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**DIRECTORATE OF INTELLIGENCE**

31 March 1987

## China's Trade: Austerity Measures for 1987 [redacted] 25X1


### Summary

China's trade totaled more than $73 billion last year, nearly double the level recorded in 1980, according to Chinese statistics. Imports continued to outpace exports for the third consecutive year, however, leaving Beijing with a deficit of $12 billion. While continuing to post a large trade deficit with Japan, China recorded a $1.6 billion surplus with the United States in 1986. Beijing's recent hard line toward imports--including a reported freeze on imports using centrally allocated foreign exchange--indicates that trade in 1987 may decline. The austere measures also indicate that Beijing's foreign exchange reserves may have dropped substantially from the $10.5 billion posted last November. Moreover, Beijing's cutback on imports and continued press for exports will probably further lower US exports to China this year and exacerbate the bilateral trade imbalance. [redacted] 25X1


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This memorandum was prepared by [redacted] Office of East Asian Analysis. 25X1
Information available as of 27 March 1987 was used in its preparation. Comments and queries are welcome and may be directed to the Chief, China Division, OEA, on [redacted] 25X1

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**Trade Performance in 1986**

China's merchandise trade grew nearly 11 percent to reach a record $73.8 billion in 1986. Exports increased 13 percent to $31 billion, while imports rose less than 2 percent, to $43 billion. Although Beijing recorded its third consecutive trade deficit, last year's deficit of $12 billion was a nearly $2 billion improvement over the 1985 record deficit. 25X1

Exports. With a drop in world oil prices crimping what had been the premier foreign exchange earner, Beijing last year turned to textiles, increasing exports 10 percent until they represented more than one-third of total foreign exchange earnings. Oil earnings plummeted an estimated $3 billion last year compared with 1985, accounting for only about one-tenth of hard currency earnings. China also increased agricultural exports in 1986, with cotton, canned products, tea, peanuts, and vegetables increasing significantly in volume. 25X1

Imports. At the same time, imports grew less than 2 percent, according to Chinese customs statistics, as more restrictive foreign exchange allocations for nonessential commodities and closer monitoring of redundant purchases took effect. Imports of television sets, for example, fell more than 70 percent from a year earlier. Beijing also reduced some industrial imports; imports of rolled steel fell by one million tons or 8 percent, copper imports were down 52 percent, aluminum and aluminum products 45 percent, and synthetic fibers 38 percent. On the other hand, imports of some industrial materials such as wool, iron ore, and rubber increased by 34, 36, and 25 percent, respectively. 25X1

Trading Partners. China's largest trading partners in 1986 were Japan, Hong Kong, the United States, and the Federal Republic of Germany, accounting for more than half of China's total trade (see Table 1). Trade with the Soviet Union reached $2.6 by Chinese accounts, making the Soviet Union China's fifth-largest trading partner. Although trade with Moscow represents less than 4 percent of Beijing's total trade, the dollar value has doubled in the last two years with the promotion of border trade and technical cooperation. Trade with the European Community is also increasing, in part because of increased concessionary financing and Beijing's attempts to buy less of its sophisticated technology and machinery from Japan. China continued to hold the largest bilateral trade deficit with Japan last year, reaching $7.7 billion. Chinese data indicate Japanese exports to China fell 17 percent as Beijing reduced imports of consumer goods, but China's exports to Japan declined 22 percent. 25X1

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Table 1 USD Millions
China: Top 10 Trading Partners, 1986*

| Country | Total Trade | China's Exports | China's Imports | Balance** |
|---|---|---|---|---|
| Japan | 17,200 | 4,764 | 12,436 | -7,672 |
| Hong Kong and Macao | 15,453 | 9,830 | 5,623 | 4,207 |
| United States | 7,336 | 2,622 | 4,714 | -2,092 |
| West Germany | 4,558 | 1,003 | 3,555 | -2,552 |
| Soviet Union | 2,640 | 1,200 | 1,440 | -240 |
| United Kingdom | 2,444 | 1,433 | 1,011 | 422 |
| Singapore | 1,768 | 1,215 | 553 | 662 |
| Australia | 1,617 | 210 | 1,407 | -1,197 |
| Italy | 1,500 | 363 | 1,137 | -774 |
| France | 1,052 | 321 | 731 | -410 |

*Based on China's customs statistics.
**Minus sign indicates a deficit for China.

