

PROMOTING THE REGIONAL ECONOMIC COOPERATION IN ASIA ADMIST ECONOMIC GLOBALIZATION

Chen Qingtai
Development Research Center of the Chinese State Council

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The economic globalization trend presents China both challenge and opportunity. China and its neighboring countries and regions are becoming increasingly interdependent in terms of industry and trade. Taking a greater part in economic globalization in order to promote the regional economic cooperation in Asia is a priority of the Chinese government and enterprises.

I. China is seeking a greater part in the course of economic globalization.

Over the past two decades China adopted the policy of opening to the outside world. The closed Chinese economy became open and the opening up gradually progressed in width and in depth. Many aspects of the country's production and operation were incorporated into the system of international division of labor. China thus became an active participant in economic globalization. In this period China's international trade increased by about 22 times. The country's dependence on foreign trade was 44% in 2001. The annual average utilization of foreign direct investment increased from less than US\$ 2 billion in the early 1980s to approximately \$40 billion now. By taking an active part in international division of labor, China promoted its economic restructuring and the adjustment of its industrial structure, created enormous job opportunities and enjoyed sustained economic growth. The country therefore shared the benefits of economic globalization.

China seized the initiative in the course of economic globalization because the Chinese government formulated the correct open policy in light of the country's comparative advantages and implemented it unswervingly. In order to solve the problems arising from the fact the Chinese economic system was not in line with international rules, China introduced the market mechanism first in selected areas such as special economic zones and development zones. This tactics of developing selected areas not only effectively encouraged the absorption of foreign capital and increased international trade but also played an exemplary role for the reform and opening up in the rest of the country.

In order to develop its economy, China used to rely mainly on its own enterprises and resources under the government leadership and tried to establish a complete and self-contained economic system. In order to develop national enterprises and keep the domestic market from being affected by foreign enterprises, China's national policy at that time focused on setting up trade and investment barriers to keep out foreign competitors. This remained unchanged for a long time even China made major policy adjustments during reform and opening up.

Since the 1980s, economic globalization has been developing rapidly. It is against this international background that China implemented its policy of reform and opening up for two decades. The Chinese have come to realize these fundamental facts: To develop its economy, a nation needs not only to mobilize its domestic resources but also to utilize international resources; participation in the international division of labor helps a country both improve its productivity and benefit from increased trade; the economic interest and competitive power of a nation are not merely embodied by the enterprises in which it invests but also in the joint ventures and wholly foreign-owned enterprises in the nation. Bearing this in mind, the national policy should be changed to gradually remove trade barriers, attract foreign investment, improve the market mechanism, lower transaction cost, take advantage of China's big market and cheap labor and take an active part in the international division of labor. On the one hand, China improved the allocation of its resources by means of the market. On the other hand, it made its environment more attractive to international resources and made its enterprises of all descriptions more

competitive.

Thanks to 15 years of unremitting efforts, China joined the World Trade Organization last December. Fundamentally speaking, that is a major strategy China takes to cope with the challenge and opportunity presented by economic globalization. More importantly, it is also an objective need of China to deepen reform, open wider to the outside world and promote its economic growth.

WTO membership will have three benefits for China:

First, China will have a relatively stable external economic environment. When China fulfils its commitment to the WTO, it has the fundamental right to the treatment as a WTO member. External economic relations governed by agreements and rules will help China to have stable expectations, stick to the orientation of reform, work out long-range programs, make more use of domestic and international markets and resources, and accelerate development.

Second, WTO membership will help the Chinese economy with comparative advantages to become more competitive. After China's entry into the WTO, major changes will take place in its industrial structure whereby resources are allocated through planning rather than the market. Allocation of resources by the market will not only enable Chinese industries to improve their specialized division of labor and social cooperation while taking a greater part in the international division of labor but also encourage more resources to go to industries and enterprises with comparative advantages so that they will become more competitive.

Third, WTO membership will boost the reform in China. Thanks to two decades of reform, a socialist market economy has been established preliminarily in China, but the tasks of the reform have yet to be accomplished. Promoting reform with opening up has been China's important secret for development for years. Fulfilling the international obligations China accepted for its WTO entry is exactly in conformity with the country's reform objectives and restructuring effort. Fulfilling the commitment and adjusting the rules will greatly expedite China's reform.

