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**THE ROLE OF CENTRAL AND SUB-NATIONAL
GOVERNMENTS IN INTERNATIONALIZATION
OF CHINESE COMPANIES**

Doctoral dissertation summary

Dissertation written
in the World Economy Research Institute
under the academic supervision
of Prof. dr hab. Günter Heiduk

Warsaw 2014

1. Justification for the topic selection

In the late 1970s China undertook market reforms and launched “Open Door” policy (*gaige kaifang*) that resulted in spectacular economic growth at an annual average of 10% and also impressive poverty reduction (World Bank 2014). This growth model resulting in such remarkable economic and social gains triggered one very specific stream of research the objective of which was to analyse the application of Asian developmental state model (ADSM) to the case of China (Leftwich 1995; Breslin 1996; Baek 2005; Boltho and Weber 2009; Knight 2012). The concept of ADSM takes its roots in American research on East Asia. The ADSM means the system where government and bureaucracy cooperate closely with the business sector for achieving developmental goals. It was formulated by Johnson (1982) in his pioneering study of Japanese industrial policy, which was later extended with analyzes of other East Asian countries such as South Korea (Amsden 1989) and Taiwan (Wade 1990).

Majority of the research comparing China with ADSM has concentrated on the factors related to internally-oriented policies, institutions and mechanisms. For example, Baek (2005) argues that China shares many characteristics with ADSM such as “state control over finance, direct support for state owned enterprises [SOEs] by the government, import substitution industrialisation in heavy industry, a high dependence on export markets and a high rate of domestic savings”. On the other hand, Howell (2006, p. 273) contradicts the applicability of ADSM due to the institutional arrangements present in China's case where local governments compete with each other for markets, resources and inward foreign direct investment (FDI), which inhibits “the political and administrative capacity for fundamental social and economic transformation.” Boltho and Weber (2009) identify both similarities and differences. Similarities include macroeconomic factors such as rapid economic growth, high savings, high investment as well as sharply rising shares in the world exports of manufacturers. Differences lie in: income distribution which is unequal in China; lack of strong role of industrial planning; external competitiveness resulting not from the promotion of specific industries or firms, but rather based on township and village enterprises (TVEs)¹, small private firms, foreign-invested firms; openness to FDI; lack of one agency in charge of economic development; as well as diffusion of economic decision-making to local governments.

¹ TVEs although nominally public were in fact private firms, not supported by central authorities (Boltho and Weber 2009, p 274).

In 2000, China's government launched the Go Global Policy that encouraged Chinese companies to venture abroad and had a goal of establishing 50 Chinese world-class corporations. The Go Global Policy was the next step in China's opening up to the outside world after the initial phase of "inviting in" foreign investment that started in the late 1970s. Between 2002 and 2011, China's outward foreign direct investments (OFDI) grew dynamically at the annual average growth rate of 45% (Reuters 2012). The number of Chinese multinationals (MNCs) on Fortune Global 500 ranking of world's largest corporations increased rapidly from only 12 in 2001 to 61 in 2011². In spite of that dynamic development, Chinese OFDI is still small compared to the country's economic potential and position in the world economy. In the period 2008-2010 Chinese OFDI outflows amounted to only a little more than 1% of the country's GDP annually (Starzyk 2009; UNCTAD 2014). Therefore, Chinese government aims at increasing OFDI (it is one of the key goals of the 12th Five Year Plan 2011-2015) as it is seen as an important tool in advancing the country's economic development. Thus, it is to be expected that Chinese MNCs will grow and new MNCs will emerge.

In the context of the above described developments, the study follows the research on ADSM initiated by the American studies on East Asia by filling the gap in the literature regarding the applicability of the ADSM to China in respect to its outward-oriented policies encompassed in Go Global Policy, specifically the ones related to OFDI. The work shows that the role of central government, sub-national governments and their relations with business sector constitute a significant difference from the Japanese and South Korean types of ADSM.

