China's Outbound Direct Investment (CODI): Regulation and Representation

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The Topic: hot but understudied

- In the West, fear of rising CODI, “state capitalism”
- In China, unsure how to assess CODI; critics abound.
- Few studies: Cai (1998) and Sun and Hong (2006), CODI similar to other investors; gov’t promotion is positive to CODI.
- The articles’ reception so far: MCS & Oriental Morning (东方早报); in E. Asia and China

Main Questions

- How has the Chinese regulatory regulation over CODI changed and what are its effects?
  - Comparison with other investors
  - Experience of China's private companies and SOEs

Outline of the talk

- Policy Change
- Analysis of Comparative Statistics
- Cases of Private and state Investment

Gov't Policy regarding CODI

- 1978-1989: highly restrictive
- 1992-1997: de facto loosening
- 2000-2005: "going out policy" (zou chu qu)
  - Govt/leaders' statement & reports
  - Vague and contradictory
  - Witnessed major increases in CODI
- 2005-2010: active state role

The Current Framework

- Late 2004 State Council Decision & 2009 Ministry of Commerce Regulation
- Goals: making the approval process more institutionalized, transparent, and effective
- Problems:
  - multi-step, complicated process
  - Narrowing goals: resources promotion; state biases
- Centralized approval: from "supervising agency" to NDRC or MOC
- Implementation: gov't access is critical

Current Policy (continue)

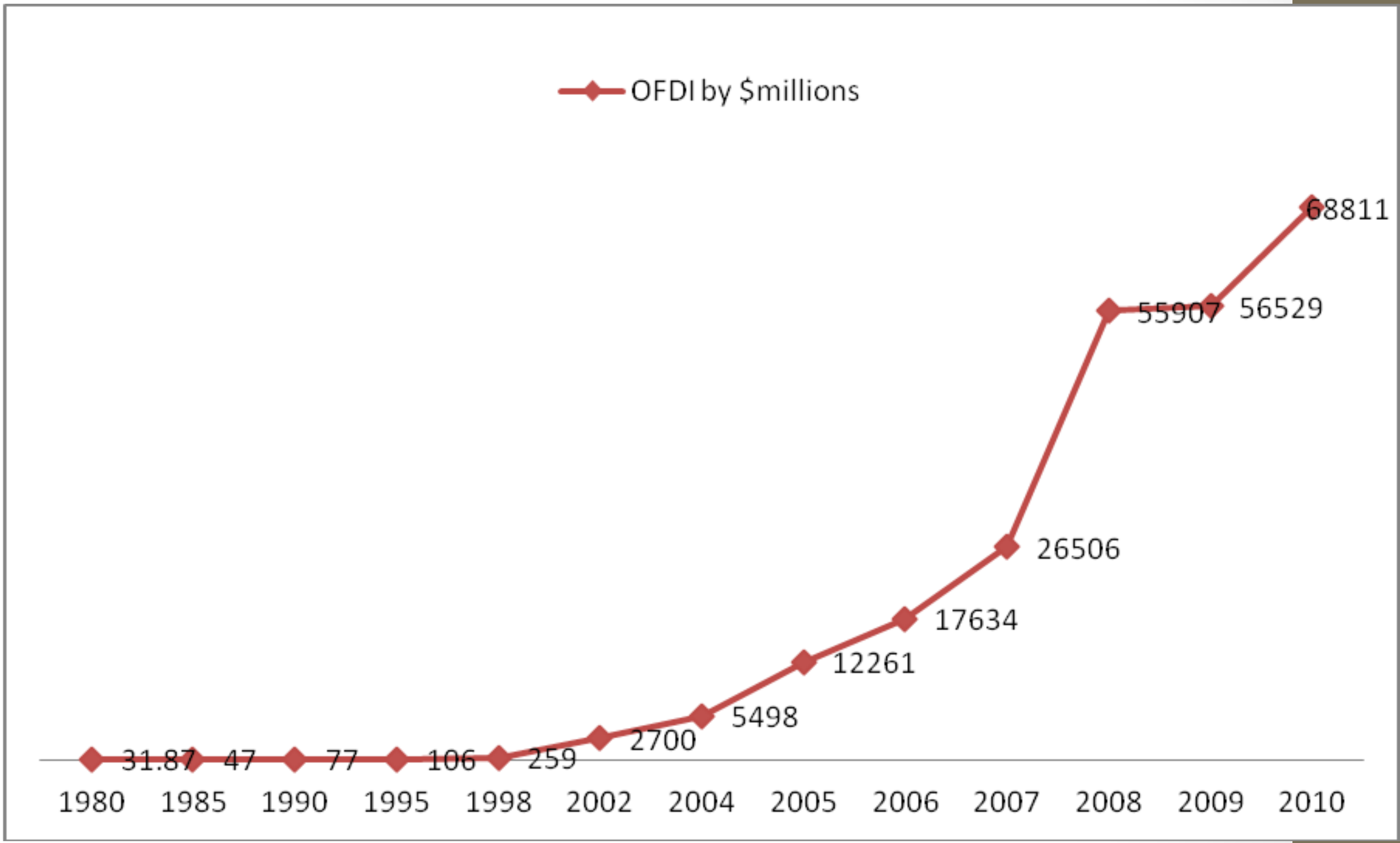
- Three-tiered approval:
  - Top-level: State council, above \$200 million (resources) & above \$50 million (non resources)
  - National-level: NDRC & MOC (\$30-200 million; \$10-50 million)
  - Provincial-level: local branches of NDRC & MOC – 2009 change (SOEs under \$50 million)
- Processing time: 10-15 days→ 3 business days
- Finance: development funds; development banks; commercial banks; corporate saving

