# Shifting away from China towards emerging countries?
## *A critical assessment of economic decoupling so far*

**10th Workshop: Turin Centre on Emerging Economies**

**Turin, 28-29 November2024**

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**Is China being abandoned by foreign, in particular American, business, as a consequence of the US-China trade war and other geopolitical tensions? Is decoupling taking place between the two major economies in the world, as put forward by a widespread opinion by many policymakers, analysts and media? What is the exact meaning of decoupling and how can we measure it?**

**Two main possible meanings of decoupling:**

**<u>Soft</u>: a process of weakening interdependence between the two nations**

**<u>Hard</u>: a disconnection of the two economies**

**Scope: to measure decoupling in trade and foreign direct investments (FDI) through various pieces of evidence :**

- **official data of international trade and FDI**
- **the behaviour and intentions of the firms involved as they appear from surveys, data bases from various institutions, case studies and anecdotical evidence.**

**Period under consideration: 2017-2023, with glimpses on the first 8 months of 2024.**

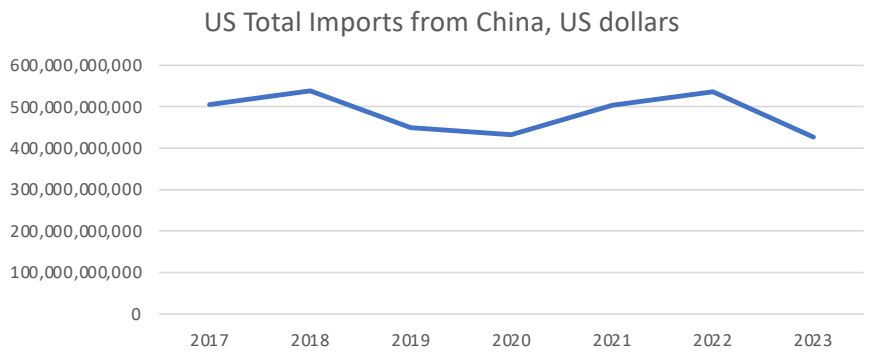
**Since we are looking for some measure of decoupling, i.e. declining trade dependency, a simple indicator - market share trends - looks more promising than just trade flows trends.**

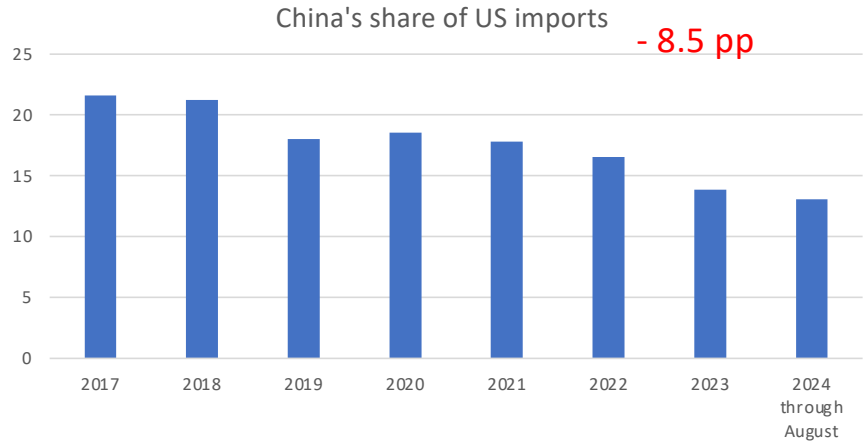
**Trade dependency may be gauged both on the import and on the export side.**

- **<u>Import dependency</u>: the value of imports from a partner as a percentage share of imports from the world. The difference between the share at the beginning of the period (2017) and at the end (2023, and when possible, Aug. 2024) will give us the losses or the gains in percentage points (pp). Market share losses means that the partner has become less important, so that some decoupling has taken place. The other way round for market share gains.**
- **<u>Export reliance</u>: the value of exports towards a partner as a percentage share of exports to the world. Losses and gains are calculated in the same way as above and the meaning concerning the decoupling process is similar.**

**Let's start from US total imports from China that are far more conspicuous than total exports to China and at the core of US policymakers' concern.**

# US import dependency on China



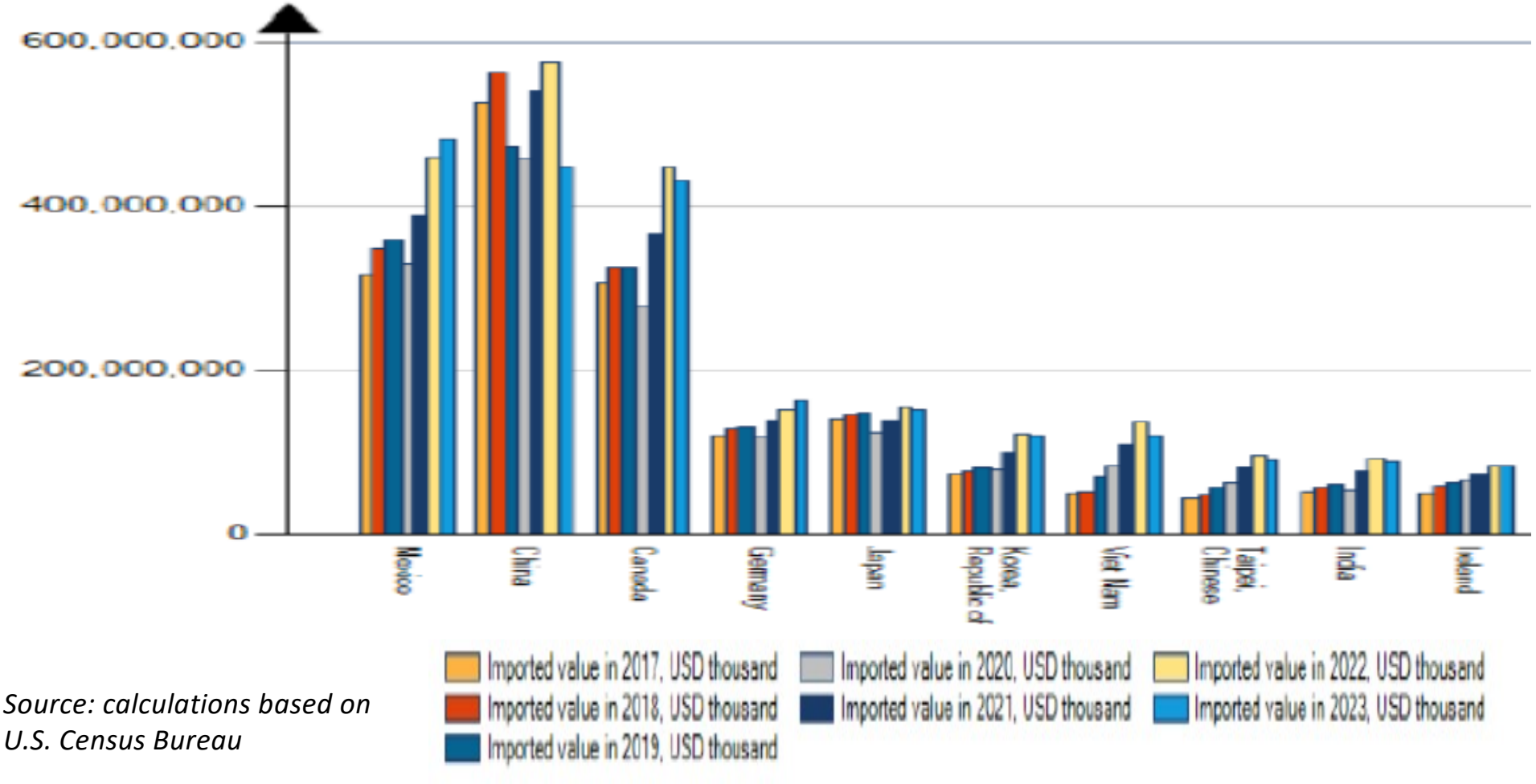

*Source: calculations based on US Census Bureau*

- **In 2023 US imports from China (428 USD billion) were well below the 2017 level, but that was due only to the last year of the period: up to 2022 the values of imports were rising.**

