Corpus Christi and Coastal Bend
Economic Pulse
College of Business and EDA University Center
Texas A&M University-Corpus Christi
2011 | No. 2

China, the Economy and the Coastal Bend

By Jim Lee

As the world's second largest economy behind the U.S., China has become the focal point of global trade and investment flows. With a massive Chinese investment project underway locally, this article provides a snapshot on economic interactions between China and the Coastal Bend region.

I am privileged to have this opportunity to talk to you about China and, in particular, its impact on our local economy. I must first admit it is a daunting task to cover this pressing topic in only 20 minutes, given this country's 5,000 years of recorded history and civilization, 1.3 billion residents (one fifth of world population), diverse ethnicities and cultures (5 major ethnic groups), and most importantly, the dramatic changes in its social and economic landscape in recent times.

I appreciate that the hosts of this "Sync with China" event have given me a list of themes to focus on. The first question that I am asked to address is: "What is China's role in the global economy and how that relates to our local economy?" A related question is: "What do you see happening globally or nationally that will affect us locally?" So, my remarks today will involve mostly Mainland China—officially the People's Republic of China—as a modern economy rather than Chinese as a race or cultural identity. That said, one cannot fully understand its economic and political development without keeping abreast of its history, civilization and religious background.

Follow the Money…in Dollar or Yuan

As we learn in the introductory economics class, one way to explore our interactions with the rest of the world is through the channels of trade flows (the exchange of goods and services) and investment flows (flows of capital or funds). Long before we saw the arrival of Chinese in large numbers, we in South Texas had interacted indirectly with China through our purchases of consumer goods. Today most household items, from Motorola cell phones and Apple iPads to Nike shoes and Barbie dolls, bear the "Made in China" label. These are examples of China as the world's largest exporter of consumer products as well as the largest recipient of foreign investment, particularly from the U.S. and other developed countries.

Relatively low labor costs are widely cited as China's competitive advantage. This phenomenon is also often described under the term "outsourcing," which has been a hotly debated topic in the U.S. But according to a basic economic principle, "in the long run, imports are paid for by exports." For the layman, it is like saying "what (money) goes around … comes around."

China's trade liberalization, particularly since joining the World Trade Organization (WTO) in 2001, has contributed to its economy's annual growth rate of 10 percent on average in the past 10 years. Now China has passed Japan as the world's second largest economy, with a $5.88 trillion GDP in 2010. When the U.S. and Europe—its largest trading partners—fell into severe recession in 2009, its GDP growth shrank by half. The emergence of China as a so-called economic superpower would not be possible without us—the American consumers.

Today China is not only the world's largest supplier, but also the world's largest *potential* consumer. The sheer size of its domestic market can exert a lot of influence on the global economy. General Motors now sells more vehicles in China than in the U.S. Last year, European manufacturers of luxury autos such as BMW and Mercedes Benz earned more profits than ever despite a worldwide recession simply because of a growing demand in China.

"Chinese are Coming to town!"

Of course, we cannot talk about the influence of China on our local economy without talking about the massive Chinese investment locally. While a Sino-American venture of this nature and magnitude is new to the region and perhaps even for the nation as a whole, our exposure to the Chinese influence is not pure happenstance. In fact, Chinese citizens have been coming in large numbers for years.

Even for such a *regional* institution as Texas A&M University-Corpus Christi, the so-called globalization has already transformed our student body. The presence of international students is now pervasive on this campus. For Corpus Christi, these students represent our export of educational services to other countries. We currently have about 500 students coming from such countries as Mainland China, Taiwan, Thailand, Vietnam, Turkey and India. Five years ago, we had about 100 of them. Ten years ago, we had almost none. What do these international students have in common? The majority of them came from so-called emerging markets with rapid economic growth.

A Bird's Eye View on TPCO

The Chinese investment in Gregory-Portland is to build a steel pipe manufacturing plant under Tianjin Pipe Corporation (TPCO). It is a subsidiary of Tianjin Pipe Group, a state-owned enterprise in the northeastern part of China. The Tianjin Pipe Group is the world's largest steel pipe manufacture. Like Corpus Christi, Tianjin has a deep sea port along the Bohai Sea between northern China and Korea. The estimated $1 billion investment for building a steel mill is easily the largest Chinese direct investment in the U.S. to date. The facility is expected to be staffed by 300 employees during its first year of operation.

Of course, we must give credit to the city officials that have spent countless hours to lure the Chinese investors to Corpus Christi instead of some other 75 locales competing for the same project. But this investment can also been viewed as part of the current trend about China's investment overseas. The U.S. is now second to Australia as a destination of China's direct investment overseas. The Chinese government has accumulated US$2.5 trillion in currency reserves. After suffering massive losses from holdings of U.S. securities during the U.S. financial crisis in 2008, the Chinese government has sought to diversify its investment portfolios. In 2010, Chinese investments in the U.S. surged to $6 billion in 2010.

