

# Contents

Executive Summary	v
I. Introduction	2
II. Reforms and Restructuring	6
A. Separating Government Functions from Enterprise Management	9
B. Attracting Investment Financing	10
C. Setting Tariffs	11
D. Public Service Obligations	11
E. Creating Specialized Profit Centers and Modifying Revenue Distribution	13
F. Creating Competition	13
G. Improving Distribution and Logistics	15
III. Expansion	18
A. Foreign Investment	19
B. Commercial Investment	21
IV. Key Policy Recommendations	24
A. Commercialize the Enterprise	24
B. Separate Regulation from Enterprise Functions	26
References	28

# Abbreviations

GDP	gross domestic product
km	kilometer
MOR	Ministry of Railways
PRC	People's Republic of China
WTO	World Trade Organization

In this publication, \$ refers to US dollars.

## Currency Equivalents

(as of 8 June 2007)

currency unit	–	yuan
1.00 yuan	=	\$0.1307
\$1.00	=	7.6487 yuan
	=	CNY 7.7842

The exchange rate of the yuan is determined under a floating exchange rate system.

In this report, the rate used is the rate prevailing at the above date.

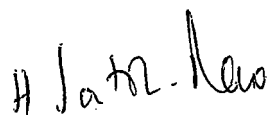
# Foreword

PRC's accession to World Trade Organization committed PRC to open and liberate its economy to better integrate with the world economy and to offer a more predictable environment for trade and foreign investment. These commitments brought significant challenges and opportunities to the country's transport sector, especially to PRC railways.

PRC railways have played a very important role in developing the national economy and in the country's industrial revolution. However, with increasing market access under WTO, PRC railways face competitive challenges in open access, pricing, reliability, service quality, and have corresponding opportunities to develop cooperative relationships. The challenges come from other modes of transport and from within the rail sector offering lower total costs, greater reliability, and better service quality.

This report evaluates some of the major challenges and opportunities for PRC railways due to WTO accession, and suggests policy recommendations that can be considered by PRC railways to overcome these challenges.

We hope that this report will generate interest among numerous stakeholders and provide a better understanding of the key issues. We also hope that transport planners, transport operators, policy makers, development partners, the private sector, and decision makers will find it useful and relevant.



Halady Satish Rao  
Director General  
East Asia Department  
Asian Development Bank

# Acknowledgment

**T**his report was prepared by Manmohan Parkash, Senior Transport Specialist, Asian Development Bank (ADB). Mr. Parkash has been closely associated with the railway development in the People's Republic of China (PRC) and has led task teams to identify, prepare and appraise large and prestigious railway projects in the PRC. He has led numerous studies on policy reforms in the railway sector and is deeply involved with the reforms, restructuring and institutional development of the railways in the PRC.

This report draws upon the findings of a technical assistance support provided to Ministry of Railways for studying the World Trade Organization (WTO) impacts on PRC railways and numerous discussions on related policy and reform issues with stakeholders including government officials and other development partners.

The report has benefited from the useful guidance provided by Nigel C. Rayner, Director, Transport Division, East Asia Department; Liu Junfu, Managing Director General, Foreign Capital Technical Import Center (FCTIC), MOR; and Madam Liu Yiqing, Deputy Director, Policy and Regulation Department, MOR.

Valuable and useful inputs were provided by Makoto Ojira, V. B. Tulasidhar, and other ADB colleagues. Muriel S. Ordoñez and Ma. Priscila P. del Rosario provided support in copy editing the report and Arleen R. Chan provided support in formatting the report.

We gratefully acknowledge the numerous other people who assisted in the preparation of this report.

# Executive Summary

**A**ccession to the World Trade Organization (WTO) required the People's Republic of China (PRC) to open and liberalize its economy and to offer a more predictable environment for trade and foreign investment. These commitments have brought significant challenges and opportunities to PRC Railways. Specifically, the PRC railways is committed to opening up its freight transport market to private operators by December 2007, and WTO accession has further increased PRC's international trade resulting in more demands on a rail system that is currently operating at nearly full capacity. Foreign competition will require PRC Railways to function as a commercial enterprise operating under market principles, and increased trade requires urgent investment in capacity. The traditional railway organizational model must be transformed to satisfy the changing needs of customers and investors in a competitive market economy and should be configured as a joint enterprise of the Government and the private and public sectors to make it more efficient, productive, cost effective, financially self-supporting, and responsive to customer needs.

The PRC has the highest freight density in the world at 10.5 times the world average and is the largest railway under one management in the world. Because of underinvestment in the past, however, PRC Railways faces recurring capacity constraints on most parts of the national network linking major industrial and commercial areas with major cities and ports. The development of railway infrastructure has lagged behind the growth of the nation's economy and the growth in total traffic, and this has adversely affected productivity and is becoming a constraint on further economic growth.

In the 11th Five-Year Plan (2006–2010), 300 billion yuan (CNY) are needed for railway investment every year to meet goals for expansion and improvement. Thus, the financial outlay for capital construction will increase fourfold compared with the average outlay of about CNY65 billion per year during the 10th Five-Year Plan (2001–2005). Clearly, this amount cannot be fully met from government and internal sources only. The Ministry of Railways (MOR) has been working over the past decade to attract foreign investment in the railway sector, but success has been very limited. Several possibilities for foreign investment are available, but low tariffs and low rates of return as well as other factors are impediments. As commercialization in operations, planning, and the selection of capital projects increases, commercial investors will be more and more attracted to railway projects. They would, however, demand a rate of return comparable with other opportunities in the market.

PRC Railways should commercialize its operations, and MOR should separate its regulatory functions from its enterprise functions. Commercialization is necessary for the railway company to adapt and prosper nationally and globally. Separating regulation is a means to harmonize regulatory structures with basic WTO legal principles.



PRC Railways has played a very important role in developing the national economy and in the country's industrial revolution.

