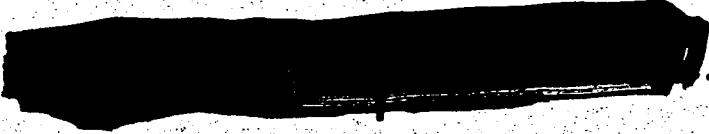




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Chinese Military and Economic Programs in the Third World: Growing Commercial Emphasis

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May 1984

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Preface

This report assesses trends in Chinese military transfers and economic aid to non-Communist less developed countries with an emphasis on events in the 1980s. The statistical data supersede those in our previous publications. This publication supplements the annual statistical reference aid *Communist Aid to Non-Communist Less Developed Countries*.

The term *military transfers* includes both the sale and grant of military equipment and related services, such as advisory support, training, and construction of military facilities. *Military transfers* occur under signed *agreements, commitments, or accords*, which constitute a formal declaration of intent. The terms *deliveries* and *shipments* also are used to indicate the movement of foreign military goods and services to the recipient.

Within the *economic aid* context, the terms *extensions, commitments, and agreements* refer to pledges of goods and services, either on deferred payment terms or as grants. Assistance is considered to have been extended when accords are initialed and constitute a formal declaration of intent. *Disbursements* and *deliveries* refer to the use of goods and services.

The non-Communist *less developed countries* referred to in this report include: (1) all of Africa except the Republic of South Africa; (2) all of East Asia except Australia, Hong Kong, Japan, New Zealand, and the Communist states of Kampuchea, Laos, and Vietnam; (3) Malta, Portugal, and Spain; (4) all of Latin America except Cuba; and (5) all of the Middle East and South Asia.

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Chinese Military and Economic Programs in the Third World: Growing Commercial Interests

Key Judgments

Information available as of 1 May 1984 was used in this report.

China's economic aid and military transfer programs in the Third World have changed dramatically over the past five years. In 1979 Beijing decided to emphasize military sales to earn hard currency and to reduce economic aid to conserve resources for its economic development. Since then, Beijing has emphasized commercial payoffs in almost all of its dealings with developing countries by:

- Increasing its arms sales almost 10 times over those of the previous four years. Since 1979 China has signed agreements to sell \$6.2 billion of weapons, 95 percent of them to Egypt, Libya, Iran, Iraq, and Pakistan.

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The new policy represents a radical departure for Beijing in the Third World. Earlier, China had provided both economic and military aid on generous terms to poor clients who often could not afford a more costly Western presence. China never attempted to compete with other military suppliers in the quantity or sophistication of weaponry. Military agreements featured mostly small arms and, for some clients, old-model tanks and aircraft. The economic program highlighted showy projects, such as the Tan-Zam Railway in Africa, and sports stadiums in a number of countries.

It may be difficult for Beijing to maintain existing levels of military sales once the Iran-Iraq conflict is resolved. More aggressive Chinese arms sales policies could have only marginal results because of increasing competition among suppliers and LDC demands for more modern military equipment. China could offset some of these factors by:

- Specializing in the export of basic military equipment, support facilities, and spare parts and ammunition for Soviet-made equipment.
- Aggressively selling a few more advanced weapon systems, such as MIG-21 jet fighters and improved medium tanks.

Even if military sales decline, we foresee an active military and economic presence for China in the Third World through the end of the decade:

- Military deliveries will be sustained at an unusually high rate under several billion of contracts still outstanding.
- Beijing sees these programs as an important means to earn foreign exchange. According to the Chinese News Agency, Beijing is looking for at least \$1 billion in hard currency earnings annually from its service program by the mid-1980s and plans to have 100,000 technicians in LDCs by 1986. We believe these levels are not achievable until at least the end of the decade but are an important signal of the importance China attaches to growth of the programs.

Prospects for marketing Chinese civilian technical services appear almost unlimited because of the low salary rates and China's reputation for quality work. A possible shortcoming is Chinese inexperience with the high technology Western equipment often used on projects where China is supplying only labor. China has undertaken a training program that will help it overcome this obstacle. We believe that economic and technical exchanges will continue to be the mainstay of China's program through the end of the century.

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Chinese Military and Economic Programs in the Third World: Growing Commercial Emphasis

Military Sales: A Product of the 1980s Agreements Soar. Since Beijing's policy decision in 1979 to expand its sales of military equipment for hard currency, China has signed agreements to sell \$6.2 billion of weapons to LDCs (including a record \$3 billion in 1981), 10 times higher than Chinese military agreements in the previous four years. The Iran-Iraq war has propelled China into second place among Communist military suppliers, ahead of all the East European countries combined (but still far behind the USSR). In addition to Iran, Beijing has picked up several other clients in the 1980s—including Jordan, Libya, and Liberia—

The new emphasis on financial returns has changed the direction of the Chinese program away from traditional Asian and African clients to wealthier Middle Eastern LDCs (figure 2).

