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FOREIGN DIRECT INVESTMENT INTO CHINA: POLICY, DEVELOPMENT AND ACCESS TO THE WORLD MARKETS

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ABSTRACT

Promotion of foreign direct investment inward into China is a significant part of open door strategy of the country. China has become one of the most important destinations for foreign direct investment since especially 1990s. Therefore, in this study China's foreign direct policy and it's the effects on FDI inflow will be examined. Furthermore, the role of the foreign direct investment on the openness of China to world markets and. the study is to assess what extent FDI inflow into the country has been affected by WTO membership of China will be assessed.

Key Words: Foreign Direct Investment, China, Open Door Strategy

ÇİN'E YÖNELİK DOĞRUDAN YABANCI YATIRIMLAR: POLİTİKA, GELİŞİM VE DÜNYA PAZARLARINA ULAŞIM

ÖZET

Çin'e yönelik doğrudan yabancı sermaye yatırımlarının teşviki ülkenin açık kapı stratejisinin önemli bir parçasıdır. Çin özellikle 1990'lardan sorar doğrudan yabancı sermaye yatırımları için önemli bir çekim merkezi olmuştur. Bu nedenle, çalışmada Cin'in doğrudan yabancı sermaye politikası ve bunun doğrudan yabancı sermaye yatırımlarına etkileri incelenecektir. Ayrıca çalışmada yabancı yatırımların Çin'in dünya pazarlarına açılımı üzerindeki rolü ve Dünya Ticaret Örgütü (DTÖ)'ne üyeliğinin ülkeye yönelik doğrudan yabancı sermaye yatırımlarını ne düzeyde etkilediği değerlendirilecektir.

Anahtar Kelimeler: Doğrudan Yabancı Yatırımlar, Çin, Açık Kapı Stratejisi

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INTRODUCTION

Foreign direct investment (FDI) is one of the important policy elements of China's open door strategy which began in 1979. This strategy is a broad package. Therefore, it requires a detailed analysis of its key elements such as foreign trade liberalization, FDI policy, and the development of the tourist industry etc. This paper focuses on only the FDI, for it is impossible to analyze all of the components of the open door strategy.

While foreign direct investment flows in China began in 1979, it has grown rapidly especially since 1991. In the next eleven years, annual contracted foreign direct investment increased from 11.9 US$ billion in 1991 to 82.7US$ billion in 2002 and annual arrived foreign direct investment rose from 4.3 US$ billion in 1991 to 52.7US$ billion in 2002. The cumulative arrived FDI reached 446.3 US$ billion by the end of 2002.

China was the largest FDI recipient country in the world in 2002, amounting almost 53US$ billion. As many of economists believe, foreign direct investment plays an important role in China's economic development. China also turned to be the largest recipient of FDI in the developing world. The FDI inflow to mainland China in 2006 was 69.47 billion US dollars, which was 18% of the developing countries and 5.32 % of the world. The accumulated FDI inflows to China until 2006, reached 293 billion US dollar, constituting over 9.27 % of total FDI into all developing countries, 2.44% of the world total FDI stocks (UNCTAD, 2007).

1. OPENNESS, FDI POLICIES AND REGULATIONS IN CHINA

The implementation of the principle of "self reliance" between 1965 and 1978 excluded all foreign capital from China. 1978, however, marked an historical turning point for China, as the country announced a dramatic programme for reforming its economic system and opening its economy to the world (Wang Zhen, 1995: 33).

Beginning the early 1979, the government began to adopt an experimental approach or so called "crossing the river by feeling the stones under the water" combining "activeness" and "caution". Reforms have occurred step by step, often province by province; with liberalization occurring first in agriculture and only later in the banking and state enterprises sectors; foreign investors were to be permitted into China in a step by step process; initially in a few designated Special Economic Zones (SEZ) regarded as "experimental labs" where business could be carried out with little state interference and much preferential treatment. If things worked well in these SEZs the practice could then be extended into other parts of the country (Wang, 1985: 4-5). In mid-1979 the Chinese government promulgated The Joint Venture Law; which was the first formal statement of commitment to foreign investment by the government. It established the principles and procedures for foreign investment. Under this law, foreign investment are permitted and encouraged in selected fields (Sun, 1988: 13).

Moreover, the four SEZs were established Shenzhen, Zhuhai, Shantou and Xiamen. The Yangtze River Delta, Zhu River Delta and three other regions in Fujian, Liaonian, and Shandong were opened to foreign investment in February 1982.

