

Study on China's Outward Foreign Direct Investment

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Abstract: Outward foreign direct investment (OFDI) is of pivotal importance to the economic development and technological progress of a country. The current situation of OFDI in China varies greatly between the eastern, central and western regions due to various reasons of history, geography and economic environment. Based on the existing studies related to the synergistic effects of China's OFDI, the influencing factors and the micro role of enterprises, this paper analyzed the current situation of China's OFDI, learned from classical theories in the field of OFDI, and put forward related policy recommendations. The paper thought that the country should improve the technology level and marketization, meantime, optimize the industrial structure and enrich the investment fields. Besides, strengthening the development and construction of the central and western regions can help those regions reach their full potential.

1. Introduction

As the world economy has entered a phase of globalization and development, economic development, and outward foreign direct investment (OFDI) have increased tremendously in all countries. Data from *the United Nations Conference on Trade and Development* show that, except for the decline in investment flows due to the impact of the COVID-19 in 2020, total world OFDI have increased from US\$13.25 billion in 1970 to US\$1.54 trillion in 2019, with a remarkable continuous growth trend. Meanwhile, a glance at the total global nominal GDP disclosed by *the World Bank* has also risen from US\$2.965 trillion in 1970 to US\$87.752 trillion in 2019. With the promotion of international investment, the global factors of production and technology have achieved free flow and fueled the growth of the world economy.

Since China's accession to WTO in 2001, China's OFDI has ushered in good external opportunities and entered a phase of rapid growth. According to *the Statistical Bulletin of China's Outward Foreign Direct Investment*, the total amount of China's OFDI was only US\$6.9 billion in 2001 and reached US\$132.94 billion in 2020. Even during the COVID-19 period, the growth rate of China's OFDI also reached 3.3%. In terms of economic development, China's total GDP was only US\$1.34 trillion in 2001, and in 2020 it has reached US\$14.73 trillion, with a per capita GDP of over US\$10,000 and an annual year-on-year growth rate of 2.3%.

Against the background, this paper aims to analyze the current situation of OFDI from Chinese provinces based on existing research and combine it with classical theories in the field of investment

in order to provide strategic suggestions for China's OFDI.

2. Literature Review

2.1 Studies on the Synergistic Effects of China's OFDI

Some scholars have studied the synergistic effect of China's OFDI, for example, Yang Lianxing and Luo Yuhui (2017) confirmed that China's OFDI shows a significant promotion effect on the upgrading of China's global value chain. [1] Lu Wanbo and Chang Yongrui et al. (2015) found that OFDI can promote domestic innovation capacity in the short term, and also has a boosting effect on total factor productivity in the long term. [2] Wang Sheng and Tian Tao et al. (2014) showed that China's OFDI in resource-scarce countries reduces China's trade export flows to these countries, and conversely there is a significant trade creation effect for investment in resource-rich countries. [3]

2.2 Studies on the Influencing Factors of China's OFDI

Numerous scholars have used empirical methods to focus on the factors influencing China's OFDI. For example, Wang Yongqin and Du Julan et al. (2014) found that six dimensional indicators including language, political stability, violence level, government efficiency, regulatory quality, rule of law level and corruption control of the host country have a significant impact on the location choice of China's OFDI. [4] Yang Hongen and Meng Qingqiang et al. (2016) confirmed that bilateral investment agreements significantly influenced China's OFDI in developing countries. [5] Zhang Li (2019) pointed out that the geographical distance between the two countries, the economic strength of the host country, the efficiency of the labor market, and the level of technological readiness all influence China's OFDI in countries on the Belt and Road. [6]

2.3 Studies on the Impact of China's OFDI on Enterprises

Some scholars have focused on the micro perspective to explore the impact of China's OFDI on the firm level. Lei Li and Zhao Zhongxiu (2015) revealed that firms investing in developed countries will reduce their own productivity and raise their operating costs. [7] Mao Qilin, and Xu Jiayun (2014) confirmed that corporate OFDI significantly contributes to the sustainability of firms' innovation capabilities, but the extent of the effect varies somewhat depending on the type of firm. [8]

3. Current Situation of China's OFDI

3.1 Trends in the Scale of China's OFDI

Since China joined the WTO in 2001, international direct investment in China has also entered a phase of rapid growth.

