

Management of Free Economic Zones at Different Stages of China's Open Door Policy

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Abstract. The article is dedicated to the study of the features of free economic zones (FEZ) management in the period of the implementation of foreign policy in the PRC in 1978-2016. Based on the analysis of regulatory and legal documents, special scientific and economic literature, 5 stages of state regulation of the national-level FEZ characterized by various management measures for their development were identified. The main criteria for distinguishing these stages were differences in the goals and objectives of the FEZ activity, their total number and management features (in particular, the tax policy pursued). The most important types of Chinese free economic zones are characterized by the time of emergence, location, the specifics of economic orientation, the role and importance in the foreign policy of the country. On the basis of statistical and economic methods, the trends in the outflow and inflow of foreign direct investment in China have been traced correlating with the stages of the FEZ development. The historical features of the use of administrative and economic mechanisms (tax and customs privileges) for the operation of various types of free economic zones are determined. The sectoral and territorial priorities of each stage of the country's foreign policy are identified. It was concluded that the "open door" policy in the PRC actively applied the tool of the FEZ and repeatedly underwent a change of development models to achieve its strategic goals – modernization of the country's economy and bringing it to the world stage.

1. Introduction

The transformation of China from a backward country into a powerful economic power over the past 40 years has often been characterized by the analysts as one of the greatest economic successes of the modern era. Thanks to the "open door" policy started by Deng Xiaoping in 1978 with the goal of restoring, further growing and modernizing the economy of the PRC and integrating the country into global economic relations it became possible. The most important mechanisms for implementing the foreign economic policy of the country were: establishing relations with the foreign countries by joining international economic and political organizations and groups – APEC (1991), G-20 (1999), WTO (2001), SCO (2001 d) and BRIC (2001), expanding scientific and technical cooperation with partner countries, intensifying industrialization by attracting the rural population as labor resources, encouraging cities and urban lifestyles on the basis of state programs of their economic development, etc.

In many respects, this was facilitated by the creation of a complex multi-stage system of the FEZ which became a priority universal tool for stimulating the economic development of the country. The preferential legislation accumulated all the elements of this reform policy in them [15; 16]. The largest inflow of FDI needed for economic transformations passed through the FEZ; they contributed to the

rapid growth of industry, research and development and exports, ensured the import of the latest production technologies and management, equipment and services from abroad and the accessibility of the domestic market to foreigners.

The scientific works of domestic and foreign scientists who made a significant contribution to the study of the features of the reform policy carried out in the PRC [4; 7; 8; 29], and the role of the FEZ in its implementation [10; 11; 13; 22; 28] were the theoretical and methodological basis of this article. The authors also relied on the separate studies on the functioning of different types of Chinese free economic zones and their impact on the development of the country's economy [14; 16; 17; 23; 27]. Particular attention was paid to the specifics of the FEZ management mechanisms and measures to attract FDI to their territory [1; 2; 5; 6; 19; 20; 21].

At present, a new stage of the FEZ development has begun – the transition from the intensification of export-import relations to the smoothing of territorial economic disproportions [3; 30]. Therefore, the study of their development trends and their role in the implementation of the country's economic policy, as well as the specifics of state management measures for their effective functioning when priorities change becomes mainstream.

2. Results

2.1. Types of China's FEZs

In 2016, in the People's Republic of China there were about 250 national-level free economic zones of various types (see Table 1).

Table 1. The main modern types of FEZ.

FEZ types (their number)	Examples of typical SEZs and their location	Main economic activities
Special economic zones (6)	Shenzhen, Zhuhai, Shantou, Xiamen, Hainan, as well as the New Pudong District, Shanghai	diversified industrial and agro-industrial production, tourism
Economic and technological development zones (90)	Beijing, Shanghai, Guangzhou, Tianjin, Dalian, Harbin, Urum-qi, Wuhan, Chongqing, Hang-zhou, Shenyang, Changchun, Yingkou, Qinhuangdao, Beihai, Xiaoshan, Wenzhou, Hefei, Xian, Nachang, etc.	industrial production: electronic communications, automotive industry, food industry, pharmaceuticals
High-Tech Industrial Development Zones (120)	Zhongguancun Technopark (Beijing), Zhangjiang High-Tech Park (Shanghai), Tianjin, Nanjing, Chengdu, Guangzhou, etc.	development of technologies: electronic and informational, bio-technologies and new medical products, new materials and their processing, aerospace, nuclear, marine operations, environmental protection, energy-saving and new energy sources, agricultural
Free trade zones (12)	Tianjin, Dalian, Guangzhou, Ningbo, Zhangjiang, Haikou,	logistics, warehouses, processing and finalization of products

