Are Chinese Firms Attracted to Political Risk? Locational Determinants of Chinese Outward Foreign Direct Investment

By: Grant DePoyster

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Sally McDonnell Barksdale Honors College

The University of Mississippi

University, Mississippi

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Approved by:

_____
Advisor: Dr. Nilufer Ozdemir

_____
Reader: Dr. Oliver Dinius

_____
Reader: Dr. Gang Guo

Abstract

This study evaluates the foreign direct investment (FDI) location choices made by Chinese firms from 1996 to 2015 and investigates the extent to which Chinese firms are attracted to investing in countries with high levels of political risk. Using new Chinese data, the study categorizes Chinese firms into Central State-Owned Enterprises and Other Chinese Firms to see the relationship between investment location and political risk for firms with varying levels of Chinese government control. Additionally, the data is divided between investments made from 1996 to 2003 and investments made from 1996 to 2015 to measure the effect that important changes in Chinese domestic policy in 2004 have had on the investment location choices of these firms. After conducting negative binomial regressions, the results show that these two types of Chinese firms have different attractions to political risk across different time periods. Central State-Owned Enterprises' FDI location choices are not significantly influenced by a country's political risk regardless of time period, but China's Other Firms change from being attracted to political risk prior to 2004 to being deterred by it after 2004. These findings show that changes to Chinese domestic policy and level of control by the Chinese central government can have a profound influence on Chinese firms' views towards political risk, and this reflects the larger ability of Chinese government intervention to enact change in Chinese firms and in the greater Chinese business environment.

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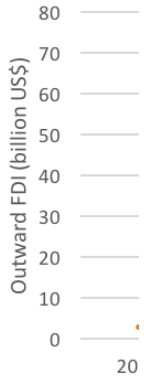
Introduction:

Over the past 30 years, no developing economy has been given as much attention by researchers, businesses, and governments as China. Long-standing economic growth has allowed it to rise on the world stage within a very short amount of time and establish itself as an economic powerhouse and a powerful political regime. During this rise, China's multinational firms have played an important role in helping facilitate this growth, and in particular, there has been a marked rise in outward foreign direct investment (OFDI) from Chinese firms. From 2003 to 2010, Chinese OFDI grew from $2.85 billion USD to $68.81 billion, rising to become 5.2 percent of total global OFDI.

Figure 1: China's Outward FDI Total, 2003-2010



Source: 2010 Statistical Bulletin of China's Outward Foreign Direct Investment

Multinational firms around the world engage in many types of trade that involve varying levels of intervention into local markets and contain distinct levels of inherent risk, but foreign direct investment (FDI) is an especially high risk, high reward form of

investment for multinational firms. While exporting, licensing, and franchising all allow a firm to enter foreign markets without investing in foreign factories or facilities, foreign direct investment (FDI) involves a firm directly owning and controlling facilities in a foreign country. There are three methods of FDI: building new facilities in a foreign country, buying existing assets in that country, or participating in a joint venture. Such FDI allows firms to have increased control over its international operations, acquire direct knowledge of foreign markets, and avoid tariffs and other barriers to investment that would affect goods being imported from overseas (Griffin and Pustay, 2015).

However, FDI also exposes a firm to greater economic and political risk. Firms engaging in FDI must meet the challenges of "operating, managing, and financing their foreign subsidiaries in a political, legal and cultural milieu different from their own" (Griffin and Pustay, 2015), and many countries restrict foreign FDI through direct controls on capital or banning intervention from foreign companies (Griffin and Pustay, 2015). Additionally, should the foreign country's exchange rates change adversely, the value of the firm's investments could deteriorate quickly (Chou, 2000). Firms engaging in FDI raise their profit capabilities but also open themselves to greater financial and political risk.

This study analyzes the relationship between Chinese OFDI in foreign countries and the political risk in those countries. Chinese OFDI stands out among that of other countries around the world for several reasons. Not only has the amount of Chinese OFDI risen at an unprecedented speed over the past twenty years as indicated in Figure 1, but the countries where Chinese firms have been investing in also do not often fit the standard profile for attractive FDI locations. Standard FDI theory states that countries

with large market sizes, stable political environments, and high economic growth strongly attract FDI (Chakrabarti, 2001); however, the regions where the bulk of China's OFDI has recently flown to are not generally characterized by these trends. Table 1 depicts the destinations of Chinese OFDI from 2003 to 2008, and it shows that over this period on average 91.87 percent of Chinese OFDI flowed into Asia, Latin America, and Africa instead of generally more economically developed and politically stable regions such as Europe and North America.

Table 1: Destinations of Chinese OFDI by Region, 2003-2008

Year	Destination of OFDI flow (%)					
	Asia	Latin America	Africa	Europe	North America	Oceania
2003	52.5	36.5	2.6	5.3	2.0	1.1
2004	54.6	32	5.8	3.1	2.3	2.2
2005	35.6	52.6	3.3	4.2	2.6	1.7
2006	43.5	48.0	2.9	3.4	1.5	0.7
2007	62.6	18.5	5.9	5.8	4.3	2.9
2008	77.9	6.6	9.8	1.6	0.6	3.5
Average	54.44	32.37	5.06	3.9	2.21	2.02

Source: Statistical Bulletin of China's Outward Foreign Direct Investment, 2003-2008

This highlights the uniqueness of Chinese OFDI and poses interesting questions as to why Chinese firms are choosing to invest in countries and areas with seemingly higher political risk. One would assume that a country with high political risk would not give investors an incentive to invest due to a higher risk on their investments; however, credible studies support this observation that political risk does not affect Chinese firms in the conventional way, and some studies even claim that Chinese OFDI is attracted to political risk (Buckley et al., 2007; Kolstad and Wiig, 2010; Quer et al., 2012).

This study plans to have four contributions to the empirical literature. First, it contributes new data to analyze Chinese OFDI's seeming indifference to host country political risk. Due to scarcity of data on Chinese firms and the relatively short period since China's boom in investment began, this new data could be valuable in helping build on the results of past literature. Second, it tests the effect that changes in domestic Chinese policy in 2004 have had on the determinants of Chinese OFDI. Finally, it analyzes the effect that political risk has on Chinese OFDI for both Chinese firms controlled by the central government and those not controlled by the central government.

Previous Literature:

Previous Literature on Chinese OFDI:

Much of the empirical literature already conducted on host-country determinants of Chinese OFDI has adopted a typology provided by Dunning (1977) which classifies OFDI according to four investment motivations: market-seeking investment looking to enter new markets; resource-seeking investment in search for natural resources; strategic asset-seeking investment to enhance the firm's intellectual property; and efficiency-seeking investments to reduce overall costs (Dunning, 1977). Those studies have shown evidence supporting that the first three of Dunning's investment motivations are significant in determining OFDI patterns of Chinese firms, and they have shown that China's OFDI stands out from those of most other countries (Buckley et al., 2007; Kolstad and Wiig, 2010).

Among these investment motivations, natural resources have been shown to be an especially significant determinant of Chinese OFDI, and the interaction between host country political risk and natural resource endowment has also been found to be significant (Buckley et al., 2007; Cui & Jiang, 2009; Kolstad and Wiig, 2009; Ramasamy et al., 2012). Host country market size and distance are two factors that are widely recognized in economic literature to influence the flow of FDI received by a country (Chakrabarti, 2001; Mascarenhas, 1992), and this has also been found to be a significant determinant of Chinese OFDI (Buckley et al., 2007).

Other studies have also analyzed the effect that a Chinese firm's specific industry has on the determinants of China's OFDI. They have concluded that Dunning's

investment motivations have different degrees of prevalence in different Chinese industries such as manufacturing, service and primary services (De Beule and Duanmu, 2012; Amighini, 2013). Chinese firms also display different investment behaviors between developed and developing countries (Cheung and Qian, 2009), and the large role that the Chinese government plays in China's multinational corporations has been studied and shown that the determinants of OFDI for state-owned firms often differ from those of privately-owned ones (Ramasamy et al., 2012).

Defining Political Risk:

Another important influence on the investment behaviors of Chinese firms is the level of political risk in each country. Political risk is considered to be "any changes in a country's political environment that may adversely affect the value of a firm's business activities." (Griffin and Pustay, 2015). This broad definition can encompass macropolitical risk that affects all firms in a country or micropolitical risk that only affects specific firms. Civil wars, for example, cause the destruction of property, disruption of production, and loss of sales for almost all firms in a country whereas tightened regulations on a country's manufacturing industry will only directly affect those firms investing in that industry.

To multinational firms engaging in FDI, political risk can greatly alter the environment in which a firm operates. For example, minimum wage laws affect the price a firm must pay for labor and environmental protection laws affect the technology a firm can use. Moreover, the extent to which a country adheres to these laws or can restrict unlawful business practices can also have a profound impact on the way a firm operates.

