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The Combined Impact of Foreign Direct Investment and Foreign Trade on China's Economic Growth: A Systematic Review

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Abstract

This paper uses PRISMA method to systematically review the comprehensive impact of foreign direct investment (FDI) and foreign trade on China's economic growth, explore the role and synergistic effect of FDI and foreign trade in different industries and regions. This paper found that FDI promotes economic growth through technology spillover, innovation enhancement and export competitiveness enhancement, especially in high-tech industries. Foreign trade optimizes export structure, promotes regional integration, and strengthens FDI. The synergies between FDI and trade are prominent in high-tech industries, but weak in labor-intensive industries. Regionally, the eastern China has obvious synergies between infrastructure and policy support, while Central and Western China has not fully released its potential due to insufficient technology absorption capacity. This paper provides new insights for promoting economic growth and realizing regional coordinated development, and also providing lessons for other developing countries' economic development.

Keywords: Foreign Direct Investment, Foreign Trade, Comprehensive Impact, Economic Growth, Systematic Review

Introduction

In the era of deepening globalization, foreign direct investment (FDI) and international trade have become critical drivers of economic growth, especially in developing countries. FDI brings in capital, technology, and managerial expertise, while trade facilitates market expansion and resource allocation efficiency. Many emerging economies, including those in Southeast Asia, Latin America, and Eastern Europe, have relied heavily on these external engines to promote industrial upgrading and economic transformation. Furthermore, similar issues are faced by many other developing countries. For instance, Vietnam has followed an export-oriented industrialization path, attracting FDI in labor-intensive sectors while gradually moving toward electronics and high-tech products. India, on the other hand, has attracted more FDI in services and digital sectors but still lags behind in export competitiveness. Latin American economies like Mexico and Brazil have also attempted to integrate FDI and trade to support manufacturing growth. However, these countries often struggle with weak policy coordination and unequal regional development, similar to the challenges faced in Central and Western China. Therefore, a comprehensive study of China's experience not only contributes to academic understanding but also provides valuable policy references for other emerging economies seeking to balance globalization benefits with domestic development priorities.

At present, the global economic landscape is undergoing profound changes, and developing countries are facing the dual challenges of industrial transformation and coordinated regional development. In this context, in-depth research on the synergistic effect of FDI and foreign trade is helpful to grasp how external economic forces jointly shape China's growth model, and also provides theoretical support and experience for realizing regional coordinated development and industrial upgrading.

The significance of this study is not only reflected in the academic theory level, but also in its practical guiding value. For policy makers, a systematic understanding of the linkage effect of FDI and trade is helpful to formulate more targeted regional development and industrial policies. For enterprises, it can provide support for them to formulate global strategy and technology cooperation path; For other developing countries, China's experience is highly transferable, which helps them to better play the role of promoting FDI and trade in the process of globalization.

China, as the world's largest developing economy, has experienced rapid growth by integrating into the global economy. Since the late 1970s, the country has attracted substantial FDI and expanded its trade volume exponentially. These two external forces have been central to China's development model and rapidly integrated into the global trading system, becoming a major manufacturing and trading country in the world. However, the specific mechanisms of FDI and trade and their regional differences are still controversial, especially in regions with different levels of economic development, where their effects and interaction mechanisms show significant differences.

The impact of FDI on China's economic growth is mainly reflected in technology spillover, production efficiency improvement and export competitiveness enhancement. Research shows that FDI promotes the eastern coastal areas' economic development through innovative activities and technology transfer, and significantly improves high-tech industries' competitiveness (Tang & Zhang, 2001; Cheung, 2010). However, this effect is not evenly distributed. In the central and western regions, FDI's technology spillover effect is weak due to weak infrastructure and insufficient absorption capacity (Kim, 2016). In addition, foreign enterprises' entry may have a certain crowding out effect on local enterprises' market share and innovation ability, and further aggravate inter-regional economic development imbalance (Lu et al., 2007).

As an important driving force for economic growth, foreign trade also optimizes export structure and promoting technological progress. Through the processing trade model, China has achieved a rapid increase in export intensity and gradually transformed to high value-added industries (Xu & Lu, 2007; Fu, 2008). However, there are significant differences in the degree of dependence on trade and the level of benefits across regions and sectors. For example, the eastern region, with its superior geographical location and policy support, has significantly improved its export products' technical content and added value, while the central and western regions' export competitiveness has improved relatively slowly (Yun, 2005; Zhang & Felmingham, 2011). In addition, trade has a profound impact on promoting regional economic integration and creating job opportunities, but its effects are also limited by regional economic conditions and policy environments (Li & Pan, 2007).

