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Assessing the factors that promote foreign direct investment in China

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by

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Abstract

This paper assesses the factors that promote Foreign direct investment in China. The development of foreign trade has played an important role in driving China's economic growth, and foreign direct investment has played an important role in promoting China's import and export growth. By analyzing the FDI data of China from 1988 to 2018, this paper explores the important factors affecting the distribution of FDI in China. I chose four variables as my research object. The data selected in this paper is from the National Bureau of Statistics. By using excel, we perform descriptive statistics on the sample data and perform OLS regression analysis on this basis. We also find that the number of labor and GDP have a positive impact on the FDI. The result we find do supporting the present evidence.

1.Introduction

FDI is an important driving force for foreign trade. It can effectively promote the flow of capital in the country and enhance international technology spillovers. It can provide developing countries with favorable conditions for enhancing competitiveness, such as providing advanced Technology, mature management concepts and marketing strategies. Since China's reform and opening up, FDI has made a great contribution to China's economic development. In 1985, China's FDI was only 2 billion US dollars. In absolute terms, China's FDI continues to surpass that of the United States, making China the first country in the world. The most important task is to promote economic growth for China. And capital, manpower, technology and other factors are generally considered to be economic growth drivers. For a developing country like China, economic development is more dependent on capital, talent, and technology. Therefore, FDI, which accounts for a large proportion of capital, plays a decisive role in China's development. Before the 2008 financial crisis, global FDI inflows continued to grow. After 2008, as the financial crisis intensified, global FDI inflows fell by 14% to \$1,671 billion. In recent years, FDI flowing into China has maintained a growth trend. More and more foreign investors choose China, which is related to a series of factors like good macroeconomic environment, huge market size, perfect infrastructure, low production costs and government incentives. Although the opening of China's FDI is still a continuous process, we have observed the positive stimulating effect of FDI on the Chinese economy, which has contributed to the success of China's recent economic reforms. The role and influence of FDI on China's national economy is increasingly important. Motivated by Qian, we examine the factors that promotes FDI (FDI) in China. We analyze the date of FDI in China from 1988 to 2018. The data selected in this paper is from the National Bureau of Statistics. By using excel,

we perform descriptive statistics on the sample data and perform OLS regression analysis on this basis. We also find that the number of labor and GDP have a positive impact on the FDI. The result we find do supporting the present evidence. So, this paper will study what factors that influence FDI and how to attract foreign investors.

2.Review literature Review.

2.1 Market variables:

The market factors include two aspects, one is the scale of market development, and the other is the level of demand in the market. China's huge and potential market is the main reason for attracting foreign investors. China has a huge market with a population of more than 1 billion. With the steady growth of China's economy in recent years, the level of disposable income of residents has been gradually improved, and the consumption ability and confidence have been continuously enhanced. The diversified consumption levels and products of Chinese residents have made China's market richer, and foreign investment in China is more guaranteed. For market-oriented FDI, large-scale market demand can make enterprises make full use of their monopoly advantages. Compared with Thailand and Malaysia, China's difference is that its huge domestic market has the potential to provide a huge sales market for global multinational companies, which is more attractive for their direct investment. Within China, the eastern coastal areas such as Guangdong, Jiangsu, Shandong, Zhejiang, Fujian, and Shanghai enjoy rapid economic development. They are provinces and cities with high consumption level, which have great attraction to FDI. The western areas have relatively low development level and demand level, and relatively few foreign investments have been introduced. For example, Mary Amiti (2016) shows the main

reason for the preference of direct investment from the United States for the eastern coastal areas is the relatively high per capita consumption level in the eastern coastal areas of China. The relatively high per capita consumption level indicates a relatively large market capacity, and the investment of American multinational companies in this area is more likely to obtain high returns. During this period, China was one of the biggest beneficiaries of foreign direct investment in the world. From 1998 to 2001, China received US \$165 billion in direct investment (hawarik, 2003).

