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The Role of Special Economic Zones in China's Economic Development As Compared with Asian Export Processing Zones : 1979 - 1995

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Introduction

Since the implementation of economic reform policy in 1979, China's economic development is quite impressive with her average annual rate of economic growth of over 10 % between 1980 and 1995 increasing her GDP from 451.8 billion yuan (or RMB) to 5,826 billion yuan (at current price, (1)). This was by far the highest rate of growth in Asia during this period. The establishment of China's Special Economic Zones (SEZs henceforth) apparently triggered her economic growth together with various growth-oriented schemes. As a result of enhanced economic growth in China after the reform-and-open door policy was launched in the late 1970s, the SEZs entered a new era when the on-going development policy needed to be reconsidered. This accelerated economic development had brought forth at the same time considerable regional disparities, economic and social problems.

Within two decades after the formation of the SEZs and introduction of new industrial policy, China stood at the crossroads and faced the challenge of pursuing further development in an entirely new environment. Problems of various type arose at each stage of development of the SEZs, leading to a heated discussion concerning the Government policy of industrialization. If China is following the 'Geese-flying pattern' of development, what took place in the Asian newly industrializing economies (NIES henceforth, i.e., Taiwan, Korea, Hong Kong and Singapore) followed by the ASEAN countries was likely to take place in China, and the lessons of East Asian Export Processing Zones (hereafter EPZs) might be applicable to the SEZs, since the role of China's SEZs in her accelerated economic development seemed to be fairly comparable to that of the EPZs in high performing East Asian countries. The first Asian EPZ installed at Kaoshiung, Taiwan, as an essential part of outward industrialization strategy was a key element in Taiwan's economic achievement from thenceforth.

However, underlying differences between China and East Asian countries might be too large to apply the East Asian development model. With its characteristic background of her socialist economy, a vast size of spread-over land and enormous regional diversity, China's industrial development may not be able to follow a similar growth pattern known as the East Asian model. Yet we have to admit that China's Special Economic Zones share some common features with Asian Export Processing Zones which were an integral component of export-oriented industrialization (hereafter EOI) policy package for

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the NIES countries specifically Korea and Taiwan. Even though some fundamental differences exist between China's SEZs and East Asian EPZs in other Asian countries, the experiences of the EPZs might be applicable and provide some lessons to China's SEZ at the crossroads.

Here in this paper an investigation is made into the changing role of SEZs in the context of China's economic development, and some of the emerging problems SEZs were confronted with at the new stage of development will be taken up for analysis. An emphasis is laid here on study of policy and performance of the SEZs in comparison with those of Asian EPZs which managed to shift their industrialization strategy from the import-substitution to the export-orientation at the critical stage of development. The SEZs were in a better position to elicit lessons from the experiences of Asian EPZs, despite various conditions and limitations prevailing in China's 'socialist' market economy.

I. Economic Reform / Open policy and the Changing Role of the SEZs

1. Background of the open policy

The SEZs originated from the 'Four Modernizations Slogan' used by former prime minister Chou Enlai as early as in 1964. After Deng Xiaoping's rehabilitation in 1977, he promoted four modernization programs, i.e. the modernization of agriculture, industry, science and technology, and national defense by the use of practical planning that involved capitalistic incentives and techniques. The main purpose of the four modernizations was to quadruple China's 1980 GNP of RMB 480 billion to RMB 1800 billion by the year 2000. Until the start of modernization programs China's external economic policy was rather self-contained and self-reliant, limiting her trade and investment to inward-looking and import-substituting type which had significantly kept her economy stagnant and underutilized. Her long-standing political and economic upheavals and series of ideological conflicts since the Mao period confined her socialist economic policy closed and isolated. Deng's reform was intended to animate her stagnant economy by opening the economy to the outside world and by revitalizing the system through the introduction of foreign capital and technology. When Asian NIES emerged with their remarkable economic success toward the mid 1970s, there was a growing awareness of China's technological backwardness far behind developed countries, inducing the government to place the top priority on technological advance to catch-up by opening the country (Oborne,1986).

Based on the decision adopted at the 11th Communist party meeting in 1978 to implement economic reform and open policy led by Deng, the SEZs were created as an integral part of this policy: four SEZs were set up in 1980, three of them - Shenzhen (near Hong Kong), Zhuhai (near Macao), Shantou (a major home of overseas Chinese) - located in Guangdong Province and one at Xiamen (across Taiwan) in Fujian Province. Fifth SEZ was installed in Hainan Island in 1988 at the time of promotion of the area to the Province status, aiming at developing still largely untapped island economically and socially. These SEZs were all located along the coast which had easy access to sea transport over centuries.

A great step came forward as a part of open policy package with the announcement in 1984 that the experiments of the SEZs would be extended to larger areas inside the country and fourteen coastal open port cities would be opened with special investment incentives for foreign joint ventures (2). Economic and technical zones were installed in these coastal cities with a view to developing emerging businesses and technology-intensive industries. In February 1985, three coastal areas (Pearl River Delta, Southern Fujian Delta, Yangze River Delta) were designated as Open Economic Zones (OEZs) endowed with similar preferential incentives to promote export production and inflow of foreign capital (3). Shanghai and its surrounding areas were thus incorporated in the open policy program.

These coastal regions were all conferred with favorable conditions and special status that were conducive to development of export-oriented economy. China's development strategy introduced in these coastal areas was therefore a natural product of the preceding experiments undertaken to achieve further economic development under new economic circumstances that had necessitated the participation in the international division of labor, exploitation of international market and resources, and at the same time establishment of market economy system in the country. The basic standpoint of the Chinese Government however was that the SEZs would remain the foundation of coastal development within the framework of reform-and-open policy.

2. Special Economic Zone policy

The SEZs were initially established after the model of EPZs, especially in Taiwan and Korea which had already achieved a significant success (4). It is to be noted that within a year before the formation of the three SEZs in Guangdong Province was announced, a small piece of land (about one square kilometer in Shekou) was marked out in Shenzhen as an export processing zone (Sit, 1985).The SEZs were originally intended to serve as a place for testing new reforms of enterprise management, finance and labor matters, which, if found successful, could be applied throughout the country. This was one of the Beijing Government's experiments undertaken for integrated development in the SEZs in order to liven her flagging economy (5). The fundamental object of the SEZs and open cities was to invite foreign investment in various industries with preferential measures and incentives such as preferential tax status to foreign investors, lower tariffs, better infrastructure, more flexible labor markets, and less bureaucratic control (Panagariya, 1993) (6).

A variety of industries including not only manufacturing industries but also service industries (such as hotels, retails, tourist industries), agriculture, housing construction and infra-structural development were all encouraged and open to foreign investment. After a careful study of the existing EPZs in East Asia, the Chinese Government has developed the original

EPZs concept into a new economic zone called the 'SEZ' (7).

China's SEZs represented a unique approach to economic development, inflow of foreign investment, and technology transfer for a country that had long advocated inward-looking self-containment policy under her socialist regime. They are also unique because Chinese policymakers sought, for the first time, to actively link foreign investment with trade in these specific areas. By providing preferential treatment and broader facilities for foreign investment and trade, the SEZs marked the turning point to break with the self-reliant, inward-looking strategy of the Maoist period to switch to the open policy or moderate outward-looking strategy.