The interaction between FDI and trade further strengthens its comprehensive contribution to economic growth. FDI enhances China's international competitiveness by promoting the export-oriented economic model, while export activities also create greater spillover space for FDI (Cheung, 2010; Xu & Lu, 2007). This interaction is particularly significant in high-tech industries, but less so in labor-intensive industries (Lu et al., 2007). However, regional differences are also reflected in this process. The eastern region has significant synergies on FDI and trade, while the central and western regions have limited synergies due to insufficient infrastructure and policy support (Yang & Zhang, 2015).

While the contribution of FDI and trade to China's economy is unquestionable, existing research falls short in several areas. First, there is a lack of systematic analysis of the long-term dynamic effects of FDI and trade, especially at different stages of economic development. Second, the quantitative assessment of the regulatory effect of policies is insufficient, and the specific effects of various policy tools in promoting the coordinated development of FDI and trade are not yet clear. In addition, there are few studies on the central and western regions in the existing literature, which limits the in-depth understanding of the balanced economic development on the national scale.

Although a wealth of literature has discussed the impact of FDI and foreign trade on economic growth, the current research has the following shortcomings: first, the specific mechanism of the effect difference between regions and industries has not been clarified; secondly, the interaction between FDI and trade is still lacking in systematic research; finally, the regulation effect of policy on the synergistic effect of FDI and foreign trade is relatively weak.

Through systematic literature review, this paper aims to comprehensively analyze the multiple impacts of FDI and foreign trade on China's economic growth and their interaction mechanisms, focusing on answering the following research questions:
(1) How does FDI promote China's economic growth?
(2) What is the role of foreign trade in promoting economic growth?
(3) How does the interaction of FDI and trade?

This paper not only fills the gap of regional and industry perspectives in studying FDI and trade interaction, but also provides a theoretical basis for policy formulation. This analytical framework is not only applicable to China, but also can be used for reference by other developing countries and provide new ideas for economic development research under the background of globalization. This paper's structure is as follows: the second part is theoretical framework, the third part introduces methodology; the fourth part summarizes results; the fifth part is discussion; the sixth part is policy implications; the seventh part is limitations and future research directions recommendations; the eighth part is conclusion.

This paper contributes to the existing literature in several important ways. First, while prior studies often analyze FDI and trade in isolation, this study explores their interaction effects within a unified framework. Second, by systematically reviewing studies across different regions and industries, it highlights the heterogeneity of impacts, especially the lagging effects in the central and western regions. Third, the inclusion of theoretical perspectives such as comparative advantage theory and endogenous growth theory enhances the conceptual clarity of the findings. Finally, this paper provides targeted policy implications for regional coordination and industrial upgrading, offering valuable references for other developing countries seeking sustainable and inclusive growth through globalization.

In general, as a systematic literature review, this paper is committed to sorting out and analyzing the comprehensive impact of foreign direct investment and foreign trade on China's economic growth. By summarizing and comparing different research results, this paper not only reveals the development vein and key conclusions of relevant research, but also summarizes the shortcomings of current research and the direction of future development. This study has strong practical guiding significance, helping to provide theoretical basis for policy making, clarifying key issues for academic research, and providing useful experience for other developing countries.

Theoretical Framework

The mechanisms through which FDI and foreign trade influence economic growth can be grounded in several classical economic theories, providing a theoretical foundation for understanding their interaction and differentiated effects across regions and industries.

First, the Comparative Advantage Theory, offers a foundational explanation for trade-led growth. This theory argues that countries should specialize in producing goods and services they can produce relatively more efficiently than others. In the context of China, foreign trade has facilitated specialization by leveraging its comparative advantages in labor-intensive manufacturing industries during the early stages of development. As China's economy evolved, the comparative advantage shifted toward more technology-intensive sectors, particularly in the eastern coastal regions. Foreign trade thus contributes to economic growth by enabling resource allocation according to comparative advantage, increasing productivity, and expanding export-oriented industries. Furthermore, the theory implies that openness to international trade leads to gains from specialization, market expansion, and competitive pressure, which collectively drive innovation and efficiency.

Second, the Product Life Cycle Theory, provides insights into the dynamic nature of foreign trade and FDI. This theory posits that the production of goods shifts internationally as products progress through their life cycles—from innovation and early adoption to maturity and standardization. Developed countries initially dominate in the early stages of the product life cycle, but as products become standardized, production tends to relocate to developing countries with cost advantages. In China's case, this has manifested in the relocation of foreign-invested manufacturing enterprises into China to capitalize on lower labor costs and expanding markets. As a result, FDI inflows have enabled Chinese industries to move up the value chain by engaging in mid- to late-stage production of global product cycles. This process not only brings capital but also facilitates the transfer of technology, managerial know-how, and global market access, contributing to both industrial upgrading and export sophistication.

