

The Institutional Factors Influencing Chinese Outward Investment in One Belt One Road Countries

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Abstract: After the belt and road initiative, China's OFDI has seen a remarkable increase in recent years. It is well known that investors pay a great deal of attention to the institutional framework of the countries in which they undertake an investment, and since receiving foreign capital contributes to the economic growth countries tend to develop sustainable conditions to attract investment inflows into their economies. But a huge amounts of Chinese outward investments go into countries with low institutional quality is raising concerns. Many kinds of research have been made to investigate the relationship between Chinese outward FDI and the quality of institutions in host countries. In general, these studies have shown different results. This article investigate the impacts of Chinese investments in host countries concerning different levels such as economic impacts, community impacts and environmental impacts and causes of those impacts, but generally we found that institutional quality indicators of belt and road countries doesn't have a significant effect in Chinese outward investment flows in those countries so this means that Chinese investors don't pay attention to these indicators while taking the decision of investments in belt and road countries.

Keywords: Belt and road initiative, China's OFDI, Institutional Factors

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I. INTRODUCTION

In autumn 2013, from Astana, President Xi Jinping launched the project, resurrecting the ancient Silk Roads linking Asia to Europe via Central Asia, the Middle East, and the Mediterranean. The concept refers to the ancient Silk Roads, more than two millennia old that have marked the history of humanity as a path of mutual fertilization of Eurasian and African civilizations, a path of rich trade and knowledge and technological advances. This initiative link between East and West is willing to overcome the physical barriers of geography between the three continents, barriers that remain today a fundamental geopolitical issue and also transcended the cultural and identity barriers between the peoples concerned without erasing the specificities of identity and minorities. The belt and road initiative has considerably increased the Chinese outward foreign investments. According to the Statistical Bulletin of China's OFDI, Chinese OFDI reached 145.67 billion US dollars in 2015, with an average increase of 34 % for 13 successive years. In 2015 China has invested in over 188 nations and classified 3rd in the world in term of OFDI flows. However, huge amounts of Chinese outward investments go into countries with low institutional quality is raising concerns. Nearly the half the of the top host countries of Chinese investments are with poor institutional quality, such as Lao, Nigeria, Zambia, Venezuela, Iran, Pakistan, Kampuchea, Mongolia, Burma, Indonesia, Russia, and Kazakhstan. Many kinds of research have been made to investigate the relationship between Chinese outward FDI and the quality of institutions in host countries.

The opportunities of belt and road initiative

Barker Mckenzie(2017) belt and road project is extremely ambitious. In fact, it is making an attempt to touches nearly all fields of improvement through its mega and historic tasks via Silk Road economic Belt and the twenty-first Century Maritime Silk Road. The OBOR initiative mainly focuses on infrastructure improvement, the trend of financial globalization, political coordination, cultural diversification and superior IT adoption for reaching policy coordination with 65 Countries. The objective is to establish 6 economic cooperation corridors: China Pakistan, New Eurasia Land Bridge, China-Mongolia-Russia, China-Central Asia-West Asia, and China Indochina Peninsula, Bangladesh-China-India-Myanmar. US\$ 953 Billion China's trade value with B & R countries reached US\$953 billion in 2016, 25.7% of China's total trade 8158. 8158 Contracts 8158 Contracts were signed by Chinese enterprises in 61 countries in 2016. EXIM Bank of China It had started financing over 1000 projects in 49 belt and road countries in 2016.

The belt and road project also focuses on economic flows, investment, resource allocation, and market integration, motivating nations for policy coordination through regional cooperation and encouraging open, comprehensive and balanced regional economic cooperation.

Chinese outward FDI motivations

Jiao-Hui Yang, Wei Wang, Kai-Li Wang, Chung-Ying Yeh (2017) after using GMM estimator on data panel of 132 countries of the period 2003-2012 to analyse preferences in Chinese OFDI, Jiao-Hui Yang, Wei Wang, Kai-Li Wang, Chung-Ying Yeh (2017) find a significant negative relationship between Chinese outward investments and institutional quality and this high institutional risk can be referred to high investments profits, which pushed Chinese investors into countries with low capital intensity, and cheaper natural resources.

