

PRC View of Contracting

Trade is built on mutual trust and respect; terms of contracts are regarded as inviolate

BY SETSUZO KOHSAKA*

Needless to say, China is a very large market for our country. As efforts are continued between now and the start of the 21st Century to carry out the "four modernizations" campaign, even greater investments will be required to strengthen China's industrial base, develop its natural resources, and expand other manufactures. Because its vast size promises immense potential, the Chinese market will become increasingly more important in world trade. Moreover, it will undoubtedly become a first-rate market in terms of the overall trade valuation.

At the present time, however, the national economy of China is going through a temporary adjustment period which is necessary to correct the damages caused by inefficient investment decisions in the past. This adjustment will take some years to complete, because it is aimed at creating conditions for healthy growth in the future and includes efforts to reform the administrative structure, balance the development of light and heavy industries, and build the nation's infrastructure.

Following this, China's national economy is expected to enter a new phase of development. During this adjustment period, China will likely attach major importance to the effective use of capital resources and to strengthening the present industrial base by concentrating on projects to restore and upgrade existing factories. It is predicted, however, that China will enter a period of growth averaging 4% to 5% per year in the first half of the 1980s, and that this growth will accelerate during the latter part of the 1980s to reach a new expansion phase in 1990.

As I mentioned earlier, China is an important market. This is especially true for sales of technology and associated plants. As shown in Table I, C. ITOH has consummated 30 contracts with China, totaling nearly \$2 billion in value. Some of our experiences provide the basis for comment.

CHINA'S BASIC APPROACH TOWARD PLANT CONTRACTS

I should stress at the outset that my references to China's basic plant contract approach does not mean

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to imply major differences with international practices in this regard. Indeed, Chinese behavior in principle has been very much in accord with standard contract interpretation. In one respect, however, the Chinese approach does seem to exhibit subtle differences which perhaps mirror China's characteristic way of thinking relative to the fundamental ideas of plant contracts.

This can best be expressed as a tendency to focus on rough, sometimes sketchy, general outlines of basic ideas rather than the precise, specific and legalistic enumeration of all details which is typical of plant contracts among Western countries.

Unlike quickly concluded agreements for the sale of specific commodities, plant contracts necessarily involve extended performance periods during which long-term cooperation between buyer and seller is essential. Obviously, the successful conclusion of such contracts depends on the maintenance of mutual trust, reliability, and confidence between both parties. The Chinese view appears to favor this concept of strengthening friendly ties and mutual goodwill as a part of such contracts.

When disputes develop, recourse is made not to contract specifications (which, as noted, are minimal) but rather to "friendly discussions" to hammer out a satisfactory settlement. In short, it would appear that China's approach to plant contracts emphasizes this maintenance of friendly relationships and mutual reliability instead of specifics.

SELECTION OF PARTNERS

Our experience suggests that China follows a very deliberate policy in selecting partners for any plant export contract, and is willing to spend a great deal of time in investigating potential candidates. Much importance is attached to choosing trustworthy partners who demonstrate proven reliability to properly carry out all phases of the construction. This selection process specifically includes two aspects: (1) The adoption of reliable techniques and processes for both the hardware and software of any plant; and (2) the selection of appropriate licensors, engineering firms, etc., who can clearly supply all required equipment and/or perform as specified.

In making the final selection of the actual partner(s), technological competence, financial ability, and overall reputation and creditability are the factors that will be stressed. In the event of equal qualifications for any potential candidate, those with an international reputation and a strong bilateral relationship with China are favored. The specific contract terms typically call for the selling side to be represented by the joint signatures of the licensor or engineering company and business firm.

SOFTWARE EVALUATION (TECHNOLOGY EVALUATION)

When we started negotiating plant contracts with China, we found that China's low evaluation of plant software and general lack of uniformity and consistency in setting evaluation standards often led to disagreements in our discussions. I think these problems stemmed from China's lack of experience in plant contracts and their difficulties in evaluating invisible goods. As the number of contracts has increased, however, evaluation standards have become more consistent and this problem seems to be disappearing. Furthermore, as the projects for the modernization of the existing plants and incorporation of improved technologies will increase, the importance of setting software evaluation standards will be increased.

EQUITY IN CONTRACTS

In 1978, China made very large purchases of plants and equipment from Japan. These very ambitious purchases were intended to rapidly expand the major chemical industry as part of the "four modernizations" campaign. Subsequently, however, China asked Japan to temporarily discontinue work on these contracts, because too much had been spent on plants and equipment and shortages in domestic and foreign capital would require readjustments in their plans. In making this request, Chinese officials frankly noted that their excessive emphasis on heavy industries had distorted the balance of the entire economy and was threatening a number of projects with bankruptcy.

The Japanese manufacturers, on the other hand, found it impossible to accept this request. Instead, they insisted that contract performance be carried out according to schedule. Most of the equipment for the plants had already been manufactured and numerous difficulties and complications would ensure if China

was to suddenly discontinue the contracts. As an alternative, the Japanese partners offered to assist China in obtaining the necessary funds for plant construction on a government basis.

The problems were eventually resolved to the satisfaction of both sides through a series of negotiating sessions. A government-to-government financing agreement of Y300 billion was concluded so that equipment shipments and construction could be immediately resumed to complete the Baoshan steelworks and Daqing complex. At the same time, arrangements were made to suspend the completion of other plants, including those in Nanjing and Shengli [Shan Dong Province], once all completed equipment had been installed and sufficient measures had been taken to provide for the good maintenance of these facilities and equipment. As a result, this issue was settled harmoniously.