2. The main objectives of the dissertation

The main aim of the research is to examine the role of the Chinese central and sub-national governments' policies on internationalization of Chinese companies since the launch of Go Global Policy in 2000. In this context, the study investigates the character of OFDI support granted by Chinese governmental bodies to domestic companies undertaking foreign expansion.

In addition, the study uses Go Global Policy as a basis for assessing whether China possesses characteristics typical for the ADSM. The relevant policies and institutions are compared with their analogues in Japan and South Korea, which are recognized in the literature

² CNN Money, <http://money.cnn.com/magazines/fortune/global500/2011/>

examples of ADSM. The results will show similarities and differences between China's model and the Japanese and South Korean types of ADSM.

3. The dissertation hypotheses

The main hypothesis of the study is: Chinese central and sub-national governments' policies facilitate outward foreign direct investment and reduce risks in foreign operations. Internationalization of Chinese companies however is hindered by the complex OFDI approval system and unequal access to financing and information of private companies when compared with state-owned enterprises.

The supportive hypotheses are:

1. Chinese governmental institutions in charge of internationalization of companies (Go Global Policy) differ from Japanese and South Korean ones in terms of features, organizational structure as well as relations with business sector.
2. China's government actively promotes OFDI through financial incentives, provision of related information and training, economic diplomacy, as well as establishment of overseas trade and economic cooperation zones.

4. The structure of the dissertation

The dissertation consists of an introduction, five chapters and a conclusion.

The first chapter provides an overview of theoretical approaches to OFDI and their application to the extant literature on the internationalization patterns of Japanese, South Korean and Chinese firms. Its first part is dedicated to internationalization theories and empirical works on motivations to engage in FDI by firms from developed and emerging economies. It also discusses types of FDI and foreign market entry modes. The second part explains internationalization of Japanese, South Korean and Chinese firms, presented in historical perspective divided into stages reflecting the relation between the level and type of OFDI and development level of a given country. This approach allowed indicating the influence of governmental policies on internationalization of companies, which is the main goal of this dissertation.

The second chapter provides theoretical contributions to the influence of institutional environment on internationalization of East Asian companies. Firstly, North's definition of institutions, OLI paradigm (ownership+localization+internalization) extended with institutional dimension as well as social network theory and *guanxi*³ business model are presented. Next part focuses on the concept of ADSM, which is the basis for analysis of the role of China's central and sub-national governments in internationalization of Chinese companies. The detailed examination of its characteristics is provided based on examples of Japan and South Korea. The last part contrasts China with ADSM in terms of character of government, bureaucracy and business, their relations as well as adopted economic policies. The comparison of China with Japan and South Korea takes into account economic policies implemented by China since 1978, which constituted a path towards internationalization of Chinese companies, including: import substitution, export promotion, attracting of inward FDI, creation of "national champions", and enhancing technological catching-up by Chinese firms. This comparison aims at showing similarities and differences between Chinese institutions and policies related to OFDI and Japanese and South Korean types of ADSM.

The third chapter presents detailed examination of China's Go Global Policy as well as the central government's role in internationalization of Chinese companies. Firstly, the motivations for launching Go Global Policy and its evolution reflected in the Five Year Plans are discussed. Secondly, the main institutions in charge of devising OFDI regulations and OFDI support are presented. Next, Go Global regulations were analyzed (especially decentralized OFDI approval system) as well as policies and tools of the central government, which are to encourage and support Chinese companies' foreign expansion. The analysis of China's OFDI decision-making model and economic policies presented in chapter two and three confirm hypothesis that China shares similarities as well as significant differences with ADSM. The investigation of central government's policies and tools allows to assess their role in internationalization of Chinese companies, and as a consequence confirm the main hypothesis.

The fourth chapter investigates the implementation of Go Global Policy by Chinese sub-national governments. The first part discusses the OFDI of China's provinces and

³ In Chinese *guanxi* means "relationship", which has enormous importance in all spheres of life of Chinese people.

municipalities⁴, taking into account their development before the introduction of Go Global Policy as well as a leading role of the coastal regions as sources of Chinese OFDI. The second part indicates the importance of sub-national governments in supporting internationalization of local companies based on illustrative examples of three municipalities: Shenzhen, Ningbo and Kunming (the first two represent China's coast and the last is located in the interior). In the final section of this chapter an attempt is taken at assessing China's vertical governance system of promoting OFDI.

