

Determinants of Chinese Outward Foreign Direct Investment in Sri Lanka, India and Pakistan

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Background

Most of the Outward Direct Investment (ODI) activities, in terms of their size and volume, are concentrated, generally, in the Industrial West. The ODI activities that expanded rapidly over the years from about 1960s, has been the predominance by the industrial West. These countries were noted as both the provider and as the host of the ODI sources. However, since about the turn of the century, some countries from outside the Industrial West also emerged as the facilitator of the ODI funds. This includes, inter alia, the economies that have shown rapid growth and expansion of Asia. China has come forth, since the turn of the century, in the focus as a significant provider of ODI funds in the world.

In fact, China has as the provider of ODI funds been growing since about the start of 1980s, to become a major facilitator of such funds over the years after 2000 (WIR, 2014). With over 100 billion dollars (WIR, 2014) that China facilitated, she emerged already during the first decade of the new century to hold the third place (after US and Japan) as the provider of ODI resources in the world (WIR, 2014).

In regard with the pledges that China has made about continued commitments in the realm of global economic undertakings, it seems China to be making quantum leaps forward as the facilitator of ODI funds. This has been indicated by the policy *formulae* that China has put forth (i.e. “go out policy” of China and those that come within the perspective of the creation of the ‘BRICS Bank’ and the ‘Asian Infrastructure Investment Bank’) which seem to render highly significant ramifications for Chinese ODI activities.

Research Problem

There are several noteworthy features about the emergence of China as a significant provider of ODI funds. This concerns, first, the rapid rate of growth of Chinese ODI activities that has never been recorded before. Second, the emergence of both the private sector as well as the public sector entrepreneurial organisations as providers of the ODI funds and related facilities. In some instances, particularly with reference to a few of the markets (i.e. those of the Industrial West), the ODI funds that have emanated from the public sector enterprises of China seem to be greater than that emanated from the private sector enterprises of China. At the same time as the public sector enterprises of China emerges as the facilitator of ODI funds, the Chinese state plays also a significant role as regulator and guarantor of the economic policy fundamentals helping the facilitation of ODI funds. This includes (i) the negotiation of bilateral agreements signed between China and other markets (the states

representing them), and (ii) the facilitation of “easy loans” provided for private sector enterprises of China that seek to invest overseas territories. The creation of the BRICS Bank and the Asian Infrastructure Investment Bank (AIIB) has also significant ramifications for this.

The inquiry about the emergence of China as the facilitator of ODI funds brings to forth several issues of importance. This concerns, first, the sufficiency and appropriateness (or their absence) of the prevailing theories and the interpretative models whose purpose to understand and clarify the proliferation of Chinese ODI activities. Perhaps the fact that China is a “state market economy” (as opposed to “private market economies” of the industrial West) adds a complication to the matter.

Main Objective of the Research

The main issue that pertains in here (as per the objectives of the research) concerns the determinants of the Chinese ODI in Sri Lanka, India and Pakistan (hereafter SLIP countries). Considering significantly high rate of growth of Chinese ODI activities in SLIP in countries over the past few decades, the proposed research aims to focus primarily on examining the determinants of Chinese ODI in these countries.

The main objectives of the research concern the following:

1. Investigate the market related factors (i.e. market seeking endeavours, raw material seeking endeavours, strategic seeking endeavours) in motivating the carrying out of ODI activities by China in the SLIP countries.
2. Investigate the institutional factors (i.e. policies that motivate the encourage Chinese ODI) in motivating the carrying out of ODI activities by China in the SLIP countries.

In this, the institutional factors focus on:

Measure of the significance of the high foreign-exchange-reserve as a push factor that determines Chinese ODI in SLIP countries.

- (i) Measure of the significance of the administrative content of ‘Go-Out Policy’ that impact on Chinese ODI in SLIP countries.
- (ii) Measure of the significance of the “strategic” factors (significance of the diplomatic alliances) that determines Chinese ODI in SLIP countries.

