A STUDY OF THE ATTRACTIVENESS INDEX OF CHINA (SHANGHAI) FREE TRADE ZONE

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Introduction

In past few decades, China had reinforced its economy by its low labor cost and low Renminbi currency value. With elapse of time, China has been under a lot of pressure, such as the decreasing economic growth, declining export value, and the increasing RMB value as well as the signing of free trade agreements between neighbor countries (Lee, 2013). Consequently, China has established the China (Shanghai) Free Trade Pilot Zone to solve these dilemmas.

Free trade zones (FTZs; also known as commercial free zones) are fenced-in, duty-free areas, offering warehousing, storage, and distribution facilities for trade, transshipment, and re-export operations (World Bank, 2008). China (Shanghai) Pilot Free Trade Zone (SFTZ) includes seven sub-zones. Differing from just focusing on the favorable tax conditions, there are four new practices implemented in the Shanghai FTZ which are listed as follows: “creating an innovative system of investment management”, “reforming the financial system”, “making trade free to the public”, as well as “transformation of government's economic function”.

However, it’s worth noting that the operation of SFTZ would be suspended if its performance is under the Chinese government’s expectation. As a result, how to attract different enterprises to move into SFTZ and understand the key attractive factors of SFTZ to further support the development of Shanghai Free Trade Zone are both critical issues for the Chinese government.

This study mainly aims at investigating the attractiveness index from enterprises’ viewpoints by firstly reviewing literatures and then surveying enterprises that have already set up their operation offices in SFTZ and the potential SFTZ users. Finally, this study employs IPA technique to analyze critical factors which can then be defined as the SFTZ attractiveness indices.

Literature Review

The spirit of most Free Trade Zones is to operate “within national territory but outside customs territory”. Cargoes are generally allowed to be imported, exported, stored, packed, sorted and processed without being restricted to traditional customs procedures. Besides preferential tariffs, enterprises operate in the free economic zone have also enjoyed preferential policies in various aspects, such as taxation, land use, and the employment of workers, etc. Although free economic zone is not set up outside of the national customs territory, almost all of the economic activities are allowed to exist without tariff charge or custom duty (World Bank, 2008).

In terms of attractiveness, Mortensen’s (2012) research shows that attractions between buyers and sellers are effected by value, trust, commitment, satisfaction on services, privileges, and dependency. As for suppliers, financial, economic, performance management, science and technology, company culture, strategic factors will influence their attractiveness (Olsen & Ellram, 1997). Chandler and Hanks (1994) considered performance of new investment and market attractiveness are relevant to resource-based capabilities. Resource-based capabilities are highly related to enterprises’ future competitive strategies. Performances of investments affect the allocation of competitive strategies and resource-based capabilities. Privatization on port operation, degrees of port congestion, leverage production, the size of ships…etc. will affect shippers’ decision on choosing the port to unload cargo (Steven & Corsi, 2012).

Pantelidis & Nikolopoulos (2008) found the factors that impact Greece and other country to attract foreign direct investment (FDI) are general macroeconomic conditions of local market, political environment and governance, labor, energy, taxes or incentives, infrastructure for transport and telecommunications, and research and development expenditures. Economic activities, opportunities for real estate investment, the depth and intelligence of capital markets, investment protection and legal

structure, the burden of administrative supervision and restrictions on government management, culture of the society and political environment will affect the attractiveness of the investment in general real estate invest (Karsten et al., 2011). UNCTAD (1997) mentioned in the 2001 World Investment Report that growth market, scale of the local market and political stability…etc. will be the main factors for enterprises to consider investing. It's worth noticing that country risk is considered as a first concern when it comes to international investing (Solnik, 1999). International Labor Organization (ILO, 1998)'s research report shows that governments can attract manufacturers to invest in EPZ by financial incentives, infrastructures, and lower labor cost. Labor regulations will also impact the decision of international trading location (Kerstin, 2002).

