Conference Summary Report

OECD-MOFTEC Conference on Foreign Direct Investment in China: Challenges and Prospects (Xiamen, 11-12 September 2000)

Overview

1. China has actively sought foreign direct investment (FDI) and technology to promote its modernization efforts and accelerate its export trade capabilities since its opening up in 1978. The total amount of incoming FDI rose from almost zero in that year to a high of about $110 billion in 1993 and $320 billion in 1999. Thus, China has become the world’s third (second until 1998) largest recipient of FDI, and the largest recipient among developing countries. The FDI volume has hovered around $40-50 billion in each of the past several years. China expects significantly increased inflows over the next five years following the anticipated WTO accession that would bring about the removal of a number of restrictions on foreign investment.

2. At present China is on the threshold of crucial developments and policy decisions concerning FDI, and keen to increase the level, quality and source diversity of incoming FDI, particularly from the OECD Member countries. The Chinese government continues its efforts to adjust its policy and institutional framework, as well as investment promotion policies, to the requirements of the changing international and domestic circumstances.

3. With a view to contributing to this ongoing process and as part of the OECD-China programme of co-operation and policy dialogue, this conference was co-organized by the OECD and the Chinese Ministry of Foreign Economic Co-operation and Trade (MOFTEC). The objectives of the conference included: (i) a thorough discussion of the driving forces and economic effects of FDI on China’s development; (ii) exchange of information and experiences on best FDI promotion practices, and (iii) elaboration of China's future FDI plans and policies.

4. The conference provided a timely forum to discuss the impact of FDI in China and investment promotion policies in a unique setting involving all the key players. It brought together a representative group of more than 120 participants from the OECD, non-OECD and the Chinese central government, provinces, business and investment groups, international organizations, and research institutes.

5. Conference participants acknowledged the value and timeliness of the Conference. They recognise that it contributed to a better understanding of the issues regarding FDI in China and different perspectives of OECD Member countries, China’s central government and provinces, and foreign/Chinese investors, particularly at a time when China prepares for WTO accession and has been going through sweeping reforms. The following key points emerged in the presentations and discussions.

6. Papers presented to the conference and the synthesis paper produced by the OECD Secretariat can be consulted at www.oecd.org/?

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FDI Trends and Economic Impact

7. In the first session, Chinese and international speakers discussed the recent FDI trends, determinants and policy challenges in both OECD countries and China. MOFTEC speakers emphasized that, although the quality of FDI in China improved in some sectors, **there was a clear need to increase high-tech investment from diverse sources.** They noted that FDI flows contributed significantly to the build up of the nation's foreign exchange reserves, export drive, financial stability, and provided more than 20 million jobs. They explained that FDI's contribution to China was not limited solely to the main economic indicators of employment, economic growth, trade and technology, but also to changing managerial concepts and invigorating the overall systematic vitality.

8. Chinese officials acknowledged the growing imbalance in regional distribution of FDI across the country – more in coastal areas and less in central and western China – and underlined the government's determination to redress this situation. They also indicated that foreign investors were increasingly interested in the less developed western regions as a result of the government's recent "Go West" development strategy. According to Chinese statistics, FDI flows to western regions increased by 19.60 percent last year. Tax revenues from foreign-invested enterprises in the country reached 36.2 billion yuan (1$=8.2 yuan as of November 2000) in January-March 2000 period, representing an increase of 31 percent over 1999.

Investment Promotion: Best Practices and China

9. The second session focused on the experiences of OECD member countries, non-member countries and regions in FDI promotion. Locate-in-Scotland (LiS) representative introduced the role of local government in FDI promotion, the institutional structures and policies deployed for this purpose, with a particular focus on the Scottish experience. LiS was working with Scottish enterprises and executives on three goals: aligning inward investment activities, integrating with the rest of the Scottish executives' network, and delivering the best of Scotland.

10. Saxony Economic Development Corporation and Korean Ministry of Commerce, Industry and Energy also elaborated on their practices that might be relevant to China. The main theme was that the host country's political commitment would play a key role in this process. Investment in France Agency and Malaysian Industrial Development Agency showed concrete examples of how best central government and local authorities could share roles in effectively promoting FDI inflows. The FIAS highlighted deficiencies and practical steps in assisting governments to attract higher levels of FDI through advice on improving the investment environment and marketing the investment environment more effectively.

11. In discussing China's national and local experiences in this area, MOFTEC highlighted the varied efforts made for close co-operation among Chinese central and local governments, as well as co-operative schemes between China and other countries such as Japan, for example in the areas of banking and services sector institutions. Beijing Foreign Investment Service Center (BFISC) elaborated the achievements of BFISC as an investment promotion agency in the capital city. As a result of specific measures to attract FDI, and of the increased confidence of foreign investors in the Chinese economic strategy, the inflow of FDI would expand substantially, Chinese experts stressed. However, there are limitations to attract further FDI, as outlined by foreign investors already operating in the Chinese market. They called for further reforms for a predictable framework if the Chinese government wanted to continue the upward FDI trend in the future.

