of many Australian companies are competitive enough to produce quality products for the Chinese market. However, all of these Australian managers have pointed out that these conditions are not sufficient enough. Often, the knowledge and expertise of being able to do business in China is the key factor attributing to the success of operation in China. This kind of factors include the capability in collecting and assessing information, and dealing with Chinese managers, companies and the governments. The importance of these 'soft' factors to the success of operation in China has been highly appreciated in the survey of this study.

Therefore, the conclusion of the study on "product life cycle hypothesis" is that the demand and technological gap between developed nation and developing nation still provides a foundation for the transfer of production from advanced industrialized countries to developing countries. However, such a transfer is increasingly influenced by large MNEs activities. Though the interference of large MNEs' activities has indeed reduced the scope and put pressures on smaller companies in securing opportunities in developing countries, it has not eliminated these opportunities at all. Under the fierce international competition, in addition to the factors such as technology condition, R&D capability and cost structure, the 'soft factors' are increasingly playing major roles in helping smaller companies from advanced countries to transfer their production and technology to developing countries. These 'soft factors' are primarily as the capability of company management in doing international business, ability in collecting and accessing information, and understanding of doing business in developing countries. In addition, in order to meet the challenges and seize the opportunities generated from globalization, there is a need for countries like Australia to have a close cooperation between government and industries and within industries. This point will be discussed in detail in the section of policy suggestions.

7.3 The comparative and competitive advantages in the era of globalization

This study has shown that under the process of globalization, the Australian manufacturing industries are increasingly subjected to international competition. In fact, a

major portion of the competition is presented in winning over the market share in developing countries.

The performance of the Australian food processing and automotive industry in the Chinese market suggest that the comparative and competitive advantages of these industries in Australia are the key factors which determine the performance of Australian manufacturing industries in the international arena.

In the case of the Australian automotive industry, the conditions in Australia for developing automotive industry are not favorable. Primarily, the small domestic market is not suitable for the development of automotive industry which require large economies of scale and support from related industries. Historically, the establishment of the automotive industry in Australia was largely due to the high tariff and protective policies of the Australian government. In order to take over the Australian market, foreign carmakers and component companies were lured to enter Australia. As a result, the Australian automotive industry is highly domestic orientated with a significant foreign ownership. Even though there are some automotive component companies in Australia very successful in developing differentiated products, a large number of companies are still dependent on imported technology (IC, 1997).

In contrast, there are significant comparative advantages available in Australia for developing food-processing industry. The number and size of Australian food processing companies are much larger than that of the Australian automotive industry. Some large

food processing companies in Australia, either foreign subsidiaries or indigenous, have built up significant scale with strong financial and R&D capabilities.

Due to the difference in comparative advantages, the competitive advantages developed by these two industries are different. The most outstanding competitive advantages developed by the Australian automotive industry is that it can innovate and produce high quality components with small volume, short time span, and low financial budget. Several Australian managers interviewed in this study emphasized that the industry is defining its position internationally as a supplementary force to other MNEs. The focus of the Australian automotive industry in international area is aimed at adjacent regions where exists weaker automotive industries such as Thailand, Indonesia, Malaysia and India.

As discussed previously, the competitive advantage of the Australian automotive industry is not in line with the Chinese government policy which is in favor of the entry of large MNEs. Therefore, this particular competitive advantage has not won a decent market share for the Australian automotive industry in China.

In contrast, the Australian food processing industry is built on a competitive and efficient agricultural sector. Many large food-processing companies are leading the investment in China. The coordination between Australian food processing companies and large international companies is much well developed than that of the automotive industry.

Some Australian food companies indicated in the survey of this study that they had benefited from a positive relation with international companies in the Chinese market.

According to Dunning's (1996) "investment path theory" there is a positive relation between the strategic importance of an economy and the inflow of FDI into that economy, and the involvement of that economy with the international market. The comparison between the performance of the Australian automotive industry and the food processing industry in China proves that ultimately it is the comparative and competitive advantages determine the performance of the Australian manufacturing industries.

