THE DIVERSIFICATION OF CHINA'S FOREIGN COMPANIES: FROM TRUMP'S TARIFFS TO THE COVID-19 PANDEMIC

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Executive Summary

1. The supply chain diversification triggered by Trump's trade policy measures has pushed foreign companies out of China. This was exacerbated further by the policy uncertainty under the COVID-19 pandemic. The Foreign Direct Investment (FDI) and trade data of China show some structural changes even though the performance remains strong.

2. A few leading foreign companies such as Dell and Foxconn (the manufacturer of Apple products) have begun to diversify production away from China since the beginning of the Trump administration. While political pressure could be a factor, economic consideration perhaps is the main driver during the COVID-19 pandemic.

3. Foxconn's move is indicative of the exodus from China. Taiwanese tech-hardware and electronic firms such as Foxconn are the major suppliers of Apple's products. The share of long-term assets of those Taiwanese firms had fallen from 43% (2017) to 31% (2021) in China.

4. The policy uncertainty during the outbreak of the COVID-19 variant, Omicron, in China has accelerated this trend. Google trend analysis suggests that the diversification from China was not very popular until then.

5. China's 2023 China Business Climate Survey by America Chamber reported that China as the top-one or top-three investment destination had dropped from 60% to 45%; another 10% of correspondents, compared with the previous survey, were considering relocating manufacturing or sourcing outside of China.

6. The European Chamber's Position Paper 2022/23, for which the analysis was made from January 2022 to August 2022, also highlighted the erosion of China's ranking as an investment destination. The uncertain policy environment to counter Omicron and geopolitics tension were the main reasons.

7. The two-month lockdown of Shanghai had also affected the operations of Japanese companies. A survey of Shanghai Japanese and Industry Club shows that 14% of the respondents plan to "reduce" or "postpone" future investments in China.

8. Even though total FDI flow to China has continued to increase since 2013, the structure of FDI inflow China has fundamentally changed. Hong Kong dominated the share of China's utilised FDI, while investment from other major partners has continuously dropped, especially during the COVID-19 pandemic.

9. One explanation is that foreign investors change their China's investment from direct to indirect via Hong Kong. Reallocation of investments seems to make more sense in light of the fact that foreign investments in Southeast Asia are booming.

10. China-US tensions led to a huge reduction of US trade with China in 2019 and COVID-19 had impacted other traders. However, China's trade performance remains strong in general. ASEAN became China's second largest trading partner in 2018 and its top partner since 2020. Meanwhile, ASEAN has also increased its exports to the United States, in a way helping China to avoid the Trump tariffs.