

**The effects of Antidumping Measures on the FDI:
A Pre-marketing Behavior Aspect Analysis in China**

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Abstract

In order to sustain its development, China is at a critical time of needing more foreign investment and advanced technologies. But China needs to make use of the anti-dumping measure to keep the order of fair trade in international trade. In the existing cases, there are some big multinational corporations involved, which are investing or planning to invest in China. Whether the anti-dumping measures affects their investment interests in China and cause them to retreat or divert their investment, thus it will possibly affect the development of China's economic growth. In this paper, we analyze the essence of the pre-marketing behavior and the general effects of the antidumping measures to the pre-marketing; analyze the relationship between the pre-marketing behavior and its investment strategy, then, we describe a theoretical model by using the game theory. We finally, found out that the Pre-marketing compliant is in essence a contemporary way of the multinational corporations enlarging the its interests under China's anti-dumping measures; and the pre-marketing is only an extra-favor that the Chinese government given to the multinational enterprises and it plays little role in its decision making of FDI in China when other conditions of the foreign investment remain unchanged. Based on the above findings and the remaining statistics, the FDI of the multinational corporations will not be affected when China imposes fair antidumping measures to keep a fair international environment and sustainable economic growth in China in the long run.

Keywords: Antidumping, FDI, Pre-marketing, Effects

1. Introduction

Since 1978, China has been sustaining its development with many successful policies, and has reached remarkable achievements. Among them, the most highlighted policy is the opening policy of attracting foreign direct investment (FDI). In recent years, statistics showed the FDI related export has played a very important role in China's export and the economic growth. But after China's accession to the WTO, as china has more of the FDI, the effects of FDI in China became one of the hot issues in nowadays. Since 1997, China has imposed more than 30 anti-dumping (AD) measures towards the imported goods, these are the rightful undertakings of the WTO AD measures and brought positive results of keeping a fair trade and protected home enterprises. Among the products involved, there are some products of the companies that are making or planning making investment in China, thus when there is a dumping duty to the pre-marketing goods, the prices will definitely arise, and the FDI companies complaining their lawful pre-marketing goods had been charged an extra AD duty. And there is a doubt of whether the AD measures will make the FDI divert their investment direction. What really pre-marketing mean to the FDI companies in their investment strategy? And will AD affect adversely the FDI in China?

2. Pre-marketing and AD analysis

2.1. What is Pre-marketing?

In the common textbook of marketing, Pre-marketing means the performance of a company's selling the target product from another market to the target market before the company can produce, it is quite normal to do so when it is a domestic company performs pre-marketing on the home market. The purpose is to prepare for the future production and selling. In essence, this is a kind of marketing tactics. If there is the anti-trust regulation, it will not do harm to the market system.

The pre-marketing that was caught in the anti-dumping measures in China is a little different from what is mentioned above. This time the pre-marketing comes from abroad, and the quantity is quite huge that caused market injury and it hit the high tension line of dumping. What make it even worse is that the pre-marketing was permitted by the government. So the companies argue that it will do harm to their investment and some even imply canceling the plan. In fact, since the investment of such enterprises may last for several years, the pre-marketing will continue to be a lasting flow of import goods. The foreign company will make use of the market share and low price tactic, thus affected the industrial development of the host country, and even impact the structure of the existing industries.

Generally, when the Multinational Enterprises (MNEs) sign the contract of investment, they may require selling the same products they

will produce to China from a third market before they can make it, so pre-marketing is permitted by the authority. The common operation in the pre-marketing stage is done by penetrating pricing (PP), by which the new products were sold at an intentionally low price, so the new product will take a bigger market share and receive an immense demand¹ At the beginning stages, holding and maintaining the market share is placed at high priority in the competitive tactics, so most of the MNEs will take PP as the main tactics in the pre-marketing period of its investment.

2.2. Pre-marketing---one policy arrangement of China

The pre-marketing agreement is a policy arrangement that China provided to help the MNEs to invest in China, since the duration of the investment is quite long and the scale is often quite big, it is quite natural to provide pre-marketing when the import license policy is still operating. This is an extra-favor that china given to the MNEs in the early 1990s.

These MNEs are mainly in the trade of Chemical and petroleum. The production line is very long and highly vertical integrated, so the investment requires high safety. Under the former foreign trade law of China, the company that has not begun its production has no right to import and export goods besides the needed material for constructing and investment. So if pre-marketing was not given to the MNEs, maybe they were still justifying the investment. By pre-marketing, the MNEs would know the market demand and prepare its future sales as well.