In summary, the comparative and competitive advantages of the Australian automotive and food processing industries laid a foundation for the performance of the export and investment of the industries in the Chinese market. However, the realization of these advantages is increasingly being affected by the MNEs activities. Because of the process of globalization, there is a triangular relationship developing between Australian companies and lager MNEs and the Chinese government and firms. Australian companies will have both encouragement and restrictions from MNEs in terms of developing business opportunities in emerging markets in developing nations. The extent of encouragement or restrictions is related to the strategic importance of the Australian industries internationally or at least regionally. Those Australian industries that have significant competitive advantages and comparative advantages are likely to establish a closer and benefiting mutual relations with MNEs. These Australian companies are likely to take part into the networks centered by MNEs for developing business in developing

countries, such as China. On the opposite, those Australian industries lack of comparative and competitive advantage, are likely to be affected by the monopolistic competition conducted large MNEs in the international market. Though these Australian companies may possess some competitive advantages, the deployment of these advantages in the overseas market will be restricted due to the intervention of large MNEs. However, this situation should not be understood as those Australian companies are being deprived of opportunities. Actually this put on more conditions for those Australian companies, should they enter international market. They will have to reinforce their capability through cooperation and spend more in collecting and assessing information of foreign markets.

7.4 Policy suggestions

Currently, under the strong process of globalization, economic activities between nations are increasingly interrelated and integrated. There are signs that economic blocks formed on regional basis, such as EU, NAFTA, and ASEAN are taking great role in international and regional trade. The driving forces behind these developments are complicated. According to the theories referred in this thesis, the pursuit of the control over foreign markets by MNEs, enlarging economies of scale and sharing competitive advantages between firms, international division of labor, and transfer of production and technology between countries are the major factors contributed to the process.

As a consequence of these developments, the influence of world economic development on Australia is becoming more important and complicated than ever. For example, the massive capital investment and technology transfer made by large MNEs to the Chinese automotive industry have altered the technological conditions between the Australian and Chinese automotive industries. These changes have not only affected the investment and trade opportunities of Australian companies in China but also the position of Australian subsidiaries in Asia Pacific region. This will generate long and profound impact to the Australian automotive industry which has a high rate of foreign ownership.

It is anticipated that the economic growth in China will be still fast for the next twenty to thirty years. The market potential for automobile in China is huge. Given the importance of the economies of scale in automobile manufacturing and the trend of reduction of platforms in making vehicles and components world wide, the development of the automotive industry in China could be more competitive than complementary to the Australian counterpart. For example, Ford plans to reduce basic vehicle platforms by a third, reduce engine and transmission combinations by 30-50%, reduce horns from 33 to 3, reduce batteries from 40 to 14 (*BIG Business,* December 1996). In the future, the competition will be fierce between subsidiaries of large MNEs for the right of producing these products. Without significant adjustment and preparation, it is doubtful that the Australian automotive industry could benefit substantially from this kind of development. Things might turn out to be opposite: the joint ventures between large MNEs and Chinese firms replacing Australian based foreign subsidiaries in manufacturing components.

This situation has coincided with a major concern in the Australian industry policy debate. That is if the strong incentives provided by governments in adjacent nations have diverted FDI away from Australia and consequently undermined the development of Australian manufacturing industries. This research has confirmed that this is a pressing challenge. In addition, it has found in this study that the Australian government economic policy has not been able to work closely and efficiently with the Australian automotive and food processing industries to deal with the challenge. The majority of the companies participated in the survey indicated that they had not received valuable assistance from the government. Very few companies sought help from Austrade, which is the major government agent responsible for promoting Australian companies exporting and investing overseas. In the interviews, Australian managers expressed that the government should have done better in providing information services to Australian companies that are willing to enter the Chinese market.

The weak cooperation between the Australian government and the automotive and food processing industries in dealing with the Chinese market has partially reflected to the position of the Australian government economic policy.

