Techno-industrial FDI Policy and China's Export Surge

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Abstract

Researchers emphasize productivity growth of China's domestic enterprises as well as the granting of permanent trade relations as causes of China's export surge to the U.S. after 2000. Less well understood is the role of Chinese industrial policy as embodied in its regulation of foreign direct investment, which encourages development of high-technology industries. This gap is troubling, since about half of Chinese exports between 2000 and 2008 originated in foreign- owned enterprises. This paper uses a quasi-natural-experiment approach to assess the effect of changes in Chinese foreign investment policies in 2002, 2004, and 2007 on Chinese exports. Our differences-in-differences analysis strongly supports the view that Chinese FDI policies are effective in promoting exports. We find that favorable treatment of foreign investment in a particular sector promotes entry of foreign firms that export, and that it raises export values in the targeted industry. Results from triple-differenced analysis show that foreign-owned exporters increase in number when such investment is encouraged and that these firms increase the value of their exports relative to their domestic peers. Using detailed China Customs data, we find that preferential treatment of an industry increases its exports at the extensive margin and is particularly effective in raising exports to the U.S. Overall, we estimate that changes in FDI policy explain almost one-quarter of China's export surge and shifted China's export composition toward high-technology industries. These results are relevant for current discussion of how China uses investment policy to shape its international competitiveness.