The fifth chapter is dedicated to the empirical research on the role of the government in internationalization of Chinese companies. It discusses design and methodology of empirical research, summary of author's findings and reference to empirical findings of other researchers. The conclusion sums up the results, also with reference to Japanese and South Korean ADSM, provides implications regarding China's vertical governance system of promoting OFDI (institutional arrangements related with promotion of OFDI and their impact on internationalization of Chinese companies), and discusses limitations of the research. In addition the directions for future research are suggested in relation to China's vertical governance system of promoting OFDI, efficiency of the government's support to OFDI and influence of such support on global competition.

5. Sources and research method

The main research method is critical descriptive analysis that is most suitable for investigating the research problem. The analysis of the role of the central and sub-national governments in internationalization of Chinese companies is based on the ADSM that includes comparative analysis of China with Japan and South Korea. The role of China's sub-national governments in internationalization of domestic companies is analyzed based on illustrative examples of three municipalities. In addition to the aforementioned descriptive analysis an empirical research was conducted using personal interviews based on standardized questionnaire that extends the existing state of knowledge. The interviews were conducted by the author in April 2011 in three cities, namely Shanghai, Hangzhou and Shenzhen. The data sources comprise of: books,

⁴ The People's Republic of China is divided into 22 provinces, 5 autonomous regions, 4 municipalities, 2 special administrative regions, and 1 claimed province (Taiwan).

scientific articles, newspaper articles in English and Chinese; information on regulations and measures related to OFDI placed on the websites of the Chinese central and sub-national government agencies and Chinese banks that are responsible for supporting OFDI. Most of the data come from “Statistical Bulletin of China's Outward Foreign Direct Investment” and “Report on Development of China’s Outward Investment and Economic Cooperation 2011-2012” issued by China’s Ministry of Commerce (MOFCOM).

6. Findings and results

The critical analysis of the literature on the internationalization of Japanese, South Korean and Chinese companies allowed the statement that institutions and policies of the government of the home country, apart from the traditional determinants, play an important role in a company’s international expansion. The findings of this research contribute to theoretical approaches to OFDI by demonstrating the significance and impact of home country institutions of central as well as sub-national level on firms’ internationalization.

The comparison of China’s institutional framework in regards to support of the internationalization of domestic enterprises with the ADSM, revealed the differences and similarities between the two models. The key finding of the study is the confirmation of existence in China of vertical governance system of promoting OFDI, which constitutes significant difference in the organization of support for internationalizing firms from Japan and South Korea. As part of the vertical governance system of promoting OFDI central government’s agencies (mainly the National Development and Reform Commission, the National Development and Reform Commission (NDRC) and MOFCOM, draw up regulations on OFDI as well as approve and support key foreign investment projects. Sub-national level bureaus of NDRC and MOFCOM approve local OFDI projects of smaller value and importance. Sub-national authorities pursue an active policy of supporting local OFDI. They have budgets dedicated to supporting OFDI and special institutions assisting local businesses in foreign expansion.

This vertical system with overlapping, complex functions of central and sub-national level agencies also implies weakening of developmental efforts of the central government. In addition, the vertical governance system of OFDI seems to generate competition between governmental institutions at the vertical level (between central and sub-national governments)

and horizontal level (between sub-national governments) in supporting their subordinate companies, which did not exist in institutional arrangements in Japan and South Korea. At the same time, this system implies inequality in terms of quality of support provided to companies and the amount of available funding. The coastal sub-national governments are more actively involved in the support of their firms than the inland ones, which results from their more advanced economies. Due to their prolonged exposure to international business (they host most of China's inward FDI) they are more knowledgeable and skilled to support OFDI than inland governments. Moreover, they are the richest areas in China, which allows them to grant greater funding for OFDI promotion.