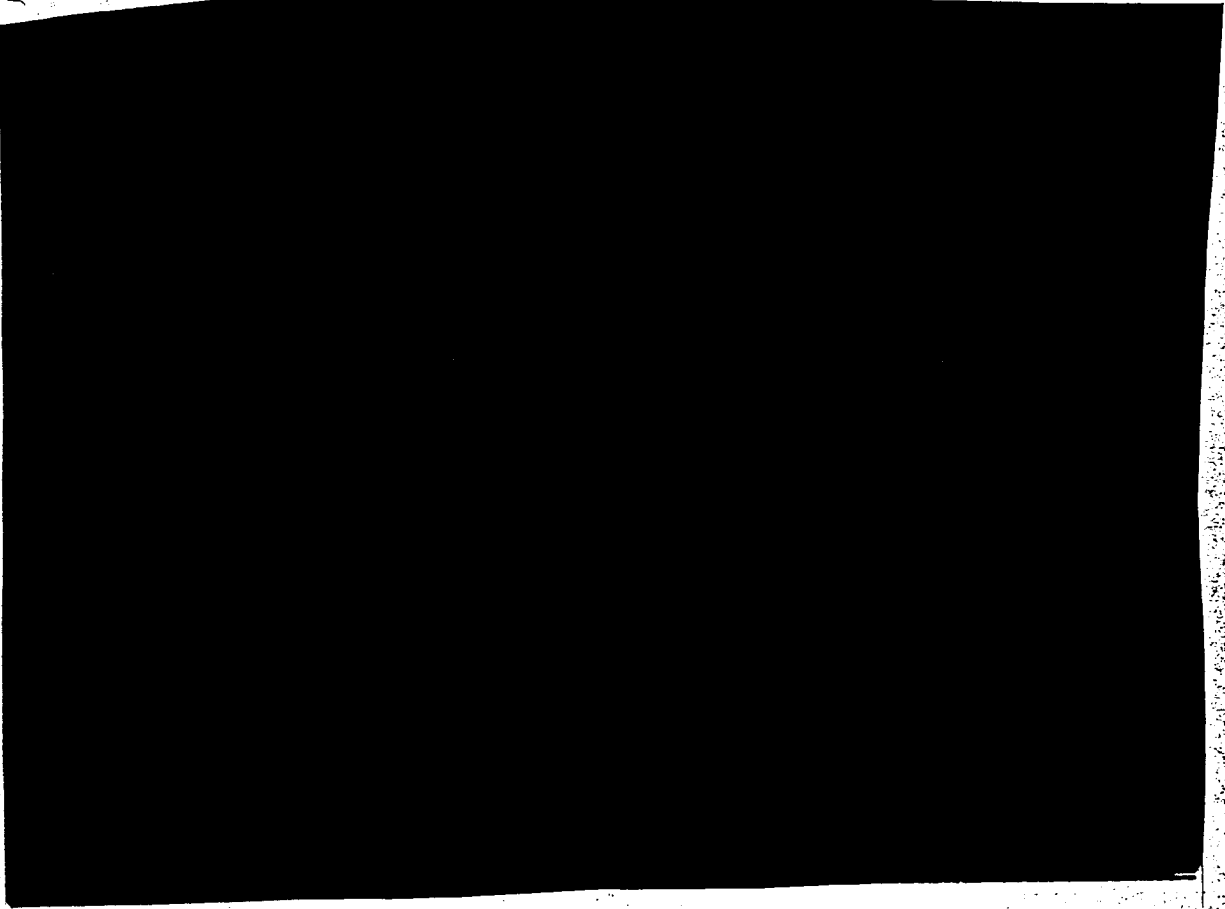
The Soviet Union's refusal to supply Iraq at the beginning of the Iran-Iraq war provided China with its most important breakthrough into the international arms market. Since then, Iraq has become China's best customer.

Table 1
China: Military Transfers to LDCs, by Year

Million US \$

	Agreements	Deliveries
Total	7,524	3,062
1958-73	516	452
1974	91	26
1975	40	101
1976	145	100
1977	74	73
1978	233	96
1979	193	100
1980	940	252
1981	2,964	437
1982	1,556	794
1983	772	631

Record Deliveries. China's drive to fill orders rapidly produced record deliveries in the 1980s. Average annual arms shipments of \$30 million to Third World clients doubled those of any previous year. Iraq has received about one-fourth of the deliveries since 1980.