As shown in Figure 1, according to the data disclosed by *the Department of Foreign Investment and Economic Cooperation of the Ministry of Commerce of China*, in the vertical time dimension, the total amount of China's OFDI was US\$6.9 billion when China joined *the World Trade Organization* in 2001, followed by a brief decline, while after 2004, China achieved a rebound in the incremental amount of OFDI and maintained a stable growth during the period until 2016. In 2017, the amount of China's OFDI once again experienced negative growth, followed by a small decline in consecutive years.

Comparing the historical values of China's GDP shown in *the World Bank database*, it can be found that the growth trend of OFDI scale is basically consistent with China's GDP before 2017, i.e.,

it is steadily in an upward trend for a long time, while after 2017, OFDI flow has a downward trend due to the lack of backwardness, but in general, there is still a certain synergy effect.

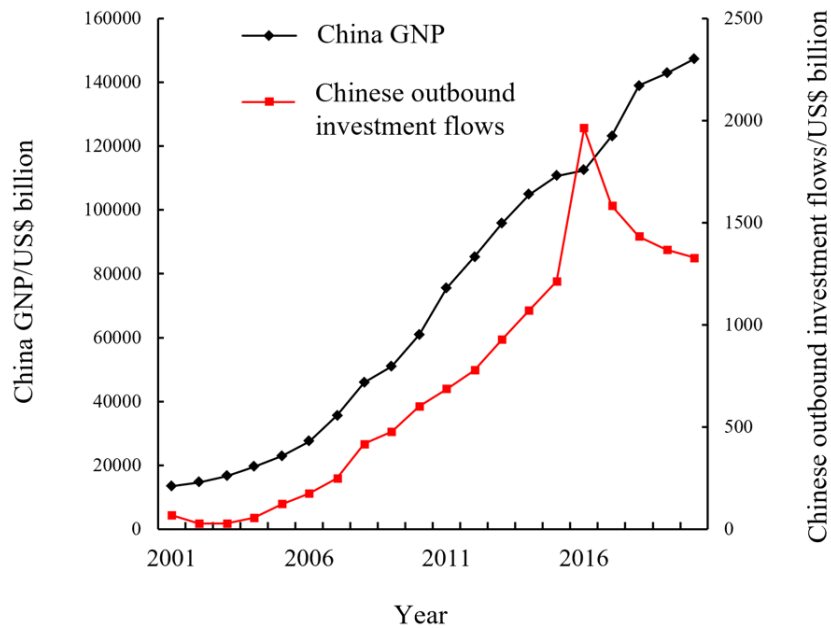


Figure 1: China's OFDI and GDP from 2001 to 2020

3.2 Trends in the Proportion of China's OFDI

According to the ratio of China's OFDI flows in GDP shown in Figure 2, it can be visualized that it shows an overall trend of increasing and then decreasing, with the value reaching a peak of 1.746% in 2016. The possible reason is presumed to be that between 2001 and 2016, China's OFDI flows showed a stable growth trend due to the rapid development of the Chinese economy and the booming import and export industry. And after 2016, OFDI showed a short-term saturation trend, and its flow and share both showed a decreasing trend.

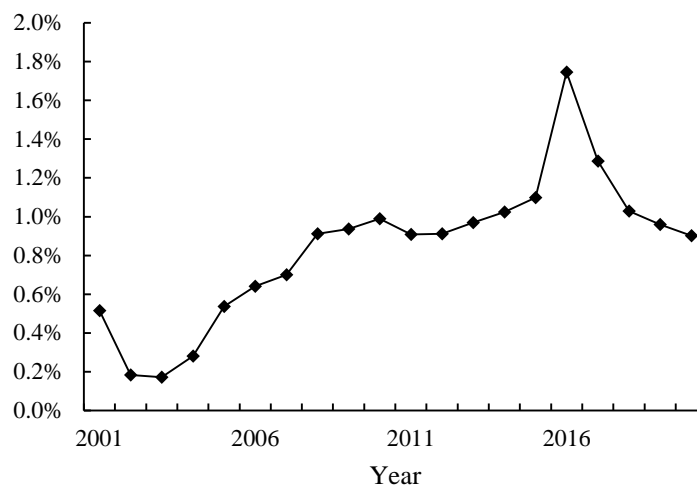


Figure 2: Proportion of China's OFDI in GDP from 2001 to 2020

3.3 Trends in OFDI Flows by Provinces and Cities

Because of the uneven development characteristics among Chinese provinces and cities, regional variability analysis is conducted for different provinces and cities.

