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Research on the influencing factors of China's OFDI location choice under the Belt and Road Initiative

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ABSTRACT
The scale of China's Outward Foreign Direct Investment(OFDI) continues to expand, with increasingly diversified investment fields and gradually increasing influence worldwide. In order to study the factors influencing China's OFDI location choices in countries along the Belt and Road(B&R), this paper firstly analyzes the current development status and distribution characteristics of China's foreign direct investment in countries and regions along the Belt and Road under the influence of the Belt and Road policy, and examines the opportunities and challenges of its development. There are numerous factors that influence China's OFDI location choices in countries along the Belt and Road, including the market development scale or market potential of the host countries, natural resource endowments, degree of openness, institutional environment, geographical distance, cultural and social connections, as well as strategic and policy orientations. These factors interact and jointly affect the foreign investment decisions of Chinese enterprises in the Belt and Road region. In terms of regional distribution, China will strengthen cooperation with countries along the Belt and Road, deepening investment relationships with Africa, Latin America, and other regions; in terms of industry distribution, high-end manufacturing, green energy, and modern service industries will become the focus of China's foreign investment in the Belt and Road region; in terms of geopolitics, we will deeply explore the specific impact of geopolitical factors in different host countries on the OFDI location choices of Chinese enterprises.

KEYWORDS
The Belt and Road(B&R); Outward Foreign Direct Investment(OFDI); Location Choice; Geopolitical Factors

The "Belt and Road" initiative represents a new opportunity and challenge for the regional economic development between China and its neighboring countries, reaching a certain level. It is a significant measure taken by a country under new historical conditions to "deepen and broaden its opening up to the outside world." In the "14th Five-Year Plan," China has proposed the "Belt and Road" initiative to promote cooperation and win-win outcomes with mutually beneficial economies around the world, providing a new historical opportunity for deepening economic cooperation between China and the countries along the Belt and Road. The initiative aims to enhance connectivity and economic development of the countries along the Belt and Road by strengthening policy communication, facility connectivity, trade facilitation, financial integration, and people-to-people bonds, while also opening up vast opportunities for Chinese enterprises to "go global." In recent years, the scale of China's direct investment in countries along the Belt and Road has grown rapidly. This is not only a natural result of Chinese enterprises seeking overseas market expansion, resource acquisition, and technological learning, but also an important measure to respond to national development strategies and achieve mutual benefit and win-win results. However, facing the complex and volatile international investment environment, how to reasonably choose the location of foreign direct investment has become a major challenge for Chinese enterprises.

1 Overview of China's OFDI in countries along the Belt and Road

Data from the Institute of International Economic and Trade Cooperation of the Ministry of Commerce reveals that the annual growth rate of direct investment by Chinese enterprises in regions along the Belt and Road remains stable at 5.7%. The total direct investment in non-financial co-construction countries is expected to reach a high point of $20.3 billion. According to the "2021 Annual Overview of Chinese Investment," by the end of 2021, China's cumulative stock of foreign direct investment (FDI) had climbed to a new high of $2.79 trillion, maintaining its position as the world's third largest recipient of foreign investment for five consecutive years. Entering 2022, China's total OFDI jumped to $178.82 billion, achieving an annual growth rate of 16.3%. Investment activities in that year covered 18 major sectors of the national economy, with investments in the leasing services, business services, wholesale and retail, manufacturing, financial services, and transportation sectors being particularly notable, each exceeding the $100 billion mark in investment scale.

1.1 China's OFDI investment scale in the Belt and Road region shows a stable growth trend

In 2021, China's direct investment in countries along the Belt and Road reached US$24.15 billion, an increase of 7.1% year-on-year. Although the scale reached a record high, the growth rate was 9.2 percentage points lower than the overall growth rate of China's foreign direct investment, and its proportion in China's total foreign investment flow also fell by 1.1 percentage points to 13.5%. According to the data published in the "Statistical Communique on China's Foreign Direct Investment", China's investment along the Belt and Road has continued to maintain a growth trend, with a growth rate higher than the overall growth rate of foreign investment. In 2013, when the initiative was proposed, the investment flow of Chinese enterprises in countries along the Belt and Road was only US$12.63 billion. Over the past nine years, the investment flow of Chinese enterprises in countries along the Belt and Road has increased by 91.2%; while during the same period, the growth rate of China's foreign direct investment flow was only 65.8%.

