The role of governments in GLOBALISATION

Special economic zones and government subsidies

Governments can also build infrastructure to attract foreign direct investment and increase trade flows. Special economic zones (SEZs), sometimes known as export processing zones, are a good example. These are often large areas of land set aside by government in locations well placed for international trade, such as seaports. Companies can import raw materials and export finished manufactures from these zones without incurring domestic taxes, so encouraging TNCs to set up branch plants (subsidiaries). This provides employment for locals, payment of payroll taxes, and technology transfer. Domestic firms can link in to supply the branch plant. In time, the strengthening of the domestic economy in and around the zone may enable these domestic firms to expand abroad themselves.

Key word

Special Economic Zones (SEZ) – Set up by national governments to offer financial or tax incentives to attract FDI, which differ from those incentives normally offered by a country. China now uses the term **'Export Processing Zones'**

Key word

Subsidies – Grants given by governments to increase the profitability of key industries.

Foreign Direct Investment (FDI) – Investment made by an overseas company or organisation into a company or organisation which is based in another country.

China

2 China

After decades of economic and political isolation, the Chinese government declared an **'open door'** policy to international business in 1978. It needed Western technology and investment to develop its economy – and from then on its government welcomed foreign businesses setting up in China.

Companies from Europe and the USA quickly saw the advantages of out-sourcing and relocating into one of southern China's four **'special economic zones'**, later known as **'Export Processing Zones'**. These zones offered tax incentives and huge pools of cheap labour. Since then, China's economy has grown rapidly and (in 2001) it became a member of the World Trade Organisation. By 2005, around 50% of Chinese exports came from foreign companies with connections in these zones.

China's rapid economic growth has altered the flow of FDI. China is still the world's largest recipient of FDI, but as growth has shifted into Asia, traditional flows of FDI have changed. Now, countries such as China and India control flows of FDI, together with governments and companies in Brazil, Russia and South Africa (collectively known as the BRICS countries). These five countries now invest heavily in the USA, EU, sub-Saharan Africa (see Figure 5) and South America. Therefore, China is now a major player in both the inflow and outflow of FDI. Investment flows from the BRICS to other countries increased twenty-fold (to $145 billion) between 2000 and 2012 – and now account for over 10% of the global total.

China and its 1978 Open Door Policy

Prior to 1978, China was a poor and politically isolated country, 'switched-off' from the global economy. Under the communist leadership of Chairman Mao Zedong, millions had died from famine. Most people lived in poverty in rural areas. This changed in 1978 when Deng Xiaoping began the radical 'Open Door' reforms which allowed China to embrace globalisation while remaining under one-party authoritarian rule.

The earliest reforms occurred in rural areas. Agricultural communes were dismantled and farmers were allowed to make a small profit for the first time. Strict controls on the number of children were also introduced, to curb population growth.

China's transformation into an urban, industrialised nation gained rapid momentum. Over the next 30 years, the largest migration in human history took place. 300 million people left rural areas in search of a better life in cities. Only a strict registration system called *hukou* prevented rural villages from emptying altogether. Soon there will be 200 Chinese cities with 1 million inhabitants or more. Many are new, rapidly built 'instant cities'. An urban mega-region of 120 million people has grown around the Pearl River Delta. It includes the conjoined cities of Shenzhen, Dongguan and Guangzhou.

Initially, urbanisation fuelled the growth of the low-wage factories that gave China the nickname 'workshop of the world'. The world's largest TNCs were quick to establish branch plants, or trade relationships with Chinese-owned factories, in newly-established coastal special economic zones (SEZs), see Figure 12.20. By the 1990s, 50 per cent of China's GDP was being generated in SEZs. Since then, the Chinese economy has matured quickly. By 2015, many workers were earning US$40 a day or more making quality goods, such as iPhones, for employers like Foxconn in the Shenzhen SEZ.

Today, China is the world's largest economy. With 400 million people said to have escaped poverty since the reforms began, China's story lends support to the 'hyper-global' view that global-scale free trade can sometimes cure poverty. However, China is still not entirely open to global flows, as Table 12.5 shows.