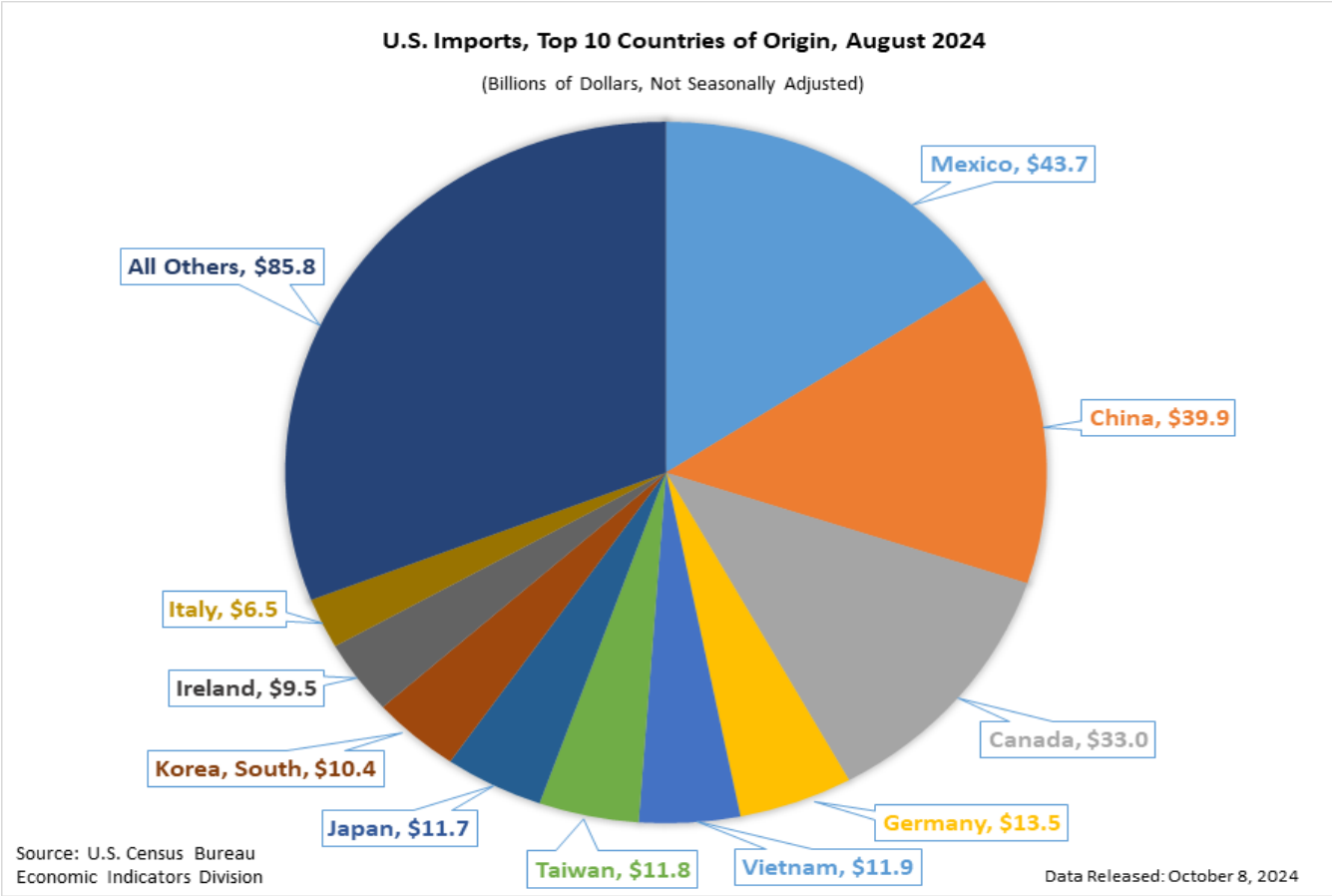
- **Since US imports from the world were increasing at a faster pace than its imports from China, the latter's share in US imports (import dependency on China) has fallen by 8.5 percentage points between 2017 and 2024 (August). On the last date China was the source of only 13.1 percent of total US goods imports, down from 21.6 percent before the onset of the trade war.**

- **Until 2022 China was the first source of US imports in the world, but only the second as from 2023.**

*Top 10 supplying markets for products imported by the US, 2017-2023, in USD thousand*

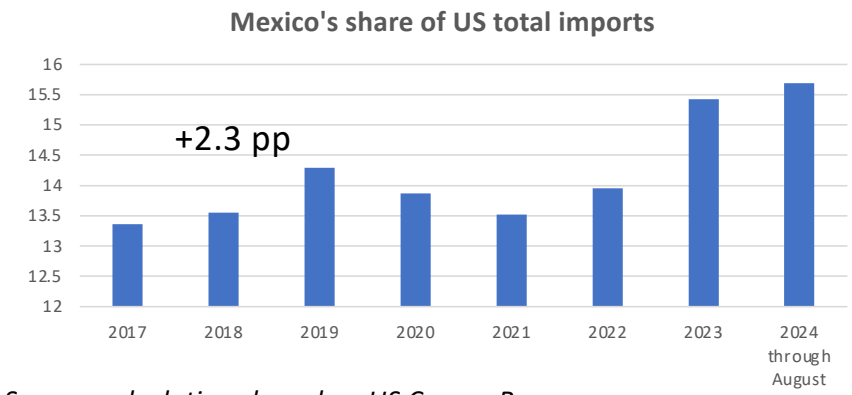


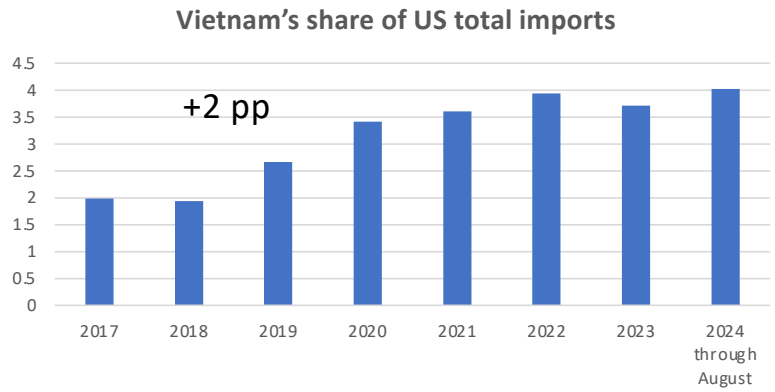

*Source: calculations based on U.S. Census Bureau*




**US imports are far more concentrated than China's. US' largest source of imported goods, Mexico, accounts for 15% of imports. Canada and China account for about 14% each. Thus, 43% of US imports come from just three countries.**

# US supply-switching




*Source: calculations based on US Census Bureau*

- **Looking at US imports, Mexico and Vietnam present a mirror image of China. Together they gained half of the market share lost by China. In 2023 Mexico has become the most important US supplying market, further increasing its position in 2024 (Aug): from 13.4% in 2017 to 15.7% in 2024. Vietnam passed from 2% in 2017 to 4% in 2024, when it became the 5$^{th}$ supplying market.**

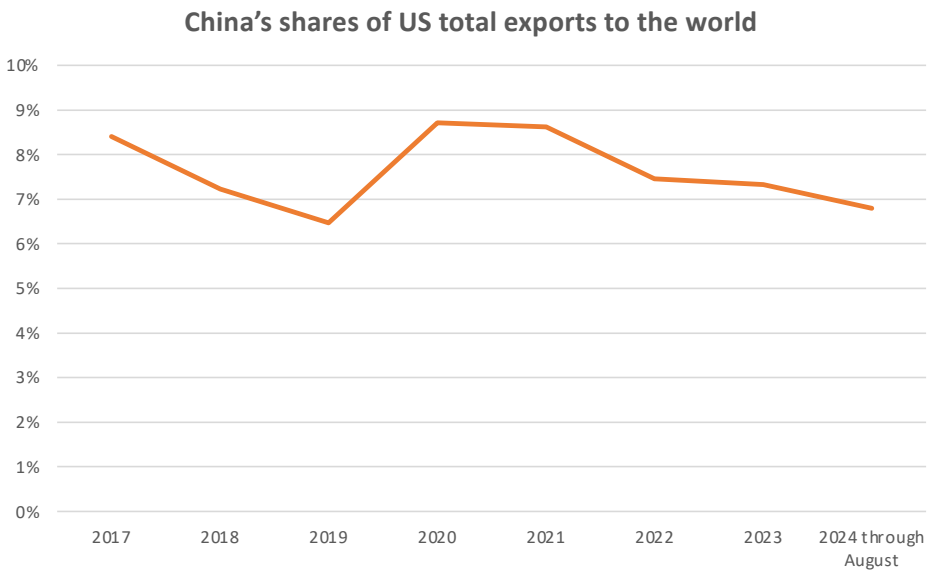
- **The downsizing of China as a source of supply has also resulted in small gains by Laos, India, Thailand, Cambodia, Malaysia and Indonesia (also by Brazil and South Africa – apart from various advanced countries, above all the European Union, that are beyond the topic of the present study).**

- **If one looks at the opposite trends of US imports from China and of US imports from other "winning" sources, one could note an inverse relation that regression results would confirm rather clearly. This is the supply-switching side of the picture on the part of the US.**

## China's export re-direction to destinations other than the US

- **Chinese exports to the world by value increased up to 2022, with a minor setback in 2023. As a share of world exports they increased from 12% in 2017 to 13% in 2023.**
- **Some reshuffle took place in the relative importance of its partners. The US maintained their position as most important outlet, but reduced their share from 19% to 14.8%. Other important losses were suffered by Hong Kong and Japan, second and third outlets respectively.**
- **Worth of note: here too, some emerging countries gained small amounts of market share each: Vietnam (now 5$^{th}$ outlet of Chinese exports), India (6$^{th}$), Malaysia (10$^{th}$), Mexico, Thailand, Indonesia, Brazil, among others. Altogether those seven countries gained 4.3 pp. against a loss of the US amounting to 4.2 pp. (***Source: calculations based on General Customs Administration of China***).**