Figure 1 Investment by China in countries along the Belt and Road since 2005 Total amount of OFDI (in billions of US dollars)

Data source: Statistical Communique on China's Outward Foreign Direct Investment

1.2 The regional distribution of China's OFDI along the Belt and Road is significantly different and each has its own characteristics

The geographical distribution of China's foreign direct investment also exhibits certain regional differences and characteristics. In Asia, Chinese enterprises have seen a rapid increase in investment in Southeast Asian countries, primarily in the fields of manufacturing, infrastructure construction, and resource development. In Europe, Chinese enterprises' investment is more concentrated in high-end manufacturing, technological innovation, and financial services.

Figure 2 shows the top 20 countries in terms of the number of overseas enterprises established by China in the Belt and Road Initiative as of September 30, 2022, as announced in the "Statistical Communique on China's Foreign Direct Investment". From a country perspective, in 2021, China's investment along the Belt and Road Initiative mainly flowed to Singapore, Indonesia, Vietnam, Thailand, Malaysia, Laos, the United Arab Emirates, Kazakhstan, Pakistan, Saudi Arabia and other countries.

In terms of investment stock, the top ten countries with the largest investment stock from China along the Belt and Road are Singapore, Indonesia, Vietnam, Russia, Malaysia, Laos, Thailand, the United Arab Emirates, Kazakhstan, and Pakistan.

Judging from the number of registered enterprises investing in countries along the Belt and Road, as of September 30, 2022, the number of registered enterprises investing in Singapore is the highest, with 1, 575, followed by Vietnam, with 1, 200. Especially in Vietnam, China's direct investment in Vietnam has increased significantly in recent years. In 2021, Vietnam surpassed Russia in China's foreign investment stock ranking, ranking third in China's investment stock in countries along the Belt and Road[1]. The growth rate of China's investment in Vietnam reached 17.6% year-on-year, higher than the growth rate of direct investment by Chinese enterprises in countries along the Belt and Road.

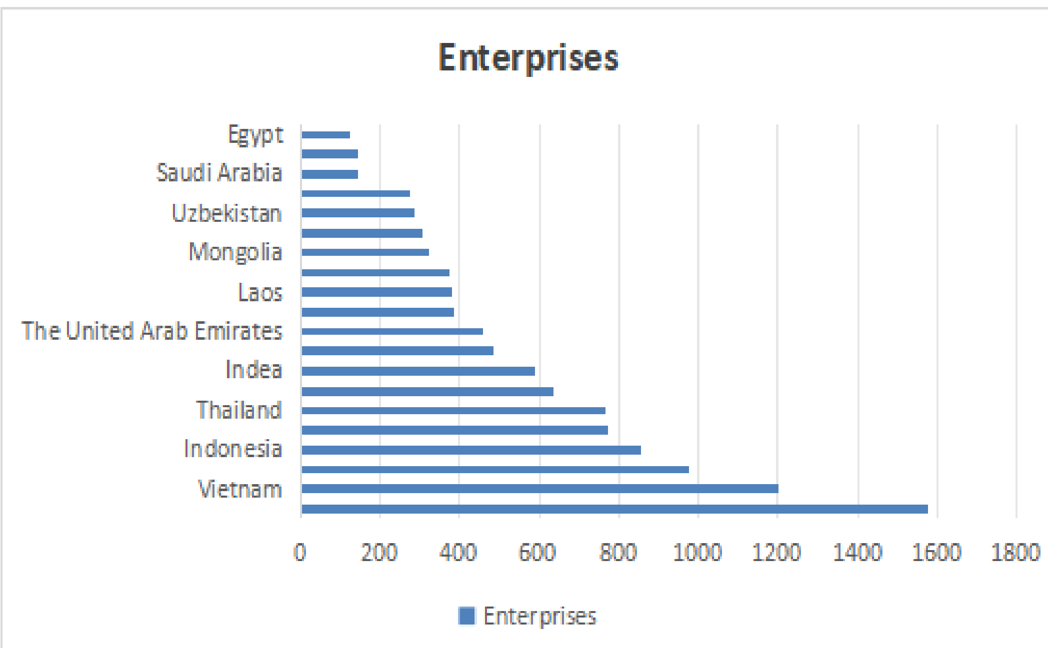

Figure 2 The top 20 countries with the highest number of Chinese enterprises established overseas in the Belt and Road Initiative

