Original Article

THE SOCIAL DIMENSIONS OF FOREIGN INVESTMENT IN CHINA

Chowdhury, Leena Priyadarshini

Fellow, India China Institute, the New School, New York, USA
DOI: https://doi.org/ 10.5281/zenodo.17121267

Abstract: In the market economy Foreign Direct Investment (FDI) become a key element for the economic growth. FDI is considered to be an essential vitamin to boost up the domestic capital, productivity and employment and it is always reflect a better economic environment in the context of globalization. Irrespective of their political ideologies countries one after the other opening up their markets and enjoying 'the glory of prosperity'. China with its 'open door policies' emerged as the most preferable destination for FDIs in the world and become a model for its followers including India. This article examines the positive and negative aspects of the growing capital in China.

Keywords: Liberalization, FDIs, inequalities, Special Economic Zones (SEZs), Real Estate

Introduction:

According to World Investment Report issued by the United Nations Conference on Trade and Development in September 2004 China is the No. 1 destination of foreign investment in 2003. China is continuing the story and is still the most attractive destinations for foreign capitals in the world. Foreign direct investment (FDI) used in China in 2006 topped 63 billion U.S. dollars; it was higher than 5 percent over the previous year[1] according to the official sources. The exact contractual value of foreign funds was not available at press time. Bo said China would make effective use of foreign funds and make the service sector a key area to attract foreign investment. According to the reports, although China has been the largest recipient of foreign investment among all developing nations for 15 years, there is much to be done to improve both of its quality and quantity.

The International Monitory Fund (IMF) latest survey report released in October 2007 (see chart 1&2) certifies the Chinese „un-reliable‟ data by saying "China is now the single most important contributor to world growth, in terms of both market and purchasing-power-party (PPP) exchange rates." The report further predicts that China‟s economy continues to grow at breakneck speed, turning it into a driving force in the global economy. China's economy gained further momentum in 2007, growing at 11½ percent, and is expected to grow by 10 percent in 2008. Other emerging markets are also growing strongly[2]. Deng‟s slogan „to get rich is glorious‟ is working in China. Work, Save and live with dignity through prosperity is the ideology on which modern day China is deriving its strength from. But the Chinese economists are perplexed looking at the magnitude of increasing FDI, reserves and high rate of savings. How to regulate wealth, how to narrow inequalities and place the country socialist path is the issue bothering the Chinese leadership and economists.

The Road Map:

Original Article

FDI is the singular factor that has put China on the economic upswing. China has been the world largest FDI recipient among developing countries since early 1990s. In recent years, FDI to China accounts for 1/4 to 1/3 of total FDI inflow to developing countries. Foreign investment has become an important source for China.s investment in fixed assets. Its share in total annual investment in fixed assets grew from 3.8% in 1981 to its peak level of 12% in 1996. After the Asian financial crisis in 1997, FDI inflow fell and its contribution to fixed assets investment has also decreased to about 9% and 7% in 1998 and 1999, respectively. According to the figures released by the government, there was an average 10 per cent growth rate in the economy during the past four years with the FDI touching 720 billion dollars. In 2006 alone China received 69.5 billion dollar FDI and in ten months of 2007 it was 67.8 billion dollars. The supporters of China open door policy always believe that foreign capital in China has played a largely positive role in its economic development. They see more benefits out of the FDIs apart from solving the capital shortage problem the country like better access to existing, local technologies, indirect productivity gains through spillovers, world class labor training and management strategies. Of course they proved right.

The success story of China high rise economy has started way back in 70s. Since late 1970s, China has gradually and in a phased manner opened its economy for foreign businesses and has attracted large amount of direct foreign investment. At each phase the Government carefully evaluated its policy and based on the experiences it has incorporated changes on their policy priorities. In the first stage during late 1970s and early 1980s, government policies are characterized by setting new regulations to permit joint ventures using foreign capital and setting up Special Economic Zones (SEZs) and Open Cities[3].