One of a very popular points in the industry policy debate in Australia is that as a small nation, Australia has little leverage over major powers and it is unrealistic for Australia to adopt strategic trade policies using tariff and other policies to protect and promote targeted industries. It is in Australia's best interests to lower tariff and other trade barriers so that Australia can urge trade partners to open their markets for Australian products (Bell, 1993).

Under this approach, a variety of microeconomic reforms have been designed and implemented to facilitate the transition of the Australian manufacturing industries from a protected situation to a free trade environment. These reforms include tariff reduction, privatization of government enterprises, industry relation reforms and etc. It is expected that such competition-enhancing reforms could reduce the cost of doing business in Australia, upgrade the productivity of Australian firms and sustain the inflow of foreign investment.

However, as confirmed in this research, many important factors affecting the development of Australian manufacturing industries exist outside of the Australian market. These factors include the strategic importance of the foreign markets, large MNEs' strategy, government policy of other countries, and differences in labor and production cost between countries. It is difficult for Australian companies to sense correctly and comprehensively all the influence of these factors, especially the small and medium companies. Against such a situation critical questions should be raised. Some of the questions are: can enhanced market competition in Australia deliver necessary signal for directing Australian companies reacting to the international competition? Can domestic competition generate sufficient advantages to convince MNEs to entrust Australian subsidiaries of important roles in their global strategy?

The competition-enhancing policy might be relatively effective to the Australian food processing industry, which has the support from a competitive and efficient agricultural sector. The size of the Australian food processing industry has already developed to such an extent that the productivity gain from enhanced competition in domestic market might

facilitate the companies expanding market share overseas. However, even though the involvement of the Australian food processing industry in China is relatively deeper than that of the automotive industry, it still faces serious challenges from other international companies in the Chinese market.

Therefore, under the process of globalization, one of the most important implications to the Australian government is that it should adopt a broad view taking account of international and regional developments in forming economic policies. It should react adequately to the challenges and opportunities generated from the restructuring of manufacturing industries globally or regionally, induced by the strategic investment of large MNEs and the government policies of neighboring countries.

With regarding to the role of government in helping the development of manufacturing industries in Australia, it is sensible to compare the situation between Australia and Sweden. Sweden is the country that shares some similarities with Australia in economic factor conditions. According to Porter (1990) both countries are rich in natural resource but limited in market size and distant from major international markets. However, the development of manufacturing industry is very much different between the two countries. Sweden has developed a range of internationally competitive industries such as the transportation machinery, forest-related industries, ferrous metals and fabricated metal products and power generation. These industries have their roots in natural resources. There is a striking frequency of cooperation and joint efforts among vertically or horizontally related Swedish companies in the development of the industries. Sweden's

exports are the most concentrated in large firms, with the twenty largest MNEs accounting for more than 40% of total exports. The Swedish government has a very supportive relationship with industry, particularly the large, established Swedish MNEs. Sweden has a large state sector with the public sector employ 31% of the workforce (Porter, 1990).

Unlike many of the large Swedish companies that their establishment went back to the latter part of the 19th century (Porter, 1990), many Australian manufacturing companies were founded with foreign investment after World War II. These Australian companies are mainly for supplying the domestic market and involved with part of the value chain of the production. Many Australian subsidiaries are heavily dependent on capital investment and technology from parent company. Normally, Australian manufacturing companies have a diverse background, which can be divided into indigenous and foreign subsidiary. Among foreign subsidiaries, they still can be divided into American, European and Japanese subsidiaries. The significant difference among Australian manufacturing companies in terms of company origination, source of capital and technology, market sectors and activities have led to a poor cooperation between them. There is no significant industry cluster available in Australia. One of special features of the Australian food processing and automotive industries is that even though some companies are able to produce world competitive products, but often they have limited horizontal connections with domestic industries. For example, some most competitive Australian automotive component companies complain that the second tier suppliers in Australia are inefficient and in general Australian automotive industry depends on imported technology (IC,

1997; 77). In the case of the Australian food processing industry, the competitiveness of the industry is being affected due to the high cost of transportation in Australia and the lack of support from food-processing machinery industries and packaging industries (Acton, 1997).