In this way, the decision for a firm to invest in one country over another can be heavily dependent on the strength of that country's political institutions and the perceived level of political risk.

With so many factors that contribute to a country's overall political risk, it is difficult to accurately quantify political risk. Each country has different laws and regulations, levels of corruption, political backgrounds, etc. that create a unique political environment for every country. However, many previous studies which analyze political risk use the quality of a country's political institutions as a proxy for level of political risk. A country's political institutions consist of the organizations which create and enforce laws and regulations. Like a referee in a sports match, these institutions "establish the rules of the game that structure interactions, and organizations are the players limited by these rules, which can be both formal—laws and regulations—and informal—customs, traditions, or codes of conduct." (North, 1990).

Previous studies have represented quality of political institutions and level of political risk with data from the World Bank's Governance Indicators (Ramasamy et al., 2012). These consist of six broad measures of host country political risk: Voice and Accountability, Political Stability and Absence of Violence/Terrorism, Government Effectiveness, Regulatory Quality, Rule of Law, and Control of Corruption. This study also utilizes these indicators to represent political risk, and the details regarding the specific implementation of these indicators in the model can be found in the Data and Model section.

When political institutions necessary for well-functioning markets are not well structured or enforced, this increases the cost of doing business in that country (Blongien,

2005). Additionally, the uncertainty and inherent risk associated with owning and operating a foreign subsidiary can also deter firms from engaging in FDI (Brouthers, 2002; Pak and Park, 2004). Therefore, it generally understood that increased political risk diminishes FDI activity (Chakrabarti, 2001). This study specifically analyzes the relationship between political risk such as this and the location of Chinese OFDI.

Influence of Political Risk on Chinese OFDI:

Some analyses on the determinants of Chinese OFDI support this conventional wisdom that as a country's political risk increases Chinese OFDI into that country decreases. For the case of Chinese firms, Duanmu and Guney (2009) found that Chinese FDI is attracted to countries with good political environments and especially those with open economic regimes (Duanmu and Guney, 2009).

However, many other studies have shown that political risk does not affect Chinese firms in a conventional way, often being attracted to political risk rather than deterred by it (Buckley et al., 2007; Ramasamy et al., 2012; Quer et al., 2012). Researchers claim that since other multinational firms from developed countries have already invested heavily abroad in the past, Chinese multinational firms are, "latecomers on the world stage." (Mathews, 2006). This combined with China's rapid economic growth has led its firms to seemingly skip certain stages of the internationalization process (Luo and Tung, 2007). This has caused Chinese firms to lack ownership advantages in these skipped stages such as access to natural resources and engage in OFDI in order to, "augment the ownership advantages that they lack." (Ramasamy, et al., 2012). They claim that the desire to augment such ownership advantages is so strong that they are "willing to adopt

aggressive, high risk [OFDI] targets." (e.g. Sudan, Dem. Rep. of the Congo, etc.) (Ramasamy et al., 2012). Others also propose that China's state-owned enterprises (SOEs) could utilize their advantages in the Chinese domestic market to get greater access to funds and allow them to invest in riskier locations (Buckley et al., 2007). Chinese multinational firms exist in a market with very unique features that could create an environment where Chinese firms contradict conventional wisdom and are attracted OFDI in high political risk countries.

China's "Go Global" Strategy:

In order to fully understand the political and economic environment surrounding Chinese multinational firms, the liberalization of China's OFDI policy needs to be taken into account. The process of China's OFDI policy liberalization can be traced through China's "走出去" or "Go Global" strategy, which was formally instigated in 1999 (Buckley et al., 2007; Luo et al., 2009). This initiative aims to encourage Chinese firms to engage in OFDI by reducing obstacles to international investment (Sauvant, 2005).

The true foundation of this "Go Global" ideology and strategy began with the institution of Deng Xiaoping as China's leader in the late 1970's and the subsequent Chinese economic reform (改革开放) of the 1980's. Deng believed that ensuring China's long-term success depended on a balance between maintaining centralized control of the country by the socialist central government and liberalizing trade relations with other countries. Deng stated that, "if China does not uphold socialism and does not uphold economic reform, then it can only go down the road to disaster." (Deng Xiaoping, 1992) (不□持社会主□，不□持改革开放，只能是死路一条). He pioneered the Chinese ideals of

foreign trade and investing in other countries, and in pursuing this road to success, he began the Chinese economic reform in the 1980's which slowly began increasing China's trade with other countries.

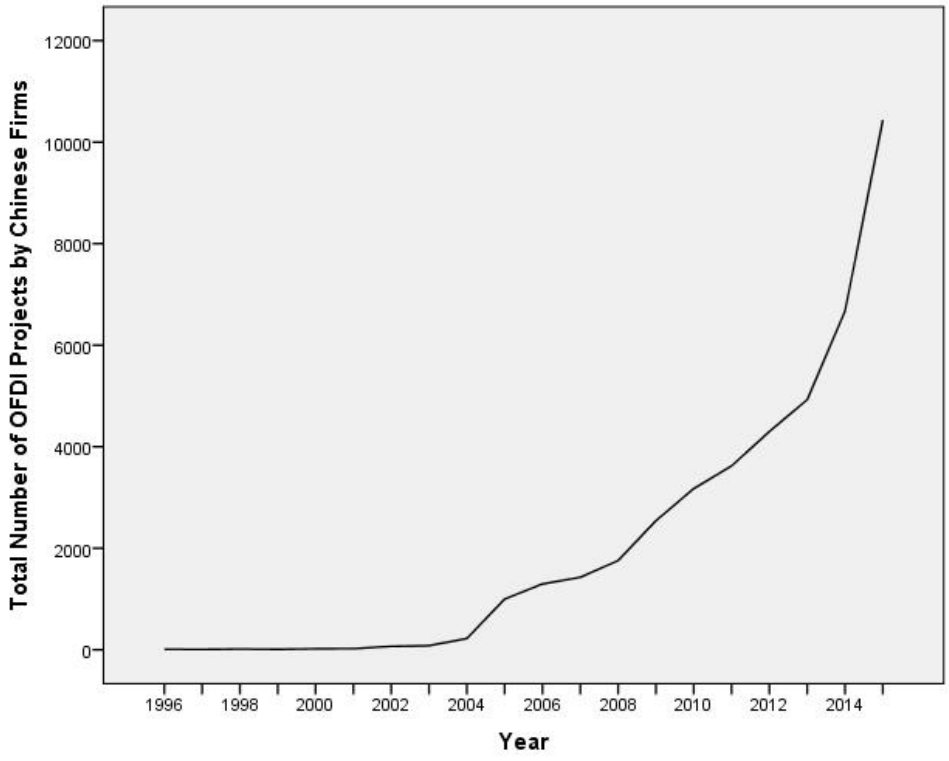
While Deng gave birth to China's "Go Global" ideology, it was not actually implemented as a government strategy until the 1990's under the leadership of China's next president Jiang Zemin. He set into motion two policies with regards to Chinese FDI, the "引□来" or "Bring Inward" and "走出去" or "Go Global" strategies. These policies were meant to both encourage foreign FDI into China and encourage OFDI from China to other countries. At the Chinese National Conference of Foreign Investment in 1997, Jiang emphasized these policies saying that "China does not only need to attract foreign companies' investments to China, but it also must lead and organize powerful domestic companies to invest abroad." (我□不□要□极吸引外国企□到中国来投□□厂，也要□极引□和□□国内有□力的企□走出去). These government goals aided in bringing foreign investment into China and posed outward FDI as important to China's future growth.

Finally, China's "Go Global" strategy truly took flight in 2004 when it went from being a government goal to a nationally implemented policy. During this time, the "Bring Inward" and "Go Global" policy strategies became important parts of a larger liberalization of China's laws pertaining to OFDI. Following the Sixteenth Communist Party Congress in October 2003, the Chinese government published a report called "Decision of the Communist Party of China on Issues Concerning the Improvement of the Socialist Economic System." In this report, it was detailed that, "the 'Go Global' strategy will be implemented to improve outward investment, to give Chinese firms more power to make their own management decisions…and promote the development of all

Chinese firms." (Central Government of China, 2003). This report signals an important turning point in the Chinese government's support for outward investment and helped promote huge surges in Chinese OFDI in the years following 2004.

Figure 2 reflects this surge of Chinese outward investment following the implementation of the "Go Global" strategy, showing how the total number of OFDI projects begun by Chinese firms went from only several hundred in 2003 to over 1000 in 2005 and eventually rising to over 10,000 in 2015.

Figure 2: Total Number of OFDI Projects by Chinese Firms, 1996-2015



The success of the "Go Global" strategy in increasing the amount of China's investments abroad can largely be attributed to how this strategy made engaging in international investments easier for Chinese firms. Through this strategy, the Chinese government transformed from a regime that directly intervenes in OFDI decisions and

commands business outcomes to a state that directs the market through a wide set of administrative bodies (Bach, Newman, and Weber, 2006). In doing so, OFDI approval processes were simplified, an information bank was established to provide guidance for firms' overseas investments, and the institution of firm annual reports allowed for the government to better monitor obstacles to companies engaging in OFDI (Luo et al., 2009).

