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Forty Years of Opening Up Has Greatly Benefited China's Foreign Trade

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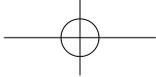
It has been four decades since China embarked on the great course of reform and opening up in 1978. Over the past four decades, the Chinese economy has maintained an average annual growth of 8%, which was unprecedented in human economic history. Meanwhile, China has grown from a closed and underdeveloped agrarian country to the world's second largest economy, the largest trader and exporter of goods, the second largest importer of goods, and the second largest trader of services. As a major country with its doors wide open, China also boasts the second largest amount of outward foreign direct investment. China has transformed itself from a least-developed country to a middle- and high-income developing country. In

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the coming years, per capita income is expected to reach USD12,000, making China a developed country. It is beyond all doubt that, within only four decades, China has greatly improved its status in foreign trade by reform and opening up, and integrated into the world economy.

The remarkable achievements of Chinese foreign trade

Four decades ago, China started from zero. By now, it has made significant headway in foreign trade, two-way direct investment, trade in goods and services, and other international economic cooperation projects. More specifically, from the early days of reform and opening up to 2017, Chinese foreign trade in goods grew 196-fold from USD21 billion to USD4.1 trillion, accounting for 11.5% of global foreign trade and ranking the first in the world. In more detail, goods worth USD2.26 trillion were exported, accounting for 12.8% of global exports and ranking the first in the world; and imports of goods reached USD1.84 trillion, accounting for 10.2% of the world total and ranking the second in the world. China's dependence degree on foreign trade in goods was 33.6%. In the meantime, China's foreign trade in services grew approximately 172-fold from USD4 billion to USD690.5 billion, accounting for 6.7% of the world's total foreign trade and ranking the second in the world.



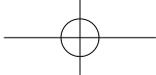
Four decades of reform and opening up produced remarkable achievements in foreign trade, which was demonstrated by the development of China's international cooperation. First, in 2017, the lump sum of foreign capital utilization reached USD136.3 billion, accounting for 9.5% of the world total, ranking the second in the world and registering a 40-fold increase over the 40 years. Additionally, China's outward foreign direct investment stood at USD158.2 billion, accounting for 9.9% of the world's total amount of foreign investment utilization, ranking the second in the world, up 55 times since the beginning of reform and opening up. Furthermore, Chinese foreign contracted projects generated an USD168.5 billion turnover, and the number of dispatched workers engaging in foreign labor service cooperation reached 522,000. Clearly, four decades of reform and opening up have made China a well-deserved "world factory."

From a wider and deeper to an all-around opening up over four decades

The 40 years of China's reform and opening up can be divided into three phases: opening up wider, opening up deeper, and opening up all-around. From 1978 through 2001, China was committed to opening up wider, mainly by setting up special economic zones, economic development zones, industrial

parks, high-tech zones, and export processing zones. This phase featured extensive opening up that focused on quantity and advanced from coastal to inland areas through the creation of industrial parks. The foreign trade policies were transformed from the import substitution strategy prior to reform and opening up to export-oriented development.

The second phase, which featured a deeper opening up, spanned the period from the end of 2001, when China joined the WTO, to 2017, before the convening of the 19th National Congress of the Communist Party of China (CPC). On the one hand, China's entry into the WTO has earned it larger markets and more opportunities for its exports. On the other hand, the previous export-oriented model characterized by labor-intensive products was challenged by rising labor costs, diminishing demographic dividends, and weak external demand as a result of the 2008 global financial crisis. During this period, China expedited economic growth by setting up 11 pilot free-trade zones to experiment on new economic reforms, improving the quality of products, especially exports, while continuing to reduce tariffs and promoting trade liberalization. During this period, the country focused on quality and intensive opening up. The foreign trade policies shifted from the previous export-oriented development



to trade liberalization.

The third phase began after the 19th National Congress of the CPC in 2017 as the country ushered in a new era of all-around opening up. Presently, economic and trade globalization are confronted with a reversing trend and undermined by some countries' trade hegemony and protectionist trade policies. To facilitate global trade liberalization and economic development, and pursue win-win outcomes through mutually beneficial global economic cooperation, the 19th National Congress of the CPC underscored the importance of "making new ground in pursuing opening up on all fronts," which was a priority in China's economic development. As of now, all-around opening up has manifested itself in three ways: expanding imports, building free-trade ports, and building the Guangdong–Hong Kong–Macao Greater Bay Area. This trio is of great significance to trade globalization.

Key practices of reform and opening up during the past four decades

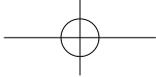
In addition to the aforementioned three phases, the reform and opening up can be analyzed from other perspectives. The dominant strategy prior to reform and opening up was the import substitution strategy, which was then replaced by an export-

oriented model in the early 1980s. Further on, as China gradually integrated into the world economy, its trade liberalization policies and accession into the WTO began to make a difference. Then, the global financial crisis broke out, stressing the need to open up deeper. Finally, understanding the influence of all-around opening up in the new era is of practical significance.

