Behind China's economic chaos lies boundless corruption

by Cho Wen-pin

By now, even the communist government of China can't deny that the country is facing an enormous economic crisis. The buzzword used to be "overheating," which polarized the supposedly authoritative opinions on China's economic disease. But, according to the July 4 issue of *China Times* weekly, the State Bureau of Statistics recently reported that China's "economic crisis is worse than just overheating."

The report reveals that among China's many problems, agriculture remains at the top of the list. Next in severity comes the infrastructure bottleneck (that is, if the bottle still holds water), followed by an excessive money supply, a real estate bubble, and stock speculation. What it did not report, of course, is the corruption among China's privileged power clique, corruption which goes far beyond the crisis people normally perceive.

From farmers to finances

China's peasants account for 80% of the population in the mainland, or 20% of the entire world's population. But investment in the countryside has remained essentially moribund during the past decades. As a result, agricultural household income has increased only 6% each year, less than the nationwide inflation rate, which is predicted to be at 10% this year. In mid-July, the *China Daily* reported on a recent survey showing that 80% of the young peasants in Henan province want to give up farming and migrate to other areas. But there are no jobs waiting for them anywhere. "Some researchers say that the migrants could become a social problem," commented the paper—a gross understatement. And when the peasants are subjected to social injustice, their political consciousness and indignation can rise to levels far beyond what the communist regime would like to see.

The transportation crisis, caused by lack of basic infrastructure, is another never-ending headache for Beijing. From January through May of this year, China's railway department transported 631 million tons (mt) of goods—14.37 mt less than proposed for the period, and 1.48 mt less than the level for the same period last year. About 9.6 mt of much-needed coal was not transported, but was left sitting at railway stations flooded by a passenger overflow of 25 million migrating people.

The third symptom of China's economic crisis, as even the government now openly admits, lies in the financial sector. Excessive money supply is fueling inflation, which feeds back to create a demand for even more money supply, draining the local banks. All three government mints have been operating full throttle, overdosing the country with 28% more paper bills than were available last year. Up through May, China issued 150 billion more yuan ($27 billion) than the previous year.

Much of the money from local government goes into pumping up the real estate bubbles in some 6,000 "special economic zones." In Shanghai, it is estimated that real estate siphoned off $2 billion in foreign investment, much of which may actually come indirectly from Chinese financial resources. As for the funds invested into export-oriented assembly lines, capital is often wasted in redundant efforts to produce the same types of consumer goods. Interested in tax benefit policies from Beijing, these investors have to compete first with the real estate contractors for building materials; then, once they have completed construction and have emptied their bank accounts, they again face price wars over raw materials.

Corrupt government officials, along with thugs from outside the mainland, are fishing in these troubled waters of "financial reform." This has already sunk the former governor of the central bank, and has cast a cloud over Premier Li Peng around a recent bond scandal involving over 1 billion yuan (about $180 million) and 100,000 victims. Another huge black hole that drains government capital and the blood of cheap labor, is the ever-accumulating offshore balances.

Beijing's money-laundering scheme

One furious Chinese intellectual, reporting in the overseas Chinese newspaper *World Journal* July 7 on his recent visit back home, summarized four major problems that shocked him. Besides moral degeneration and the calamitous state of education, he mentioned the expanding power of Chinese managers of joint ventures or chiefs of state-owned group enterprises, who are either the next generation of the Communist Party founding members or government bureaucrats on leave. He saw such people spending $100 for admission to enter an exclusive bar in Beijing; tipping an escort girl with $200 in Guangzhou; or paying $16,500 to join a nightclub in Shanghai, where a bottle of cognac may have a $1,000 price tag; while some starving peasants in remote areas live on an annual income of as little as $40.

On July 4, the *Sunday Morning Post* of Hong Kong reported that Larry Yung, chairman of China International Trust and Investment Corp. (CITIC), has spent at least $7.5 million to purchase the family home of the late British Prime Minister Harold Macmillan. The new owner of this 14-bedroom country house in east Sussex, is the son of Chinese Vice President Rong Yiren—the famed "red capitalist."

But where does this kind of capital come from? Co-authors Shang Hai and Wan Runnan tried to solve the puzzle in their report in the June 30 issue of *China Focus,* a monthly newsletter published by the Princeton China Initiative. They first examined the striking but often ignored question of why China's yuan has depreciated 50% against U.S. dollar, while Beijing's official statistics claim that the total foreign capital invested in China from the beginning of 1992 through the second quarter of 1993 has exceeded the total amount for the previous 12 years combined. Their investigation revealed that over the last few years, Hong Kong has become the "the Switzerland of China's privileged clique—i.e., a money-laundering center," and a springboard of China's capital flight. Shang and Wan reported how mainland capital first lands in Hong Kong, and then magically gets back into the hands of Chinese empowered via various routes.

It works as follows: First, the value of export goods from the mainland is under-declared in order to evade controls from the foreign exchange administration and Chinese customs. When a company trades with Hong Kong partners, it claims in China far less than the true value of its exports, and then gets kickbacks from its agents in the form of direct deposits, stocks, or bonds. The inverse form of the same trick is to over-declare on imported goods in order to earn commissions from Hong Kong, Taiwan, or Japan.