The four SEZs and Hainan Island together with other fourteen open coastal cities constituted multi-functional and multivarious front for open door policy. The location of four SEZs were chosen because they were in close proximity to Hong Kong and Taiwan enabling them easy access to information, technology, management know-hows and capital from neighboring as well as from foreign developed areas with their relatively developed facilities of communication and transport. In addition to these economic factors, political considerations were also involved in determining the location of SEZs in Guangdong and Fujian Province. With the anticipated return of Hong Kong, Macao and Taiwan to China, it was important for the Government to reduce income gap as much as possible between SEZs and these neighboring areas so as to undertake integration process smoothly. Another consideration in the selection of SEZs location far away from the major centers of population and industry was to confine the possible disruptions of the SEZs within the existing order (Wong, 1987; UNCTC, 1991, p.242). The expected role of these SEZs could be spelled out as follows (Oborne, 1986; UNCTC, 1991, Wall, 1991; Park, 1996) :

(i) transfer of hi-tech industries into the SEZs;
(ii) experiment and acquisition of modern technology and management expertise;
(iii) creation of employment;
(iv) earning of foreign exchange through promotion of exports;
(v) promotion of economic development and regional development;
(vi) creation of economic links to the domestic economy with Hong Kong (close to Shenzhen), Macao (close to Zhuhai), Taiwan (close to Xiamen) and overseas Chinese communities (Shantou);
(vii) experiment of new economic reform with market forces;
(viii) setting-up of a link between the economic hinterland and overseas.

The SEZs were virtually integral pillars to support the outward-looking strategy. China's SEZ, though it had evolved from the free trade zone concept, had developed into a unique model of its own particularly in light of its socialist setting (Wong, Cai & Chen, 1992).

3. The role of the SEZs compared with those of EPZs

The EPZ introduced as one tool of the policy packages of the outward-oriented development strategy in Taiwan and Korea has been highly responsible for the rapid economic development of those countries. Flourishing free port cities in Hong Kong and Singapore had long been another example of the economic potential of such deregulated trade zones. The success of the EPZs and free port cities in the Asian NIES apparently set the model for China's SEZs to learn the lesson from.

The SEZ and EPZ are both variations of a free trade zone, but the SEZ is a more comprehensive economic zone of considerable size than the EPZ, not a small enclave within a city engaged in modern export-processing of manufacturing production. The physical space of the SEZ is generally much larger than the average size of the EPZs which were often less than 10 square kilometers (Crane, 1991). The original zone of Shenzhen SEZ, for example, had an area of 327 square kilometers and expanded Xiamen SEZ included the whole of Xiamen Island. Hainan Island was in fact China's largest SEZ.

However, the scope of the SEZ is much limited when compared with that of free port cities such as Hong Kong and Singapore fully equipped with absolute autonomy. As opposed to the EPZ, SEZ's economic activity is far more extensive covering a wide range of business activities whereas the conventional type of the EPZ mainly focused on processing and assembly in the manufacturing industry for export. The SEZs were, by all accounts, more ambitious than the EPZ in terms of industrial policies and activities.

Asian EPZs provided with their combined strength of both free trade zone and industrial zone (8) were, at the initial stage of development, mainly engaged in the production of export-oriented, labor-intensive, light manufacturing goods produced with their cheap wages and they gradually began to shift to the production of technology-intensive goods. The SEZs, by contrast, the concept of which being born out of bold economic reform and open policy, were accorded a wider range of status and functions, i.e. a substantial autonomy assured to the SEZs and simplified administrative structure encompassing planning administrations, state banking and insurance (9).

Nonetheless the roles of the SEZs are shared by the EPZs in many ways. Among afore-mentioned eight roles, what the SEZs had basically differed from the EPZs were, (i) transfer of high-tech industry into the SEZ, and (vii) experiment of new economic reform with market forces. Major differences between the two may be attributable to the fact that Chinese government expected the SEZs to serve not only as laboratories for economic reform but also as a window and a bridge to link with the developed countries. But the fundamental difference between the two is that the former operates in a market economy, while the latter are set in a centrally planned environment. Within the EPZs the governments simply removed or eased constraints which had limited the operation of market forces elsewhere in the economy. In China's SEZs, however, the aim was to create market environment in the zones, while maintaining intensive control mechanisms for the rest of the economy (Wall, 1991).

A majority of operating firms in the EPZs were of foreign origin and established by foreign investment (in most cases jointly ventured) and they were only engaged in export production of manufactured goods, as against firms and capital invested in SEZs were either of domestic or foreign origin, and their manufactured products were sold in China as well as overseas markets, though their emphasis was placed on export.

After all, the SEZs were special but enlarged enclaves endowed with limited administrative autarky within a planned socialist economy, and were allowed to perform in line with the policies especially designed for them under direct State planning, whereas the EPZs were established mainly for export promotion with various preferential measures within a market economy. The characteristics of China's SEZ as a development policy should be evaluated taking into account the following. The EPZ was introduced at the time when East Asian countries especially Taiwan and Korea intensified their efforts to produce light industry manufactured goods for export after they had abandoned their import-substitution industrialization (ISI hereafter) strategy to switch to the EOI strategy.

When we look back economic development in Asian countries since the 1950s, this ISI strategy was commonly adopted at the earlier stage of development to foster fledging industries provided with various protective measures. Important measures, above all, included limitation of import of foreign competitive goods except capital goods with prohibitive tariffs imposed. At this stage, strenuous efforts were made by the government as well as by firms to introduce advanced technology and know-hows to upgrade quality of their products. This inward-looking ISI strategy only held good until developing country's (hereafter DC) manufactured goods became fully competitive at international markets. This protective ISI strategy will have to shift to the EOI sooner or later as the production capacity of a DC expands, fulfilling its limited market with her domestic products, and as her balance of trade ran into deep deficits, which was in due course inevitable as development stage advanced under the ISI strategy. At this stage, an outward-looking EOI strategy will be pursued. The DCs started producing predominantly for export by introducing various measures especially in the EPZs to enhance inflow of foreign capital and technology through which the DCs could proceed industrialization.

In contrast with this typical development pattern in East Asia and other DCs operating within a market economy, China's inward-looking development strategy differed substantially from the so-called import-substitution industrialization policy. China's development policy during the Maoist period was fundamentally self-reliant with her limited dependence on foreign capital and technology with an emphasis laid on heavy industry rather than on light industry. Unlike the Asian EPZ established as an integral tool of the EOI strategy after the completion of the ISI stage of development, China's SEZs were not created as a natural outcome of economic development under the ISI strategy. In a way, China, skipping the development stage of the ISI, had entered the EOI stage with the experimental implementation of economic reform. China's SEZ was certainly an essential tool of outward-oriented strategy but at the same time many of foreign-funded firms in the SEZs were engaged in import-substituting production. In this sense the role of the SEZ in China's economic development reflected the dual character of the EOI and ISI (Crane, 1991).

4. Asian EPZs and its Transformation

The idea of modern EPZ was initially an Irish invention. After the first EPZ began operation at Shannon Airport in Ireland in 1959, the EPZs began to appear in the developing world in the mid-1960s. The first Asian EPZ established at Kaoshiung, Taiwan in the mid 1960s was one of the most successful EPZs out of more than hundred EPZs of the same type, setting the model to be followed in terms of foreign trade and efficiency. The EPZs were starting up in increasing numbers by the 1970s throughout Asia, Latin America, Africa and the Middle East. This swift diffusion can be partly explained by the initial successes of the Irish Shannon Export Free Zone, Taiwan EPZs and partly by several attractive features connected with the enclave structure of the zones in developing countries (10) since many of DCs had been disappointed with the ISI strategy commonly adopted. The principal aim of the EPZ was to promote the inflow of foreign direct investment to serve as a vehicle for :

1) increasing foreign exchange earnings by exporting new products and finding markets,
2) providing jobs, supplementing the incomes of their families thereby raising the standards of living,.
3) upgrading skills of the local manpower,
4) creating linkages with the hinterland,
5) transmitting new technology by training local people (11).

This EOI strategy followed closely on the coming of age of multinational corporations (henceforth MNCs) which had since the 1950s rapidly developed from their earlier involvement in the extractive and infrastructure sectors into the manufacturing sector in the developing countries. The MNCs, many of which were operating in the EPZs, had played an important role of expanding exports of manufactured goods from the DCs in raising the DCs' share of world exports of manufactures almost three times within twenty years from 1965 (from 4.6% in 1965 to 13.1 % in 1984) (ILO, 1989). It turned out that the EPZs have not only attracted the large and well-established MNCs from Europe and the US but also have formed a breeding ground for inexperienced MNCs and even for MNCs from the DCs. This was especially the case in Asia, where the rapid industrialization and accumulated experience primarily in the NIES countries had enabled them to engage in foreign production (Johansson, 1994). The establishment of the EPZs or FTZs (Free Trade Zones) was instrumental in pursuing this EOI strategy undertaken by the Asian NIES countries during the 1960s and 1970s.