Third, the Endogenous Growth Theory, emphasizes the role of knowledge, human capital, and technological innovation in driving long-term economic growth. This theory highlights that economic growth is primarily generated from internal factors rather than external inputs. FDI plays a critical role under this framework by serving as a channel for knowledge spillover and technological transfer. When foreign enterprises invest in China, they often bring with them advanced technologies and management practices. If the domestic economy has sufficient absorptive capacity—measured in terms of human capital, R&D intensity, and institutional quality—these spillovers can lead to sustained productivity growth. Foreign trade similarly contributes to endogenous growth through learning-by-exporting and importation of advanced intermediate goods, which expose local firms to international standards and practices. The eastern regions of China, with higher R&D investment and stronger innovation ecosystems, benefit more prominently from these effects, while the central and western regions lag due to weaker institutional and technological foundations.

Taken together, these theories help to explain why the impacts of FDI and foreign trade on economic growth vary by industry and region in China. Comparative advantage facilitates trade-based growth; product life cycle dynamics shape FDI inflows and industrial upgrading; and endogenous growth factors determine whether these external forces can be transformed into long-term, sustainable development. These theoretical insights also justify policy recommendations that aim to strengthen technology absorption, improve infrastructure, and promote innovation capacity in less developed regions. By aligning trade and investment policies with these theoretical underpinnings, policymakers can better harness the synergistic potential of FDI and foreign trade to promote balanced and inclusive economic growth.

Methodology

Using a systematic literature review approach, this study focuses on the impact of FDI and foreign trade on China's economic growth. The literature screening and analysis process strictly follows PRISMA (Preferred Reporting Items for Systematic Reviews and Meta-Analyses) standard to ensure the systematic and transparent screening process.

Literature Retrieval and Screening

Literature search was conducted in Scopus and Web of Science (WOS) databases, using two Boolean search statements: "1. ("Foreign direct investment" OR "FDI") AND ("Foreign trade" OR "export" OR "import") AND ("Economic growth" OR "GDP") 2. (" Foreign direct investment" OR "FDI") AND (" Foreign trade" OR "export" OR "import")". The search covered the period 2001 to 2024, and a total of 902 articles were retrieved, including 506 in SCOPUS and 326 in WOS.

After the duplicate literature was de-duplicated, 403 papers remained. For further screening, 304 literatures that did not involve China were excluded, and only 99 literatures related to China were retained. On this basis, 44 literatures that did not conform to the theme or were not based on empirical analysis were excluded, and the remaining 55 literatures were excluded. Finally, through in-depth reading of the full text, 14 literatures with excessive research scope, insufficient evaluation methods or unclear research results were further excluded, and 41 high-quality literatures were finally included as research objects.

Inclusion and Exclusion Criteria

To ensure the relevance and quality of literature screening, this study was based on clear criteria for screening. Table 1 shows inclusion and exclusion criteria.

Table 1
Inclusion and exclusion criteria

	Criteria
Inclusion	1. Publication in a peer-reviewed journal
	2. The research topic should be directly related to FDI, foreign trade and economic growth, and be based on empirical research
	3. Quantitative analysis methods were used in the literature
	4. Related to China's economy, analyze the role of FDI and foreign trade on China's economic growth
Exclusion	1. Studies with unclear data sources or insufficient sample size
	2. Literature containing only theoretical discussion or review without empirical analysis
	3. There are no literatures related to China or unrelated to the research topic

Through rigorous screening criteria, this study ensured the high quality and research relevance of the included literature.

Quality Evaluation

In the literature selection process, this paper combined with quality assessment tools such as CASP (Critical Appraisal Skills Programme) and JBI (Joanna Briggs Institute) to conduct a comprehensive evaluation of the selected literature. The evaluation includes study design's scientific nature, data's completeness and method's rationality. Firstly, by reading title and abstract for preliminary screening, eliminate obviously irrelevant literature; Secondly, the literature that meets preliminary screening criteria is read in full to further evaluate the relevance of its content to the topic. In the end, only 41 articles that met the evaluation criteria were included for subsequent analysis. The specific steps and results of the literature screening process are visually presented by PRISMA diagram (see Figure 1).

