

Policy Briefing

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These include the stricter regulations on intellectual property protection both in China and across the world, the trade war between China and the USA which has led to a heightened tariff on goods and so a knock-on cost for traders, and the COVID-19 pandemic which led to a loss in production capability prior to March 2020 due to China's initial lockdown and a loss of subsequent orders following lockdown outside China.

This briefing is based on over 200 interviews conducted with entrepreneurs, policy makers, Chinese diaspora, foreign traders, think tank researchers and consultants based in China, USA, UAE, Hungary, Brazil, Indonesia, UK and Spain between 2016 and 2019, as well as a large amount of secondary data from books, government documents, media and other sources.

Briefing 4: Leveraging trade for development: policy implications from the Yiwu experience

INTRODUCTION

Yiwu's economic development through trade over the past four decades has been described as a miracle¹, yet the city is currently facing unprecedented political and economic challenges. Is Yiwu's continued growth sustainable? Can Yiwu's development experience be replicated in other cities or countries? This briefing addresses these questions and highlights the policy implications that need to be addressed to achieve positive outcomes.

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¹ e.g. Rui, 2018; State Council 2014; Chen 2011; Wang 2009; Lu et al. 2014

LEVERAGING TRADE FOR DEVELOPMENT: POLICY IMPLICATIONS FROM THE YIWU EXPERIENCE

International trade has long been recognised as the engine for development² for its ability to broaden markets and promote investment, productivity, division of labour and specialization, and the efficient use of resources and welfare. Numerous factors have been found to be important to leverage trade for development, including trade-related infrastructure³, trade facilitation and the improvement of rules and procedures that govern trade⁴ and state–business relations⁵. However, extant research still lacks details about the interaction of these factors and how they work together to promote development. This policy brief firstly shows the specific factors that leveraged Yiwu's trade into development, and then proposes policy implications and recommendations accordingly. After that it will summarize the interaction of these factors and highlight overall policy implications for Yiwu and elsewhere regarding how to promote trade to development.

Risk-taking and innovative entrepreneurs are the key factor

An entrepreneur is willing and able to convert a new idea or invention into a successful innovation. Entrepreneurship employs 'the gale of creative destruction' to replace, in whole or in part, inferior offerings across markets and industries, simultaneously creating new products and new business models⁶. Yiwu's entrepreneurs were extremely risk-taking and capable of discovering and creating business opportunities, fostering innovation, dealing with institutional voids and overcoming resource deficits⁷. The practice of locals in Yiwu exchanging 'feather for sugar' in which home-made sweets were traded for goods dates back to the 16th century⁸ and continued during the era of planned economy from the 1950s until the 1970s, when local farmers were no longer allowed to trade. During this time, farmers travelled around China in search of potential markets and sold goods wherever there was demand. They became known as *walking traders* in contrast to the *sitting traders* who sat in the market established by Yiwu government in the 1980s. One of these walking traders recalled: "*Despite the illegal status of trading, I still took great risks and found excuses to leave my hometown to trade, because*

otherwise I would not have money to buy food and clothes for my family"⁹. 'Yiwu spirit' is described with 12 Chinese words: '*qin geng hao xue, gang zheng yong wei, cheng xin bao rong*', meaning '*diligent and studious, upright and brave, integrity and tolerance*'¹⁰.

Entrepreneurship requires innovation, including new ways of doing business and products with new features and prices. My findings concur with the existing literature (e.g. Si et al. 2015) that local entrepreneurs are ceaseless in their attempts to test out new ways of doing things, from trading to producing and e-commerce. As a result, constant rapid improvement of products and services won them competitiveness.