Cross-border economic co-operation zones (14)	Xiamen, Fuzhou, Qingdao, Shantou, Zhuhai, Shenzhen Heihe, Suifenhe, Manzhouli, Erlian, Hunchun, Dandong, Yining, Bole, Tacheng, Pingxiang, Dongxing, Ruili, Wanting, Hekou	agriculture and industry (production of food, electrical and textile goods)
Experimental free trade zones (11)	Cities of central subordination: Shanghai, Tanjin, Chongqing and in the provinces of Guangdong, Fujian, Liaoning, Zhejiang, Henan, Hubei, Sichuan, Shaanxi	various specializations aimed at the development of basic industries and regions in general

Source: Annual Review of the Status and Main Directions of Foreign Economic Activity of the People’s Republic of China in 2016, http://91.206.121.217/TpApi/Upload/1ec16458-cabe-41bc-9873-f4cb5933cc19/obzor_economy_China_2017.pdf, last accessed 2019/04/22; [1]

Special economic zones are the first type of FEZ created in 1980 in the South-East of the country due to the proximity of Hong Kong, Aomen (Macau) and Taiwan Island – the sources of investment huaqiao, ethnic Chinese living outside the PRC [25; 26]. They are diversified, but differ in their economic orientation (Shenzhen is industrial, Shantou is agro-industrial, Xiamen is industrial and tourist, and Zhuhai is predominantly tourist, Hainan is tourist and agro-industrial). Despite the small number, they played an important role in the country's economy: due to their successful functioning in the initial stages of the open door policy, the foundation was laid for the formation and development of other types of FEZ [9; 20]. At the end of 2016, their foreign trade turnover amounted to \$ 537 billion (14.7% of the total in the PRC).

In today’s China, the most important are the zones of high-tech industrial development. About half of them are state-owned, their creation was carried out in accordance with the Torch national scientific and technical program [12]. This type which has been forming since the late 1980s has acquired the greatest value in the last decade. It is represented by technoparks and high-tech parks which are located mainly in the eastern and southern parts of the country where the main universities and research institutes are located, and the infrastructure is developed. An important feature is their narrow specialization which brought them world renown: Zhongguancun Technopark in Beijing (electronic and information technologies, production of biomedical), Zhangjiang high-tech park in the Pudong district, Shanghai (information technologies), Guangzhou (biotechnologies and technologies of new medicals).

The second in importance in the PRC are the economic and technological development zones (ETDZs) organized since 1984 more often in “open” ports when attracting FDI, equipment and advanced technologies for the development of the processing industry for export [2]. According to information of Foreign Economic Information Portal of the Ministry of Economic Development of the Russian Federation, 2016, the main activity lies in the production of electronic communications (over 60%) and the automotive industry (10%), the food industry (7%) and pharmaceuticals (5%). In the total volume of industrial products of this type of SEZ, the proportion of scientific and technical sphere is 55%. Most of them are also concentrated in the east and south of the country due to the huge volumes of export-import operations and the concentration of labor resources [17].

“Open” port cities are located on the coasts of the Yellow, East China and South China Seas. The beginning of their formation is 1984, the goal is to create a modern infrastructure of export-oriented ports, including container and other special terminals [6]. Also, their activities, along with the areas of technical and economic development, are related to the industry the 2/5 of which is for export purposes. The share of their industry in the total industry of the country is about 1/4, they provide 40% of ex-

port supplies and sell almost 100% of the turnover of all seaports. Often, the experts call them technological and economic development zones of a complex type [1].

The creation of free trade zones began in the mid-1980s to boost exports, mainly in the southeast. There are enterprises engaged in processing, improvement and packaging of imported products and semi-finished products for export, as well as the warehouses. Over the entire period of operation, the foreign trade operations of these zones brought the PRC \$ 317 billion. At the same time, the cross-border economic cooperation zones (CBECZs) were actively developed. Their goal is to activate the economy of the border regions of the PRC by expanding the trade relations with neighboring countries – the Russian Federation, the DPRK, Kyrgyzstan, Mongolia, Kazakhstan, Laos, Vietnam and Myanmar. They encourage the production of various industrial and agricultural products for external consumption.