Hence, it is necessary to develop an industry policy in Australia to encourage the cooperation of the manufacturing industries. Government policies should encourage the development of large firms in industry sectors where Australia has comparative and competitive advantages. Based on these large firms Australian manufacturing industries should complete the value chain in selected sectors and develop industry clusters. It is impossible for Australia to be competitive in a broad range of manufacturing industries, however, it is feasible for Australia to be competitive in a narrow range of manufacturing industries internationally.

In coordination to such a policy, the Australian government should reconfirm its commitment in developing an intimate relation with Asian countries. Currently, Korea, Thailand, and other East Asia nations are recovering from the East Asia financial turmoil, China's admission into WTO will lift the activities of trade and investment of the region to new levels. Asia will remain as a most dynamic region in terms of economic development in the world.

The integration with Asia should not be only considered as a policy for satisfying the growing demand from Asian markets, but a strategic move by Australia to develop and

consolidate its manufacturing industries. The penetration of Australian manufacturing industries into Asia should be linked with the restructuring of Australian manufacturing industries and the development of industry clusters.

Currently, many Australian industries still hold technological advantages over the counterparts in developing nations. Given the closeness to Asia and being an active member of APEC, it is logical that the most important market for Australian products, technology and investment will be in Asia. However, under the process of globalization, Australian companies will face competition from international companies in the Asian market. For example, large American, European and Japanese MNEs will further expand their investment and trade in the Chinese market when China is admitted into WTO. If Australian manufacturing industries still exist in isolation, it will be very difficult for them to expand market share substantially in China.

Australian companies and the government should work together to find common interests. Such a cooperation should reinforce the strength of Australian manufacturing industries and facilitate them to seize opportunities in international markets. In fact, there is successful example of this kind in the Australian automotive industry, the aXcess, a high tech car developed in 1998 and astonished the world, "is the result of three-year work by 130 Australian component companies and probably cost about 20 million"(*Herald Sun*, Feb 9, 1998). The development of this car showcases Australian expertise in component designing and manufacturing. Australian manufacturing industries need these activities, which will provide bases to improve value chain and

develop industry clusters in Australia. Furthermore, only in the context that Australian industries have developed localized specific advantages that they can secure more business opportunities based on technology transfer to developing countries, including China, and Australian subsidiaries could be more active with their parent companies in projects in developing countries.

7.5 Direction for the further research

Actually, this research can be seen as a part of series studies that deal with the impact to the Australian economy due to globalization. There are many important questions needed to be addressed. However, as next step of this research the future of the Australian manufacturing industries should be investigated. The investigation should identify the position of the Australian manufacturing industries in the economic development in Australia and answer the question that based on what conditions Australia is facing globalization. The investigation should look into the export performance of the Australian economy; the function of government industry policy to the development of the Australian economy in the time of globalization.

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APPENDIX:

Questionnaire A

For Australia based food processing companies that do not export or invest in China.

MA Student, REN Zegang

Centre for Asia and Pacific Studies
Victoria University of Technology

The information collected in this study will be treated with strict confidentiality. No name and address is needed. The data will be analysed statistically and the questionnaire will be destroyed.

1. Please indicate the number of employees in your company

1.1 less than 100

1.2 between 100 to 500

1.3 between 500 to 1000

1.4 more than 1000

2. Please indicate the ownership of your company

2.1 solely Australian owned

2.2 jointly owned by Australian and foreign investors

2.3 subsidiary of a foreign company

2.4 others (please specify)

---

3. Please indicate the reasons listed below that explain your company not having business activity in China.

(tick one box in each row)

4: major significance; 3: moderate significance; 2: minor significance; 1: not applicable

	4	3	2	1
3.1 our priority is not at the Chinese market				
3.2 the tariff and trading barrier in China is too high				
3.3 the Chinese market is taken care by our parent company or other companies within the group				
3.4 imported products from other developed countries have dominated the Chinese market				
3.5 foreign funded enterprises operating in China have dominated the Chinese market				
3.6 our product is not compatible with the local requirements				
3.7 the price of our products is too high for ordinary Chinese consumers				
3.8 difficult to find a reliable distributor in China				
3.9 too much investment will be required to enter the Chinese market				
3.10 we are not familiar with the way of doing business in China				

