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As a manuscript

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Political Factors of Chinese Outbound Foreign Direct Investment (1991-2017)

SUMMARY OF THE DISSERTATION
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1. The research problem and its urgency

Since 2013, the Chinese government started to pursue a new strategic pattern of all-around opening up—the “Belt and Road Initiative”. (Xinhua News Agency, 2013). With the implementation of the Belt and Road Initiative, Chinese multinational enterprises (MNEs) have engaged in more—and diversified—foreign direct investment (FDI) activities. By the end of 2017, Chinese MNEs have invested a total number of 2276 large-scale projects worldwide with aggregate investment exceeding US\$1.63 trillion. However, as tensions and even conflicts are inevitable in the inter-dependent relations between MNEs and host country governments because both sides are divergent in goals, interests and understandings on development patterns, under the backdrop of rapid internationalization, investment projects of Chinese MNEs are continuously plagued by **political factors of Chinese Outward Foreign Direct Investment (OFDI)**.

It is to be pointed out that “**political factors of Chinese OFDI**” in this research are **not China-related-factors or variables**, on the contrary, **these are host-country-related factors or variables**, in other words, they are specifically relating to “uncertainties confronting Chinese OFDI due to changes in the political environment of the host countries” and are usually interpreted as “*host country political risk*”, a concept that is believed to be one of the most destructive and unpredictable factor which prevents multinational enterprises (including Chinese MNEs) from successfully pursuing their overseas investment interests. In stark contrast to MNEs from western or emerging economics, whose internationalization is driven by economic gains; majority of Chinese OFDI is undertaken by state-owned enterprises (SEOs) with the aim to implement the state’s national strategy, in this regard, it would be interesting to know how Chinese MNEs understand “host country political risk”. However, quite a number of existing measurements on “host country political risk” were formulated from the standpoint of developed-country MNEs (DMNEs) or emerging-economy MNEs (EEMNEs) whereas how Chinese MNEs (or Chinese investors) perceive this concept, has been-under-represented (Alon et al, 2017; Lattemann et al., 2017) and

lacks enough attention from the academic circle. This is problematic for Chinese MNEs with the needs for OFDI as “biased measurements” on host country political risk that fails to capture the authentic views of Chinese investors on this concept may lead to flawed decision-making and put their investment projects at risk.

As Chinese OFDI continues to expand, in order to fill the above mentioned research gap, it is imperative for think tanks, researchers, and universities to develop new evaluation systems that reflect the authentic understanding of Chinese investors on “host country political risk”, provide decision-makers with informed guidance based on down-to-earth evaluations and enable Chinese MNEs to better mitigate the adverse effects of risks and improve the quality of their overseas investments. On the other hand, the rise of Chinese MNEs will inevitably affect or even reshape the geopolitical order (in fact, their investment behaviors have already brought changes to this globalized world), therefore, it is crucial to investigate interdependence between Chinese MNEs’ investment behaviors and sovereign states and enrich theories of International Political Economic (IPE) from the experiences of Chinese MNEs.

2. Statement of the research question and hypothesis

The aim of this research is to **find out** the political factors of Chinese OFDI and **explore the role of political factors** in the decision-making and investment strategies of Chinese MNEs. The research question is stated as the following:

What factors in host countries are perceived as “political factors” by Chinese investors when investing overseas and how will host-country-related political factors impact the decision-making and investment strategies of Chinese MNEs?

In order to answer this research question, the following objectives have been set:

—Disseminate a questionnaire among senior managers with management experience of overseas projects, Chinese scholars in the field of OFDI and government officials who are responsible for the making of FDI-related policies to see what factors in a host countries are considered “political” by Chinese investors and how big their impacts can be.

—On the basis of the identified political factors in a host country, develop a new assessment technique that reflects the authentic views and understanding of Chinese investors on the concept of “host country political risk” and divide sampling economies into “high-risk” countries, “moderate-risk” countries and “low risk countries”.

