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Editorial

Special issue on FDI and integration of Chinese economy

1. Overview

After more than 40 years of development and growth, China's economy has now entered the period of transformation against a backdrop of the sluggish world economy, the demise of its population advantages, and the rise of competitors in various labor-intensive industries. Moreover, the renewed trade protectionism has caused frictions and tensions between China and its most important partner, the United States. In the year of 2019, the trade friction between China and the United States continues escalating, along with the COVID-19 outbreak in China and the rest of the world. The tense atmosphere, such as in trade and manufacturing, casts a shadow over China's economic growth, while teeming doubts and concerns on China's economic sustainability spring up (Berger, Axel, et. al., 2018, Casanova et al., 2018).

How does China realize the transformation and upgrading of her economy? How could it achieve its “peaceful rise”? The answer is to contemplate the international economies built upon the traditional “center-periphery” division with the initiatives for approaches based on mutual benefits and economic integration. As the process of integration progresses, various forms of economic arrangements have been negotiated between China and its partners and neighbors, mainly as a way to support the market-integration process. The most important one of them is the “Belt and Road Initiative” (BRI) proposed by China in 2013. This arrangement is of importance. Let's give more detail on this Initiative.

The BRI, based on the “Ancient Silk Road”, is intent to supporting the recovery of the global economy, exploring regional integration, and overcoming the growing economic gap. This Initiative is an idea of international cooperation that helps promote internationalization in an open, balanced, and beneficial way. It is moved along as soon as it was proposed six years ago. At the opening ceremony of the 2nd BRI Summit held in 2019, Chinese President Xi Jinping proposed that the multi-country “corridor-road-port” interconnection be formed, and about 150 countries and international organizations expressed interest in working on this initiative.

China's further integration raises myriad economic and political-economy-related issues critical to the future of east and central Asia and their trading partners worldwide. This Special Issue focuses on Chinese economic and investment activities under the integration of the international economy and brings together 10 papers that coalesce around three themes: a) determinants of foreign direct investments (FDI); b) the mechanisms behind the BRI influences; and c) the impact of cross-border investment activities on host countries. Each of the themes sheds light on one distinct aspect of international economic and investment behaviors.

2. Determinants of FDI

There are five articles in this Special Issue discussing the determinants of FDI. One of them examines the participation in Global Value Chains (GVCs) (Ge et al., 2020). It focuses on the relationship between political institution quality and GVC participation. The article indicates that institutional quality is positively related to GVC participation by employing regional-level evidence in both macro and micro scenarios. In its country-level research, this article suggests that countries with better institutional quality have a higher level of GVC participation in institutionally-sensitive sectors. After distinguishing the BRI-participating countries and the non-BRI ones, the authors show that the institutional sensitivity of GVC participation is more prominent in the former than in the latter ones. These results imply that weak institutions are a major barrier to GVC development and regional integration in BRI regions. In its firm-level analysis, local institutions (or local investment climates) are linked to the firm-level decision on GVC participation. Results also show that firms' GVC participation is increased if there are fewer government interventions, a higher customs efficiency, a better contracting enforcement and a better access to bank loans.

Another article in this Special Issue studies the location choice of Chinese outbound foreign direct investment (OFDI) along five dimensions: geographical distance, cultural distance, institutional distance, economic distance, and informational distance. The

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results show that economic distance and informational distance promote Chinese OFDI significantly, while institutional distance restrains it. Cultural distance has no significant effect on OFDI. These results are at odds with the predictions of the traditional theories. To solve this dilemma, the authors distinguish two types of motivations for Chinese OFDI: natural-resource-oriented and market-oriented. The search for natural resources leads Chinese OFDI to the Middle East countries that are far away from China, while the market-seeking motive guides OFDI to countries with inferior information access and economic development (Ren et al., 2020).

Two other articles in this Special Issue evaluate the impact of cultural differences on FDI. One study (Zhao et al., 2020) regards cultural differences, including language, religious belief, and legal origin, among countries as the primary cause of cultural risks for FDI. Enterprises should take corresponding precautions. The other article (Wang et al., 2020) employs the number of Confucius institutes as the indicator of cultural distance between China and host countries in cross-border mergers and acquisitions (M&As). The findings suggest that Confucius Institutes have an effect on the completion of M&As in the BRI countries. The existence of bilateral investment treaties with China as well as superior economic development reinforces this effect.

In this group of the articles, one focuses on the relationship between International Development Aid (IDA) and FDI, both of which are important external financing channels (Liao et al., 2020). This article confirms that IDA promotes social and manufacturing infrastructure and business environment of recipients among BRI countries in the long run, but its crowding-out effect over FDI is also noteworthy, especially in the short-term. This article employs a vector error correction model (VECM) for time-series analysis. The results show that IDA in “complementary factor form” does promote FDI flows to IDA recipients while material capital forms of IDA restrains FDI into the recipients. This article highlights the importance of understanding the unique economic status of each recipient country when delivering IDA. Only then can their social welfare be efficiently elevated.