To determine the size of the "window" created by "mis-invoiced" import-export deals, one can evaluate trade balances between China and its major trading partners. For instance, China has publicly denied the $18 billion trade deficit which the United States claimed to have with China in 1992. Research by a French investment bank shows that Chinese had under-declared at least $10 billion in its trade with the United States. Much of this discrepancy was "captured" in Hong Kong. The *Far Eastern Economic Review* on July 15 quoted another source from Lehigh University in Pennsylvania which estimated this capital flight at $15-25 billion in 1990, $13-28 billion in 1991, while in 1992 it rose still further, at an accelerating rate of 23%—more than the boasted growth rate of China's Gross Domestic Product. And this leakage figure would be much larger if China's "invisible" military trade were also included.

Next, Chinese parent companies take this opportunity of privatization to obtain money from the state treasuries, and inject the capital into their Hong Kong subsidiaries at far below market prices. A large chunk of the difference becomes stock or deposits of the Chinese managers in their phony Hong Kong fronts.

Finally, part of the capital becomes re-invested back into joint ventures on the mainland, thus giving them a tax-free ride. The scheme reduces not only genuine foreign investment in the mainland, but also government revenues. Or, going beyond that, Hong Kong companies engineer deals to turn over ownership rights, and become the holding companies of mainland enterprises. This puts the managers of mainland companies on the boards of directors of both sides—with top job security, since, as long as the reform policy remains, no one is able to fire these communist bureaucrats.

This explains why the newly rich, corrupt communists are so zealous about joint ventures and privatization. It may be a true tale that in 1989 George Soros was accused of being CIA-connected and was kicked out of Beijing after the Tiananmen Square massacre; but now China has lured swindlers from Hong Kong—so-called "overseas Chinese patriots"—to skim and share the best part of the pie.

'Malmarmaoism' can't save China

"Farmers may rebel!" This possibility has the Chinese Communist Party quaking in its boots, and they have issued a 36-point policy to try to ease tensions in the countryside. Many peasants live no better than their exploited grandparents did in the 1930s, and the enraged laborers, whom Mao led against the Nationalists, may become the major force for creating the potential to overthrow a regime which has already fooled them once before.

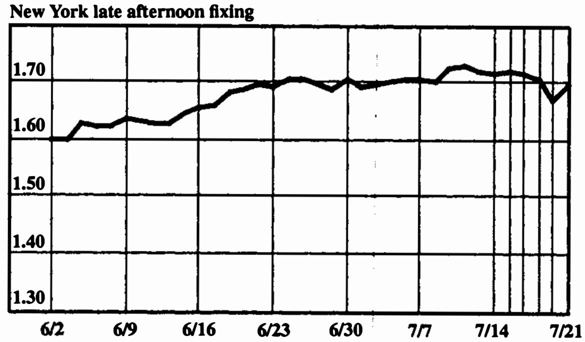
To counter this, Beijing is attempting to restore the system of militia among the workers and peasants on the one hand, and on the other hand claims it is combatting corruption and decadence among ranking party leaders—a move to stop those who trade in power now, but to allow their underlings to come into power later.

With the worship of money emerging as China's new religion—based on the same corrupt image of man as that of the communists—China is doomed, whether it sticks with the communists or turns to the monetarists. The only difference between Mao Zedong and Deng Xiaoping, is that Mao claimed that "power comes from the barrel of a gun," whereas Deng now believes that power can also come from a pile of cash. Deng's regime makes deals with "red capitalists" and calls it a "socialist market economy" with Chinese characteristics—his unique modern blend of "malmarmaoism" (a mixture of Malthus, Marx, and Mao)—equivalent to the ancient Taoist legalism that ended many Chinese dynasties disgracefully in past centuries.

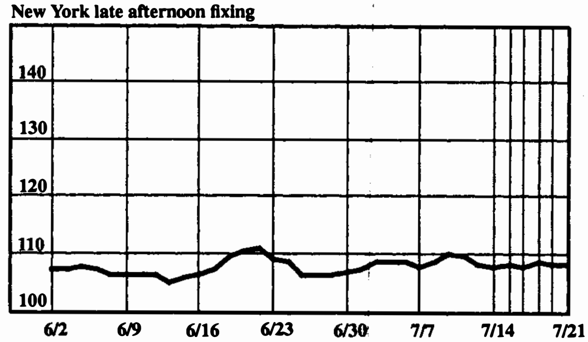
The drama of Chinese history of today is digging a gigantic grave for communism—but it could end in a terrible tragedy, sacrificing millions of lives, unless the Confucian "way of commonwealth," in the tradition of Sun Yat-sen, prevails.

Currency Rates

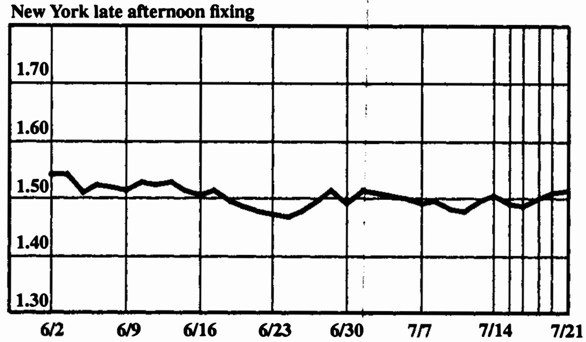
The dollar in deutschemarks
New York late afternoon fixing



The dollar in yen
New York late afternoon fixing



The British pound in dollars
New York late afternoon fixing



The dollar in Swiss francs
New York late afternoon fixing