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**Sino-US Trade in 1986**

According to China's customs statistics, total trade with the United States fell about 1 percent last year, to $7.3 billion. Beijing recorded a 12-percent increase in exports to the United States and a 7-percent decline in US imports, leaving it with a $2.1 billion trade deficit. 25X1

US trade statistics, however, show the opposite, with a US deficit with China of $2.1 billion, underscoring the large discrepancies between US and Chinese calculations of trade data (see figure 1). Although discrepancies frequently exist in trade partner data, Chinese statistics have shown consistently higher figures for imports and lower figures for exports for only one major trading partner--the United States. In large measure, differences in US and Chinese valuation and classification methods have led to the discrepancy. Time lags in recording trade flows also contribute to the gap, as do differences in the conversion and aggregation of trade data between renminbi and US dollar equivalents, and the treatment of transshipments through third parties, especially Hong Kong. 25X1

China's exports to the United States increased 21 percent to $4.7 billion last year, according to US Department of Commerce statistics, led by a nearly 70-percent increase in exports of clothing, apparel, and footwear, which together accounted for more than one-third of total US-bound exports. Beijing also significantly increased its exports of electrical and power-generating machinery to the United States. At the same time, the value of China's exports of petroleum and petroleum products, and nonferrous metals showed substantial declines as prices dropped. Stricter US import controls on nonferrous metals such as tungsten also contributed to lower sales. China's imports of US goods fell by 19 percent to $3.1 billion, reflecting significant declines in purchases of consumer goods and textile fibers, yarns, and fabrics as Chinese production of these products increased. The value of US exports of petroleum and petroleum products, inorganic chemicals, and some machinery and equipment showed gains. 25X1

**Prospects for 1987**

**More Controls on Imports.** Conservative Chinese officials opposed to trade liberalization have called for a belt-tightening since the mid-January resignation of General Secretary Hu Yaobang, indicating that trade levels--at least for imports--may fall in 1987. In early February, People's Bank of China President Chen Muhua told a visiting US diplomat that foreign exchange controls would be tightened and import substitution policies followed more strictly--even to the extent of banning foreign products of higher quality than those produced domestically. Later in the month, Vice Premier Li Peng told a visiting French diplomat that foreign businessmen should be prepared for possible contract cancellations and a closer review of future contracts. Some cooperative projects would also be reviewed, according to Li, and possibly cancelled. 25X1

There is increasing evidence that Beijing is implementing even more control over hard currency spending. Some US Embassy sources report that a moratorium on