In 2013, the Shanghai first experimental free trade zone was opened which specializes in services (financial, professional, social, cultural) and differs from the other types of FEZs in that attracting FDI is not the main measure of its development. Its functioning is connected with the accumulation of experience of an open economy and the increase of its effectiveness due to the effect of reforms. Attention is focused on testing new ways of regulating trade at the international level, as well as managing the financial sector and investments [23; 24]. Due to its successful experience in 2015, it was decided to create 3 new zones with similar working conditions in the provinces of Guangdong, Fujian and Tianjin, in 2016 – to create another 7 zones with their own specialization. In 2016, the foreign trade turnover of the four first experimental zones amounted to \$ 1.6 trillion (44.4% of the total in the PRC) [11].

To smooth out the disproportions between the western and eastern territories of the country in 2014 the concept of the Silk Road Economic Belt “One Belt, One Road“ was proposed. Its key points in China are 3 special economic development zones – Kashgar, Khorgos in the Xinjiang Uygur Autonomous Region and the international cooperation zone Tumangan (Hunchun) on the border with the RF and the DPRK [27]. Such a geography marks the modern aspect of the formation of FEZ aimed at raising 4 remote regions and their integration into the country’s economy – eastern and western, central and northeast ones. The individual concepts have been developed for each of the zones, for example, Kashgar is associated with the import of energy resources and rare metals, the production of agricultural products and light industry goods.

To analyze the change in the economic priorities of the activities of the Chinese FEZs, let us highlight the main stages of their development and management.

2.2. State regulation of the activity of the FEZ

The legal framework of the FEZ was created only after the government was convinced of their political integrity and the absence of a threat to national security, and only later - the economic benefits of FDI [15; 19]. The development of the FEZ can be traced to 5 main stages, distinguished by their tasks of state regulation, the nature of tax and other benefits, etc. (see Table 2).

Table 2. Stages of the FEZ functioning management.

Stage	Main tasks	Tax policy	Number of FEZ	Priority types of SEZ
I. 1978–1982	Testing the mechanisms of the FEZ activity	Providing significant tax benefits to joint ventures and foreign enterprises on a territorial basis	4	Special FEZs
II. 1983–	Attracting FDI, the development of new	Partial or complete exemption from income tax in high-tech and knowledge-	16	Free trade zones, economic

1989	advanced technologies of production and management; foreign trade activation	intensive engineering industries. Profit tax to foreign enterprises in the FEZ territories - 15%	and technological development zones
III. 1990-2000	Enhancing scientific and technological development and education; development of manufacturing industry; expansion of the commodity structure and the foreign trade volume	Cancellation: VAT and unified commercial and industrial tax to foreign enterprises in the field of high technologies, duty-free imports, income tax for export-oriented enterprises in the innovation sphere (non-payment in the first 5 years and payment of 50% of the base rate from the 6th to the 10th year, exemption from land tax for construction companies) Joint ventures pay taxes on real estate, urban repair and construction; surcharge on education, VAT, income, real estate transactions, vehicles, customs duties, excise taxes.	Technical and economic development zones, High-tech industrial development zones
IV. 2001-2013	The development of high-tech industrial production based on national achievements in science; export of national technologies	The profit tax rate increased from 15% in 2007 to 25% in 2012. Preferential rate of 15% for new and high technologies enterprises; 50% and 75% discount on R & D expenses. For the new and high technologies enterprises created after 2008 inclusive: two-year tax holidays, the next three years - the tax rate is 12.5%	High-tech industrial development zones
V. 2014-present	Smoothing disproportions of spatial development of the economy; stimulating the development of remote backward regions of the country	Special conditions for the SEDZs: five-year tax holidays for enterprises 70% of whose income falls on a number of industries; then a lower profit tax rate (-40%) for 2 years. For EFTZs: termination of actions on a temporary basis of individual articles of the main regulations on the use of foreign capital.	Experimental free trade zones, special economic development zones