# A slight decline of US export reliance on China

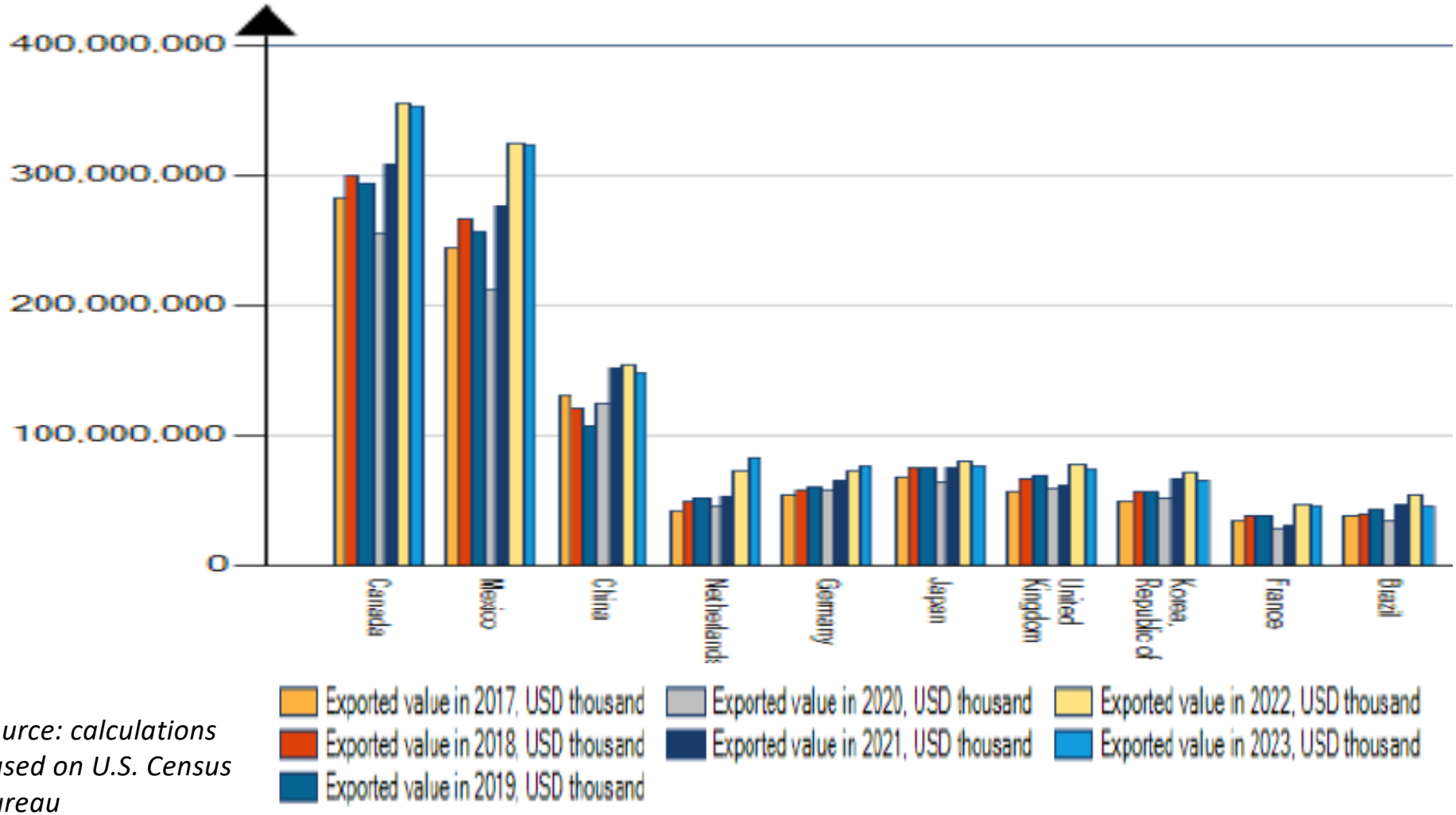




*Source: calculations based on U.S. Census Bureau*

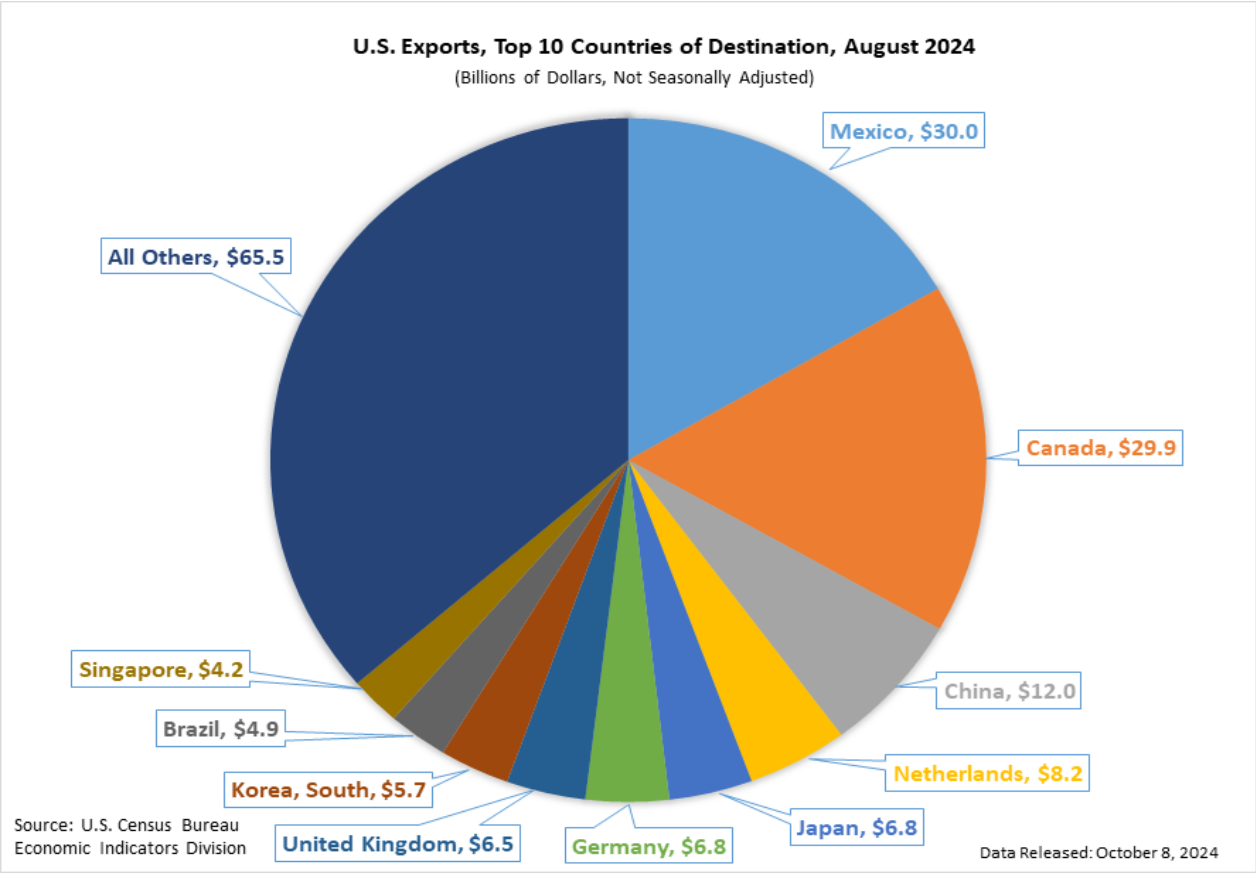
**In 2017-2023 the evolution of the value of US exports to China (149 USD billion in 2023) showed an increasing trend that was however less steep than the rise of US exports to the rest of the world.**

**As a consequence China's share of US exports (US export reliance on China) showed a slight decreasing trend with only a pick up in 2020: from 8% in 2017 to 7% in 2024.**

***Top 10 outlets of US total exports, 2017-2023***




*Source: calculations based on U.S. Census Bureau*




- **On the US export side, the shifts of importance are less sizable than on the import side.**
- **By 2024 Mexico surpassed Canada as the main US outlet, with China in third position.**
- **Noteworthy is the presence of some emerging countries both among the first ten (Mexico and Brazil) and among the second ten most important outlets (India). But on the whole they seem to be less relevant for US exports than on the import side.**

***But how does this reduction in trade ties between the two superpowers look from China's perspective?***

## China's import dependency

| *China's total imports from:* | *% share of total Chinese imports 2017* | *% share of total Chinese imports 2023* | *Share losses or gains, in pp. 2017-2023* |
|---|---|---|---|
| United States | 8.4 | 6.5 | -1.9 |
| South Korea | 9.6 | 6.3 | -3.3 |
| Taiwan | 8.4 | 7.8 | -0.6 |
| Malaysia | 2.9 | 4 | 1.1 |
| Vietnam | 2.7 | 3.6 | 0.9 |
| Indonesia | 1.5 | 2.9 | 1.4 |
| Europe | 17.7 | 19.4 | 1.7 |

***Source: calculations based on General Customs Administration of China statistics.***

# The US have become also less important as an outlet for Chinese exports

| *China's exports to:* | *2017* | *2023* | *share of Chinese exports: gains or losses, in pp.* |
|---|---|---|---|
| United States of America | 19.0% | 14.8% | -4.2 |
| Hong Kong, China | 12.4% | 8.2% | -4.2 |
| Japan | 6.0% | 4.7% | -1.3 |
| Korea, Republic of | 4.5% | 4.4% | -0.1 |
| Viet Nam | 3.2% | 4.1% | 0.9 |
| India | 3.0% | 3.5% | 0.5 |
| Russian Federation | 1.9% | 3.3% | 1.4 |
| Germany | 3.1% | 3.0% | -0.1 |
| Netherlands | 3.0% | 3.0% | 0 |
| Malaysia | 1.8% | 2.6% | 0.8 |
| Mexico | 1.6% | 2.4% | 0.8 |
| United Kingdom | 2.5% | 2.3% | -0.2 |
| Singapore | 2.0% | 2.3% | 0.3 |
| Thailand | 1.7% | 2.2% | 0.5 |
| Australia | 1.8% | 2.2% | 0.4 |
| Taipei, Chinese | 1.9% | 2.0% | 0.1 |
| Indonesia | 1.5% | 1.9% | 0.4 |
| Brazil | 1.3% | 1.7% | 0.4 |
| United Arab Emirates | 1.3% | 1.6% | 0.3 |
| Philippines | 1.4% | 1.6% | 0.2 |
| Canada | 1.4% | 1.3% | -0.1 |