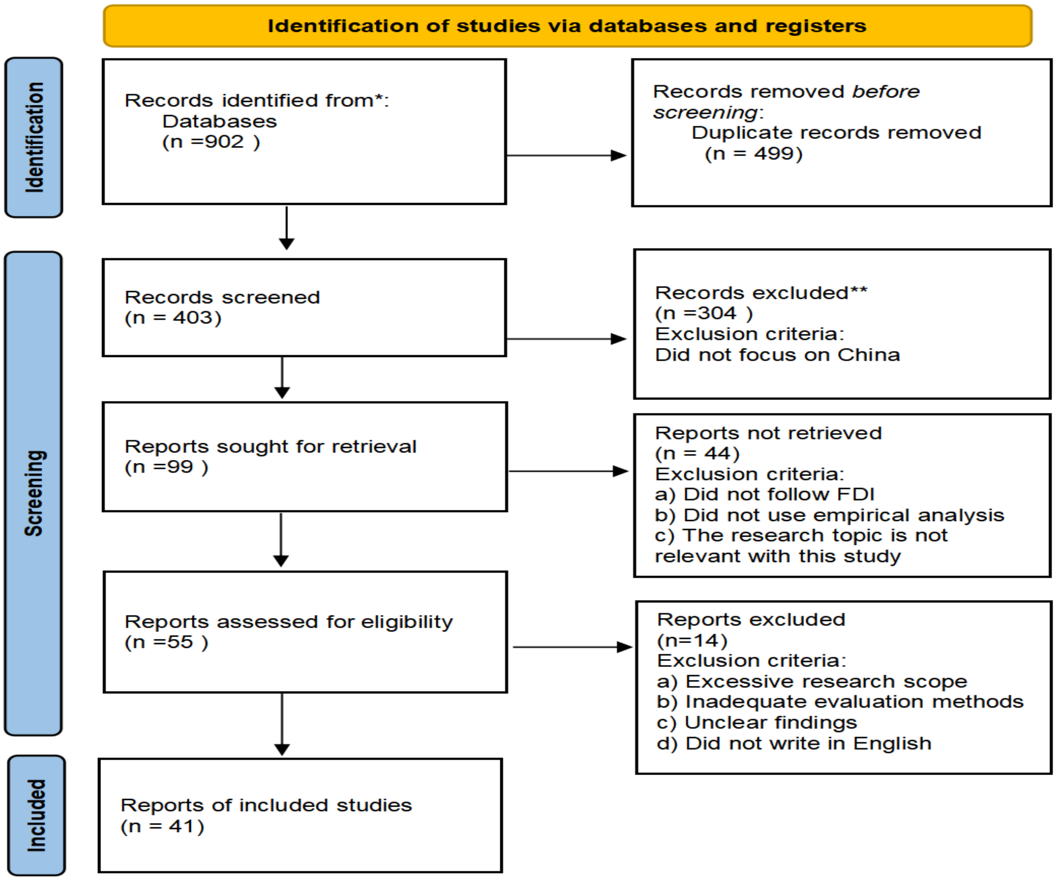

Figure 1 PRISMA flow diagram

Results

This section introduces impact of foreign direct investment (FDI), influence of foreign trade, and interaction between FDI and trade.

Impact of FDI

FDI plays an important role in China's economic development, and its combined effect on technology spillover, export competitiveness improvement, regional economic differentiation and economic growth has become a hot topic in academia and policy research. The following is a systematic summary of the impact of FDI from the aspects of technology spillover and innovation, export effect, regional economic differences, policy regulation and other social and economic impacts.

The Impact of FDI on Technology Spillover and Innovation

FDI promotes China's technological progress and innovation capability through technology spillover effect, which is particularly significant in the eastern coastal areas. Research shows that R&D activities of foreign-funded enterprises can significantly promote high-tech industries' innovation capability (Cheung, 2010; Lu et al., 2018). In addition, the eastern region, with its high human capital and research and development capabilities, has significantly enhanced its ability to absorb FDI technology spillovers (Tang & Zhang, 2001). In contrast, due to the lack of technology absorption capacity, FDI's technology spillover effect is weak in the central and western regions, especially in high-tech industries (Kim, 2016). The above results show that there are significant regional differences in FDI's promotion effect on China's economic growth through technology spillover mechanism. This finding supports RQ1 and suggests that policies should focus on improving the ability of central and western regions to absorb foreign capital in order to achieve balanced development. However, FDI's technological spillover is not entirely positive. Some studies have found that the entry of foreign enterprises may reduce local enterprises' market share, thus inhibiting the technological innovation of the latter (Lu et al., 2007). Therefore, FDI's technology spillover effect needs to be comprehensively evaluated in conjunction with local enterprises' absorptive capacity.

The Promotion Effect of FDI on Export

FDI has played a key role in enhancing export competitiveness. Research shows that foreign-funded enterprises promote export intensity and export quality improvement through the processing trade mode (Xu & Lu, 2007). For example, in Guangdong Province of Eastern China manufacturing industry, FDI has significantly promoted export intensity, and this effect is particularly significant in labor-intensive industries (Yun, 2005). In addition, FDI in the eastern coastal areas enhances export industry's international competitiveness by promoting the export-oriented economic model (Yang & Zhang, 2015; Zhang & Song, 2009). On the other hand, FDI has a double effect on export added value. Some studies have found that FDI may inhibit the increase of export added value in low-tech industries, but in high-tech industries, it significantly increases the added value through horizontal spillover effect (Lu et al., 2007). This shows that FDI's specific effect on exports depends on industry characteristics and technical level.