These changes to China's OFDI process increased the relative ease for firms to independently engage in OFDI. While firms currently need to report and confirm their investments with the central government, their investment decisions are no longer as tied to national economic imperatives set by the central government that might have previously pushed firms to engage in investments that were risky and not profit-maximizing (Buckley et al., 2007). Also, the "Go Global" and "Bring Inward" strategies increased the ability for firms to make more informed, profit-maximizing decisions on their investments. In addition to the greater resources provided by the Chinese government for providing investment guidance, firms have greater access to foreign companies that can also provide investment advisory services. The development and implementation of China's "Go Global" strategy greatly changed China's business environment by making it easier for domestic firms to make investments abroad.

Increased Chinese Firm Privatization:

Just as China's domestic OFDI policy has gradually changed and influenced Chinese firms' business environment, the types of firms that exist in China have also greatly changed and have adapted the way that Chinese firms invest abroad.

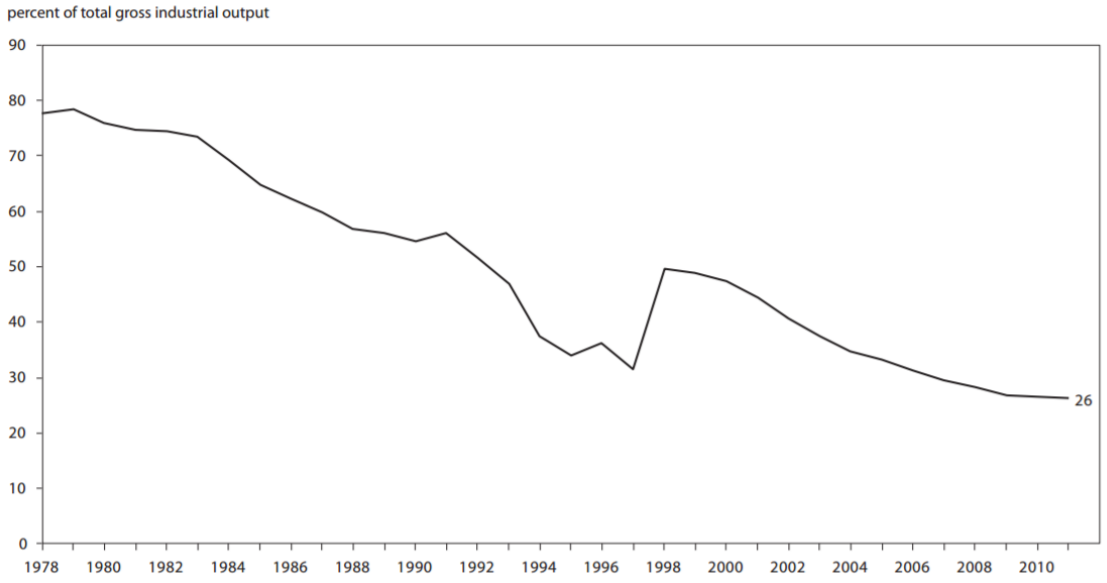
Following China's Cultural Revolution in the late 1970's, the vast majority of

Chinese firms were wholly owned by the Chinese central government, and China's private sector was insignificant in comparison. In fact, the share of private sector employment out of China's total national employment in 1981 was less than 2 percent (World Bank, 2000). Additionally, after OFDI was formally permitted during the 1980's economic reform, "the internationalization of Chinese firms was still tightly controlled by the Chinese national and provincial governments, either directly, by fiat, or indirectly via economic policy." (Buckley et al., 2007). The clear dominance of state-owned enterprises in China's domestic and international markets alludes to the fact that any OFDI conducted during the 1980's was likely conducted by state-owned enterprises or given official endorsement by the Chinese central government.

However, in recent years the Chinese government's administrative controls have been relaxed. Up until the early 1990's China's state-owned enterprises (SOEs) were wholly owned by the central Chinese government; however, in 1995 China adopted the "grasp the large and let go of the small" SOE reform policy (Ralston, 2006). This policy allowed for some of China's small, local SOE's to be sold to private individuals, beginning the process of firm privatization. Subsequently, in 1999, "private ownership and the rule of law were incorporated into the Chinese constitution." (Ralston, 2006). As laws against privatization of firms were slowly liberalized, China's private sector began growing at an incredible rate. Between 1991 and 1997, the number of Chinese private firms grew at an annual rate of 46 percent, employment in these firms grew at 41 percent, and the value of their output grew at 71 percent (World Bank, 2000). Then, in March 2004, firms' "private assets and capital were finally legalized and protected under the country's constitution." (Ralston, 2006).

Today, China's private sector has grown to become as integral a part of the Chinese economy as the state-owned sector. For example, the share of China's state enterprises in many industries has been reduced significantly to make way for the rise of private firms. Figure 3 shows how the share of Chinese state enterprises in gross industrial output has fallen from over 75 percent in 1978 to 26 percent in 2011. Similarly, in 1980 state-owned firms accounted for around three-quarters of the value of China's construction sector, but by 2010, the share of construction value contributed by the state had fallen to less than 40 percent, the rest undertaken by private and foreign firms (Lardy, 2014). Along with the development of the "Go Outward" strategy, Chinese firm privatization has grown at an incredible rate, and the private sector's contribution to China's total economic output and OFDI has increased significantly.

Figure 3: Gross Industrial Output of Chinese State Enterprises, 1978-2011



Notes: Data include only above-scale firms, with sales greater than RMB5 million (1998–2011) and firms with sales greater than RMB20 million (beginning in 2011). This data series appears to have been discontinued.

Source: Lardy, N. (2014). *Markets over Mao: The rise of private business in China*.

Effects of Financial Crises on Chinese OFDI:

Various financial crises which have occurred globally from the 1990's to present day have also had direct and indirect impacts on Chinese OFDI. During the Asian financial crisis of 1997, widespread policy changes occurred in China where OFDI approval procedures became increasingly strict and each OFDI project was subject to a screening and monitoring process (Wong and Chan, 2003). This crisis served as a catalyst for OFDI reform during the 1990's and limited the opportunities for firms engaging in OFDI.

However, other financial crises around the world have conversely created opportunities for Chinese international investment. Following the global financial crisis in 2008, with US$ 1.9 trillion in foreign-exchange reserves and a current account surplus, Chinese multinationals had the opportunity to cheaply acquire market share and brands in the developing world through outward investments (Davies, 2009). Also, this economic crisis triggered a "new wave of organizational restructuring for Western companies which urgently needed liquid capital to fund their operations." (Luo et al., 2009). This generated more opportunities than before for emerging Chinese multinational firms to venture abroad through mergers and acquisitions. The 2008 financial crisis helped enable emerging Chinese multinationals to acquire cheap assets in developed countries and obtain a foothold in those markets. Global financial crises have promoted the development of Chinese OFDI both through direct policy changes and indirect cheapening of foreign assets.

New Types of Chinese Firms:

With China's "going global" policy towards international trade, the increasing importance of its private sector, and the effects of global financial crises, the entities and people who own Chinese companies have become much different than they were several decades ago. While in the 1970's only the central government or extensions of the central government could own companies, today Chinese firm ownership structures are much more complex. These differences in firm ownership structures are very important to account for in properly understanding what influences Chinese OFDI. Previous studies have shown that the investment decisions of state-owned firms and private firms are often different where private firms are found to be more market-seeking (Ramasamy et al., 2012). Also, the financial performance of Chinese firms often differs based on ownership type (Chen et al., 2009), and firms that are more successful are generally better equipped to make international investments. Therefore, who owns and operates a Chinese firm can have a significant influence on how that firm engages in OFDI.

To summarize who owns and controls Chinese companies today, the Chinese government currently allows for six types of shares in a listed Chinese company: state, legal person, individual, foreign, management, and employee shares (Chen et al., 2009). However, the first three types of shares constitute the vast majority and are generally controlled by four different types of shareholders:

1. *State asset management bureaus (SAMBs)*

   SAMBs are shareholding institutions that belong to the state. They appoint the board of directors and managers of the firm, collect the earnings, and transfer them directly to the state treasury (Ramasamy et al., 2012).

2. *SOEs affiliated with the central government (Central SOEs)*

Central SOEs refer to the 157 SOEs controlled directly by the central government's State-owned Assets Supervision and Administration Commission (SASAC). These SOEs belong to and are strictly monitored by the central government.

3. *SOEs affiliated with local governments (Local SOEs)*

   Local SOEs are SOEs controlled directly by a local provincial or county government. These firms constitute the largest group of controlling shareholders of listed firms in China (Chen et al., 2009).