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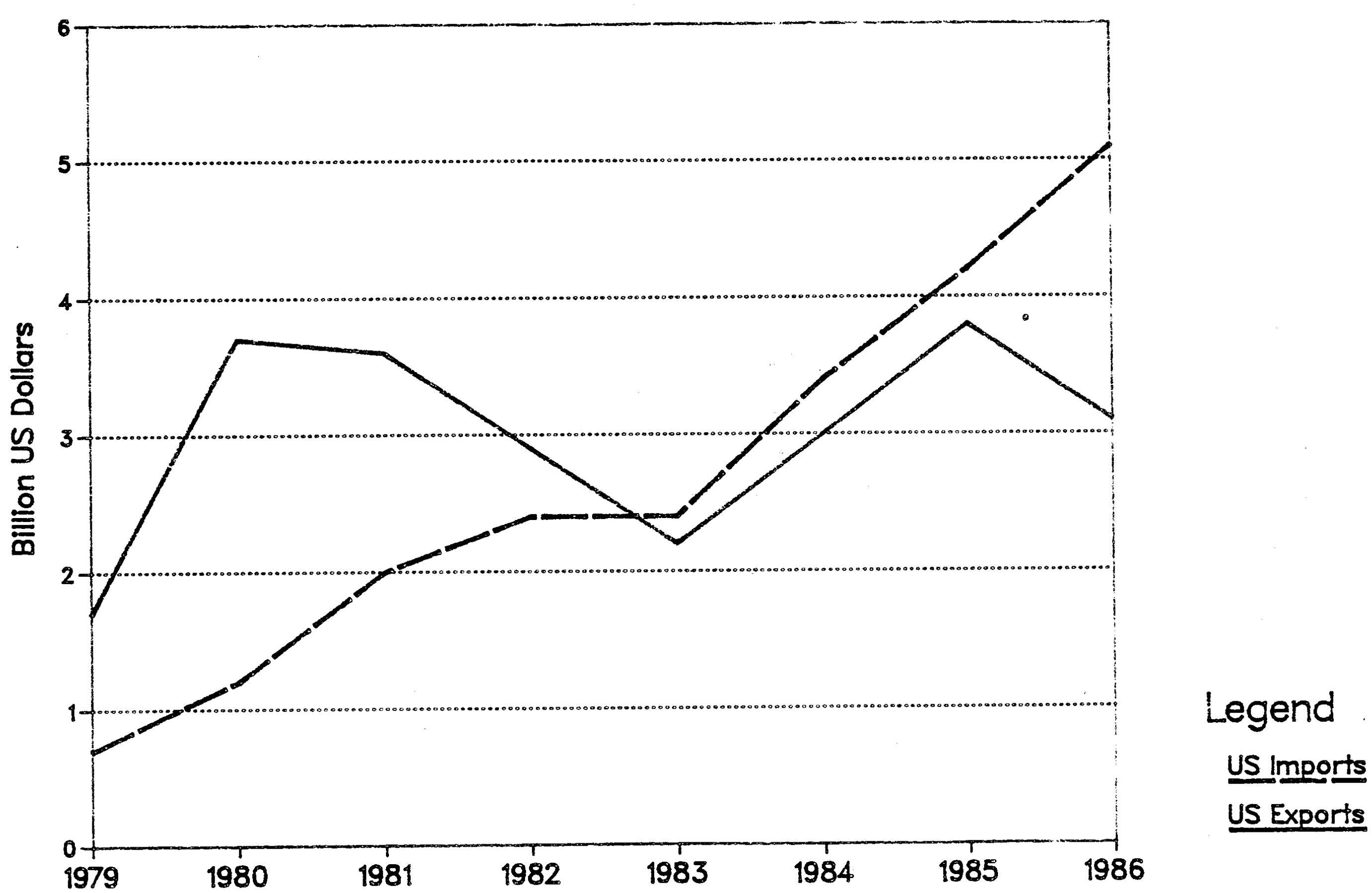
**Figure 1.**
**United States—China Trade***




* Based on US data.

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imports has been instituted that may last six months--paralyzing import-dependent industries that do not have long-term supply contracts. Last year, China imported roughly $3 billion in raw industrial materials, a large portion of which were used in export industries. A moratorium therefore would eventually affect hard currency earnings from exports as well. We believe many of the large export-oriented state enterprises that are dependent on imports are covered under long-term supply contracts. However, many of these are only umbrella agreements under which short-term contracts are carried out--most often quarterly--and therefore they, too, may be affected by the new directive. [redacted] 25X1

**More Controls on Foreign Exchange.** The new import restrictions build on already tight foreign exchange controls imposed in response to the rapid decline in foreign exchange during 1985 and early 1986. These controls, moreover, appeared to be taking effect as the growth in imports was held to less than 2 percent last year and as reserves were beginning an upward trend, according to the official reserves position last November (see figure 2). This suggests that Beijing is facing a foreign exchange shortage more severe than indicated in the $10.5 billion level of reserves posted last November. [redacted] 25X1

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**Outlook for Bilateral Trade.** According to US Embassy officers in Beijing, the effects of China's foreign exchange crunch have been felt by many foreign companies, and rumors that Beijing was suspending negotiations on foreign contracts for machinery and equipment were generating significant concern. In their contacts with US businessmen, most believed they would face increasing difficulty in obtaining future contracts. Beijing's recent shift toward imports from the European Community may also reduce the US market share in China. Given the more limited access by Chinese enterprises to foreign exchange, we believe there will be more pressure for increased use of barter and countertrade in purchases, possibly increasing the level of technology imports from the Soviet Union. [redacted] 25X1