Through scale of market, wages, education level, industrialization level…etc., the investing environment of each province in China can be examined (Xin & Ni, 1995). Huang (2001) conducted a survey of 600 Taiwanese companies that have invested in Central China and South China. Among 125 samples collected, lower labor cost, cheaper rent, local premium terms, and policy are the main reasons for Taiwanese enterprises to invest in China. Based on the oversea investing theory, Yang (2003) created an SEM model from the aspect of manufacturers to investigate factors influence enterprises to invest in the FTZ. Political stability, premium terms, efficiency of local government's administrating, labor cost and energy cost are the top five factors the enterprises valued most.

After summarizing relevant literatures of the Free Trade Zone, it was found that the functions of the free trade zone were no longer limited to loosen merely tax restriction, but the restrictions on investment, finance and transportation. Despite the considerable benefits generated to the country or region during the establishing of a free trade zone, it may also incur certain risks when setting up a free trade zone and providing relevant preferential tariff break and tax cut.

Setting up FTZ will reduce production cost and trading cost for manufactures, effectively boost the international flows by allocating global resources and production elements, increase consumers' welfare, replace bilateral and multilateral trade, gain local or national employment opportunities, and enhance regional economic diversity. Besides, there may be problems such as excessive trade, excessive consumption, deindustrialization, conflicts on capital and financial openness, destructive competition among enterprises in FTZ, waste of resource and clash against urban planning (Lu, 2014).

Via integrating literatures of attractive factors for enterprise, it could be divided into seven aspects and 27 factors. (See Table 1)

Important-Performance Analysis

Importance-Performance Analysis (IPA) was firstly proposed by Martilla and James (1997) which analyzes the degree of importance and degree of performance of each factor and each alternative from the customer's viewpoint. The pivotal point of the two-dimensional matrix is represented by the average degree of importance and average degree of performance to develop the matrix into four quadrants. Thereafter, enterprises can develop their marketing strategies to enhance their own competitiveness according to the location of the factors in the matrix.

The purpose of this study is to investigate whether there is a gap between the degree of importance and the degree of performance on each of the attractiveness indices perceived by the respondents. Afterwards, IPA analysis is applied to find out the indices with high degree of importance and low degree of performance to be improved in the Shanghai Free Trade Zone.

In this study, the average degree of importance and average degree of satisfaction will be the pivot of the matrix. Axis X is defined as the degree of importance, and axis Y is defined as the degree of satisfaction (see Figure 1). By means of sorting the factors, the importance and satisfaction of enterprises can be explored on the attractive factors of the Shanghai Free Trade Zone as well as can we understand the differences.

Aspect	Factor	Supporting Literatures
Political Status	Political Environment	Karsten et al.(2011)
	Political Stability	UNCTAD(1997)
	Governance	Pantelidis & Nikolopoulos(2008)
	Country Risk	Solnik(1999)
Corporate Strategy	Competitive Strategy	Chandler & Hanks(1994)
	Investment Strategy	Chandler & Hanks(1994)
	Performance Management	Olsen & Ellram(1997)
Soft Power	Value	Mortensen(2012)
	Commitment	Mortensen(2012)
	Privileges	Mortensen(2012)
	Satisfaction on Services	Mortensen(2012)
	Information System Integration and Resources	Chandler & Hanks(1994)
Physical Facility	The Size of Hinterland	Huang(2001)
	Geographical Location	ILO(1998)
	Availability of Infrastructures	ILO(1998)
	Transportation and Distribution Capability	Pantelidis & Nikolopoulos(2008)
Human Resource	Labor Regulation	Kerstin(2002)
Managerial Policy	Availability of Resources	Pantelidis & Nikolopoulos(2008)
	Local Premium Terms	Pantelidis & Nikolopoulos(2008)
	Budget on Innovating	Pantelidis & Nikolopoulos(2008)
	Privatization on Operation	Steven & Corsi(2012)
	Amicable Investing Regulations	Karsten et al.(2011)
	Efficiency of Government's Administrating	Yang(2003)
Current Market Situation	Scale of Market	UNTCAD(1997)
	The Depth and Width of Local Market	Karsten et al.(2011)
	Local Economic Activity	Karsten et al.(2011)
	Degree of Industrialization	Xin & Ni (1995)