—Apply this new evaluation system to China Global Investment Tracker dataset to compare the proportion of Chinese OFDI absorbed by economies with different levels of political risk in the years between 2006 to 2017 and find explanations behind the political distribution of Chinese OFDI from China’s FDI-related policies since 2000s using theories on “state policies and their implications for the internationalization of MNEs” from the standpoint of International Political Economy.

It's widely recognized that Chinese OFDI is predominantly undertaken by state-owned enterprises (SOEs), guided by the Chinese government. This leads to the inference that the primary impetus behind the internationalization of Chinese MNEs is to implement the state's macro-control and to fulfill China's national strategic objectives, in this regard, political gains are likely to supersede economic benefits in the strategic calculations of Chinese MNEs. Therefore, some scholars suggest that Chinese MNEs are "risk insensitive" and may not allow "host country political risk" to obstruct their investment decisions. In addition, it is noteworthy that the the Chinese government provides a variety of "safety nets" to motivate Chinese MNEs to seek overseas investment opportunities. Drawing from these observations, the author anticipates a propensity for Chinese OFDI to be concentrated in countries with higher political risk levels and proposes the following hypothesis:

"By proportion (or percentage), countries with higher political risk levels are more likely to be the investment destination of Chinese MNEs".

If this hypothesis is verified, that means Chinese MNEs are insensitive to the risks caused by political factors in host countries where they make investments, in this regard, the author may conclude that "political factors" are not crucial for the location choice of Chinese MNEs, and the role of "political factors" could therefore be neglected in the decision-making and investment strategies of Chinese MNEs.

The research object is political factors that can cause uncertainties to the investment interests of Chinese MNEs when investing in a host country.

The research topic is the influence of political factors in a host country (host country political risk) on decision-making and investment strategies of Chinese MNEs.

3. The Timeframe of the study

As for the timespan of this dissertation, initially, the author held an ambition in his mind and intended to cover a period of the last 30 years, however, two obstacles prevented the author from doing this: The first obstacle is that from 1990s till early 2000s, the volume of Chinese OFDI was rather small and Chinese MNEs were still going through “reforms”, they were not powerful enough to venture overseas as MNEs from western or some developing countries could do, this period may not be worthy of research. The second obstacle is that in the year 2018, when many Chinese MNEs have become important actors (many of them grew into World’s top 500) in this interdependent world, trade war broke out and the China—US relations deteriorated, exacerbated by the pandemic as well as suspicions of “creating debt trap and over-reliance on China” and criticisms of “bringing corruptions” rather than “job opportunities”, the entire world tend to view Chinese OFDI not as “opportunities” but as “threats” and the good momentum for Chinese OFDI was interrupted by various political events and came into the period of “adjustment” showing completely different features. Amid this rather volatile period, Chinese OFDI from 2018 onwards needs a separate and far-more in-depth study that could be my future research focus in the next 5 years. Therefore, the author slightly changed the title of this dissertation and concentrate his research more on a “stable period” (2006 to 2017) when Chinese OFDI witnessed substantial growth meanwhile the entire world was relatively friendly towards Chinese MNEs, however, a review on Chinese OFDI from early 1990s was also briefly elaborated by the author.

4. Methodology

Research Thread



4.1. Theoretical and methodological foundations

The author understands that it is rather difficult to find out these factors directly and almost impossible to “measure their impacts”. However, the concept of “host country political risk” serves as a “bridge” and helps the author achieve the aim of this research. The first reason, as stated previously, is that among all risks that MNEs (including Chinese MNEs) face today, “host country political risk” is widely believed to be the most destructive and unpredictable factor which prevents them from successfully pursuing their overseas investment interests (it should be regarded as political issues rather than an economic one) meanwhile the relations between the location choice of Chinese MNEs and hosts country political risk has already been extensively studied in theoretical and empirical terms by Chinese and foreign scholars. The second reason is that extensive studies have shown that even though the perception or understanding of “host country political risk” varies from MNEs to MNEs and depends largely upon the environment these MNEs grown up from, a consensus has been reached by scholars that it is “measurable”. Most importantly, “host country political risk” are the results of tensions or even conflicts between MNEs and sovereign states that can not be easily reconciled because both sides pursue different goals and have different understanding on international investment activities. This describes a situation of “hostility” between state and non-state actors in this globalized world and indicates that theories of “complex interdependence” in International Political Economy (IPE) should be the theoretical foundation of this research. In this regard, starting with the concept of “host country political risk” is a pragmatic approach for the author because it helps iron out the huge gap between the research question and

research design and most importantly, it provides this research with a solid theoretical foundation and endows this dissertation with IR-nature.