***Source: calculations based on General Customs Administration of China statistics***

## Summing up on global bilateral trade

- **So, as far as total trade is concerned, a clear dropping of import dependency and export reliance on either side seems to be confirmed by official data.**

- **However trends in global trade may mask different trajectories of the product groups entering that trade.**

- **Did the weakening of Chinese importance in US trade and vice versa applied uniformly to all products?**

## The devil is in the details: some examples of US manufacture imports from China by commodity groups

- **If we look at commodity groups at a very high level of aggregation, we find a reflection of the trends highlighted above: US import dependency on China has fallen in most of the 97 HS sectors at the two-digit level.**
- **But if we dig at a more disaggregated level, from the 4digit to the 10digit level, the picture appears to be more complex. China lost market shares in all products hit by 25% US tariffs, and in many other products, either hit with lower tariffs or not hit with tariffs at all.**
  - **Take the case of semiconductor devices (HS 8541): in 2017 China, together with Malaysia, was the main source of supply for US imports. By 2023 China has regressed to the 9th source of supply and lost 17.3pp in market share, while five emerging countries have become the main sources of supply: Vietnam, Thailand, Malaysia, Cambodia and India, in the order. These five countries together account for 67% of US imports of semiconductor devices. Excluding Malaysia, they have gained, taken together, 39pp in market share, more than doubling the amount lost by China.**
  - **At the level of individual products the picture is similar: for example, as for US imports of routers, China's market share showed an increase up to 2020 and a sharp decline thereafter, ending up with a loss of 11.7pp, exactly equal to the market share gained by Mexico, while Vietnam, which in 2020 was practically not an exporter to the US, gained 6.6pp.**
  - **Finally another case of remarkable reduction in import dependency from China is represented by furniture: China lost 23.7pp, more than half of them accrued to Vietnam and Mexico. The two latter countries, together with Malaysia, Indonesia, India and Thailand gained roughly three quarters of China's loss.**

# Import dependency, up and down

- **However China's market share losses were not so great for all the products hit by the 25% US tariffs: such is the case for instance of parts of motor vehicles, where she lost just 3.7pp, more than compensated by Mexico's gain of 5.6pp.**

- **The decline in US import dependency occurred also for many products hit by lower tariffs or not targeted at all.**
  - **Such is the case for instance of footwear, where imports from China rose up to 2022, sharply declining in the last year (total loss = 18.1pp, as against a gain of 21.4 by Mexico and Vietnam),**
  - **or of TV receivers incl. video monitors, where China's loss was equal to 15.2pp, as against a gain of 14.9pp by Mexico and Vietnam taken together.**

- **Even in the case when Chinese exports to the US have increased (i.e. toys), in most cases they did not rise as much as the world exports to the US, so that a decline in China's market share has ensued (a loss of 10.5pp, as against a gain of 7.2pp obtained by Vietnam and Mexico, followed by Indonesia, Malaysia and Thailand (all together another 1.7pp)**

- **Finally, let's remember that the global trends seen at the beginning mask the fact that many products have on the contrary seen a Chinese market share gain. Apart from the case of toys until 2022, such is the case for instance in US imports of lithium-ion batteries, where China passed from a share of 42.7% to a whopping 71.8%. Further market share increases were obtained by China in many other products hit with lower US tariffs or no tariff at all.**

## Summing up on US imports by commodity groups

- **US import dependency on China has not decreased in the same way for the various products involved. In many cases there was even an increase of dependency, especially where protectionist measures were not applied. The latter, however, was obviously not able to offset the weight of the above shown negative trends.**

- **The decline in bilateral trade between the US and China has been offset by trade with other countries. The major role in market share gains by Mexico and Vietnam already highlighted for total US imports appears evident also at the level of individual product groups, their relative role and place for the various industrial sectors being dictated by their export specialization, factor intensities and trade agreements.**

- **Other emerging countries have gained smaller market shares at least in a few products: mostly India, Malaysia, Indonesia, Thailand and Cambodia.**

## US export reliance and China's import dependency by commodity groups

**On the US export side as well not all product groups behaved in the same way. We consider here only four of the major manufacturing product groups at the 2digit level.**

**Three out of the four major export product groups showed a loss in the share of China in US exports to the world (US export reliance) more important than the average in total exports (-1pp.). Such is the case of Aircraft and Spacecraft (-7pp.), Vehicles (-4.6pp) and Electric Machinery (-1.3pp.). In Nuclear Reactors, Boilers, Machinery Etc.; Parts, China lost only 0.5pp.**

**As for China's import dependency on the US, the pattern is that of a general reduction, more marked for Vehicles (-4.7pp) and Aircraft & Spacecraft (-2.3), milder in the case of Nuclear Reactors, Boilers, Machinery Etc. (-0.7pp) or of Electric Machinery Etc; Sound Equip; Tv Equip (-0.6).**

**China's import dependency however might have declined even further at a more disaggregated level: such is the case for instance of its imports of machinery for the manufacture of semiconductor devices, which showed a sharper decline of market shares (-5.3pp). At the end of 2023, only 0.7% of China's total imports of such machinery came from the US (***calculations based on U.S. Census Bureau and on General Customs Administration of China statistics).* **Here the US export control policy enacted as from 2022 appears to have been effective.**

## Summing up on trade

**We have tried to quantify the supply-switching and export re-orientation taking place on both sides of the Pacific.**

- **As a whole, import dependency and export reliance seem to have declined for both contenders.**

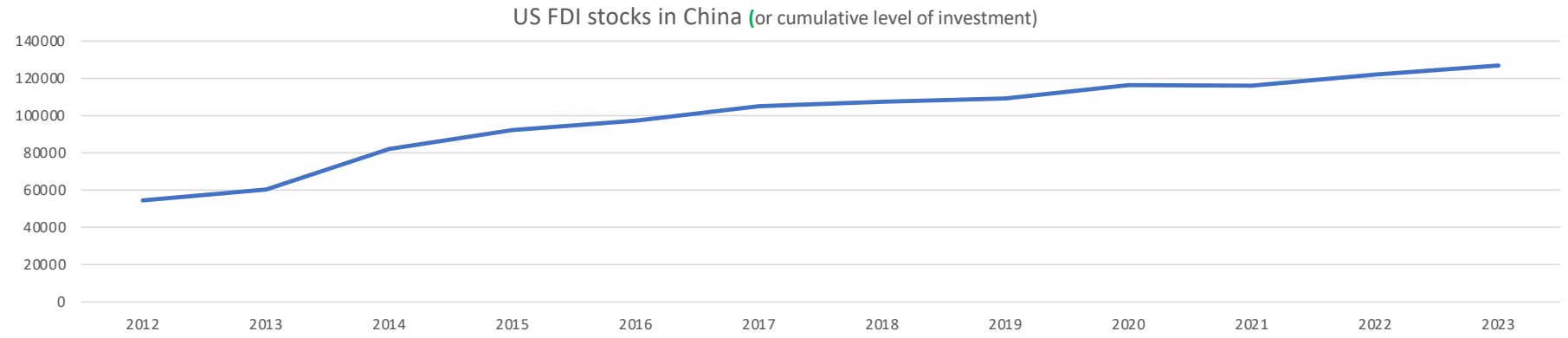
- **However, such decoupling is not taking place uniformly, but varies according to the different products and does not materialize for many of them, which even show an increase of dependency.**

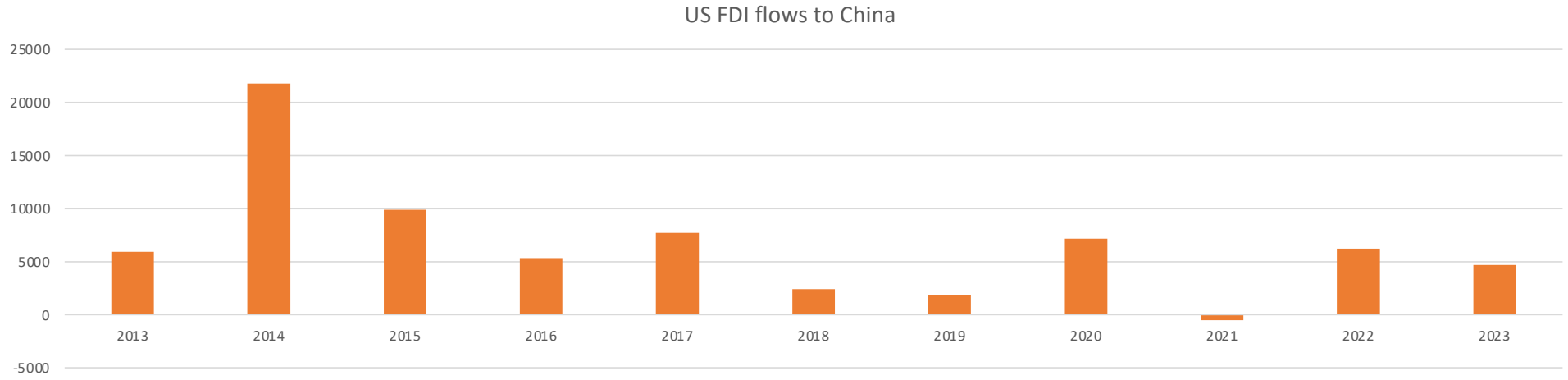
- **China and the US seem to have re-directed a substantial amount of imports and exports away from each other in favour of different destinations.**