However, WTO membership is a double-edged sword as far as China is concerned. Neither excessive optimism nor indifference is advisable. As a member of the WTO, China has many unfavorable factors and some uncertainties and has to take up the three formidable challenges as follows:

First, making institutional transition and innovations. The institutional foundation of economic globalization is the market mechanism. We will not be able to share the benefits of economic globalization if we fail to reestablish main players of the market, improve the market mechanism and set up a market-oriented government administration system so as to form a unified market which is protected by law and encourages competition on an equal footing. However, the deep-seated conflicts involved in institutional transition will not be resolved overnight.

Second, adjusting the industrial structure and reorganizing enterprises. Traditional Chinese industries and enterprises are far from internationalized. In the past Chinese industries were distributed according to domestic or regional markets and sold what they produced. Although some changes were made after the policy of reform and opening up was introduced, much remains to be done to bring the industries into the system of global division of labor. The outstanding problems are excessive redundant investment, uneconomical scale of production, backward technology and equipment, and poor competitive power of products. If China wants to give full play to the comparative advantages of its industries, it must ascertain its position in the system of global division of labor. Effective resources must be concentrated in industries with an especially obvious scale of economy so as to have large scale of production and operation. Failure to adjust the industrial structure and reorganize enterprises will become the bottleneck for giving play to comparative advantages.

Third, improving the social security system. As a result of keen market competition, enterprises

with superior goods will survive whereas those with inferior goods will be eliminated and their workers will lose their jobs. Many scholars predict that after China joins the WTO, its problem of unemployment will become more conspicuous. They also predict that as changes have taken place in the distribution pattern of income, there will be new disadvantaged groups and more persons in poverty. While establishing the market system, it is therefore essential to improve the social security system. This must be made a fundamental national policy of China that should not be overlooked in the process of institutional transition. The Chinese government has attached great importance to this respect since the mid-1990s. However, with an urban population of 400 million alone, it is a challenging task for China to establish an effective social security system and an insurance system in endowment, medical care, unemployment, etc.

All this cannot reverse the overall situation in which WTO membership means more opportunity than challenge for China. This is because many of the challenges arising from WTO membership are problems China must solve for its economic growth and social development, and taking up these challenges is in conformity with China's economic development. In this sense, as a member of the WTO, China should follow a "proactive strategy." By this I mean the country should take the challenges as the motive force and opportunities for deepening reform and accelerating industrial restructuring. While striving for benefits of its WTO membership, it should seek solutions to its problems and create a virtuous circle of "development – overcoming difficulties – redevelopment."

II. Government reform is the key to adapting to economic globalization.

If China wants to share the benefits of economic globalization, it must have breakthroughs in industrial restructuring and institutional transition. Institutional transition is of fundamental significance.

In form, most of the challenges the Chinese government has after China's accession to the WTO are found in the foreign-related economic management system. However, a further analysis will show that the problems originate more from the economic system. In other words, the problems in foreign-related management are only a manifestation of the problems of the economic system. Now that China is a member of the WTO, on the one hand it should lose no time in adjusting its foreign-related systems, laws, regulations and policies that contravene WTO rules. On the other hand and more importantly, it should make greater efforts to deepen the market-oriented economic restructuring and improve the new socialist market economy.

The transition of the economic system is an extremely profound process. This involves the transition of the economic resources allocation mechanism from planning to the market; the transition of the economic resources allocator from the government to hundreds of thousands of market players; and the transition of the economic resources allocation mode from centralized government decision to the decisions by market players. Obviously in this market-oriented reform, the relationship of the government, the market and enterprises must be redefined, and the economic management function of the government and the way the government functions must be changed.

In this process the change of the role of the government is of fundamental importance. Under the new open pattern, and especially after the Asian financial crisis, the government's powerful intervention and its support for the development of some enterprises and industries must be reevaluated and rethought. In contrast, it is of greater significance to create an efficient market environment. However, the institutional transition and the market environment will not appear automatically. Therefore, stressing the importance of the market does not necessarily mean negating the role of the government. However, the effectiveness of the government role is reflected, to a great extent, by the effectiveness of the market. In this sense, the primary and the most difficult aspect of China's accession to the WTO is to "get the government to adapt to WTO rules."