The institutional traits common for China and ADSM are:

- strong, authoritarian party in power during the period of intensive economic reforms;
- close government-business ties, which in China are even stronger because of SOEs that play a major role in Chinese economy;
- export promotion;
- support of technological catching-up by Chinese companies;
- support of OFDI.

Other important differences in institutional arrangements, besides the discussed earlier vertical governance system of promoting OFDI, indicating that China is not adapting the ADSM, include:

- general lack of highly qualified economic officials representing elite of the country;
- business sector dominated by SOEs;
- lack of support for competition of domestic companies;
- opening of the country to inward FDI.

Significant differences between Chinese institutional model and ADSM indicate that China does not possess basic features of ADSM which is in line with earlier studies (e.g., Breslin 1996).

Next, the role of central government in internationalization of Chinese companies was investigated. The analysis of central government's Go Global Policy regulations and measures indicated that they facilitate foreign market entry and mitigate risks in overseas operations. The facilitating role is exemplified in financial support to OFDI, economic diplomacy and provision

of OFDI-related information. Financial assistance to OFDI comprises of subsidies, preferential credits, tax reductions and exemptions, awards, etc. Economic diplomacy is carried out especially in developing countries rich in natural resources, which China needs for its economic development. China's economic diplomacy tools comprise mostly of development aid and preferential loans, which not only contribute to safeguarding access to natural resources but pave the way for Chinese companies from other industries such as construction and telecommunication into these foreign markets. Central government provides OFDI-related information by issuing Country and Industry Catalogues that aim at guiding companies as to countries and industries recommended for investing. In addition, central agencies engage in organizing OFDI-related conferences and match-making events. Policy-makers at central agencies recognizing the challenges Chinese MNCs face in internationalization process (mainly lack of experience operating on foreign markets and no established brands) try to devise measures limiting risks in foreign operations. The governments' OFDI risk-reducing measures comprise of: encouragement to start foreign operations with locating in Hong Kong, which is close in terms of culture but highly international; promotion and support of establishment of overseas economic and trade cooperation zones (OETZs); promoting OFDI conducted by groups of firms; promotes the awareness of the importance of brand building and implementation of corporate social responsibility (CSR).

However, the study discovered some features of central government's policies that constitute important hindrances to internationalization of Chinese companies. OFDI approval system is complex, time-consuming (long waiting period for the decision between 20 to 40 days), and companies face uncertainty whether the approval will be granted. Private firms are still disadvantaged when compared with SOEs in terms of access to financing, information on overseas investment environment and opportunities.

The examination of sub-national governments' OFDI policies allows to state that they actively engage in support of local firms' foreign expansion. The most common support measures can be classified into four categories: financial assistance, provision of OFDI-related information, creation of international links (through the usage of sister cities platform, participation in establishment of overseas economic and trade cooperation zones), and facilitation of OFDI-related procedures.

Summing up, the analysis of the literature, examination of three municipalities' support of OFDI, as well as empirical study based on interviews allowed to confirm the hypotheses of the dissertation. It has been shown that in China, both the central government and sub-national authorities actively promote the internationalization of domestic enterprises. Chinese government policy towards OFDI is primarily focused on facilitating the entry into foreign markets, and reducing the risks faced by Chinese companies in foreign expansion. The dissertation highlights the important issue of the impact of the institutions of the home country, with their breakdown between central and sub-national ones, on the process of internationalization of enterprises. The key finding of the vertical governance system of promoting OFDI with its significant deficiencies shows that China's Go Global Policy lacks the basic elements of institutional system of ADSM that proved highly effective; and as a result implies weakening of Go Global Policy goals. However, a final answer as to application of ADSM to China requires an additional research that would combine the results of this dissertation with the extant research on China's domestic-oriented policies and the respective framework. The weaknesses of the vertical governance system of promoting OFDI should be of interest for Chinese policymakers responsible for implementation of Go Global Policy.

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