POLICY IMPLICATIONS:

Existing policy documents and research in general on Yiwu entrepreneurs mainly focus on their role in Yiwu's early development, i.e. how they took risks to trade when they were not allowed to do so between the 1970s and 1980s, and how their hard work and innovation contributed to Yiwu's success. Minimal research however has been done exploring the other challenges facing them concerning:

- family business management
- the newly emerged yet significant impact of e-business
- the collapse of many businesses due to a failure to control financial risks in irrational business expansion
- stricter regulations on intellectual property protection
- the rising costs of labour and products across China
- the trade war between China and the USA which led to raised tariffs and a direct increased cost for traders
- the COVID-19 pandemic which has led to lost production capability since before March 2020 due to China's own lockdown and the loss of subsequent orders resulting from lockdowns outside China

² e.g. Adam Smith in 1776 and David Ricardo in 1817

³ Calli and te Velde, 2011; Duval and Utoktham, 2011

⁴ OECD, 2012; Portugal-Perez and Wilson, 2011

⁵ Ash, 2011; Rugwabiza, 2011

⁶ Schumpeter 1942

⁷ Hirschman 1958; Acs 2006

⁸ Chen 2011

⁹ Liu and Yao 2014

¹⁰ Chen 2011

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POLICY RECOMMENDATION:

New policies are urgently needed to guide and facilitate local entrepreneurs to deal with these challenges.

Overseas Chinese traders are heroes behind the scenes

Local merchants alone could not have transformed Yiwu from a domestic trading city into an international hub for the small commodity trade if no foreign traders were importing goods from them. Foreign traders, and especially overseas Chinese traders, have been identified as the “heroes” of this transformation. The overseas Chinese diaspora, numbering over 30 million and living in over 136 countries/areas, are now the most widespread ethnic group in the world. Holding assets of several trillion US dollars, they contribute significantly to regional, national and international development. Between 1979 and 1995, for example, investment by overseas Chinese traders accounted for 80% of the total foreign direct investment (FDI) in China, making it ‘the world’s factory’¹¹. My research has discovered the significant connection between the Chinese diaspora, network and development in home and host countries. Through my research I have identified that the Chinese diaspora not only source goods from Yiwu, but also operate factories around China, apply technologies developed in their host

countries to China’s business practice (or vice versa), and penetrate European and US markets by establishing and managing global supply chains which connect Yiwu with the world.

POLICY IMPLICATIONS:

There is little research and understanding at a micro-level regarding how individual members of the Chinese diaspora connect Yiwu to the world and how they, as a whole, contribute to the economy, society and culture of Yiwu, China and host countries. The function and value of the overseas Chinese population has not been properly assessed. Chinese government at all levels has not adopted concrete measures to exploit the huge financial and intelligent resources owned by the overseas Chinese. Meanwhile, overseas Chinese traders face various challenges when they source or produce goods in Yiwu and more widely in China, ranging from obtaining visas, finding appropriate education for their children to financial controls on bank transfers.

POLICY RECOMMENDATION:

There is an urgent need to have a systematic evaluation of the contribution of overseas Chinese diaspora towards Yiwu and set up a comprehensive strategy to utilise the diaspora to maintain Yiwu’s sustainable development.

A risk-taking and supportive local government has ensured a “bottom up” Yiwu model

Archival data presented in the museum inside Yiwu’s Futian Market shows that the original certificates issued by township and municipal governments in Yiwu were dated back to the early 1970s, long before the nation’s economic reform started in 1978. “*This was unique as governments in neighbouring counties or the entire China did not approve trading*”.¹² On 4 Dec 1982, a file from the Yiwu County Government (No. 172) granted the ‘Four permissions’ which officially allowed farmers to trade which was ‘ahead of the central government policy’ at the time¹³.

¹¹ Huang and Khanna, 2003: 81

¹² CCTV 2009

¹³ Liu et al. 2015, 126

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Managing trade required a capable and supportive local government. In 1992, Yiwu Municipal Government implemented a massive and pioneering reform which categorized commodity location in the Futian Market. This reform saved customers significant time in searching for goods and ensured that the price of goods in the same category were relatively transparent. This gave a competitive advantage to Yiwu Market, compared with other Chinese markets which hadn't adopted such practices.

Local government was praised for implementing a 'reasonable' and 'friendly' tax policy, i.e. "not too high or too low"¹⁴ which contributed to a lower price for Yiwu goods, improved local merchants' profit making and consequent market prosperity. Likewise, Zhejiang provincial government was praised for being "very reasonable and cautious in guiding the market and did not intervene in the market excessively".

