The Opening-Up of China and Other East Asian Economies

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The Opening-Up of Developing Economies

- Economic globalisation benefits all economies because the choice sets facing all participating economies are expanded. But even though this seems obvious today, it was not always the case back in the 1950s, when it was widely believed that "import substitution" rather than "export promotion" is the correct economic development strategy for a developing economy. "Import substitution" is the precise opposite of openness. This is also reflected in the debate at the time among economists of "trade versus aid", that is, Is it better for developed economies to allow imports from developing economies than to give them foreign aid?
- In addition to the imports of goods and services, openness also applies to inbound foreign direct investment (FDI) and foreign loans. Foreign investors play an important role in the promotion of exports from a developing economy because they have access to captive markets and can provide quality assurance for the potential exporters in the developing economy.

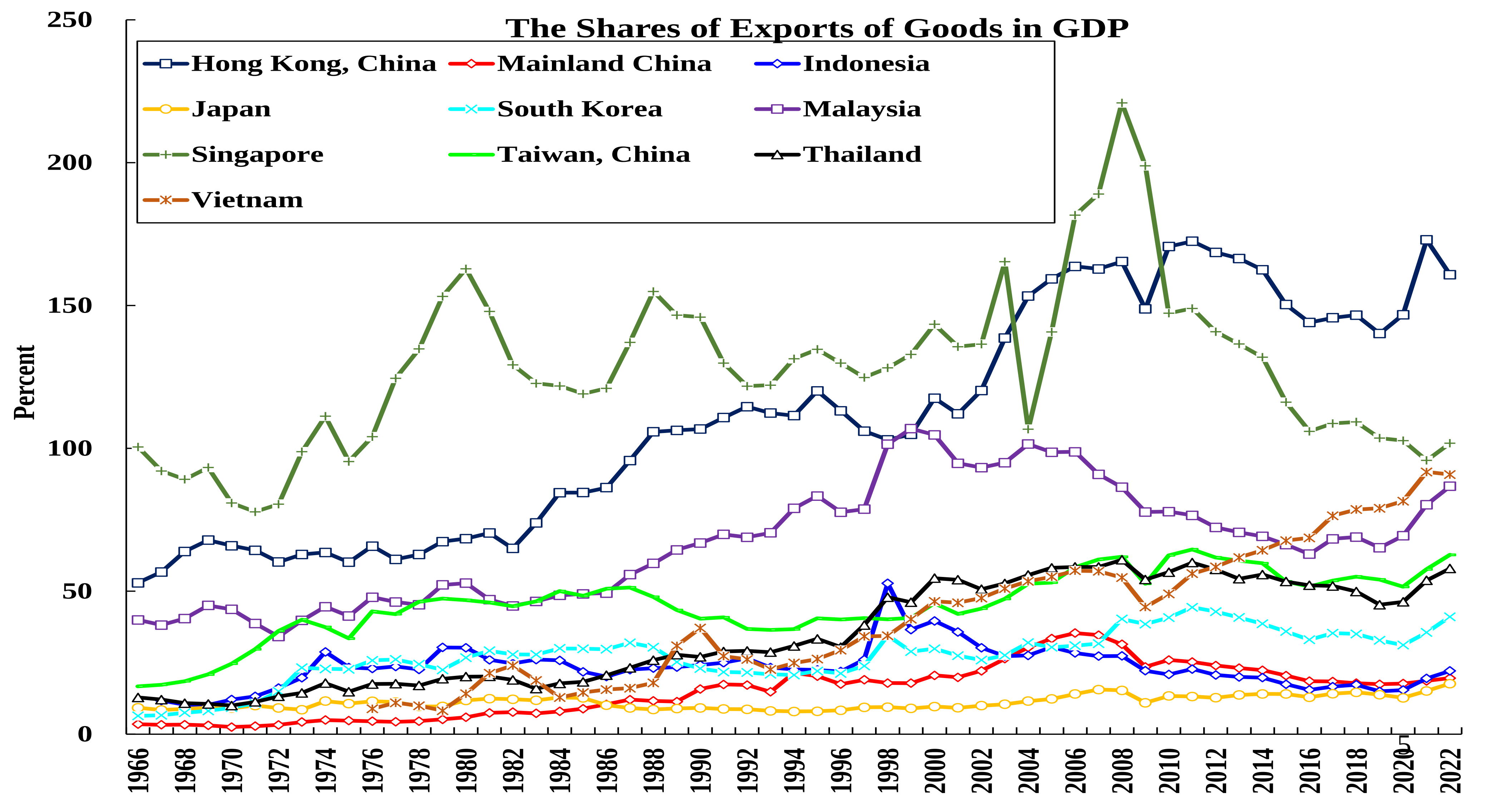
The Opening-Up of Developing Economies

- However, openness alone is not sufficient; it must be accompanied by marketisation, so that the prices of exports and imports are determined in a free and competitive market.
- For the free and competitive market to work properly, there must be an exchange rate that reflects the true scarcity value of the local currency. An over-valued exchange rate will kill exports, and an under-valued exchange rate will make imports of equipment and raw materials too expensive.
- Reciprocity per se between countries in trade is an important principle in maintaining openness. Countries should be free to export to and import from one another. This is where the World Trade Organization (WTO) and its predecessor, the General Agreement on Tariffs and Trade (GATT) come in.

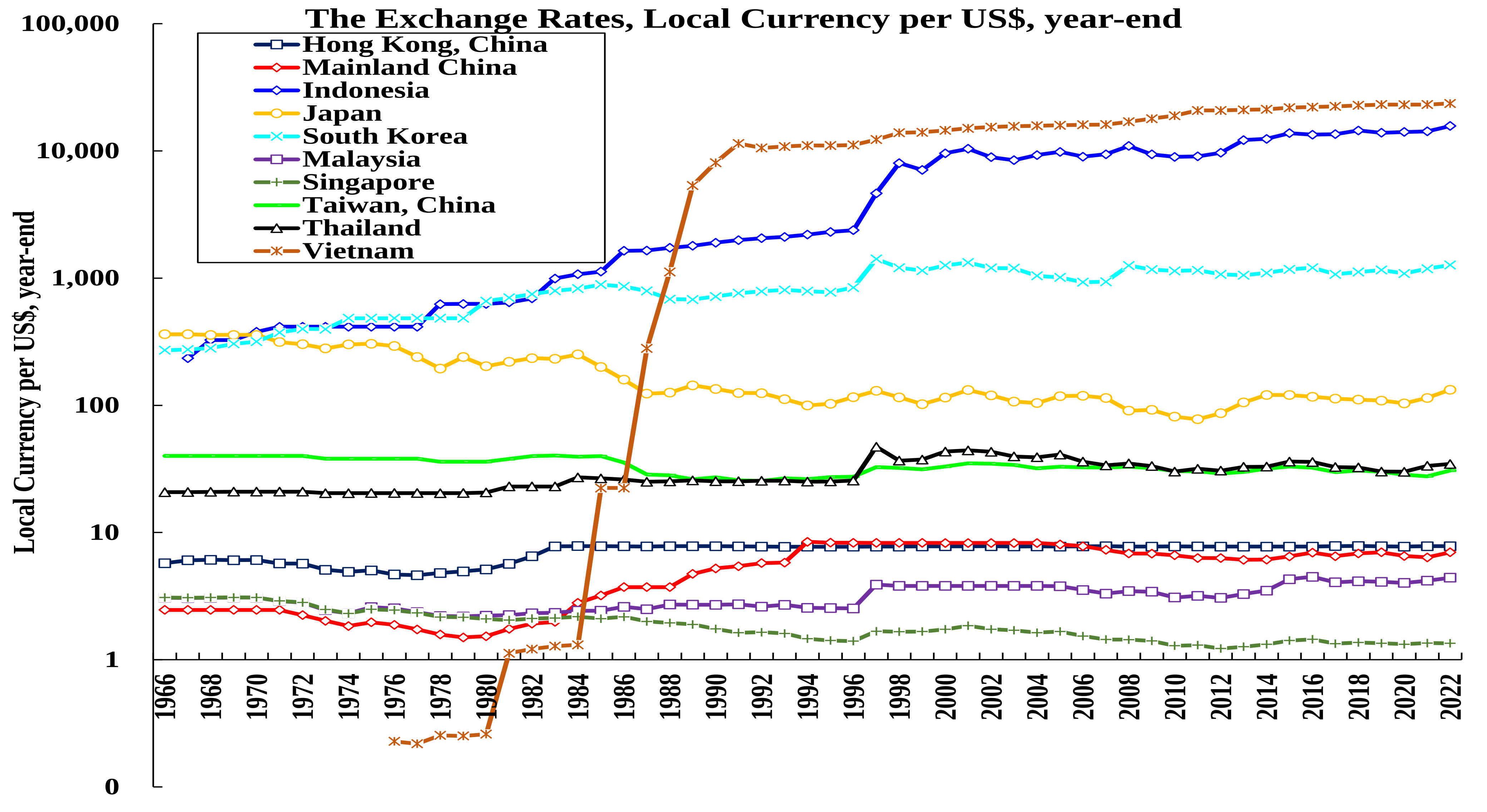
The Commonalities of East Asian Economies