In the early 1970s when the EPZs were gaining popularity, three major objectives of the EPZs were articulated: foreign exchange earnings, employment creation and technology transfer. Competition among host countries for "footloose" processing activities meant that individual countries generally had found it more difficult to attract foreign investment. While the first two objectives were somehow met to the extent that firms were attracted, the substantial gains from "technology transfer" had not occurred at the earlier period, since the EPZs were generally isolated from the domestic economy (Warr, 1988). Major industries in the EPZs were confined to the following two footloose industries in the earlier stage; textile / clothes industry and electronics industry. The products in these industries were low skilled and labor-intensive. The MNCs had invested in the EPZs in many cases to exploit cheap labor and generous incentives offered which were, in the main, the sources of international competitiveness. The success of the EPZs made possible by an increase in exports has led to a rapid economic growth together with an increase in income level.

The wage increase gradually began to erode their competitive edge which had stemmed from low-cost labor. An impending option for Hong Kong and South Korea or Taiwan, for example, was to relocate existing production based on low-cost labor to countries where cheaper labor were available and non-binding quotas were imposed. As economic development advanced in these countries, an emphasis had shifted from labor-intensive, low value-added to high-tech, high value-added technology industry in the selection of inward FDI, forcing their industries of comparative disadvantage to relocate in the less developed, lower wage countries/regions including the SEZs.

The performances of Asian EPZs were, however, quite varied ranging from poor to satisfactory. Out of 21 Asian EPZs that had existed toward the end of 1970s, only a few could have matured after passing through formative periods (12). Among the successful are the Taiwan and South Korean EPZs established in the mid-1960s and early 1970s. About two-thirds of the total number of firms (483) in Asian EPZs at the end of the 1970s were located in five EPZs in Taiwan (three EPZs) and Korea (two EPZs). The EPZs in both countries were entering a new stage of development at that point. Due largely to their continued rise in labor costs brought forth by economic development, a number of new investments became marginal, being directed mainly to technology-intensive industries. Labor-intensive industries were rapidly losing international competitiveness.

In Taiwan's EPZs, many of those labor-intensive industries were closed down or forced out of EPZs to transfer to other less developed countries such as Thailand, Indonesia, Mexico, etc., where sufficient labor force was available at lower wage (Asian Productivity Organization, 1983, (13)). The number of closures in Taiwan EPZs was rapidly increasing over the years, i.e. 9 in 1975, 15 in 1976, 18 in 1977 and 21 each in 1978 and 1979 (14), though Taiwan's EPZs are reputed to be most successful together with Korean EPZs. However the number of incoming firms into the Taiwan EPZs made up for and kept the total number of operating firms fairly constant between 220 and 250 after the mid-1980s up to the mid-1990s. But the total amount of FDI into the Taiwan EPZs had dramatically increased over 100 times in 30 years from US$ 15.6 million (1967) to US$ 1,930 million (1997) reflecting the changing pattern of FDI into more technology and capital intensive type (15).

In Korean case, the total number of firms in the Masan EPZ established near Pusan in 1970 first rose drastically earlier from 4 firms in 1970 and reached its peak of 115 firms in 1973 but gradually reduced to 75 around the mid 1980s and stayed constant between 70 and 75 during the 1987-1995 period. Like the Taiwan case, the total value of export from the Masan EPZ had increased dramatically almost 250 times in 23 years fromUS$ 9.7 million in 1972 to US$ 2.4 billion in 1998 (Korea Ministry of Industry and Trade, 1998).

The contribution of the electronics and electric appliance goods export (83% (1998) in Taiwan, 84% (1995) in Korea) is responsible for the rapid increase in the value of total export of the EPZ in both countries (16). In view of the declining export earnings in the labor-intensive industries, however, Taiwan had decided to shift to the production of higher value-added products both inside and outside the EPZs. The establishment of Science Park near Taipei aimed at encouraging research and development of high technology was the efforts initiated by the Government along this line. Korea introduced more or less similar policy. However as offered tax incentives and other motives expired, the relative importance of the EPZ began to gradually decline in spite of increased inflow of FDI. This phenomenon seems to indicate that as the country develops, the comparative advantages offered by the zones in terms of infrastructure and special privileges would diminish and result in the role of EPZs being more or less indistinguishable from the rest of the country.

II. Economic Performance of the SEZs

1. Economic development in Guangdong, Fujian and Hainan Provinces

Of all economic reform measures and open policies implemented since the late 1970s, the most important contribution to remarkable economic growth achieved in Guangdong, Fujian and Hainan provinces was the establishment of the SEZ which had provided a focus to investment activity, both domestic and foreign. Growth rates of GDP and industrial production in three provinces with SEZs were much higher than the national average (Table 1).

China, the largest recipient of foreign direct investment (FDI) in the developing world, actually had received the cumulative amount of US$128.1 billion of FDI between 1979 and 1995, which accounted for over 40 % of all FDI directed to all developing countries (17). But the distribution of the FDI flowed into China is geographically concentrated. The coastal areas accounted for over 90% of all FDI received since 1979. Among coastal regions, Guangdong, Fujian, Shanghai and Jiangsu have been major hosts to substantial amounts of FDI. Above all, Guangdong took the lion's share. During the first 10 year period (1979 - 87) after the reform, about 60 % of the total FDI flowed into Guangdong, and 10% into Fujian Province (18) (Pomfret, 1989). In terms of cumulative FDI up to 1992, Guangdong comes first on regional basis, accounting for 40 % (US$ 12.1 billion) of the total inflow (US$ 30.3 billion), followed by Fujian with the share of 10 % (US$ 2.9 billion) (Table 2). Towards the late 1980s and onwards, the FDI inflow into Guangdong Province had grown larger but its share of total FDI continued to decline from 60% (1979-87) to 40% (1979-92) because of increasing regional dispersion of FDI since the mid-1980s as fourteen open coastal cities and three open economic zones were established and as the Government adjusted the regional distribution of FDI by sector. Hainan Province, in contrast, designated as the fifth SEZ in 1988 started to develop by introducing an increasingly large volume of FDI, but the size of FDI inflow was still limited and its growth was much slower than its counterpart in Guangdong and Fujian (Tables- 2, - 10). The Hainan economy with its small size and its lower level of industrial output is still far behind Guangdong and Fujian.

Table- 1 GDP and Industrial Production : China and Provinces with SEZ, (100 million yuan)

		1980	1985	1990	1995	Annual average growth rate (%)	
National	GDP	4,518	8,964	18,531	58,261	9.8	(1979-94)
	Industrial production	5,154	9,716	23,924	91,894	14.9	
Guangdong	GDP	250	577	1,559	5,734	14.4	(1979-96)
	Industrial production	234	505	1,907	7,458	21.7	
Fujian	GDP	87	200	523	2,160	23.9	(1980-95)
	Industrial production	81	173	531	2,881	26.9	
Hainan	GDP	19	57*	102	364	21.8	(1980-95)
	Industrial production	7	21*	44	177	24.1	

Note: 1. Figures with * indicate the 1987 data. **2.** Average growth rates of Fujian and Hainan were computed based on current price, whereas National and Guangdong growth rates were official figures from the yearbook. Current price figures tend to be much higher. **Source:** China Statistical Yearbook, various issues. Guangdong Statistical Yearbook, various issues. Fujian Statistical Yearbook, various issues. Hainan Statistical Yearbook, various issues.