But beyond the expectation of the Chinese government, the pre-marketing volume is so big and the price is so favorable to the customers in China that the domestic enterprises may suffer from this low price competition. The MNEs are at a favorable market position because of their scale and advanced technology and superior cost advantage compared to Chinese counterparts. The entry of MNEs in the field will definitely cause material injury or impede the establishment of the domestic industry in that trade. So the pre-marketing becomes a dumping performance in China, and it met the anti-dumping measures. According to the present AD law, this pre-marketing is under the governance of the AD law. The problem is that when the formerly agreed pre-marketing encounters AD measures whether it will affect the investment decision.

2.3. Pre-marketing and AD

In China, we have begun launch AD since 1997, there are only 30 more the cases, and mainly in 4 industries. Most of the AD measures brought about positive protection effect. But some MNEs argue that the AD towards the pre-marketing is inadequate, and it will affect their investment decision.

2.3.1. What is AD?

AD is the common trade policy in protecting the domestic enterprises under the WTO framework. Firstly, the recognition of

dumping. Dominick Salvatore (1997) defines dumping as the export of a commodity at below cost or at a lower price than sold domestically. Article VI of GATTs(Hanlin Zhang,2003) has that an industry in one country is materially injured or threatened with material injury, or that the establishment of an industry is materially retarded, by reason of imports that are being, or are likely to be , sold in this country at less than fair Value(LTFV).

Here we analyze the relationship between pre-marketing and Dumping. 2 more elements need to be considered, the dumping should cause material injury to the domestic market or cause the establishing of the companies difficult; and the injuries are directly caused by the dumping of the like products.

3. The effects of AD to the FDI ?

3.1. The effects of an AD to the exporters

The imposition of AD may cause multiple results to the interested parties. The most prominent result the price of the imported goods would be corrected to the fair trade level, and superficially the exporters may face a reduction of demand to its goods due to the raised price. Thus the volume of export will sharply decrease or force the products out of the domestic market. There have been some related empirical literatures.

Dutz (1998) finds that antidumping cases led to a decrease in import competition faced by domestic firms as a consequence of the increase in prices resulting from this trade remedy. He estimates that less than 0.6 percent of manufacturing shipments were covered by

antidumping duties in 1990, but that this does not include the costs of a decrease in competition for the domestic industries, nor the ripple effect on downstream industries, as users of the products subject to antidumping duties face a decrease in the availability of low-cost inputs.

Prusa (1999) estimates the effect of antidumping for the United States. His findings are that antidumping investigations have a substantial effect on imports, whether or not antidumping duties are applied. The decrease of the value of imports for the countries targeted by antidumping investigations is in the 50 to 70 percent range. For those cases that are turned down, there is a decrease of imports of 15 to 20 percent. Prusa also mentions the high level of protection that results from the application of antidumping duties, particularly when compared to the currently low levels of average tariffs: the level of the median antidumping duty was 16 percent, when the industries thus protected faced MFN tariffs of 4 percent in average. There were antidumping duties of over 50 percent (20 percent of the cases) and of over 100 percent (10 percent of the cases).

The main and direct AD effect which is related to Pre-marketing (PM) is the price effect. When imposing AD measures, the AD duty added to the PM Price may cause it rise, thus it will make the PM volume decrease. In fact, there is possibility of keeping the same level of revenue even after the AD. Then we need know how much does PM matter in the FDI in China.

4. The role of Pre-marketing in FDI

4.1. What are the factors that determined a FDI in China

Modern theories about the motives of FDI denote that there are 4 kinds: market –oriented motive; factor searching motive; potential advantage motive; global strategic development motive. (Weiguo Xiao, 2002, P135-151)

If we analyze the economic situation in China, we can find abundant evidences for each of the specific motives for the MNEs to invest in China.

As China has the largest population in the world, the potential demand will definitely enormous if China can sustain its development, so the market is irresistible to the MNEs in the world. Thus the potential market is the first important factor that attracts FDI from the other part of the world. This is consuming aspect of the issue.

In relating to the investment, production is one of the core procedures. In China, we have the most valuable and advantageous factor in the 21st century---human resources, which is quite expensive in the home country. Although what the MNEs need most in China is the well-educated employees, the low cost of labor is still attractive to the labor –intensive industries.