**Does that necessarily involve a progressive separation of the two economies, that is to say, are we witnessing a decoupling in the hard sense or are we just in front of a milder form of disentanglement, a soft decoupling?**

**In order to answer to this question, we must first analyse briefly the other major strand of international economic relations: foreign direct investment. Do we witness here too the same decline in reciprocal importance between the US and China?**

# US outward FDI flows to China showed a declining trend, although they remained positive

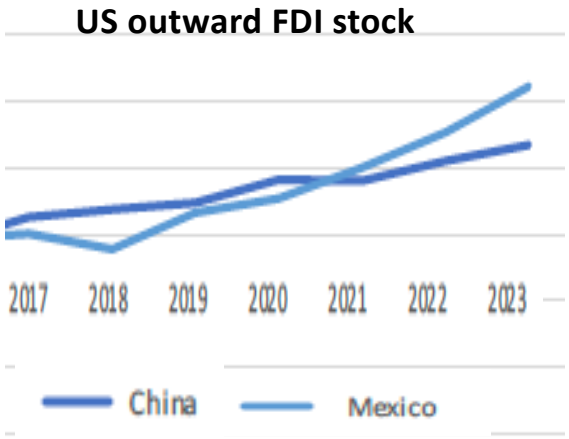



*Source: calculations on the basis of Bureau of Economic Analysis, U.S. Department of Commerce*

## The US outward FDI stock increased much more in some emerging countries than in China

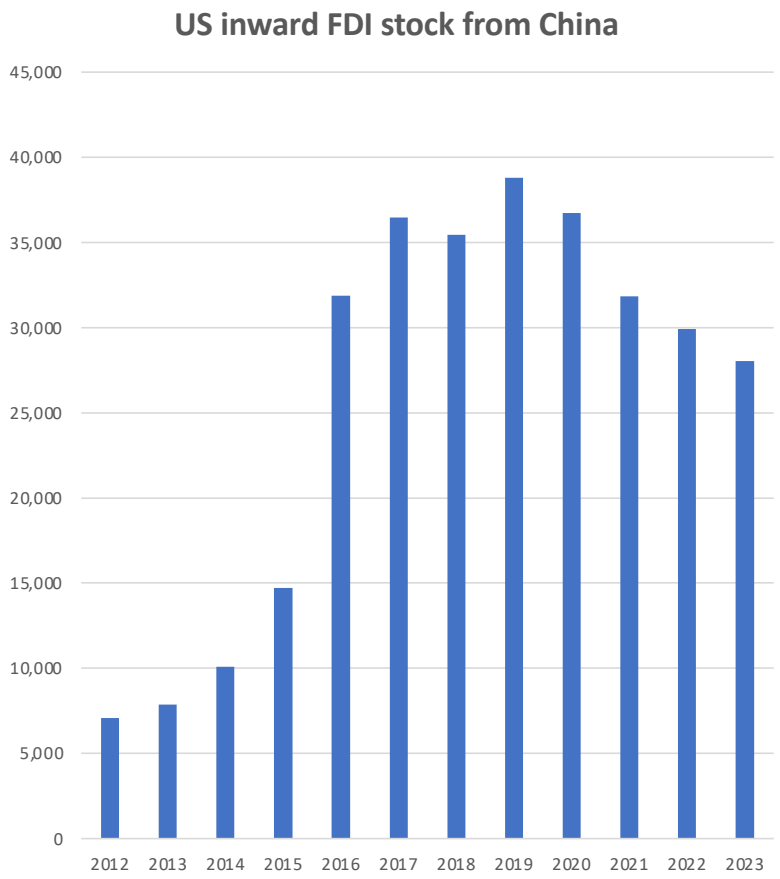
| | Increase of US outward FDI stock 2017-2023, in % | | |
|---|---|---|---|
| | | | |
| China | 20.7 | | |
| Mexico | 44.3 | | |
| Vietnam | 54 | | |

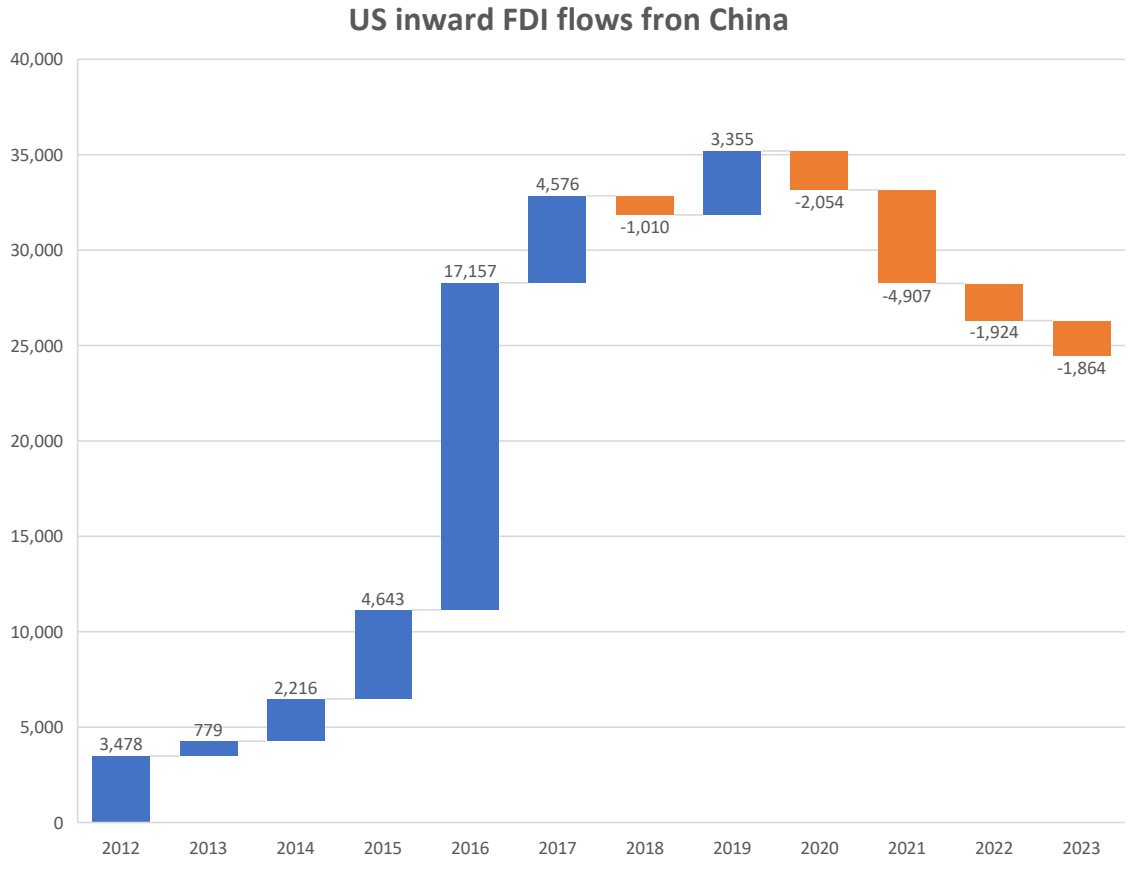



**As from 2021 the value of US outward FDI stock in Mexico was larger than in China. In 2023, 144.5 billion US dollars as again 126.9 billion.**

*Source: calculations on the basis of Bureau of Economic Analysis, U.S. Department of Commerce*

# US inward FDI from China




*Source: calculations on the basis of Bureau of Economic Analysis, U.S. Department of Commerce*

# FDI from China to the US

- **As the previous graph shows, FDI from China to the US (US inward FDI from China) has collapsed since 2017 at the exception of 2019. China has gone from one of the top five US investors to a second-tier player. Additional investment flows since then have been offset by divestitures or write-offs.**

- **Not only has investment slowed, but assets, revenues, and employment at Chinese companies in the US have all declined in recent years.**

- **US policymakers started to shut Chinese companies out of certain markets for national security reasons, for example banning the use of Chinese telecommunications equipment.**

