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Contents

Has outward foreign direct investment contributed to the development of the Chinese economy?

Jan Knoerich*

Research and literature on foreign direct investment (FDI) and economic development have to date focused almost entirely on development in the host economy, sidelining the question of any contribution to development in a multinational enterprise's country of origin. To address this shortcoming in research on FDI, this study investigates whether Chinese outward FDI can be seen as having made a contribution to the development of the mainland Chinese economy over the past three decades. It finds that the activity of Chinese enterprises in pursuing assets and advantages abroad through outward FDI yields four categories of returns: financial, capability, capacity and macroeconomic. These returns have addressed some of the specific challenges that China has faced in the process of its economic development, although the extent and importance of the development contribution remains uncertain. Outward FDI can play both a complementary and a supplementary role to development benefits realized from opening up to international trade and inward FDI, and from emigration.

1. Introduction

Research and literature on foreign direct investment (FDI) and economic development has to date focused almost entirely on development in the host economy where investment is made (Crespo and Fontoura, 2007; Saggi, 2002; JBICI, 2002; Fan, 2003; Görg and Strobl, 2001; Lim, 2001; UNCTAD, 2013; Javorcik, 2004), sidelining the question of any contribution to home country development. In an era predating the appearance of the emerging multinational enterprises (MNEs) as important global players, this focus on the host economy – and relative negligence of home-economy development – was reasonable: FDI was largely an activity reserved for MNEs from countries that were already developed, and theories about FDI – from Hymer's (1960) market power hypothesis and Vernon's (1966) focus

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on product innovation to Dunning's (2001) ownership advantages – emphasized the technological, innovative and managerial superiority of the investing MNE as an essential explanation for the occurrence of FDI. The investment development path similarly assumed FDI to occur as a consequence of economic development (Dunning, 1981). These theories were formulated at a time when most FDI flows were unidirectional, from more to equal or less advanced economies. Development in poorer economies was also associated with the inflow of productive capital, technologies and economic activity from advanced-economy MNEs, rather than with any form of capital outflow.

The ascendance to global significance of the MNEs from emerging economies after the turn of the century ushered in a new era in the study of FDI. Since then, researchers have begun to revisit some of these assumptions, often suggesting the necessity of expanding existing theories and common understandings about the nature of FDI (Gammeltoft, Barnard and Madhok, 2010). Yet somewhat missing from these discussions is the possibility that, because the MNE is the primary beneficiary of its investments, its overseas operations and investments could support the development of its country of origin – especially if the enterprise comes from a developing or emerging economy. Hardly any research has examined in detail the development contribution of *outward* foreign direct investment (OFDI) in emerging economies or developing home countries. More generally, a comparatively small number of studies have examined the impact of FDI on home countries, with many of them focusing primarily on the potential "hollowing out" of the advanced home economies and the resulting necessity of economic restructuring, an issue that would be of lesser significance to developing home countries.

In view of these shortcomings in research on FDI, the purpose of this study is to explore the nature and importance of the gains and potential benefits for a developing home country from OFDI. As this study seeks to inductively develop a framework that focuses on the development contribution of OFDI in less advanced economies, it is analytically prudent to explore this issue by making use of the case study method. For the purpose of such an examination, I chose mainland Chinese OFDI as a particularly appropriate case for a number of reasons. First, China has so far been the source of the highest amount of OFDI among developing economies. Second, Chinese firms started to go abroad as early as the 1980s, when China was clearly undergoing processes of rapid economic development. Figure 1 illustrates that already during the 1990s, China's OFDI stock as a percentage of gross domestic product (GDP) was between 1 and 3 percent, substantial enough to justify consideration of its potential contribution to China's economic development. After 2003, a stronger outward push became visible with the accumulated stock of Chinese OFDI rising to an impressive US$614 billion in 2013. Third, although China is a country with strong economic fundamentals, it faces severe economic and developmental challenges related to technological deficiencies, resources shortages, food security, population pressures, environmental degradation, pollution and more. Despite rapid economic growth of more than 8 per cent in most years since economic reforms were launched in 1978, China's GDP per capita is still relatively low. For these reasons, China is a particularly useful case for exploring mechanisms that link OFDI to the development of the home economy.

Figure 1 . China's OFDI stock