The Differentiated Impact of FDI on Regional Economy

There are significant differences in the impact of FDI on China's regional economy. Coastal areas, with their superior geographical location, infrastructure and policy support, have attracted a large amount of FDI, which has significantly promoted regional economic growth and export competitiveness' improvement (Yang & Zhang, 2015; Zhao et al., 2023). For example, the positive spillover effect of wholly foreign-owned enterprises in coastal areas is significant, while that of joint ventures is limited (Ouyang & Yao, 2006). In contrast, the role of FDI in the central and western regions is limited due to the lack of infrastructure and technical capacity (Kim, 2016). However, it is worth noting that FDI in the central and western regions shows great development potential with policy support and improved absorption capacity (Ouyang & Yao, 2006). For example, through policy guidance, the gradual transfer of foreign-funded enterprises to the central and western regions will help achieve balanced regional economic development.

Policy Regulation of FDI

Policy plays a key role in determining FDI effects. For example, the Catalogue for the Guidance of Foreign Investment Industries implemented by the Chinese government since 1995 has significantly improved the role of FDI in promoting foreign trade development (Zhao et al., 2023). In addition, export tax rebate policies and investment guidance policies have a significant impact on the effect of FDI in different regions, especially in the differentiated performance of eastern and central and western regions (Zhong & Wei, 2017). The uneven implementation of policies also leads to differences in FDI effects between regions. For example, the eastern region benefits from higher policy preferences and a stronger economic foundation, and its FDI effect is significantly higher than that of the central and western regions. However, after the policy adjustment in recent years, FDI effect in the central and western regions has improved, for example, some provinces have attracted more foreign enterprises by strengthening infrastructure construction and reducing tax incentives (Kim, 2016).

Socio-Economic Impact of FDI

In addition to technological and economic effects, FDI also significantly promotes employment and migration in China through labor-intensive export industries (Li & Pan, 2007). Studies show that long-distance migration driven by FDI is mainly concentrated in the eastern coastal areas, while short-distance migration is more affected by local marketization process (Zhang & Felmingham, 2011). In addition, the stabilizing role of FDI in alleviating international economic fluctuations cannot be ignored (Gu & Yu, 2017). For example, under the pressure of CNY appreciation, FDI, as an inherent stabilizer of trade balance, provides support for economic growth.

To sum up, the impact of FDI on China's economy is multidimensional, and its effect is not only reflected in technology spillover and export competitiveness' improvement, but also plays an important role in regional economic differences and policy adjustment. However, FDI's effect is not balanced, and its inter-regional differences and policy adaptation still need further attention. Future studies should further explore FDI's specific performance in different industries and regions, especially how to achieve balanced regional economic development and industrial upgrading through policy optimization.The above findings verify RQ1, indicating that FDI's promoting effect on China's economic growth has significant regional and industrial differences. Policies should focus on improving the technology absorption capacity of the central and western regions, and guide FDI into high value-added industries through industrial policies.

Influence of Foreign Trade

As an important force to promote China's economic growth, the influence of foreign trade is reflected in export structure optimization, technological progress promotion, regional economic differentiated role and policies' regulatory effect. The following is a systematic summary of the relevant research results.

Influence of Foreign Trade on Export Structure Optimization

Foreign trade has significantly promoted the improvement of technology content of China's export products, especially in high value-added industries (Xu & Lu, 2007). Studies have shown that China's export structure has gradually shifted to technology-intensive industries, mainly due to processing trade expansion (Fu, 2008). Processing trade has enhanced China's export intensity, but also limited local enterprises' technological innovation ability to a certain extent (Lu et al., 2018). However, the effect of export structure optimization in different regions is different. With superior infrastructure and technical capabilities, export products' technical content in the eastern coastal areas has improved significantly (Yun, 2005). In contrast, the speed of export structure optimization in Central and Western China is significantly slower due to their weak technical capabilities (Kim, 2016). These findings validate RQ2 that foreign trade not only plays an important role in optimizing export structure, but also promotes regional economic integration through spillover effects, but the effect in Central and Western China is relatively limited. The future policy should strengthen support for the central and western regions' export competitiveness.

Promoting Effect on Technological Progress

Foreign trade plays an important role in promoting technological progress. Import provides local enterprises with access to international advanced technologies, thus enhancing their technological innovation capability (Cheung, 2010). In addition, export also promote enterprise technology level improvement to a certain extent through competition effect and learning effect (Xu & Lu, 2007). However, the literature also points out that import has certain limitations in promoting local technological innovation. For example, in labor-intensive industries, import may lead to foreign technology dependence, thus inhibiting local technological capabilities improvement (Liang, 2013).

Differentiated Impact on Regional Economy

Foreign trade has a differentiated impact on economic growth in different regions of China. Studies show that export expansion significantly promotes economic growth in the eastern region, but has a limited effect on Central and Western China (Zhang & Felmingham, 2011). With geographical advantages and policy support, the eastern region has a more active export industry, while Central and Western China face insufficient export competitiveness challenge (Yang & Zhang, 2015). In addition, foreign trade has significantly promoted interregional economic integration. The trade spillover effect of coastal areas has a certain promoting effect on the economic growth of inland areas, especially in regions with better infrastructure (Ouyang & Yao, 2006). However, such spillovers' strength is constrained by regional policy and economic conditions.