However, the regulatory environment for foreign investment was still quite restrictive, with restrictions on foreign equity share in joint ventures (generally less than 50 percent) and industrial scope (FDI was not permitted in finance and banking, transportation, telecommunication-post, and retail). There also restrictions on FIEs access to the domestic markets as well as their use of local labor and land. In 1983, Chinese government put the Joint Venture Implementing Regulations into effect in order to improve the investment environment. The Implementing Regulation legally clarified the status of joint ventures and provided greater detail about China's policy on important issues such as profit penetration, technology transfer, and foreign exchange. In April 1984, the Chinese government announced that 14 coastal cities (including Dalian, Qinhuangdao, Tianjing, Yantai, Qingdao, Lianyungang, Nantong, Shanghai, Ningbo, Wenzhou, Fuzhou, Guangzhou, Zhanjiang, and Beihai) would open to foreign investment, expanding the open door policy from SEZs to other coastal regions (Sun, 1988, 13-14).

This was designed to attract further foreign capital, technology and management in order to improve overall economic development in these coastal cities, and to develop an export base that would generate foreign currency earnings and meet rapidly growing capital needs. Following the approach adopted in SEZs, the 14 cities were given more autonomy in economic decision-making. They could initiate and approve FDI projects up to a stated level of capital investment. In 1986-87, when priority was given to the task of "improving the domestic investment environment", the central government took several resolute steps towards controlling FDI. An attempt was made to bring foreign trade under better control by imposing stricter regulations on foreign exchange allocation in 1985. In 1986 a more restrictive import and export licensing system, and strict controls on bank credits and loans to foreign-invested enterprises (FIEs) were implemented. Foreign investment projects in hotel construction and other travel services were abandoned or placed under strict control (Whang Zhen, 1995, 39-40).

All these policy adjustment had a very negative impact on FDI growth. In order to maintain investor's confidence, the government launched a number of efforts to increase FDI by reformulating its policies. Although a FIE was allowed to sell its products in the local market, but if this represented a significant share of its output, the FIEs faced great difficulty in converting profits realized in local currency into hard currency, which was necessary in order to remit profit home. In order to help FIEs to achieve a balance between foreign exchange revenue and expenditure and to facilitate the remittance of profits abroad, on 15 January 1986 the government promulgated the "Regulations on Joint Ventures" Balance of Foreign Exchange Revenue and Expenditure (Mr He, 1987: 6-7).

On April 1986, the government took another step forward by publishing 'The Law of the People's Republic of China on Wholly Foreign-owned Enterprises' (WFOEs) which allowed foreign investors to establish WFOEs while protecting their investment, profits and other lawful rights and interests in China. This law stipulated that all WFOEs were to be free from interference in their operation and management activities, provided they opened account books in China and paid taxes according to the relevant regulations; and would accordingly enjoy preferential treatment concerning taxation exemption and deduction. The most important laws during this period were the "Provision of the State Council on the Encouragement of Foreign Investment" (the 22 Provisions) promulgated on 11 October 1986, followed by 13 detailed regulations published in the following year or so. "The 22 Provisions" provided more specific measures for coping with a comprehensive set of problems; such as enterprise autonomy, profit remittances, labour recruitment, and land use. Most of the provisions simply reemphasized the incentives and regulations already in existence or provided additional investment incentives to foreign investors. During the ex-Party leader Zhao Ziyang's inspection trips to the coastal provinces in the winter of 1987-88, he made frank comments on the need to promote a wider economic opening towards the outside world and launched the "Coastal Development Strategy", based on the theory of "Great International Circulation". This strategy declared the entire coastal strip (including the Yangze River Delta around Shangai, The Pear River Delta near Guangzhou, the Southern Fujian triangle, and the Liaoning and Shandong Peninsulas) would be opened up to foreign investment. This strategy called for "(placing) two heads outside" –relying on the outside world for both input supplies and market outlet, and declared that China could fallow the path of South Korea, Taiwan, Hong Kong and Singapore in order to benefit from the international investment and commodity follows and generate extra foreign earnings for domestic finance, without exposing the centralized industrial core to the outside world (Kueh, 1992: 638). The central government also decided to make Hainan -China's second largest relatively underdeveloped island- the biggest SEZ and a separate province providing an even better investment environment with additional incentives to enhance development (Whang Zhen, 1995, 41-42).

