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Roaring tigers, rising dragon

By Tilak Abeysinghe

IN 2003, then Malaysian Prime Minister Mahathir Mohamad expressed a general concern in the region. "There is a tendency in Malaysia to say: 'Well, we are not attracting enough foreign direct investment because it is all going to China.' That is true," Tun Dr Mahathir said.

In the wake of the 2008-09 global financial crisis, when Beijing adopted measures to help China's exporters, that caused serious concerns among its Asian neighbours, Indonesia in particular.

A China that sucks up foreign direct investment (FDI) and produces low-cost exports to compete in the same American and European markets they target is one of the fears of China's Asian neighbours. Despite these concerns, data suggests that China's economic role in the region has been more complementary than competitive.

FDI inflow into China rose from about US$2 billion in 1986 (the year China applied to enter the General Agreement on Tariffs and Trade, the predecessor of the World Trade Organisation) to more than US$108 billion (S$152 billion) in 2008. That is phenomenal for a developing country. In comparison, FDI inflow into Singapore increased from US$17 billion in 1986 to US$23 billion in 2008.

Whether China has been diverting FDI away from other Asian countries is a question some researchers have addressed. After carrying out an extensive data analysis presented in an International Monetary Fund working paper in 2005, Dr Benoit Mercereau concluded that China did not have much impact on FDI flows to other countries. Nevertheless, he finds some negative impact on Singapore's and Myanmar's FDI inflows.

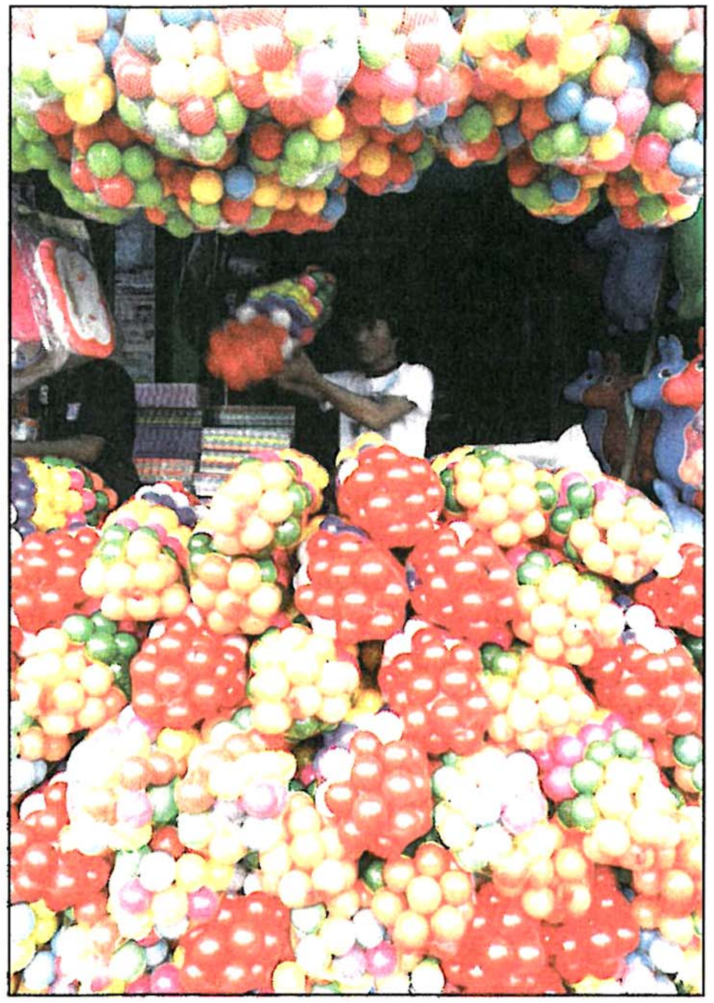
Singapore's share of FDI in the world, however, does not show any downward trend between 1986 and 2008. Singapore's share has fluctuated around 2 per cent and does not show any significant relationship with China's share, which shows only a mild upward trend over this period. Actually, some have argued that a substantial portion of China's FDI inflow consists of Chinese funds making round trips back to China so as to take advantage of the concessions Beijing gives to foreign investors.

The incremental benefits that China has brought to others by opening up its market have been larger than the benefits others have brought to China.

If FDI flows to China did not make much of a dent on FDI flows to other Asian countries, the next question to consider is whether China's expanding trade has affected other Asian countries competing in the same export markets.

Trade data does not reveal the full supply-chain impact of one country on its trading partners. To account for the full impact, I computed the multiplier effects of gross domestic product (GDP) growth in one country spreading to other countries through trade. My calculations indicate, for example, that a 1 per cent growth in China's GDP transmitted (directly and indirectly through other trading partners) a 0.43 per cent growth to Indonesia based on 1986 trade patterns and 1.98 per cent growth based on 2006 trade patterns.

This analysis reveals a number of important points. First, with shifting trading patterns, China's GDP multiplier effects, once relatively small in 1986, have grown at impressive rates over the two decades. Significantly, these effects actually accelerated after China's entry to WTO in 2001.



Cheap toys from China for sale at a Jakarta market. Data suggests that China's economic role in the region has been more complementary than competitive. PHOTO: REUTERS

Second, the multiplier effects based on 2006 trading patterns show that China has overtaken Japan in generating beneficial effects on most of its trading partners.

Third, the loss of Japan's foothold in these countries is more pronounced than that of the United States and other Organisation for Economic Cooperation and Development countries.

Fourth, the multiplier effects generated by the Asean-4 economies – Indonesia, Thailand, Malaysia and the Philippines – and the NIE-4 (Newly Industrialised Economies) – South Korea, Taiwan, Hong Kong and Singapore – also have grown over this period, but their magnitudes remain well below that of China's. This indicates that despite the large difference in per capita incomes between China and these countries, China could offer substantial benefits to its trading partners because of the sheer size of its market.

Fifth, the incremental benefits that China has brought to others by opening up its market have been larger than the benefits others have brought to China.

As the Chinese economy powers ahead, it will need more imports for both export production as well as domestic consumption. Despite the interest expressed in the 1996-2000 five-year plan to boost the GDP share of domestic consumption, that share has continued to fall. After seeing the fragility of a purely exports-driven growth strategy during the 2008 financial crisis, Chinese policymakers are now more determined to boost domestic demand, including consumption.

Given this fact, the positive multiplier effects of an open China on its trading partners are likely to increase further in the coming years, not diminish.

The writer is the deputy director of the Singapore Centre for Applied and Policy Economics, Department of Economics, National University of Singapore. The seven-part ST-NUS Economics Department Series On China's Economy will appear on Tuesdays and Thursdays this month.