CHAPTER 6. CONCLUDING REMARKS AND POLICY IMPLICATIONS

6.1 Concluding Remarks

Since the implementation of opening policies in 1979, China has increasingly utilized overseas funds actively to accelerate industrialization and industrial promotion. In addition, China has maintained one of the highest growth rates since its opening up. Even after the 1997 Asian financial crisis, China's annual growth rate has been over 7%. Today, China's economic growth rate is over 10%. Its high growth rate results from a good deal of overseas funds and foreign technology progress. Thus, FDI has played a key role in the integration of China into a market-oriented economy. As a matter of fact, numerous political and economical reasons will attract foreign direct investment (FDI). This paper mainly explores how region's political power in the central government affects regional FDI in China. Thus, this paper adopts a panel data analysis to capture regional-specific and time-specific effects. By using a regression model, this study evaluates the impact of region's political power on FDI. Moreover, most of the data used in this paper are acquired from the *China Statistical Yearbook*.

The primary finding of this paper is that region's political power in the central government (*CCPB*) has a positive and significant impact on regional FDI at a 5% significance level in the model specification. This paper uses political power as a new variable that no one has considered it as a political factor of determining FDI before so this paper can be regarded as a complementary paper in studying regional distribution of FDI in China. In addition, other results of this paper show that economic size (*GPP*), purchasing power (*PER*), transportation infrastructure (*HIWAY*) and agglomeration (*AFDI*) are positive determinants of regional FDI. However, the degree of openness (*OP*) and the relationship between provincial political power and time trend (*CCPBT*) are found to be negative determinants. In addition, labor cost (*WAGE*) and dummy variable (*COASTAL* and *Time*) are statistically insignificant variables.

Surprisingly, *AFDI*, representing agglomeration effect, has a positive impact on FDI at a 1% significant level. However, the result does not conform to Sun et al. (2002), but it is consistent with Heid and Ries (1996) and Cheng and Kwan (1999). That is, this paper suggests that FDI can create a "herding effect", which means the more FDI accumulated relative to the domestic investment accumulated, the more inflow of FDI invested by foreign investors. In addition, *OP* is also surprising to our expectation. The degree of openness has mixed blessings on FDI.[83] However, the result of this paper conforms to Wheeler and Mody (1992) that *OP* has a negative impact on FDI which means higher degree of openness does not improve the amount of FDI in China after 1997.

Finally, several tests have been conducted to ascertain whether the empirical results can provide accurate conclusions. Based upon some tests for econometric issues, such as model misspecification and multicollinearity, it is implied that conclusions provided by this study are reliable.

6.2 Policy Implications

From the beginning of the "Open Door" policy in 1979 to 2006, China has received $882.038 billion in foreign direct investment (FDI). Indeed, China is the

[83] On the one hand, a more open economy attracts FDI because it welcomes foreign capital and foreign investors are more familiar with the host economy. But on the other hand, openness can have a negative impact on FDI due to keen competition.

largest developing country of FDI. Although China's attraction of FDI is impressive, potential problems exist. The distribution of FDI is an unequal development among regions in China, especially between the coastal and inland provinces. In 1999, the amount of actually utilized FDI declined in China for the first time since the implementation of the open-door policy. Accordingly, the Chinese government gradually attaches great importance to this inequality.

Actually, Sun et al. (1997) found that the difference of regional FDI between the coastal and inland provinces exists because coastal regions attract FDI by larger market demand and higher degree of openness. On the other hand, the inland areas influence the determinants of regional FDI by lower labor costs and infrastructures. To be sure, the authorities in China have begun to recognize the importance of distributing FDI more equally. They are focusing on developing infrastructure facilities to previously disadvantaged inland regions to make them more inviting to foreign capital, and are fashioning polices to provide equal footing for FDI inflows to certain manufacturing industries and underdeveloped services sectors.

However, according to regression model of this paper, region's political power in the central government actually affects FDI positively but the effect of influence is decreasing in course of time. It is because the provinces with higher degree of political power acquire preferential policy earlier than those with lower degree of political power. With the increase of time, provinces of lower degree political power intend to follow the higher degree political power provinces so lower degree political power provinces ask for the Chinese government to offer preferential policies. In the long run, all provinces get preferential policies from the central government and attain equal development, which is concerned by the Chinese authorities. Thus, the Chinese government should set up a complete mechanism to balance the differences between the coastal and inland regions by providing opportunities for foreign investors to take advantage of locational and internalizational advantages for their cross-border investment decisions.