

China's Changing Trade Patterns: *Implications for Asean-China Trade*

*Ellen Palanca**

China's external trade: trends and patterns

In 1979, China announced its open door policy to the world. Since then, China has been trading and investing with an increasing number of countries as it continuously adopted important features of the market economy. From an almost autarkic economy before, China has become very dependent on the world economy for markets as well as for inputs, products, and technology. The export dependence of the Chinese economy, as measured by the ratio of its total exports to its GDP, increased from 9 percent in 1980 to more than 20 percent in the 1990s. The increase in its import dependence ratio, i.e., import as a percentage of GDP, is just as dramatic—from 10 to 17 percent for the same period. The increase in trade volume has definitely stimulated its economic growth as its 1980 GDP quadrupled by 1995, five years earlier than the target year 2000.

In more specific terms, trade volume grew from US\$38 billion in 1980 to US\$290 billion in 1996, at an average annual rate of 13.5 percent. The rates for exports and imports were 14.2 and 12.9, respectively. As to the structure of exports, from 1980 to 1993, export of primary products declined from a share of 50 percent in total exports to just 18 percent while export of manufactured goods rose from 50 to 82 percent. During this period, labor-intensive exports grew at a remarkable rate as the manufacturing sector took advantage of China's low wage comparative advantage. This trend is expected to continue for several more decades especially in the inland areas even as the wage rates in the coastal areas are likely to rise.

The structural change is similar for imports. Manufactured imports increased much more than agricultural imports, with the ratio of agricultural to manufactured products declining from 35:65 to 14:86 for the period 1980-1993. Capital-intensive imports also rose very rapidly, occupying 72 percent of total imports and 82 percent of manufactured imports in 1993. Dominating such imports are machinery and technology as well as materi-

**Dr. Palanca is a Professor of Economics and the Director of the Chinese Studies Program at the Ateneo de Manila University.*

PIDS Policy Notes are observations/analyses written by PIDS researchers on certain policy issues. The treatise is holistic in approach and aims to provide useful inputs for decisionmaking.

This *Notes* is based on PASCN Discussion Paper No. 99-20 with the same title and by the same author under the auspices of the Philippine APEC Study Center Network (PASCN). The views expressed are those of the author and do not necessarily reflect those of PIDS or PASCN or any of the study's sponsors.

als and equipment necessary for the manufacturing of exports. Labor-intensive imports declined due to replacement by domestic production. With increasing per capita income, the demand for consumer goods imports is likewise on the rise and can be expected to increase more sharply.

Reforms and China's external trade

China's trade expansion and changing commodity structure can be attributed to several factors, most of which are related to its economic reforms. The market-based economic reforms oriented the trade system towards trade based on comparative advantage while the trend towards export-oriented industrialization was promoted by rural reform and foreign direct investments.

"Foreign direct investments in China have increased rapidly as a result of liberalization reforms and structural changes in the domestic economy."

Reform in the foreign trade system means adopting market liberalization policies. China's exports and imports, initially centrally managed, gradually conformed to the country's comparative advantage. Mandatory export plan and export subsidies were abolished in 1991. In 1994, the Chinese government further liberalized the foreign trade system by relaxing the import plan, thus freeing more foreign exchange for nonmandatory imports. The local governments and exporting enterprises were given the privilege of retaining a share of the foreign exchange earned and could purchase foreign exchange from the central bank. Tariff rates were reduced for a few products and nontariff barriers were lowered.

Rural reform was essentially in the form of rural industrialization. Boosted by foreign direct investment,

rural reform has promoted the growth of nonstate enterprises, most of which are engaged in the manufacturing of exports. In 1991, 74 percent of rural enterprises' output value focused on the industrial sector engaged in exports, thereby increasing the share of rural enterprise export to total exports from 5 percent in 1985 to 16 percent in 1991.

Foreign direct investments in China have increased rapidly as a result of liberalization reforms and structural changes in the domestic economy. China's potential market and abundant supply of low cost labor are important pull factors for investors. Devaluation of its currency in 1988 and 1994 also increased foreign investments, many of which are in the export manufacturing sector. The contribution to total exports of foreign-funded enterprises rose from 1.1 percent in 1985 to 41 percent in 1996.