4.2. Research methods employed

By narrowing down the abstract research question to the discussion on the relations between “hosts country political risk” and Chinese OFDI, this research becomes more feasible. However, the author decides not to follow the path of an economist by running various regression models and interpret the results using theories from International Economy. On the contrary, the author decides to conduct this research from the perspective of an IR scholar. The first reason is that theories of International Economy may not be sufficient to explain why Chinese MNEs, who does not seem to enjoy any “comparative advantages” as their counterparts from developed or some developing countries do, could still venture overseas, and expand globally. The second theoretical drawback is that theories of International Economy cannot explain why the internationalization of MNEs would cause tensions and even conflicts between MNEs and sovereign states (especially host countries) neither. The third, as well as the most underlying reason is that when conducting empirical research, many scholars often use existing measurements on “host country political risk”; however, these indexes either fail to capture the multi-dimensional characteristics of this concept or their assessment methodology are inconsistent and flawed; therefore, they are unable to reach a consensus on relations between host country political risk and Chinese OFDI.

By comprehensively using the following research methods, the author managed to ensure the the reliability of the research outcomes:

1) First-hand data collection

In order to find out the political factors of Chinese OFDI, the author employs **survey strategy (Questionnaire Survey)**. The author’s working and internship

experience in China's MNEs, compounded by his connections in various government agencies, MNEs, think tanks and universities in China not only helped him in forming, refining and validity-checking of the questionnaire made by the author but also helped him reach out to the right people (the representative sample), successfully get feedbacks so that their understanding on concept of "host country political risk" could be collected (primary data). The author's good network not only guarantees that the samples chosen by the author is representative of the target population and ensures the quality of the data collected. In addition to that, **T-test** has been run to delete all irrelevant variables and the author managed to collect 15 variables that most closely related to Chinese companies' views on "host country political risk" (host-country-related political factors).

2) Composite index development

On the base of the 15 identified variables, the author decides to construct a new composite index as the measurement model that represents the authentic views of Chinese MNEs on the concept of "host county political risk" because composite indices are ideal for the measurement of abstract concepts by combining a plurality of variables. To avoid and mitigate the problem of arbitrary weighting in the construction of composite indices, the author employed **principal component analysis (PCA)** in the calculation of the weights of component indicators of this composite index. **Two methods (missing data treatment and correlation)** were used to test the robustness of the newly created composite index and it was concluded that this index is robust and adequate for use in further analysis.

3) Data-analysis

In order to measure the role of political factors in the investment strategies of Chinese MNEs, the author applies the newly constructed Country Political Risk Index (CPRI) to a more accurate measurement on Chinese OFDI—CGIT dataset. Exploratory

data analysis approach has been used to compare the proportions/percentages of Chinese OFDI absorbed by low, moderate and high risk countries, this helps reveal the distribution of Chinese OFDI in host countries with different risk levels. As the validity and reliability of both CGIT dataset and CPRI index have been checked, it can be judged that the outcomes obtained in this research is objective and impartial.

4) Document-analysis

In order to find out why Chinese OFDI is proven to be concentrated more in “moderate” and “low” risk countries, the author systematically analyzed FDI-related legal documents, policies, and regulations concerning by the Chinese government since 2000. For various reasons, including language barriers and a lack of familiarity with the undertones and narratives in China’s official documents, these policies have not received enough attention from the academic circle. The author made full use of his language advantage as well as familiarity with the discourse, narrative and undertone of governmental documents and made a detailed summary of FDI-related policies from a semi-insider’s view. This not only strengthen the credibility of this research but also facilitates the author’s elaborations on how “promotional polices” help Chinese MNEs form comprehensive advantages to invest abroad and how “protection polices” empower Chinese MNEs in the face of the adverse effect of host country political risk.