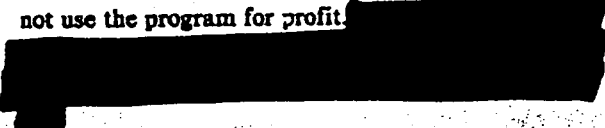


Small Military Technical Presence. Unlike the cases of the Soviet Union and the East European countries, China's expanding arms sales have not led to a larger increase in military technicians and advisers. Only about 500 Chinese military personnel were in LDCs in 1983, about the same number as over the past decade. China generally has been reluctant to send large numbers of military technicians to LDCs because they fear involvement in conflict. China, on occasion, has even denied requests to augment its military presence in client states.

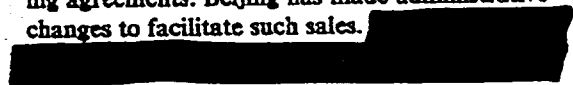


Additionally, the unsophisticated Chinese military equipment eliminates the need for

a larger advisory presence and keeps training requirements to a minimum. Finally, China apparently does not use the program for profit.



Basis for New Policy. Beijing's new aggressiveness in the international arms market underscores China's intent to pursue a competitive commercial arms export policy that emphasizes hard currency earnings rather than politics as the basic criterion for concluding agreements. Beijing has made administrative changes to facilitate such sales.



Military Transfers

China's military program historically has run a distant second to economic aid as a means of influencing LDC governments. Hampered by deficiencies in its own military establishment and committed to avoiding military entanglements with LDCs, Beijing responded reluctantly to requests from LDC clients. China made occasional arms transfers to Third World countries in the late 1950s and early 1960s, but did not provide arms as a regular feature of assistance until 1965.

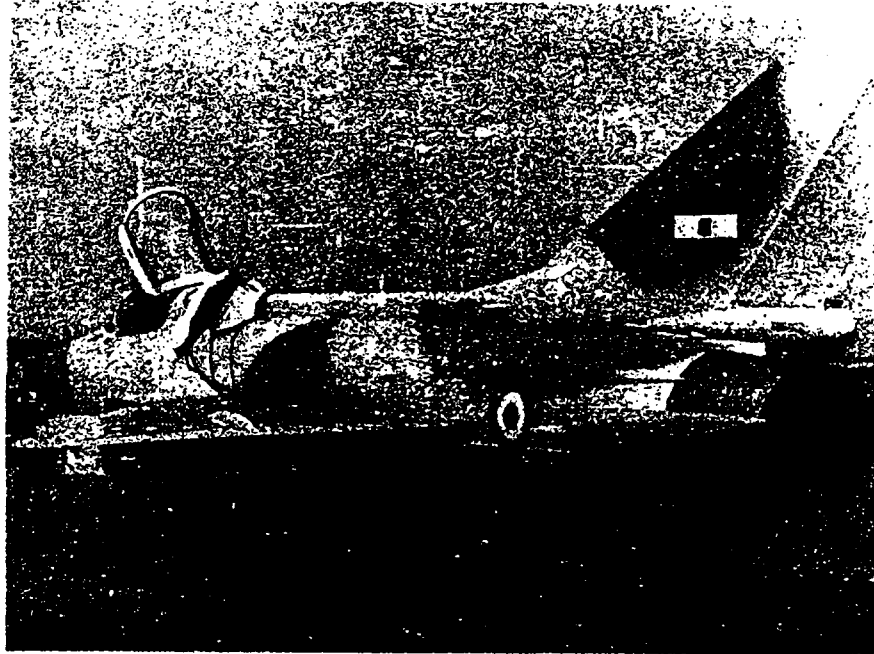
China's small military program never competed seriously with the USSR or Western suppliers, except in Pakistan and Tanzania, before 1979. For the most part, China provided small quantities of outmoded aircraft, ground forces equipment, small arms, and ammunition to the poorer less developed Third World nations.

Since its decision to sell arms commercially, China has increased its hard currency sales sixfold, and the focus of the program has shifted to the Middle East. Giveaways have virtually disappeared from the program.

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Figure 3. Chinese F-7 fighter aircraft.



[REDACTED]

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China does still seek political gains. Beijing is providing grant aid for dissident groups that have little prospect of buying equipment elsewhere.

In addition to financial returns, Chinese arms sales sometimes benefit China's domestic weapons development program by allowing access to foreign military technology.