Another competitive advantage for Yiwu¹⁵ came in 2011 when Yiwu was nominated by the State Development Reform Commission (SDRC) as 'the pilot city for comprehensive international trade' and in 2013 it was exclusively granted a special tax claim code by China's Custom Authority for its traded goods. This code simplified the previously complicated procedure required to export goods. For example, many different types of goods could now be placed together in a single container which hadn't been the case previously. This speeded up the process and kept costs down.

Since then this new system has significantly sped up custom claiming, enhanced quality control of goods¹⁶.

POLICY IMPLICATIONS:

Yiwu's development was widely termed by Chinese informants as a "bottom up model". The Municipal government's risk-taking, creative policies, especially before 2000, and the principle of "leaving wealth with the people", which is still the case until today, are considered vital in ensuring Yiwu's initial trade development and continued success. However, there is a consensus among local informants that local governments are now less inclined to be risk-taking, supportive or creative which threatens Yiwu's sustainable development. For example, industrialization in China has resulted in the rising cost and relocation of manufacturing, which is "particularly disadvantageous to Yiwu because Yiwu's goods are based on negligible margins"¹⁷. The Municipal Government encourages

local merchants to upgrade their products regularly which is a positive step. However, there are no compatible policies available to merchants that deal with the challenges of recruiting suitable talent, shifting away from lower-cost customers, and transforming from imitation to innovation. Another example is the internationalization of Yiwu's commerce which, historically, was 'very limited' despite about 60 percent of its goods being exported. Governments at all levels have no accurate information on the final destinations of Yiwu exported goods and the extent of foreign investment made by Yiwu merchants. Shang Cheng Group, the state-owned company managing Yiwu Market, has dispatched personnel to visit markets in host countries aiming to facilitate Yiwu goods being sold on online platforms through those countries. This strategy has been criticised as being too little, too late.

The latest move by the Municipal Government has been to sign an agreement with Alibaba, the largest online business group in China, to form a partnership promoting Yiwu goods to international markets. This has caused considerable concern among merchants and officials fearing that Yiwu would potentially lose the competitive advantage it had previously held through the use of its unique tax claim code. The code, granted by the Municipal Government, had benefitted Yiwu exclusively and made trade very cost effective (explained in more detail on p.5). While Alibaba would benefit from that advantage, Yiwu's sustainable development would be of less concern to Alibaba as the city would be seen as a minor player in the company's global business.

POLICY RECOMMENDATION:

Governments at all levels are urged to conduct forward-looking research and make comprehensive strategies and policies ensuring Yiwu's future prosperity.

¹⁴ Interview, 7 Aug 2017

¹⁵ Interview, 9 September 2019

¹⁶ Interview, 6 April 2017

¹⁷ Interview, 6 April 2017

Truly inclusive trade has made Yiwu unique and sustainable

It is a widely held belief in Yiwu that *“Finding and focusing on its correct position made Yiwu’s success”*¹⁸ and this position is trade. Since China began its reform in 1978, three major rural industrialization and regional development models have emerged:

- the Wenzhou model
- the Pearl River model
- the Sunan [South East China] model

Yiwu has benefited from the ‘Wenzhou model’ which was founded on ‘specialized markets and rural industrialization’. However, Yiwu continued to focus on the original market model whilst Wenzhou turned to light industry and even heavy industry. While it is not yet clear which model is more effective, it is worth considering the fact is that Yiwu continues to grow steadily whereas Wenzhou’s growth has declined considerably.

Moreover, what Yiwu has been focusing on is not just trade, but inclusive trade. In 1982 local people including women, the unemployed and young people were given municipal-issued certificates which enabled them to trade inside a market established by the local government at the beginning of 1980s. Notably the majority of merchants in Yiwu Market are women. The goods they trade within the market benefit mainly lower income customers across the globe due to their competitive pricing. This affordability is the major reason that both the United Nations and Walmart are, amongst others, procuring goods from Yiwu.