Table – 2 Chinese FDI Inflows by Region (Cumulative FDI in China, US$ Million)

Region	1985	1987	1989	1990	1991	1992	Total	Per Capita*
Coastal	1,181.42	1,578.44	3,107.03	3,201.33	4,092.21	10,046.50	27,455.99	54.35
Guangdong	651.31	736.87	1,252.06	1,582.31	1,942.88	3,701.11	12,051.49	184.70
Fujian	118.60	55.35	348.03	348.89	472.16	1,423.64	2,944.64	75.25
Jiangsu	33.47	86.35	126.93	133.97	219.22	1,463.24	2,222.45	32.16
Beijing	88.82	105.79	320.16	278.95	244.95	349.85	2,041.41	185.25
Shanghai	107.54	214.01	422.12	174.01	145.19	493.61	1,938.55	144.13
Hainan	------	-----	94.97	103.02	176.72	425.55	944.70	137.71
Other regions		-- ---		(data skipped)		------		
Inland	136.09	203.75	330.30	234.82	333.71	957.52	2,838.51	4.30
Total	1,317.51	1,782.19	3,437.33	3,436.15	4,425.92	11,004.02	30,294.50	25.99

Notes: Figures with * indicate per capita US dollar income as of 1992. Total includes the figures of other regions. **Source:** China Statistical Yearbook, various issues.

1- 1 Guangdong Province

Economic development in Guangdong Province with three SEZs (Shenzhen, Zhuhai and Shantou) was quite dramatic with the average growth rate of GDP of 14.2 % between 1978 and 1995, which is by far greater than the national average of 9.9 %. Before the reform was implemented, Guangdong Province ranked 6th nationally in 1978 in terms of GDP, accounting for only 5 % of China's total GDP, but its rapid growth raised the Province to rank no.1 in 1995 with its enlarged share of 9.3 % of national GDP (19) (Table – 3). External trade of Guangdong Province grew at a faster rate than the national average, resulting in no.1 among all the provinces in terms of the volume of exports. Economic performance of Guangdong was far better by all accounts than that of national China as shown in the Table 3. Guangdong accounted for 38 - 40 % of China's total exports In the mid-1990s (Table 4). A rapid economic development in Guangdong was predominantly led by impressive growth realized in three SEZs especially Shenzhen with its enlarged shares in the Province during 1980-95 period (Tables 5, 6). Most spectacular growth achieved in Shenzhen SEZ is expansion of exports and industrial output. A rapid rate of economic development in Shenzhen was principally achieved by a large volume of FDI inflow and exports expansion.

Table- 3 Macro Economic Indicators of Guangdong with the National Average

(annual average rate of growth) (%)

	Guangdong		China		Share of Guangdong	
	1991-95	1978-95	1991-95	1978-95	1978	1995
Population	1.7	1.7	1.2	1.4	5.3	5.6
GDP	19.1	14.2	12.0	9.9	5.1	9.3
(per capita)(Yuan)	(365)	(7,927)	(373)	(4,810)	(0.98)	(1.65)
Agricul. Production	5.7	6.7	6.7	(a) 6.7	6.1	7.1
Industrial Production	32.4	21.9	22.2	(a) 15.7	4.7	9.9
Invest. In fixed Asset	43.6	29.0	34.7	(a) 22.9	4.2	12.0
Exports	31.9	22.2	19.1	17.4	14.2	37.2
Foreign capital Utiliz.	43.0	(b) 30.9	36.1	(b) 26.3	19.8	25.1
Budget revenue	37.1	17.7	16.3	10.6	3.5	6.2

Note: 1.GDP, agricultural and industrial production is real terms, but the rest is nominal.

2. Figures (a) are for 1980-95, and figures (b) are for 1985-95.

3. Per capita GDP figures are nominal value of 1978 and 1995.

4. Figures in the parenthesis are per capita income in Yuan.

5. Abbreviations: Agricul.= Agricultural, Invest.= Investment, Utiliz.=Utilization.

Source: Derived from China Statistical Yearbook 1996, and Guangdong Statistical Yearbook 1996.

Table- 4 Import and Export by Location of China's Foreign Trade, (US$ Billion)

	1994		1995		1996	
Region	Exports	Imports	Exports	Imports	Exports	Imports
National Ranking	121.0	115.6	148.8	132.1	151.1	138.8
	(100%)	(100%)	(100%)	(100%)	(100%)	(100%)
1. Guangdong	50.2	46.5	56.6	47.3	59.3	50.6
Share (%)	(41.4)	(40.2)	(38.0)	(35.8)	(39.2)	(36.5)
2. Beijing	8.3	20.9	10.2	26.8	8.1	22.2
3. Shanghai	9.2	8.9	12.9	11.4	13.0	14.1
4. Fujian	6.4	5.8	7.9	6.5	8.4	7.1
Share (%)	(5.2)	(5.0)	(5.3)	(4.9)	(5.6)	(5.1)

Notes : Figures in ( ) are percentage shares. **Source:** Derived from the figures in China Statistical Yearbook 1997.

Table- 5: The share of Shenzhen SEZ in Guangdong Province

	1980	1995		1980	1995
Population	0.6 %	5.1%	Export	0.5%	36.3%
GDP	1.1 %	16.6	Import	1.7%	38.6%
Inflow of FDI	22.7%	12.7%			

Source : Data derived from Guangdong Statistical Yearbook 1997, and Statistics and Information Yearbook of Shenzhen 1998.

Table – 6: Shenzhen, Macro Economic Indicators

	1980	1985	1990	1995	1996
Population (10,000)	33.29	88.15	201.94	345.12	358.48
GDP (10,000 yuan)	27,012	390,222	1,716,665	7,956,950	9,500,446
Per capita Disposable Income (yuan)					
(Urban resident)	---	1915	4127	12,771	16,296
Gross Industrial Output (10,000 yuan)					
	10,632	246,662	2,202,180	12,264,893	14,276,969
Consumer Price Index					
(1979=100)	105.0	167.2	331.2	584.1	629.1
Export (US$10,000)	1124	56,340	815,165	2,052,736	2,120781
Import(US$10,000)	627	74,292	754,971	1,824,224	1,784,561
FDI (US$10,000)	2755	17,989	38,994	130,989	205,065
Equity Joint Venture	252	6993	26,849	33,120	89,228
CJV	1891	10,316	4917	28,003	26,776
WFO	612	680	7228	69,866	89,061

Note: FDI=Foreign Direct Investment. CJV=Cooperative Joint Venture. WFO=100% foreign owned.

Source: Statistics and Information Yearbook of Shenzhen 1998

1- 2 Fujian Province

Fujian province, a hometown of hundreds of thousands of overseas Chinese, one of least developed areas in the country before the reform, had also achieved rapid economic development apparently spurred by the establishment of SEZ in Xiamen area. The reform-and-open policy was responsible for accelerated growth in the region, raising the average annual growth rate from 11% during the 1980 -1990 period to 19.3 % during the 1990 –1995 period with a resultant rise of GDP from one of the lowest rank in the country to 11th in 1995 (Table 7). Fujian's annual average growth rate of GDP was enhanced drastically to 19 % in the first half of 1990s, almost twice as high as the rate recorded during the previous decade (1980s), enabling a significant increase in industrial production (annual average rate of growth: 30.2%). This rapid growth was achieved predominantly by an increasingly huge inflow of FDI (annual rate of increase of 131% in 1990-95), which has in due course brought forth a rapid increase in export. Export share of primary goods was reduced to half from 45% to 20% in ten years (1985-1995), while the export share of industrial goods was on gradual increase from 55 % to 80% (Table 8).

Fujian Province, as a result, had become one of the major centers of international trade in the country to be ranked 4th in 1994 having successfully achieved the targeted goal as early as in 1992 to increase its regional GDP four times by year 2000 (Table - 4). The size of FDI inflow and industrial production in Xiamen SEZ remained relatively small through the mid-1980s however it accelerated in the early 1990s. A dramatic increase in export had taken place reaching from US$140 million (1980) to US$3.48 billion (1995) (Table 9).