Over the past two decades progress at varying degrees has been registered in changing the way the

governments at various levels in China function, but many problems have yet to be solved. Generally speaking, the reform of the government lags behind the transition of the economic system; and greater efforts are being made in carrying out institutional reforms than in changing the way the government functions. With regard to the relationships between the government and enterprises, between the government and the market, and between the government and social self-government, a series of deep-seated conflicts have yet to be resolved.

-- The government has too much intervention in the microeconomy and especially in state-owned enterprises. An effective state assets management system has to be established. This prevents state-owned enterprises from becoming "qualified market players," i.e., independent legal person entities that are free from government intervention and have clearly defined ownership.

-- The reform of the investment and financing systems is insufficient. The government has many administrative examination requirements for the investment of enterprises and has too many barriers for enterprises to gain market access, thus greatly limiting the market's basic role in allocating resources.

-- Capacity and efforts are not enough for standardizing and regulating the market. Market laws and regulations are incomplete. From time to time laws are not enforced rigorously, and local protectionism and departmentalism often reassert themselves. The flow of economic resources is difficult. All this prevents a unified national market from taking shape.

-- Some government institutions have the tendency to abuse their powers for their own interest. Some government departments have the power both to work out state plans, laws and regulations and to implement them and supervise their implementation. In performing their official duties, these departments are often confined to the interest of their own or of the industries under their jurisdiction, so their public functions and service awareness are weak.

-- The relationship in responsibility, power and benefit between the central and the local authorities has yet to be straightened out. The financial power, financial resources, economic and social functions, responsibilities and rights of the central and the local authorities have to be defined clearly. It is very likely that these problems may cause the macroeconomy to be out of control, widen regional gaps and separate the market.

-- Performance of official duties according to law is far from unified and transparent. There is a lack of coordination between the economic restructuring and legislation. There are often contradictory laws, regulations and documents resulting from conflicting departmental interests. No effective supervision has been exercised over the failure to fully observe or enforce laws and even to prosecute lawbreakers. The failure to strictly enforce laws hinders the establishment of good credit among members of society.

This shows that given the opportunity and challenge of economic globalization, as far as China is concerned, the government, not enterprises, is the first put to the test, that is, its ability to effectively allocate resources by means of the market and to create a favorable market environment.

Right now the Chinese government not only is obliged to safeguard the market but also should adjust the relationship between the government and the market, between the government and enterprises, and between the government and social self-government. It should also play the leading role in cultivating the market. To attain this objective, it is crucial to rationally define the role of the government.

Priorities for changing the role of the government and the way it functions are:

1. The role of the government should shift from direct allocation of resources to macro-control, and great efforts should be made to develop an efficient market.

2. The focus of policy should change from relying on domestic resources and protecting domestic market and enterprises to opening the market and striving to make use of domestic and international markets and resources.

3. The focus of the trade policy should be shifted from setting up barriers to participating in the formulation of international trade rules and protecting the rights and interests of enterprises by means of the WTO dispute settlement mechanism.

4. Industrialization effort should shift from trying to establish a complete self-contained industrial system only with domestic capital to giving play to comparative international advantages and seek a favorable position in the new international division of labor.

5. The nation should be made more competitive by shifting from merely relying on domestic enterprises to creating a favorable market environment and making it more attractive to all economic resources.

III. The economic complementarity between China and Japan and other Asian countries.

The scope of industrial division of labor between nations and regions is rapidly expanding as a result of economic globalization. The nations and regions produce and manufacture products in which they have comparative advantages to exchange for products in which they have no comparative advantages. The transnational allocation of economic resources greatly improves the efficiency of economic operation.

However, no nation has comparative advantages in all areas. Most backward countries do not have only comparative disadvantage without any comparative advantages. If each nation gives play to its advantages, it will benefit all other nations.

1. Complementarity in the industrial structure.

Obviously, the Chinese and Japanese economies are currently in different stages of development. The former has just entered the middle period of industrialization while the latter is in the postindustrial period. The economies in different stages of development have their own comparative advantages. To be more specific, China now enjoys comparative advantages mainly the products of labor-intensive industries such as textiles, garments and some agricultural products. Japan, however, has comparative advantages in the products of capital- and technology-intensive industries such as automobiles, electrical and mechanical equipment, chemical fiber and semiconductor devices. As far as the economic structures are concerned, the two countries are more mutually complementary than mutually competitive. In addition, China's foreign trade relations show that Japan is more important to China as a source of import than as an export market (Japan is China's largest import partner and third largest export partner in the world).