Table 1 Literatures of Attractiveness Factors for Enterprises

The study started on April 13, 2015, and ended on May 15, 2015. The questionnaire has aimed at the enterprises in the Free Trade Zone and the potential enterprises in the Shanghai Free Trade Zone. 400 questionnaires were issued, and a total of 138 questionnaires were collected. The incomplete

questionnaires were excluded from the analysis, and 129 valid questionnaires were included in this research analysis. The overall effective questionnaire response rate is 32.25%.

Industrial Classification	Numbers of participate enterprise	Ratio
Real Estate Industry	1	0.78%
Public Administration and National Defense	7	5.43%
Supportive Service Industry	2	1.55%
Wholesalers and Retailers	6	4.65%
Other Service Industry	4	3.10%
Finance and Insurance	9	6.98%
Professional, Scientific, and Technical Service	9	6.98%
Educational Service	1	0.78%
Information and Communication Industry	1	0.78%
Agriculture, Forestry, Fishery and Husbandry	4	3.10%
Transportation and Warehousing	64	49.61%
Manufacturer	21	16.28%

Table 2. Questionnaire Respondent's Basic Information

Introduction of IPA Matrix

IPA Matrix contains four quadrants which classifies 27 factors from Table 1 into four Quadrants.

Quadrant I (High Importance/High Performance): Keep up the good work. Attributes fall into this quadrant are the strength and pillar of the enterprises, and they should try to maintain or improve the status in case other competitor step in.

Quadrant II (Low Importance/High Performance): Possible Overkill. It denotes attributes that are overly emphasized by the enterprises; therefore, enterprises should reflect on these attributes, instead of continuing to focus in this quadrant, they should allocate more resources to deal with attributes that reside in this quadrant.

Quadrant III (Low Importance/Low Performance): Low Priority. Any of the attributes that fall into this quadrant are not important and pose no threat to the enterprises.

Quadrant IV (High Importance/Low Performance): Concentrate Here. Attributes that fall into this quadrant represent key areas that need to be improved with top priority.