As shown in Table 1, from the OFDI flow data disclosed by *the National Bureau of Statistics* for each province and city, ranking according to the average from 2001 to 2019, it can be found that Guangdong Province, Jiangsu Province, and Shanghai City become the first echelon, with their OFDI flows in the forefront and annual average OFDI exceeding US\$400 billion. The second tier, Zhejiang Province and Beijing, also have OFDI of more than US\$200 billion, but there is still a gap with the first tier. Liaoning Province, Shandong Province, Fujian Province, and Tianjin constitute the third tier, with smaller differences in their OFDI, all located within the range of US\$100 billion to US\$200 billion. Combined with the local GDP disclosed by *the National Bureau of Statistics* from 2001 to 2019, it can be found that, except for Beijing, Shanghai, and Tianjin, the ranking of OFDI flows of each province is roughly equal to the ranking of local GDP. Figure 3 also further supports that OFDI flows have a close relationship with economic development, and the higher the regional GDP, the correspondingly larger the OFDI flows.

Table 1: Top ten provinces and cities in terms of average OFDI flows and GDP from 2001 to 2019

Region	Average OFDI (ranking) (Unit: USD million)	Average GDP (ranking) (Unit: yuan hundred million)
Guangdong	640671.89 (1)	50493.69 (1)
Jiangsu	545511.68 (2)	45923.33 (2)
Shanghai	421160.68 (3)	18963.96 (8)
Zhejiang	208172.47 (4)	29574.63 (4)
Beijing	201782.89 (5)	16635.56 (12)
Liaoning	168949.00 (6)	14303.16 (14)
Shandong	168057.11 (7)	36103.21 (3)
Fujian	144119.58 (8)	17771.28 (11)
Tianjin	128098.74 (9)	7216.21 (23)
Sichuan	65433.53 (10)	20111.95 (6)

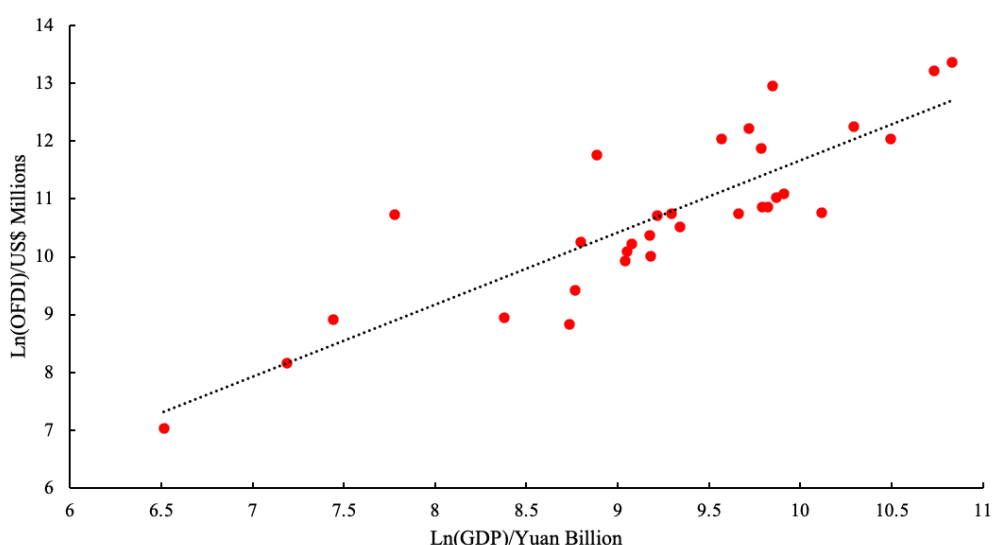


Figure 3: Average OFDI and GDP fitting by province from 2001 to 2019

4. OFDI-related Theories

There are numerous theoretical studies related to OFDI, and since we focus from Chinese provinces and cities perspective, this paper makes more reference to the FDI theories proposed for developing countries.

4.1 The Theory of Small Scale Technology

Wells argued that the outward investment advantages of developing country firms are of a special nature, often in response to the home market environment, and that these advantages are relative rather than absolute competitive advantages, specifically, he still classified the small-scale technology theory as a type of technological passivity theory, arguing that developing country production employs technologies have long matured in developed countries, which makes developing country processing and production industries that are often downstream in the chain. With the economic development of developing countries, more and more scholars are also gradually arguing that developing countries can develop their own specific advantages by learning and mastering the manufacturing technologies of developed countries, and gain economic benefits under small-scale production conditions.