5. Evaluation of the primary sources

Primary source in this study are divided into seven groups as presented in the following:

- 1) IPE theories on interdependent relations between sovereign states and MNEs, research papers on political risk and empirical studies on Chinese OFDI.
- 2) Literature concerning the development of composite index.
- 3) Existing political risk assessment models such as WGI, ICRG and EFI database.
- 4) A more accurate firm-level measurement on Chinese OFDI—the the China Global Investment Tracker database (CGIT database)
- 5) Laws made by Chinese government with the aim to protect the investment interest of Chinese MNEs.
- 6) Policies and regulations made by various Chinese departments responsible for the promoting Chinese OFDI as well as protecting the investment interest of Chinese MNEs since 2000.
- 7) First-hand data on 74 respondents as well their understanding on “host country political risk”.

6. Research Contribution

6.1. Scientific Novelty

First, this research focuses on a topic that has not been fully investigated. The study offers a glimpse of “how China achieves the objectives of its foreign policy and other national strategies via the means of OFDI”.

Second, well-designed research methods has been appropriately employed to address the research question. “Using mathematics to explore IR questions” is a trend among many IR researchers, in this research, the author has carefully used quantitative

methods in gathering and analyzing data, doing his best to fit this method with the research design and have reaped rather effective outcomes: the use of standardized questionnaire was proven to be relatively successful in identifying “host-country-related political factors” from Chinese MNEs from senior managers with management experience of overseas projects, Chinese scholars in the field of OFDI and government officials who are responsible for the making of FDI-related policies; while composite index construction and statistic analysis are also instrumental in addressing the author’s research question of how “political factors” have impacted the distribution of Chinese OFDI and the location choice of Chinese MNEs during the last decade.

Third, this research offers a better understanding on China’s foreign policy and other national strategies and indicates new policy-related-sources and directions for future studies. The author has made full use of his language advantage and targeted on FDI-related policies issued by the Chinese government since 2000. These policies, although not directly related to China’s foreign policy or other China’s grand national strategies, concerns Chinese MNEs whose responsibility is to carry out China’s foreign policy via economic means. Making a detailed summary of the policies that lacks enough attention from academic circle and dividing them into “promotion” and “protection” categories gave the author a chance to further elaborate how the promotional policies help Chinese MNEs form comprehensive advantages to start internationalization meanwhile how protection policies empower Chinese MNEs in the face of the adverse effect of host country political risk in this research.

Fourth, drawing from the experience of Chinese MNEs, this research enriches theories of International Political Economy (IPE). International Political Economy studies the interactions among state-actors (sovereign states) and between non-state actors (MNEs, international organizations or individuals) in the world system. This research contributes to the discussion on the interdependent relations between Chinese

MNEs and sovereign states, especially how political factors and state-policies influences the location choice of Chinese MNEs when facing host country with different political risk levels. In this regard, this research adds new knowledge to IR studies.

6.2. Theoretical Significance

Theoretical significance of this dissertation are twofold:

First, the author addressed his research questions and proves that “political factors” are crucial in the investment strategies of Chinese MNEs. Moreover, evidenced by excellent overall investment performance, this research demonstrated that state-policies are also indispensable for the location choice of Chinese MNEs.

Second, drawing from the experience of Chinese MNEs, this research enriches IPE theories by adding more knowledge to the field of “implications of state-policies on the internationalization of MNEs”.

6.3. Practical Significance

Among the risks facing Chinese MNEs today, “host country political risk” is the most destructive and unpredictable factor preventing them from pursuing their overseas investment interests successfully. Therefore, it is imperative for think tanks, researchers and universities to develop new evaluation systems that reflect the real understanding of Chinese enterprises on “host country political risk” and provide decision makers with informed guidance based on their more practical assessment techniques. This will certainly enable Chinese MNEs to better mitigate the adverse effects of risks and improve the quality of their overseas investments. Existing measurements on political risk, however, do not meet these requirements or demands due to their drawbacks and flaws. By filling this gap, the practical significance this dissertation are threefold:

First, this research deepens Chinese government's understanding on the concept of "host country political risk" and therefore has the potential to offer more targeted FDI-related suggestions for various ministries and departments responsible for the Internationalization of Chinese MNEs. This will definitely help China more effectively achieve objectives of its foreign policy and other national strategies via the means of OFDI".