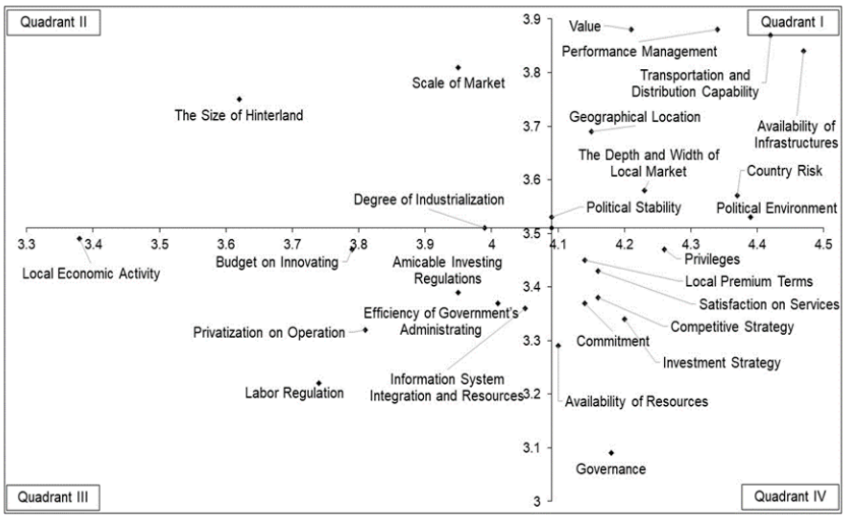

Figure 1. IPA Matrix

No.	**Factors**	**Importance**	**Satisfaction**	**IPA Matrix**
A1	Political Environment	4.39	3.53	Quadrant: I
A2	Political Stability	4.09	3.53	Quadrant: I
A3	Governance	4.18	3.09	Quadrant: IV
A4	Country Risk	4.37	3.57	Quadrant: I
B1	Competitive Strategy	4.16	3.38	Quadrant: IV
B2	Investment Strategy	4.20	3.34	Quadrant: IV
B4	Performance Management	4.34	3.88	Quadrant: I
C1	Value	4.21	3.88	Quadrant: I
C3	Commitment	4.14	3.37	Quadrant: IV
C4	Privileges	4.26	3.47	Quadrant: IV
C5	Satisfaction on Services	4.16	3.43	Quadrant: IV
C7	Information System Integration and Resources	4.05	3.36	Quadrant: III
D1	The Size of Hinterland	3.62	3.75	Quadrant: II
D2	Geographical Location	4.15	3.69	Quadrant: I
D3	Availability of Infrastructures	4.47	3.84	Quadrant: I
D6	Transportation and Distribution Capability	4.42	3.87	Quadrant: I
E1	Labor Regulation	3.74	3.22	Quadrant: III
F1	Availability of Resources	4.10	3.29	Quadrant: IV
F2	Local Premium Terms	4.14	3.45	Quadrant: IV
F3	Budget on Innovating	3.79	3.47	Quadrant: III
F4	Privatization on Operation	3.81	3.32	Quadrant: III
F5	Amicable Investing Regulations	3.95	3.39	Quadrant: III
F6	Efficiency of Government's Administrating	4.01	3.37	Quadrant: III
G1	Scale of Market	3.95	3.81	Quadrant: II
G2	The Depth and Width of Local Market	4.23	3.58	Quadrant: I
G3	Local Economic Activity	3.38	3.49	Quadrant: III
G4	Degree of Industrialization	3.99	3.51	Quadrant: III
	Average	**4.09**	**3.51**	

Table 3. The Importance and Satisfaction Figures to 27 Attractiveness Factors
Note: The overall average degree of satisfaction of the abovementioned factors is 4.09 and the overall degree of perceived importance of these factors is 3.51.

From Figure 1. we can see that "Political Environment", "Political Stability", "Country Risk", "Performance Management", "Value", "Geographical Location", "Availability of Infrastructures", "Transportation and Distribution Capability", and "The Depth and Width of Local Market" factors are situated in quadrant I. It means that enterprises were very satisfied with these important attractiveness factors.

Since "The Size of Hinterland" and "Scale of Market" are factors of low importance and high satisfaction of the enterprises, it is not necessary for Shanghai Free Trade Zone to make excessive invest in this quadrant.

From enterprises' viewpoint, "Information System Integration and Resources", "Labor Regulation", "Budget on Innovating", "Privatization on Operation", "Amicable Investing Regulations",

“Efficiency of Government Administrating”, “Local Economic Activity” and “Degree of Industrialization” factors can be defined as satisfying and have no threat for enterprises.

However, “Governance”, “Competitive Strategy”, “Investment Strategy”, “Commitment”, “Privileges”, “Satisfaction on Services”, “Availability of Resources” and “Local Premium Terms” are the factors located in the quadrant IV which should be strongly emphasized but were not satisfied from enterprises’ viewpoints. This indicates that SFTZ should make an improvement for these factors.

Attractiveness Factors Analysis

First of all, the driving factor for enterprises to invest in Shanghai Free Trade Zone is the consideration of the international market strategy. Due to rapid rise of China's economy in recent years, China has gradually become an economic leader in the Asia-Pacific region. Shanghai's position in the Asia-Pacific region has turned step by step into the economic center of the Asia-Pacific region. Therefore, most companies choose to set up international branch even headquarters in Shanghai. The advantages of location in Shanghai is the main attractiveness for most companies to invest in the Asia-Pacific region. Therefore, for enterprises, the amount of Research and Development budget invested by the government, the size of the local market, the local economic activities, and investment in local industrialization are not the main factors of determining the entry for enterprises to the Shanghai Free Trade Zone. It’s worth noting that since the consumption power of the people in Shanghai ranks first place among the provinces in 2016 and the enterprises are satisfied with current market size in Shanghai.