Take manufacturing industry for example. The Chinese manufacturing industry is still at a very low level, though it has developed rapidly during recent years:

1) The Chinese manufacturing industry depends mainly on foreign technology and does not have its own intellectual property rights for many technologies and products.

2) The Chinese manufacturing industry has a limited scale as it is only one-fifth of the American manufacturing industry and a little more than a quarter of Japan's.

3) The productivity of the Chinese manufacturing industry is low. Its per capita productivity is only one-twenty-fifth of America's and one-twenty-sixth of Japan's.

4) The added value is low. The proportion of the OEM attached to foreign enterprises is big. The average added value is only 26%, far lower than 49% in the United States and 38% in Japan.

5) The proportion is excessively small. The equipment manufacturing industry accounts for only 26.5% of the manufacturing industry, far lower than 41.9% in the United States and 43.6% in Japan.

6) The Chinese manufacturing industry mainly produces low-end products. In the international division of labor, the Chinese manufacturing industry mainly produces low-value and labor-intensive products.

7) Chinese manufacturers are small and their production is far from concentrated.

8) During recent years some technology-intensive industries of China grew rapidly and their proportion was higher, but this was mainly due to contribution from foreign-funded enterprises and the growth in processing trade.

These characteristics show that although the Chinese manufacturing industry enjoys some advantages at the low end, it complements the industries in Japan, the Republic of Korea and Southeast Asian countries.

2. Processing trade gives impetus to the growth of import, benefiting both the importer and the exporter.

The proportion of processing export in the export of goods in China soared from 4% in 1980 to 55% now and is larger than the proportion of general export. This is unique in China's foreign trade.

Processing trade often goes with the import of raw and semi-processed materials or intermediate products and the equipment needed for production. Foreign companies use China's cheap labor to expand their processing capacities. They directly run factories in China or have Chinese companies as their processing agents and export the manufactured goods. Their processing enterprises in China engage only in processing and production and have low added value while the design of products, technology research and development, key materials, spare parts, brands, distribution channels and other high-added value links are all in the hands of foreign companies. Every \$100 worth of exported goods include \$50-\$70 imported intermediate products. Under this mode of division of labor, the growth of processing trade promotes the growth of import. Products "made in China" contain many parts made in Japan and in the four little dragons in Asia. When it comes to sharing the benefit, China gets the low added value in the processing and manufacturing links, most of which is the cost of its labor.

3. Products of foreign-funded enterprises in China account for a large proportion of the products China exports.

By the end of December 2001, China had approved the establishment of 390,484 foreign-funded enterprises. Their contracts involved \$745.91 billion in foreign capital, \$395.47 was actually utilized. The proportion of the export of the products of these enterprises in China's total export volume kept increasing. It exceeded 50% in 2001. Foreign-funded enterprises account for an even larger proportion in China's processing trade. For example, the foreign-funded enterprises in China that engage in foreign trade with Japan and the Republic of Korea are mostly funded by Japanese and Korean investors. About 42.0% and 27.4% of the bilateral trade between China and Japan and between China and Korea come from the Japanese and Korean enterprises in China respectively in the form of processing trade.

In a word, the economic and trade relationship between China and the rest of Asian is predominantly one of cooperation based on mutual economic complementation and mutual benefit, not one of competition and antagonism. There is no such thing that one will grow at the expense of the others. The development of China's processing trade will give impetus to the rapid development of its import, and especially import from other Asian countries. China's economic relations and trade with other Asian countries include the tremendous interests of the China-based

enterprises of these countries. Strengthening the economic and trade cooperation between China and other Asian countries and promoting the economic integration of Asia are in the interest of both China and other Asian countries.

IV. Striving for common development in a win-win situation.

Along with economic and technological development, there are irresistible laws governing industrial upgrading and structural transition. With the number of barriers to the transnational flow of economic resources decreasing drastically, developed countries are transferring some of the industries in which they do not have advantages successively to developing countries. This will benefit both developed and developing countries.