4. *Private investors (Private)*

   PIs include both private firms and individual shareholders.

These shareholders constitute the four main ownership types of Chinese firms. However, since the OFDI undertaken by firms controlled by the first type of shareholder (SAMBs) are mainly affiliated with the firm's local government (Ramasamy et al., 2012), SAMBs can be merged with Local SOEs to create the three main types of firm ownership: Central SOE, Local SOE, and Private.

Classification of Chinese Firms in This Study:

To account for the potential differences in OFDI trends between these distinct types of Chinese companies, this study groups Chinese firms based on the ownership structure detailed above and on level of supervision by the central government. Due to their direct control by the SASAC, Central SOEs are the most tightly state-controlled firms in China. Their chairmen are carefully chosen by the central government and they are subject to close monitoring from central government offices such as the Chinese National Audit Office (Chen et al., 2009). Therefore, Central SOEs are expected to adhere more so to the central government's plans of acquiring strategic assets and their OFDI determinants could be influenced as a result.

On the other hand, Local SOEs and Private firms do not have such stringent monitoring and state control. While Local SOEs are still managed by China's local governments, laws, regulations, and supervision are "more difficult to enforce the further away the parties are from China's center of power," and Local SOEs are allowed to independently make investment decisions, create their own policies, and establish their own organizational hierarchies (Chen et al., 2009). Private firms are not subject to such direct monitoring by the state; thus, their investment decisions are similarly independent and their goals are aimed more towards profit maximization. Due to their relative independence from direct central government control, this study combines Local SOEs and Private firms into one group labeled "Other Firms" and compares them to Central SOEs.

Hypotheses:

Attraction to Political Risk:

Given the mixed results of previous studies regarding Chinese OFDI and its relationship to political risk, this study plans to contribute to the empirical literature by testing this relationship as well. Utilizing new data on Chinese OFDI (see page 18), I propose that Chinese OFDI is attracted to host country political risk due to the Chinese government's powerful desire to acquire strategic resources which might be located in countries with high political risk.

Hypothesis 1: Chinese OFDI is attracted to host country political risk.

Changes to Chinese Domestic Policy:

The changes brought by China's "Go Global" strategy in 2004 allowed for Chinese firms to engage in more profit-maximizing and less risky investment decisions, and I propose that this will cause Chinese firms to be less attracted to political risk following these changes in 2004.

Hypothesis 2: Chinese firms will be less attracted to political risk after 2004.

Different Chinese Firms Have Different Attractions to Political Risk:

I argue that China's changing firm ownership structures and the difference in level of state control between Central SOEs and Local SOEs/Private firms could reflect different OFDI patterns and different attractions to political risk. I predict that due to Central SOEs close monitoring by the central government, they will be attracted to political risk across all years of the study in order to conform to the larger national plans

of the Chinese government to acquire natural resources. However, I believe that due to the relative independence of Other Firms from central government control, their investment will be more profit-maximizing and less attracted to host countries with high political risk.

Hypothesis 3a: Chinese Central SOEs will be attracted to political risk across all years of the study.

Hypothesis 3b: China's Other Firms will not be attracted to political risk after 2004.

Data and Model:

The sample for this study is based on a firm-level dataset downloaded from the Chinese government's Department of Outward Investment and Economic Cooperation website located at http://fec.mofcom.gov.cn/. This dataset contains 41,716 approved overseas investments made to 192 countries by Chinese firms between 1983 and 2015, and it contains valuable information including the destination country, name of the Chinese investor, name of the affiliate firm or branch, function of each affiliate firm, regional origin of each investor, and approval date of OFDI. The regional origin of each investor is also classified into 31 different provinces or economic zones, 5 cities, and Central State-Owned Enterprises (中央企业 in Chinese).

The inspiration for using this dataset largely came from analysis of a study conducted by Marukawa et al. (2014) of the University of Tokyo which used the same dataset to, "clarify the reality of China's OFDI on the basis of official approval information." (Marukawa et al., 2014). Publicly available data on Chinese investments is very limited, and while the Chinese government releases an annual "Statistical Bulletin of Chinese Outward Foreign Direct Investment," the data made available in these Bulletins concentrates more on overarching industrial and global trends than on country-level statistics. Like the study conducted by Marukawa et al. (2014), this study utilizes statistics from China's Department of Outward Investment and Economic Cooperation which go further into detail regarding each investment's target country, the name of the investor, the name of the subsidiary, and why each investment was made. This data provides a clearer picture about the nature of Chinese OFDI. Additionally, this data spans

from 1983 to 2015 which goes from when Chinese OFDI began to almost current day. Other studies analyzing political risk's relationship with Chinese OFDI do not use data with such a long time period; therefore, this data could more accurately portray the overall investment behaviors of Chinese firms.

Dependent Variables

Using the firm-level data included in this dataset, two country-level dependent variables were created for analysis. First, the total number of investments made into each country for each year was compiled from 1996 to 2015. Although the investments from 1983 to 1995 were not included in the analysis, these investments account for approximately 0.2% of the dataset's total investments and therefore do not have a significant impact on the analysis.

This new country-level data represents the total amount of Chinese OFDI into a given country for each year. Then, this total OFDI was separated into two categories based on regional origin of the investor: OFDI by Central State-Owned Enterprises and OFDI by all other firms. These represent the amount of OFDI by Central SOEs and the amount of OFDI by all other firms into a given country for each year. These two variables, CentralOFDI and OtherOFDI, serve as the dependent variables in the analysis.

Independent Variables

The study includes several host country independent variables that influence FDI location choice by global and Chinese firms. Host country market size and distance are two factors that are widely recognized in economic literature to influence FDI

(Chakrabarti, 2001; Mascarenhas, 1992). Host country real GDP is used in this study to control for market size, and distance is measured by distance in kilometers between China's capital of Beijing and each host country's capital (Real GDP and Distance in Table 2, respectively). Membership in the Organization for Economic Cooperation and Development (OECD) is also used to delineate between developed and developing countries (OECD_dummy in Table 2). Moreover, Chinese OFDI is often directed towards the acquisition of information and knowledge such as advanced technology or intellectual property (Buckley et al., 2007). Host country technological innovation is represented by the number of total patent applications in the host country (Patents).

Based on previous studies (Ramasamy et al., 2012), host country political risk was represented by the World Bank's Governance Indicators which consist of six different measures of host country political risk: Voice and Accountability, Political Stability and Absence of Violence/Terrorism, Government Effectiveness, Regulatory Quality, Rule of Law, and Control of Corruption. These six aggregate indicators are based on 31 underlying data sources reporting the perceptions of governance of a large number of survey respondents and expert assessments worldwide (Kaufmann et al., 2010). All six indicators denote values from approximately -2.5 to 2.5 for each country annually where low values represent weak government performance and high values represent strong government performance. Due to the highly correlative relationships between these six indicators, the Rule of Law indicator was selected as the measure of political risk in this study to avoid problems of heterogeneity in the results (PolRisk).

Host country natural resource endowment has also been shown to have a significant influence on Chinese OFDI location choice (Buckley et al., 2007; Quer et al.,

2011; Ramasamy et al., 2012); therefore, host country ore and metal exports (% of total merchandise exports) are used to proxy host country natural resource endowment (OreExports). Additionally, political risk and ore and metal exports have been found to have a significant interaction (Kolstad and Wiig, 2012; Ramasamy et al., 2012). A similar interaction variable is used between political risk and ore and metal exports as used in their study, labeled as OreRiskInteraction.

Many host country economic factors have also been shown to influence Chinese OFDI determinants. Volatile and unpredictable inflation rates in host countries, "discourages market-seeking FDI by creating uncertainty and by making long-term corporate planning problematic…" (Buckley et al., 2007). Host country annual inflation rate (Inflation in Table 2) is used to account for the effect of inflation on FDI location choice. "As home country exchange rate appreciates, more profitable opportunities for outward FDI occur since foreign currency denominated assets become cheaper." (Buckley et al., 2007). Using host country annual change in exchange rate, this is accounted for in the analysis. Another economic indicator that can influence OFDI is current account balance as it reflects the likelihood of a country to be approaching a financial crisis (Current Account). For current account balance, negative values denote a current account deficit and positive values denote current account surplus, and when a country's current account balance reaches approximately -5 percent, it is indicative of an approaching financial crisis in that country (Croke et al., 2005; Obstfeld and Rogoff, 2005).

Finally, in order to test the difference between Chinese firms' OFDI determinants before 2004 and those spanning all years in the study, Pre2004_dummy is included as an

independent variable. The other independent variables listed in Table 2 are also multiplied by Pre2004_dummy to create new interaction variables. These new variables indicated in Table 2 by Pre2004* "x" include: Pre2004_RealGDP, Pre2004_Distance, Pre2004_Inflation, Pre2004_Patents, Pre2004_PolRisk, Pre2004_OECD, Pre2004_OreAndMetal, Pre2004_OreRiskInt, Pre2004_CurrentAccount, and Pre2004_ExRateChange. By including these 10 interaction variables, the effects on Chinese firms' OFDI before 2004 can also be seen.