Form a dynamic view, China is now undergo a healthy developing, the potentialities of China will be the realistic advantage to the MNEs in

the near future. The possible potentialities would be same luring to the MNEs.

From the strategic view, China has been a member of the WTO, China is now going to a more liberalized economy, and emerging to be one of the largest economic body in the world. Most of the 500 world biggest MNEs (more than 400) have invested or investing in China to cater to their needs of global development strategy.

So, the fact that matters most to the MNEs in China is the market capacity; the cheap and abundant labor forces; promising potentialities and the increasing role of China in the strategy of its global development.

4.2. The role of Pre-marketing in FDI

The above analysis shows that the most decisive matter in the FDI decision making is their **STRATEGIC** interest in China. And the problem of **PM** that caught in the Chinese AD measures is only a tactics in the FDI. Will that AD duty powerful enough to drive the FDI away from China? Before we get to this question, we should know the general risks for an FDI.

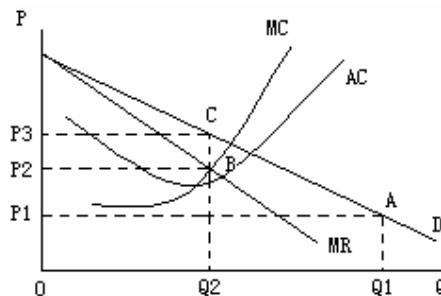
If we consider the whole process of the investment, there will be building risks, production risks, and management risks, sales risks; if from the elements of the operation, there are human resource risks, market risks, financial risks, technology risks, and systematic risks (external risks), contract risks, exchange rate risks.

Among the risks, PM could do little help in avoiding them, it can only make the investment a bit easier to undergo. But when signing the contract, the Chinese government did not restrict the price and quantity of the PM, thus left room for the PM to be a negative element in the FDI process to the domestic enterprises (became a dumping.)

5. How to Prevent the Problem of PM into Dumping?

5.1. The monopolistic Market power of the PM enterprises

According to economic theory, dumping occurs when the PM enterprises (PME) can affect the prices of the PM goods in the host country market, so it is likely to happen in an incomplete-competitive market. From the micro-economics theory, if the PME wanted to acquire optimal profit, there are two conditions need to be realized: the average revenue of the product equals to the total average variable cost, i.e. $AR \geq AVC$; and the marginal cost equals to the marginal revenue, i.e. $MC = MR$.



The Pre-marketing of the MNEs in China under the monopolistic competition

This graph is about short term equilibrium of the Pre-marketing of the

MNEs in China under the monopolistic competition. According to rule of maximizing profit, the equilibrium point of production point is B(P₂, Q₂), while the MNEs wanted to expand the demand to their products, they sell the products at a lower price P₁, if there is no quantity restriction, the whole sales is Q₁, thus a dumping is happening.

5.2. The trivial quantity of the PM-causing dumping control

There is a rule about the trivial quantity control. If the import of the products is less than 3% of the whole import of the like products in China, and the total sum of those under 3% is no more than 7% of the general imports of the nation, and the margin of the dumping is less than 2%, this kind dumping is forgivable. Also, we take the average increase rate of China's GDP as the increase rate of the trade, and assume that if the increase rate of the PM is less than that of the trade, it will be no harm to the domestic enterprises. Since the PM is a previously authorized policy to the MNEs, if apply this rule to PM dealing, it will be suggestive. The above deduction can be shown by the following equations:

$$\begin{aligned}
 (\Sigma dq_i^{im} / \Sigma dq_T^{im})_t &\leq 10\% & (i=1, 2, 3, \dots, n) & \quad (1) \\
 (Q_i^{im} / \Sigma Q_i^{im})_t &\leq 3\% & (i=1, 2, 3, \dots, n) & \quad (2) \\
 (Q_i^{im} / \Sigma Q_T^{im})_t &\leq 7\% & (i=1, 2, 3, \dots, n) & \quad (3) \\
 (P_i^p - P_n) / P_n &\leq 2\% & (i=1, 2, 3, \dots, n) & \quad (4)
 \end{aligned}$$

among them:

ΣQ_i^{im} stands for the total imports of i product, which is the like product of the PM goods in China;

Σdq^{im}_i stands for the increase of the total imports of i product of a certain PME

dQ^{im}_T stands for the increase of the total imports of i product in China

Q^{im}_i stands for the quantity of the imported i product of a certain PME

P^p_i stands for the price of the imported i product of a certain PME

P_n stands for adjusted normal value of the imported i product of a certain PME

From equation (1)—(4) we can easily calculate the PM price and Volume that does not cause any material injury. If the equation changed, the PM should be under the investigation of Anti-dumping. We also need to take a dynamic look, if the volume of PM and the market share are increasing along with the reduction of the PM price continues.