Source: Bazhanov, P.: Doing business in China: Legal Aspects. Issue 1: Overview of the legal environment for business. Infotropic-Media, Moscow (2015); Ter-Akopov, S.G.: Special economic zones as an important part of economic growth. Accounting in budget and non-profit organizations 24, 38-43 (2013); Brunschweiler, A.: Introduction to special economic zones in China, illustrated by the Special Economic Development Zones of Horgos and Kashgar (Xinjiang province). Jusletter (16.06.2014),

http://www.lalive.ch/data/publications/Introduction_to_special_economic_zones_in_China.pdf, last accessed 2019/04/22; UNCTAD Homepage, <http://unctadstat.unctad.org/>, last accessed 2019/04/22; Annual review of the status and main directions of foreign economic activity of the People's Republic of China in 2016, http://91.206.121.217/TpApi/Upload/1ec16458-cabe-41bc-9873-f4cb5933cc19/obzor_economy_China_2017.pdf, last accessed 2019/04/22; Taxation and Investment in China 2017. Deloitte, <https://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-chinaguide-2017.pdf>, last accessed 2019/04/22.

The first stage is characterized by the formation of the legal and organizational framework for attracting FDI in the FEZ. The first laws on taxation, labor relations, technology transfer, currency and customs regimes, credit and financial support are adopted. The principles of market regulation and control activities tested at the first special SEZs were then introduced into the economic mechanism of all subsequent types. [18]

Creating a favorable investment climate the government of the People's Republic of China invested significant budget funds in the form of concessional loans from state-owned banks on the terms of repayment (for a period of 7–10 years, 4% per annum). The loans were targeted and were given for specific projects of the FEZ [14]. To successfully attract FDI foreign and joint ventures in the FEZ were exempted from paying taxes or the tax burden could be reduced for them to 12–13% within more than two decades from the beginning of their creation. The taxation was conducted on a territorial basis and only in 2007–2008 the reforms on the unified taxation of the enterprises with the participation of foreign capital and national ones came into force [11].

The implementation of *the second stage* was characterized by the expansion of the country coastal areas openness for investment from abroad. Having improved the legislation China aided by it began to manage the geography and the industry cut of the investments inflow [8]. Thus, the needs of foreign trade transactions began to be provided by open port cities and FCTZs.

In 1982, the list of economic activities most preferred for the infusion of FDI – export-oriented industries aimed at the production of finished industrial products – engineering, clothing and food production was approved [4; 5]. The ETDZs with the production of mass products of labor-intensive industries of manufacturing, R & D, as well as trade and sales were spread. According to information of Foreign Economic Information Portal of the Ministry of Economic Development of the Russian Federation, 2016, about 50% of all products were exported from the areas of technical and economic development to foreign markets. This ensured a high growth rate of the Chinese industry in the mid-1980s, but the expenditures from the state budget for the formation of the FEZ significantly exceeded the FDI [13].

At *the third stage*, the government of the PRC began to gradually orient the FEZ towards self-financing in order to reduce costs from the budget. Their number in this period grew very quickly – by the end of the stage there were more than 180 different types of FEZs, the main role was played by technical and economic development zones, but new and high technologies zones were being already created, by 1998 about 40% of the production of FEZs in the country belonged to the high-tech sector [1]. Since 1988, 53 technoparks were founded in which 65 thousand small and medium-sized innovative enterprises functioned which was one of the main factors of the “economic miracle” of the country.

The state sought to gradually expand the scope of foreign capital infusion extending it to financial insurance, real estate, trade, tourism.

At *the fourth stage*, the new and high technology zones were especially actively developed. Special tax conditions were received by innovative enterprises (see Table 2). According to "Taxation and In-

vestment in China 2017" (Deloitte), these benefits were implemented in 21 cities, as well as in several regions of the country. The attraction of FDI and new technologies has become the main motive for the transformation in the legal regime of the FEZ regulation. The governing bodies of FEZ could edit legal acts and regulations based on the changes in business needs and market conditions. Special attention was paid to technologically-intensive sectors with high added value; in this regard, the policy in the field of FDI was adjusted [17; 29]. Foreign enterprises working in the sphere of high technologies or export-oriented were provided with non-tax benefits in the form of exemption from land tax upon decree of local authorities [13].