2.2 Infrastructure:

The basic industry and infrastructure are the basic conditions for the survival and development of a society. They are important signs of a country's comprehensive strength and modernization. Chinese scholar Wei Houkai(2001) conducted a survey of foreign-funded enterprises, The eastern coastal area of China has a flat terrain, superior geographical location, convenient transportation, and has obvious advantages in attracting foreign investment; the central and western areas are mostly mountainous terrain, and the traffic construction is limited. In terms of railway and highway mileage, the eastern region and the central region are in turn, and the western region is the least; the main lines of telecommunication network are mainly distributed in the eastern and central region, with advanced equipment, while the western region has a small distribution density and outdated equipment. The infrastructure construction in the eastern coastal area is relatively perfect, and the information is developed, which helps to reduce the cost of market search and access to market information. The product design can be adjusted as soon as possible according to the market feedback information at any time, so as to localize the product and promote the direct investment activities of multinational companies in the eastern area.

2.3 Human capital and natural factors

Human capital is another determinant of FDI inflow. Human capital includes the cost of human capital and the quality of human capital. One of the purposes for most FDI to choose China is to use the cheap labor force in China. Developed countries have advantages in science and technology as well as market scale, but China's relatively cheap and high-quality labor resources are a powerful advantage for China to attract foreign investment. Shen Kunrong (2002), a Chinese scholar, found that sufficient high-quality talents can promote the technology transfer and production expansion of multinational companies, reduce the cost of training, accelerate the localization process of products, and have strong attraction for foreign investment. Human capital plays an increasingly important role in the development of enterprises. The higher the level of human capital, the lower the cost of finding efficient workers. In China, generally speaking, the areas where FDI is concentrated are the areas where talents are concentrated. Not only that Compared with domestic M&A companies, foreign capital stocks can greatly improve the financial situation and exports of the target company. Research also shows that foreign acquisitions can increase the production, employment and wages of the target company. China is a country rich in natural resources, especially some rare metal resources necessary for the development of high-tech industry in the future. If multinational enterprises can directly produce in areas rich in natural resources, they can greatly reduce production costs. Chen jiyong(2014) mentioned that many multinational companies in China and the United States signed joint development contracts in the early 1980s. Direct investment in the United States is mainly in the field of energy development, and American enterprises get a lot of profits from these investment projects. It can be seen that China's abundant natural resources have a strong attraction to global multinational companies, including American multinational

companies.

2.4 Laws and policies

Since 1979, China has continuously revised and improved its foreign investment policy, which has played an important role in guiding the inflow of FDI. China has successively promulgated more than 200 laws, regulations, rules and measures on foreign investment, covering direct investment, customs administration, technology introduction, industrial and commercial administration, foreign economic contracts, import and export management, taxation, labor wage system and other aspects. In addition, foreign investors will also consider the continuity and stability of foreign investment policies, which can ensure economic stability and avoid major changes. Since the reform and opening up, China has gradually opened up its domestic market, and its policies to encourage foreign investment have maintained continuity, which is also an important factor for China to become the main host country to attract FDI. Institutional factors play an increasingly important role in site selection decisions (Zheng, 2009). Institutional factors change the cost of doing business in one country rather than another, which affects all aspects of TNC behavior, including location choices (Henisz & Swaminathan, 2008).

In recent years, interest in FDI research has grown rapidly. It would be good to know what factors are important to attract foreign investment. However, there are not many studies. This paper therefore examines the important factors influencing the distribution of FDI in China by analyzing China's FDI data for the period 1988 - 2018. In one country, we could look more closely at the economic determinants of FDI attraction.

We examine the factors that promote FDI. We analyze the data of FDI (FDI) in

China from 1988 to 2018. The data selected in this paper is from the National Bureau of Statistics. By using excel, we perform descriptive statistics on the sample data and perform OLS regression analysis on this basis. We also find that the number of labor and GDP have a positive impact on the FDI. The result we find do supporting the present evidence.

2.5 GDP and FDI relationship

FDI has been identified as an important source of financing for developing countries. In this regard, China is actively attracting FDI and creating and maintaining an investment friendly environment through major reforms to facilitate the start-up of FDI. The relationship between the acquisition of FDI and the GDP in registered enterprises, closing enterprises, information requirements, working library, government protection of investment, distribute resolution, financial transfer. Our survey of per capita income of public-private cooperatives shows that there is a strong positive relationship between FDI flows and per capita GDP during 2008-2012, which has a positive impact on economic growth.

The practice of China's reform and opening up for 20 years has proved that without foreign investment, China's Ministry of economy cannot develop at such a fast speed, and foreign-funded enterprises have become an important part of Chinese enterprises. To some extent, the decline of the ratio between FDI and GDP reflects the adjustment of China's policy or structure of FDI, or the change of the dependence of China's economic growth on FDI, which does not mean that economic growth does not depend on FDI.