From the import substitution strategy to an export-oriented strategy

Since 1978, China has made significant headway in economic restructuring and industrial upgrading and has turned to development strategies in alignment with its comparative advantages. China adopted the "dual track" reform to provide temporary shelter to outdated capital-intensive industries. Such incremental reforms approached Pareto Optimality and were easy to implement. The government has proactively contributed to industry assessing and economic upgrading. The successful economic restructuring and upgrading of manufacturing have also created more jobs for urban and rural workers. As a result, the poor population has sharply decreased. During this phase, which spanned a period of 30 years, China has grown from a under-developed country to a middle- and high-income country.

From 1992, when China announced the establishment of the



socialist market economic system, to 2008, when the global financial crisis hit, China's economic development should be mostly attributed to its export-oriented strategy. In this context, what is the relationship between international trade and an export-oriented strategy? Further, how did the export-oriented strategy supercharge China's economic development? The export-oriented strategy was necessary in light of the country's demographic features and low urbanization rate. A low dependency ratio and urbanization rate resulted in an excessive amount of labor supply and a slow growth of income, which consequently helped accumulate capital rapidly and fueled the manufacturing development. However, they also meant that the domestic market was inevitably small, which rendered exports the only solution for market clearing. The analysis of China's processing trade based on highly detailed transaction data from 2010 showed that free-trade zones were important for facilitating the development of processing trade. According to the customs data from 2000 to 2005, the abundance of processing enterprises in China led to a comparatively lower productivity in export enterprises. Therefore, distinguishing processing trade from non-processing trade was crucial for correctly understanding the performance of Chinese export

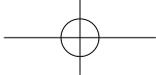
enterprises.

Trade liberalization and WTO's influence

To expedite WTO accession, China, first as an "observer" in 1994, sharply slashed import tariffs from 35% to 17% within only three years, securing its membership by the end of 2001 as the 143rd member state. Subsequently, China has been adhering to a trade liberalization strategy. More specifically, based on highly detailed trade and production data from 2000 to 2006, it can be investigated how the tariff cuts and exemptions for imported intermediate goods and final products influenced the productivity of major Chinese enterprises engaged in international trade. The results show that the cuts and exemptions had a positive impact on productivity, and the impact decreased as the share of imports increased in the processing trade. In general, tariff cuts for imported intermediate goods had a greater positive impact on productivity compared to tariff exemptions, whereas the opposite was true for enterprises not involved in processing trade. In addition, the reduction of tariffs on intermediate goods would enhance enterprise R&D.

Opening up deeper amid the global financial crisis

The 2008 global financial crisis has plagued the world economy, especially developed economies which suffered from weak external demand.



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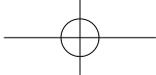
In China, the previous export-driven development model was no longer viable. Due to the financial crisis, Chinese businesses were facing overwhelming credit constraints. In July 2005, China adopted a managed floating exchange rate mechanism, and the Chinese yuan appreciated against the U.S. dollar. China's export model has shifted from simply relying on cost advantage (low wages) to quality improvement of exports. China has also transformed its strategy from opening up wider to opening up deeper. Moreover, exchange rate fluctuations might affect enterprise decision-making through other, previously unknown channels, and competition is the decisive factor in quality improvement.

Policy suggestions for the all-around opening up strategy

Facing the new international economic landscape with weak external demand, and rising protectionism in Western countries, China is also stepping into a complicated situation in its opening up. As mentioned above, at the 19th National Congress of the CPC in 2017, the Central Party Committee proposed to “make new ground in pursuing opening up on all fronts.” Profound changes have taken place since the beginning of the new century. To achieve sustainable industrial upgrading and continuous productivity improvement, reform and

opening up policies should be refined to adapt to the needs of the new era. Therefore, “internal reform and external opening up” was changed to “external reform and internal opening up.” External reform means identifying new trading partners to disperse systemic risks of over-reliance on a few developed countries. Furthermore, free-trade areas among neighboring countries should be quickly established and the model of processing trade should be adjusted. Internal opening up aims to break down regional trade barriers, liberalize factor markets, and open up product markets further. Industrial upgrading will gain ceaseless momentum from external reform and internal opening up.

Over the past 40 years, China has adopted a series of measures to facilitate trade and investment, such as reducing import tariffs, building interregional free-trade areas, signing bilateral investment agreements, opening up pilot free-trade zones, streamlining administration and delegating powers, providing favorable policy in land and tax, and aiding infrastructure construction. These measures have boosted productivity, improved consumers' benefits, and drove economic development. China still has a large room for improvement in interregional free-trade zones, pilot free-trade areas, and infrastructure construction.



CHINA ECONOMIC TRANSITION

To address the challenges of anti-globalization and stay active in international economic and trade relations, China is ready to build free-trade ports that are more open and liberalized by drawing upon the experiences of existing bonded free-trade ports and free-trade zones. The free-trade ports serve as a global hub for goods, professionals, and capital.

China should stay aligned with advanced international experiences and blaze a new trail for building free-trade ports. Hopefully, the country will achieve new breakthroughs in facilitation of trade in goods, flow of people, and financial openness.

(This article is based on *The Remarkable Achievement of Chinese Trade: Forty Year's Opening Up*, a book written by Professor YU Miaojie.)