Second, up until today, the Country Political Risk Index (CPRI) developed by the author has accumulated political risk scores and risk levels of 139 countries from 2006 until now. This database could be used by academics, think tanks, companies and government agents for research, consultancy, or as a reference for decision-making and policy-improvement.

Third, the author has also set up a database on China's FDI-related policies (open-sources) since 2000. Via fair collaborations, the author is willing to share this database with experts, institutions, companies or personals for academic or other purposes so that they have a better understanding on China's foreign policy and other national strategies.

7. Summary of the findings

The aim of this research is to **find out** the political factors of Chinese OFDI and **explore the role of political factors** in the decision-making and investment strategies of Chinese MNEs. To operationalize this research, the author disseminated a standardized questionnaire among senior managers with experience in overseas projects, Chinese scholars in the field of outbound foreign direct investment (OFDI), and government officials responsible for FDI-related policies, in order to gauge their understanding of the concept of "host country political risk". The respondents, representative samples of the target population, were asked to select variables that best reflected Chinese multinational enterprises' (MNEs) understanding of "host country political risk" from 34 indicators developed by authoritative political risk assessment

institutions and think tanks. The author then developed a new evaluation model by incorporating 15 identified host-country-related political factors as perceived by Chinese investors. This new assessment model is called “Country Political Risk Index” (CPRI), it reflects the authentic views and understanding of Chinese MNEs on the concept of “host country political risk”, and categorizes all sampling economies into three groups: “high-risk”, “moderate-risk”, and “low-risk” countries. Next, the author applied the CPRI to a more accurate dataset on Chinese OFDI—the China Global Investment Tracker. By comparing the proportions of Chinese OFDI absorbed by low, moderate, and high-risk countries from 2006 to 2017, the study revealed the role of “political factors” in the internationalization of Chinese MNEs. Moreover, by analyzing the location choices of Chinese MNEs in the face of investment destinations with different political risk levels (measured in proportion of investment volumes), the study found that Chinese MNEs exhibited a risk-averse characteristic. This finding contradicts the author's hypothesis and refutes some scholars’ research on the “political risk insensibility” characteristic of Chinese MNEs during their internationalization. The study also observed that Chinese MNEs demonstrated a strong “awareness of risk prevention”, which can be explained by FDI-related policies issued by the Chinese government. Through a systematic investigation of laws, policies, and rules concerning FDI crafted by the Chinese government since 2000, the author identified four categories of promotional policies: foreign exchange, fiscal, taxation, and financial; industry-specific support; and information services. The Chinese government's policies helped Chinese MNEs form comprehensive OFDI advantages for internationalization, successfully guided Chinese OFDI into appropriate industries and countries, and minimized the trial-and-error cost of their foreign direct investment decisions. At the same time, the coordinative effect of the four-dimensional protection system consisting of laws and rules, regulatory policies, preventive measures, and emergency mechanisms empowered Chinese MNEs in the face of adverse effects caused by changes in host country political risk. This provided more effective protection of their investment interests and ensured the continuous growth of Chinese OFDI. In

conclusion, the study highlights the crucial role of “political factors” and “state policies” in the investment strategies of Chinese MNEs.

8. Research Limitation and Future Research

As for limitation of this research, the following scopes ought to be indicated and suggestions on future research is also stated: Firstly, this research is limited by the lack of comparisons between the PRD of Chinese OFDI and that of other countries due to the unavailability of data on their OFDI distribution (to date, I have not found any other databases that provide detailed information on Chinese OFDI similar to the CGIT database provided by the AEI or EMENDATA). However, given more data, future research could be conducted to explore the similarities and differences between the PRD of Chinese OFDI and that of other countries. Comparisons could be made between developed economies, such as those of the US, Japan, and Western Europe, and between emerging economies, such as those of Russia, Brazil, India and South Africa, to better understand the locational choices of Chinese enterprises during international expansion; also, differences in the Political Risk Distribution of Chinese OFDI in recent five years (2018-2022) and that in the previous ten years (2006-2017) could also be examined and explained from the policy-shifting perspective to find reasons behind.