- East Asian industrialisation started out in Japan and spread to first Hong Kong and then Taiwan in the 1950s, and then Singapore and South Korea in the 1960s, and then the ASEAN economies of Thailand, Malaysia and Indonesia in the 1970s, and then to the provinces/municipalities of Guangdong, Shanghai, Jiangsu and Zhejiang in Mainland China as China undertook economic reform and opened to the world beginning in late 1978.
- Each of these economies adopted in turn an export promotion strategy. It would also adopt a significantly devalued official exchange rate. This would result in a rapid expansion of exports and a rising share of exports of goods in its GDP during this phase. Eventually, however, the share of exports in its GDP will decline.
- After a while, the growth of exports would slow down as surplus labour ran out, real wage rates rose, and exports began to be restricted by the quota imposed by the importing country.
- Almost all of these East Asian economies had similar characteristics (such as high national savings rate and surplus agricultural labour) and initial conditions, adopted similar strategies, policies and measures, such as export promotion, and experienced similar development paths.
- And they have all benefitted from economic globalisation, with quite a few of them—for example, Japan, Hong Kong and Singapore—achieving developed economy status. In 2022, China also achieved a real GDP per capita of US$12,309, exceeding the middle-income threshold of US$12,000.

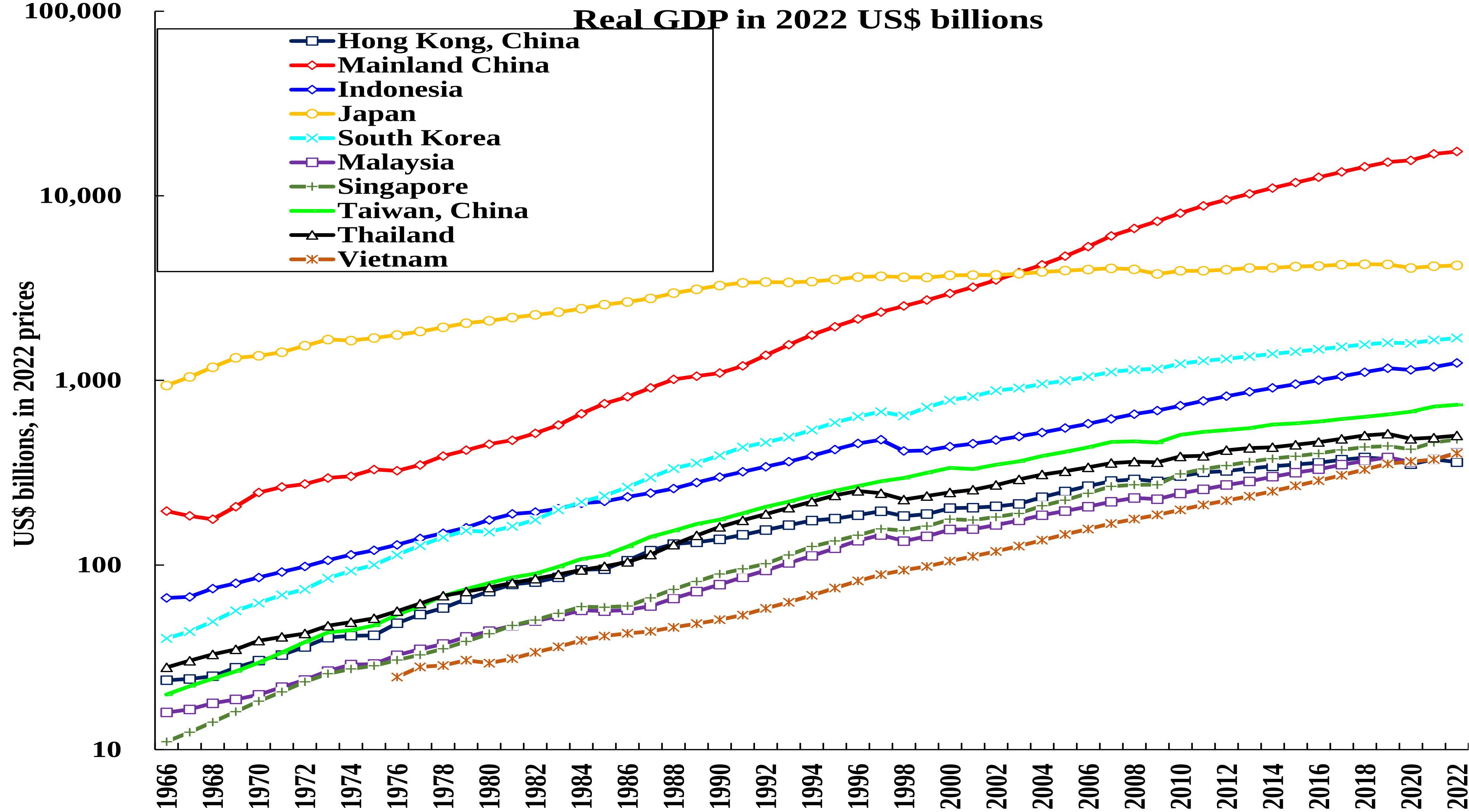
The Shares of Exports of Goods in GDP: Selected East Asian Economies, 1966-2022



The Evolution of the Exchange Rates (Local Currency per U.S. Dollar), Selected Economies



Real GDP in billion 2022 US$: Selected East Asian Economies, 1966-2022



The Prospects of Continued and Further Opening of the Chinese Economy

- China is committed to be a "dual-circulation" economy. Continued opening-up is good for the Chinese economy and good for the rest of the World.