China's import demand, on the other hand, also transformed due to the ensuing economic prosperity of the population and the change in industrial structure. The increase in the people's ability to purchase in recent years as well as the changing demographic structure have accelerated China's import potential for certain consumer goods. In particular, the demand for personal services, geriatric goods, household appliances as well as quality food items has increased and is expected to rise further.

Consistent with its modernization and reform program, China continues to place great emphasis in building up its infrastructure and technological capability. Hence, the import of advanced technologies to upgrade its technological level and develop its communication and

"Consistent with its modernization and reform program, China continues to place great emphasis in building up its infrastructure and technological capability. Hence, the import of advanced technologies to upgrade its technological level and develop its communication and information industries is given high priority."

Table 1. Average growth rate of exports: China, Asean-5 and the World, 1980-1996

	1980-1988	1988-1996	1980-1996
China	12.84	15.52	14.17
Asean	5.59	15.67	10.51
Philippines	2.47	14.25	8.20
Singapore	9.25	15.56	12.36
Indonesia	-1.52	12.53	5.27
Malaysia	6.28	17.80	11.89
Thailand	11.88	16.94	14.38
World	4.91	8.46	6.67

Source: International Monetary Fund. *Direction of trade statistics*.

information industries is given high priority. Direct investments that provide such technologies are very welcome and have been a strong mechanism for technological upgrading and thus a source of rapid productivity increase in China.

China's trade with Asean-5

In the last couple of decades up to the Asian financial crisis in 1997, the external trade of the Asean-5 countries also grew very rapidly. The average annual growth rate for the external trade volume of these countries for the period 1980-1996 was 11.01 percent, much higher than the world average of 6.64 percent. The growth of exports of these countries, which was already remarkably high in the 1980s,¹ even accelerated significantly in the 1990s (Table 1).

Meanwhile, the growth in national income for all the Asean-5 countries was faster in the 1990s than the 1980s (Table 2). The average annual growth of GDP for all the Asean-5 countries increased in the 1990s despite the decline in the world average due to the long-drawn recession in the advanced countries during the time. Average annual growth in total exports of all the five Asean countries increased from 5.6 percent for the period 1980-1988 to an average of 15.7 percent for the period covering 1988-1996. These statistics show that the rapid

¹The Philippines, along with Indonesia, was an exception due to the political and economic crises and instability it faced in the 1980s.

growth in the 1980s of China's economy, in particular its foreign trade, has not been at the expense of the growth of trade activities of the Asean countries. Instead, China's economic growth provided a synergistic effect on the region, promoting economic growth in the Asean-5 countries.

Merchandise trade between the Asean-5 and China was active and grew at double-digit rates in the last couple of decades. For all the Asean-5 countries, trade volume with China increased at rates faster than for the country's total trade volume. For the period 1980-1996, Asean-5's total export to China grew at an average annual rate of 17.8 percent while their total exports combined increased at 10.5 percent. The Asean countries saw the trade advantage they could gain from China's rapidly growing market as well as its industrial growth. They also considered China a good source of light manufactured goods and machines and equipment.

Table 2. Average annual growth rate of GDP: China, Asean-5 and the World, 1980-1996

	1980-1990	1990-1996
China	10.2	12.3
Philippines	1.0	2.9
Singapore	6.6	8.7
Indonesia	6.1	7.7
Malaysia	5.2	8.7
Thailand	7.6	8.3
World	3.1	2.2

Source: The World Bank. *World development report*, various issues

For the most part of the period, the value of China's export to the Asean countries exceeded the value of its import from the bloc. However, the trade imbalance has gradually declined as exports of the Asean countries to China have been increasing much faster than the countries' imports from China. Trade between China and the Asean as a bloc is now roughly balanced.

Despite the high growth in each of the Asean-5's bilateral trade with China, the share of this bilateral trade

Table 3. Asean-5 countries' trade volume with China, 1996

	<i>Trade volume with China (in \$US million)</i>	<i>Trade volume with China % of Asean trade volume with China</i>	<i>Trade volume with China as % of total trade volume</i>
Philippines	1343	7.31	2.46
Singapore	7147	38.88	2.79
Malaysia	3256	17.71	2.08
Thailand	3127	17.01	2.42
Indonesia	3509	19.09	3.78
Asean-5	18382	100.00	2.67

Source: International Monetary Fund. *Direction of trade statistics*.

to the country's total trade remains small. This is because the country's total trade volume also increased with the bilateral trade value. The share of trade with China has, however, been increasing since 1980 for all countries—from approximately one percent in the early 1980s to almost three percent in 1996.