Data source: China's Foreign Direct Investment Statistical Communique

1.3 Diverse development in the fields and industries of China's OFDI investment along the Belt and Road

With the continuous increase in global foreign investment, countries have different industrial needs based on their own development situations. Enterprises also have preferences for investment industries from the perspective of global strategic development. China's investment in the Belt and Road countries is very extensive, and the investment amount has also broken through historical highs. When investing in the Belt and Road countries, both the home country and the host country need to consider their own development and plan industrial layouts accordingly. As can be seen from Figure 3, China's investment in the Belt and Road countries is mainly concentrated in the manufacturing industry, which is a major investment adjustment made by China based on its industrial structure.

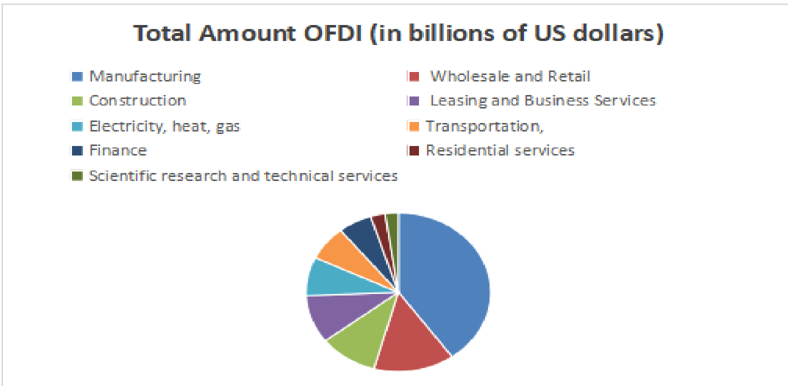

Figure 3 Industry distribution of China's outward direct investment

Data source: China's Foreign Direct Investment Statistical Communique

2 Analysis of the influencing factors of China's OFDI location choice under the Belt and Road Initiative

The motivation for Chinese enterprises' OFDI is guided by national interests. The location choice of outward direct investment is largely influenced by factors such as the geopolitical environment, comparative advantages in natural resource conditions, infrastructure construction in the host country, and the efficiency of industrial transfer.

2.1 Impact of geopolitical environment

The strategic and policy orientation of the Chinese government has also influenced the location choices of enterprises' foreign investments to a certain extent. For example, the implementation of the Belt and Road Initiative has promoted economic and trade cooperation and investment exchanges between China and the countries along the route. The demand for infrastructure construction in these countries is strong. Chinese enterprises, with their rich contracting experience and technological advantages, have made these regions an important direction for Chinese enterprises' foreign investments. Political stability is one of the important factors affecting China's foreign direct investment. When the political situation in the recipient country or region is stable, the investment environment for Chinese enterprises is relatively good, which can reduce investment risks and increase investment returns. Conversely, if the political situation in the recipient country or region is unstable, such as civil unrest, war, or regime change, Chinese enterprises' investments may face difficulties such as inability to produce, sharp decline in earnings, or even total loss. Due to Singapore's well-established and stable political environment and sound laws and regulations, compared to other Southeast Asian countries with political instability, Singapore can provide a better investment environment for foreign investors.

2.2 Impact of the development scale or market potential of the host country's market

When selecting locations for foreign investment, Chinese enterprises tend to prioritize regions with large market sizes or significant market potential. A large market size indicates strong consumer purchasing power, which is conducive to the sales and promotion of enterprise products. Meanwhile, significant market potential signifies vast future development space, benefiting the long-term layout and development of enterprises.