The 1988 "Coastal Development Strategy" stirred up some new expectations among foreign investors (Southerland, 1988:A1, A30). Especially small and medium-sized investors willing to exploit the cheap labour resources of the country responded immediately to this new drive. As a result, FDI flows into China boomed in 1988 and the early of 1989. But it was abruptly interrupted first by the adoption of a rectification and readjustment programme in late 1988 and then by the political upheaval of "Tiananmen Square Event" on June 1989. Moreover, since the early 1990s, China has allowed selected provincial governments to establish Economic and Technology Development Areas (ETDAs), offering tax and duty concessions to exporters and foreign investors. During this period the Chinese government continued to improve the FDI legal framework. The "Regulation Concerning Charging and Settling in Foreign Currencies within the Territory" promulgated on 1 March 1989 stipulated that a JV could apply to sell its products within China in foreign currencies, as long as its products were a substitute for imports within the state plan, or could be sold to the SEZs, ETDAs and other FIEs, or could be used instead of imported materials and parts for local manufacturing enterprises. "The Regulation Concerning FIEs Opening a Foreign Exchange Account Outside China" promulgated on 1 March 1989 allowed FIEs in China to open banking accounts outside China if required by their special business needs. "The Law of the People's Republic of China on Sino-foreign Contractual Joint Ventures" promulgated on 13 April 1989 encouraged foreign investors to establish export-oriented or technology-advanced manufacturing CJVs in China. Since the early 1990s, the government has made further special efforts to expand economic and technological cooperation and promote FDI by strengthening FDI regulations. The government, first of all, strengthened FDI regulations by revising "The Law of the People's Republic of China on Equity Joint Ventures" on 4 April 1990. In December 1990, the central government promulgated another regulation "Detailed Rules and Regulations for the Implementation of the People's Republic of China Concerning Joint Ventures with Chinese and Foreign Investment. In April 1990, the Chinese government made a decision of developing and opening up the Pudong New Area –A triangular area lying to the east of the Huangpu River in Shanghai- as the priority in China's economic reform in the 1990s in order to turn Shanghai into an international hub for finance, economy and trade (Wang Zhen,1995, 43-45).

Deng Xiaoping called for more reform and the further opening of the Chinese economy during his tour of Southern provinces of China. Since then, China has developed a new framework for opening up its economy to the outside world. Early in 1992, central government made further efforts to encourage export-oriented and technologically advanced FIEs in China. Foreign investors were to be allowed to operate in specific sectors, such as wholesaling and retailing, accounting and information consultancy, banking and insurance. Beijing, Shanghai, Tianjin, Guangzhou, Shenzhen and Zhuhai were also granted approval rights for FIEs in tertiary sector. Furthermore, administrative procedures have been simplified and decentralized in order to create a more conduct commercial environment and reduce bureaucratic complexity (Wang Zhen, 1995, 43-45).

To direct foreign investment to go along with the development scenario of Chinese industries, in June 1995 the Chinese government promulgated the Interim Provisions for Guiding Foreign Investment. The industrial projects in the catalogue are divided into four categories- the encouraged, permitted, restricted and prohibited. In late 1997, the Chinese government revised this catalogue in line with the development of the national economy. The revised catalogue reflects expansion in the investment scope encouraged by the state and highlights priority industries. It embodies the principles of compliance with structural readjustment, of being conducive to the introduction of advanced technology, and encouragement of foreign investment in China's central and western areas. In order to coordinate economic development in different areas, Chinese government is encouraging foreign investment in central and western China. The state has approved and issued the Catalogue of Advantageous Sectors for Foreign Investment in Central and Western regions. Projects included in this catalogue enjoy the same policy as offered to projects of encouraged category in the industrial catalogue for foreign investment, and favorable tax policy applies to import of necessary equipment, parts, spares and technology used in such projects. To encourage transnational companies to invest in China and attract advanced foreign technology and management experience, the Ministry of Foreign Trade and Economic Cooperation promulgated in April 1995 Provincial Regulations Concerning Establishment of Foreign Funded Investment Companies, permitting foreign investors to establish investment companies in China. In 1999, The Ministry of Foreign Trade and Economic Cooperation made amendments to the Provincial Regulations in order to expand the functions of such investment companies China entered the WTO on December 2001. As a result, the Chinese government is reexamining its existing laws and status in accordance with the framework of the WTO. It has abolished certain absolute laws and regulations and will gradually revise the laws and regulations that are incompatible with the rules of the WTO. For instance, in 2000 China revised the Law of the People's Republic of China on Chinese-foreign Contractual Joint Ventures and The Law of the People's Republic of China on Wholly Foreign-owned Enterprises, and discarded certain restrictions regarding the balance of foreign exchange account and localization of supplies in 2001. The Law of the People's Republic of China on Chinese-foreign Equity Joint Ventures was also revised (20 Questions on Investing in China, 2001: 5).