While the bilateral trade with China has been increasing for all the Asean-5 countries, the volume and patterns of their bilateral trade, however, are not homogenous. The bilateral trade patterns depend on the level of economic development of the Asean country, its trade policies, resource endowment relative to China's and its diplomatic and economic ties with China.

Singapore, accounting for an approximately two-fifths share in both total exports to and imports from China of the Asean-5 countries since 1980, is the leading trader with China among the Asean-5 countries. Table 3 shows the trade volume with China of the Asean-5 countries for 1996. As a percentage of total Asean trade volume with China, the trade volumes of Malaysia, Thailand,

and Indonesia are between 17 to 19 percent each while the Philippines' share is the lowest at about 7 percent.

As a percent of total country's trade figures for 1996, trade with China ranked highest for Indonesia at 3.8 percent while for the rest of the Asean-5 countries, the percentage was somewhere between 2 and 3 percent.

Changes in China's comparative advantage

The change in the trade commodity structure of China reflects changes in its comparative advantage. With trade liberalization policies and institutional changes, the demand for economic efficiency has gradually moved its trade pattern towards conforming to its resource structure. Over the last couple of decades, China has experienced a sharp decline in its comparative advantage in agricultural and mineral-intensive products. On the other hand, its comparative advantage in labor-intensive manufacturing products has increased significantly. A slight increase in the comparative advantage in its capital-intensive products has also been observed.

China and the Asean-5 countries have been following a similar growth strategy that focuses on the promotion of labor-intensive manufactured exports. The result is that these countries have become more similar in their export profile as revealed in the commodity structure of bilateral trade between China and the Asean-5 countries. With focus on industrialization, these countries are moving away from agricultural production to manufacturing activities. For them, the development of comparative advantage has been in the direction of the production of machines and basic manufactures.

However, due to the decline in its comparative advantage in primary products and to its expanding in-

"China and the Asean-5 countries have been following a similar growth strategy that focuses on the promotion of labor-intensive manufactured exports. The result is that these countries have become more similar in their export profile as revealed in the commodity structure of bilateral trade between China and the Asean-5 countries."

dustrial activities, China now imports many raw and basic materials for industrialization and agricultural products for consumption from the Asean countries. Wood and rubber are among the top ten exports of Malaysia to China. These products, plus crude petroleum and pulp waste paper, are also among China's top imports from Indonesia. From Thailand, its top imports consist of primary products such as rubber, rice, and sugar. Fresh fruits, vegetable oil, and metal ore concentrates are the basic import products from the Philippines. The only important primary product China supplies to a few Asean-5 countries is tobacco. The pattern of trade between the Asean-5 countries and China shows that bilateral trade is increasingly being focused in basic manufactures and machines and equipment.

The remarkable growth in the bilateral trade between China and the Asean countries in the face of growing

"Many of the trade activities between China and the Asean-5 countries are based on intra-industrial exchanges with the patterns of their bilateral trades showing horizontal division of labor as well as trade niches."

similarity in their trade profiles contradicts the traditional trade theory wherein trade between countries is based on differences in factor endowment and industrial structure. In fact, the growth of bilateral trade has been most significant for Thailand and Indonesia whose export profiles are most similar to that of China. Manufactured products, which dominate trade between the Asean countries and China, consist of a broad spectrum of goods. Because product differentiation characterizes manufactured products, the opportunities for intra-industry exchanges of manufactured goods are particularly plenty. Specialization can also be based on the capital intensity of the products. Many of the trade activities between China and the Asean-5 countries are based on intra-industrial ex-

"With the adoption of more liberal policies as well as institutional changes and international exposure, China's economy is becoming more efficient. This rise in efficiency level can gradually erode the competitive advantages that the Asean countries now have over China."

changes with the patterns of their bilateral trades showing horizontal division of labor as well as trade niches.


Prospects and recommendations

With the adoption of more liberal policies as well as institutional changes and international exposure, China's economy is becoming more efficient. This rise in efficiency level can gradually erode the competitive advantages that the Asean countries now have over China. For the Philippines, it is therefore important to work on the efficiency of its industries, particularly the export industries, making them more globally competitive. This means that we should work towards the improvement of our labor productivity and efficiency of our government bureaucracy and infrastructure—power, telecommunication, and transportation. We should also be on guard that our currency is not overvalued.