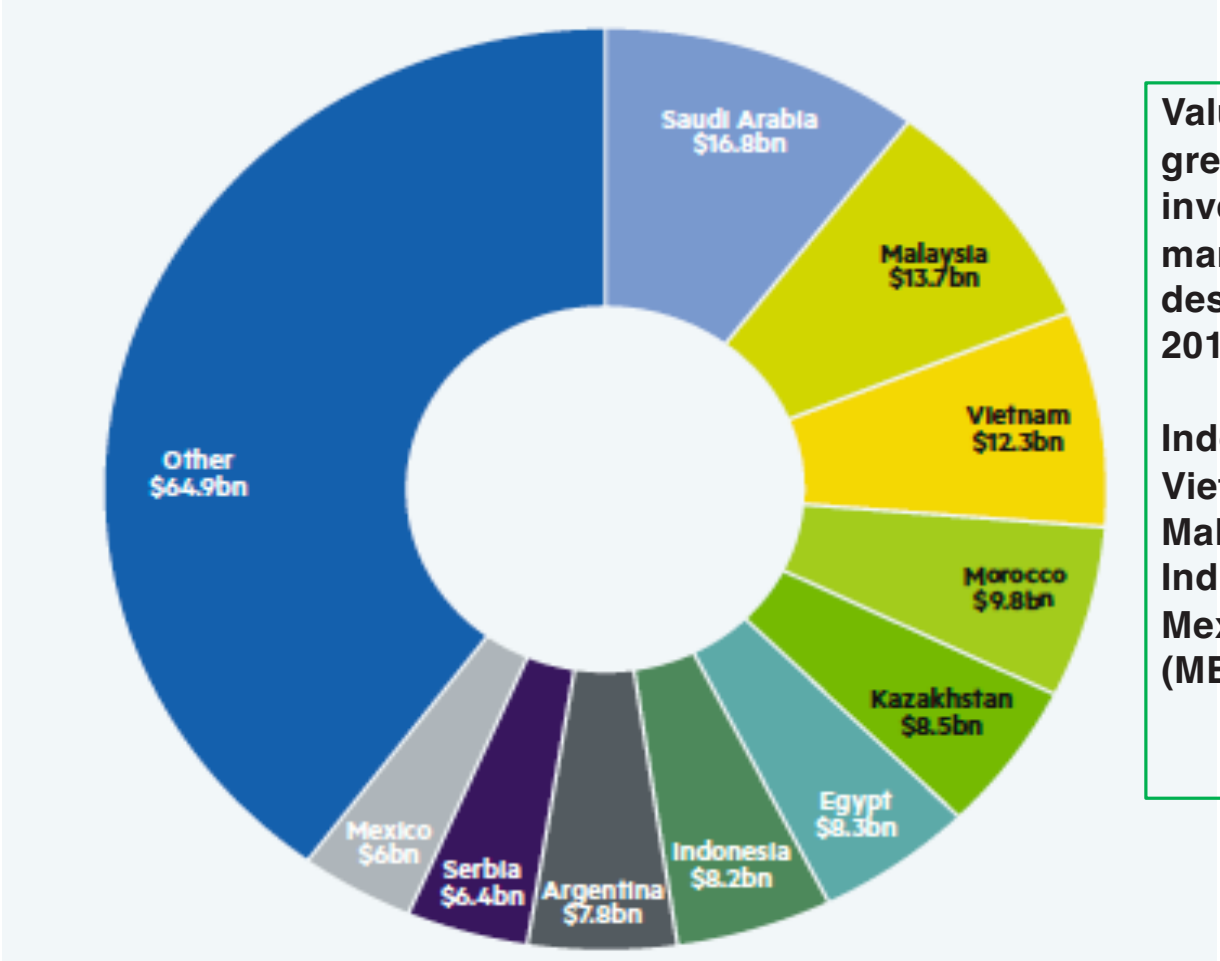
- **The Biden administration further expanded export controls and sanctions against Chinese companies. Most importantly, Congress enacted powerful new industrial policies that incentivize large capital expenditures into US manufacturing, but explicitly forbid or restrict the participation of Chinese investors, most notably the CHIPS Act and the Inflation Reduction Act (IRA).**

## On the other side, China: from capital importer to capital exporter

**On the basis of the balance-of-payments statistics released by the State Administration of Foreign Exchange, China's net direct investments revealed a deficit of $142.6bn in 2023, that is the outflows of Chinese investments abroad have substantially exceeded the inflows of FDI into China.**

**As a consequence, as from 2023 China, from being a capital importer, has become a capital exporter.**

## Top destinations of Chinese FDI in 2023




**Value of Chinese greenfield foreign direct investment in manufacturing by destination country, share 2015-2023:**

**Indonesia 7.2%**
**Vietnam 6.0%**
**Malaysia 4.9%%**
**India 4.7%**
**Mexico 4.1%**
**(MEMO: USA 5.4%)**

*Source: The Fdi Report 2024*

## Summing up on FDI

- **The data shows that FDI flows in both directions have declined, those coming from China went even negative as from 2020.**

- **On the contrary FDI flows remained sustained towards the rest of the world, in particular towards some emerging countries.**

- **In 2017-2023 the percentage increase of US outward FDI stock towards Vietnam and Mexico was more than the double compared to the one directed to China.**

- **In 2023 China turned for the first time into a capital exporter country.**

- **Unlike in the past, most of the Chinese outward FDI went to emerging countries. The value of Chinese greenfield foreign direct investment in manufacturing by destination country in 2015-2023 has seen Indonesia and Vietnam taking the lead in front of the US, closely followed by Malaysia, India and Mexico.**

- **In 2023 the US were not among the top ten destinations of Chinese greenfield foreign direct investment in manufacturing. More than half of the total was represented by emerging countries.**

# Firms' actions and intentions

**Trade and FDI reshuffling is obviously the consequence of reactions of thousands of firms.**

**The third piece of evidence on decoupling comes from the actions and the intentions of firms, mostly Multinational Enterprises (MNEs).**

**Here no complete set of data exist. We have to rely on surveys, case studies, anecdotical evidence, MNEs' callings and the like.**

**All this evidence enriches the previous analysis and sheds some light on the possible interpretation of the trends, as we shall see in the last part of the presentation.**

**Let's start from some anecdotical evidence of firms shifting away from China.**

# The “ China+1” strategy

**Recent disruptions in regional supply networks have shifted the focus from supply chain efficiency to supply chain resilience. Firms started replacing single-sourcing of critical components with multiple and geographically diverse supply chains.**

**For the first time in about 25 years, China is not a top three investment priority for a majority of US firms, an American Chamber of Commerce in China survey showed. The survey also found that the proportion of companies moving supply chains elsewhere, or considering doing so, has almost doubled from a year ago.**

**A trend away from China-based sourcing had already begun in the 2000s, when companies started to adopt “China+1” sourcing, as China started looking less attractive relative to other Asian countries and countries like Mexico.**

# Apple

- **Apple and most or all technology firms that have previously been entirely dependent on China, have been working to move away from that reliance, in part because of continued US/China trade tensions.**

- **It has already moved some of its iPhone production to India. However, for the iPhone, the majority of production remains centred in China, but recent investments in India are just starting to create a new manufacturing hub where the company could export large volumes to the US, and it was exploring moving its iPad manufacturing there, too.**

- **Vietnam has evolved into a major production hub for computers in recent years and small volumes of MacBooks, iPads, and the Apple Watch are already being manufactured there.**

- **Apple and its 188 major suppliers are all investing outside of China. Apple's suppliers, including iPhone manufacturer Foxconn, have invested $16 billion since 2018, in an increasing plan to move manufacturing away from over-reliance on China.**

## Foxconn

**70% of Foxconn's revenue comes from China. However, the proportion of revenue from outside the country will continue to grow.**

**Foxconn has already announced a $700 million iPhone production plant will be built in India and is spending $300 million on leases in Vietnam. However, it is also continuing to expand in China.**

**Double strategy:**

- **relocate its high-end manufacturing to the United States. Once situated in the US Foxconn could take advantage of geographical proximity to develop new deals with partners such as Apple as they create new technology.**
- **relocate low-end manufacturing to Indonesia. Indonesia is attractive for Foxconn due to its large labour market, low costs, yet modest manufacturing skills. As a member of ASEAN, Indonesia has duty free export status on all products within the ASEAN bloc and as such has tax treaties and free trade agreements with China – meaning certain products can be made at comparatively cheaper wage levels and then exported to China duty free and to the US without incurring into the US tariffs. Furthermore, Foxconn intends to invest US$10 billion over five years in conjunction with its Indonesian partner Erajaya Swasembada.**

## Other cases

**TSMC, the worlds largest contract chipmaker, is not leaving China altogether — but it is expanding elsewhere, including Taiwan and the US. Two out of 18 TSMC plants are located in China — the vast majority of the factories are still in Taiwan. In December, TSMC announced it would be opening a second factory in Arizona. Apple is TSMC's largest customer, accounting for 26% of its revenues last year.**

**Japanese carmaker Mazda used to produce car parts in China — but it has changed position, asking its parts suppliers to manufacture components outside China.**

**Elon Musk last year unveiled plans for a new Tesla Gigafactory outside Monterrey in Mexico. However, the electric car company is yet to break ground on the $10bn plant.**

# China’s multinationals join the race

**Minth Group, which makes structural body parts for cars, last year signed an agreement with Renault to set up a joint venture to make battery boxes at a plant in France, and broke ground for a factory in Poland. These add to factories in Thailand, Germany, Serbia, the Czech Republic, Britain, Mexico and the US.**

**Chinese tech suppliers are rapidly expanding into Southeast Asia, posing a significant challenge to Taiwanese and other long-standing suppliers for major tech companies like Google and Apple.**

**Similarly, China's BYD is vying to produce Pixel phones in Southeast Asia.**

**The single largest outbound Chinese project in 2023 was a $10bn investment by automotive giant Zhejiang Geely, to establish a car making hub in Tanjung Malim, Malaysia. The hub will serve as the headquarters of Proton, a local manufacturer of which Geely owns 49.9%.**

