

# bulletin

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## *The Chinese Army's Conversion to Supplement Defense Budgets*

by Tai Ming Cheung

Although the People's Liberation Army's (PLA) primary goal is to be a professional fighting force, it has also become a major commercial presence in the country's economy since the mid-1980s. The PLA has a sprawling business empire of thousands of enterprises which generates hundreds of millions of dollars. These profits are used to either supplement inadequate defense personnel spending or to allow for military investment. These activities—completely under-represented in current research—form an important source of military expenditures, though in some cases, may demonstrate successful conversion endeavors.

Officially, there are around 10,000 factories, trading companies, farms, and other commercial entities owned by military units, scattered in all spheres of the Chinese economy. The vast majority are small-sized and barely profitable, but between 500 to 1,000 large-sized enterprises generate as much as three-quarters of total production output and profits which is believed to be equivalent to that of a small province such as Hainan or Qinghai.

Many of these large enterprises are being merged into conglomerates which will spearhead the military business complex's growth into the next decade. Around 30 enterprise groups have so far been formed, each comprised of between several dozen and more than a hundred subsidiaries.

One of the most well known of these rising behemoths is the China Poly Group, the PLA's primary weapons trading firm which is also engaged in property development, telecommunications, and financial services. The Poly group, run by a son-in-law of the late Deng Xiaoping, has its sights set on becoming one of the country's corporate powerhouses.

The formation of these conglomerates is part of a broader effort by the military high command to centralize control of this disparate network of enterprises and clean up their malpractices. When the

military authorities gave the go-ahead for military units to engage in business in the mid-1980s, little effort was made to supervise their activities.

This laissez-faire policy quickly led to a sharp rise in corruption, smuggling, profiteering, and other abuses. Military readiness and cohesion also began to suffer as soldiers neglected their duties in order to make money. These problems became so acute that the military authorities launched a two-year rectification campaign at the end of 1993 and closed down 40 per cent of PLA commercial entities and banned combat units from running businesses. Many of the enterprises run by these units were transferred to military authorities at the regional and central levels.

This allowed the General Logistics Department (GLD), which is in charge of managing the PLA's business operations, to collect a greater share of profits and taxes which lower-level units had previously kept themselves. With declared profits from the PLA's business activities in 1997 of around Rmb 4 to 6 billion (US \$480 million to \$780 million) from a total turnover of more than Rmb 50 billion, between half to two-thirds of this sum may have gone into central coffers.

PLA enterprises can be found throughout the Chinese economy and have carved out lucrative niches in some of the fast-growing parts of the economy:

- Transportation: PLA firms have converted an extensive military-dedicated transportation system to commercial use. The air force has its own airline using military transport jets which serve less-popular domestic routes and the navy has several inland and ocean-going shipping companies.
- Vehicle Production: Seventy army-run factories produce about 20 percent of China's passenger cars and trucks. However, because of poor efficiency and a lack of orders, most operate at less than half-capacity. The most successful of these firms, Liaoning Songliao Vehicle Corp., belonging to Shenyang Military Region, was listed on Shanghai's stock market in 1995.

***"...PLA enterprises have carved out lucrative niches..."***

- Pharmaceuticals: The PLA has nearly 400 pharmaceutical factories producing around 10 per cent of the country's annual output of pharmaceutical goods. The 999 Enterprise Group in Shenzhen, owned by the GLD, is the country's largest pharmaceutical company.
- Hotels: There are more than 1,500 PLA-owned hotels across China, ranging from converted army guesthouses to five-star luxury hotels.
- Real Estate Development: Military companies are heavily involved in the country's booming property sector. China Poly Group, for example, is one of the most active PLA property developers with a real estate portfolio ranging from the new home of the Shanghai stock exchange to luxury villas in Beijing.
- Telecommunications: The PLA has a major commercial presence in the country's fast growing mobile telecommunications market, largely because of its control of crucial radio wave-bands. Military construction units also lay most of the country's fiber optic communications lines.

Military conglomerates have also begun to expand into overseas markets as they face growing competition at home. Overall, PLA companies are estimated to earn as much as US \$1 billion annually from foreign trade, excluding arms sales.

When the PLA began to go into business, it was a temporary expedient to make up for inadequate defense budgets. But after nearly 15 years of spectacular growth, the military business complex is likely to be a permanent and powerful presence in the Chinese economy.

While many of the thousands of small-sized military enterprises are unlikely to survive in the coming years, especially since the Communist Party in 1997 endorsed a massive privatization of the state sector, a small core of giant military conglomerates is taking shape. The workforce which was mostly recruited from demobilized military personnel will then lose an important mean of reintegration into civilian life.

The military's relationship with these conglomerates will be as passive owners or majority shareholders rather than as hands-on managers. These enterprise groups are likely to become a major force in the Chinese corporate landscape over the next few years providing a long-term source of earnings for their PLA masters.