China's Future FDI Policy Orientation

12. Chinese speakers underlined that rational and active utilization of FDI was a long-term strategic goal for China and that imminent WTO accession would further brighten the FDI prospects. Service industries would be the next target of FDI liberalization. Despite some continuing challenges faced by foreign investors, the effort to make China a more hospitable environment for foreign investment, both in terms of rules at the sovereign level and operations on the ground, would continue slowly and steadily.

13. Chinese Academy of Social Sciences introduced China's future FDI policy agenda, as embodied in the draft next five-year (2001-2005) plan: (i) further promotion of FDI into central and western region, (ii) more opening up of services sector, (iii) encouragement of the new technology transfer, and (iv) expedition of reform process of state-owned enterprises (SOEs) and (v) finally, more stimulation of mergers and acquisitions in the form of FDI. Chinese officials also stressed that China would continue to uphold the principle of "socialist market economy" and that SOEs would be financially reorganized with further liberalization of small scale SOEs and more opening up of internationally competitive SOEs, but it would proceed gradually. China expects FDI to contribute to the painful process of SOE reform.

Prospects and Challenges

14. The third session "Experiences of FDI Companies in China" witnessed quite frank exchanges of opinion on the significance of China for foreign investment and specific problems that private investors have been facing. A.T. Kearney Group introduced the comparative FDI confidence index, which it developed for a number of emerging markets including China. China has ranked third on this index after the U.S. and the U.K. Speakers from foreign businesses in China such as Kodak Eastman Company, Xiamen Schaeff Engineering Machinery Corporation, Bayer China Limited, China International Capital Corporation, and BP Amoco offered insights as to how the existing problems could be addressed. The two particular cases from the petroleum and the telecommunications sectors were discussed, particularly with regard to CNPC and China Telecom's going international through initial public offerings (IPOs) in New York, London and Hong Kong Stock Exchanges.

15. International speakers stressed the need for international co-operation and rules to provide the basis for greater stability and stronger economies. They emphasized the importance of a sound regulatory framework such as removing administrative barriers, rule of the law, efficiency and integrity of the public sector, good corporate governance, and national treatment. One panelist mentioned that, with 13 per cent share of FDI in total Chinese domestic capital, FDI was not a threatening force for the Chinese economy and that further liberalization would be needed. **There was a word of caution for foreign investors that the competition in China had become more intense in certain sectors and past habit of overestimation of Chinese market in those sectors should be cooled down.**

16. In the concluding panel, it was stressed that China's expected entry into the WTO would be a big step for FDI as it would reduce regulatory risks and open up sectors, previously off limits to foreign companies. Though there will be more growth in FDI in the services sectors, manufacturing is expected to account for a larger share of overall investment. The new areas that will open to foreign investment include telecom, energy, commercial banking, insurance, retail distribution, and agriculture. China's adoption of laws, regulations and policies that are more consistent with international norms would mean greater transparency and a more level playing field for investors and this would lead to an improved

investment climate. One speaker suggested that more provincial representation (reflecting the growing importance of provincial authorities in the relatively decentralized decision-making procedure) in future FDI conferences was needed for such discussions to be comprehensive. Chinese officials were also invited to pay more attention to economics rather than politics of FDI.

Next Steps

17. At the end of the conference, MOFTEC expressed appreciation for the wealth of information, exchange of experiences and views that occurred during the conference, and underlined that they would serve as useful inputs to China's policy-making. MOFTEC also asked for the continuation of similar meetings in order for the Chinese and the international investors to better understand each other's positions.

18. As for future work, the following activities have been suggested during the concluding session of the conference for China's possible participation and consideration:

- OECD Global Investment Forum (currently under consideration),
- Regional Corporate Governance Roundtable,
- OECD Convention on Anti-Corruption and Asian Anti-Corruption Forum (scheduled for December 2000 in Seoul),
- OECD Guidelines for Multinational Enterprises,
- OECD Forum on Enterprise Development, and
- 2000-2010 "Istanbul Action Programme" (adopted in September 2000 by the Network of Foreign Investment Promotion Agencies).

19. On the margins of the conference, the OECD/ MOFTEC Steering Group discussed the possibilities of undertaking further specific follow-up activities on: (i) FDI and mergers and acquisitions in China, (ii) FDI and regional development in Western China, (iii) improving China's FDI statistical methodology and reporting, and (iv) the comparative review of China's FDI policies. These suggestions will be further fleshed out for implementation in 2001.