[REDACTED]

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China also has remained somewhat flexible in its dealings with old customers and has exempted some of its long-time African clients from its cash-and-carry terms.

[REDACTED]

Economic Relations: Developing Commercial Potential

Entering the International Contracting Field. As with the military program, China is cutting down on giveaways in its economic aid and is now emphasizing commercial returns and hard currency earnings from technical services. The economic program has evolved from a modest effort featuring liberal amounts of grant aid to a major campaign to sell technical services and equipment for profit. Beijing's current leadership is trying to push China into the world economy by introducing its most salable items—such as cheap labor—into the international marketplace. In its aid program, China is seeking to combine enhanced hard currency earnings with benefits to LDC economies.

On the commercial side, China is working on housing in Kuwait, a number of construction projects in Iraq, and a \$375 million railway line in Nigeria. Last year, Beijing signed a \$1.6 billion railway construction agreement with Libya and is negotiating a similar contract with Algeria. Even though they are newcomers in the international commercial contracting field, the Chinese have been named general contractor on several major projects in LDCs, where they select subcontractors (generally Western or Japanese companies) and arrange for local services. According to Chinese news sources, since 1980 China has earned \$500 million in hard currency through its construction contracts, has an additional \$1.2 billion of contracts in hand, and expected to sign \$1 billion in new contracts in 1983.

New Aid Hits Record Lows. Since 1980 China's new economic aid pledges have fallen dramatically a victim of China's economic retrenchment in the post-Mao period. Only a few traditional recipients have received significant new commitments to continue programs. Agreements in the 1980s comprise less

Economic Aid

China began its aid efforts in the Third World in 1956 with a few scattered economic commitments to its East Asian neighbors. The program escalated rapidly in the early 1960s, as China competed with the Soviets for influence by extending assistance to newly independent countries in Africa. Over the past 28 years, China has used its \$6 billion aid program to serve a number of political ends, including:

- *Competing with the Soviets for leadership of the Communist movement in the Third World.*
- *Gaining support for its membership in the United Nations and other world organizations.*
- *Competing for leadership among Third World countries.*
- *Rewarding Soviet clients that have made the break with Moscow.*

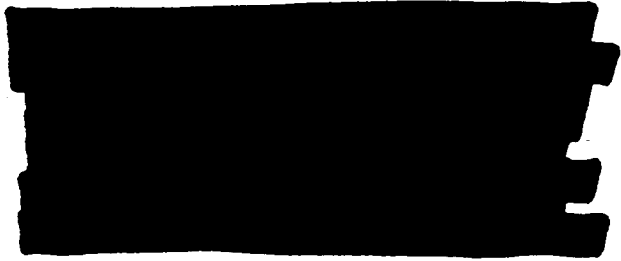
China's economic program historically has been more important than military sales as an instrument of influence in the LDCs. Until 1980, China's total economic aid pledges outweighed military commitments by 4 to 1. Several characteristics set China's economic aid program apart from that of other donors:

- *More than half of its aid has been concentrated on Africa, an area generally neglected by other donors.*
- *Project implementation is fast. About two-thirds of China's total commitment since 1956 has been delivered.*
- *Aid has been focused on infrastructure, primary industries, and agriculture—prominent deficiencies in LDCs.*

- *Projects are easy to operate and are import saving, such as simple processing facilities for food and raw materials, textile plants, and agriculture implements factories.*
- *Beijing provides adequate technical support and finances local costs of projects through commodities or cash transfers under credit or grant agreements.*

China's unwillingness—because of competing domestic priorities—to provide economic aid as it had before marks the demise of one of the most generous and most popular aid programs in the Third World. China has never had the resources nor the inclination to become a major aid patron: its economic aid to the Third World has accounted for less than 1 percent of total aid to LDCs over the past two and a half decades. Chinese officials have always stressed that self-help programs are the only way that LDCs can improve their economies and care for their growing populations. Still, China is the most popular donor in many countries, particularly in Africa, because it has focused on LDC development objectives often ignored by other countries. China's assistance has been simple and relevant to LDC needs. Most of the aid was interest free, repayable over 10 to 20 years after a 10-year grace period.

than 15 percent of China's total economic aid since 1955 and have followed a downtrend that began in the mid-1970s. Chinese economic aid increased in 1983 over 1982; most was provided on somewhat harder terms than before—shorter repayment periods, low interest charges, and almost no grant aid. The terms of Chinese assistance still are far more generous than those of most other Communist and some Western donors.