Table – 7 Macro Economic Indicators of Fujian Province

(annual average rate of growth) (%)

	1980-90	**1990-95**	**1996-2000** (9th 5-year Plan)
GDP	11	19.3	11
Industrial Production	17.3	30.2	13
Agricultural Production	7	10.1	5
Budget Revenue	13.8	26.3	11
External trade	19.9	35.9	14
Inflow of FDI *	16.8	131.0	150.0
Price Change	7.8	14.4	8

Note : FDI* indicates 100 million US dollars of Foreign Direct Investment.

Source: Jetro Hong Kong (1997)

Table – 8: Fujian, Composition of Export Items, %

Items	1985	1990	1991	1992	1993	1994	1995
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
Primary goods	44.7	21.8	21.8	18.0	16.0	18.5	20.3
Industry goods	55.3	78.2	78.2	82.0	84.0	81.5	79.7
1)Heavy Industry goods	18.6	27.4	23.1	21.4	22.8	21.2	22.2
2)Light Industry goods	34.1	48.6	53.4	59.5	61.2	60.3	41.0

Source: Fujian Statistical Yearbook 1996

Table – 9: Fujian, Major Indicators of Xiamen SEZ

Item		1980	1985	1990	1995
Industrial production	(million yuan)	9.66	21.85	64.91	337.65
FDI	(million yuan)		3.63	36.50	247.18
Export	(US$ 10,000)	14,027.00	16,527.00	78,148.00	347,915.00
Foreign Capital actually used	(US$ 10,000)		8,624.00	7,273.00	161,823.00

Source: Fujian Statistical Yearbook 1996

1- 3. Hainan Province

Hainan Island, one of the poorest regions in the country through the mid-1980s, began to develop rapidly after the establishment of the SEZ by attracting FDI with its increasing comparative advantage of cheap labor cost as wage level became higher in Guangdong. The underdeveloped infrastructure in the island, one of the most serious bottlenecks for inviting FDI, was gradually developed with various preferential policies (such as income tax incentives). With its decentralized and market-oriented approach, Hainan economic development was spurred toward the late 1980s and its per capita income caught up with the rest of the country in the early 1990s (Tables 3, 10). Foreign capital used in the province increased rapidly in seven years after the designation of the SEZ from US$ 9 million (1987) to US$ 145 million (1995). But growth of GDP and exports was disproportionately smaller than the growth of foreign capital utilization. Due to increase in imports the balance of trade ran into deficits from the mid 1990s. Compared with Shenzhen, Hainan's economy was still lagging far behind Shenzhen as of 1995 with its per capita income (4,850 yuan) being less than 40% and its total export value (US$ 830 million) accounting for 4% of Shenzhen's equivalents respectively (Tables 6, 10).

Table – 10; Major indicators of the Hainan Province

	1980	1987	1990	1995	1997
Population (10,000)	553	615	651	702	725
Per capita income (yuan) (only urban areas)	354	986	1650	4850	5,698
Retail price index (1978=100)	109.3	157.8	257.3	483.6	491.2
Foreign Capital actually used (US$10,000)	28	911	18,982	145,501	112,134
Export (US$10,000)	1829	11,545	47,138	83,000	88,966
Import (US$10,000)	-	17,696	46,559	143,774	105,935

Source: Statistical Yearbook of Hainan 1999

2. The SEZ as the engine of growth

A rapid growth in Guangdong was brought about primarily by fast economic development in three SEZs. Since the adoption of the open policy in 1979, economic growth in four SEZs located in Guangdong and Fujian Provinces was overwhelming. Above all, the role of Shenzhen SEZ was quite significant in expanding trade and attracting FDI, which contributed largely to the development of the Province. In contrast, growth in Hainan Province was rather slower because of its short history as a SEZ and partly because of its locational disadvantage. Industrial output of four SEZs at Shenzhen, Zhuhai, Shantou and Xiamen had increased at a fast rate, amounting to 22.57 billion yuan (6 billion US dollars), or 10.7 times in eight years after the establishment of the SEZs (Yeung & Hu, 1992).

This fast growth is quite striking considering that the SEZ localities were sleepy towns of negligible economic significance before 1979. Of the four SEZs, especially Shenzhen's growth of industrial expansion is extraordinary, that is, the gross industrial output had increased from 27 million RMB in 1980 to 142.7 billion Rmb in 1996 (Table-6**).** This accelerated growth was achieved for the most part by a huge volume of FDI flowed into the SEZs. However international trade in the SEZs has been rather sluggish and limited until toward the late 1980s (Table - 11), even though the SEZs were conceived primarily as a means of promoting exports, absorbing FDI and technology transfer. Shenzhen's export had started to increase at a accelerated pace from the mid 1980s prodded by urgent measures undertaken in 1985 by the Government to promote export (20). These measures have taken effect in raising an annual average growth rate of export from four zones to 83% in 1985-87 (Wang, 1993). After a decade of investment and growth, the four SEZs generated a total of US$ 9.7 billion of export value in 1990 (Table - 11). The export of four SEZs started to grow at a dramatic rate from the mid 1980s. This exceptionally rapid expansion of trade apparently has been propelled by foreign as well as domestic investment. A majority of FDI that had flowed into Guangdong was concentrated in the three SEZs, above all, in Shenzhen SEZ.

Table – 11 Export Value from China's SEZS 1979-95

(Million US$)

SEZ	1979	1980	1981	1982	1983	1984	1985	1990	1995
Shenzhen	9	11	n.a	16	21	265	563	8152	20,541
Shantou	---	----	---	n.a	n.a	4	35	419	2,129
Zhuhai	---	9	n.a	n.a	n.a	18	57	348	2,518
Xiamen	---	----	---	----	----	1	25	781	3,479
Total	9	20	n.a	n.a	n.a	289	680	9700	28,667

Source: The data Until 1985 were derived from Wang (1993). The data of 1990 and onwards are derived from Guangdong Statistical Yearbook, various issues. Xiamen data of 1990 and 1995 are derived from Fujian Statistical Yearbook 1996.

A cumulative total of roughly US$4.1 billion actual foreign investment had flowed into the five SEZs (including Hainan) within ten years after the reform (Crane, 1991). By 1986 about 21 % of total amount of agreed FDI in China was already accounted for by the four SEZs (Pearson, 1991). Among the four SEZs, the Shenzhen SEZ with its largest size and the powers it had possessed to offer concessionary terms to FDI, still continued to enjoy a dominant position as a major absorber of FDI (21). Leading the country in the amount of FDI actually realized, even surpassing Beijing and Shanghai, Shenzhen had accounted for approximately 20 % of the national and 40% of the Guangdong provincial total foreign capital in the late 1980s, contributing significantly to the absorption of foreign capital into the country (22) (Wong, Cai & Chen, 1992) (Table 2, Table 6). As for the case of Xiamen SEZ in Fujian Province located across Taiwan, by contrast, an inflow of FDI had remained nominal at the early stage, but it gradually increased from the mid 1980s and started to grow phenomenally toward the late 1980s, though Xiamen lagged far behind Shenzhen in terms of absorbed amount of FDI (Tables 6, 9). A huge increase in the inflow of FDI was caused by a flood of Taiwanese capital as the political tension lessened between the mainland and Taiwan. As a result, Taiwan finally replaced Hong Kong in 1988 as the most important source of 'foreign' capital received by Xiamen (Li & Zhao, 1992). WFO (wholly foreign-owned) form of investment had increased in the mid 1990s to account for more than half of FDI inflow predominantly from Taiwan (Table 12).