In the report, Premier Zhu Rongji stressed that the nation will stick to the path of reform and opening up. Zhu also called for efforts to open wider to the outside world and support multiple forms of cooperation between Chinese enterprises and transnational corporations. It said the government should continue to actively and effectively use foreign capital, emphasize bringing in advanced technologies, modern managerial expertise and specialists. He also said that vigorous efforts should be made to improve our investment environment and standardize procedures for attracting investment (China Daily, 2003: 1-6).

Furthermore, in early March 2003 First Session of the 10th National People's Congress (NPC) and Chinese People's Political Consultative Conference were held in Beijing. Both of them have great importance for China in the next years. At the sessions, the NPC deputies and the CPCC members discussed and endorsed a series of reports and proposal that are closely tied to the development of China in the future. One of them was former Premier Zhu Rongji's Report on the work of the government that was also significance in terms of foreign direct investment.

After 2006, in particular in 2007, China conducted a series of policy adjustments related to foreign investment, mainly including: unifying the income tax of domestic and foreign-funded enterprises, upgrading processing trade by prohibiting and restricting the processing trade of certain products; adjusting the export valued added tax rebate policy by reducing the rate of export tax rebates on energy-intensive, high emission and resource-poor products; adjusting land use policy; promulgating and implementing the Labor Contract Law; and revising the Industrial Catalogue for the Guidance of Foreign Investment (WTO: Trade Policy Review Body, Report by China, 2008).

2. TRENDS OF FDI INFLOW IN CHINA

China's data on contracted and arrived FDI during the period of 1979 to 2002 are given in Table 1. The table shows contracted and arrived FDI grew from modest amounts in the late 1980s, the arrived value of FDI was about 3.4 US$ billion annually in 1989.

Although contracted foreign investment 4.078US$ million between 1979 and 1981, the arrived FDI inflow was approximated one fifth of the contracted FDI for the same period. China's policy towards liberalization of FDI regime has realized gradually therefore, regulatory environment for FDI was restricted and incomplete from 1979 to 1982. As a result, capital flows into China remained limited during that period. From 1983 to 1985, China's efforts to attract FDI were more vigorous. The opening up of 14 coastal cities brought about the first boom of FDI in 1984. As contracted value of FDI grew at a rate of 53% and 124% in 1984 and 1985 respectively, arrived FDI grew at 98% and 32% respectively. In 1985, contracted and arrived value of FDI reached 5.932US$ million and 1.661US$ million respectively. Arrived FDI inflow was approximated one third of the contracted FDI in 1985. Between 1983 and 1985, the number of projects increased rapidly from 470 to the grand total of 3.078. However, immediately following the period of 1982-1985, there was great decline of contracted and arrived FDI (Table 1). The overheated economic problems in 1986-87 led to a policy retrenchment that reversed the trend of FDI growth (Wang Zhen,1995, 33).

As shown in Table 1, contracted FDI had a negative growth rate in 1986. The contracted value of FDI drastically diminished to about 52%. You will note the difference between the above mentioned percentages as compared to the previous year. In addition, the number of the projects declined from 3.078 in 1985 to 1.498 in 1986 then, the contracted of FDI grew to 30.9% and the arrived value of FDI grew 23.5% in 1987. Moreover, the number of the projects increased from 1.498 in 1986 to 2.233 in 1987.

The second boom in FDI followed the introduction of the "Golden Coast" development strategy and increased preferential treatment of foreign investors in 1988 (Wang Zhen, 1995: 33). In 1988 the number of projects was about 2.5 times higher than 1987. The contracted and arrived value of FDI grew 42.8% and 38% respectively in 1988. This boom, however, was accompanied by high inflation and other domestic economic problems. The tragic political turmoil in the Spring of 1989 abruptly terminated the boom and curtailed FDI growth (Wang Zhen,age, 33). As a result, the number of projects decreased from 5.945 in 1988 to 5.779 in 1989. Growth rate of arrived and contracted value of FDI fell sharply to 5.7% and 6.2% respectively in 1989.

In recognition of the negative reaction of foreign investors to the worsened investment environment, the Chinese government issued the Amendments to the Joint Venture Law in April 1990. These amendments codified several rules designed to encourage investment. Particularly important was the elimination of the duration limit applied to some ventures, and granting of permission for foreigners to act as joint venture board chairmen (Robertson and Chen, 1990: 487-488).