4.2 Investment Development Path

J. H. Dunning proposed the theory in the 1980s. The theory argued that the outward investment of developing countries depends fundamentally on the level of economic development of the country. In addition, Dunning also proposed that the combined indexes of ownership advantage, internalization advantage and regional advantage of developing countries also affect the actual effect of developing countries' outward investment to some extent. Dunning's investment development cycle theory plays a good theoretical reference role for developing countries' outward investment.

4.3 State on Localized Technological Capacities

State on Localized Technological Capacities was refined by Sanjaya Lall on the basis of the theory of small scale technology. According to Lall, developing countries learn advanced technologies from developed countries, but in the process of actual application, they will make "localized" adjustments according to local production conditions, factor prices, supply and demand. Secondly, he believed that usually, what developing countries learn from developed countries is not only technology, but also reform of enterprise structure and management. He also argued that for developing countries, labor-intensive industries are often the first to begin the process of outward investment. Lall's theory of technology localization emphasizes the importance of technology and the innovative and irreversible nature of technological learning compared to small-scale technology.

4.4 Technology Innovation and Industry Upgrade

After studying the trend of outward investment from developing countries over the years, two scholars, John A. Cantwell and Paz Estrella Tolentino, pointed out that there is a certain trend in the geographical choice and industrial choice of outward investment from developing countries, often with technology as the internal driving force. With the accumulation and progress of technology, there is a gradual shift from labor-intensive to technology-intensive. This theory well explains the overall geographical migration of outward investment from developing to developed countries and the overall industrial migration from production factor-intensive to industrial technology-intensive in

developing countries during the past 20 years.

5. Policy Recommendations for China's OFDI

5.1 Improve the Level of Technology and Marketability

China should vigorously develop its economy and promote the technological progress of domestic enterprises, meantime, encourage foreign investment, learn to master advanced technologies, and improve industrial productivity. Improving the marketization of provinces and cities can effectively promote the formation of a good economic system environment for enterprises in the region. In addition, the government and related departments should improve the legal system environment and financial system environment in each region to form a good market competition environment, which will promote the standardized operation of enterprises to a certain extent and enhance their competitiveness through a virtuous cycle.

5.2 Optimize the Industrial Structure and Enrich the Investment Field

The country should continue to promote the transformation of the old and new dynamics, and advance the process of optimizing the economic structure as soon as possible. Only by continuously enhancing the country's economic and scientific hard power, improving the development and production of materials, equipment and technologies in key areas and high technology fields, can we promote the transformation and upgrading of industries and move up the global value chain as soon as possible. This will not only help China to gain more commodity revenue, but also help to improve the effectiveness of China's OFDI. In addition, China's OFDI can also enrich the field dimension, transfer from secondary industry to tertiary industry, in order to feed the development of domestic service industry and promote the system reform and structural optimization of China's service industry.

5.3 Stimulate the Development of the Central and Western Regions

As the region with an average level of economic development in China at present, the central and western regions have a great potential for development. Therefore, we must increase the reform of the dual structure model of China's economy, stimulate the economic development of the central and western regions, and gradually narrow the gap with the more developed economic regions in the east, so as to improve the structure of China's OFDI, promote the construction of the marketization process, and narrow the gap between the economic development of provinces and cities.

6. Conclusions

A country's OFDI not only indicates the country's economic strength, but also plays a crucial role in the country's enterprise development and even socio-economic development. China, as the world's largest developing country, has accomplished rapid economic development in the past few years. At the same time, China's OFDI is also huge in volume. Through an in-depth analysis of the current situation of OFDI, we can find that its flow has gradually started a declining trend since 2017, and the investment situation in the east, middle and west regions vary greatly.

Combined with the relevant theories already put forward for direct investment in academia, the paper puts forward three policy recommendations: (1) Improve the level of technology and marketization in order to promote the release of OFDI flow potential. (2) Optimize the industrial structure and enrich the investment dimension in order to adapt to the development in the era of economic globalization. (3) Stimulate the development of the central and western regions, which are

the back-up force of China's future economic development and whose economic potential needs to be mobilized to narrow the differences between the east, central and west to balance economic development.

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