- However, there are head-winds—de-globalization, de-coupling and de-risking; restrictions of critical raw materials and high-technology exports by the U.S. and its allies; and geo-political tensions.
- Just as economic globalisation brings net benefits to every economy that participates in it, economic de-globalisation imposes net costs on every economy. The same is true of de-coupling and de-risking to the extent that they are not supported by the free market.
- However, the Chinese economy has already grown into a sufficient size that it is largely immune to external economic disturbances. Moreover, it has sufficient human capital, savings, scale and resilience to survive these challenges.
- Moreover, de-globalisation, de-coupling and de-risking will eventually lead to multiple supply chains around the world for the same product or service, which will enhance global economic resilience, increase competition, reduce monopoly power and ultimately lower prices to the benefit of all. Continued opening-up also enables the Chinese economy to maintain global competitiveness in its markets and prevents the rise of domestic monopolies.

The Prospects of Continued and Further Opening of the Chinese Economy

- More specifically, going forward, China can negotiate with its trading partner countries <u>reciprocal</u> reductions in tariffs and elimination of non-tariff barriers within the framework of the World Trade Organization (WTO). It can also enter into investment agreements with other countries.
- China can consider opening up to competitive supply chains located outside of China on a reciprocal basis.
- China can also consider accession to the WTO Agreement on Government Procurement (GPA).
- China can undertake further relaxation of its capital controls at a controlled and measured pace—for example, by allowing a foreign enterprise such as Airbus to have a secondary listing of their shares as Chinese Depositary Receipts on the Shanghai Stock Exchange. Airbus gains a source of capital. Chinese investors can invest in a foreign enterprise with renminbi. And it does not affect the capital flows except on an one-off basis. It is win-win for all.