In April 1991, The Income Tax Law for Enterprises with Foreign Investment and Foreign Enterprises (The Unified Tax Law) was passed by the People's Congress of China. This tax law, as the most significant tax legislation for a decade, replaces both the foreign enterprise and joint venture income laws, which had governed foreign operations in China since the early 1980s. It standardized the income tax rates for different forms of FIEs, and eliminated the prior tax discrimination against the wholly foreign-owned enterprises (WFOEs), which had previously been subject to unfavorable treatment. In addition, the Chinese government concluded the austerity program in early 1991 and replaced it with a promotion for investment through loosening the control over the domestic loans and opening up the domestic market to foreign investors (Sun,1988, 16-17).

In 1992, the growth rate of foreign investment even was more remarkable. Following Deng Xiaoping's "grand tour" of the south early that year, the central government adjusted the economic policy in order to speed up economic reform and to further open the economy to foreign investment. Consequently, the policy on FDI became more favorable. The new policy permits foreign companies to invest in fields such as retailing, real estate, trading, transport, finance and banking, and also permits them to establish stock-holding companies and secondary business to foreign affiliates (M. Hirano, 1993: 2-8). In September 1992, the Chinese government announced the adoption of the "socialist market economy" strategy and began to build a legal framework to standardize market operation. Regulations covering corporation law, bankruptcy law, individual income law and stock trading law, and some other commercial regulations have been passed since 1993 (Sun, 1988, 17).

China attracted a greater inflow of FDI both on the year 1990 and almost the years following; which is largely due to the congenial investment environment of China. The contracted value of FDI grew to 17.7% in 1990 and further grew to 81.5% in 1991. Moreover, arrived value of FDI grew 2.8% and 25% respectively in the same period. Even more impressively, the contracted and arrived FDI increased considerably by 385% and 152% respectively in 1992. In 1992, the growth rate of contracted and arrived value of FDI reached its peak during the period of 1979-2002. Furthermore, the contracted value of FDI increased from 58.124US$ million in 1992 to 111.436 US$ million in 1993. The contracted value of FDI in 1993 exceeded the cumulative total value of FDI during the period 1979 to 1992. The arrived value of FDI also reached a high value, amounting to the sum of 27.515 US$ million in 1993. From 1993 to 1998 the growth rate of arrived FDI dramatically decreased from 150% to 0.46% respectively. In comparison to the 1998 value, arrived FDI growth rate was a negative value of 11.3% in 1999.

Table 1. Contracted and Arrived Foreign Direct Investment in China 1979-2002

Year	Number of Projects	Contracted Value (US$ Billion)	Arrived Value (US$Billion)
1979-1981	783	4.078	0.738
1982	139	0.53	0.43
1983	470	1.732	0.635
1984	1.856	2.651	1.258
1985	3.078	5.932	1.661
1986	1.498	2.834	1.874
1987	2.233	3.709	2.314
1988	5.945	5.297	3.194
1989	5.779	5.6	3.392
1990	7.273	6.596	3.487
1991	12.978	11.977	4.366
1992	48.764	58.124	11.007
1993	83.265	111.436	27.515
1994	47.549	82.680	33.767
1995	37.011	91.282	37.521
1996	24.556	73.276	41.726
1997	21.001	51.004	45.257
1998	19.799	52.102	45.463
1999	16.918	41.223	40.319
2000	22.347	62.380	40.715
2001	26.140	69.195	40.878
2002	34.171	82.768	52.743
2003	41.081	115.07	53.505
2004	43.664	153.5	60.6
2005	44.019	189.0	60.3

Source: State Statistical Bureau (SSB): Statistical Yearbook of China, Ministry of Foreign Trade and Economic Cooperation**,** (MOFCOM, mws[1], 2009)**,** (CHINABILITY, mws, 2009)

[1] Editorial note, _mws_ is abbreviation of "Mentioned Website"

In addition, the number of projects declined from 83.265 in 1993 to 16.918 in 1999. The number of projects continued to decrease during this period. One of the consequences of the Asian financial crises was that the FDI inflow in China was adversely affected during 1997 and 1998 (See Table 1). After this setback, not only did the contracted value of FDI grow to 10.9%, and the arrived value of FDI grow to 15.1% but also the number of the projects grew to the rate of 17% in 2001 compare to the previous year. Furthermore, contracted and arrived value of FDI reached 82.7US$ billion and 52.7US$ billion respectively in 2002. A further surge in FDI preceded and accompanied China's accession to the WTO in December 2001, promoting China to top position as an FDI destination in 2003. In 2003, China has overtaken the US as the number one destination for FDI (Prasad and Wei, 2005). In 2005 the arrived value of FDI reached 60.3 billion US $ (Table 1). In 2006, China was the third largest recipient of FDI in the world, after the United States and the United Kingdom.[2] China has continued to provide a business environment conducive to FDI, which, often embodying new technology has consequently played a key role in the country's economic development. Foreign investment has been encouraged particularly in manufacturing with particular emphasis on high value-added production (WTO, 2008: 38).