Outcome: summary

- Imbalance between private and state investment: 2008, central SOEs, 85%, 0.3% by private companies
- Low manufacturing shares: unlikely manufacturing spillover to other countries
- Performance: two thirds losing money or breaking even

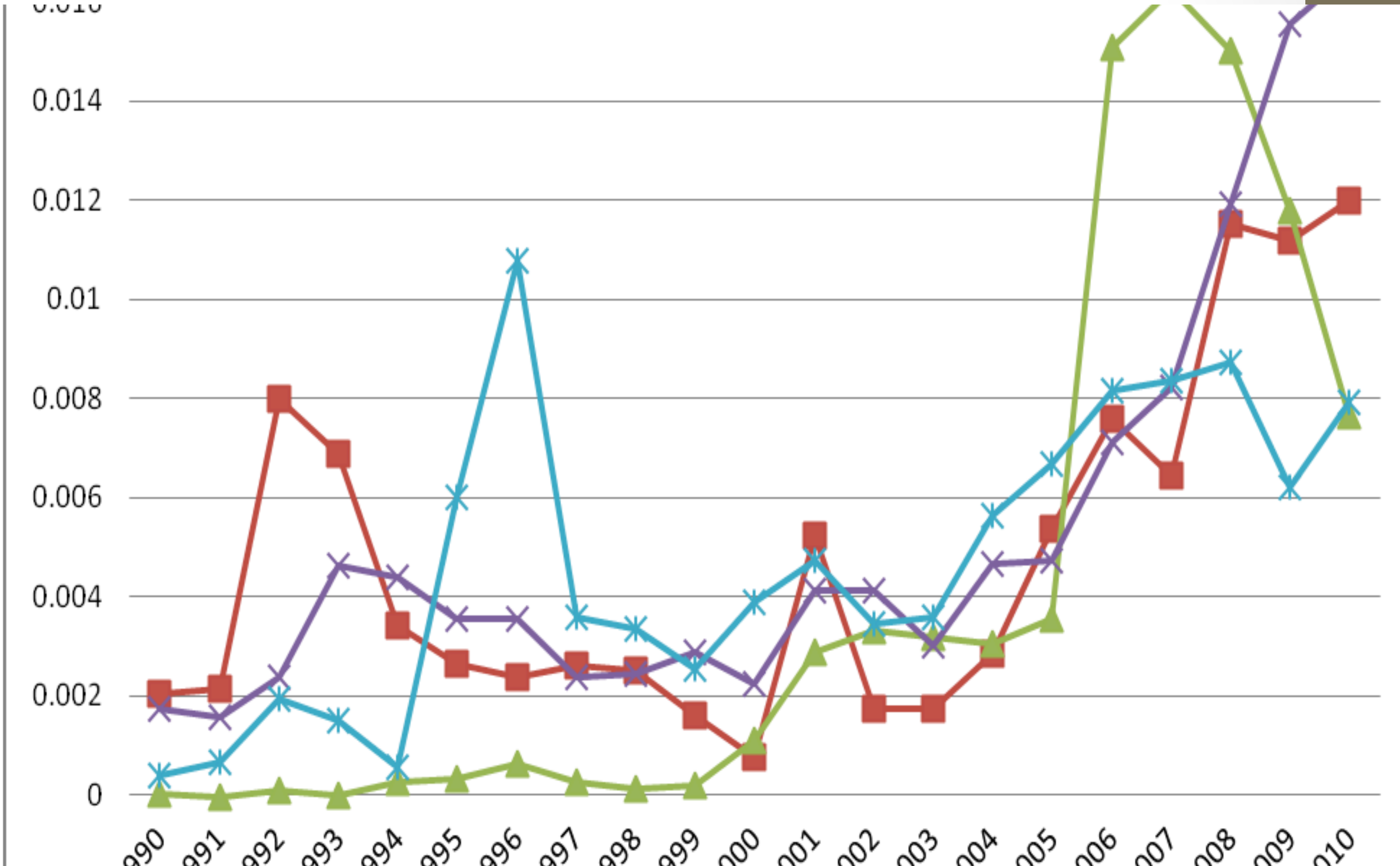
ANALYZING CODI IN STATISTICS

Rising CODI



OFDI by $millions
68811
55907
56529
26506
17634
12261
5498
2700
31.87
47
77
106
259
1980
1985
1990
1995
1998
2002
2004
2005
2006
2007
2008
2009
2010