Regulation of the Role of Policies in Foreign Trade

The influence of policy on foreign trade plays an important regulating role. Export tax rebate policy plays a key role in enhancing export intensity and optimizing export structure (Zhong & Wei, 2017). For example, export tax rebate policy in the eastern region has significantly enhanced its export competitiveness, while the central and western regions have not fully benefited due to insufficient policy coverage (Zhao et al., 2023). In addition, China's trade policy reform after its accession to the World Trade Organization (WTO) has significantly improved foreign trade environment and provided more market opportunities for export enterprises (Fu, 2008). The implementation of these policies has not only increased foreign trade's total volume, but also improved export products' technical content and added value to a certain extent.

Comprehensive Impact on Social Economy

Foreign trade has had a profound impact on China's social economy by creating jobs and driving migration. Studies have shown that labor-intensive export industries' development has significantly facilitated long-distance migration, especially from inland areas to coastal areas (Li & Pan, 2007). At the same time, export industry expansion has provided more employment opportunities for female workers, thus having a positive effect on gender equality and socio-economic development (Xu & Lu, 2007). On the other hand, foreign trade also promotes local enterprises's production efficiency through the effect of technology spillover and market competition. However, this uplift is mainly concentrated in coastal areas and has a relatively limited impact on inland areas (Cheung, 2010).

To sum up, foreign trade has provided an important driving force for China's economic growth through mechanisms such as export structure optimization, technological progress promotion and regional economic integration. However, regional differences and uneven implementation of policies limit the full effects of foreign trade. Future studies should pay more attention to the potential role of foreign trade in the central and western regions, and how to achieve a balanced contribution of trade to social and economic development through policy optimization. These results provide compelling evidence that foreign trade positively contributes to economic growth, particularly through export expansion and industrial upgrading. Moreover, the stronger effects observed in the eastern region suggest that trade openness interacts with regional development levels. These findings directly support RQ2, which investigates how foreign trade affects economic growth across different sub-industries and regions.

Interaction between FDI and Trade

FDI and foreign trade, as the two major engines driving China's economic growth, not only play an independent role, but also have a profound impact on the economy through complex interaction mechanisms. The following is a systematic summary of the interaction between FDI and trade from four aspects: export promotion, technology spillover mechanism, regional effect and policy regulation.

The Role of FDI in Promoting Exports

FDI has contributed significantly to export growth by enhancing China's export-oriented economic model. FDI has a direct effect on improving export intensity and export quality. For example, Cheung (2010) finds that foreign firms outperform local firms in high-tech products' export, and these firms' R&D activities further enhance export competitiveness. Foreign-funded enterprises in processing trade also significantly promoted export intensity improvement (Xu & Lu, 2007).

The results of this part reveal the comprehensive contribution of the interaction between FDI and trade to economic growth. Through export-oriented economic model and technology spillover mechanism, the two jointly promote regional economic differentiated development. This finding answers RQ3 and highlights the critical role of policy in optimizing FDI and trade synergies.

Moreover, the interaction between FDI and exports varies regionally. The effect of FDI driven export growth in the eastern coastal areas is significant, while the effect is limited in the central and western regions due to insufficient infrastructure and policy support (Yang & Zhang, 2015). However, with the improvement of infrastructure and preferential policies in the central and western regions, FDI's role in promoting exports has gradually increased (Kim, 2016).

The Enhancement of Trade Spillover Effect on FDI

Foreign trade, especially import, enhances FDI's spillover effect by providing technology input and market demand. For example, imported technical equipment and intermediate products provide opportunities for local enterprises to learn and imitate, thus improving their ability to absorb FDI technology spillovers (Liang, 2013). In addition, export activities also create greater spillover space for FDI through competition effect and market expansion (Zhong & Wei, 2017). However, the effects of this interaction vary by industry and region. The synergy between FDI and export activities is more obvious in high-tech industries, while the effect is relatively weak in labor-intensive industries (Lu et al., 2007).

Influence of Inter-Regional Heterogeneity

The interaction between FDI and trade shows significant heterogeneity in different regions. The synergies between FDI and trade are more significant in coastal areas because of their higher technology absorption capacity and marketization level. For example, Yang & Zhang (2015) pointed out that FDI in the eastern region significantly promoted export industry's international competitiveness, while this effect was limited by the infrastructure and market environment in Central and Western China. Although the interaction effect of FDI and trade in Central and Western China started late, it has great potential. Research shows that through policy support and infrastructure improvement, the central and western regions can gradually realize FDI and trade's coordinated development (Ouyang & Yao, 2006).