**Fuling Plastics moved a factory to Indonesia and then opened a factory in Pennsylvania.**

**Most of Chinese outward FDI is in manufacturing. But online brands such as Alibaba, TikTok, and JD.com are also going global. Bytedance, TikTok’s parent company, was the fifth-most active Chinese investor last year, announcing nine FDI projects.**

# Firms' intentions to shift away from China

**A second piece of evidence comes from earnings conference calls conducted by listed firms. Many speak of potential shifts in offshoring arrangements away from China.**

**According to a recent AmCham Shanghai report, approximately 13 percent of surveyed firms said they were considering shifting production outside of China. References to nearshoring, friendshoring or reshoring have been on the rise in companies' earnings calls since 2018 and a good share of these discussions pertains to potential moves away from China toward Vietnam or Mexico.**

**At the same time, China has dropped off in prominence as a preferred destination for greenfield FDI originating not only from the US but from other FDI source countries as well.**

# Nearshoring

**In order to diversify their supply chains away from China many companies decided to invest elsewhere, in particular in a process of nearshoring. Nearshoring, the movement of production closer to final consumers, is not new, but is on the rise. More companies mentioned nearshoring in 2023 earnings calls than any previous year since 2010. A recent study from AlixPartners shows that close to 94% of respondents are seeing more nearshoring. Nearly all respondents have developed actions to reduce dependency on China. Roughly a quarter have already reduced exposure by 10%; an additional one-third of respondents will hit that threshold within the next year. Companies are targeting an overall 35% reduction in China's sourcing share.**

**Manufacturing FDI into nearshoring destinations can:**

- **target the locations in themselves, where there are growing domestic markets and middle classes**

- **nearshore production in order to bypass tariffs and other trade impediments**

**One set of firms targeted South Asia and ASEAN countries close to China. According to fDi Markets, more than $124bn was pledged to greenfield FDI manufacturing projects in ASEAN in 2022 and 2023. The five largest Asean economies — Indonesia, Thailand, Singapore, Vietnam and Malaysia — accounted for 96.5% of manufacturing FDI pledged to the region in 2022 and 2023. The ASEAN region has recently overtaken China as the destination of choice for manufacturing investment for investors from OECD countries by an amount pledged equal the double of that announced for China. In 2017 it was exactly the reverse.**

# Nearshoring to Mexico, with an eye to the US market

**Many US firms have increased their announcing of nearshoring in 2023. According to a survey conducted by McKinsey, Mexico attracted 80% of nearshoring cases and 74% of nearshoring jobs, while Canada took the rest.**

**In recent years, Mexico has been the preferred destination of nearshoring FDI targeting the US. In 2023, an all-time high of $25.5bn was pledged to manufacturing FDI in the country, according to fDi Markets.**

**Advantages:**

- **Cheap, skilled labour**
- **Access to the USMCA Agreement**
- **Reduction of manufacturing time and cost**

**Two main groups are driving nearshoring to Mexico: US companies already established in Mexico looking to expand, and Asian companies attracted by the benefits of producing in North America.**

**FDI in Mexico is mostly directed toward manufacturing plants and regions that export to the US. Mexico is a natural location for the final stages of assembly of goods, such as motor vehicles, destined for the US market. The Mexican manufacturing sector has been the target for 47 percent of US investment, of which the automotive sector accounted for roughly one-third of those outlays. The US auto industry relies heavily on parts produced in Mexican *maquiladoras* plants that produce primarily for export. Most motor vehicle parts produced in Mexico are for foreign markets and include such global brands as General Motors, Ford, Honda, Hyundai, Kia, Toyota, Mercedes-Benz and Nissan.**

# Anecdotical evidence on Chinese firms' relocation to Mexico

**A large part of this nearshoring FDI to Mexico has been made by Chinese companies, which now represent the fastest growing source of foreign investment in Mexico. Their investment predominantly targets the manufacturing sector, ranging from computer equipment (e.g., Lenovo's "mega site" investment in Mexico on computer, server and computer rack assembly), construction equipment (e.g., Lingong Heavy Machinery) and electric-vehicles.**

**The auto industry accounts for over half of the value invested by Chinese companies. Three of the country's largest car makers — MG, BYD and Chery — are investing billions of dollars to build factories in Mexico. Tier 1 and 2 automotive suppliers have invested in Mexico to support these factories and supply the North American market. This includes aluminium part maker Ningbo Xusheng Group, tyre manufacturer Jinyu Group and Bethel Automotive Safety Systems, a China-based braking specialist.**

**Beiqi Foton Motor, a China-based automobile manufacturer has earmarked a $1bn investment for a new EV manufacturing facility in the country, with potential sites being considered in the states of Jalisco and Aguascalientes.**

**The Man Wah Furniture has a factory in Monterrey that produces reclining armchairs and leather sofas destined for large retailers in the US, like Costco and Walmart.**

**Fuling Plastics around 2019 moved some production to Monterrey, Mexico.**

**Two Chinese companies, LGMG and Jetour, made announcements totaling $8 billion last year, or over 60% of the total expected FDI for China.**

# Mexico as a backdoor to the US market?

**Several media (The Economist, among others) reported that Chinese companies are using Mexico as a "backdoor" to the United States, as products made there can be exported tariff-free to the US. Hence the concern of US policy-makers (see the bi-partisan letter from 4 US senators to the US President in September 2024) that the role of Mexico is countering US efforts to restrict the import of Chinese goods.**

**Although not all China's manufacturing outward FDI has been motivated by the desire to access the US market, a sizable portion of it might have been so. One suggestion derives from the fact that this FDI concentration is reflected in Mexico's exports and export growth to the US: for instance, Mexican exports of autos and associated products grew 40% between 2017 and 2023. They represent Mexico's largest export to the US, accounting for 27% of total exports.**

## Anecdotical evidence on firms' relocation to Vietnam

**Investor-friendly policies, along with tax breaks and emerging industrial hubs, have made Vietnam an attractive destination for foreign investors.**

- **Samsung subtended its first FDI in Vietnam in the early 2008 for the construction of a mass production mobile handset plant in Northern Vietnam. Samsung has established Vietnam as its largest Southeast Asian product development center.**
- **Japanese AEON Tan Phu has expanded its network of shopping malls and stores in six provinces.**
- **Taiwan's Formosa Plastics Group reported underwhelming results for its steel manufacturing arm in the north-central region, Formosa Ha Tinh, in 2023.**
- **Google, Dell, and Amazon have also begun setting up production facilities in Vietnam.**
- **Intel has invested US$1.5 billion in Vietnam since 2006 with a chip manufacturing and testing facility in Ho Chi Minh City.**
- **Amkor Technology increased its capital in its Bac Ninh factory by over USD 1.07 billion in 2024.**
- **Foxconn Circuit Precision is building a USD 383.33 million factory in Nam Son-Hap Linh Industrial Park.**
- **Dutch semiconductor company BE Semiconductor Industries N.V. (BESI) invested over 115 billion VND (USD 4.9 million) in a new project at Saigon Hitech Park, expected to begin operations in early 2025.**
- **In addition to manufacturing and retail, Vietnam continues to attract foreign investment from the banking sector. HSBC Vietnam, the first wholly foreign-owned bank in the country, reported record profits in 2023.**

# Evidence on Chinese FDI to Vietnam

**The role of China as a source of inward FDI into Vietnam is even more pronounced than in Mexico. Using proprietary Vietnam Annual Enterprise Data China's share of inward FDI by value rose from almost 0 at the end of the 90s to 7% in 2017. Public data from Vietnam's General Statistics Office confirm that this trend has been sustained : China's share by value of all FDI projects granted licenses by Vietnam in 2021 was 7.7%. By comparison, US multinationals have a smaller presence in Vietnam, with a 2% share of all new FDI projects in 2021.**

**Chinese firms have thus been increasingly active as a source of FDI into Vietnam, with the timing of this rise coinciding with the US' imposition of tariffs on imports from China. Foreign direct investment (FDI) into Vietnam rose by 8.8% year-on-year to USD 19.58 billion from January to October 2024, according to data from the Ministry of Planning and Investment.**

**Meanwhile, FDI pledges, which serve as an indicator of future disbursements, increased by 1.9% from a year earlier. The largest investors were Singapore, China, South Korea, Japan, and Hong Kong, accounting for 76.5% of total FDI over the period. Singapore, China, and South Korea topped foreign investments, with $7.79 billion, $3.61 billion, and $3.56 billion, respectively.**

## Anecdotical evidence of Chinese firms investing in Vietnam

- Foxconn Technology Group announced its new plant in Vietnam that has just been put into operation. Foxconn has so far factories in five provinces in Vietnam with a total investment of 4 billion USD, employing about 80,000 workers. Notably, Foxconn said it has decided to pour nearly 400 million USD to build a factory producing electronic components and assembling and processing PCB circuit boards in Nam Son Industrial Park in northern Bac Ninh province
- Nokia announced cooperation with Foxconn to produce AirScale products, including the latest generation of massive MIMO AirScale radio devices serving 5G infrastructure. A Nokia representative said the project will start in July, and products made at this factory will be used in both the domestic and international markets. Foxconn is Nokia's global manufacturing partner, and will expand its capacity to produce Nokia’s 5G products in Vietnam.
- Google has enlisted its Chinese supplier Goertek to manufacture Pixel watches in Vietnam, a role previously held exclusively by Taiwanese companies.
- Chinese companies such as TCL Technology have increased their manufacturing capacities in Vietnam.
- The photovoltaic (PV) module supplier Trina Solar plans to open a third manufacturing plant in the province of Thai Nguyen. Announced investment: $400m.
- Alibaba announced plans to launch teams across Vietnam’s emerging manufacturing centres.
- Chinese makers of car parts are facing growing pressure from overseas customers to set up factories in places like Vietnam and Indonesia.
- China’s Sunrise Elc Technology, has already established a plant in Vietnam that makes set-top boxes for the consumer market overseas.
- Luxshare Precision Industry, a Chinese supplier for U.S. Apple, has recently partnered with Taiwan-based Foxconn to start trial production for the Apple Watch in northern Vietnam with the aim of producing the device outside of China for the first time.