Table 2: List of Variables and Sources

Variables	Description	Source
CentralOFDI	Count of Central SOE OFDI	China's Ministry of Commerce
OtherOFDI	Count of Other Firm OFDI	China's Ministry of Commerce
RealGDP	Host country's Real GDP (US$, constant)	World Bank Development Indicator
Distance	Distance between China's capital and the host country's capital	CEPII
Inflation	Host country's rate of inflation (annual %)	World Bank Development Indicator
Patents	Host country's total patent applications	World Intellectual Property Association
OECD_dummy	Dummy variable coded as OECD member = 1, non-OECD member = 0	World Bank's Governance Indicators
Pre2004_dummy	Dummy variable coded as OFDI before 2004 = 1, after 2004 = 0	
PolRisk	Rule of Law- A measure of the political stability of host country	World Bank's World Governance Indicators
OreAndMetal	Host country's ore and metal exports (% of total merchandise exports)	World Bank Development Indicator
OreRiskInt	Interaction variable of "OreExports" and "PolRisk"	World Bank Development Indicators
CurrentAccount	All transactions other than those in financial and capital items (% of GDP)	IMF World Economic Outlook
ExRateChange	Host country's percent annual change in exchange rate	World Bank Development Indicator
Pre2004 * "x"	Represents the interaction between "Pre2004_dummy" and each of the independent variables listed above	

Descriptive Statistics:

Table 3 depicts the descriptive statistics of each independent variable used in the study including the number of occurrences (N), minimum value (Min), maximum value (Max), average of all of the values (Mean), and standard deviation (Std. Dev.).

Table 3: Descriptive Statistics

Variables	N	Min	Max	Mean	Std. Dev.
RealGDP	3112	2.801 E8	2.533 E13	3.572 E11	1.3822 E12
Distance	3720	809.5	19297.5	8970.5	3858.61
Inflation	3126	-35.8	24411.0	18.496	444.14
Patents	2072	1	589410	13007.3	57393.5
OECD_dummy	3838	0	1	.17	.373
PolRisk	3006	-2.40	2.12	-.0288	.98530
OreAndMetal	2842	0	86.42	8.33	14.428
OreRiskInt	2339	-101.1	98.22	.3146	13.702
CurrentAccount	3473	-112.9	51.11	-2.52	11.078
ExRateChange	2985	-0.32	694043.8	234.93	12703.8
Pre2004_dummy	3920	0	1	.40	.490
Pre2004_RealGDP	3532	0	2.53 E13	1.22 E11	8.61 E11
Pre2004_Distance	3840	0	19297.5	3476.1	4987.34
Pre2004_Inflation	3568	-16.12	4145.1	5.7835	74.8068
Pre2004_Patents	3139	0	440248	2952.3	25904.4
Pre2004_PolRisk	3228	-2.23	1.97	-.0080	.51533
Pre2004_OECD	3888	0	1	.0628	.24256
Pre2004_OreAndMetal	3473	0	78.40	2.3693	8.36893
Pre2004_OreRiskInt	3030	-75.12	75.87	-.0489	5.38238
Pre2004_CurrentAccount	3713	-112.93	49.98	-1.058	6.24004
Pre2004_ExRateChange	3688	-0.28	6882.2	2.0132	116.46

A few interesting conclusions and outliers can be determined from the descriptive statistics. First, based on the mean of OECD_dummy, only 17 percent of countries from 1996 to 2015 classify as OECD countries, but the mean of Pre2004_OECD shows that before 2004 only 6.28 percent of countries were OECD members. Second, the maximum value for Inflation is 24,411 percent inflation and the maximum value for Exchange Rate Change shows an annual currency depreciation of 694,043 percent. Both of these extremely high values stem from the data for Zimbabwe in 2007 who experienced a severe currency crisis in that same year that brought about unforeseen inflation and exchange rate depreciation. Finally, the minimum value of Current Account Balance is a very low -112.9 percent and the maximum value is a very high 51.11 percent. This minimum value comes from Equatorial Guinea in 1996 which suffered economically until the discovery and exploitation of oil fields in the late 1990's that propped up its economy. The maximum value is that of Libya in 2006 whose oil-dominated economy allowed for it to maintain such a high current account surplus.

Model: Negative binomial regression

Since the dependent variables in this analysis are the number of approved Chinese overseas investments per country per year, the data is classified as count data, and a widely-used model for analyzing count data is the negative binomial regression model.

The economic theory behind negative binomial regressions is based on data that follows a "Poison distribution." A random variable Y is said to have a "Poison distribution" with parameter μ if it can take the values 0, 1, 2,… with probabilities of the following expression

$$\Pr[\mathrm{Y} = \mathrm{y}] = \frac{e^{-\mu}\mu^{y}}{y!}, y = 0, 1, 2, \ldots$$

where μ is the observable expected (mean) rate of occurrences and the first two moments are

$$E[Y] = \mu$$

$$Var[Y] = \mu$$

It can be seen above that a critical assumption of Poisson distributions is that the mean and the variation of the distribution are equal, or E[Y] = V[Y] = μ (Cameron and Trivedi, 2007). Negative binomial models also specifically assume that the parameter μ is random, rather than being totally determined by a set of x variables. In such cases, the first two moments of a negative binomial distribution are instead

$$E[Y|\mu, \alpha] = \mu$$

$$Var[Y|\mu, \alpha] = \mu(1 + \alpha\mu)$$

where α denotes the function of non-observable heterogeneity in the count data. Therefore, the variance exceeds the mean in a negative binomial distribution since $\alpha > 0$ and $\mu > 0$ (Cameron and Trivedi, 2007). In this way, the negative binomial model serves

as an effective model for analyzing how variables can influence count data that is affected by overdispursion and unknown, unobservable factors.

Understanding the economic theory behind the negative binomial regression model, it was determined that this model was best suited for conducting the analysis in this study. Due to large variance in the data, the data is overdispersed. Overdispursion occurs when a data set has greater variability than normally expected in a given model. In the data used in this study, this likely occurs since certain countries such as Hong Kong and the United States receive greatly more OFDI projects from Chinese firms than most other countries. This creates the existence of outliers in the data that can skew the results of the regression. Recall that negative binomial models are specifically designed to account for count data than is overdispersed; therefore, a negative binomial regression is used for the analysis in this study.

Results and Discussion:

Table 4a shows the results of the negative binomial regression without the Pre2004 interaction variables included.

Table 4a: Original Results

Variables	(1) Central SOE			(2) Other Firms		
	β	Std. Error	Exp(B)	β	Std. Error	Exp(B)
Intercept	.006	.1693	1.006	3.029***	.1296	20.68
RealGDP	3.975 E-13***	5.3040 E-14	1.000	7.115 E-13***	5.898 E-14	1.000
Distance	.000***	1.1894 E-5	1.000	.000***	8.873 E-6	1.000
Inflation	-.040***	.0088	.960	-.036***	.0073	.964
Patents	-3.404 E-6**	1.2705 E-6	1.000	-4.185 E-6***	1.004 E-6	1.000
PolRisk	.085	.0632	1.089	.146**	.0492	1.157
OECD_dummy	1.226***	.1323	3.408	.632***	.0988	1.882
OreAndMetal	.026***	.0029	1.026	.033***	.0026	1.034
OreRiskInt	.026***	.0035	1.026	.039***	.0036	1.040
CurrentAccount	.007	.0048	1.007	.015***	.0041	1.015
ExRateChange	2.870***	.3892	17.63	2.358***	.2841	10.57

Dependent Variables: (1) Central SOE OFDI, (2) Other Firms OFDI- Sum of Local SOE and Private OFDI

ϕ $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Control Variables:

Of the control variables found to be significant in the original results shown in Table 4a, many confirm the findings of previous studies on Chinese OFDI. Host country Real GDP and distance from China are found to be significant for both types of firms at the 1% level. This is consistent with standard economic gravity theories regarding market size and distance which state that the larger a country's market size and the closer a

country is to the investor, the more likely that investor is willing to invest in that country (Chakrabarti, 2001). This potentially explains the phenomenon observed in Table 1 where from 2003 to 2008 the majority of Chinese OFDI was made into countries in Asia. The distance between China and other Asian countries is comparatively small and many of them have large market sizes such as Japan and Hong Kong; therefore, Chinese multinational firms would be very attracted to investing in Asia.