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Tai Ming Cheung is a consultant on Chinese affairs for Kim Eng Securities Ltd. in Hong Kong. In April 1998 he gave a presentation on this topic at BICC which generated wide interest and contributed to a project proposal to scrutinize the impact of military business on defense budgets.

## Staff Spotlight:



*Corinna Hauswedell*

Corinna Hauswedell (Germany), has been responsible for the publishing management and public relations policy at BICC since 1994, and Head of the PR Department since 1997. During this time, she has contributed to building up the Center's corporate identity and the conceptual image of BICC's publication series, such as *reports, briefs, papers*, and the Center's annual *conversion survey*, the third of which has just been published. She has also been instrumental in building up numerous external contacts for BICC's various work areas.

As a graduate historian with an academic background in contemporary history (Cold War), she has been working in the peace and conflict studies field since the early 80s, trying to link the interdisciplinary research work provided in the 'community' with the practical needs of a policy-oriented network for peace and disarmament issues. She is also co-editor of the German quarterly journal *Wissenschaft und Frieden*. Her Ph.D. thesis *Friedenswissenschaften im Kalten Krieg (Peace Research in the Cold War)* was published as a book in late 1997.

At the moment, Corinna is shifting her activities at BICC to more project-oriented work. She is currently project leader for BICC's *ConverArt* students competition and exhibition, one of the activities planned to mark the 350th anniversary of the Westphalian Peace. In autumn she will start shaping and conceptualizing a project on post-conflict peace-building in Northern Ireland.

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*"Many thanks to all external partners for a fruitful cooperation in previous years"*  
Corinna Hauswedell

## *Supporting Conversion of Defense-Related Enterprises in Moldova*

Moldova is one of the smaller republics of the former Soviet Union. Its economy was severely affected by the collapse of the vertically integrated economic system. Due to drastic decreases in industrial production, unemployment has risen quickly. Many of the unemployed are skilled workers who used to be employed by state-owned defense companies or were involved with the scientific research supporting this sector. Since 1990, two rounds of privatization have been carried out, and a third is underway.

BICC is leading a consortium (with ISA-Consult, Price Waterhouse, Dresdner Management Consult and TÜV Rheinland) to support the development of the Moldovan electronic sector, which will be able to hire skilled labor formerly working in the defense sector. The project is being conducted under the auspices of the European Commission's Tacis Programme and provides technical assistance to three privately-owned Moldovan enterprises (electronic sector), outsourced from the defense sector. One of the companies has developed an automotive testing system which it plans to market throughout the Newly Independent States with the support of the other two companies. The Moldovan partners are especially interested in benefiting from Western European automotive experience.

One goal of the project is to promote and support cooperation among the three enterprises—particularly in the fields of research and development, production, and marketing. It is especially important to promote 'market-driven' R&D projects in advanced technologies and to train new management to be more market-oriented (rather than product-oriented). In order to provide this expertise to the former military-related companies, BICC has assembled an interdisciplinary consortium to support their transition to civilian activities in a market economy.

The project is scheduled to last 12 months, and was launched in early May. In addition to several short-term experts BICC employs a long-term expert, Ernst-Thilo Roetger, an industry restructuring consultant, formerly with Price Waterhouse. He is based in Chisinau and leads the project.

→ For further information, please contact Herbert Wulf at [wulf@bicc.uni-bonn.de](mailto:wulf@bicc.uni-bonn.de) or Steven E. Sokol at [sokol@bicc.uni-bonn.de](mailto:sokol@bicc.uni-bonn.de) or E.-T. Roetger at [roetger@tacbic.mldnet.com](mailto:roetger@tacbic.mldnet.com)

## *ConverArt Exhibition opening on 21 August 1998*

The exhibition *ConverArt - The Art of Disarmament* in the Westfälisches Landesmuseum Münster (21 August to 27 September) will show the works of young artists from Bosnia, Germany, Nigeria, Rumania, Russia and Vietnam. An expert jury selected these works of art from the participants of a competition initiated by BICC to mark the 350th anniversary of the Westphalian Peace. On 20 August, the jury will choose the winners of the competition. The pictures, collages, photo work, film and video projects, sculptures, and architectural plans impressively reflect—using both metaphorical and documentary means—the virtual and real complexity of the topic *Conversion*. Both the 'hardware' of arms production and the military remnants as perceived by the artists, are covered in the contributions to the *ConverArt* competition. A catalogue containing all the competition entries will be available during the exhibition and from BICC.

The *ConverArt* exhibition will be held in parallel with an information display "Disarmament and Conversion after the Cold War".