2.3 Comparative advantages of geographical environment and natural resource endowment

When investing abroad, China often considers resource complementarity. Natural resources hold strong appeal for Chinese enterprises. For resource-based enterprises, regions rich in natural resources such as oil, natural gas, and minerals are particularly attractive, given China's significant demand in these areas. These resources can provide enterprises with a stable supply of raw materials, reduce production costs, and enhance competitiveness.

With the gradual enhancement of Asia's political status, China's voice in the international arena is increasingly strengthening, and Southeast Asia has become an important investment target for China. The strategic deployment of other countries in Southeast Asia is directly related to regional political stability. Singapore, located at the entrance and exit of the Malacca Strait, serves as an important hub connecting the Pacific and Indian Oceans. This unique geographical location has made Singapore an important entrepot and shipping center, also prompting countries and regions such as China to be willing to establish closer economic and trade relations with it.

2.4 Impact of efficiency on marginal industrial transfer

When investing overseas, Chinese enterprises consider their own comparative advantages and select suitable locations based on the principles of marginal industry transfer. China's applicable technologies, medium-level technologies, and certain products entering their mature stage possess a comparative advantage in developing countries, making these nations often the focal points of China's outbound investments. Simultaneously, China relocates certain marginal industries to developing countries to optimize its industrial layout and elevate its value chain.

3 Strategic Suggestions for China's Outward Direct Investment

3.1 Differentiated location selection strategy

3.1.1 Southeast Asia: Cooperation in infrastructure construction

The infrastructure construction demand in Southeast Asia is huge, covering multiple fields such as transportation, energy, and communication. China can leverage its advantages in infrastructure construction, carry out in-depth cooperation with Southeast Asian countries, and jointly promote the implementation of infrastructure construction projects. For example, by providing funds, technology, and management experience, China can participate in the construction of railways, highways, ports, power stations, and other infrastructure facilities, enhancing local transportation and energy supply capabilities.

3.1.2 Northern Europe: Leveraging resource advantages to deepen energy cooperation

As a resource-rich country, Russia possesses abundant energy resources such as oil, natural gas, and coal. In light of this characteristic, China can deepen its energy cooperation with Russia and jointly develop Russia's energy resources to meet China's energy demand. This can be achieved by signing long-term energy supply agreements, jointly constructing energy infrastructure, and other means to ensure the stability and security of energy supply.

3.1.3 Central and Eastern Europe: Promote the construction of overseas industrial parks and strengthen economic and trade cooperation

As an integral part of Europe, the Central and Eastern European region boasts a unique geographical location and abundant economic resources. Promoting the construction of overseas industrial parks with Central and Eastern European countries provides a more convenient investment environment for enterprises from both regions. By constructing industrial parks, logistics parks, etc., we can attract enterprises from both regions to settle in, promoting industrial agglomeration and upgrading.

3.2 Strengthening international cooperation and multilateral mechanisms

In the context of global economic integration, China's foreign direct investment faces a more complex and diverse international environment. Strengthening international cooperation and multilateral mechanism building can not only provide a more stable and predictable investment environment for Chinese enterprises, but also facilitate the smooth implementation and long-term operation of investment projects. Through international cooperation and multilateral mechanisms, we can jointly address potential risks and challenges in the investment process and achieve mutual benefit and win-win results. China can take the following measures to strengthen international cooperation and multilateral mechanisms:

3.2.1 Strengthen cultural exchanges

By deepening cultural exchanges with countries along the Belt and Road, we promote the liberalization and facilitation of trade and investment. Many participants in the Belt and Road initiative engage in exchanges by disseminating their own cultural concepts, ways of behavior, ideologies, technologies, etc., aiming to enhance understanding and mutual support among people from different countries. Such cultural exchanges can promote mutual understanding and support for various activities among people from different countries, which is more conducive to promoting international trade cooperation.

3.2.2 Strengthen policy communication and coordination

Establish a regular dialogue mechanism with countries along the Belt and Road, and engage in in-depth exchanges and discussions on policy issues of mutual concern. Through this dialogue mechanism, mutual understanding and trust can be enhanced, laying a solid foundation for cooperation.