Table – 12: Fujian, Foreign Direct Investment by form, (US$ 10,000)

Year	FDI	EJV	CJV	WFO	other FDI
1979	83	15	68		320
1980	363	288	75		527
1985	11,782	8,566	2,950	266	78
1990	29,002	12,617	2,780	13,605	3,113
1995	403,881	124,872	54,073	224,936	509

Note: EJV=Equity Joint Venture, **CJV**=Cooperative Joint Venture, **WFO**=Wholly Foreign Owned

Source: Fujian Statistical Yearbook 1996

When we break down FDI received by the four SEZs by country origin, a dominant position of Hong Kong and Macao was apparent in the 1980s. For example, more than 80 % of equity joint ventures (EJVs) into the SEZs had originated from these two 'foreign' regions in the latter half of 1980s (Table 13). In the Shenzhen SEZ, more than 90% of investment cases and two-thirds of actually invested amount of FDI during the first 10 years (1979 - 89) came from Hong Kong. Japan was the second largest investor during the same period (Mituida, 1996). Macao's FDI was mainly directed into neighboring Zhuhai. Hong Kong remained no.1 investor in Shenzhen over seventeen years (1979-95) since the establishment of the SEZ with its total cumulative amount of US$ 6.1 billion, followed by Taiwan which had abruptly increased FDI since the late 1980s（Table 14）.

Table- 13: Origin of Investors of EVJs in the SEZs. 1985 –1988 (Sample)

Location of Investment	Origin of Investors: **HgKg / Macao**	**United States**	**Japan**	**Other Asia**	**W.Europe / Canada**	**Total**
Shenzhen (a)	164	14	3	11	4	196 (62.0%)
Shantou	16	0	0	2	0	18 (5,7%)
Zhuhai	30	1	2	3	1	37 (11.7%)
Xiamen	40	5	3	14	3	65 (20.6%)
Total(all SEZs)	250 (79.1%)	20 (6.3%)	8 (2.5%)	30 (9.5%)	8 (2.5%)	316 (b) (100.0%)

Note: (a) Shenzhen figures exclude cases listed in the Almanac as located in Baoan County, which surrounds Shenzhen SEZ, and cases for which the origin of the investor not identified.

(b) Of these, 56 were established in 1985, 129 in 1986, 98 in 1987, and 33 in 1988.

Source: Pearson(1991).

Table - 14 Inflow of FDI into Shenzhen : 1979 –95

	No. of Agreements	Actual Investment (US$ 10,000)
1.Hong Kong	15,348	613,723
2.Taiwan	579	245,551
3.U.S.A	441	55,068
4. Japan	276	170,289

Source : Jetro Hong Kong (1997)

These foreign investments in the SEZs were primarily undertaken jointly by foreign investors and local partners (23), but towards the late 1980s Chinese firms had increasingly invested in the SEZs with a view to taking advantage of various preferential measures (24).

Chinese manufacturers in the SEZs were predominantly engaged in the production of consumer products in the light industry such as electrical /electronics goods, handbags, toys, watches, shoes, garments, etc., which were generally manufactured by simple labor-intensive assembly and processing plants operating on a small scale. Many of those firms from Hong Kong had been producing under subsidiary contracts with their parent companies for re-export from Hong Kong. The Hong Kong's re-export share of her total exports increased from 20 % in the mid-70s to 75 % in 1992. In the initial stage of SEZ, however, a significant portion of investment had been directed to the tourist, property and commerce sectors, whereas manufacturing industry had still played a very minor role. Thus export of industrial products was quite limited, being unable to earn an expected amount of foreign exchange.

III. Evaluation and Implications of the SEZs

China's SEZs, an integral component of the reform and open policy initiated in 1978, was a major driving force in pushing economic development in the Guangdong and Fujian provinces. As we have seen in the preceding analysis, an overall performance of the SEZs has been quite satisfactory when we look at regional growth figures and development of physical facilities in these two provinces. The economic impacts generated by the establishment of the SEZs were extensive, covering not only above mentioned two provinces but also the rest of the country. However, the relative importance of the SEZs has gradually dwindled with the shift of development strategy, and the role of the SEZs had undergone some changes as the stage of development advanced.

The economic performance of the SEZs and types of problems inherent to the SEZs varied substantially at each stage of development. Tentative evaluation of their performance in each stage of the SEZ will be undertaken in the following section. Three stages are distinctly divided from the start of reform and open policy until 1995 ; the first stage is from 1978 to the mid

1980s, the second stage from the mid 1980s to the early 1990s, and the third stage from the early 1990s to the mid 1990s.

1. First stage of the SEZ : 1979 – the mid 1980s

The performance of the SEZs during this experimental period revealed some disappointment among Chinese policymakers and created much criticism despite a considerable economic growth achieved in the SEZs. Even the SEZ policy itself was attacked. A relatively limited amount of FDI flowed into four SEZs in this stage. Shenzhen is said to have failed in its role as a SEZ as it was not able to sufficiently achieve targets originally intended such as technology transfer, earnings of foreign exchange, creation of employment, etc.. External capital invested in Shenzhen was at first channeled mainly toward the tourist and property development sectors. In 1980, for example, only 10 % of total FDI was in manufacturing (Sit, 1985). During this period, a majority of FDI which had flowed into the manufacturing sector took the form of small scale sub-contracting or intermediate processing of light industrial products or assembly for the purpose of producing labor-intensive, low value-added goods such as textiles, food and beverages, household items and electronics, etc..

In this period it is estimated that about 90% of FDI in Shenzhen had originated from Hong Kong (Wong, 1987). Moreover, a significant volume of investment in the SEZs involved domestic capital which had flowed into the SEZs to take advantage of preferential status accorded to the firms within the SEZ (Yao, 1995). Thus transfer of high technology was hardly possible. Difficulties in accessing to the Chinese Market, the non-convertibility of the Chinese currency and unfamiliarity with the rules deterred foreigners from investing in China. The most popular form of investment during this period was through cooperative operation or CJVs (cooperative joint ventures) to reduce the risk (Table - 6).

The SEZs having failed to establish an export-oriented, foreign-financed industrial base, "entrepot" economy has thus developed with unsatisfactory achievements in foreign exchange earnings and technology transfer (Wong, Cai & Chen, 1992). Disappointingly, majority (up to 80% in 1984) of products which consisted largely of traditional goods were sold domestically, leaving only 20% for exports (Wang, 1993). With a high rate of inflation and cost ineffectiveness in attracting FDI in addition to economic crimes and related social problems coupled with a huge volume of infra-structural investment and mounting deficits in the balance of trade due to staggering exports and a rapid increase in imports, the controversy surrounding Shenzhen SEZ was triggered. The debate had called into question the acceptability and long-term viability of the SEZs. The central government had thus reoriented its reform policy in 1984 by designating fourteen coastal cities as open cities and extended its SEZ experiment to inner provinces. Unprecedented experiments undertaken to accommodate capitalist elements were not without some success, though not satisfactory (25). Yet the potential benefits of the open door policy were recognized.

2. Second stage of the SEZ: mid 1980s - early 1990s

The high economic growth rate, a large inflow of FDI and its increased role in the economy, and higher export ratio (Export/GDP) realized during this period indicate a remarkable success of the four SEZs and fourteen coastal open cities as shown Table 15. However a unique role of SEZs began to decline towards the mid 1980s and the dominant position of the SEZs had been reduced (Pomfret, 1989) as more and more newly opened coastal cities were opened and granted similar preferential incentives accorded to the SEZs. A larger part of FDI tended to shift to other regions such as Pearl River Delta and Jiangsu area partly because of a wage increase (26). In 1985, three large coastal regions, i.e. Pearl River Delta, South Fujian Triangle area Delta and Yangze River Delta were declared Open Economic Zones (OEZs). Open cities were extended along the coast from the south to the north. This was another big breakthrough towards to opening up to the world.

The installation of the OEZs was a new way devised by the State Council to absorb FDI to meet the growing demand for foreign capital as the problems in the SEZs became evident (Pearson, 1991). Because of a failure of the SEZs to achieve intended targets in its first stage, Deng Xiaoping stressed that the SEZs should serve as a "window for hi-technology" through which advanced technology and management know-hows be introduced. The SEZs had thus undergone noticeable changes in the major sectors of manufacturing industry. Above all, the electronics industry which was almost negligible before the reform, had witnessed a dramatic growth, accounting for, in 1987 for example, 45% of total value of manufacturing production in Shenzhen. This growth had substantially contributed to an increase in export of electronics products from Guangdong province (Wong, Cai & Chen, 1992)(27). However, backward and forward linkages of the firms in the SEZs operating in predominantly weak domestic economy needed to be established.