5.3. The effectiveness of an AD

Here we make use of the Nominal and effective tariff method to analyze the effectiveness of AD duty, and the Price undertakings can also be transformed into AD duties.

Assume the price of the product of trade j is X_j , the value added is V_j , and V_j can be calculated by the following equation (before the imposition

of AD duty):

$$V_j = X_j - \sum a_{ij}X_j \quad (5)$$

after the imposition, the price will be $X_j + X_j t_j$ for this trade, then V_j is:

$$\begin{aligned} V_j &= X_j(1-t_j) - \sum a_{ij}(X_i + t_i) \\ &= X_j - \sum a_{ij}X_i \end{aligned} \quad (6)$$

If we assume the ratio of input and production remain the same before and after AD duty, then relationship between t_j' , the real effectiveness of AD duty and, t_j , the nominal duty can be shown in the following:

$$\begin{aligned} t_j' &= \frac{V_j' - V_j}{V_j} = \frac{(X_j' - \sum a_{ij}X_i') - (X_j - \sum a_{ij}X_i)}{X_j' - \sum a_{ij}X_i} \\ &= \frac{t_j - \sum a_{ij}t_i}{X_j' - \sum a_{ij}X_i} \end{aligned} \quad (7) \square \square$$

if $X_j' = 1$,

$$\text{then,} \quad t_j' = \frac{t_j - \sum a_{ij}t_i}{1 - \sum a_{ij}X_i} \quad (8)$$

From (8), we can see the clear relationship between nominal and real effectiveness of the AD duty. To a trade that has little V_j , an increase of the nominal duty brings a bigger increase in the same direction; and the variance of the nominal duty of the input goods that has a bigger the input-production coefficient will cause the effectiveness of the AD duty go to the opposite direction even further. To a trade that has bigger V_j , the situation is just the adverse case.

So if we need to provide protection to the trade injured by the dumping of the MNEs, we can make use of the above method. Thus it will a comparatively certain effect.

6. An analysis of the conflict between PM and AD in the FDI of the MNEs in China from the angle of game theory

In the game, the two parties are the MNEs and the Chinese authorities, the game can be differentiated into two stages, the stage before and after the actual investment. We assume that this is a game of complete information game and the MNEs as the first movers. α stands for MNEs, β stands for Chinese side(Ministry of Commerce)

	α	β	
	invest in China	succeed in attract FDI in China	
	invest in a third country	fail to attract FDI in China	

In the first stage of the

game, the action set and payoff of α and β are the following:

α	β
Profit and development(3)	Growth and development(1.5)
invest in a third country(1.2)	fail to attract FDI in China(0)

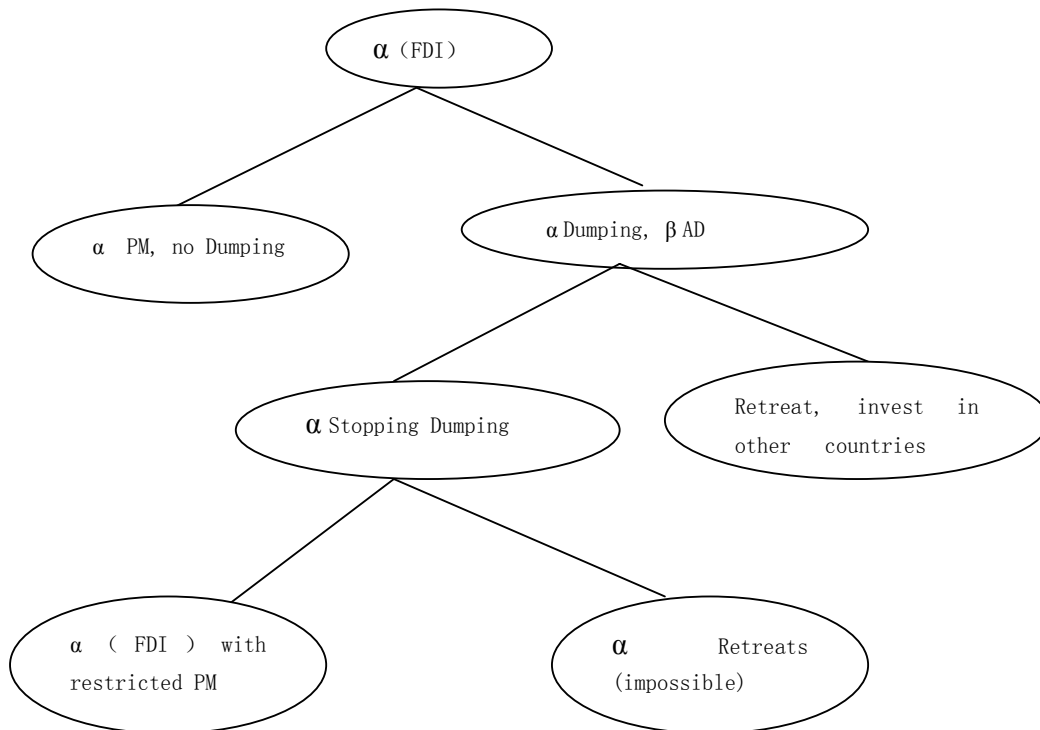
Action set:

Payoffs:

The above payoffs are based on the general analysis of the investment

environment of China, thus it is the common information. And in this round of negotiation, β is always to grant α , the super-national treatment, here it is the unrestricted Pre-marketing (PM) (no restriction to the quantity and price). So the equilibrium of this cooperatives game can reach is (3, 1.5).

In the second stage of the sequential game, we use the game tree to show it:



In this game stage, if there is a restriction to the quantity and price of the PM goods, the PM will not become dumping, but it isn't the case. So the reality is it does dump to China by PM, we just take the dumping confirmation process a black box, that is to say we assume the PM is confirmed to be dumping in China. Then whether AD will cause the FDI

divert its direction of investment? That depends what role of PM in the FDI.

As we discussed earlier in this paper, FDI is a strategic option of the MNEs, PM is just a tactics of realizing the profit in a short time (before the MNE produce the like product in China), so we amend the game in the first stage.

If China take the AD measure, then the payoff of the MNE is $3-\gamma$ (γ is the AD duty):

α	β
Profit and development($3-\gamma$)	Growth and development($1.5+\gamma$)
invest in a third country(1.2)	fail to attract FDI in China(0)

Then what matters is how much is γ ? One comparison should be made between γ and the already paid investment c and the whole gainings of the MNE. That is:

If there is $3-\gamma-c > 0$, the MNE will not be affected in continuing its investment although there is an AD duty; if there is $3-\gamma-c < 0$, the MNE will be affected in continuing its investment when there is an AD duty, especially when c is almost 0; that means γ is too great that it guards off the FDI. According to the common information about China's policies, it isn't the case.

As shown in the game tree, the only equilibrium in the game is $(3-\gamma, 1.5-\gamma)$, $(1.5-\gamma)$ is the payoff that china has is the adjusted gain, and $(3-\gamma)$ is that MNEs should pay for the FDI.

7. Conclusion

By the above analysis, we can see the essence of the PM is a tactics in the MNEs FDI strategy, We finally, found out that the Pre-marketing compliant is in essence a contemporary way of the multinational corporations enlarging the its interests under a changed condition of China's anti-dumping measures; and we also find ways of guarding the domestic enterprises from this dumping. AD is the way to correct the absence of the restrictions to the quantity and Price of the PM in the investment contract. It will not affect the investment of the MNEs if we can sustain a promising growth in the future or at least the investors can expect the trend will continue, which we take this precondition as a presumption. So what is more attractive to the MNEs is the prosperous Chinese economy and the immense market demand.

Thus the government needs to take practical action to foster the realization of the goal of both China and the MNEs. According to WTO regulations, China should improve its market system by amending the legal system, such as integrating the laws of investment, trade, and anti-dumping, anti-trust and countervailing. Especially, the absence of the anti-trust law is the most urgent.

In dealing with the PM related dumping, in order to get an accurate assessment of the AD duty, we can integrate the minimum control of the

imports of the AD with the growth of the market, and the increase of the imports. And we need to make use of the effectiveness of the AD duty so as to keep the side effect to the FDI to the minimum degree. In order to avoid this dispute, we should contain this information in the investment contract. As contract perfected, this kinds of disputes can be largely reduced.

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