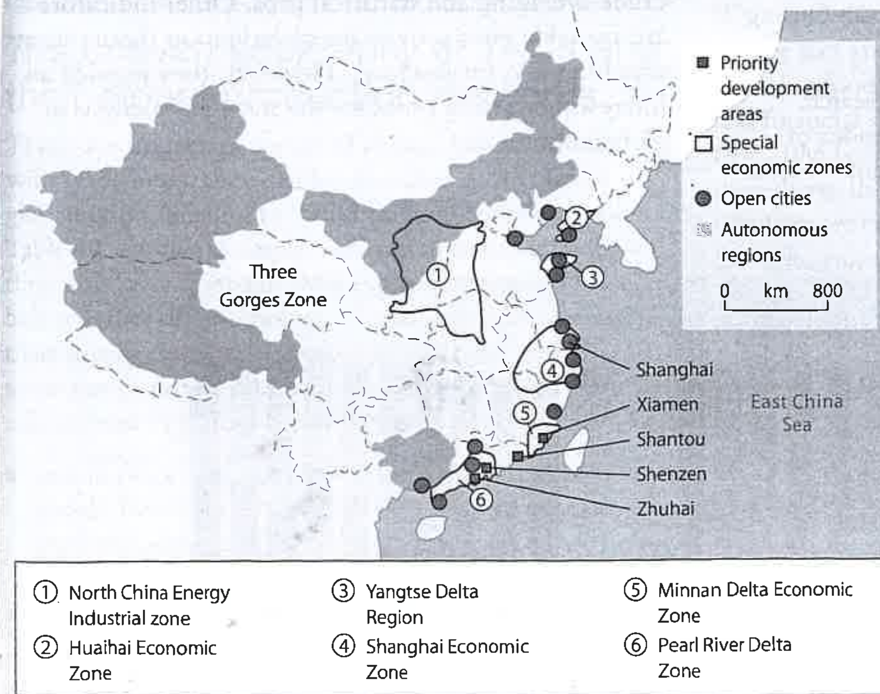

Figure 12.20 Economic development areas in China

Synoptic themes:

Players

The world's nations, trade blocs and international organisations have re-written their own rules, or created new ones, in order to foster globalisation

Table 12.5 China's varied attitudes towards globalisation and global flows

'Open door' approach to global flows	'Closed door' approach to global flows
FDI from China and its TNCs is predicted to total US$1.25 trillion between 2015 and 2025 (of this, over US$100 billion is destined for the UK).	Google and Facebook have little or no access to China's market (instead, Chinese companies like Youku provide social network services).
China agreed to export more 'rare earths' minerals to other countries, in line with a WTO ruling.	China's Government sets a strict quota of only 34 foreign films to be screened in cinemas each year.
Foreign TNCs are now allowed to invest in some sectors of China's domestic markets, including its rail freight and chemicals industries.	There are strict controls on foreign TNCs in some sectors. China's Government blocked Coca-Cola's acquisition of Huiyan Juice in 2008.

The UK

1 The UK

Just as important to the globalisation process is the willingness of individual national governments to promote international strategies for growth. In the 1980s, the Conservative government, led by Margaret Thatcher, was the first to embrace globalisation strategies fully. Some industries were left to close if their profitability depended on government **subsidies**, and the government also refused to artificially support industries facing competition from cheaper overseas products (e.g. the coal-mining industry, which was decimated by cheap foreign coal imports during the 1980s and 1990s).

Instead, the Conservative government developed two strategies for growth:

- It gave tax breaks – i.e. subsidies – to companies investing in areas such as London Docklands. Almost all companies establishing themselves in London's Canary Wharf development since the late 1990s have been given life-long tax breaks. This is a highly attractive benefit, which has encouraged a number of large overseas financial institutions to relocate to London.
- It also gave grants and subsidies to encourage foreign companies to locate new manufacturing plants in the UK. Nissan's Washington, Tyne and Wear, factory and Toyota's factory in Burnaston, Derbyshire, were each subsidised in order to attract investment from their Japanese parent companies – known as **Foreign Direct Investment** (FDI). By 2015, the UK was the fourth largest recipient of FDI.

CASE STUDY: Privatisation and market liberalisation in the UK

The Conservative government of Margaret Thatcher started a programme of deregulation and privatisation after the general election of 1979. This included British Telecom (1984), local bus services (the Transport Act 1985), British Gas (1986) and British Rail (1993). In 1997 a Labour government took the Bank of England out of direct government control and removed its power to control the financial activities of banks in the UK. The Legislative and Regulatory Reform Act 2006 was introduced to enable ministers to make Regulatory Reform Orders (RROs) to deal with older laws that they deemed to be out of date, obscure or irrelevant.