Zhaobin Fan, Ruohan Zhang, Xiaotong Liu, and Lin Pan (2016) Employed stochastic frontier gravity model on to data panel from 2003-2013 to study Chinese outward FDI efficiency and its motivations in 69 countries of the Belt and Road countries, by analysing gravity parameter estimates Zhaobin Fan, Ruohan Zhang, Xiaotong Liu and Lin Pan (2016) have found that geographical distance deter the chinese ODIs along belt and road countries, the natural resource indicators have a positive effect on China's ODI, affirming that Chinese investments searching for natural resources. By studying components of Economic Freedom Index and the Governance Indicators Zhaobin Fan, Ruohan Zhang, Xiaotong Liu, and Lin Pan (2016) have found that Chinese ODI is blocked by some barriers like investment barriers, intellectual property protections, trade barriers, and fiscal barriers. The progression of the Chinese outward investments is spectacular, Chinese ODIs in the world rose 40% in 2016 to reach 200 billion dollars, the investments made by public and private Chinese companies in European Union alone (EU) jumped by 77% to reach 35 billion dollars FabriceNodé-Langlois (2013). in Latin America Miguel Pérez Ludeña (2014) says that Chinese ODI has exploded in 2010 by series of acquisitions made by oil companies in Brazil and Argentina since then Chinese investments were around 8 billion a year, for distribution of China's ODI along Latin America were somehow stable during this period, they were more concentrated in Peru and Brazil while in Venezuela and Excuator Chinese investments have declined during the few last years. Concerning the distribution by sector, Miguel Pérez Ludeña (2014) declare that the most of Chinese ODI's flows in Latin America are mostly concentrated in mining industries but there are some other important investments in other sectors.

FodéSiréDiaby (2014) says in his report that in recent years Chinese ODI flows to Africa (except FDI flows in the financial sectors) have grown strongly, from 74.81 million dollars in 2003 to 2.11 billion dollars in 2010 that is an increase of over 2000 percent. South Africa the main receiver country of Chinese ODI, has attracted 51% of total Chinese FDI to Africa since 2006. Today, more than 2,000 Chinese companies are based in Africa, operating mainly in sectors such as agriculture, energy, telecommunications and more.

Quality of institutions and FDI

Understanding why firms decide to internationalize and choose to locate in a particular country or region rather than in another one is an issue that is of greater interest to economists, but the answer is difficult. Not only are the variables shaping the behavior of multinational firms multiple and disparate, but their strategies are always changing in response to the changing global political and economic environment. Capturing the behavior of multinational firms within a theoretical framework remains difficult task. For 30 years, several theories have emerged with the common objective of explaining the development of multinational corporations, the deployment of their activities, the process of economic globalization and the emergence of transnational networks. Each theory was held, given its scope, to explain the behavior of firms viewed in a comprehensive manner or under certain specific aspects.

Investment is affected by both risk and profitability that are highly dependent on the institutional quality of the host countries. Thus, as pointed out by Daude and Stein (2004), foreign investors want to operate in an environment characterized by reduced uncertainties and transaction costs, Hall and Jones (1999) in their study, from a large sample of 133 countries, find that good institutions favoring production and private ownership encourage the accumulation of human and physical capital and, in the long term, increase overall factor of productivity. This environment is related to the regulation seen in the legislation governing the activity of foreign firms. Such regulations may contain barriers that impede the establishment of foreign firms and thus have the effect of diverting FDI flows to countries with more flexible and transparent legislation. Moreover, since this environment determines at the same time the system of incentives of local firms, their efficiency, their specialization and their competitiveness, their quality will largely determine the quality of inward FDI flows.