Open cities obviously opened their doors to FDIs by taking advantage of reforms. The State Council also awarded rights of autonomy in foreign trade to Guangdong and Fujian Provinces and, in 1980, set up four Special Economic Zones (SEZs) in Shenzhen, Zhuhai, Shantou, and Xiamen. Later on in December 1982, the decision to open up China to the world economy was formally included in the 1982 state constitution adopted by the Sixth National People‟s Congress. Late in 1983, Regulations for the Implementation of the Law of the People.s Republic of China on Joint Ventures using Chinese and Foreign Investment was formulated in 1983 to further liberalize the domestic market and to clarify the business environment for foreign joint ventures. Since 1984, China has also moved to further open up the country to FDI. In 1984, the concept of SEZs was extended to another fourteen coastal cities and Hainan Island. Twelve of the fourteen cities were designated Technology Promotion Zones in 1985 to expedite the transfer of technology. In 1985, development triangles- the Yangtze River delta, the Pearl River delta in Guangdong, and the Min Nan region in Fujian, Liaodong and Shandong Peninsulas, and the Bohai Sea Coastal Region- were also opened to foreign investors. Later in 1990, the Pudong District of Shanghai was designated as a new development zone to lead development along Yangtze River.

Article-22[4] for the Encouragement of Foreign Investment adapted (1986) more favorable regulations and provisions are helped in attracting FDI inflow, especially export-oriented joint ventures and joint ventures using advanced technologies. This amendment allowed wholly foreign-owned enterprises and provided foreign joint ventures with preferential tax treatment, the freedom to import inputs such as materials and equipment, the right to retain and swap foreign exchange with each other, and simpler licensing procedures. Additional tax benefits were offered to export-oriented joint ventures and those employing advanced technology. The government also attempted to guarantee further the autonomy of joint ventures from external bureaucratic interference, to eliminate

Original Article

many „unfair‟ local costs, and to provide alternative ways for joint ventures to balance foreign exchange. Privileged access was provided to supplies of water, electricity and transportation on par with other State owned companies and further facilitated to provide interest-free RMB loans.

To strengthen the Article -22 another regulation known as Article-3[5]which explicitly linked (Article 3) the establishment of wholly foreign-owned enterprises to the development of China‟s national economy, and required such enterprises either to be exported-oriented or to use advanced technology and equipment. The amendment of 1979 Joint Venture Law (1990) further relaxed the rules by allowing non-Chinese to act as Chairman of the Board of Directors, extensions to the terms of operation of joint ventures, and removed the upper limit to the proportion of the registered capital contributed by the foreign partner, which resulted in increasing inflow of foreign capital in the late 1980s and, in particular, early 1990s. From mid 1990s, while maintaining favorable environment for foreign businesses, government policies began to focus more on linking FDI promotion to domestic industrial objectives.

Generally speaking, China.s policies toward FDI have experienced roughly three stages: gradual and limited opening, active promoting through preferential treatment, and promoting FDI in accordance with domestic industrial objectives. These changes in policy priorities inevitably affected the pattern of FDI inflow in China. Between 1978 and 1982 about 920 companies invested just 1.8 billion dollars while the investment went up billion by billion and in the next decade and has attracted about 48,764 companies by 1982. Yet the FDI did not cross 4.5 billion mark. Stepping up the economic reforms China started Special Economic Zones (SEZs), Autonomous business zones along the coastal region. This resulted in a ten-fold growth of FDI in just ten years. Hong Kong, Macau besides Taiwan, Japan, America and European nations are today investing millions of dollars in the country and the average income increased from $200 in 1979 to $1269 in 2004.

„The Glory of Prosperity‟:

Before making the China wo\rlds destiny of prosperity Deng destroyed several „old‟ practices and reformed the China from gross roots. He reversed the Mao‟s slogans and trained Chinese how to live with money. One of Deng's first reforms was to abolish Mao's rural agricultural communes and allow peasants to cultivate family plots. Grain harvests quickly increased, and other reforms followed. City dwellers were allowed to start small-scale businesses, ordinary Chinese were allowed to buy consumer goods, and Deng actively courted international investors. As he said long back now an average Chinese city dweller firmly believes “Poverty is not socialism. To be rich is glorious”.

