The influence of international capital flow on China's economic growth rate

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Abstract. Recently, with continuous expansion of social globalization, the scale of international capital flow has been increasing. Moreover, international capital has increasingly become one of the important factors affecting the development of world economy and international market. Capital flow has far-reaching influenced on payments balance, international reserves, exchange rate stability, currency supply, etc. Combined with the trend of economic globalization, this paper mainly analyzes that under the background of the post epidemic era, central banks continue to print money in response to inflation, thus increasing the total amount of international capital flows and providing the possibility for market expansion. Based on this, this paper focuses on the impact of this change on China's economic growth rate. To predict the future development trend of China's financial market.

Key words: international capital; capital flow; central bank; economic growth rate.

1. The Impact of International Capital on China's Economic Growth

The root cause of the international flow of capital is that the return on investment of capital flows from exporting countries is higher than that left in the domestic market. As far as the world economy is concerned, the use of surplus capital can only be maximized when capital flows internationally. The flow of capital can also accelerate the trend of economic globalization and deepen the currency internationalization.

As far as exporting countries are concerned, capital flows can improve marginal benefits and promote import and export trade activities. They can also enable exporting countries to export domestic products to overseas markets, thereby finding an investment outlet for excess domestic capital. The export of capital reduces domestic investment, employment opportunities, and fiscal revenue, while also intensifying domestic market competition. For capital importing countries, capital flows can make up for the lack of capital that flows into countries. They can introduce foreign science and technology equipment, as well as advanced administrative management experience. They can also create more job opportunities, increase fiscal revenue, and improve people's living standards in capital importing countries. However, capital importing countries also have to bear the risks of debt crises and passive political status.

Against a backdrop of economic globalization, China has attracted a large amount of foreign investment due to its huge market, clear international division of labor, multiple investment forms, and openness policy. The introduction of a large amount of foreign capital will inevitably have an impact on China's economic development. The impact of international capital on China will also vary according to the forms and duration of capital flows.

It has shown that foreign direct investment has played an important role in economic development both in developed and developing countries.

Since the reform and opening up, China, as the largest market in Southeast Asia, has naturally attracted a large number of investors. On the one hand, the introduction of foreign capital has opened up a new pattern of reform for China and has increased China's economic growth rate. It has also helped China gain advanced management experiences from major foreign companies, laying the foundation for subsequent corporate development and China's market development. In addition, the introduction of foreign capital has made up for the lack of China's financial capacity by reserving a large amount of investment funds, which has provided the feasibility for China's early implementation of the southeast coastal city development policy. At the same time, foreign-owned enterprises have made up for China's technological backwardness, improved the asset quality of Chinese enterprises, shortened the update cycle of technology and products, and thus laid the foundation for the subsequent transformation of technological industries. The entry of foreign-invested enterprises into China has changed the monopolistic structure of the domestic market, accomplishing corporate restructuring and management upgrades.

Amid the COVID-19 pandemic, the forecast issued by the United Nations pointed out that the world will undergo five fundamental changes and adjustments in the future, the fifth of which is about capital flows. The gradual transfer of global capital to China reflects China's market position, which shows that China's development at present and even in the future will still need to rely on foreign capital. For more than 40 years of reform and opening up, the large-scale introduction of foreign capital has been driving the development of the entire Chinese society and economy. However, it is also a double-edged sword as the aim of capital is to maximize benefits. Once the investment environment of the Chinese market changes, the impact of the withdrawal of capital will also be huge.

In recent years, due to the continuous depreciation of the U.S. dollar and the appreciation of the renminbi, foreign investors have invested a large amount of foreign capital in China in order to earn the difference after exchange rate appreciation. As a large number of investors are attracted by the development prospects of China's real estate and stocks, speculative capital has quickly entered China's real estate and stock markets for speculation, which has increased the instability of the domestic market environment. Once the bubble economy collapses, foreign investors will quickly withdraw in order to preserve their capital, leaving the risk to the domestic market. The lack of domestic capital supply can easily lead to a financial crisis, increasing the risk of inflation.

2. The New Pattern of Capital Flow in China

As one of the most common forms of international capital flows, direct investment has an important impact on a country's economy, both externally and internally. It can change the industrial structure, promote economic policy adjustment, ease financial controls, facilitate import and export trade, speed up commodity circulation, improve the market environment, and so on.

2.1 The Impact of FDI on China's Industry

As mentioned above, capital inflows have been affecting China continuously, slowly and thoroughly. China's economic development policy follows a sustainable strategy. This strategy aims to effectively protect natural resources and the environment while also supporting economic development in order to promote the quality of human life. To achieve sustainable economic development as soon as possible, China has to optimize its industrial structure.

