

# **Assessing Social and Economic Risk in China**

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With its rise as an economic power, China is emerging as an influential force on the international political, military and regional security stage. However, rapid development has also led to imbalance and social unrest in China, resulting in suspicions and negative assessments of China's rise in the international community. In cross-strait relations, political ties remain chilled despite years of frequent social and economic exchanges. Consequently, there is still no means of securing protection for the Taiwanese people through normalized cross-strait negotiations. Under such circumstances, we need to make an in-depth and multi-dimensional assessment of China and an overall analysis of information on existing risks in China. This is aimed at helping the formulation of risk management concepts as well as avoiding misunderstanding or misinterpretation of the situation.

Social stability and a good economic and trade environment are important foundations for national development. On social and economic fronts, China faces numerous difficulties and problems that will become critical factors affecting its overall development. Both social and economic fronts are closely related and influence the other, as shown by the analysis below:

## **(1) Social Risk in China**

The major social risks faced by China today include: public demonstrations and protests, the "three agricultural issues (agriculture, rural areas and farmers)," unemployment, the "three disparities (rich-poor, rural-urban and east-west)," as well as public security and public safety.

### **1. Demonstrations and Protests:**

Despite the Chinese media's deliberate restriction on the coverage of demonstrations and protests, such incidents continue to occur in China with increasing frequency. Between 2002 and 2004, Chinese workers have held over

40,000 protests each year. The number of incidents of public unrest rose to 74,000 in 2004, with an average of 203 each day. Such protests are growing steadily in number. The number of protest participants has continued to increase and they have come from different social strata (workers, farmers, urban residents and students).

Furthermore, the attitudes of "money is paramount" and utilitarianism bred by the pursuit of economic growth have weakened social morality. Cases in which outsiders have been cheated by locals through investment schemes are prevalent in China today. There have also been numerous cases in which workers in foreign-invested enterprises have defected en masse to other companies. Since the Chinese authorities do not allow workers to strike, factory workers often show their discontent by resorting to factory slowdowns as a less rational and passive form of protest. The increasingly deteriorating labor-capital relations in China have become a root cause of social unrest.

## 2. "Three agricultural issues":

China has 900 million farmers. The success or failure of rural development in China pertains closely to whether China can successfully complete its so-called mission of "building a moderately prosperous society in all aspects." However, poverty has remained in rural areas of China in recent years. In 2004, the annual average income of farmers is only equivalent to one-fourth of the income earned by their urban counterparts. Nearly 350 million farmers exist below the poverty line. The average amount of arable land per farmer is only 0.1 hectare. Seventy million Chinese farmers are either landless or have less than 0.3 Mu (Chinese acre. One Mu equals to 670 square meters) of arable land, and the number of farmers is expected to rise to 100 million. Over-farming and neglect of environmental protection issues have led to the degradation of nearly one-third of the farmland in China. As a result, the "three agricultural issues" as described in a widely used expression "farmer hardship, rural poverty and agricultural risk," have become a critical problem facing China today.

## 3. Unemployment:

According to China's official figures, the unemployment rate in China's

urban and township areas reached 4.5% in 2004. However, the actual unemployment rate should be higher. The Economist magazine estimates that China's unemployment rate should have exceeded 10%. China's overall unemployment figure is likely to be between 20% and 26% if the number of rural unemployed workforce is included. Unemployment in recent years has already become a major fuse for protest activities in China.

#### 4. Three Disparities

Due to the speed of economic reforms and development in different provinces and areas, China faces a severe problem in the gaps between rich and poor, east and west, and rural and urban. The rich and poor gap has widened to such a degree that the assets of the country's wealthiest families are 359 times greater than the assets of the poorest group. The gap between high and low-income groups in urban and township areas was 11.8 times. In 2004, China's Gini coefficient for average household income reached 0.561 (A Gini coefficient of more than 0.5 is considered highly irrational and countries with a coefficient of over 0.6 are prone to social unrest). With regard to the east-west regional gap, statistics indicate that of the 600 impoverished counties in China, ninety percent are located in the central and western regions. In 2004, the GDP of the east was 2.62 times greater than the west and the composite talent gap between the east and west was 10:1. In terms of the urban-rural disparity, the gap between urban and rural areas is 3.35 times in 2004. Moreover, China's "three disparities" have been deteriorating and expanding in recent years.

#### 5. Public Security:

Acute disparities, combined with a weakening of the Chinese government's governance, have created an environment of serious social confrontation and increased crime rate in recent years. The number of criminal cases in which people seek to profit from illegal means has grown daily, membership in organized crime groups has risen to at least one million, and seventy percent of criminal acts have been gang-related. According to a survey conducted by China's State Statistical Bureau, "social morality issues" have become the top source of insecurity and concern among the public.