The flood of FDIs and other investments have completely changed the social and economic structure of China. This has changed the life style of people living in cities and those migrating to cities. Seventy per cent of the people living in Chinese cities have an annual income between $ 2,000 and $8,000 while in Indian cities people earn not more than $2,000. While people in the annual income group of more than $7,500 are about 6 per cent, in India it is just 1.2 per cent. More than six lakh foreign companies are operating in China and employment was created to over 15 crore people. China has attracted more FDI than any other country, including US, in the world. The country achieved 15 per cent industrial growth since 1980 and diverted the profits to develop infrastructure. It has built 30,000 km express highway while India could not build one-tenth of that stretch. Chinese investment in these projects is very nominal. The 1.3 billion strong country has turned its manpower into a major factor in

Original Article

the development process. People above 16 years form one billion and 76 per cent of the populace take part in development process.

At least 60 per cent of the population have primary or secondary education and have some technical knowledge and the education system trains them in some vocational course. This is how China‟s workforce from 78 to 80 crore which is working to its advantage. There are no legal hurdles for those who want to invest in China, which provides workforce. There is no „serious "implementation of minimum wage rule. Earnings vary from the nature of work, place of work and the industry one works. This method is always beneficial to the company and workers hardly have any bargaining power and there is no chance of any trade union activity or workers organizing themselves. This is a major attraction for companies to set up shop in China and is the reason for the swelling FDI.

Shadow of Inequalities:

Because of the reforms taken up by Deng and the construction of vast SEZs, the coastal areas became industrial villages and production factories. Thus, compared with villagers‟ income, their income increased from 500 to 1000 times. During the Reforms time, the facility of free medicine for rural people in China was abolished and insurance methods were introduced. With this, medicine became an unbearable burden for the rural poor. On the other hand, the divide increased as not all could possibly access new jobs and ways of income earning that were coming into reach. Migrating from one place to another without permission from the government is banned in China.

Even to migrate to urban areas, they require government‟s permission. Government will not permit any one without a stable employment appointment letter. Those who are becoming imprisoned forcibly to land (agriculture) are being subjected to intense griefbecause of this.

On the other hand, the number of people who are migrating discretely, working illegally and settling down is in millions. Such people who are mortgaged for very low wages cannot access any government facilities. Cannot be escaped rigorous punishment, if they caught. Growth of investments and decrease of liberty is going to become another major problem for China. As a result of Liberalisation, the state completely changed many laws which were favorable to workers. Many public limited companies were closed on the pretext of losses. Private and public-private partnership companies are growing in number.

According to a study by Li ChengShui, chief of the State Statistics Bureau (SSB) in 1981-84 that was made public on October 12, 2006, the public sector employed only 32% of China‟s industrial and service workers, and accounted for 37% of the country‟s GDP. This represents a remarkable change from just what it was a decade ago. In 1995 the public sector accounted for 78% of GDP. Li presented his findings in a report first completed in May 2006[6].

With its new found wealth, China has embarked upon a massive urbanization plan and infrastructure development plan is percolating to rural areas as well. Beijing is trying to reduce the dependency of its populace on agriculture. Swelling of investments is creating heartburn among the people. There are warnings that the socialist philosophy of the country would be harmed unless the growth in wealth, facilities and assets in cities are not regularized. Increase of income has changed the life style in cities.