Comparison with other Asian investors: Japan, South Korea, and India

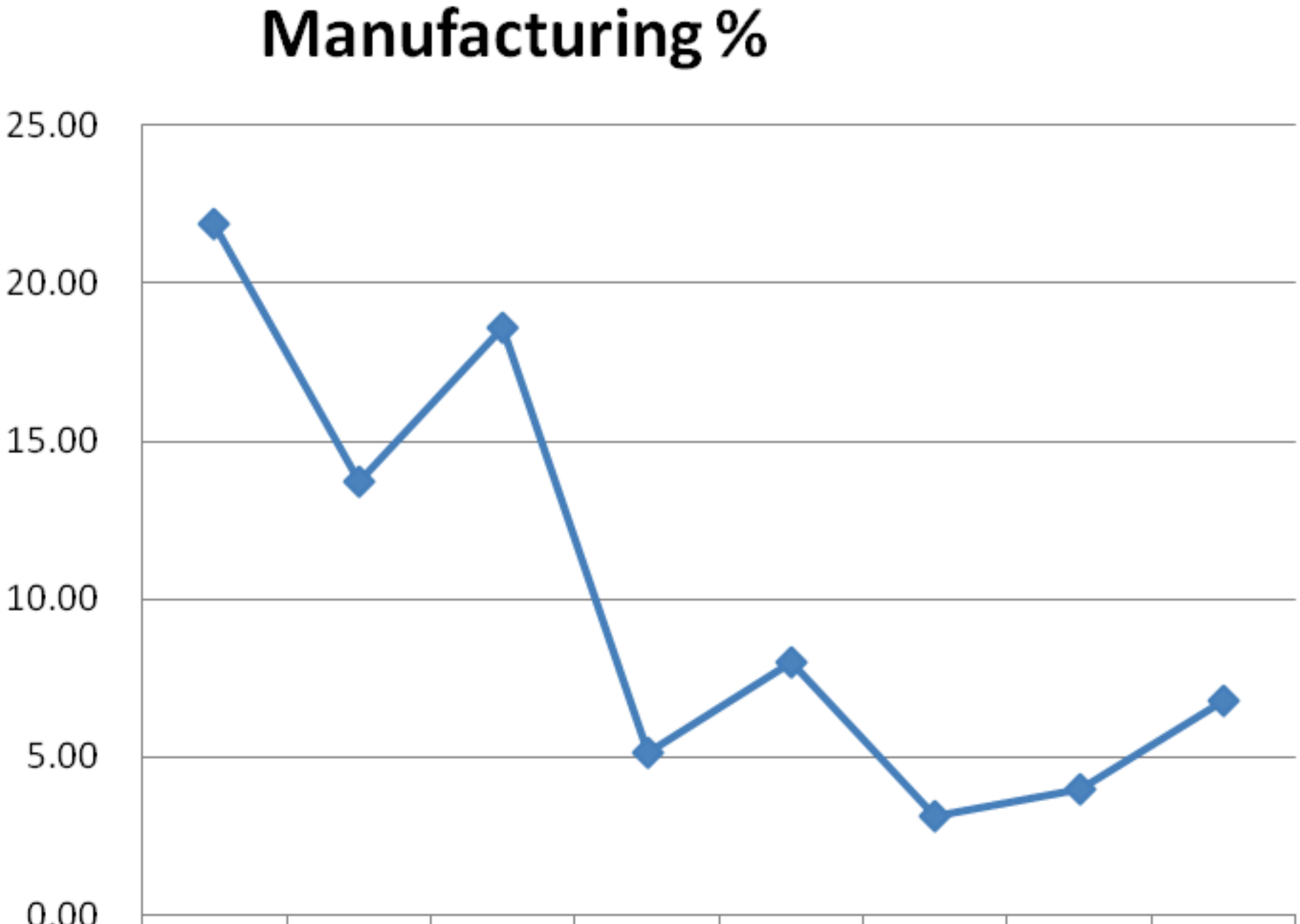


Unique features

- Hong Kong's shares in CODI, %

	2005	2006	2007	2008	2009	1010
%	*27.9*	*39.3*	*51.8*	*69.1*	*63.0*	*56.0*

Declining shares of manufacturing, %



	2003	2004	2005	2006	2007	2008	2009	2010
Manufacturing %	21.86	13.74	18.60	5.14	8.02	3.16	3.96	6.78

Underrepresentation of private shares

% of private companies	2006	2007	2008	2009	2010
Industrial output	21.24	23.21	26.87	29.55	30.54
R&D expenditure	6.5	6.99	8.73	10.02	10.27
Patents granted	7.34	6.41	9.54	10.03	11.94
New products			10.87	11.6	13.60
Outbound FDI	1	1.2	1	1	1.5

CASES OF PRIVATE AND STATE INVESTORS

Cases: Private Companies & Barriers

- Strength of private companies in China
- Imperative of investing abroad
- Yet, low representation in CODI
- Policy & irregular approval
  - **Feiyue**: Small appliances maker in Zhejiang
  - **CHINT**: electrical machinery maker in Zhejiang
    - Avoiding approval
  - **Tengzhong**: automaker in Sichuan
    - Lengthy, non action by approval agencies, de facto rejection

Barriers to Private Investment

- SOE control of commodity market excludes private investors
  - Mr. Liu's experience: iron ore acquisition
  - CHINT: electrical equipment
- SOE advantages overseas additionally disadvantage private investors
  - CHINT
  - Andong Oil
  - Mr. Mi: water machinery
- Long-term disadvantage: credit; human talent; informal connection

State companies: Diverse

- Centrally-affiliated, resources-based SOEs:
- Large, local SOEs: active and interventionist local governments
- Other SOEs: disincentives to invest abroad
  - Political risks, few incentives for CEOs to promote outbound investment
  - Short-tenure of managers
  - Domestic market monopoly—why go abroad?

Conclusions & implications

- There is a growing trend of state capitalism in China
- Private entrepreneurs & “informal coping strategy” (Tsai 2005, 2006)
- Challenge to Western theory of investment and late development
  - Patterns may differ
  - Effect may be different to host society