Win Some, Lose Some

As economic textbook theory implies, recent surges in China's imports and investments in other countries can be explained by its *own* exports and foreign investment inflows that have contributed to its overall economic growth. This is testimony of the wisdom that "trade benefits all nations." Our local community welcomes such investment because it will create more business and more jobs in the region. But oddly enough, the decision of the Chinese officials to produce steel pipes in the U.S. rather than in China is in fact an outcome of bad economic policy on the part of U.S. government. In response to complaints of U.S. steel makers and labor unions against China's selling steel pipes at below costs—a practice known as dumping—the U.S. International Trade Commission decided on February 7 to impose a tariff averaging 86 percent on future Chinese imports of steel pipes.

The rationale for this ruling is to protect U.S. jobs from foreign competition. But an import tax on steel pipes used mainly for oil drilling will also mean higher gas prices for U.S. consumers. According to the Institute for

International Economics, it costs a whopping $750,000 per year to save one job in the U.S. steel industry through existing trade restrictions. This new policy decision will be equally costly in comparison with the annual wages of about $50,000 for a typical job in the steel industry.

Déjà Vu?

Our "success story" is by no means unique from the perspective of the U.S. trade history. In the early 1980s, the U.S. government sought to protect its domestic automobile industry by imposing a so-called voluntary export restriction on Japanese autos. The Japanese auto industry responded by building assembly factories, or "transplants," in the U.S., such as the Toyota plant in San Antonio.

This is evidence of the impact of U.S. foreign policy on us locally. The decision to produce steel pipes in the U.S. instead of China is a preemptive act to sidestep the latest U.S. imposed tariff. While the region stands to reap the benefit of a foreign transplant, this new venture also reaffirms that trade protectionism time and again failed to achieve its intention to save jobs for U.S. steel union workers or to protect U.S. steel firms.

Are You Globalized?

The case of China highlights the importance for us to pay particular attention to developments beyond our region and our nation. The world has become increasingly globalized, meaning that more countries are open to interaction with the rest of the world. Globalization has changed the definition of a market. Prices have become increasingly sensitive to changes in supply and demand on a global scale. We can no longer fully understand what happens around us without a good grasp of what happens abroad, particularly among those so-called emerging markets in Asia and South America.

As for China, its rapid growth at 10 percent per year on average in the last decade has translated the country into a driving force for the commodity markets of oil and building materials like iron, steel and copper. According to the popular press, the hike in gas prices in the past two weeks was a response to the growing demand in China as large numbers of factory workers in cities returned home in rural areas for the week-long Chinese New Year holidays.

Aligning with China Inc.

China is now more as our business partner than our rival. It is our largest creditor, holding the largest share of U.S. Treasury securities by country. In this sense, our federal government's $800 billion Stimulus Package of 2010 has been funded largely by borrowing from the Chinese government.

Earlier this year, an article in *Economist* magazine reported how a surge of the cotton price benefitted cotton farmers in the Coastal Bend. This region is the largest cotton producer in the U.S. The Port of Corpus Christi has sought to be an official delivery point for cotton shipments bound for Asia once the expansion of the Panama Canal is completed in 2014. Rest assured that the journey of the cotton will not end in China or India. Much of it will return to the U.S. in the form of fashion apparel and brand-name linens sold in our local department stores.

All these would not be impossible without free trade and openness.

Myths and Reality

I have also been asked to give advice on how to offer a welcoming environment for future Chinese investors. It is helpful to first dispel this myth: China is now a rich country with huge savings so it is gearing up investments overseas. Here is the reality: Despite rapid growth, China remains a poor country with an average annual income of US $4,000 per person, which is only one-tenth of the U.S. level. The high Chinese saving rate of over 30 percent—as compared to less than 5 percent for the U.S.—stems from many socioeconomic factors, including the lack of retirement, social welfare and healthcare programs that most Americans take for granted. As a result of a lack of social and economic security, saving for the "rainy day" is more a necessity in China. The largely underdeveloped financial system also contributes to a huge gap between domestic saving and investment in China. China's investment overseas largely comes from government agencies, not private individuals or firms.

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(cont'd)

Soon after Chairman Mao Zedong's death in 1976, former Premier Deng Xiaoping said, "It doesn't matter whether it is a white cat or black cat. As long as it catches mice, it is a good cat." And the history of a new China as we know it today began to unfold. Yet more than 30 years of economic reform through privatization, China still ranks 135 out of 179 countries in terms of economic freedom, as reported by the Heritage Foundation. Its score still places this economy in the "mostly unfree" category. Many socioeconomic aspects of life in China remain under the control of the Communist Party that liberalized the country back in 1949. By comparison, Hong Kong (now part of China but under a separate legal system) has consistently ranked number one, and the U.S. has always been on the top 10 list.

Thank you for your attention. In this New Year of the Rabbit, I wish you all "*Gong Xi Fa Cai*," which literally means "wish you good fortune and prosperity." This greeting captures the essence of the Chinese culture.

*** This article is an excerpt of remarks given by the author at the "Sync with China" series on February 17, 2011.*