I believe that one of the special features of China's approach to contracts is a willingness to strictly adhere to all aspects of contracts that must be faithfully fulfilled. Although we have completed many contracts with China in the past, we have not had a contract unilaterally cancelled. The incident I mentioned is an example. Despite the severe problems the country was facing in raising both domestic and foreign capital, I feel that China clearly proved its sincere commitment to contract performance by its understanding of Japanese reactions and its agreement to pay for completed equipment.

In conclusion, trade with China is built on a foundation of mutual understanding and mutual trust. I believe that this trade will develop further as long as each side adheres to these principles. As China continues its policies of economic liberalization, decentralization of decision-making authority and other reforms to make its economy more open, I think that we can expect this trade to expand in many ways.

C. ITOH'S CONTRACTS WITH THE PRC FOR PLANT CONSTRUCTION SINCE 1973

TYPE OF PLANT	SITE	CAPACITY	LICENSOR/ CONTRACTOR	CONTRACT DATE
1. 120 Channel Submarine Coaxial Cable System			Fujitsu	Apr. '73
2. Ethylene Plant	Beijing (Yanshan)	300,000 T/Y	TEC/Lummus	Sep. '73
3. Polypropylene Plant	Beijing (Yanshan)	40,000 T/Y X 2 UNITS	MES/MPC	Sep. '73
4. Titanium Trichloride Catalyst Plant	Beijing (Yanshan)		Toho Titanium	Jan. '74
5. 1700 mm Continuous Hot-Strip Mill & Silicon-Steel Sheet Mill	Wuhan	Hot-Strip: 3,000,000 T/Y Silicon-Steel Sheets: 70,000 T/Y	NSC	Jun. '74
6. Melamine Decorative Laminated Board Plant	Shanghai	3,000,000 M ² /Y	Ibigawa	Jul. '75
7. Paraxylene-Benzene Plant	Tianjin	Paraxylene: 64,000 T/Y Benzene: 20,000 T/Y	JGC/UOP	Dec. '75
8. Color TV Picture Tube Plant	Hanyang	960,000 units/Y	Hitachi	Jul. '78
9. MDI Plant (Diphenyl- Methane Diisocyanate)	Yantai	10,000 T/Y	JGC/Nippon Polyurethane	Aug. '78
10. Loading & Unloading Equipment for Iron Ore Transshipment	Beilunshan	10,000,000 T/Y	Hitachi	Nov. '78
11. HDPE Plant (High- Density Polyethylene)	Nanjing	140,000 T/Y	MES/MPC	Dec. '78
12. HDPE Plant (High- Density Polyethylene)	Nanjing (To be Transferred to Daqing)	140,000 T/Y	MES/MPC	Dec. '78
13. PTA Plant (Purified Terephthalic Acid)	Shanghai	225,000 T/Y	MES/MPC	Dec. '78
14. Phenol & Acetone Plant	Beijing (Yanshan)	Phenol: 50,000 T/Y Acetone: 30,482 T/Y	MES/MPC	Dec. '78
15. Ethylene Plant	Shengli	300,000 T/Y	TEC/Lummus	Dec. '78
16. Ethylene Plant	Nanjing	300,000 T/Y	TEC/Lummus	Dec. '78
17. Ethylene Plant	Nanjink	300,000 T/Y	TEC/Lummus	Dec. '78
18. Paraxylene & Orthoxylene Plant	Shengli	Paraxylene: 64,000 T/Y Orthoxylene: 20,000 T/Y	TEC/UOP	Dec. '78
19. Hydrocracking Plant	Maoming	80,000 T/Y	JGC/Union	Dec. '78
20. Hydrocracking Plant	Nanjing	80,000 T/Y	JGC/Union	Dec. '78
21. Aluminum Smelting Plant	Guiyang	80,000 T/Y	NLM	Dec. '78
22. Baoshan Steel Mill Blast Furnace	Baoshan	3,000,000 T/Y	NSC	Dec. '78
23. Color TV Tube Metal Parts Plant	Beijing	For Producing 1 M. CRT units/Y	Hitachi	Jul. '79
24. Color TV Set Assembly Plant	Shanghai	14" 120,000 Sets/Y 22" 80,000 Sets/Y	Hitachi	Dec. '79
25. Water Treatment Plant for Baoshan Steel Mill	Baoshan		NSC	Dec. '79
26. Process Oxygen Plant for Baoshan Steel Mill	Baoshan		Kobe Steel	Dec. '79
27. Color TV Tube Materials Plant	Beijing		Hitachi	Jul. '79
28. Color TV Tube Assembly Plant	Beijing		Hitachi	Jul. '79
29. Oilu Petrochemical Complex Off-Site Facilities	Shandong		Alone	Jul. '80
30. Soybean Protein Plant	Jilin	1,000 T/Y	Fuji Oil	Dec. '81

TOTAL: Approx. US\$2,000 Million

Remarks:	MPC:	Mitsui Petrochemical Industries, Ltd.
	MES:	Mitsui Engineering & Shipbuilding Co., Ltd.
	NSC:	Nippon Steel Corp.
	JGC:	JGC Corp.
	TEC:	Toyo Engineering Corp.
	NLM:	Nippon Light Metal Corp.
	Lummus:	Lummus Corp., U.S.A.
	Union:	Union Oil, U.S.A.

TABLE I