Third World countries in 1983 were serving under commercial contracts with the rest financed through aid agreements [REDACTED]

Beginning in 1980, China moved rapidly to export some of its abundant labor on commercial terms and began to bid on construction projects in Arab oil states. To handle its new sales in the Middle East and elsewhere, China opened offices in Dubai, Iraq, Jordan, Kuwait, and North Yemen. China also merged its Ministry of Foreign Trade with its Ministry of Economic Relations in mid-1982 to integrate aid and trade interests more closely. According to the Chinese press, some 42 companies are involved in construction projects abroad and 40 new labor contracts were signed during the first half of 1983 alone. In 1983, China exploited another potentially lucrative source of funds for the first time by providing labor to projects financed by multilateral agencies in Morocco, Nepal, Nigeria, and Somalia [REDACTED]

China has been successful in marketing services because of the reasonable salaries—from \$2,000 per month for project managers down to \$400 a month for laborers. These charges compare with as much as \$8,000 a month for personnel from other Communist countries. The Chinese are also industrious and able to endure difficult working conditions that would not be tolerated by skilled workers from other countries. [REDACTED]

China still is providing a substantial number of technicians to LDCs under aid agreements. Most of the technicians that China provides free are delivering basic services in public health and education. We estimate that 1,200 doctors and at least 500 teachers from China worked in the Third World (mainly Africa) in 1983. [REDACTED]

Prospects

China's new approach in its economic aid and military transfer programs in the Third World will provide Beijing with a number of opportunities to expand its

Technical Services: A Hard Currency Resource

The provision of project personnel has become the mainstay of China's economic program in LDCs as commitments of capital to aid projects dwindle. The number of Chinese employed in the Third World in 1983 has doubled since 1980—mostly in Iraq, Jordan, and North Yemen. Beijing also is using a small technical presence to build relationships with such Soviet-oriented Marxist states as Angola and Mozambique. [REDACTED]

Technical services, which formerly were provided free by Beijing to almost all aid recipients, are now being promoted to earn foreign exchange. About half of the 29,000 Chinese economic technicians employed by

China's "Four Principles" Encourage Profitability

China's new policy has received public endorsement from the highest levels of government. In a rare interview on China's aid program with the Paris daily *Jeune Afrique* in 1983, Vice Minister Gong Dafei reiterated his country's interest in the Third World, particularly Africa, but cautioned that the day of large Chinese aid projects such as the Tan-Zam Railway is over. According to Gong, "We are, therefore, obliged to reduce our foreign aid and modify the nature of that aid. We now prefer to offer our African friends modest development projects . . . which have rapid returns."

During a trip to Africa in January 1983, Premier Zhao Ziyang further enunciated "four principles" for aid to the Third World:

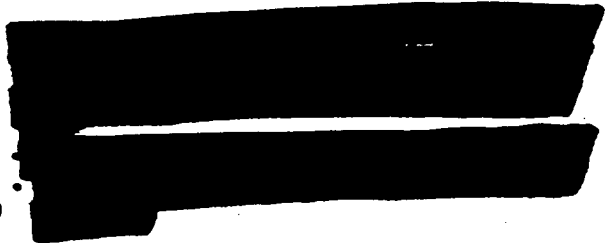
- "In carrying out economic and technological cooperation with African countries, China abides by the principles of unity and friendship, equality and mutual benefit, respects their sovereignty, does not interfere in their internal affairs, attaches no political conditions and asks for no privileges whatsoever.
- In China's economic and technological cooperation with African countries, efforts will be made to achieve good economic results with less investment, shorter construction cycles, and quicker returns.
- China's economic and technological cooperation with African countries takes a variety of forms suited to the local specific conditions, such as

offering technical services, training technical and management personnel, engaging in scientific and technological exchanges, undertaking construction projects, and entering into cooperative production and joint ventures. With regard to the cooperative projects it undertakes, the Chinese side will see to it that the signed contracts are observed, the quality of work guaranteed, and stress laid on friendship. The experts and technical personnel dispatched by the Chinese side do not ask for special treatment.

- The purpose of China's economic and technological cooperation with African countries is to contribute to the enhancement of the self-reliant capabilities of both sides and promote the growth of the respective national economies by complementing and helping each other."

This new policy updates the eight principles of aid to foreign countries formulated by Chairman Mao in the early 1960s. It no longer formally precludes China from profiting from its foreign aid efforts. China already has proposed joint ventures in geology and light industry to Nigeria and Tanzania (its first such offers in the Third World) and appears close to agreement with Bangladesh on a joint fishing venture.

influence in the LDCs and to strengthen its domestic economy. We expect Beijing will continue its opportunistic approach to arms sales, moving in where a client with a large Soviet inventory—as Iraq—is denied resupply in a crisis because of political reasons.



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