In social capital theory, Marx clearly stated an inevitable condition of socialist mass production. That is to say, how to make each industrial unit in the national economy adjust according to a certain proportion, which is also one of the universal laws of changes in industrial structure.

The new deployment of upgrading of China's industrial structure is to form an industrial pattern, with high-tech industries as the forerunner, basic industries and manufacturing as the support, and the comprehensive development of service industry. The primary tasks are to develop advanced manufacturing, increase the proportion of service industry, and strengthen the construction of industrial infrastructure.

In the initial stage of reform and opening up, foreign investment in China was mainly concentrated in labor-intensive manufacturing. However, this phenomenon changed in 2011. For the first time, the proportion of foreign investment in the service industry exceeded that in the manufacturing industry. As of 2018, the number of newly established foreign companies in three major industries had increased significantly in China. Among them, 639 companies are about agriculture, forestry, animal husbandry, and fishery. 6,152 companies are about manufacturing, and 53,696 are about service industry. These three kinds of companies represent a year-on-year increase of 10.4%, 23.4%, and 78.6%, respectively.

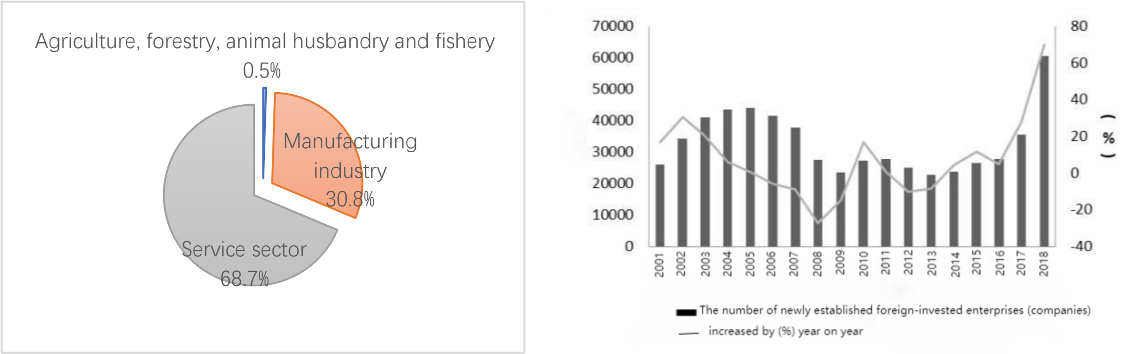

Fig. 1 Industry proportion and change of foreign investment in China

Currently, foreign direct investment in China has some notable features. First, as of 2015, the proportion of direct investment in the primary industry had remained at a low level. Although the investment had been stable for a long time without major fluctuations, the proportion of investment remained at about 1.8%. Second, the innovation and investment of the secondary industry would occupy an absolute dominant position. In the mid to late 1990s, FDI from major international multinational corporations and companies flooded the Chinese market wildly. Their investment was mainly in China's industrial market, especially the real estate market. Real estate investment accounted for one-third of the total investment in the secondary industry. The proportion of FDI in the secondary industry had been increasing year by year since 1995 and had stabilized at around 70% in 2005. Third, in the early 1990s, the absorption of FDI by the tertiary industry was in a downturn. However, since China formally joined the WTO, China's economy has gradually integrated with the world, with various policies being implemented. During this period, the investment of large multinational companies in China stimulated the growth of China's national economy. The prosperity of import and export trade enabled the tertiary industry to develop rapidly.

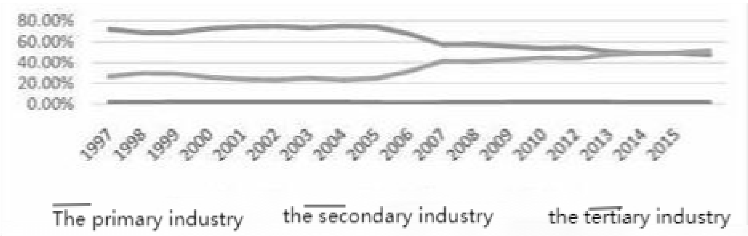

Fig. 2 1997-2015 Trend chart of foreign direct investment in three industries

On the whole, the impact of FDI on China's industry is manifold. In terms of scale, by absorbing FDI, China has realized the transition from coordinating domestic industries to developing higher-level industries in accordance with the country's economic laws. China has gradually moved towards the goal of continuous optimization and upgrading of the industrial structure. Through the absorption of FDI, China's productivity has grown as well. As a result, the output of various commodities has increased dozens of times, and the quality and variety of products have also improved. In terms of market structure, the subsidiaries of large multinational companies rely on the strong market appeal of their parent companies. Thus, they have more advantages in the competition with local small and medium-sized foreign companies in China. As their market competition has a more significant impact on China's market structure reforms, they have become an important role in the improvement of China's market structure.