Total patent applications (Patents in Table 4a) is also found to be significant for both types of Chinese firms. Previous studies have claimed that Chinese firms could be attracted to investing in countries that are more technologically innovative and developed than China itself (Ramasamy et al., 2012). Many global firms invest in countries with better technologies than those domestically available to learn from foreign firms and bring that more advanced technology back to their home country (Griffin and Pustay, 2015). This is especially important in today's technologically advanced world where advanced machinery can greatly reduce the total cost and required labor for a firm to create its products. The number of total patent applications is often used to represent the level of a country's technological innovation, and the results in Table 4a show that technological innovation is significant in determining FDI location choice for both Chinese Central SOEs and Other firms. However, the coefficient for both variables is very small, meaning that while it is significant, technological innovation does not have a substantial influence on Chinese firms in choosing investment locations.

Host country natural resource endowment (OreAndMetal) is also found to be significant and positive for both types of firms, supporting theories that Chinese OFDI is attracted to countries with access to abundant natural resources (Buckley et al., 2007;

Ramasamy et al., 2012). In recent years, there has been increasing amounts of research dedicated to understanding Chinese OFDI in Africa as well as in other developing countries, and one of the central points brought up by these researchers to explain this phenomenon is that African countries export relatively large quantities of natural resources (Teunissen and Akkerman, 2006). The strong relationship between Chinese OFDI and natural resources is supported by the results, and this could help explain Chinese firms' relative interest in investing in Africa.

Some studies have also found that in addition to being attracted to countries which export many natural resources, Chinese firms are also attracted to countries that both endowed with natural resources and politically risky (Ramasamy et al., 2012; Kolstad and Wiig, 2010). These studies claim that the higher the level of political risk is in a country, the more likely Chinese OFDI is being attracted due to the natural resources in that country (Kolstad and Wiig, 2010). This study also tests for such with the interaction variable between natural resource endowment and political risk (OreRiskInteraction). This variable is significant and positive for both types of firms, supporting the results of these past studies which found that Chinese OFDI is attracted to countries that are both endowed with natural resources and have high levels political risk.

With regards to Chinese OFDI's relationship with approaching financial crises, the results confirm previous studies and conventional wisdom. Current account balance (CurrentAccount) is used to measure a country's likelihood of approaching financial crisis where negative values indicate approach towards financial crises. Countries approaching financial crises would not seem to be attractive locations for FDI since, in the event of a financial crisis occurring, the value of the firm's foreign assets in that

country could depreciate significantly. Table 4b shows that current account balance is a significant determinant of OFDI for both types of Chinese firms, and the values are positive both before and after 2004. This indicates that Chinese firms are attracted to countries with a current account surplus, not ones with current account deficits and those likely to approach a financial crisis.

Other results in Tables 4a and 4b also show some control variables that do not support the findings of previous studies on Chinese OFDI. Inflation for both types of firms is significant and negative in the results spanning all years in the study (Inflation). This shows that as host country inflation increases, Chinese OFDI into that country generally decreases. These results are consistent with standard economic theory that as inflation rates become volatile and unpredictable host country FDI is more likely to decrease (Buckley et al., 2007). However, inflation before 2004 shown in Table 4b (Pre2004_Inflation) is not found to be significant for either type of Chinese firm. This implies that inflation rates were not a significant determinant in Chinese firms' investments prior to 2004.

Another variable that contradicts past literature is the annual change in exchange rate (ExchangeRateChange). Central SOEs and Other Firms are both significantly and positively affected by annual changes in exchange rate from 1996 to 2016. This shows that as a country's currency appreciates, Chinese firms are generally more likely to invest in that country, and this result contradicts the findings of previous studies (Buckley et al., 2007). On the other hand, annual exchange rate change before 2004 (Pre2004_ExchangeRateChange) for both types of firms is significant and negative. This

Table 4b: Pre2004 Interaction Results

Variables	(1) Central SOE			(2) Other Firms		
	β	Std. Error	Exp(B)	β	Std. Error	Exp(B)
Intercept	-.892	1.847	.410	-1.219	.5116	.295
RealGDP	4.114 E-13***	5.9553 E-14	1.000	6.897 E-130***	6.476 E-14	1.000
Distance	.000***	1.286 0 E-5	1.000	.000***	9.773 E-6	1.000
Inflation	-.048***	.0114	.953	-.021*	.0097	.979
Patents	-4.127 E-6**	1.4099 E-6	1.000	-4.721 E-6***	1.125 E-6	1.000
PolRisk	.104	.0699	1.110	.223***	.0549	1.250
OECD_dummy	1.189***	.1418	3.283	.581***	.1112	1.788
OreAndMetal	.021***	.0031	1.022	.027***	.0028	1.028
OreRiskInt	.021***	.0036	1.022	.031***	.0036	1.032
CurrentAccount	.009ϕ	.0051	1.009	.016***	.0046	1.016
ExRateChange	4.488***	.4789	88.926	3.49***	.3552	32.92
Pre2004_dummy	-.419	.9421	.658	4.88***	.3284	131.73
Pre2004_RealGDP	8.276 E-13*	3.3201 E-13	1.000	-5.058 E-13***	1.069 E-13	1.000
Pre2004_Distance	-.001***	.0003	.999	.000***	3.781 E-5	1.000
Pre2004_Inflation	.069	.0775	1.071	-.015	.0246	.986
Pre2004_Patents	-8.961 E-6	9.0145 E-6	1.000	7.839 E-6**	2.562 E-6	1.000
Pre2004_PolRisk	-.213	.5832	.808	-.396*	.2105	.673
Pre2004_OECD	1.683	1.8346	5.380	-.337	.4293	.714
Pre2004_OreAndMetal	-.055	.0460	.947	-.003	.0145	.997
Pre2004_OreRiskInt	.016	.1322	1.016	.009	.0228	1.009
Pre2004_CurrentAccount	-.043	.0446	.958	.037*	.0182	1.038
Pre2004_ExRateChange	-22.84**	7.5379	1.203 E-10	-3.19***	.5886	.041

Dependent Variables: (1) Central SOE OFDI, (2) Other Firms OFDI- Sum of Local SOE and Private OFDI

ϕ $p < 0.10$, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

suggests that before 2004 both types of Chinese firms were attracted to depreciation in host country exchange rate.

Chinese firms' indifference to inflation and attraction to currency depreciation before 2004 could be the result of Chinese firms seeking to acquire cheap foreign assets in countries with currency depreciation. High inflation rates often lead to currency depreciation which subsequently causes the cost of production, wages, and assets in that country to decrease relative to foreign currency. This is consistent with results of past studies on OFDI that show that as host country exchange rate depreciates, "more profitable opportunities for OFDI occur since foreign currency denominated assets become cheaper." (Buckley et al., 2007). Chinese multinational firms before 2004 could have seen opportunities to cheaply enter new markets due to foreign currency depreciation and influenced the location choice of their OFDI.

Political Risk:

While the results both support and oppose the findings of many past studies, in analyzing Chinese OFDI's relationship to political risk, the empirical results yield mixed outcomes. The original results in Table 3a show that political risk (PolRisk) for Central SOE's is not significant, but Other Firms' political risk is significant and positive. This positive value indicates that the OFDI from China's Other Firms is actually attracted to countries with low political risk, not supporting the claims of many previous studies (Buckley et al., 2007; Cui & Jiang, 2009; Kolstad & Wiig, 2009; Ramasamy et al., 2012, Quer et al., 2012). In fact, according to the results, a one unit decrease in host country political risk is associated with approximately a 16% increased chance in the likelihood

of a Local SOE or Private firm investing there. Therefore, these empirical results do not support Hypothesis 1, which claims that Chinese firms are attracted to political risk.

