ADDRESS BY SENIOR MINISTER LEE KUAN YEW AT THE EAST ASIAN INSTITUTE'S 5TH ANNIVERSARY, WEDNESDAY, 17 JULY 2002, MANDARIN HOTEL

"CHINA IN TRANSITION"

I am happy to be with you on the 5th anniversary of the East Asian Institute (EAI). In 1983 Dr Goh Keng Swee first established the Institute of East Asian Philosophies (IEAP) to study Confucianism and its value for social cohesion. The institute was later renamed the Institute of East Asian Political Economy (IEAPE) and its focus shifted to political, economic and social developments in an emerging East Asia. As East Asia changed over the last twenty years, the IEAPE matured and evolved into the EAI, set up in 1997 as an autonomous research organisation within the National University of Singapore (NUS).

The EAI's academic and policy-oriented research on East Asia has concentrated on contemporary China. This is because the strong and steady growth of China has the most profound impact on East Asia, indeed on the world.

Transformation of China

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Since my first visit to China in 1976, I have returned regularly. China's transformation during this period has been startling. It is not confined to improvements in its physical and tangible hardware, such as improved infrastructure and communications. More impressive are the changes in the Chinese people – their openness to new ideas, their hunger for progress and their great desire to learn and catch up.

China's development since 1949 can be broadly divided into three periods. First, the Maoist era: Ideologically driven, China was striving for a communist utopia while bent on exporting revolution to the world. They were wasted years. Its reliance on the Soviet model of a command economy denied China the knowledge, capital and technology which it needed for economic and social development. China's share of world GDP declined from 5.8% in 1952 to 5% in 1978 – a dismal performance considering its

vast resources and the relatively low income base that it was starting from. In 1978, about 250 million Chinese lived below the international poverty line. The mass of the Chinese people wore drab dark blue or dark gray ill-fitting unisex Mao jackets. Communist slogans were shouted from loudspeakers in railway stations and public parks and big character slogans were displayed everywhere including wheat and rice fields visible from the roads. This was the China of my first visit in 1976.

1978 marked the beginning of the second era with the launch of Deng Xiaoping's "reform and opening up policy". Deng said in 1979 that China should aim at achieving a "*xiao kang*" (小 康) – translated as modestly comfortable - standard of living by the year 2000. On most counts, China has surpassed its "*xiao kang*" targets. They have had a difficult transition, culminating in the Tiananmen incident of 1989. Despite many setbacks, Deng never lost sight of his broader objectives. His "southern tour" in 1992 injected fresh impetus into his policy, best demonstrated in the development of Shanghai. In 1992, Puxi was a dilapidated old town and Pudong a stretch of farmland. Ten years later, Shanghai has been transformed, poised to become one of the major cities of the world.

Deng's policies, consolidated and built upon by President Jiang Zemin and Premier Zhu Rongji, have set China on a path of phenomenal economic growth. In the 1970s, China was the 11th largest economy in the world. Today, it is 7th. Over the last decade, China has achieved an average growth rate of 10% per annum, and this notwithstanding the Asian financial crisis in 1998 and the recent global economic downturn.

China is now entering the third phase of its transformation. By pushing ahead with WTO membership, the Chinese leadership has signalled its determination to stay the course towards greater openness and integration with the rest of the world. This decision is a strategic one, and not without risks for China. China's WTO membership is estimated to bring a US$800 billion increase in FDI between 2001 and 2010. But it also means that China's reforms are now subject to an externally imposed timetable. This, coupled with leadership transition and a widening economic disparity between the coastal and inland regions, will pose serious domestic challenges for China. But barring major dislocations, Beijing's hosting of the 2008 Olympics is set to be a major coming-of-age party for China as it joins the ranks of the major economies of the 21st century.

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Impact of China on East Asia

A rising China is both a competitor and a partner for the rest of East Asia. It is better that regional countries recognize China's growth as a fact and devote their attention to dealing with it. Besides exploring ways to tap into China's growth, the region must also improve its own competitiveness.

For Japan, South Korea and Taiwan - the industrialised Northeast Asia - China will initially be more of a partner. Its low unit cost of production and abundant supply of cheap and skilled labour makes it an attractive base to relocate industries seeking to remain globally competitive. The relocation of manufacturing industries from Japan, South Korea and Taiwan to China today is similar to Hong Kong's light industries move into China during the 1980s and 1990s.

For Southeast Asia, China will initially be more of a competitor. Of the Foreign Direct Investments that flow into East Asia (excluding Japan), China now receives the lion's share of 50% compared to 20% for the ASEAN countries. This is a reversal of the proportions of the early 1990s. With China's emphasis on investment in human capital and technology catch-up through FDI, China has, within a short span of 10 years, moved from labour-intensive low-end products to high-end capital intensive industries such as semi-conductor foundries.

Nevertheless, as China adapts to the latest technologies, improves its R&D and learns new production techniques, we can expect a reversal of China's role in the region. As it grows, China will be a huge potential market for unfinished goods produced in Southeast Asia. China's burgeoning middle class will translate into more tourists for ASEAN. China's outbound FDI has also been rising gradually in the past few years. Its overseas investments in 2000 amounted to US$551 million, of which US$108 million went to Southeast Asia. This is but a trickle compared to the flow that will come in the course of the next 20 to 30 years.

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Role of EAI

To engage China we need a deep understanding of the country. The EAI does research on the political, economic and social trends in China. The

demand for objective research and analysis on China will increase. The EAI should build up its reputation as an institute that specialises in policy-oriented research on contemporary China and other East Asian economies. I congratulate the EAI on its 5th anniversary and wish it every success.

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