Employment creation effects generated by a rapid economic growth triggered by an enhanced large inflow of FDI in the SEZs were quite substantial, though accompanied by inflation, i.e. a skyrocketing hike in land price, rents and price of commodities. Per capita income in the SEZs also rose at a considerably higher rate than the national average. As a result, a serious regional income disparity was produced between the provinces with SEZs and national China (28). At the same time, an increasing number of social and economic crimes such as corruption, illegitimate trading, smuggling, environmental contamination, labor strikes, etc. had also taken place leading to a controversy concerning the justifiable role of the SEZs. Some hard-lined opponents had strongly repudiated the SEZ itself and its policy.

Table – 15: Selected Indicators of SEZs and 14 Coastal Open Cities.1991

	Actual Industrial Growth Rate, 1984-91[(a)] (in percent)	Exports / GDP, 1991 [(b)] (in percent)	Foreign Investment, 1991 (in millions of U.S. dollars)	Foreign Investment / GDP, 1991 (in percent)
14 coastal open cities	9.9	116.8	2434.0	7.2
As percent of China total	82.2	701.3	24.0	262.1
Shenzhen	41.2	382.6	477.0	18.5
Zhuhai	45.4	186.3	157.0	13.6
Shantou	27.0	252.9	197.0	27.0
Xiamen	24.7	118.7	183.0	17.1
4 SEZs	34.2	273.5	1013.0	18.3

Note: (a) The national consumer price index was used to deflate industrial output to constant prices.

(b) Trade data for the coastal cities reflect their use as entrepots for the surrounding region.

Source: Bell, Khor & Kochar (1993).

3. Third stage of the SEZs: early 1990s - mid 1990s

Reviewing the overall performance of the SEZs from its inception in the framework of reform policy, some policy changes were made in this stage by the government. In response to Deng Xiaoping's speech made in 1992 during his tour of Southern provinces urging local governments to speed up the opening of the economy for further development, there was a surge in the inward FDI between 1992 and1993 which had increased at a unprecedented rate. New sectors and areas were opened for FDI. Even previously forbidden sectors such as domestic retail, finance, tourism, real estate, shipping, and resource development were allowed. Thus thousands of SEZs were established by local governments in an effort to attract FDI, though most of them had failed due to shortage of the projected amount of FDI (Wei & Liu, 2001).

Despite the fact that the open policy was extended to the inner part of the country to promote development in the backward areas, regional disparities had not been much reduced, rather worsened in this period. Quite a rapid economic development was achieved in open coastal cities such as, among them especially Shanghai while a majority of inland areas still remained underdeveloped. Shenzhen SEZ was criticized for its corrupted practices, inferior working conditions and frequent labor strikes (29). It was no longer possible to continue the same development strategy as before. The SEZs were losing many of advantages and competitive edges once they had enjoyed. Their relative position in terms of inflow of FDI and industrial output began to deteriorate. The SEZs stood at the crossroads in the face of inherent contradictions. From the mid 1990s onward the investment boom seemed to have cooled down. The number of new projects approved each year continued to decline (30).

The major target set for regional development policy projected for the national 9th Five Year Plan (1996-2000) was to reduce regional income disparity. It was announced that the tax incentives accorded to foreign investment in the SEZs were partially lifted to achieve balanced growth among regions. Several inland cities were granted the same open status as the SEZs. According to a development plan prepared by Shenzhen, a further emphasis was laid on hi-technology industry in the selection of incoming FDI with a view to gradually modernizing industrial structure by shifting labor-intensive to technology and knowledge-intensive industry (Kojima,1990). In June 1997, an ambitious construction plan called 'Hong Kong - Shenzhen Hi-tech Corridor' was announced to promote hi-tech industry. This was exactly the challenge what the EPZs in East Asian countries such as Taiwan and Korea had encountered in the 1980s in their shift to high value-added industrial structure capable of higher wage. Development of economic and social infrastructure will assist achievement of targeted goals of reducing regional disparity by distributing fruits of development to the inner provinces and also of reorganizing outdated industrial structure.

Conclusion

Economic growth in China has been impressive since the reform-and-open door policy was adopted. The role of the SEZs in regional as well as national economic development was quite significant despite all the surrounding and inherent problems. The installation of the SEZ, after the successful model of the Export Processing Zone in East Asia, was indeed an unprecedented experiment to animate its economy by introducing capitalist elements into China's socialist economy which had been stagnant for long under self-contained protective industrialization policy. The SEZ was virtually the key instrument in the open–door policy, though its relative importance declined as the stage of economic development advanced.

However the overall economic performance of the SEZs at the first stage through the mid 1980s, was rather disappointing. Entangled with various social and economic problems caused by drastic changes the SEZs had invited scrutiny and criticism. Many of these problems may be attributable to the fact that China was then at the period of transition, i.e., transition from low income to middle income developing country, and transition from centrally planned economy to market economy. The reform-and-open policy had to be modified to cope with the problems such as expanding inequity and regional disparity, and the experiences of the SEZ were extended to the wider areas opened with similar preferential incentives. The experience gained through the management and operation of the SEZs helped considerably contributing to enhanced growth in the opened regions.

The SEZ has played a more important role in China's economic development than what the EPZ had played in the development of Asian NIES and ASEAN countries. China's transformation to a market economy was enhanced rapidly with the success achieved in the SEZs. Notwithstanding the lessons of the EPZs seem to have a limited applicability to the SEZs operating in fundamentally socialist system in China. Economic and political considerations made it all the more complicated to pursue economic efficiency through operation and management of the SEZs within “socialist market economy”. The SEZs were given more autonomy in economic activities than in political and social areas. Economic activity in the SEZ was predominantly market-oriented rather than controlled by the central government, but the scope of freedom was still limited compared with that of EPZs in developing countries. However as the experiment of capitalist economic management, the expected role of the SEZ was quite comprehensive. The impacts of the SEZ were indeed wide and far-reaching upon national economy.

The EPZs in East Asia were established as an integral tool of the Export -oriented Industrialization (EOI) policy package after the successful completion of the Import-substitution Industrialization (ISI) strategy, whereas China’s SEZs were assigned dual roles of promoting ISI and EOI at the same time since China was forced to achieve the targeted goal of industrialization. China’s inward-oriented protective industrialization policy during the Mao period focused on self-reliant heavy industry with the initiative led by the State Council, which does not fit in the ordinary ISI adopted by a developing market-economy. However, not a few lessons of the EPZs could be learned from by the SEZs. As Warr once said, the EPZs ran into troubles when a developing country reached a certain stage of industrial development with pushed up wage level (Warr, 1988). At this stage for the EPZ, development of high-value added, hi-tech industry was the only alternative. As the experiences of Asian EPZs suggests, unless China shifts to production of higher value-added products, China's economic development will be slowed down sooner or later as her comparative advantage of low wage diminishes since China’s major attractive advantage was its absolutely low labor cost coupled with various schemes of incentives.

Krugman pointed out that China’s economic growth which was typically based on increasing inputs will have to meet decreasing returns, i.e., deceleration in economic development as long as China is dependent on the inflow of foreign capital and technology (Krugman,1994). The SEZs will have no choice but to upgrade productivity by shifting to hi-tech, high-valued technology-intensive industries. It is hoped that the SEZs, the catalytic role of which should be highly appreciated in China's economic development, will play again a catalytic role in this process. One of the most serious constraints that should be urgently resolved in economic sphere may be infrastructure development not only in the SEZs but also throughout the rest of the country. The overall performance of China's SEZ will depend to a considerable degree upon the improvement of their physical and social infrastructure. China has indeed set a model to follow for other Asian socialist countries.

Notes:

1) Average annual rate of growth was 10.2% between 1981 and 1991, and 12.0% between 1991 and 1995 (China Statistical Yearbook 1996).