The priority of the activity of the FEZ was the training of national personnel, mastering the experience of managing the latest machinery and technology, the transfer of advanced technologies to the internal regions of the country, etc. [7]. The FEZ regime was introduced in the west and north of the country – zones of cross-border economic cooperation developed. The government allowed foreign nationals to obtain land rights in China for the construction of infrastructure facilities. At the end of this stage, the stimulation of national demand begins in connection with which the FEZ focuses on industries oriented towards domestic trade as well.

At the fifth stage, experimental free trade zones and special economic development zones were stimulated in development. Special conditions (see Table 2) apply to the companies from the approved list: electricity and renewable energy, construction, agriculture and forestry, nonferrous metallurgy, transport infrastructure, IT, logistics, education, culture, health care and sports. According to Annual Review of the Status and Main Directions of Foreign Economic Activity of the People's Republic of China in 2016, the benefits are limited to the period until 31.12.2020, the similar conditions are also applied to the high-tech service enterprises in 21 approved cities until 31.12.2018 and in some regions of the country until 31.12.2020.

The government measures are aimed at enhancing business activities in the relatively remote provinces of China, tax breaks are applied on a territorial basis. When carrying out the activities in low-profit industries (for example, agriculture) and in remote regions the joint ventures receive a 15–30% discount of income tax for 10 years after its after full or partial payment for 5 years. For experimental free trade zones, the use of foreign capital in the country is limited on a temporary basis.

Timely adjustment of tasks at each stage of the FEZ formation and changes in the legal and other modes of their management led to differences in the dynamics of FDI in the Chinese economy.

2.3. FDI Dynamics in China Economy

At the first and second stages of creating FEZs in China, the volume of FDI in the country's economy was relatively small compared to the subsequent stages, but their growth over the period reached maximum values – mainly due to the low start effect (see Fig. 1). For 1990–2000 China's GDP has increased 3 times, and FDI has increased 12 times which exceeded the growth rate of the investment outflow from the country. For the first half of the 1990s, 230 billion dollars of foreign capital was attracted (about 20% of all investment flows in developing countries) [8]. At the beginning of the XXI century, China was able to become a leader in actual attraction of FDI in the world.

In 2013, 9 High-tech industrial development zones were opened which determined the entry of China's policy into the global level ("Go Global") which was announced back in 2000 and which markedly reduced administrative barriers to outcoming investments in the form of export of capital, national technologies and accumulated experience [19]. The increase in the share of private property in all spheres of economic zones of the FEZ has led to an increase in the efficiency of their activities and contributed to the expansion of China into the world economy (mainly in African countries), including through the opening of branches of national TNCs.

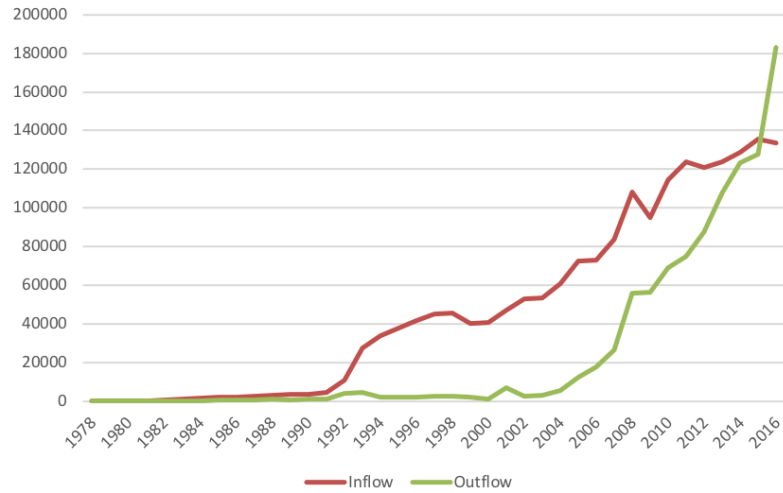


Figure 1. Dynamics of the FDI inflows and outflows volume into the economy of the PRC, 1978–2016, million dollars.

Source: UNCTAD Homepage, <http://unctadstat.unctad.org/>, last accessed 2019/04/22.