With the large-scale entry of foreign capital, it has effectively alleviated the shortage of construction funds in China. Foreign capital has become an important source of funds for the rapid development of China's economic construction, especially in the coastal

areas. The turnover tax of foreign-funded enterprises has grown rapidly year by year, which has become an important part of China's national economy and a new economic growth point of China's national economy. It is a rapid development of China's economy FDI has created a lot of employment opportunities for our country, which shows that FDI is closely related to economic growth. For example, the global financial crisis in 2008 proved the importance of FDI to China's economic growth. Since the financial crisis broke out at the end of 2008, a large number of foreign-invested enterprises and funds have withdrawn from China, resulting in hundreds of factories closing down, thousands of workers losing their jobs, and economic growth slowing down The National Bureau of Statistics announced that the GDP growth rate in the fourth quarter of 2008 was 6.8%, the annual GDP growth rate was 9.0%, and the growth rate in the fourth quarter hit a new low for nearly seven years.

2.6 import and export volume

In 2007, China's exports accounted for 8.8% of the world's total exports, ranking second in the world. China's share of total world trade increased from less than 1% in 1978 to nearly 8% in 2007, and it has become a veritable trading nation, of which foreign direct investment plays an important role. Sun(2009) Foreign direct investment has a strong outward expansion force. Without the export performance of foreign-funded enterprises, it will be difficult for China to achieve a steady and rapid growth of foreign trade. It is extremely obvious that the massive inflow of foreign direct investment and the development of foreign trade by foreign direct investment enterprises have promoted the rapid development of China's foreign trade and promoted the increase in total foreign trade.

3.Methodology

This paper uses the import and export volume, GDP and employment from 1988 to 2018 to study the impact on FDI. In this part, the author reviews the research methods, explains the data collection methods and the models used to answer the research questions.

3.1 Discussion of Data and Sample

As shown in Figure 1, author choose 1988 to 2018 FDI yearly data and the China's GDP, total import and export and employed player data. Import and export data are from the General Administration of Customs. 1978 is the statistics of foreign trade business, and 1980 is the statistics of customs import and export. National employment data for 1990 and beyond are calculated based on labor force surveys and censuses. Data for 2001 and after are revised based on the sixth census. Data for urban units do not include private units. In 2012, the industry adopted a new classification standard, which is incomparable with the previous period. The data is provided by the Ministry of Commerce. Since 2001, neither the contractual value of foreign investment nor the actual use of foreign capital includes foreign borrowing. Since 2007, the Ministry of Commerce no longer publishes data on the amount of foreign investment contracts. And the data source come from National Bureau of Statistics.

3.2Discussion of Methodology & Model

Dependent variable: FDI

Independent variable: China's GDP, import and export volume and employee player

3.3 Hypothesis

In fact, one of the main motives of FDI is to find new markets. The more important

a country's market is, the more FDI the province attracts under other conditions. Per capita turnover and turnover used to determine demand and scale effects.

H1: The markets size has positive impact on the FDI.

This variable that the number of persons employ reflects the size of the national labor market. Generally, when the labor market is large, the oversupply of labor tends to occur, which in turn leads to lower wages for workers. In accordance with the principle of maximizing benefits, investors will also reduce costs as much as possible in terms of cost control. Therefore, foreign investors will tend to invest in countries with larger labor markets. Based on this, this article makes the following assumptions.

H2: The number of persons employ has positive impact on the FDI.

openness reflects the degree to which a country's openness reflects the acceptance and welcome of a country's foreign capital, and to a certain extent can promote the increase in foreign investment. The more open the country, the more welcome foreign capital. At the same time, foreign investors will become more familiar with the economic situation of the host country and better control the risks of expected returns. Based on this, we make the following assumptions.

H3: The openness has positive impact on the FDI.

4. Data and regression analysis

4.1 Variable design

Table 1

Variable name	Variable symbol	Variable description
Market demand and market	$\text{Ln}(\text{GDP}_{t-1})$	GDP
Number of persons employ	$\text{Ln}(\text{labor}_{t-1})$	Number of persons employ
Degree of Openness	Openness	Total trade amount Import/GDP
FDI	FDI	FDI

Table 1

As shown in Table 1, we have identified eight potentially important factors in China's FDI distribution. First, market demand has a positive influence on FDI. Because They have a direct impact on the expected return on investment, we use GDP to understand the demand and impact of scale. Because a single indicator cannot fully reflect the factors, we also choose the indicators as follows: Number of persons employ and openness reflect a country's ability and degree of openness.