Policy Regulation of Interaction

Policy enhances the interaction between FDI and trade. Export tax rebate policy not only promotes export growth, but also indirectly enhances the spillover effect of FDI on exports (Zhong & Wei, 2017). In addition, the Catalogue for the Guidance of Foreign Investment Industries promulgated in 1995 has significantly improved the role of FDI in promoting exports, especially in high value-added industries (Zhao et al., 2023). However, uneven implementation of policies has also led to differences in interactions between regions. For example, the synergies between FDI and trade in the eastern region are much higher than those in the central and western regions due to higher policy support (Kim, 2016). In the future, the potential of FDI and trade interaction can be better exploited by optimizing policy coverage and implementation effects.

The interactive analysis confirms that the combined effect of FDI and foreign trade is more significant than their individual impacts, particularly when supported by policy and institutional alignment. This supports the hypothesis in RQ3 that FDI and trade act synergistically, and their interaction can shape regional economic imbalances. The results highlight the necessity of coordinated development strategies.

To sum up, FDI and foreign trade have jointly promoted China's economy sustained growth through complex interaction mechanisms. This interaction is not only reflected in export-oriented economy formation, but also in technology spillover, differentiated development of regional economy and policy adjustment. Future research should focus on synergies and policy optimization in the central and western regions to achieve balanced development and sustainable growth of FDI and trade.

Discussion

This paper systematically summarizes the multiple impacts of FDI and trade on China's economy, and reveals their complex interaction mechanism. The following are discussed from four perspectives: policy, mechanism, regional differences and lack of research.

Policy plays a crucial role in enhancing the synergies between FDI and trade. Policies such as export tax rebate policy and the Catalogue for the Guidance of Foreign Investment Industries have significantly enhanced the role of FDI and trade, especially in the eastern region (Zhao et al., 2023; Zhong & Wei, 2017). However, the uneven implementation of these policies across regions limits the potential of FDI and trade in the central and western regions. For example, Kim (2016) pointed out that although the role of FDI in the central and western regions has increased, the coverage and intensity of policies are insufficient, resulting in its overall effect still being lower than that of the eastern region. Future policies should pay more attention to the balance between regions in order to fully tap the central and western regions' potential benefits.

The interaction mechanism between FDI and trade is diverse and complex. On the positive side, FDI enhances China's international competitiveness by promoting export-oriented economic model, while export activities also create greater spillover space for FDI (Cheung, 2010; Xu & Lu, 2007). However, this interaction varies significantly across industries and regions. For example, the synergy between FDI and export activities in high-tech industries is significant, while labor-intensive industries' performance is limited (Lu et al., 2007). This difference indicates that the interaction mechanism between FDI and trade needs to be deeply studied in light of specific industry and regional characteristics to formulate targeted policy support.

The heterogeneous effects of interregional FDI and trade deserve great attention. The eastern region, with its superior geographical location, infrastructure and high technology absorption capacity, has significantly benefited from the interaction effect of FDI and trade (Yang & Zhang, 2015). However, the synergies in the central and western regions are limited due to their late start and weak infrastructure (Ouyang & Yao, 2006). Nevertheless, the central and western regions show great potential for development, and through infrastructure construction and policy guidance, regional economic balanced development can be gradually achieved.

In addition, the future interaction between FDI and trade should incorporate the new trends of green and digital development. With increasing global emphasis on sustainability, many countries are adjusting their FDI guidance to attract environmentally friendly and low-carbon industries. China has also committed to carbon neutrality, and policies should therefore align FDI and trade incentives with sustainable development goals. Promoting green technology transfer, low-emission exports, and digital trade platforms can create new channels for regional growth, especially in underdeveloped areas with natural resource advantages or digital potential. This implies that future FDI–trade synergies must be built not only on traditional industrial logic, but also on ecological and innovation-oriented foundations. Policymakers should consider integrating green finance tools, environmental performance evaluation, and eco-industrial parks into FDI-trade promotion strategies. Such forward-looking approaches will ensure that regional growth is both economically robust and environmentally sustainable.

Policy Implications

This study's findings highlight several important policy implications aimed at promoting coordinated regional development. First, for the central and western regions, the most urgent task is to improve their infrastructure and technology absorption capacity. While these regions have shown potential in attracting FDI under favorable policies, the lack of innovation capability, skilled labor, and industrial supporting systems limits the effective utilization of foreign capital and trade opportunities. Policymakers should prioritize investments in transportation networks, digital infrastructure, and education and training systems to enhance human capital and institutional efficiency. Additionally, strengthening the linkages between foreign-invested enterprises and local firms can promote technology spillover and facilitate the upgrading of local industries. Tailored industrial policies and incentives—such as subsidies for technology adoption or tax relief for R&D activities—may help boost local firms' absorptive capacity and integration into global value chains.