Others, please specify:

If your company has never tried to enter the Chinese market in any stage before, please stop here. Thank

you very much for support.
If your company has tried to invest in the Chinese automotive industry, but has failed or withdrawn from it, please answer question 4:

4. Please indicate the factors preventing your company from investing in China

4: major significance; 3: moderate significance; 2: minor significance; 1: not applicable

	4	3	2	1
4.1 difficult to find a right Chinese partner due to local firms' limitations such as: high debt too many redundant employees limited market coverage poor management poor technological conditions distant from major industrial areas poor infrastructures others:				
4.2 not in line with the strategy of your parent company				
4.3 unfamiliar with the procedure of establishing a production facilities in China				
4.4 too much international companies competing in the Chinese market				
4.5 limited financial capacity in conducting a major investment in China				
4.6 afraid of technology being copied				
4.7 uncertain about the development of the Chinese food processing industry				
4.8 Chinese firms are preferring to incorporate with large international companies				
4.9 our technology is not compatible with the local needs				
4.10 Chinese firms raise unrealistic conditions, such as : major investment export opportunities the latest technology others:				
4.11 disapproval from the Chinese government authorities				
4.12 the demand for our products is limited				

Others, please specify :

The End

Questionnaire B

For Australia based food processing companies that export or invest in China currently.

MA Student, REN Zegang

Centre for Asia and Pacific Studies
Victoria University of Technology

The information collected in this study will be treated with strict confidentiality. No name and address is needed. The data will be analysed statistically and the questionnaire will be destroyed.

1. Please indicate the number of employees in your company

1.1 less than 100

1.2 between 100 to 500

1.3 between 500 to 1000

1.4 more than 1000

2. Please indicate the ownership of your company

2.1 solely Australian owned

2.2 jointly owned by Australian and foreign investors

2.3 subsidiary of a foreign company

2.4 others (please specify)
---

3. Please specify the business activities of your company in China:
(please tick multiple appropriate answers)

3.1 have a representative office in China

3.2 export to China from Australia

3.3 have a production facility in China, in the form of:

a, license agreement

b, joint venture

c, wholly owned

others (please specify)
---

4. If your company is exporting to China, please describe your export to China:
(please tick multiple appropriate answers)

4.1 growing steadily

4.2 fluctuated all the time

4.3 decreased

4.4 a trading company is appointed to carry out the export

4.5 your company solely develops the export

4.6 the export is mainly developed by your company and helped by your parent company
4.7 the export is highly dependent on your parent company's strategy for the Chinese market
4.8 the export to China of your business is

a, very important
b, fairly important
c, minor important
d, potentially important

4.9 the exported products are classified as:

a, mainly consist of highly transformed products
b, mainly consist of raw material
c, mainly consist of semi processed products
d, a mixture of the three types products listed above

5. Please indicate the factors contributing to your export to China. (tick one box in each row)

4: major significance; 3: moderate significance; 2: minor significance; 1: not applicable

	4	3	2	1
5.1 our parent company has set up a company in China which imports our products				
5.2 our customer has built a plant in China which imports our products				
5.3 we have built a plant in China				
5.4 the trading company distributing our products in China has been effective				
5.53 investment has been made to improve our products and delivery				
5.6 we have established an effective marketing network in China				
5.7 the demand in China is growing strongly				
5.8 our products are of unique features				
5.9 our products can meet the special demands of the Chinese customers				
5.10 our price is competitive				
5.11 we have sufficient knowledge of doing business in China				
5.12 we have employed the people with the Chinese cultural and language background				
5.13 the Australian government export promoting schemes have played an important role in our export to China				

others (please specify)
---

6. What are the impediments that prevent your company from expanding the export to China: (tick one box in each row)

4: major significance; 3: moderate significance;
2: minor significance; 1: not applicable

