Partnerships crucial to sustaining China's boom

Foreign and domestic firms in China need to work in partnership if the country's economic boom is to continue in the face of the worldwide financial crisis, new research has shown.

A study by the Globalisation and Economic Policy Centre has revealed how joint ventures are more likely to succeed than enterprises that are entirely domestic or foreign-owned.

Academics examined data from more than 21,500 Chinese firms between 2000 and 2005 to investigate the influence of foreign ownership on productivity and profitability.

They found performance was boosted until the share of foreign ownership exceeded around 64%, at which point it began to decline again.

According to economists, the lesson is that foreign and domestic firms need each other if China is to sustain its extraordinary growth during the current downturn.

The findings will be presented by GEP's Dr Alessandria Guariglia at the Royal Economic Society's Annual Conference, being staged at the University of Surrey, on April 22.

Dr Guariglia, one of the study's authors, said: "Both parties in these joint ventures bring attributes essential to achieving high performance.

"Domestic firms contribute knowledge of the Chinese market and legal environment, as well as important political connections with local governments.

"Foreign partners, meanwhile, bring modern technologies, capital, managerial and international networking skills and better corporate governance.

"Domestic firms that operate alone miss out on this crucial input. Equally, foreign firms that operate alone miss out on the valuable contribution local producers can offer."

China, which last year celebrated three decades of economic reforms, continues to attract enormous levels of foreign direct investment (FDI).

Although it has not escaped the global financial meltdown, it has suffered far less than its competitors and still managed to achieve "significant and positive" growth in 2008.

It also possesses the best fiscal conditions in the world, with its debt accounting for only 20% of GDP – compared with around 60% in Europe and 80% in the US.

Professor Shujie Yao, co-ordinator of GEP's *China and the World Economy* programme, recently suggested the credit crunch has massively accelerated China's rise.

He believes its economy may already have overtaken Japan's – a decade ahead of most predictions – to become the second-largest in the world and could catch up with the US's within 20 years.

In addition, China's leaders have vowed to act "quickly and decisively" in the event of the country's economy needing more help.

Earlier this month Premier Wen Jiabao announced that government spending would grow by 24% this year in a bid to maintain an 8% growth target.

And Zhou Xiaochuan, governor of the Central Bank, claimed the economy was "stabilising and recovering" and that policies to date had achieved "significant results".

Dr Guariglia said partnerships between domestic and foreign firms would be vital to sustaining the boom in the midst of the challenges presented by the downturn.

Joint ventures represented almost half of the foreign investment in China in 2000, but the share is now down to less than a quarter.

Dr Guariglia said: "The high-profile failure of some domestic-foreign partnerships – the Danone-Wahaha deal, for example – seems to have given them a bad reputation.

"But our research suggests these failures are the exception to the rule and that foreign investors should be looking for partnerships with Chinese producers.

"We have shown that the effect of FDI on the performance of recipient firms could be an important channel through which FDI affects economic growth."

GEP's findings are contained in a research paper entitled *The More the Better? Foreign Ownership and Corporate Performance in China*.

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