3. MAIN SOURCES OF FDI BY COUNTRY

Throughout the period of 1979-2000, Hong Kong SAR (Special Administrative Region) has always been the most important source of FDI in Mainland China. It contributed 48.50 % of the total cumulative contracted investment and 48.89% of the total cumulative arrived investment respectively. Other important sources of FDI include the U.S., Japan, Taiwan province and Singapore. They accounted for 8.96%, 5.74%, 7.07%, 5.23% of the total cumulative contracted investment and 8.62%, 7.98%, 7.51%, 4.88 % of the total cumulative arrived investment respectively. East Asian economies dominate FDI to China. Combined together, they contributed over 65% of both total cumulative contracted and arrived investment (MOFTEC, 2001). The top eight countries/ investing in China by the end of 2006, in order of realized investment, are: Hong Kong (US$279.77 billion), Japan (US$57.97 billion), the Virgin Islands (US$57.16 billion), USA (US$53.95 billion), Taiwan (US$43.89 billion) (Dang, 2008: 7).

4. SECTORAL COMPOSITION OF FDI IN CHINA

During the period of 1983 to 1987 the agreement of FDI by sector was mainly focused on the tertiary sector, after that time secondary sector value exceeded the tertiary sector value. The secondary sector then became the major focus of FDI agreement during 1988-2001. Cumulative value of contracted FDI in this sector reached 482.4US$ billion during the period 1983 to 2001, fifty percent higher than the one in the tertiary sector.

Between 1988 and 2001 the secondary sector accounted for 69% on average of total agreement of FDI in China. The major component of the secondary sector was industry. This industry sector in China has included manufacturing, mining and quarrying, as well as the production and supply of electricity, water and gas.

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[2] In 2006, inflows of FDI into China were US$69.4 billion; those into the United States and the United Kingdom were US$175.4 billion and US$139.5 billion, respectively (UNCTAD 2007).

Table 2. Sectoral Composition of Contracted FDI in China 1983-2001

(In millions of US Dollars)

Sector	1983-87	1988-91	1992-93	1994-95	1996-97	1998-99	2000-01
Primary Sector(1)	410	673	1.870	2.708	2.130	2.675	3.245
Secondary Sector(2)	6.147	24.378	89.558	109.859	88.426	63.783	100.267
Tertiary Sector (3)	11.063	4.419	78.134	61.395	33.723	26.867	28.062
Total	17.620	29.470	169.562	173.962	124.279	93.325	131.574

Notes: 1. Primary sector: agriculture (including farming, forestry, animal husbandry and fishery), 2. Secondary sector: sector (including mining and quarrying, manufacturing, production and supply of electricity, water and gas) and construction, 3. Tertiary sector: all other industries not included primary and secondary sector (circulation sector and service sector)

Sources: MOFTEC, Almanac of China's Foreign Economic Relations and Trade, 1984-1995, and SSB: China's Statistical Yearbook 1990-2002.

Since mid 1990's, FDI recipient of tertiary sector has not significant as beginning of the reform period. As shown in the table 2, the agreement of FDI in the tertiary sector accounted for 62% during the period of 1983 to 1987 in China. The FDI's share in this sector declined 28% on average in the period from the mid-1990s to 2001. The primary focus of FDI in this sector has been real estate management and public services for the last two decades. FDI agreement in primary sector accounted for only 2% on average during the period of 1983 to 2001.

5. FDI IMPACT OF ACCESS THE WORLD MARKETS

The small amounts of foreign direct investment in the late 1970s and early 1980s initially made a negligible contribution to China's total exports. As late as 1985, six years after the passage of China's foreign investment law and five years after the establishment of special economic zones, the exports of foreign invested enterprises were only 320 US$ million, barely 1% of China's total exports (Lardy, 2000: 499). FIE's share in total exports increased dramatically, reaching 133.2 US$ billion by 2001, which at that time was equivalent to 50% of China's total exports. FIE's share of China's total imports also rapidly increased especially in the 1990s. In 1985, the imports value of FIE's was 2.06US$ billion, about 5 % of China's total imports. In 1990, imports of FIE's accounted for 23.07% of total imports, amounting 12.81 US$ billion. Moreover, the imports value of FIE reached 117.3US$ billion in 2001, 52% of China's total imports. Imports by foreign invested enterprises were relatively higher than the exports of the same period of 1985 to 2001 (Table 3).