# Vietnam as a gateaway to the US?

**Traditionally, Asia has long provided goods to China for the country to process and re-export to meet final demand elsewhere. This is known as processing trade. According to Nomura analysis, Asia's processing exports to China have declined, reflecting both trade diversification and trade diversion away from China.**

**Trade diversification away from China is benefiting India and ASEAN. Vietnam stands out as a key beneficiary, as supply chains have relocated from China to Vietnam across electronics, textiles and toys segments over the last 5 to 7 years.**

**I have previously shown that, like in the case of Mexico, Vietnam gained part of the China's market share lost in the US market. Like Mexico did for auto parts, Vietnam did in the case of semiconductors, smartphones, routers and other electrical and electronic parts and components, with the Chinese financing at least some of the capacity required to increase its market penetration of the US. China's manufacturing-related outward FDI to Vietnam has been dominated by investment in the capital goods sector. About one-third of projects are related to electronic components, semiconductors, and communications equipment.**

**Paradoxically, the "comprehensive strategic partnership" between the US and Vietnam includes an agreement on semiconductors, with the United States committing to help Vietnam develop its capabilities and expand production. The country's semiconductor industry has become a vital component of global supply chains, positioning itself to play an increasingly important role strategically located within ASEAN.**

- ***The data on trade and FDI seem to point to a decreasing interdependence of the two superpowers.***
- ***But do these measures capture the size of decoupling correctly?***
- ***Problems of measurement arise both for FDI flows and for trade flows***

## Caveats about FDI data

**FDI data based on Balance of Payments often under report the actual FDI (by 6 times, as in the case of Chinese FDI in Mexico!). The official stock figures reflect well-known gaps and distortions in balance of payments FDI data, due to investments through offshore entities in Hong Kong, the British Virgin Islands and elsewhere, which only channel, rather than originate investments. In our case, some of the latter may pertain to Chinese entities in disguise.**

**The most reliable and widely used private database on FDI, fDi Markets, tracks crossborder investments in new physical projects or expansion of existing investments which create new jobs and capital investment, but does not include mergers & acquisitions (M&A) and other equity investments. Moreover, as companies do not always release information on investment amount or job creation, a proprietary econometric model estimates the jobs and investment where the actual value is not known.**

**The result is that US FDI dependency on China might be larger than it appears at first sight.**

## Some caveats about the measurement of US-China trade flows

**The major problems about a correct measurement of decoupling relate to trade flows. Some portion of the export boom by emerging countries and part of the official contraction of Chinese exports to the US might be due to fraudulent re-routing of Chinese products through other countries with the help of fake local product-origin certificates, as companies try to sidestep U.S. tariffs. The most blatant example being Vietnam, where the government revealed that it had discovered numerous Chinese products fraudulently labelled "Made in Vietnam", ranging from textiles to agricultural goods and destined to the US market. According to some other anecdotical evidence, products, such as plywood produced in China, may have been shipped to the U.S. in such a way.**

**Evidence of less overtly fraudulent trade diversion tactics include the process known as "knockdown"—that is, "knocking down" a product into its component parts and reassembling them outside China.**

**But the greatest problem derives from the very nature of conventional trade, as documented in the official national and international database. These database show data on gross trade as it appears at the border of each nation, that is, for example, the final assembly country that is the source of US imports of a good. However, manufactured goods most of the time embody value added coming from other countries. Goods that are not exported from China anymore, but, say, from Mexico or Vietnam, may incorporate inputs from China. In this case, a portion of dependency would not appear openly, but would still be there in disguise.**

# In search of value-added trade

**If we could measure exactly the role of emerging countries and the triangular connections between them, China and the US , we could also quantify how much dependency on China goes beyond the level that appears from the official data.**

**To have an exact measure of such a phenomenon we would need detailed databases on trade in valued added for all the countries involved. So we could calculate the value added at each step and how much Chinese value added is embodied in such trade flows for each of the products involved.**

**The only international database containing value added trade is TiVA, that provides insights into global production networks and supply chains beyond conventional trade statistics. TiVA tracks the origins of value added in exports, imports and final demand. Unfortunately it stops for the moment at the year 2020, so that it is not useful for our purpose: most of the crucial changes in decoupling have materialized after that date. But this would be a fruitful direction of research for this topic.**

## Do some emerging countries function as hotspots to the US market?

**Some of the trends evidenced by the trade and FDI flows and by the MNEs' behaviour suggest that some emerging countries may function as hotspots for the two contenders to avoid the new impediments to the reciprocal economic relations.**

**There are interesting associations in the data presented at the beginning:**

- **an inverse relationship between the evolution of market shares of China and of some emerging countries in US imports**
- **a positive relationship between China's outward FDI to some emerging countries and the exports of the latter towards the US**
- **a positive relationship between China's exports to some emerging countries and the exports of the latter towards the US**

**These correlations, plus the anecdotical evidence, are at best suggestive of some emerging countries, Mexico and Vietnam in particular, functioning as hotspots. Unfortunately, they cannot quantify the impact on decoupling.**

## Shifting away from China: easier said than done

**Finally, one must remember that "shifting away from China" remains a contradictory process.**

**The decision to leave or partially leave China through shutting subsidiaries still remains a difficult choice for many multinational enterprises (MNEs). Despite its rising labour costs, China remains competitive, thanks to its current workforce availability, extensive supplier base, logistics infrastructure, and key role in certain industrial value chains. A vice president of government affairs for GM China put it this way: " If an American company is not in China, it cannot be a global leader and cannot benefit from economy of scale."**

**Supply switching does entail higher costs in the near-term, although there are benefits to the product costs in the longer term, once the ex-China capacity is fully at scale. It takes up to 18 months for a company to establish a new manufacturing plant and potentially even longer to organize the whole supply chain and to reap full operating benefits.**

**Next to the China+1 model, many US MNEs have moved toward a business model of "In China, For China" to produce for local consumption rather than export and to invest in local research and development. Since 2008, many US MNEs also accelerated their efforts at management localization to reduce management cost, develop and retain local talent with more local competencies, and maintain good relations with local governments.**

**According to the AmCham 2023 China Business Report, a notable 42 percent of member companies with research and development (R&D) activities in China are increasing R&D investment within the country. This reflects the renewed support by the Chinese government in this field.**

# Import dependency remains high in some sectors

- **Import dependency remains high in some labour-intensive sectors: toys, 73.2%; footwear, 37.2%; furniture, 23.8%.**

- **But also in some capital intensive sectors: lithium-ion batteries, 71%; routers, 23.3% ; tv receivers, 32%; smartphones, 76%; personal computers, 78%; laptops and computer monitors, 92%.**

- **About half of US total imports from China depend on the latter for 50%.**

# China is still a pillar of manufacturing GVC

**The US-China commercial relationship remains a crucial pillar to manufacturing supply chains. While some delinking is taking place with the U.S., China is still one of the main hubs of global value chains. Chinese supply chains may be less visible, but they remain extremely important to the American economy. According to the latest data from the WTO, China is still one of the two main world importers and exporters of intermediate goods, together with the US.**

**In their quest to diversify sources, companies will find it difficult to replace the immense production capacity and relatively low costs that China offers. Economic efficiency, provided by China's huge scale and manufacturing expertise, is a powerful force in favour of the status quo.**

**Two examples:**

- **for a company like Apple, which has moved some assembly of its iPhones to India, China's workforce and production ecosystem are virtually irreplaceable. The country has hundreds of smaller suppliers feeding into huge assembly plants, giving Apple the scale and flexibility to respond to demand.**

- **in shipbuilding: China has 76 port terminals able to service ships carrying more than 14,000 20-foot containers, while potential rivals across South Asia have a combined 31. So moving manufacturing away from China ultimately means higher costs for merchandise importers.**

## The main ingredients of the “economic embrace” are still there

**Finally, let’s remember that, although trade and FDI present some evidence on declining interdependence between the two superpowers, the main ingredients of the “economic embrace” are still there:**

- **masses of cheap Chinese consumer goods are still flooding the US market. China is still the manufacturing powerhouse of the world. The US-China commercial relationship remains a crucial pillar to manufacturing supply chains.**

- **at the same time they continue to fuel China’s export-led growth, providing it with millions of jobs**

- **US FDI flows to China, albeit declining, have continued to be positive, increasing the US outward FDI stocks.**

- **China is still the second world holder of US debt behind Japan**

## By way of conclusion

- **Real dependency on China is possibly larger than it appears and, conversely, the process of decoupling might be milder than generally thought. A portion of disguised dependency may be due to the ties created through some emerging countries functioning as gateaways to the US market. Unfortunately, these are not easily quantifiable.**

- **The hard version of decoupling doesn't look yet in sight. Both countries are still very important to each other. But the process of decoupling seems to be accelerating…**

*Thank you for your attention!*