Strengthen cooperation with countries along the Belt and Road Initiative in the field of infrastructure, jointly promote the interconnectivity of railways, highways, ports, communications, and other infrastructural facilities, and enhance the economic development and welfare of the people in these countries.

3.2.3 Establish bilateral and multilateral investment cooperation mechanisms

Entering into intergovernmental agreements, including investment protection treaties, double taxation avoidance agreements, and judicial assistance agreements, with relevant countries, to provide legal protection for enterprises' foreign investments.

Investment protection agreements are legal documents signed between two governments to protect mutual investments, with the core focus on ensuring that the legitimate rights and interests of investors in the host country are not infringed upon. China should actively negotiate and sign such agreements with target investment countries, clarifying key provisions such as the scope of investment protection, treatment standards, and dispute resolution mechanisms. For example, the agreement can stipulate that investors enjoy national treatment or most-favored-nation treatment, ensuring a fair and transparent investment environment in the host country. At the same time, the agreement should also establish effective dispute resolution mechanisms, such as international arbitration or inter-state consultation, to quickly and fairly resolve investment disputes.

Double taxation is a common issue in cross-border investments, which increases the tax burden on enterprises and reduces the return on investment. To avoid this phenomenon, China should sign a double taxation avoidance agreement with the investment target country, clarifying provisions such as tax jurisdiction, tax credit, and information exchange. This will help reduce the tax burden on enterprises and enhance their international competitiveness.

The judicial assistance agreement aims to strengthen cooperation between the two countries in the judicial field, including legal assistance, evidence collection, recognition and enforcement of judgments, etc. This is crucial for protecting the legitimate rights and interests of Chinese enterprises overseas. By signing such agreements, China can more effectively safeguard the intellectual property rights, contractual rights and interests, etc. of enterprises overseas, ensuring the smooth progress of investment activities.

3.3 Promote industrial upgrading and innovation

Due to the need for industrial transformation, traditional manufacturing industries can no longer meet the demands of our country's development. At this point, enterprises can transfer some traditional industries or low-end manufacturing processes to countries or regions with cost advantages in labor, land, and resources, thereby optimizing resource allocation and reducing production costs. After traditional industries are transferred to overseas markets, they can leverage local markets and resources to explore new sales channels and increase product sales. For instance, Vietnam and Malaysia have abundant and inexpensive labor and raw materials. According to the theory of factor endowment, we can transfer the light manufacturing industries along the coast of Guangdong, which not only brings labor benefits to the investment regions but also promotes our own industrial optimization.

In addition to industrial transfer, outward direct investment helps extend the industrial chain, especially investments in high-end productive service industries and high-end manufacturing industries, which can drive domestic industries to develop towards higher levels. Chinese enterprises have invested in a large number of infrastructure projects in Southeast Asia, such as highways, railways, and ports. The construction of these infrastructures not only improves local transportation conditions but also provides strong support for the subsequent extension of the industrial chain. Southeast Asia is rich in mineral resources, agricultural resources, etc. Chinese enterprises, by investing in the exploration and processing of these resources, provide a stable supply of raw materials and components for subsequent manufacturing industries.

4 Conclusion

In recent years, with the continuous transformation and optimization of China's economic structure, Chinese enterprises have not yet fully demonstrated significant leading advantages in the field of foreign investment. However, the proposal of the Belt and Road Initiative has opened up new opportunities for Chinese enterprises to step onto the world stage, while also bringing unprecedented challenges. Against this backdrop, China should actively strengthen exchanges and cooperation with countries participating in the Belt and Road Initiative, continuously deepen friendly relations, and jointly explore a mutually beneficial and win-win development path. Through joint cooperation, we are expected to jointly cope with the complexities of the globalization process, promote high-quality economic development, and achieve a more prosperous and sustainable future. China should fully leverage its advantages in terms of investment strategies towards countries participating in the Belt and Road Initiative. By optimizing resource allocation, exploring overseas markets, promoting regional coordinated development, technological spillover effects, extending industrial chains, innovation-driven development, and improving investment management systems, the quality and efficiency of China's foreign direct investment can be further enhanced.

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