The opening of the *ConverArt* exhibition in the Westfälisches Landesmuseum, Domplatz 10, 48143 Münster, is open to the public and will take place on 21 August 1998 at 7 p.m. Speakers will be Anke Brunn, former Minister, and Member of Parliament for North Rhine-Westphalia and Patron of *ConverArt*, Prof. Dr. Klaus Bußmann, Director of the Westfälisches Landesmuseum Münster, and Dr. Herbert Wulf, Director of BICC.

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### Bonn International Center for Conversion bulletin No. 8

The Bonn International Center for Conversion (BICC) is an independent non-profit organization dedicated to promoting and facilitating the processes whereby people, skills, technology, equipment, and financial and economic resources can be shifted away from the defense sector and applied to alternative civilian uses.

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## BICC Publications

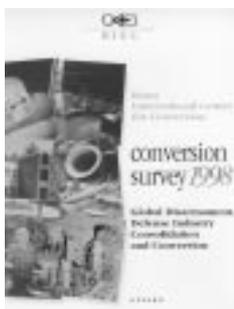
In addition to its annual *conversion survey* and other books, BICC publishes series such as *reports*, *briefs*, and *papers* which analyze the international conversion process, report on conversion projects and experiences, and offer scientific as well as practical know-how. Forthcoming publications include:

**report 12: Kiflemariam Gebrewold (ed.), *Converting Defense Resources to Human Development, Conference Proceedings, Summer 1998***

**brief 11: Ingo Cremer, Hartmut Kühle and Steven E. Sokol, *Integrierte Arbeitsmarktprojekte auf Konversionsflächen: Auswertung ausgewählter Beispiele verschiedener Bundesländer, Summer 1998***

In June, BICC published its third yearbook ***Conversion Survey 1998: Global Disarmament, Defense Industry Consolidation and Conversion.*** (Oxford University Press)

The 1998 survey updates and reviews key information and data on the international disarmament and conversion process. This year's edition focuses on the defense industries' strategies and the government policies to counter the negative effects of defense industrial change. The full text of the concluding chapter, the press releases, order information and selected background papers are available on BICC's Internet service at:  
→ <http://bicc.uni-bonn.de/general/survey98>



A paper on "***Demilitarisation, Reintegration and Conflict Prevention in the Horn of Africa***" by Kees Kingma and Kiflemariam Gebrewold will be published jointly by BICC and Saferworld (UK) in July 1998. It can be ordered from Saferworld (Contact: [sworld@gn.apc.org](mailto:sworld@gn.apc.org)).

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## Upcoming Events

International workshop on sociocultural aspects of defense restructuring and conversion organized by the Management Committee of COST A 10. "**Defence Restructuring and Conversion**" and the University of Ljubljana, Faculty of Social Sciences, Defence Research Centre at Grand Hotel Toplice, Bled, Slovenia. 9–12 July. Contact: <http://www.uni-lj.si/converconf>

Pugwash Conferences on Science and World Affairs: The 48th Pugwash conference "**The Long Road to Peace**" will take place in Oaxtepec, Mexico. 29 September–4 October. Contact: [pugwash@iol.it](mailto:pugwash@iol.it)

3rd International Security Forum "**Networking the Security Community in the Information Age**" Kongresshaus Zürich, Switzerland, 19–21 October 1998. Contact: <http://www.isn.ethz.ch/Securityforum/>

## BICC Notes

From 1 April, BICC has been asked by the European Commission to prepare an interim **evaluation of the KONVER II program in Germany's five new 'Länder'**. The objective of this interim evaluation is a comparative analysis of the current status of the conversion process in each of the new 'Länder' and Berlin. Both the effectiveness and efficiency of the KONVER II activities to date—as well as the prospects for activities during the remaining time-frame—are to be analyzed.

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The World Bank organized a conference in Paris on 20th April 1998 entitled "**Conflict Prevention and Post-Conflict Reconstruction**". BICC Director, Herbert Wulf presented a paper on "**Military Conversion and Economic Development**".

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In late-April, BICC was contracted by the Royal Norwegian Ministry of Foreign Affairs to prepare background documentation for an inter-governmental conference on small arms control in mid-July 1998 in Oslo. The resulting paper "**Reasonable Measures: Addressing the Excessive Accumulation and Unlawful Use of Small Arms**" defines the nature of the problems, reviews the effectiveness and relevance of the various initiatives that have been developed to address several aspects of the issue, and outlines a full range of options to extend or improve upon current activity.

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Two trade unionists from the National Union of Metal Workers of South Africa (NUMSA) visited Europe from 7 to 19 June 1998. They visited BICC and also several converted or converting industrial plants in Scotland, Northern Germany, and Slovakia. The purpose was to learn about conversion experiences and approaches, and the responses of the European trade unions. The visit was part of **ongoing cooperation between BICC and the Group for Environmental Monitoring (GEM)** in their effort to strengthen the capacity in South African civil society to monitor, support and implement conversion processes. It was supported financially by the Heinrich Böll Foundation.

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