Second, for the eastern coastal region, policy efforts should focus on promoting high-quality FDI and export structure upgrading. Given that this region already benefits from advanced infrastructure, innovation clusters, and global integration, the next stage of development should emphasize the attraction of FDI in high-tech, green, and knowledge-intensive sectors. Policymakers should refine the current FDI guidance catalog to align with national strategic goals such as digital transformation, environmental sustainability, and industrial upgrading. Trade policies should also encourage export sophistication by supporting enterprises engaged in advanced manufacturing and innovation-driven exports. In addition, regional innovation platforms and public–private partnerships can be enhanced to stimulate collaborative R&D activities between foreign and domestic firms.

Third, at the national level, it is essential to establish a coordinated and differentiated regional FDI and trade policy system. A one-size-fits-all policy framework is no longer suitable for a country with such pronounced regional disparities. Instead, a "region-specific, function-oriented" approach should be adopted, whereby different regions are guided by differentiated objectives—such as innovation leadership in the east, industrial capacity building in the center, and catch-up development in the west. The central government can play a key role by designing an integrated regional development strategy that harmonizes trade and investment policies across provinces, encourages regional cooperation, and avoids unhealthy competition for foreign capital. Moreover, a robust evaluation system should be established to monitor the effectiveness of FDI- and trade-related policies across regions and make timely adjustments based on empirical feedback.

Limitations and Future Research Directions

Although existing studies provide a wealth of evidence, there are still some limitations that constrain a comprehensive understanding of the relationship between FDI, foreign trade, and economic growth in China. First, most of the literature focuses primarily on the direct and static effects of FDI and trade, while relatively little research investigates their long-term dynamic impacts, such as delayed spillover effects or cyclical fluctuations under different economic phases. Second, although the role of policy is widely acknowledged, there is a lack of quantitative assessments of specific policy instruments, making it difficult to identify which tools are most effective in promoting synergistic effects across regions and industries. Third, the geographical coverage of existing research is uneven, with the eastern region receiving much more attention than the central and western regions. This imbalance limits a full understanding of regional disparities and the potential for coordinated development.

Although this study provides a comprehensive synthesis of existing literature on the impact of FDI and foreign trade on China's economic growth, there remain several avenues for future research to deepen understanding and address unresolved questions. First, future studies should focus on employing dynamic panel data models or structural vector autoregression (SVAR) frameworks to explore the long-term and lagged effects of FDI and trade. Most of the existing empirical studies rely on static models, which may not fully capture the temporal transmission mechanisms or delayed spillover effects, especially in the context of policy shifts or global economic changes. Incorporating time dynamics would help clarify the cumulative or diminishing returns of FDI and trade over different phases of economic development.

Second, future research could benefit from comparative studies between China and other emerging economies, such as India, Vietnam, or Brazil. While China's experience with export-led growth and FDI absorption is unique in many ways, comparative analysis may provide more generalizable insights into the effectiveness of policy frameworks, institutional quality, and regional integration. Such studies can also identify common success factors or policy pitfalls in managing foreign capital and global trade participation in a developing country context. Third, more research is needed to examine the interactions between different policy instruments—such as tax incentives, trade liberalization, innovation subsidies, and investment guidance—and how they jointly influence FDI–trade–growth linkages. Disentangling the effects of specific policies will allow policymakers to better design targeted interventions, particularly in the context of balancing regional disparities. Furthermore, integrating qualitative policy evaluation methods or case study approaches may enrich the understanding of how policy implementation affects outcomes across different provinces and industries. Fourth, firm-level microdata can provide more granular evidence on how foreign and domestic enterprises respond to trade and investment policies. Investigating heterogeneity in firm behavior—based on size, sector, ownership structure, or innovation capacity—could shed light on how FDI and trade impact productivity, employment, and technological upgrading at the microeconomic level. This direction is particularly relevant for designing inclusive policies that benefit both large exporters and smaller domestic enterprises.

Conclusion

Through systematic literature review, this paper comprehensively analyzes the comprehensive impact of FDI and foreign trade on China's economic growth and their interaction mechanism. The results show that FDI significantly promotes China's economic growth through technology spillover and innovation capability improvement, while foreign trade provides an important driving force by optimizing export structure and promoting regional economic integration. The interaction mechanism between FDI and trade is complex, and its effects show significant differences between regions and industries. The regulatory role of policy is crucial in enhancing the synergies between the two, but more attention needs to be paid to the central and western regions' development potential. Moreover, this paper contributes to understanding the growth dynamics of China but also offer valuable implications for other developing countries such as Malaysia, Thailand, Vietnam, and Indonesia. These economies, like China, are striving to balance regional development, attract high-quality FDI, and enhance export competitiveness. The experience of China's western region highlights the importance of coordinated policy frameworks, long-term investment in human capital and innovation, and region-specific development strategies. For Malaysia, efforts to upgrade its industrial base and move up the value chain could benefit from a more integrated approach that links FDI inflows with export performance and technological learning. Thus, the lessons drawn from China's regional experience can serve as a useful reference for similar emerging economies navigating globalization and domestic disparities.

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