Trade opportunities are expected to multiply following China's upcoming accession to the World Trade Organization (WTO). Demand for imports will increase when China opens up its entire economy in terms of both geographical areas and industries. Moreover, China's huge population, whose standard of living is growing very fast, is a market for many of our consumer products and services.

Due to China's rural industrialization focus, the import demand for food and primary inputs is also increasing. The Philippines can explore the gaps in agricultural and mineral resource supplies in China and fill up said insufficiencies by exporting agricultural and mineral products to China.

As earlier shown, intra-industry trade now dominates Asean–China trade. In this regard, the Philippines should coordinate with China in the conduct of joint research to identify trade opportunities and niches based on comparative advantage as well as on intra-industry division of labor. The Philippines should also, on its own, do intensive research to identify the areas of export, particularly the nontraditional ones, and market possibilities.

Greater liberalization will also mean that China's foreign investments, both inflow and outflow, are expected to increase. Special attention should thus be given to attract Chinese direct investments to the Philippines since these investments will not only provide capital but also technology that may be more appropriate than those from the advanced countries. At the same time, the Philippines should also explore the investment possibilities in China which will help facilitate and expand the growth of the country's export of inputs and services. 

References

- Palanca, E. 1999. China's changing trade patterns: implications for Asean–China trade. *PASCN Discussion Paper No. 99-20*. Makati City, Philippines: Philippine APEC Study Center Network.
- Song, L. 1996. Institutional change, trade composition, and export supply potential in China. In *Inflation and Growth in China*, edited by Guitian, Manuel and Robert Mundell. Washington, D.C.: International Monetary Fund.
- Tan, R. 1999. Foreign direct investment flows to and from China. *PASCN Discussion Paper No. 99-21*. Makati City, Philippines: Philippine APEC Study Center Network.

For further information, please contact

The Research Information Staff
Philippine Institute for Development Studies
NEDA sa Makati Building, 106 Amorsolo Street
Legaspi Village, Makati City
Telephone Nos: 8924059 and 8935705;
Fax Nos: 8939589 and 8161091
E-mail: jluguton@pidsnet.pids.gov.ph

The *Policy Notes* series is available online at
<http://www.pids.gov.ph>

Partial List of Discussion Papers for 2000*

- 2000-26 Key Indicators for Public Expenditure in Agriculture, Natural Resources and the Environment
Cristina C. David and Arlene B. Inocencio
- 2000-27 Agricultural Biotechnology: Opportunities and Challenges for the Philippines
William G. Padolina
- 2000-28 Philippine Productivity Performance in the 1990s: An Assessment
Myrna S. Austria
- 2000-29 Property Rights Reform in Philippine Agriculture: Framework for Analysis and Review of Recent Experience
Roehlano M. Briones
- 2000-30 Fiber Crops Program Area Research Planning and Prioritization
Corazon T. Aragon
- 2000-31 Coconut Program Area Research Planning and Prioritization
Corazon T. Aragon
- 2000-32 Oil Price Increase: Can Something be Done to Minimize its Effects? (A Computable General Equilibrium Analysis)
Caesar B. Cororaton
- 2000-33 Philippine Computable General Equilibrium Model (PCGEM)
Caesar B. Cororaton
- 2000-34 Transforming Land Bank into a Microfinance Development Institution
Mario B. Lamberte
- 2000-35 Philippine Tariff Reforms: A CGE Analysis
Caesar B. Cororaton
- 2000-36 An Analysis of Philippine Trade Reforms in 1995-2000 Using the 1994 APEX Model
Caesar B. Cororaton and Janet S. Cuenca
- 2000-37 Reforming the International Financial Architecture: The East Asian View
Mario B. Lamberte
- 2000-38 E-Commerce in Southeast Asia: A Review of Developments, Challenges and Issues
Aniceto C. Orbeta, Jr.
- 2000-39 Constraints, Opportunities and Options in Irrigation Development
Wilfredo P. David
- 2000-41 Managing Capital Flows to Developing Economies: Issues and Policies
Josef T. Yap
- 2000-42 Increasing Globalization and AFTA in 2003: What are the Prospects for the Philippine Automotive Industry?
Rafaelita A.M. Aldaba
- 2000-43 The President's Budget for 2001: Depleted Economic Choices
Rosario G. Manasan

*Discussion Papers released from July to November 2000. These can be downloaded from our website at <http://www.pids.gov.ph>