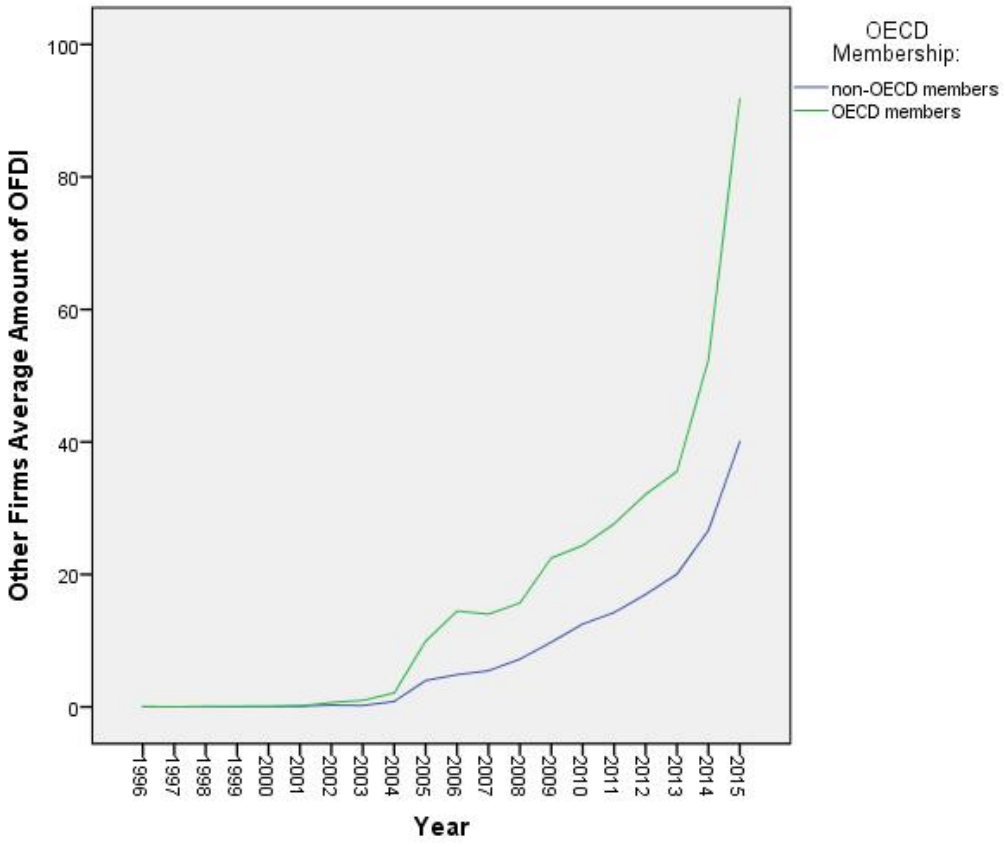
However, when the Pre2004 interaction variables are also factored into the model, the effect that political risk has on Chinese OFDI is complicated. Table 3b depicts the results of the model that includes the Pre2004 interaction variables. The results in Table 3b show that for Central SOEs before 2004, political risk (Pre2004_PolRisk) is not significant in determining where Central SOEs engage in FDI. Therefore, the results do not support Hypothesis 3a which claims that China's Central SOEs are attracted to political risk across all years of the study. For Other Firms, on the other hand, political risk before 2004 is significant and negative. This shows that before 2004 Local SOEs and Private firms were attracted to investing in countries with high political risk, but when looking at the years 1996 to 2015 as a whole, these firms display the opposite behavior, actually being attracted to countries with low political risk. This suggests that China's Local SOEs and Private firms' attention to political risk significantly changed after 2004, and they changed from being attracted to political risk to being deterred by it. These results support Hypothesis 3b that China's Other Firms are not attracted to political risk after 2004.

Several explanations can be found for China's Other Firms' change from attraction to political risk to deterrence from it. First, the increased implementation of China's "走出去" or "Go Global" domestic policy helped begin a rapid increase in Chinese OFDI after 2003 that was coupled with increased Chinese firm privatization. Recall that previous studies have found that China's Private firms are more market-seeking than its state-owned firms (Ramasamy et al., 2012); therefore, an increase in the

number of private multinational firms as a proportion of total Chinese multinationals would likely cause the overall trend of Chinese investment to become more market-seeking and deter from investments into politically risky countries.

Second, Chinese firms appear to be turning to more developed countries for investment rather than continuing to invest in developing and likely politically riskier countries. Membership in the Organization for Economic Cooperation and Development (OECD_dummy) is used in this analysis as a proxy for classification as a developed or developing country, and for both Central SOEs and Other Firms, OECD membership was significant and positive from 1996 to 2015. This shows that both types of Chinese firms are generally attracted to investing in developed countries. However, OECD membership before 2004 (Pre2004_OECD) for both types of firms is not significant. This implies that before 2004 a country's status as developed or developing did not have a significant effect on where Chinese firms chose to engage in OFDI. Moreover, previous studies have found that the bulk of Chinese FDI has historically been engaged in developing countries that, as a group, record higher levels of political risk (Buckley et al., 2007). This study's data supports this claim, showing that the mean value for political risk for OECD countries is 1.266 while the mean value for non-OECD countries is -.3192 where higher values denote less political risk. Based on this data, it can be seen that as Chinese firms become more attracted to investing in developed countries, they would similarly become more attracted to investing in less risky host countries.

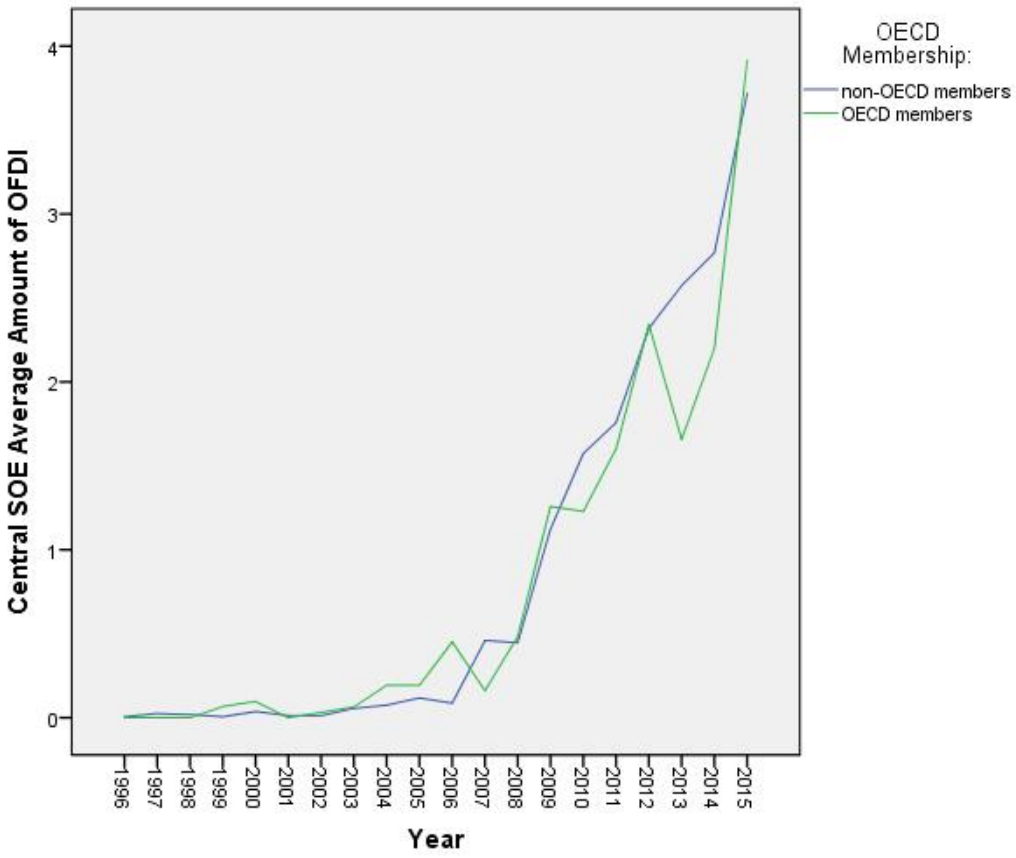
Figure 4: Average Annual Amount of OFDI by Other Firms



Another interesting conclusion that can be derived from the results is that recent changes to China's overall business environment seem to affect the investments of China's Local SOE and Private firms more than those of firms directly controlled by the central government. Figure 4 shows the average amount of OFDI projects engaged by China's Other Firms annually, and it shows that after 2004 significantly more OFDI by China's Other Firms went to developed countries than to developing countries and this trend even persisting until 2015. This supports previous findings that China's Private firms are generally more market-seeking and would likely turn to stable countries with large markets for investment (Ramasamy et al., 2012).

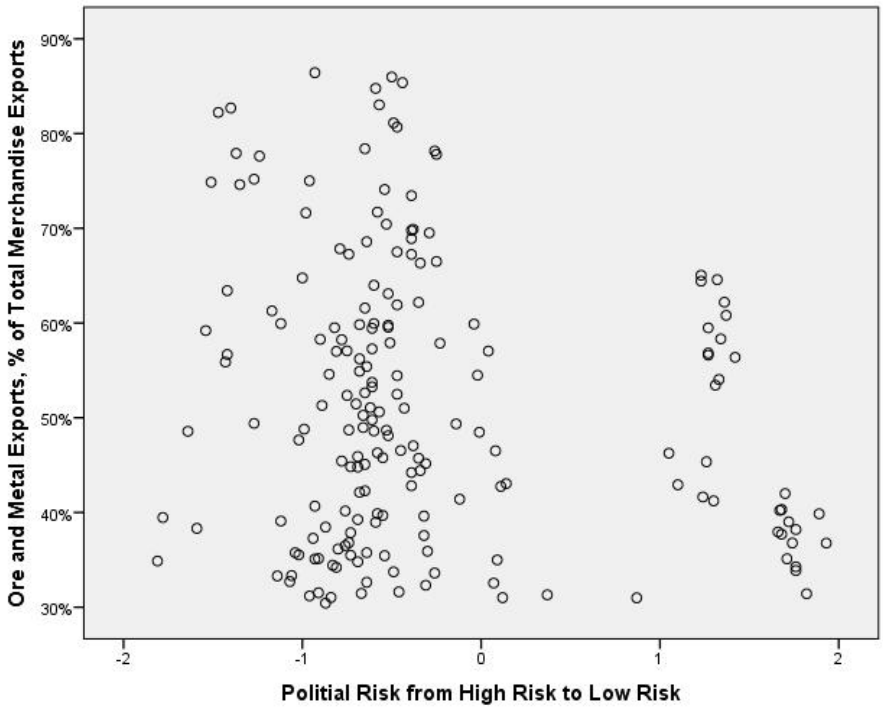
However, when compared to Figure 5, which shows the annual number of OFDI projects by Central SOEs, this trend is not shown. Instead, the investment trend by Central SOEs into developed and developing countries is almost the same across all years of the study. Central SOEs invested in developed and developing countries at about the same rate from 1996 to 2015. This indicates that the observed changes to Chinese firms' investment behaviors in the year 2004 apply to China's Local SOE and Private firms but do not apply to Central SOEs. Huge domestic policy changes such as the "Go Global" strategy and China's rise to become one of the largest economies in the world still did not influence Central SOEs to invest more in developed countries over this time period.