3. Mechanisms behind BRI

There are three articles as a group in this Special Issue discussing the mechanisms behind the impact of BRI on trade and investment. One of the articles (Yang et al., 2020) carries out an innovative study by using the Global Trade Analysis Project (GTAP) simulation model. It assumes that transportation infrastructure investment can enhance total factor productivity (TFP) and reduce trade costs, which are the two essential indicators of economic growth. This article estimates the effects of infrastructure investment under the BRI via the GTAP model, and finds that most countries would have net gains in social welfare through this process. China's industrial transformation and upgrading also benefit from this kind of investment as a result of growing high-tech manufacturing and service industries, along with the optimization of factor allocation. Meanwhile, BRI infrastructure investment consolidates the existing pattern of industrial specialization between developed and developing countries.

Another article explores the role of international cooperation and political risks in shaping today's international direct investment allocation pattern (Shao, 2020). A high-level international political cooperation in BRI is expected to greatly increase China's outbound FDI, mainly by reducing host countries' policy uncertainty and political risks for Chinese corporations. Nevertheless, the author finds that BRI's impacts on reducing investment losses are limited.

The third article finds that BRI improves China's export potential by about 8% and upgrades China's export structure (Yu et al., 2020). This kind of improvement varies across regions and industries: Central Asian countries and capital-intensive industries respond most positively to the implementation of BRI while other countries and natural-resource-intensive sectors react neutrally. The important part of this article is its delicate measurement of China's “export potential”. The authors define export potential as the difference between the predicted and actual export values from China to BRI countries and use the ratio of the actual export value to the predicted one as the measure, which perfectly avoids the potentially misleading and biased estimates caused by absolute values.

4. Impacts of cross-border investments

In this group, one of the articles investigates the influences of FDI on host countries (Liu et al., 2020). It studies the effect of FDI on Chinese employment and its underlying mechanism for labor markets with different flexibilities, different regions, and employees with different skill levels. The article selects data from 30 municipalities in China in 2000–2015 and analyzes the effect of FDI on labor market flexibility. It then explores regional and skill differences in the employment effects in various sub-samples. This article argues that wages, human capital, and R&D investment are the three conveyors of FDI's effects on employment. After confirming the mechanisms for FDI's employment effects, the article employs integrated models of moderating and mediating effects to test the three aforementioned mechanisms. Finally, this article demonstrates that FDI can improve the total labor employment in China, and has a significantly positive relationship with the labor market flexibility. It then confirms the favorable employment effect in the east coastal megaregion of China for high-skilled labor.

The other article (Chen et al., 2019) in this group constructs a set of investment facilitation evaluation systems. It reflects the characteristics of the countries along BRI. The article calculates the investment facilitation level of 77 countries along the route from 2007 to 2016 by using principal component analysis, and it compares the results with the findings from the Doing Business Report (DBR) published by the World Bank. On the basis of an extended investment gravity model, the relationship between the level of investment facilitation of partner countries along the route and China's OFDI is tested empirically. The research shows that the evaluation system of investment facilitation is fundamentally consistent with that reflected by DBR, and the evaluation system of investment facilitation is more stable, centralized and representative. The differences in the investment facilitation level of the countries along BRI are significant, and on the whole present a “wave shape” development in time and a “W-shape” structure in space. The study finds that Southeast Asia and America-Africa-Oceania are more sensitive to the business investment and regulatory environment, respectively.

5. Concluding remarks

To conclude, the readers will find the articles selected for this Special Issue to be useful. While evolutions of growth and development in East Asia and the emergence of China as an important player in the global economic system are frequently cited and debated in the academic literature and popular press, much less attention has been paid to the rapid rise in China's inward and outward FDI, which is the result of the pursuit of further development against the world economic stagnation. In acquiring momentum, China does not indulge in the sheer quantitative growth of FDI and OFDI but requires better foreign investment structure and profitability, and more contributions to the further development of the Chinese economy from them.

This Special Issue places an emphasis on the implications of China's BRI for the determinants of FDI and OFDI. The studies consistently affirm the gravitational mechanism in FDI (i.e. cultural differences) while nevertheless recognize the impacts of institutional quality on FDI location choices and labor market flexibility in FDI employment effects. They also shed new light on the pathways of benefits brought by BRI by focusing on infrastructure, political risks, and import and export structures. Considering the importance of regional integration in Asia, we believe that the potential growth to be spurred by the further pursuit of deeper collaborations is compelling. The key will be to upgrade the economic and business environment, including institution quality, infrastructure, cultural communication, and managing regional industrial transitions in accordance with participation in GVCs and expansion of regional integration.

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