Secondly, the industrial structure in Shanghai has gradually changed from a labor-intensive manufacturing industry into service industry. Therefore, the factors influenced the manufacturers such as the size of land and labor regulations are gradually weakened. Currently, the scope of the Shanghai Free Trade Zone has expanded from 28.78 square kilometers to 120.72 square kilometers. It appeals manufacturers who want more space to accommodate their new investment. By reason of the rise of labor awareness in China, the government has further protected labor rights in accordance with labor regulations. The limitations of labor regulations will cause the advantages of lower production cost to vanish, so enterprises have relatively lower satisfaction with labor regulations factors comparing with the overall general average score.

Thirdly, in order to improve administrative efficiency and anticorruption reform, the Chinese government has actively targeted the development of mixed ownership enterprises and the establishment of information sharing platforms and public credit information service platforms. However, it needs time for state-owned enterprises to transform themselves into mixed ownership enterprises. On the path of organizational restructuring, there must be an adjustment period. In addition, China has actively cracked down on corruption and has been looking forward to monitoring the overall administrative process through the establishment of a regulatory platform and a public credit information service platform. This anti-corruption approach seems to be helpful. However for some enterprises’ do not have ability to follow the implicit rules, this has inevitably hinder enterprises to move in and operate in SFTZ. Even if the degree of importance of the government's administrative efficiency is located in a low-priority area, but it’s importance is near the average degree of the overall importance. This means that the government's administrative efficiency factors will more or less affect the enterprises’ willing to invest in SFTZ.

Fourthly, Shanghai Free Trade Zone has liberalized the FDI scope by using the negative trading list. The advantage of negative trading list provide foreigners a large area of investment opportunity. Reviewing the contents of the negative list, it can be found that Shanghai Free Trade Zone still has restrictions and prohibitions for FDI on certain specific industries, which has not fully opened up for foreign investment. Thus, the performance of the friendly investment regulations in the Shanghai Free Trade Zone has not reached the average degree of satisfaction, and the degree of importance perceived by the responding manufacturers on the negative list is below the average degree of importance. This is because of the potential SFTZ investors have already understood some business scope have to be included in the negative list, which means that their perception on the degree of importance on the negative list factor is relatively low.

Finally, regarding to the information system integration and resource-based factors, due to the exclusive account for cross-border payment and financing functions of the trade has only been launched recently and the promotion on this factor is insufficient, which made the respondents unaware of these services and the degree of their satisfaction on these factors were below average.

Conclusion

This research target is to figure out the attractiveness factors of Shanghai Free Trade Zone. Through reviewing relevant literatures and distributing questionnaires to survey international enterprises, 27 SFTZ attractiveness factors were constructed. This study analyzes enterprises' perception on the factors influencing Shanghai Free Trade Zone's attractiveness via questionnaire survey and IPA technique.

IPA matrix analysis on various industries shows that different industries are basically have the similar perception on the degree of importance and performance of the SFTZ on these 27 factors in this study. For example, the enterprises in transportation and warehousing industry benefited less from the preferential measures introduced by the Shanghai Free Trade Zone, as the result, the degree of importance on the "Local Premium Terms" was lower than that perceived by the other industries.

As for financial industry, it focuses on the preferential measures proposed by the Shanghai Free Trade Zone. Factors such as: "The Size of Hinterland", "Labor Regulations", "Availability of Resources", "Budget on Innovating", and "Information System Integration and Resources" are perceived to have the lower degree of importance when comparing with the other industries.

There are two major contributions achieved from this research. Firstly, multifaceted literatures are reviewed to form Shanghai Free Trade Zone enterprises' attractiveness index. It provides not only a direction for SFTZ's future development as well as indices for FTZ in other countries. In addition, the development of unique enterprises' attractiveness indicators will enable SFTZ regulators a real-time adjustment and improvement opportunities during their starting-up stage.

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