The deteriorating public security situation has often put the lives and safety of businesspeople and their families at risk in China. For example, in 2001 the Straits Exchange Foundation (SEF) handled 67 cases related to the personal safety of China-based Taiwanese businesspeople, with the figure rising to 91 in 2002, 107 in 2003, and 124 in 2004. In the first eleven months of 2005, the SEF has already handled 115 such cases.

#### 6. Public Safety:

At least 800,000 people in China die each year from unnatural causes related to daily life and workplace safety. China has the world's highest incidence of traffic accidents, which claim over 243,000 lives and leave more than two million people injured each year. China also accounts for eighty percent of all the mining-related deaths globally. In 2004, at least 803,700 cases were related to various workplace and public safety incidents. They produced an economic loss as high as 250.5 billion renminbi.

### **(2) Economic Risk in China**

Businesspeople need to consider the legal, economic and business risks involved when investing in China. Risk indices in China, such as tax inspection difficulties, anti-dumping retaliation and severe power shortages, have all clearly increased in recent years.

#### 1. Legal risk assessment:

Due to the excessive discretionary authority of the customs administrative systems in China, it is frequently reported that businesspeople were arrested because of their unintentional violation of relevant regulatory laws. Moreover, under China's complicated and confusing tax laws, it is easy for inspectors to single out people and find some small error. China can use tax inspections as a source to boost its national coffers. Therefore, the manifold forms of tax inspection come as no surprise.

Since the launch of reform and opening measures, China's economy and consumers have suffered considerable loss as a result of corruption. On average, such loss has amounted to between 980 billion and 1.25 trillion renminbi annually.

Every year, over 2.35 million Chinese Communist Party members are disciplined for cases involving corruption and other economic crimes. Beijing's failure in the battle against corruption is due to its systemic and structural problem. Specifically, China's long-term single party dictatorship system has concentrated power in a few hands and left the country without the transparent supervising mechanisms common to democratic countries. Consequently, China-bound enterprises are often forced to do business in China through the back door, causing them to shoulder the unnecessary burden of business cost.

## 2. Economic risk assessment:

The Department of Development Strategy and Regional Economy under the Development Research Center of China's State Council indicates that between April 2001 and October 2004, the General Administration of Quality Supervision, Inspection and Quarantine of the People's Republic of China seized counterfeit and shoddy goods worth 11.1 billion renminbi. Moreover, media reports have indicated that seventy percent of the world's counterfeit goods are produced in China. In just the four months between February 24 and June 10, 2003, the Chinese authorities confiscated about 5.02 million counterfeit goods. In the first half of 2004, government agencies in charge of industrial and commercial affairs nationwide seized counterfeit food products accounting to 257 million renminbi. In 2004, the value of seized counterfeit building materials totaled 1.24 billion renminbi.

Every year U.S. businesses lose around 250 billion U.S. dollars due to counterfeit goods, most of which are produced in China. China's inadequate patent policy and poor supervision of counterfeit goods have prevented many brand name goods from entering the Chinese market. For example, in 1994, Nintendo (USA) and other U.S. electronic game makers accused the Chinese government of turning a blind eye to piracy. Nintendo claimed that its losses from piracy in China had amounted to 720 million U.S. dollars as of 2003.

## 3. Business risk assessment:

According to Beijing-based weekly newspaper, *Economic Observer*, 26 out of China's 31 provinces face power shortages. In a survey conducted by the Zhejiang Private Economy Research Society, half of the 1,000 surveyed enterprises

said that their operations had suffered power cuts on average for more than one-third of the days in each month. Statistics show further that in 2004, China faced power shortages of 3,000 megawatts nationwide, affecting three-fourths of its provinces.

In addition, ninety percent of the rivers passing through China's cities are heavily polluted, seventy-five percent of the lakes suffer from eutrophication, and one third of China's land areas suffer from acid rain. This means that the extra costs of doing business will not only affect industries in sectors requiring stable electricity supply, such as the cement, plastics, and high-tech industries, but also heavily water-dependent industries, such as the food, electroplating, textile dyeing, and the restaurant and hotel industry.

Some Taiwanese people and international figures see China as a "window of opportunity." However, they should not overlook the latent risks lurking behind China's rapid economic growth. After all, China is still a totalitarian country. The modes of thinking that most people take for granted in a democratic society may not necessarily be applicable to China's regime. Only a careful assessment will ensure that people can successfully manage the risks and prevent unnecessary losses when they invest in China. At the same time, the Chinese authorities should actively make improvements and eliminate problems systemically, so that China can soon become a responsible member of the international community.