A VAR ANALYSIS ON RELATIONSHIP OF INTERNATIONAL TRADE, FDI AND ECONOMIC GROWTH IN CHINA

By

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ABSTRACT

The role of foreign direct investment (FDI) and exports continues to be debated and tested in the literature on international economics and development economies. This paper extends the previous empirical studies on the issue by providing some evidence from time-series data period over 1980-2010 of People's Republic of China. In this study, the dependent variables were economic growth. The model tested using unit root test, Granger causality, Vector Autoregressive (VAR) and Impulse Response Function (IRF) to analysis that dynamic relationship between economic growth, FDI, export and import. In terms of causality the result shows economic growth will provide a positive influence on the level of FDI, that is, economic growth (GDP) granger causes on Foreign Direct Investment (FDI), and there is a mutual influence between export and import because of intra-trade and imports of intermediate goods. The Vector Autoregressive (VAR) and Impulse Response Function (IRF) approach is to investigate the response of the system to economic shocks; the results showed that, the country's economic growth is influenced by its lagged values of GDP. Finally this paper draws some policy implications for the further studies to focus on the economic growth in China, to ensure that economic growth would not be drop.

ABSTRAK

Peranan pelaburan langsung asing (FDI) dan eksport terus dibahaskan dan dipersoalkan dalam konteks ekonomi antarabangsa dan pembangunan. Penyelidikan ini meliputi kajian empirikal terdahulu dengan menyediakan beberapa bukti data dari tempoh masa sepanjang tahun 1980-2010 di Republik Rakyat Cina. Dalam kajian ini, pembolehubah bersandar adalah pertumbuhan ekonomi. Model yang diuji menggunakan “unit root test”, “Granger casuality”, “Vector Autoregressive (VAR)” dan “Impulse Response Function (IRF)” untuk menganalisa hubungan dinamik antara pertumbuhan ekonomi, FDI, eksport dan import. Dari segi sebab-musabab hasilnya menunjukkan pertumbuhan ekonomi akan memberikan pengaruh positif terhadap FDI iaitu pertumbuhan ekonomi (GDP) Granger penyebab kepada FDI, dan terdapat pengaruh di antara eksport dan import disebabkan oleh perdagangan dan import barangan pengantara. Pendekatan VAR dan IRF adalah untuk mengkaji tindakbalas sistem terhadap kejutan ekonomi dan keputusan menunjukkan bahawa pertumbuhan ekonomi negara adalah dipengaruhi oleh nilai-nilai yang tertinggal daripada GDP. Akhir sekali, kertas ini menarik beberapa dasar polisi untuk kajian lanjut terhadap pertumbuhan ekonomi di Cina disamping memastikan pertumbuhan ekonomi tidak akan menurun.

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ABBREAVIATIONS

WTO	World Trade Organization
SEZs	Special Economic Zones
GDP	Gross Domestic Product
FDI	Foreign Direct Investment
MOC	Ministry Of Commerce
ELG	Export Led Growth
PPP	Purchasing Power Parity
IMF	International Monetary Fund
ADF	Augmented Dickey Fuller
ECM	Error Correction Model
VAR	Vector autoregressive
IRF	Impulse Response Function
FCI	Foreign Capital Inflow

CHAPTER ONE

INTRODUCTION

1.1 Background

Trade openness plays an importance role in economic growth in many countries. International trade in the nineteenth century and early twentieth century, generally encouraged the growth of the development countries of today, and it often been referred to as the “engine of growth”. The growth of domestic demand, rapid expansion of trade, particularly in the export sector, led to the creation of large-scale industry to provide a further stimulus.

Openness in trade refers to the degrees to which countries or economies permit or have trade with other countries or economies. The trading activities include export and import, foreign direct investment (FDI), borrowing and lending, and repatriation of funds abroad. Open economies generally have greater market opportunities, at the same time they also face greater competition from foreign businesses. In terms of financial development international trade enables a channel to obtain funds from other countries, and also invest its surplus funds in other countries.

International and domestic trade across Chinese provinces appears to be high and rising even as China has become more integrated with the global economy (Young, 2000; Poncet, 2003). China’s rapid GDP growth in recent decades has been impressive, averaging 10.3% per year from 1978 to 2010. Since 1978, the adoption of “reform and opening” policy initiated by Deng

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