There has been a significant growth in China's foreign trade since 1978. The total trade (equivalent to exports plus imports) grew from 21US$ billion in 1978 to 509.8US$

billion in 2001. Between 1985 and 2001, the trade share of China's GDP also increased considerably. The total trade value divided by the gross domestic product (GDP), gave a ratio of 9.89 % in 1978, 24.15% in 1985 and further 44% in 2001. The simplest measure of the economic openness is received by calculating imports plus exports as a share of the GDP. This measure also indicates to what extent China really has become integrated into the world's economy. As shown in the Table 3, China's integration within the world's economy has dramatically increased since 1985. The acceleration in FIE's share in total trade shows the growing contribution of FIEs in the increase of China's integration in the world market.

Table 3. Foreign Trade of Foreign Invested Enterprises 1985-2001

Year	Billions of US$	Percentage of Total Exports	Billions of US $	Percentage of Total Imports
1985	0.32	1.1	2.06	4.9
1986	0.48	1.6	2.43	5.7
1987	1.20	3.0	3.12	7.2
1988	2.46	5.2	5.75	10.4
1989	4.92	8.3	8.80	14.9
1990	7.80	12.5	12.81	23.1
1991	12.10	16.8	16.91	26.5
1992	17.40	20.4	26.37	32.7
1993	25.24	27.5	41.83	40.2
1994	34.71	28.7	52.93	45.8
1995	46.88	31.5	62.94	47.7
1996	61.51	40.7	75.60	54.5
1997	74.90	40.9	77.72	54.6
1998	80.96	44.0	76.72	54.7
1999	88.63	45.4	85.88	51.8
2000	119.44	47.9	117.27	52.1
2001	133.23	50.0	125.86	51.7

Source: State Statistical Bureau (SSB): China's Statistical Year Book, Various Years.

Moreover, studies (such as Lardy 1996, and Liu et al. 2001) have shown that foreign-invested firms have contributed significantly to China impressive export expansion and economic growth. Using panel data at the provincial level in the period of 1986-97, Tse, et al. (1997) proved inward FDI positively affect provincial manufacturing export performance. However, Sun (2001) argued the role of FDI changes across the regions in China. Although FDI shows a positive and significant impact on exports from coastal region to the central region, its impact on the western region is found to be insignificant (Li, 2003: 1).

6. DEVELOPMENT OF FDI AFTER WTO MEMBERSHIP OF CHINA

After long period negotiations, China has completely begun to join world economy. China's entry into World Trade Organization (WTO) will make China more open. As a result of the membership, China has agreed to fulfill a series of obligation.

China will give equal treatment to every WTO member. All individual and institutional foreign investors will enjoy at least the same treatment in terms of trading rights as domestic enterprises. China will make significant reductions in tariff and non tariff barriers and eliminate of export subsidies (China Economic News, 15 October, 2001: 3).

By joining the WTO, China commits to reduce its industrial tariffs to an average rate of 9.4 percent by 2005. In information technology, tariffs on products including computers, semiconductors and all internet-related equipment will reduce to zero by the end of 2005. For agricultural products, tariffs will reduce from an average level of 31.5 percent to 14.5 percent. Foreign firms will also be granted full rights to engage in distribution activities in China, including wholesale, retail and after-sale service, repair, maintenance and transport. They will also be permitted to control their own distribution networks in China. China is also committed to opening its telecommunication sector to foreign investment. With the WTO agreement, China will allow foreign participation in all telecommunication services and will allow 50-percent foreign ownership for value-added paging services in two years. For mobile services, China will also allow 49-percent foreign ownership in 5 years. With the WTO agreement, China will allow 50 percent foreign ownership of life insurance companies. Foreign life insurance companies will be allowed to choose their own domestic joint-venture partners. For non-life insurance, China will permit 51-percent foreign ownership. In banking, China will allow foreign banks to conduct local currency business with Chinese enterprises. China will also allow minority foreign-owned joint ventures to engage in fund management under the same conditions as domestic Chinese firms. China agrees to implement WTO agreement on trade-related investment measures. From this point of view, trade and foreign exchange balancing requirements and local content requirements to some foreign direct investors will be abolished. Laws related to the transfer of technology will also have to be in accordance with the WTO agreement on the protection of the intellectual property rights (K.C. Fung, 2002: 16)

Since January 1st, 2008, China has basically fulfilled its commitments of tariff reduction for WTO entry, with the overall level of tariff rates down to 9.8%; of which, the average tax rate of agricultural products was 15.2% and that of industrial products was 8.92% (ADB, mws, 2008).