	sig 4	3	2	not 1
6.1 the market share is increasingly taken by multinationals that have major joint ventures in China.				
6.2 being challenged with the imported products from other industrialised countries in the Chinese market				
6.3 the tariff and other entry barriers are too high				
6.4 lack of feedback from the Chinese market due to the dependence on distributors or other companies				
6.5 uncertain about the development of the Chinese market				
6.6 difficult to penetrate into the other markets in China				
6.7 the small export volume to China prevents us from investing major resources to expand the export				
6.8 a tight financial situation prevent your company from conducting a vigorous marketing promotion in China				
6.9 the product needs further improvement				
6.10 the price is not competitive				
6.11 difficulties in collecting the sales on credit				
6.12 the demand from the Chinese market is shrinking				

others (please specify)

If your company is not involved in direct investment in China currently, please stop here. Thank you very much for support.

Companies that have tried to conduct a direct investment in China but failed or withdrawn, please answer question 7. Companies that have direct investment project operating in China, please answer question 8 and 9.

7. Please indicate the factors preventing your company from investing in China

4: major significance; 3: moderate significance; 2: minor significance; 1: not applicable

	4	3	2	1
7.1 difficult to find a right Chinese partner due to local firms' limitations such as: high debt too many redundant employees limited market coverage poor management poor technological conditions distant from major industrial areas poor infrastructures others:				
7.2 not in line with the strategy of your parent company				
7.3 unfamiliar with the procedure of establishing a production facilities in China				
7.4 too much international companies competing in the Chinese market				
7.5 limited financial capacity in conducting major investment in China				
7.6 afraid of technology being copied				
7.7 uncertain about the development of the Chinese food processing industry				
7.8 Chinese firms are preferring to incorporate with large international companies				
7.9 our technology is not compatible with the local needs				
7.10 Chinese firms raise unrealistic conditions, such as : major investment export opportunities the latest technology others:				
7.11 disapproval from the Chinese government authorities				
7.12 the demand for our products is limited				

8. Please indicate the factors that contribute to the establishment of the production facility(ies) of your company in China
(tick one box in each row)

4: major significance; 3: moderate significance;
2: minor significance; 1: not applicable

	4	3	2	1
8.1 giving great importance to the potential of the Chinese market				
8.2 effective consultation from: Austrade private consultation firms in Australia Hong Kong based consultation firms Australian government organisations				
8.3 encouragement from the parent company or foreign partner due to: your company's closeness to China availability of Chinese descendants in Australia capability of your company in developing products suitable for the Chinese market				
8.4 local and international companies operating in China use your products as an important input				
8.5 a strong relation of supplying raw material or semi processed products to major multinational companies which have joint ventures operating in China				
8.6 possession of the technology which is urgently needed by the local firms				
8.7 capability of injecting a major investment into the China project				
8.8 offering export opportunities to local firms				
8.9 having selected a good partner				
8.10 having selected a good location				
8.11 rich experience in doing business in China				
8.12 employ professionals with Chinese ethnic background				

others please specify: -------

9. Please indicate the factors that prevent your China operation from further expansion. (tick one box in each row)

4. major significance; 3: moderate significance;
2: minor significance; 1: not significant

sig

not sig

	4	3	2	1
9.1 pressure from other foreign funded auto manufacturers operating in China				
9.2 financial limitation of you company in further investment in China				
9.3 difficulties to reach other markets in China				
9.4 difficulties in teaming up with major local corporations				
9.5 difficulties in maintaining a good cooperation with local partner				
9.6 different agenda from that of parent company				
9.7 demand for your products is weak				
9.8 fear of your technology being copied				
9.9 chaotic local distribution system				
9.10 inconsistent quality of material supplied locally				
9.11 lack of experience in doing business in China				
9.12 difficulties in hiring qualified employees in China				

others, please specify :

The End

Thank You Very Much For Support

Notice:

The questionnaire to the automotive industry is identical to the questionnaire to the food processing industry. Only some worlds in the cover page are different.