While the import restrictions will most likely further lower US exports to China this year, we believe Beijing will continue to press hard for exports to the United States. The new position of textiles as China's premier foreign exchange earner will make Beijing less amenable to limiting sales to the United States. Consequently, we expect Beijing to take a hard line in this year's negotiations for a new bilateral textile agreement. [redacted] 25X1



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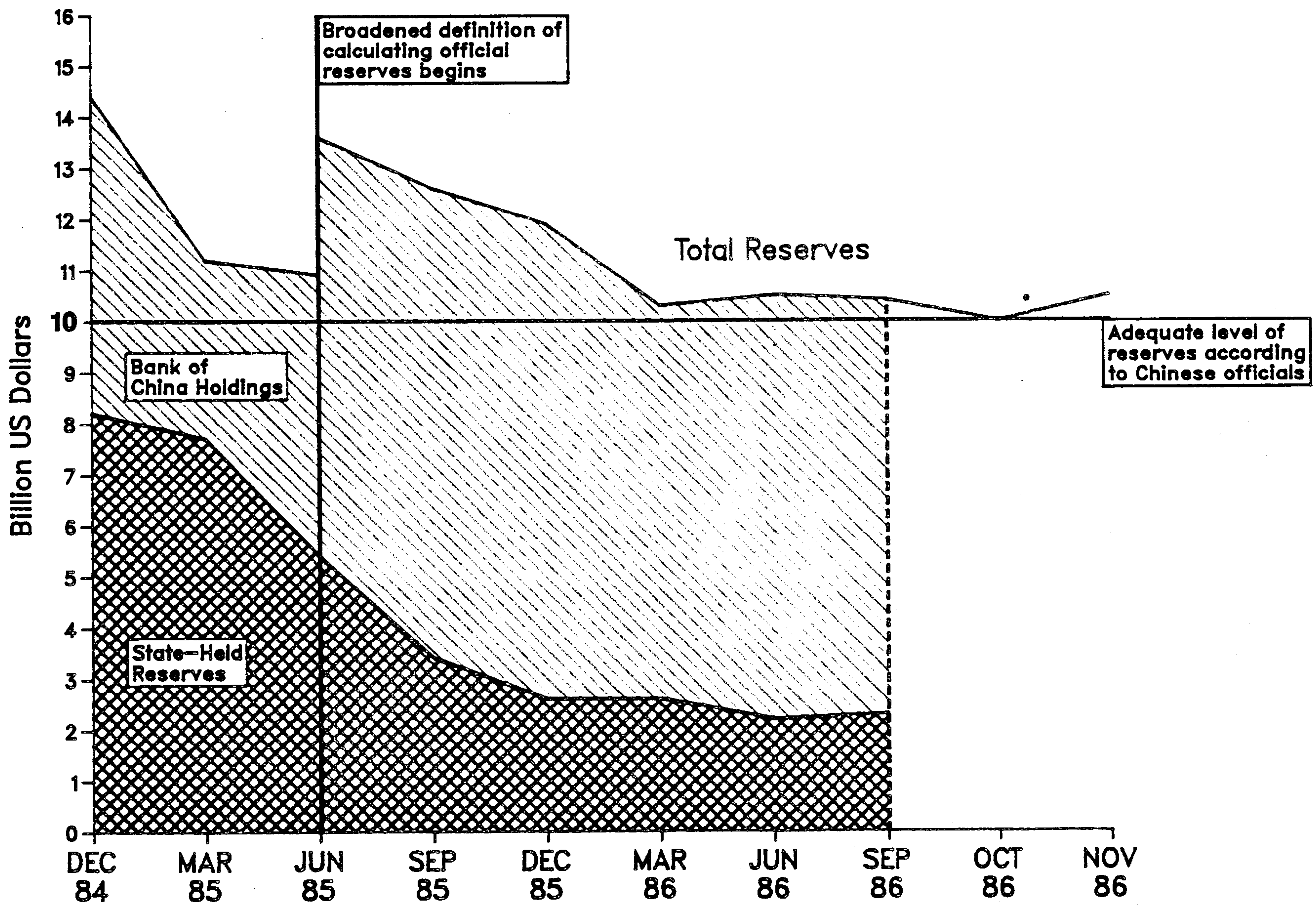
Figure 2.
China's Official Foreign Exchange Reserves

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