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Research Article

Discussing on The Need of Examining the Effect of FDI on Western China

Zibo Ma

Corvinus University of Budapest, Hungary

Abstract: Western China, where the over-all economic performance is the most lagged-behind in the country, exhibits significant differences in status of FDI (Foreign Direct Investment) and factors attracting FDI compared with its Eastern counterparty. The positive effects of FDI on economy has been proven in the East during decades of rapid development, while the interaction of FDI with local economy in the West has not been sufficiently studied.

Keywords: FDI; Economy; Western China; Interaction

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[*]***Corresponding author:*** Zibo Ma, colinma2010@hotmail.com

1 Introduction

The interaction between incoming FDI and local economy has been studied extensively. The major focuses are the one-way relationship that how FDI promotes economic development, or the mutual-enhancing relationship between the two. Also a few studies pointed to the negative effects of FDI on local economy, or on the sub-categories of local economy (such as joint venture versus 100%-domestically-owned firms). Regardless of the economies being observed and conclusions reached, the key factors always center on issues such as recipient country (region)'s human capital (population & education), location, level of economic development, infrastructure, size of market, technology, degree of openness, labor cost, level of financial market development, etc. There is not sufficient detailed research on the effects of FDI on Western China, besides a few policy papers promoting FDI with rather-general analysis.

The absolute Gap between Western and Eastern China have been widening, regardless of the governments' emphasis and efforts such as 'developing the West' and 'shifting industries to the West' . The economic success of Eastern part of China is largely attributed to FDI, which has been proved by facts and reckoned by academy. While the Western region as a whole, still has insignificant FDI presence until today. The performance of FDI in the West is also lower than the performance of FDI in the East in terms of asset turnover, profitability, and other key performance indicators. Besides the results (FDI's presence and performance), the causes (drivers for FDI, or factors attracting FDI) also show significant differences across Western and Eastern China. Faced with such differences, it's reasonable to question whether FDI impacts West in the same way as it does to the East or not. Thus there is need to study the actual effects of FDI on local economy in the West, which should not be deemed as a copy of their Eastern counterparties.

2 Detailed comparison between Eastern and Western China

Eastern China consists of Beijing, Tianjin, Hebei, Liaoning, Shanghai, Jiangsu, Zhejiang, Fujian, Shandong, Guangdong and Hainan. Western China consists of Sichuan, Chongqing, Guangxi, Inner Mongolia, Guizhou, Yunnan, Shanxi, Gansu, Qinghai, Ningxia, Xinjiang and Tibet. The rest (within mainland China) belongs to Central China, which is not in the scope of discussion in this paper.

To start with, Western China should not be overlooked due to its size – it takes up nearly three quarters of China's total land area. After 'opening-up' since around 1980's, Chinese economy experienced rapid development, and most economic activities were concentrated in the East due to it's location advantages and being the first tier of areas to 'open up'. The gap between East and West has been widening since then, although Chinese government has been trying to balance the development between East and West. FDI has been especially 'unresponsive' – the increase of FDI in the West does not catch up with the efforts in 'developing the West', and thus the role of FDI in economic development in the West has been insignificant.

2.1 The distance in FDI stock

FDI districbution - Eastern and Western Region

	Eastern Region	Western Region		Absolute distance
Year	Value(billion USD)	Value(billion USD)	As a Percentage of East	Value(billion USD)
2005	538	28	5%	511
2006	598	30	5%	568
2007	664	34	5%	630
2008	742	40	5%	702
2009	819	47	6%	772
2010	909	56	6%	853
2011	1006	68	7%	938
2012	1098	78	7%	1020
2013	1195	89	7%	1107
2014	1293	99	8%	1194
2015	1399	109	8%	1290
2016	1508	119	8%	1390

Source: Ministry of Commerce of the People's Republic of China

2.2 The distance in economic performance

As discussed earlier, there exists significant gap in other economic indicators as well between East and West. Due to the limitation of precise data on aggregated regional level, the following table gave a quick overview of the West-East distance on regional level regarding a collection of both conventional and non-conventional economic indicators.