POLICY IMPLICATIONS:

Many Yiwu people are wondering what the “correct” position should be for Yiwu’s future. They face daily questions including whether they should shift away from imitating other products’ technology or image to self-innovation, hire professionals to help them avoid potential accusations of violating IPR, establish a dedicated e-business department or invest in international markets. Crucially, the answers to these questions are all related to Yiwu’s overall development strategy. For example, one CEO is considering whether to completely alter his business model because

he predicts that Yiwu will be positioned as a global logistics centre rather than a trade centre. Governments have the responsibility to position Yiwu correctly to ensure a successful future for both the city and those invested in its trading networks.

POLICY RECOMMENDATION:

Yiwu’s future position in global trade needs to be explored as a collective effort by all levels of governments, local and overseas traders, researchers and supply chain firms.

The Yiwu experience and overall policy implications

My research indicates that Yiwu’s development was the optimal result of the interaction of many factors. Initially extreme poverty drove local entrepreneurs to trade, and it was entrepreneurs’ hard work, ability to risk-take and wisdom that promoted trade into development.

*“Yiwu people were not satisfied by the status quo – poverty – so they were determined to change that status. However, they were more wise than brave. They searched tirelessly and eventually discovered a development model suitable for Yiwu”*¹⁹.



Amin Azfar / Shutterstock.com

¹⁸ Interview, 2016

¹⁹ Interview, 6 April 2017

These entrepreneurs were facilitated by a helpful local government which provided innovative ways to support them. “Yiwu’s unique factor is that the Market has never been privatized. It has always been in the hands of the local government. At the same time, the local government is wise. It did not excessively control nor lose control of the Market. Jinjiang in Fujian, Hanzhengjie in Wuhan and other specialized markets were largely privatized and controlled by one or a few individuals. Pursuing maximum profit and minimum social responsibility was the consequence. Somehow Wenzhou also lacked the wise government possessed by Yiwu. In Yiwu, the government controls the market through implementing policies to improve the quality of goods and service of trading ... to ensure the best service with lower cost”²⁰.

Furthermore, Yiwu’s successful trading business would be impossible without the support of the nationwide industrialisation in China, which supplies the most diverse and competitive products for trading. Yiwu started trading without its own industry, and gradually established small firms to support trading. However, it was the numerous factories and businesses in the entire nation that ensured the insatiable supply of goods and services.

POLICY RECOMMENDATION:

In the short term, immediate government policies could be issued to motivate entrepreneurs, foreign traders and especially the overseas Chinese, and all related service providers to promote trade. In the long term, more forward looking and comprehensive policies need to be in place to promote industrialisation, inclusive trade and even Belt and Road Initiatives.

They first need to assess whether they can meet the following conditions conducive to growth:

- a significant number of local entrepreneurs
- a supportive institutional environment
- a history of industry in the area

Many African and Afghan traders connected to Yiwu Market are already entrepreneurs, who source goods from Yiwu and can bring significant changes to their local community as well as global markets. However, they may face great difficulty in expanding their business, or transforming from trade to industry, due to a lack of funding, infrastructure, technology, raw materials or appropriate machinery, and more crucially, the industrialisation of their home country.

Conclusion

The United Nations is keen to promote trade for development and emphasises *inclusive trade* by which it means **trade aiming for inclusive and sustainable economic growth**. Various conditions need to be met to enable potential traders in developing countries. However, the strategy so far has not been very effective. Yiwu’s experience shows that a supportive institutional environment for trade should be almost “*regulation free*” to achieve results. In the early stages of a region or country’s development, the priority should be to “*make a larger pizza*”. In the latter stages of development, governments need to step in to ensure “*the pizza is shared fairly*”.

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FURTHER INFORMATION AND RESOURCES

For more information about the TRODITIES project and the Sussex Asia Centre:

<http://www.sussex.ac.uk/global/research/researchprojects/yiwu>

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²⁰ Interview, 6 April 2017