Conversion of China's currency ''RMB Yuan' into US dollar is complicated. China has changed her exchange rate several times. Until 1980 several exchange rates were used for trade transactions. After a single exchange rate was established in 1981, the official exchange rate was progressively devalued until 1984 when the rates were unified. In 1986 official exchange rate was pegged to the US dollar. But by 1993 the official exchange rate had depreciated 33% more than in 1986 and 70% more than in 1980 (Bell, Khor & Kochhar (1993), Pp.35-37). Sample average exchange rates of RMB Yuan against US dollars are as follows: in1981, 100 US dollars =170.50 RMB yuan, while in 1995, 100 US dollars = 835.10 RMB yuan (China Statistical Yearbook, 2001).

2) Fourteen open coastal cities include Dalian, Qinhuangdao, Tianjin, Yantai, Qingdao, Lianyungang, Nantong, Shanghai, Ningbo, Wenzhou, Fuzhou, Guangzhou, Zhanjiang and Beihai. Foreign capitals or firms such as EJVs (Equity joint ventures), CJVs (Cooperative joint ventures) and WFOEs(wholly foreign owned enterprises) in these cities paid only 80% of the current enterprise-income tax applied to local firms. If these ventures were located in the economic and Technical development districts within these cities, the tax rate was only 15% (Wei & Liu, (2001), P.15).

3) A gradual opening of the economy followed by setting up new economic zones after the SEZ which can be classified as one type of open economic zone. Beside SEZ and open coastal cities, there are delta areas and the development zones (opened since 1992) in this category (Bell, Khor & Kochhar, (1993), p.33).

4) According to Wang , the conceptual inception of the SEZ can be dated back to the 19th century treaty ports which played a significant role in the economy (Wang, (1993)).

5) Deng Xiaoping noted in June 1985 that the SEZs were "experiments" and as such they might fail. If so, China would have to learn from that experience.

6) Foreign firms in SEZs were provided with following attractions: (a) exemption from import/export duties and from after-tax profit remittance, (b) tax rates were 15%, (c) wages 75-80% lower than in Hong Kong, (d) foreign personnel pay no taxes (Walters, (1997), pp.52-53).

7) Asian EPZs was first established at Kaohshiung, Taiwan in 1966 based on Mr.Li's idea. Korean EPZs were established, according to Li , at the advice of Mr.Li from whom Korean officials studied Taiwan EPZ. First Korean EPZ was set up at Masan in 1970 (Li, 1990).

8) Chi-Kang Wang's congratulatory address at the 30th anniversary of the Installation of Kaoshiung EPZ (Taiwan Ministry of Economic Affairs, 1996).

9) The SEZs could approve a project of up to RMB 50 million in heavy industry and up to RMB 30 million in light industry (Wei & Liu, 2001). Local authorities in SEZs are allowed to attract foreign

investors through preferential policies (Bell, Khor & Kochhar, 1993).

10) Johansson (1994).

11) Asian Productivity Organization, (1983), P.8. According to Shoesmith, (1986), the central tactic of the broader EOI strategy stressed the basic elements as follows:

1) Emphasis on the rapid expansion of exports,
2) Free international trade,
3) A free, 'open door' environment for foreign companies in the less developed countries.

12) The total number of world export processing zones (or free export zones) increased from about 200 to over 300 in more than 75 countries during the1980 – 1990 decade. UNCTC (1991).

13) For example, during the 13 years until 1979, 116 factories closed down, 33 electronics, 26 plastics and leather, 22 leisure goods, 21 garments etc.. (Asian Productivity Organization, 1983). According to the ESCAP estimates made in the early 80s, there may be more than 50 EPZs located in almost every country in the region by the year 2000 (UN ESCAP, 1985).

14) Asian Productivity Organization, (1983).

15) Taiwan Ministry of Economic Affairs, (1996).

16) Taiwan Ministry of Economic Affairs, (1996). Korea Ministry of Industry and Trade (1998). The shares of EPZ exports in the total exports of Taiwan and Korea are quite substantial respectively. The export value of Taiwan's EPZs accounted for 6% (1986) and 5.6% (1995) of Taiwan total exports and the export value of Masan EPZ accounted for about 4% (1978) and 2% (1995) of Korea total exports. The Central Bank of China(1999), Taiwan Ministry of Economic Affairs (1996) and Korea Ministry of Industry and Trade (1998).

17) Out of this total value of inflow of FDI, it is estimated that about one fourth is so called 'round-ripping' FDI which actually originated from domestic sources but returning as foreign, simply to take advantage of the tax incentives provided to foreign-invested firms. Broadman & Sun (1997).

18) This figure for 1979 - 87 is only contract base. Pomfret, (1989).

19) In 1996 Guangdong's GDP recorded 6,519 million Yuan which ranked 1st in the country, followed by Jiangsu (6,004 million yuan) and Shandong (5,960). Fujian's GDP was 2,606 million Rmb. (China Statistical Yearbook 1997).

20) In view of sluggish export growth in the SEZs, plus the rise in the importation of consumer goods, which had led to a substantial deficits in China's balance of trade, in addition to the failure to develop export-oriented industrial bases, the government adopted in 1985 a number of measures to promote exports (Refer Wang, 1993).

21) Even on a national basis, Shenzen SEZ's share of total FDI in China was substantial. By the end of 1986, US$ 1.1 billion of cumulative FDI flowed into Shenzhen on a contract base (Pearson, 1991). In 1987, for example, Shenzhen SEZ alone accounted for 17% (Actual

FDI was US$393.8 million). Utilized FDI inflows to China in that year was US$ 2.31 billion (China Statistical Yearbook, 1996; Shenzhen SEZ Yearbook, 1996).

22) Actual foreign investment in Shenzhen had exceeded US$400 million annually since 1986, when it reached its peak at US$498 million by 1990, whereas pledged foreign investment is much higher, climbing to a reported US$1.02 billion in 1985 (Crane, 1991).

23) A majority of foreign investors were overseas Chinese and Hong Kong Chinese. Refer Tables-13, -14.

24) Toward the end of 1980s many Chinese manufacturers established their plants in the SEZs, partly because of higher foreign exchange retention quotas* 80 % of the value of goods manufactured in SEZs can be retained, versus about 30 % for goods manufactured elsewhere in China (UNCTC, 1991).

25) Wei & Liu, (2001). According to UN estimate, growth of industrial output during initial years (1979 - 83) in Shenzhen SEZ were relatively moderate as follows.

(unit: million RMB)

	1979	1980	1981	1982	1983
Gross industrial output:	60	84	243	362	720

Source: UNCTC (1991).

26) Regional priority on FDI shifted in 1985-86 from Shenzhen and Zhuhai to Pearl River Delta. The share of FDI inflow to Jiangsu area rose from 2 % (1984) to 10 % in 1988. Pomfret, (1989).

27) The export of electronics products from Shenzhen accounted for 67% of Guangdong province's export and about 15 % of the national exports of electronics products in 1987 (Wong, Cai & Chen, 1992).

28) Growth of income differentials between national China and Provinces with SEZs up to 1993.

Income per capita (RMB)	**China**	**Guangdong**	**Fujian**
1978	315	319	236
1988	1066	1518	1090
1993	2111	3939	-----

Source: China Statistical Yearbook, Guangdong Statistical Yearbook, Fujian Statistical Yearbook, various issues.

According to Kwan, labor costs in Southern China inside the SEZs are one-fifth those in Hong Kong while those outside the zone are mere on-tenth towards the late 1980s (Kwan, (1994), Pp.127-8).

29) Far Eastern Economic Review, July 6,1995.

30) The number of projects of utilization of foreign capital through signed contracts of agreements approved in Guangdong dropped from 8177 (1995) to 3744 (1997). Among three forms of FDI (i.e. EJV, CJV and wholly foreign-owned), the number of cooperative joint venture dropped most sharply from 2416 to 743 during this period. Guangdong Statistical Yearbook 1999.

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