4.2 Describe statistics

Table 2

	$\text{Ln}(\text{labor}_{t-1})$	$\text{Ln}(\text{GDP}_{t-1})$	openness	FDI
Observations	30	30	30	30
Standard error	0.0165	0.2139	0.0088	7633471330
Median	20.4155	28.0773	0.1838	56915000000
Standard deviation	0.0906	1.1713	0.0485	41810244396
Variance	0.0082	1.3720	0.0023	1.7481E+21
Min	20.1132	26.7011	0.1296	3392000000
Max	20.4702	30.1289	0.2886	1.34966E+11
Average	20.3853	28.3165	0.1931	67350433333

Sum	611.5599	849.4955	5.7928	2.02051E+12
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Table 2

4.3 Regression model

For testing the factors which have impact on FDI in China, a regression model will be used as follows:

$$LN(FDI_{it}) = \alpha_i + \beta_1 LN(Labour_{it-1}) + \beta_2 LN(GDP_{it-1}) + \beta_3 Openness_{it} + \mu$$

4.4 Summary outputs

Table 3

Regression statistics	
Multiple R	0.9906
R Square	0.9813
Adjusted R Square	0.9791
Standard error	6042503254
Multiple R	0.9906

Table 3

Table 4

	df	SS	MS	F	Significance F
Regression Analysis	3	4.97E+22	1.66E+22	454.1493	1.44E-22
Residuals	26	9.49E+20	3.65E+19		
Total	29	5.07E+22			

Table 4

Table 5

	Coefficients	Standard error	t Stat	P-value
Intercept	-2.008E+12	4.72E+11	-4.2569	0.0002
Ln(labor _{t-1})	5.784E+10	2.53E+10	2.2845	0.0307
Ln(GDP _{t-1})	3.196E+10	1.79E+09	17.8545	0.00002
openness	-4.281E+10	2.74E+10	-1.5630	0.1301

Table 5

The regression is to assessing the factors that promotes FDI in China. The result obtained is that p-value equal to 0.0002, which means that there is a significant correlation between GDP and FDI. There is also a correlation between the number of employees and IDF. Since the p value is 0.0307, the p value indicates that there is no significant correlation between openness and IDF, and these coefficients indicate that as GDP increases, the impact of GDP and the correlation between the two will increase, which is consistent with the assumption. The reason for this situation is likely to be that because it directly affects the expected revenue of the investment. Moreover, combined with the surveys of the recent years, the size of the market is considered as one of the reasons for increasing the FDI Sun Q, Tong W H, Yu Q, 2002, and the conclusion is that the bigger the size of the market is, the higher of the FDI. Generally, when the labor market is large, the oversupply of labor tends to occur, which in turn leads to lower wages for workers. In accordance with the principle of maximizing benefits, investors will also reduce costs as much as possible in terms of cost control. Therefore, foreign investors will tend to invest in countries with larger labor markets. However, there is no significant relationship between openness and FDI, and we speculate that it is due

to the limitations of the data.

4.5. Results

The result is that the number of labors is significantly positive with a t-value of 2.2845. Such a result seems to suggest that the more the labor, the more the amount of FDI that will come. It is consistent to the given fact that studies typically find agglomeration effect of FDI. Meanwhile, we found that GDP and FDI show a positive correlation and are significant at the 90% level which support our hypothesis. However, there is no significant relationship between openness and FDI, and we speculate that it is due to the limitations of the data. This supports the hypothesis that the Gross National Product have a positive impact on attracting FDI.

5. Conclusion

The research contributions of this paper are mainly reflected in the following two aspects. First, this article enriches and expands the research content and dimensions of promoting FDI in this article. Existing studies have shown that the country's market size can promote FDI, but most of the research objects are concentrated in Western countries. This article uses relevant Chinese data as a research sample and analyzes China's basic national conditions to analyze the fact that foreign investors have chosen to invest in China considering that China's huge market size and consumption level will bring optimistic expected income. Second, the research content of this article has certain practical significance, which provides empirical evidence support for Chinese enterprises to attract foreign investment by improving market size and labor quality.

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7. TABLES AND FIGURES

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