Empirical Investigation

This study's objective is filling the gap in the current debate concerning the effect of institutions on the Chinese outward direct investments in countries belonging to belt and road initiative by doing an analysis of institutions indicators affecting Chinese direct investments inflows in belt and road 60 countries, namely, Afghanistan, Albania, United Arab Emirates, Armenia, Azerbaijan, Bangladesh, Bulgaria, Bahrain, Bosnia and Herzegovina, Belarus, Brunei Darussalam, Cyprus, Czech Republic, Egypt, Estonia, Georgia, Greece, Croatia, Hungary, Indonesia, India, Iran, Iraq, Israel, Jordan, Kazakhstan, Kyrgyz Republic, Cambodia, Kuwait, Lao PDR, Lebanon, Sri Lanka, Lithuania, Latvia, Moldova, Maldives, Macedonia, Myanmar, Mongolia,

Montenegro, Malaysia, Nepal, Oman, Pakistan, Philippines, Poland, Qatar, Romania, Russian Federation, Saudi Arabia, Singapore, Slovak Republic, Slovenia, Thailand, Tajikistan, Turkmenistan, Turkey, Ukraine, Uzbekistan and Vietnam in the period between 2006-2016. We are trying to explain if there is any connection between the qualities of institutions and the amount of Chinese investment inflows in the examined countries. We use a model that combines the classical FDI determinants and the institutional indicators developed by Kaufmann (Voice and Accountability, Political Stability and Lack of Violence, Government Effectiveness, Regulatory Quality, Rule of Law, and Control of Corruption) that are expected to present a significant impact in decision making of the location of investments made by Chinese companies in belt and road countries.

Institutional Variables

World Governance indicators by Kaufman: In the late 1990s, the World Bank and its research department initiated a long-term research agenda on governance indicators. In fact, at that time, there was no measure that would allow for a global comparison of governance and corruption. Since 1996 Daniel Kaufman developed six indicators to measure governance, named "World Governance indicators". The database of this indicators is in fact, developed from composite data. These come from surveys of companies or individuals, but also from evaluations conducted by specialized risk analysis agencies, non-governmental organizations and a number of multilateral aid. They cover more than 214 countries from the period 1996 to 2016. The World Governance indicators bring six aspects:

Voice and Accountability: measures how the citizens of a country participate in the selection of their government, as well as freedom of expression, association, and the press. Kaufmann al. (2007). Generally, it includes the political and individual rights enjoyed by citizens. And it focuses on the indicators that facilitate control of the government.

Political Stability and Lack of Violence: estimate the probability that government can be destabilized and by unconstitutional or violent ways, including political violence and terrorism, it's quality of policy formulation and the credibility of the government's commitment. Political stability is also understood as the absence from the real threat of illegitimate violence.

Government Effectiveness: measures the quality of public services, the performance of the public service that includes the performance of civil servant and its level of independence from political stresses, the quality of policy development and implementation, and the credibility of public authorities with regard to these policies.

Regulatory Quality: this indicator is based on the government capacity to formulate and implement appropriate and sound policies and regulations that promote private sector development. It's more about laws themselves like if there are market unfriendly laws inappropriate bank supervision, tax borders imposed in foreign trade.

Rule of Law: this indicator measure citizens' trust in society's rules and the way they respond with them, and in particular, the respect of contracts, the powers of the police and the courts, and the perception of crime and violence. So this indicator measures the respect of citizens for laws that protect property rights. An institutional system in which the public power is subject to the law. It is based on the essential principle of respect for its legal norms, each one in the community has the same right whether individual or public authority.

