



U.S. DIRECT INVESTMENT IN CHINA

By K. C. Fung, Lawrence J. Lau, and Joseph S. Lee

With a foreword by George P. Shultz

FOR IMMEDIATE RELEASE: October 5, 2004

With an average annual growth rate of almost 10 percent since it adopted the “open door” policy, China has become a global economic powerhouse and has attracted tremendous foreign direct investment, not least from the United States. (Foreign direct investment, or FDI as it is known, is the investment of foreign assets into domestic structures, equipment, and organizations. It does not include foreign investment into the stock markets.) While critics frequently allege that U.S. direct investment in China costs American jobs, K. C. Fung, Lawrence J. Lau, and Joseph S. Lee argue in *U.S. Direct Investment in China* (AEI Press, September 29, 2004) that it is not so. On the contrary, empirical survey data presented in this new study does not support these claims.

The authors argue that U.S. direct investment in China is good for both countries. Using data from both official and unpublished sources, Fung, Lau, and Lee shed light on the trends, characteristics, motives, and policy implications of this investment. Among their findings: 90 percent of the output of U.S.-invested firms in China is sold in the Chinese domestic market and less than 10 percent is exported back to the U.S. home market—clearly indicating that fears of offshore outsourcing to China are exaggerated.

Fung, Lau, and Lee identify significant and growing mutual economic benefits from the investment ties between the United States and China:

- The two countries seldom compete in the same world markets.
- China cannot produce what the United States exports.
- The United States long ago generally stopped producing what China exports.
- China needs U.S. capital goods and technology, and the United States needs a reliable source of low-cost yet high-quality consumer goods.
- The two countries can provide markets for each other.
- U.S. firms invest in China fundamentally to implement a strategy for acquiring potential market shares in goods, services, and technology.
- U.S. direct investment in China is likely to increase trade between the two countries in both the short and the long run.
- U.S. multinational corporations operating in China are becoming increasingly profitable.

- American affiliates participate actively in the production of goods aimed at the rapidly growing domestic Chinese market.
- At the same time, significant amounts of Chinese exports shipped to the United States are produced by foreign-invested firms operating in China.

The authors conclude that, although U.S. direct investment in China is quantitatively rather small, it does have important implications. The investment significantly affects the amount of trade between the two countries and introduces subtle complications in the formulation of trade policies toward each other. Current U.S. direct investment in China affects the future ability of U.S. firms to sell in the rapidly growing Chinese domestic market. Finally, U.S. investment also affects the long-term growth prospects of the Chinese economy.

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