Due to the work of FEZ at the third and fourth stages of development, the volume of FDI inflows into the PRC grew almost 3 times, and the outflow – 15 times. By 2014, the FEZs produce about 22% of GDP, attract 46% of FDI, their share in exports is 60%, they created more than 30 million jobs, and the income of the involved peasants increased by 30%. Due to their functioning, industrialization, modernization of agriculture and urbanization in China were accelerated [29].

At the fifth stage, the rapid growth of FDI outflow from the country the volume of which already exceeds the volume of capital inflow is especially pronounced which indicates a decline in the need for China to import machinery, raw materials and materials from abroad due to the organization of its own production in the interior regions.

The most striking example of the development of the country’s cities and the economy as a whole by creating FEZ on the basis of attracting foreign investment is Shenzhen. For three decades, from a fishing village with a population of 30 thousand people it became the fifth largest megalopolis of the PRC (about 12 million people, 2016) characterized by the post-industrial structure of the economy.

This transformation during the reform period was carried out gradually. As long ago as the first year of operation of the zone it attracted 50.6% of all FDIs to the country; the average annual GDP growth rates from 1980 to 1984 accounted for 58% (vs. 10% in the country); by 1986, it had a capital, labor, land, technology, etc. market. [28]. The reasons for success were the close proximity to Hong Kong with the market economic model and the innovative experimental policy of the authorities. By 1992, Shenzhen obtained the right to legislative power having previously become an independent entity within the province of Guangdong. For the first time it gave access to the market to foreign banks, privatized the part of the state enterprises and opened the stock exchange (1990). It started-up the land reform which allowed selling land by auctions.

Having started with the organization of diversified industrial and agro-industrial production the city subsequently became a financial and transportation center, developed tourism, science, education and high-tech industry. It is one of the largest centers of fine chemicals, electronics and electrical engineering (for example, most iPhones and iPads are made here) and contributes greatly to the development of China in the field of high technologies. In 2008, Shenzhen was in first place in the country in terms of the number of registered patents (2,480), ranked third in attracting foreign capital; the headquarters of world famous companies are located there [28].

3. Conclusions

As the objectives of each stage of the FEZ formation were achieved, the necessary adjustment of their state regulation was carried out. If at the initial stages the inflow of FDI and privileges of export-oriented joint ventures and foreign enterprises were stimulated the measures in FEZ management were taken at the latter one to enhance entrepreneurship among the local population and ensure the export of national technologies from the country.

In connection with the policy of modernizing the country's economy technical and economic development and new and high technology zones (over 80% of the total) were most prevalent in China. A special role is also played by the latest by time of emergence free economic zones – experimental free trade zones and special economic development zones which reflect changes in the modern economic policy of the country.

Managing the FEZ development depended on their location. Spatially, the first FEZs were organized in the more developed coastal regions of the PRC which provided good opportunities for foreign relations. Over time, their distribution vector changed from the south-east to the less developed north-west which is related to the pattern of transport routes, power supply lines, the natural resource base and settlement. Their deployment has become associated with a fundamentally new vision of the goal of their creation aimed at smoothing the territorial differences in the country's economy. [3] Thus, from a tool of foreign economic policy FEZs are transformed into an instrument of spatial economy development.

The analysis of the FEZ creating experience in the PRC makes it possible to argue that a well-built long-term strategy for the development of a country's foreign policy by means of a FEZ tool had a positive result. The gradual emergence of new types of FEZs and the increase in their number ensured the mass production of export-oriented competitive products, the development of the economy along the innovative path. As long ago as 2013, China came out on top in the world in terms of the volume of foreign trade turnover (however, in 2016 ceding the leadership to the USA – \$ 3.7 trillion), and in terms of GDP at PPP – In 2014, retaining primacy in 2017 (\$ 23.1 trillion) as to information of World Trade Statistical Review, 2017 (WTO) and The World Factbook, 2017 (CIA).

Despite the significant differences between the Chinese zones and the Russian ones (by the objectives, their existence time, the main types, the number and scale of their contribution to the economy, etc.), for the Russian Federation a number of aspects of the PRC experience in their organization seem significant. In particular, it is: a long-term strategy when changing tasks for specific programs of the FEZ development in connection with the changing realities in the economy, the diversity of types of zones and measures of their state regulation, the introduction of decentralization and a differentiated management approach, preferential production for external consumption and innovative manufacturing methods, stimulation of the regional economy.

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