The neo rich class in the industrialized areas is a cause of concern. Boom in real estate has led to luxury cars and jazzy life style. Real estate prices are going up at 15 to 20 per cent annually since 2000. Shanghai, Beijing and

Original Article

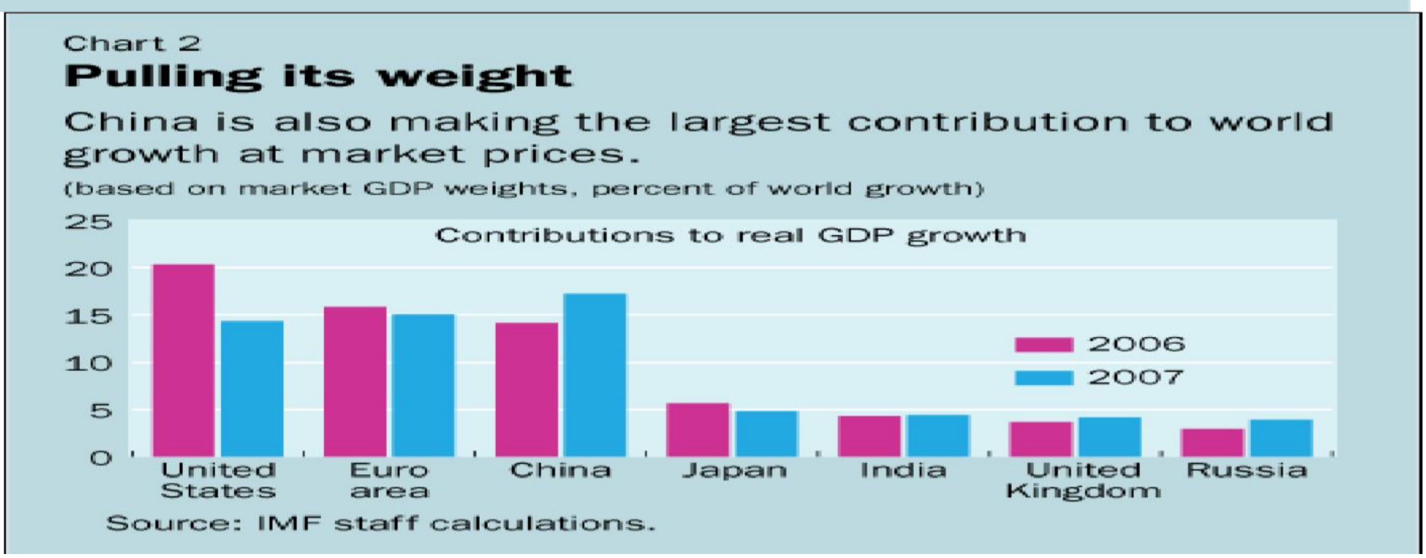
ten other cities have become out of bounds for middle class, according to a survey. Statistics reveal a 25 per cent hike in real estate investment from 2005 to 2006 and in the last six months construction activity was taken up in about 1.41 billion square feet.

Conclusion:

No doubt capital will create economic growth but for the countries like India and China development is more important, and the development should be inclusive and equitable in terms of social, geographical aspects.

FDI has created a flutter in the Communist country, for sure and the development was achieved by swimming against the stream. China has now achieved fourth place in world in GDP, third in international trade, second in FDI and is first in exports and imports. But within the country there is social divide and dissent is growing. This is going to be a hindrance to the country. Bearing this in mind, China has taken up remote area development besides focusing on rural areas. It has started the exercise of narrowing regional inequalities and has plans to ban FDI in some core areas. The country which preached to development through FDI is now trying wriggle out of the web FDI created wealth. The way China is now reciting the socialist mantra vouches that FDI has created further complications in the social structure of the country.

Charts and Tables



Original Article

References

Callen, T. (2007, January 15). Emerging markets: Main engine of growth. IMF Survey Magazine.

Chen, L. H. (1979, July). Law on joint ventures using Chinese and foreign investment. In Proceedings of the Fifth National People's Congress (2nd session). Beijing, China: National People's Congress of the People's Republic of China.

Zhang, Y. M. (1986, October 11). Provisions of the State Council of the People's Republic of China for the encouragement of foreign investment. Beijing, China: State Council of the People's Republic of China.

Wang, Q. (1986, April 12). Law of the People's Republic of China on enterprises operated exclusively with foreign capital. In Proceedings of the Sixth National People's Congress (4th session). Beijing, China: National People's Congress of the People's Republic of China.