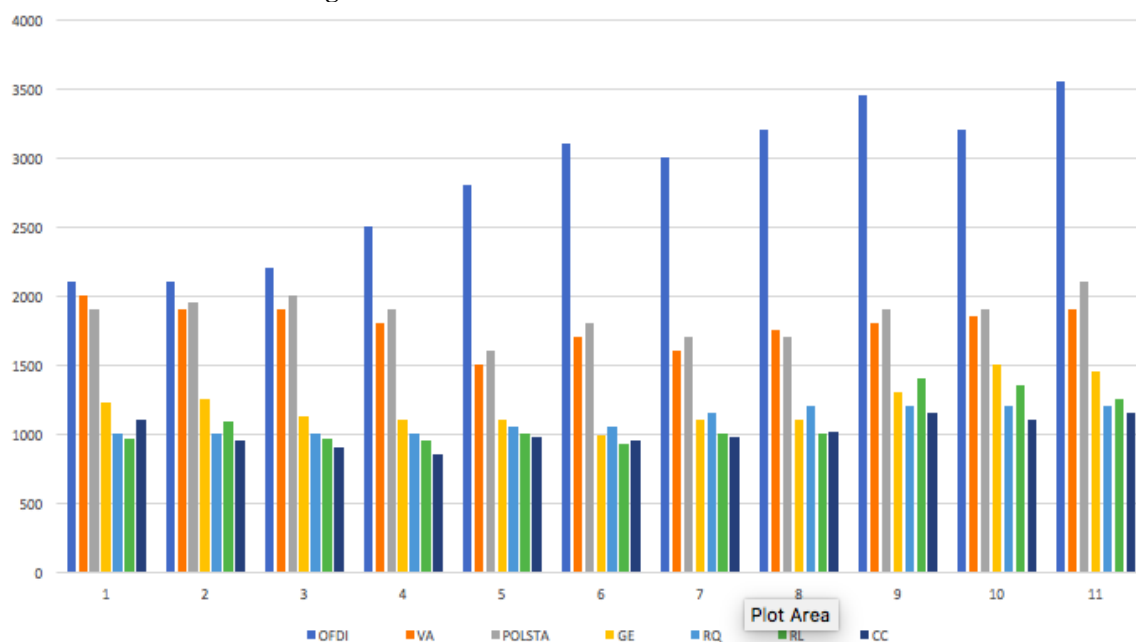
Control of Corruption: This indicator measure assesses perceptions of corruption by agents. This is defined as the use of public power to increase private earnings. These various indicators of governance are rated with indices ranging from -2.5 to +2.5 and, in this scale, a high value means a very good institutional quality.

The table below summarizes the information about institutional variables, and considering the previous results from the previous literature we estimate that the institutional qualities affect positively Chinese outward investment in OBOR countries, this means more the institutional indexes are higher in OBOR countries the more Chinese investments inflows in these countries.

Institutional Variables

Variable	Data source	Symbol
Voice and Accountability	WGI (world governance indicators)	VA
Political Stability and Lack of Violence	WGI (world governance indicators)	POLSTA
Government Effectiveness	WGI (world governance indicators)	GE
Rule of Law	WGI (world governance indicators)	RL
Regulatory quality	WGI (world governance indicators)	RQ
Control of Corruption	WGI (world governance indicators)	CC

Institutional factors influencing OFDI in OBOR countries



II. CONCLUSION

The results have shown that regulatory quality indicator of belt and road countries doesn't have an important effect in Chinese outward investment flows in these countries so this means that Chinese investors don't pay attention to this indicator while taking the decision of investments in OBOR countries. But we mostly find that Chinese companies choose to invest in countries with low level of rule of law, government effectiveness, and Control of corruption, this because of that Chinese investors are equipped with the experience of dealing with weak institutions, so Chinese companies perceive this kind of investment environment with confidence unlike Western companies who like to invest in high institutional quality countries. In the other hand, we find that Chinese firms are more likely to invest in countries with high quality of voice and accountability, and political stability indicators so it's important for belt and road countries to maintain their political stability in order to attract more Chinese investment.

The results of our study have important functional implications. The good news about this results is that belt and road countries with weak institutional indicators still can attract Chinese investment inflows, Chinese investors are confident with low institutional factors, and weak belt and road countries can increase their Chinese outward FDI inflows by maintaining their political stability.

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