The Asian financial crisis five years ago was a financial crisis apparently, but it had its deep-seated cause, that is, the economic structure in East Asia was weak. It is imperative for East Asian economies to expand their industrial division of labor and improve their economic structure. Since the 1990s there has been an obvious trend of regional economic integration from Europe to North America. Adjoining countries and regions are close to each other geographically and have similar culture, but they have different natural resources. With different resources and being in different stages of development, these countries and regions need each other and complement each other. By facilitating trade, they make use of each other's advantages to offset their disadvantages, increase trade and investment for the benefit of all. Regional economic integration has the benefits as follows:

1. Helping the countries concerned to promote their economic growth, further boost market demand and increase their trade.
2. Helping give full play to the advantages of the countries concerned and bring about large scale of production and operation on the basis of international division of labor.
3. Making it possible to allocate resources and plan for production in more areas, promoting the transfer of industries, industrial upgrading and the rational distribution of the industrial chains of enterprises and making enterprises more competitive.
4. Helping attract more investment and creating more job opportunities.
5. Encouraging full competition which helps promote technological progress.
6. Making the countries concerned more economically interdependent and contributing to regional security and stability.

As trade and international investment keep increasing, developed countries have advantages in technology, skilled personnel and capital. They are in a more favorable position in regional trade and have more leverage. They should therefore take the initiative in promoting regional trade and transnational investment.

Over the past two decades China shared the benefits of its part in economic globalization and of its economic cooperation with its neighboring countries. However, China today is still in a stage of development different not only from that of Japan but also from those of the four little dragons. Difference leads to complementarity. The Chinese economy now has some obvious characteristics of the development stage:

1. China's current per capita GDP is approximately \$1,000, and the country is in a stage of rapid economic growth. In the next 10 to 15 years the Chinese economy will probably continue to grow at an average annual rate of 7%. With a population of 1.3 billion, China has great market potential, which will become increasingly evident as the economy grows. There will be a large diversified market for China and for its neighboring countries.

2. Having just entered the middle period of industrialization, China has large numbers of qualified and cheap laborers. It also has a relatively good industrial foundation and comprehensive supporting capacities, so the potential for growth in general processing and manufacturing industries is great. The country is in a position to have more industry transfers from developed countries in order to provide its neighboring countries and the rest of the world with cheap manufactured goods.

3. Now that state affairs are being run according to law in China and the country has joined the WTO, the software and hardware of the Chinese market will improve constantly. Conditions will be improved so that Chinese enterprises will go global and more foreign enterprises will invest in China. As a result of the different characteristics of the stages of development and the different resources, China and its neighboring countries and regions complement each other in their market development orientation and market structures; in the production distribution and division of labor; and in the development and utilization of their natural resources. If China and its neighboring countries strengthen their cooperation and increase their trade and investment, it will benefit enterprises and economic subjects.

Since the 1990s, regional economic integration, an additional form of the international multilateral trade system, has shown strong development momentum under the framework of the WTO. Since 1997 East Asia has established the Ten Plus Three mechanism for meetings of state leaders and other high-ranking officials at different levels. In 1999 Chinese, Japanese and Korean leaders held for the first time a breakfast meeting during the summit to discuss an economic cooperation mechanism of the three countries.

The foundation is now solid for China to establish economic cooperative relations with the other countries (regions) in Asia, and it is quite possible for China to do that. China's export to and import from other countries (regions) in Asia account for 53% and 60.4% of its total export and import volumes, both figures being higher than with other regions. The investment in China of ten other Asian countries (regions) takes up about 60% of the country's total foreign investment, which is very important. Consequently, China's import from other Asian countries and regions exceeds its export to them. This mutually beneficial relationship provides the condition for long-term cooperation between China and the rest of Asia. Moreover, there is a foundation for institutional economic cooperation between East Asian economic subjects, though there are many barriers as well. Although a free trade zone is not possible within a short period of time, a good start can be made now by facilitating trade and investment.

In addition to the lowering of tariffs and the removal of non-tariff barriers, regional trade cooperation involves many measures for facilitating trade including, for example, simplifying the visa application procedures for businesspeople; coordinating the product standards and hygiene and quarantine standards of member countries; simplifying examination and approval procedures for cross-border investment; establishing customs management systems compatible with e-commerce and paperless trade. This will create the conditions for member countries to increase the industrial trade based on comparative advantages and accumulate experience needed for strengthening trade relations in East Asia under the Ten Plus Three framework in the future.

In short, in order to cope with the trade and investment liberalization around the globe and the tendency to establish regional blocks, it is necessary for Asia to strengthen regional economic cooperation and promote regional trade and investment liberalization as its long-range objectives.