As of 2016			as a percentage of East
GDP (billion RMB)	East	456044160	\
	West	156461130	34%
Average disposable income (RMB)	East	28223.3	\
	West	16868.1	60%
Urbanization rate	East	62.20%	\
	West	44.80%	72%
Number of 'Top100' cities	East	61	\
	West	16	26%
Number of counties in poverty	East	66	\
	West	448	679%
Number of highly qualified universities	East	71	\
	West	24	34%

(Sinanews. 2017)

The data above shows the significant difference in the status of FDI between Eastern and Western China.

3 Analysis by drawing reflection upon existing studies

The effects of FDI have been extensively studied in various areas with a variety of emphases. Different studies are not highly interconnected on theoretical level (for example: J. Carbonell and R. Werner, 2018) because the practical effects are largely affected by the practical situation which consists of numerous variables which are not fully incorporated in the standard economic theories. However the methods adopted as well as prominent economic relationships identified in previous studies shed a light on current

research projects.

Audretsch (1998) Identified geographical proximity as a necessary condition to facilitate knowledge spillovers as 'knowledge is vague, difficult to codify, and often only serendipitously recognized' . However this geographical proximity refers to the distances between domestic firms and foreign firms, not necessarily the excellence of firm's locations themselves. Transmission costs increases with distance, thus the closer the domestic firms and foreign firms are, the easier and faster the spillover would be. In Western China firms are more scattered around due to its less density compared with East, however with the popularity of industrial parks and easy access under today's developed transportation network and information system, geographical proximity is not deemed as an important factor in analyzing the effects of FDI in this paper.

Competition is also a key factor which influences spillovers. Although the merits of competition differ in different studies. Aitken and Harrison (1999) found competition negatively impacts spillover – foreign firms reduce the productivity of domestic firms through competition effects. multinationals have lower marginal costs due to some firm specific advantage, which allows them to attract demand away from domestic firms, forcing them to reduce production and move up their (given) average cost curve (H, Gorg and D, Greenaway. 2003). In Aitken and Harrison's study, evidence of negative spillover was found in the case of Venezuela through a time period of fourteen years, while positive effect of competition was found by Kokko (1996) through the analysis of industry-level cross sectional data based on Mexico.

Technology gap is another key factor which shapes the story of spillover. As pointed out by Glass and Saggi (1998) – Any technology gap signals something to the MNE about absorptive capacity. The bigger it is, the less likely the host is to have the human capital, physical infrastructure and distribution networks to support inward investment. In response to technology gap, other relevant factors were also found to be crucial for spillovers. Other conditions being equal, the smaller the technology gap, the bigger the absorptive 'capacity'. Likewise, faced with same technology gap, the more intensive R&D domestic firms carries, the quicker the absorptive capacity is built up. Thus Kinoshita (2001), through the case of Czech Republic, found positive spillovers for domestic firms which are intensively engaged in research and development, while overall there is no significant spillover towards domestic firms.

Last but not the least, the openness of domestic economy is also a crucial factor for facilitating spillovers. One example is Barrios and Strobl (2002)'s study on Spain during 1990-1994, where the overall spillover is insignificant with the exception to exporters. The clear contrast between exporter and non-export shows the importance of exposure to international (foreign) market (competition) in driving technological advancement (where foreign firms excel), thus spillovers. This is especially the case for Eastern China. Details can be seen in following chapters.

4 Summary

The FDI-driven success in Eastern China has not copied its own story in Western China, and differences between these two regions renders the validity to examine the actual effects of FDI to local economy in Western China. The existing researches have reached no concrete formula in between 'FDI effect' and 'FDI factors', which further calls for the importance of the actual field study. However, a set of further questions needs to be considered in regard of the feasibility of the study such as how to obtain data on Western-regional level and how to pin down a specific sector to examine as opposed to analyzing on the general economy.

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