Secondly, this research is also limited by the measurement of both political risk and Chinese OFDI. Because CGIT dataset only accounts for the ultimate global ownership of Chinese OFDI and thus reduce the problem of underestimation due to tax havens, an inevitable drawback of this dataset is that it only includes investment of more than 100 million USD. This threshold excludes hundreds of small investors and, therefore, under-represents investments made by small Chinese firms. Moreover, the CPRI index extracted 13 political risk indicators from ICRG, that, according to Alon, Anderson, Bailey, and Sutherland (2017) often yields negative results regardless of the measurement of Chinese OFDI (whether official or commercial) and can affect modeling results. Recognizing that complex measurement issues concerning Chinese

OFDI and political risk could lead to biased and even inaccurate results, it is proposed that a highly nuanced and well-reasoned approach to measuring both Chinese OFDI and political risk should be adopted. This is accomplished by adding to the CPRI more relevant indicators that can better represent the views of Chinese MNEs on political risk, and by using more nuanced firm-level measurements of Chinese OFDI, which can be achieved by matching data from several available sources to make possible new empirical analyses of the internationalization of Chinese MNEs.

9. Dissertation Validation

1) The 1st ASEAN Think Tank Forum of Peking University 2017—working paper titled “Impact of Political Risk on Chinese OFDI in Southeast Asia from 2006 to 2015” accepted for forum.

2) The 3rd Summer Workshop of Institute of World Economics and Politics, Chinese Academy of Social Sciences 2018—invited for oral presentation; title of the report: “Impact of Political Risk on Chinese OFDI from 2006 to 2017”.

3) The 4th International Symposium Earth Observation for Arid and Semi-arid Environments, Chinese Academy of Science 2018—invited for oral presentation; title of the report: “Political Risk Distribution of Chinese OFDI from 2006 to 2017”.

4) VI International Scientific Conference of Young Orientalists on the theme “East Asia in a Changing World”), Institute of China and Contemporary Asia of the RAS 2018 —invited for oral presentation; title of the report: “Political Risk distribution of Chinese Outward Foreign Direct Investment”.

10. Coverage of Dissertation Materials in Publications

1. GAOYAN, QY. Political Risk Distribution of Chinese Outward Foreign Direct Investment // International Journal of Emerging Markets. 2021. Vol. 16. No. 6. <https://www.emerald.com/insight/content/doi/10.1108/IJOEM-06-2018-0344/full/html>

2. GAOYAN, QY. Protection System for Investment Interests of Chinese Enterprises Abroad // World Economy and International Relations. 2022. Vol. 66. No. 9. Pp. 82-89. <https://www.imemo.ru/en/publications/periodical/meimo/archive/2022/9-t-66/china-domestic-and-foreign-policies/protection-system-for-investment-interests-of-chinese-enterprises-abroad>

3. GUO, J. & GAOYAN, QY, A New Connotation of Political Development as a Tool for Analysis of Political Processes in China // Polis. Political Studies. 2022. No. 5. Pp. 151-164. <https://www.politstudies.ru/article/5948>

4. ZHANG, SH., GUO, J., GAOYAN, QY. Development of a National School of Political Science in China // World Economy and International Relations. 2020. Vol. 64. No. 11. Pp. 84-95. <https://www.imemo.ru/en/publications/periodical/meimo/archive/2020/11-t-64/non-western-political-theories/development-of-a-national-school-of-political-science-in-china>

5. GAOYAN, QY. Distribution of political risks in China's foreign direct investment (empirical study based on data from 2006-2017) // Humanitarian sciences. Bulletin of the Financial University. 2019. Vol. 9. No. 4. Pp. 126-135. <https://doi.org/10.26794/2226-7867-2019-9-4-126-135>