2.2 OFDI's Impact on China's Industry

As the world's second-largest economy, China has abundant capital. With the deepening of economic globalization, the primary issue of China's current economic growth has been how to make the most effective use of China's surplus production factor. Encouraged by policies, more and more

Chinese companies choose to go abroad and explore foreign markets. According to data from the Ministry of Commerce of China, China's foreign trade continued its growth momentum in the first quarter of 2021. The total value of imports and exports reached 11.62 trillion yuan, a year-on-year increase of 28.5%, with exports increasing by 33.8% year-on-year. Foreign direct investment is the product of a country's economic development to a certain degree. It will grow with the development of a country's economy. The most direct impact of foreign direct investment is to stimulate economic growth and increase employment rate.

2.2.1 Research on 1OFDI's Impact on Economic Growth.

Wei Qiaoqin and Yang Dakai (2003) used Granger test and ADF test to demonstrate the relationship between economic growth and OFDI in the article "Research on the Relationship between the Economic Growth of the Home Country of Foreign Direct Investment". They believed that the relationship between China's economic growth and OFDI is not obvious at this stage, but this correlation will increase with the development of foreign direct investment. Hu Huzi (2011) analyzed the panel data of China's provinces from 2003 to 2008 in the article "Research on the Relationship between Economic Growth, Exports and Foreign Direct Investment". He found that the role of foreign direct investment in promoting China's economy is not evident. However, Luo Changyuan's (2006) research showed that foreign direct investment as "capital" itself has no significant direct effect on economic growth, but foreign direct investment can indirectly have a positive effect on economic growth by promoting total factor productivity. The research of Cao Qiuju (2004) also indicated that foreign direct investment can improve the allocation of resources on a global scale, thereby increasing the marginal benefit of capital and promoting domestic economic growth. Zhang Weiru (2012) and Feng Cai (2012) used provincial panel data and found that the effect of foreign direct investment on the economic growth of eastern China is greater than that of the central and western regions, and the short-term effect is much smaller than the long-term effect. This study highlights the positive effect of foreign direct investment on China's economic growth.

2.2.2 Research on the Impact of Foreign Direct Investment on Employment

Table 1. Research on the Impact of Foreign Direct Investment on Employment

Variable	ADF Value	1%Threshold	5% Threshold	10% Threshold	Probability	Result
FDI	-2.93867	-4. 58265	-3.32097	-2.80138	0.083	Stability
GDP	-3.70059	-4. 58265	-3.32097	-2.80138	0.0304	Stability
PW	-3.33741	-4. 20006	-3.17535	-2.72899	0.0388	Stability

After data analysis, results show that foreign direct investment has a positive effect on China's economic growth and employment. This effect will become more and more positively correlated as the total investment increases.

3. Conclusion

At present, the key issue of China's capital flow is the contradiction between the maximization of foreign business interests and the upgrading of China's industrial structure, as well as the economic risks resulting from China's low investment efficiency. The interests of foreign businessmen contradict the upgrading of China's industrial structure mainly because the pursuit of maximum profits by foreign businessmen runs counter to China's strategic transformation goal of making use of foreign capital.

In terms of effective measures to improve China's industrial structure, most of the previous studies have tended to analyze the correlation between total FDI and economic growth, as well as the impact of total FDI on the changes in the three major industrial structures. However, the realization of industrial optimization and upgrading is not determined by the total amount of FDI absorbed. To achieve a reasonable proportion of FDI in the three major industries, all departments should follow the laws of economic development to absorb FDI in a certain proportion. In response to this, the

Chinese government should formulate policies to guide the industrial orientation of absorbing FDI, cultivate the technology transfer and independent innovation capabilities of Chinese enterprises, improve supporting systems, and establish a sound market competition mechanism.

In response to the low efficiency of China's OFDI, the Chinese government should focus on improving the scale of foreign investment, which should be in line with domestic economic development. Otherwise, excessive investment will cause domestic capital vacancies, thereby increasing the dependence of domestic industries on foreign capital and making the domestic market lack complete autonomy. In addition, China should formulate different policies for different regions. The return on investment of OFDI in the southeast region is significantly higher than that in other regions. Thus, it is necessary to ease the economic policies of OFDI in the southeast region and strengthen OFDI restrictions on other regions. Also, it is necessary to improve the international competitiveness of private enterprises, encourage large-scale enterprises to make direct investment abroad.

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