China also made substantial market access commitments of most sectors of its economy, especially service sectors. With more sectors open to foreign companies, FDI flows to China are thus expected to increase considerably. Non-financial FDI in China was $60 billion in 2005, thus registering a slight decline (from $60.6 billion). By contrast, flows into financial services surged to $12 billion, driven by major investments in Chinese banks. While the opening-up of the banking industry to FDI has happened gradually, it is only in the past two years that foreign banks have rapidly entered the Chinese market by acquiring ownership stakes in Chinese banks. By the end of 2005, 18 foreign financial institutions had invested in 16 banks. The largest deals involved four of the five top Chinese banks. The real estate industry has become another hot spot for FDI. According to the Ministry of Commerce (MOFCOM), inflows to China in this industry surged to $5.4 billion in 2005. This may still be an underestimation as the data do not include real estate purchases. According to the State Administration of Foreign Exchange (SAFE), purchases of real estate by foreign institutions amounted to $3.4 billion in 2005. If these were included, FDI in real estate would in fact be some $8.8 billion (UNCTAD, 2007: Investment Brief, Number 2: 1).

Before WTO membership, China's service sector has been largely closed to competition, both to domestic and foreign services competitors. Foreign services providers faced restrictions in licensing, equity participation, geographic location, business scope and operations. All these will be relaxed over time or eventually removed after a transition period.

In telecommunications, China's telecommunication corridor in Beijing, Shanghai and Guangzhou, which represents 75 percent of all domestic traffic, will open upon accession to all telecommunications services. Fourteen other major cities have been opened within one year after accession. Foreign ownership of joint ventures will increase over time, eventually reaching 49-50 percent, depending the types of services to be provided. At the same time, geographic restrictions will be eliminated gradually.

China will open its markets for financial services. In banking, foreign banks will be allowed to undertake foreign currency business with Chinese as well as foreign clients upon accession, and within two years after accession, foreign banks are allowed to conduct local currency business with Chinese firms. Full market accession will prevail within five years after accession; all business and geographic restrictions will be eliminated.

In insurances, foreign non-life insurance companies will be allowed to establish as a branch or as a joint venture with 51 percent foreign ownership and wholly foreign owned subsidiaries will be allowed within two years after accession. Foreign life insurance companies are allowed to take 50 percent equity share in a joint venture upon accession. Similarly, foreign ownership of 50 percent in joint ventures is allowed upon accession for brokerage for insurance of large scale commercial risks, reinsurance and international marine, aviation and transport insurance and reinsurance, to be increased to 51 percent within five years after accession. Wholly foreign owned subsidiaries will be permitted within five years after accession. A wide range of other services industries will open to foreign competition. These include distribution, travel, and tourism, professional services and audiovisuals (Worldbank, mws, 2003).

CONCLUSION

This paper confirms that open door strategy has accelerated the flow of FDI into China. China's government has made some regulations and promulgated some laws to attract foreign investment and technology. It has found that Chinese government use FDI policy for coordinate economic development through preferential treatment in different areas of mainland China.

As known, China is an attractive destination for foreign investors not only because of its fast growing national economy, and its relative advantage in labour and resources but also very stable political structure and stable currency. The most of FDI into China has came from overseas Chinese since 1979. After WTO accession, FDI of the other memberships of WTO has been considerably increased.

While the annual average of FDI inward flows over the period 1990-2000 was 30.1 billion US dollars, FDI inward flows into China in recent years have been much higher, 72.4 billion US dollars in 2005 and 69.5 billion US dollars in 2006 (UNCTAD 2007). The large amounts of foreign direct investment made a significant contribution to China's total exports. FIE's share in total exports increased dramatically, reaching 133.2 US$ billion by 2001, which at that time was equivalent to 50% of China's total exports. FIE's share of China's total imports also rapidly increased especially in the 1990s. In 1990, imports of FIE's accounted for 23.07% of total imports, amounting 12.81 US$ billion. However, the imports value of FIE reached 117.3US$ billion in 2001, 52% of China's total imports. The acceleration in FIE's share in total trade shows the growing contribution of FIEs in the increase of China's integration in the world market.

With the WTO agreement, China has further opened up domestic market. China's accession to the WTO supported to China to deepen economic reforms to carry out its WTO obligations it is obvious that China's WTO membership brought more FDI inflows from foreign countries to China. Therefore, China sustains the position as one of the most attractive destinations with respect to foreign direct investment in the world.

In terms of sectoral distribution of foreign investment in China has concentrated on secondary industries, but tertiary industries have become the latest destination for China-bound FDI. As China fulfills its WTO commitments, it will further open up the financial, insurance, telecommunications, energy, and water, commercial, accounting, auditing and legal sectors, which are expected to attract more foreign investment to tertiary sector.

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