Figure 5: Average Annual Amount of OFDI by Central SOEs



This poses interesting questions regarding why over a period of time where Chinese firms and China itself changed so drastically did China's Central SOEs not similarly change. Strict supervision of these firms by the Chinese central government could push Central SOEs to support China's national agendas at the expense of profit. For example, China is one of the largest importers of natural resources in the world. With such a need for natural resources, the Chinese government could utilize these large firms to enable its acquisition of natural resources despite the level of political risk in host countries. Figure 6 depicts the levels of political risk in countries where more than 30% of exports are ore and metal exports, and of these countries, the vast majority rest to the left of center and are considered countries with higher political risk. In pursuit of investing in countries with abundant natural resources, the Chinese central government could encourage Central SOEs to invest in higher risk countries such as these.

Figure 6: Political Risk in Natural Resource-Abundant Countries



Moreover, for the natural resource-abundant countries shown in Figure 5, the data shows that only 8.5 percent of these countries are OECD members while 91.5 percent are not. This could also help explain the phenomenon shown in Figure 5 where Central SOEs invested in developed and developing countries at very similar rates from 1996 to 2015. Central SOEs could be pushed by the Chinese central government to prioritize the acquisition of natural resources, limiting the pool of potential investment targets to those dominated by developing countries and those with higher political risk. The results show that China's Other Firms and Central SOE's OFDI displays different relationships with political risk over time, and 2004 marked a significant year in the change from Local SOE and Private Firms being attracted to political risk to being deterred by it.

Conclusion:

Chinese investment into other countries has been increasing at an incredible pace in recent years, and this is especially true for Chinese outward foreign direct investment. As China's OFDI policy has liberalized and its private sector become larger, it has become easier for Chinese firms to engage in OFDI, and the year 2004 served as a critical year in this development.

Utilizing new data on Chinese OFDI, this study shows that two different stories emerge with regards to Chinese firms' relationship to political risk from 1996 to 2015. For China's Local SOEs and Private firms, limited investment opportunities prior to the implementation of the "Go Global" strategy in 2004 likely drove them to invest in countries with high political risk. However, after Chinese OFDI policy liberalized, these firms began turning to more developed countries for investment and their attraction to political risk similarly changed. On the other hand, political risk did not have a significant influence on the OFDI of China's Central SOEs both before 2004 and after. With their relatively large size and tight control by the Chinese central government, they are expected to follow national economic imperatives and potential political agendas that might lead Central SOEs to make investments regardless of the target country's level of political risk.

This study also supports and contradicts various aspects of past research on what country-level factors influence Chinese OFDI. The results of this study are similar to those found by past studies with regards to Chinese OFDI's relationship with market size, distance, technological innovation, and current account balance. Inflation, exchange rate

change, and political risk on the other hand do not exhibit results consistent with past studies.

For countries that seek to attract Chinese FDI, this research suggests that targeting specific types of Chinese companies would be most effective. Countries with large markets, technologically developed economies, and abundant natural resources can approach any type of Chinese firm for investment, but countries that suffer from high political risk or a looming financial crisis should target Chinese Central SOEs whose large size and backing by the state could allow them to take on riskier investments.

These findings ultimately reveal that intervention by the Chinese government can have an immense influence on the behavior of Chinese firms and the nature of China's business environment. Following OFDI policy liberalization in 2004, China's Other Firms' view of political risk changed completely while, for the Central SOEs under the government's direct control, political risk was not important and did not become important after 2004. The common denominator in both of these relationships is Chinese government intervention. In one, the government enacted change indirectly through policy and, in the other, through direct control and supervision. Although it is true that any government can have huge direct and indirect impacts on the business environment in that country, few governments can match the speed at which China has made these sweeping changes, doing so only over the span of about two decades. The changes in Chinese firms' relationships with political risk shown in this study are, at their root, a testament to the ability of the Chinese government to quickly manage the Chinese economy.

China's OFDI will only continue to grow in the near future, and this could have serious implications for China as well as those countries it invests in. Future Chinese FDI could help stimulate the economies of many developing countries and also increasingly contribute to the markets of more developed economies. Then, in a world with increasingly more Chinese intervention in foreign markets, the influence of the Chinese government will also similarly extend. Domestic Chinese goals and national policies could begin to have indirect influences on the business environments of other countries. Globalization has already achieved this to a certain extent in countries such as the United States and organizations such as the EU which are already intricately linked to the global economy, but China appears to be a rising player in the field of internationalization. Chinese firms' relationship with political risk may change in the future, but those changes will likely be guided by the direct and indirect influences of the Chinese central government, and as the amount of Chinese OFDI continues to increase, the role that the Chinese government's national policies and imperatives play in the global economy will also increase.

Appendix

Host Country List: 192 Countries and Territories, 1983-2015

Afghanistan
Albania
Algeria
Angola
Antigua and Barbuda
Argentina
Armenia
Australia
Austria
Azerbaijan
Bahamas
Bahrain
Bangladesh
Barbados
Belarus
Belgium
Belize
Benin
Bermuda
Bolivia
Bosnia and Herzegovina
Botswana
Brazil
British Virgin Islands (UK)
Brunei
Bulgaria
Burkina Faso
Burundi
Cambodia
Cameroon
Canada
Cape Verde
Cayman Islands
Central African Republic
Chad
Chile
Colombia
Comoros
Congo, Democratic Republic
Congo, Republic
Cook Islands
Costa Rica
Cote d'Ivoire
Croatia
Cuba
Cyprus
Czech Republic
Denmark
Djibouti
Dominica
Dominican Republic
Ecuador
Egypt
Equatorial Guinea
Eritrea
Estonia
Ethiopia
Fiji
Finland
France
French Guiana
Gabon
Gambia
Georgia
Germany
Ghana
Greece
Grenada
Guatemala
Guinea
Guinea-Bissau
Guyana
Hong Kong (PRC)
Hungary
Iceland
India
Indonesia
Iran
Iraq
Ireland
Israel
Italy
Jamaica
Japan
Jordan
Kazakhstan
Kenya
Kiribati
Korea, Democratic Republic
Korea, Republic
Kuwait
Kyrgyzstan
Laos
Latvia
Lebanon
Lesotho
Liberia
Libya
Lithuania
Luxembourg
Macao (PRC)
Macedonia
Madagascar
Malawi
Malaysia
Maldives
Mali
Malta
Marshall Islands
Mauritania
Mauritius
Mexico
Micronesia
Moldova
Monaco

Mongolia
Montenegro
Morocco
Mozambique
Myanmar
Namibia
Nepal
Netherlands
New Caledonia
New Zealand
Nicaragua
Niger
Nigeria
Norway
Oman
Pakistan
Palau
Palestine
Panama
Papa New Guinea
Paraguay
Peru
Philippines
Poland
Portugal
Puerto Rico
Qatar
Romania
Russian Federation
Rwanda
Saint Lucia
Samoa
San Marino
Saudi Arabia
Senegal
Serbia
Seychelles
Sierra Leone
Singapore
Slovakia
Slovenia
Somalia
South Africa
South Sudan
Spain
Sri Lanka
Sudan
Suriname
Sweden
Switzerland
Syria
Taiwan
Tajikistan
Tanzania
Thailand
Timor-Leste
Togo
Tonga
Trinidad and Tobago
Tunisia
Turkey
Turkmenistan
Uganda
Ukraine
United Arab Emirates
United Kingdom
United States of America
Uruguay
Uzbekistan
Vanuatu
Venezuela
Vietnam
Western Samoa
Yemen
Zambia
Zimbabwe

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