Theoretical Basis

Careful survey of the existing theories (and their interpretative models) indicates that there are noteworthy *lacunae* with them about their applicability to interpret the factors that determine Chinese ODI in SLIP countries. Therefore, two theories (two approaches) have been juxtaposed with one another for the proposed purpose. Thus, it applies in the investigation the Eclectic (OLI) Paradigm *a la* Dunning (2008) juxtaposed with Institutional Approach as has been promoted by North (1990). The former emphasises (i) the market-seeking, (ii) resource-seeking, (iii) efficiency-seeking, and (iv) strategic-asset seeking

endeavour of the enterprises as the central determinants of ODI. The latter (Institutional Approach) emphasises the political economic argument indicating the significance of “institutional organisation” as a determinant of the ODI. It is the integrated model of these two “approaches” that is taken up as the basis for inquiry of the questions outlined.

Research Methodology

Both quantitative and qualitative research methods are applied in the study. Qualitative research methods are used when analysing primary data gathered by way of structured and semi-structured interviews/surveys. This includes, first, the data gathered from the representatives of the concerned enterprises of China and the organisations involved with policy making as well as the representatives of public sector organisations as well as the individuals from private and public sector organisations in the SLIP countries.

The quantitative methods of the inquiry refer to the application of the Multiple Regression Model (MRM) which favour the examination of the Chinese ODI from empirical perspective (Drodendijk and Blomkvist, 2013; Buckley et al, 2007; Chang, 2014) engaging the Cross Sectional Data. This is for investigating how the relevant variables could be used following the rules of RMR for estimating the determinants of OLI advantages and other country specific advantages. To support the quantitative method, secondary data are applied, and the main sources are from UNTCAD, WDI, Central Banks of relevant countries etc.

Proposition Development

To understand the determinants of the Chinese ODI in SLIP countries, the proposition of the hypotheses is based on the integration of OLI Paradigm juxtaposed with Institutional Approach. The determinants of market-seeking, resource-seeking, efficient-seeking, and strategic asset-seeking are derived from OLI paradigm, whilst the duality in the character of the state of China (which refers to the phenomenon that the state is not just playing the role as a legislator but also as “an entrepreneur”) is derived from the Institutional Approach. The equation may be designed as follows:

$$\text{Chinese outward ODI}_i = \alpha + \beta_a \text{ market} + \beta_b \text{ natural resources} + \beta_c \text{ efficiency} + \beta_d \text{ strategic asset} + \beta_e \text{ entrepreneurship character of Chinese state} + \beta_f \text{ controls} + \beta_g \text{ dummy} + \varepsilon_i \quad \text{Eq 1}$$

Conclusions

Different enterprises of China have been conditioned by different determinants when it concerns their involvement through ODI in the world economy. When it concerns the private sector enterprises of China, they seek to promote their entrepreneurial efficiencies through market-seeking, resource-seeking, efficient-seeking, and strategic asset-seeking. When they seek to invest in relatively larger economies (i.e. India) they are generally keen on market-seeking aspect. Some Chinese private sector enterprises in Sri Lanka are determined by resource seeking.

However, the state sector enterprises that seek to invest their funds in SLIP countries show other determinants when they opt to invest their resources in SLIP countries. Most of these projects are determined by the strategic advantage each SLIP country can provide when it concerns their investments. Strategic alliance making, access to international routes (enhanced the silk route and safety and security on it) made two such determinants for the state owned enterprises. The “go out policy of China” and the funds that have been made available for these enterprises by way of “easy loans” (BRICS Bank and Asian Infrastructure Investment Bank (AIIB) are reasonably new comers to the market and which have not had the opportunity yet to make any impact in the field of ODI activities). The economic fundamentals that China has been in the process of strengthening (i.e. signing of bilateral cooperation agreements between Sri Lanka and China, India and China and Pakistan and China) are significant in this regard. The purpose of these agreements has largely been to promote investment activities, trade and financial cooperation between the countries.

There are several policy issues that Chinese ODI in SLIP countries calls one’s attention. This concerns the need to conduct comprehensive feasibility studies (including the consideration of long-term wider implications for all involved countries) prior to taking up large investment activities including infrastructure work or the establishment of communication networks. This includes some major infrastructure development of Sri Lanka as well as the establishment of road network from Chinese boarder of Pakistan to its new harbour in the Indian Ocean.

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