

ASEAN and the rise of China's southwest

Blog post by Senior Associate Jens Presthus, 9 October 2019

Beijing announced this summer it would establish new free-trade zones in the country's southwest. This represents a significant development in China's strategy to boost growth and expand its influence in Southeast Asia through its Belt and Road Initiative. China's eastern provinces have until now been at the core of Beijing's "opening up" strategy. But now, amid the ongoing trade war with the US, China is rebalancing its domestic economy as well as international relationships. This has shifted Beijing's attention to the southwest.

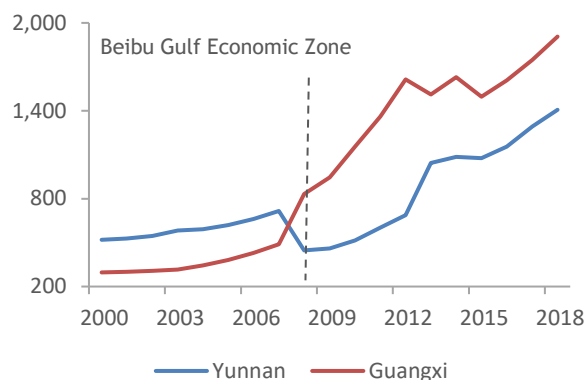


The long-time focus on development of the country's east has widened inequalities within China. GDP per capita in southwestern provinces is less than one third of that in Beijing and Shanghai, and the value of goods trade is only a fraction of that in most eastern provinces. While investment in the southwest has increased over the last few years, it is still on average less than half of that in industrial hubs like Jiangsu and Shandong in the east. Chinese policymakers hope that future growth in the periphery will reduce inequalities and ensure social order. Helping the peripheral provinces catch up is also part of Beijing's plan to sustain overall high economic growth - Premier Li Keqiang recently admitted that a 6%

growth target might be unrealistic. Opening up the southwest where wage growth has been much slower than around cities such as Shanghai and Guangzhou might convince multinationals to relocate within China rather than venture abroad to countries like Bangladesh or Vietnam.

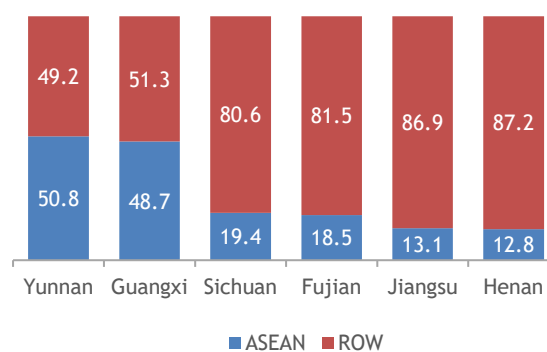
The establishment of FTZs in the southwestern provinces of Yunnan and Guangxi has to be seen as an extension of Beijing’s Belt and Road Initiative. While deepening its ties with Southeast Asia has been the plan for some time, the trade war with the US has likely fast-tracked the process. ASEAN countries are the two provinces’ largest trading partners and trade and transport links between ASEAN, Guangxi, Yunnan and other western provinces such as Hunan, Guizhou and Sichuan have dramatically improved. Policymakers hope they can replicate the success of the Beibu Gulf Economic Zone. After its establishment in 2008, trade volumes quadrupled in Guangxi and doubled in Yunnan.

Fig 1: Freight carried annually
Mn tons



Source: CEIC

Fig 2: H1 2019 trade by province with ASEAN
%



Source: Chinese Belt and Road Portal

Guangxi in particular, as the only province sharing a land and sea border with an ASEAN country, is considered a future hub linking China and Southeast Asian countries through the Belt and Road. The new zone in the capital Nanning - Hong Kong will take note - will function as a financial gateway for ASEAN and focus on the development of a modern services industry - including finance, smart logistics and digital economy. The FTZ in landlocked Yunnan - spread across the capital Kunming, as well as two towns close to the border - will link China’s eastern provinces - through the Yangtze River Economic Belt - with Myanmar, Laos and Vietnam. Also, here, the hope is that special terms for investors will boost growth and foster economic integration with China’s neighbours.

Beijing’s increased focus on its immediate neighbourhood is a clear reaction to the trade dispute with the US but is not without challenges. In China’s centrally planned economy, money will likely flow from Shanghai and Beijing and Chinese companies will set up shop in Nanning and Kunming. However, the extent to which foreign companies and investors will flock in will likely depend on the outlook for China’s trade relationships and domestic economy - which remains uncertain. A more economically influential China in ASEAN, especially one that is perceived as politically aggressive, could spark a backlash and also pit China against US, Japanese and European interests in the region. Beijing’s rebalancing in favour of the southwest will not only have an impact on its domestic economy, it also has

the potential to reshape geopolitical dynamics in Southeast Asia and China's future relationship with the US.