Chinese Outbound Direct Investment in Sri Lanka, India and Pakistan: Some Emerging Facts

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ABSTRACT

During last decade, Chinese Outbound Direct Investment (ODI) in Sri Lanka, India and Pakistan (SLIP) has shown its strong growth tendency more than its average expansion rate in whole Asia. Despite Pakistan is still facing higher political risks issues, Chinese ODI has maintained its highlighted performance in the country; whilst, India as the most favourable ODI destination in South Asia, Chinese ODI activities yet seem to be lukewarm. Therefore, this study is to investigate the key factors that are pushing the proliferation of Chinese ODI in SLIP countries.

The combination of OLI paradigm and institutional approach has been applied as the theoretical framework which OLI paradigm is focusing on firm specific advantages and host country specific factors, whilst institutional approach emphasises on business strategy which is based on interactivities of firms, organizations and institutions. This study reviews previous studies on Chinese investment in countries of South Asia (SLIP countries in particular) as well as applies secondary data with descriptive research method to investigate the emerging facts of the proliferation of Chinese ODI in these countries.

From the systematic discussion on firm specific advantages, host country factors, home country factors and other policy related factors four key ODI elements, the finding shows that Chinese ODI in SLIP countries is not merely motivated by traditional firm specific advantages, but Chinese firms has also taken the advantages of strong support from home country to implement Chinese long term economic strategies.

Keywords: firm specific advantages; home country specific factors; institutional approach; Chinese Outbound Direct Investment

Introduction and research problem/issue

While “Brexit” shows the dilemma of the UK and EU economic policy movement, the USA has unveiled anti-globalization economic views. However, since economic recession in 2008, emerging economies have shown their strength in facing global economic crisis and maintaining an admirable economic growth speed. Hence, China has played a leading role in promoting globalization in both trade and outbound direct investment (ODI) perspectives.

The fast growth speed of Chinese ODI in last decade has attracted attention both from policy makers as well as number of researchers around the world to understand the determinants of the proliferation of Chinese ODI.

In this study, Sri Lanka, India and Pakistan (SLIP countries) have been considered as a specific region in South Asia that attracts Chinese ODI. According to Ministry of Commerce in China, Chinese ODI stock in South Asia between 2004 and 2013 shows that the largest recipient country is Pakistan; and in terms of investment stock per capita Sri Lanka comes to the first place. Yet, Chinese ODI in India is mild despite India is one of most popular FDI destinations in the world. Therefore, the objective of the research is to investigate the key factors that promote Chinese investment in SLIP countries.

Traditional FDI theories are built on the basis of the observation of MNEs from industrialized economies where government interference is negligible, whist firm specific advantages are the key elements of the studies. However, in the case of Chinese ODI, it is believed that Chinese government has played a crucial role (Buckley et at., 2007). Therefore, many researches (Wei, 2010) have indicated that any of the existing FDI theories is not sufficient to explain the emerging phenomenon Chinese ODI.

OLI paradigm (Dunning, 2000) is a comprehensive ODI theory that covers both micro and macro economic factors. Both Ownership (O) advantages and Internalization (I) advantages focus on firm specific factors, whilst, Location (L) advantages emphasis on host country specific factors. However, home country specific advantages/factors that played essential role on proliferation of ODI from emerging economies had not been focused in OLI paradigm. Therefore, in this study OLI paradigm is combined with institutional approach (Peng, 2009) which emphases on the interactivities among firms, organizations and institutions for carrying out business strategies.

Research Methodology

This study reviews previous studies on Chinese investment in countries of South Asia (particular Sri Lanka, India and Pakistan) and applied secondary data with descriptive research method to investigate the emerging facts of the proliferation of Chinese ODI in SLIP countries. It systematically covers four aspects: a. Chinese firm specific advantages in comparison of firms from SLIP countries; b. home country (Chinese) specific factors that promote Chinese ODI in SLIP countries; c. SLIP countries' specific factors that encourage Chinese ODI; d. and other related bilateral economic activities, and policies that can encourage Chinese ODI.

The data is collected from the publications provided by ministry of commerce of China (MOFCOM) and UNCTAD. And these data covers information on Chinese company characteristics, Chinese ODI involved sectors, political risks, bilateral trade activities, and bilateral agreement between China and SLIP countries.

Results and Findings

This section follows firm specific advantages, host country factors, home country factors and other policy related factors four segments for discussion.

First, in terms of firm specific advantages, Chinese firms lack of traditional advantages such as production technology, international market access, sophisticated management skills and international brand recognition when compare with MNEs from industrialized economies. However, Chinese firms seem to have strong skills in handling bureaucratic issue in countries where higher political risk has been involved such as Pakistan. Hence, Chinese firms heavily rely on local Chinese business networks (also called "Guanxi") to avoid liability of foreignness in host country.
And in terms of firms' characteristics, majority of Chinese ODI are conducted by State owned enterprises (SOEs) which enjoy the priority of receiving financial supports, tax exemptions (or reduced tax), risk-safeguard mechanisms such as insurance of assets and accountability of important data/information relevant to their firms. In the case of private owned enterprises (POE), they are more sensitive toward foreign market climate and also suffer less from liability of foreignness. In addition, both Chinese SOEs and POEs have enjoyed the advantages of low cost on production, and low cost of innovation that offered by Chinese domestic business market.

Second, the liberation of Chinese ODI sector which followed "Go Out" policy in early 2000s has had a great push on its proliferation. And "One Belt, One Road" initials which followed marine silk road idea has further promoted regional cooperation especially in infrastructure development. Gwadar port and its road access that connects between Pakistan and China, Colombo harbour terminal, Hambantota harbour and their road accesses in Sri Lanka etc. all the infrastructure development shows that Chinese firms are not only having strong capitals, expertises and capability to maintain comparative low cost, but more importantly it is the strong supports from their home country. And these infrastructure relate investments also indicate China's concern on international transportation security. Therefore, these Chinese ODIs is not merely commercial activities, but part of strategy for Chinese long term economic sustainability.

Third, SLIP countries all have shown their strong openness toward receiving FDI, however, their attitudes towards Chinese ODI has been quite different due to their different diplomatic relationship with China. The diplomatic relationship between China and Pakistan has been strong and stable for decades, Chinese ODI development is more secured than what it has experienced in India especially in infrastructure sector. And in the case of Sri Lanka, certain state to state projects became political dispute targets. Therefore, Chinese ODI may suffer more from liability of foreignness and "political risks" due to poorer diplomatic relationship.

Fourth, China has become major export partners with all SLIP countries. And the increased trade activities are believed of having positive impact on attracting Chinese ODI in SLIP countries. Chinese ODI in India covers widest range of sectors despite the small amount of value of investment. This indicates that when institutional support becomes weak such as poor diplomatic relationship, Chinese ODI is determined by traditional economic factors.

Conclusions, implications and significance

In SLIP countries, investments by Chinese SOEs are different from Chinese POEs and this is particularly so with reference to the financial support, information support, and strategic support which are accessible for the state sector enterprises whilst the private sector enterprises are devoid of them. For this reason, the state sector enterprises have far more been inclined to invest in the SLIP countries than the private sector enterprises of

China. Most of these projects have been motivated and determined by their ‘strategic advantage’ for China. Two such advantages are more frequently referred: (i) the unencumbered access for China for the ‘Silk Road’ and (ii) the safety and security that they can provide for the cargo and transportation vessels. It is perhaps for this reason that China has undertaken to invest in SLIP countries more in the development of transportation infrastructure than the Chinese private sector enterprises.

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