Scientific Journal of Economics and Management Research Volume 3 Issue 12, 2021
ISSN: 2688-9323

Foreign Direct Investment in the US from China

-- Book Review of Investing in the United States: Is the US Ready for FDI from China?

Qingming Zhang[1, a], Yuan Jin[2, b]
[1]Law School of Shandong University of Technology, Shandong, China
[2]Law School of Qingdao University, Shandong, China
[a]alanzhangchina@hotmail.com, [b]comeononon@163.com

Abstract

America market should be the favorable choice when Chinese MNCs are looking for foreign market. However, due to diverse ideology and strategic competition relationship, Chinese MNCs are experiencing unprecedented challenges and difficulties. The Book, Is the Us Ready for FDI from China?, analyzed the issue from politics, institutions, and marketing skills and tried to find some hints from previous cases.

Keywords

FDI; Entering Mode; CFIUS.

1. Introduction

From founding of the People's Republic of China to 1990s, China became the second largest country attacking foreign direct investment (FDI). With the development of China, Chinese Multinational Corporations (MNC) prepare to go abroad. "Within the span of fewer than ten years (2000-2007), Chinese Multinational National Corporations have invested an estimated $68 billion abroad, for a total stock of $96 billion at the end of 2007, catapulting china into the ranks of the leading outward investors among emerging markets" (P1).

Compared to other emerging markets, Chinese MNCs are mostly consisted of state-owned enterprises directed by both central and provincial government. These corporations account for 83 percent of outward direct investment in 2005 (P1). As to the entering mode, "just like their competitors from developed countries, Chinese firms rely more and more on mergers and acquisitions (M&A) when entering foreign markets, as opposed to Greenfield investment "(P1)

Just like china, the United States of America is in the top two countries attracting foreign direct investment. The facilitated infrastructure, incomparable legal system attacks investment from China. Just like the CEO of China Ocean Shipping Corporation said, America market should be the favorable choice when Chinese MNCs are looking for foreign market. However, due to diverse ideology and strategic competition relationship, Chinese MNCs are experiencing unprecedented challenges and difficulties, especially in the USA.

2. Politics of Chinese Investment in the US

In order to invest in the United States, Chinese MNCs should learn to deal with bilateral level government. On the one hand, investors need to familiar with committee network in Congress and Executive; On the second hand, they should recognize that "preferences are partly determined by local interests and constituencies"(P86). The author discussed the policy-making from both demand and supply sides.

ISSN: 2688-9323

From the demand side, economic demands of host countries come from stakeholders and competitors. If the technological relationship is complementary and substitutable, local stakeholders will welcome the investment. However, if foreign investment substitutes for local production, one might expect opposition from host country producers. The non-economic factors include national security and political externality. In fact, economic and non-economic factors are related to form of entry, potential investing areas, ownership and governance structure of parent corporation.

From the supply side, according to suggestions of author, first, "it is critical to identify the preference s of constituents in particular legislative districts to determine their stance on the issue"; second, "it is important to determine whether representatives reside in safe or marginal seats"; third, "Congress members create and participate in informal groups aimed at advancing their political agenda on specific issues" (P94).

In the supply part, committees in congress, Department of the Treasury's Committee on Foreign Investment in the United States who deciding the extent of national security and the multiple veto points in policy-making in the United States all play an important role.

3. U.S Regulatory and Institutional Framework for FDI

Just like the former president George W. Bush mentioned, "as both the world's largest investor and the world's largest recipient of investment, the United States has a key stake in promoting an open investment regime. The United States unequivocally supports international investment in this country and is equally committed to securing fair, equitable, and nondiscriminatory treatment for U.S investors abroad"(P51). However, America has almost the most complex regulatory rules. From the standing of George W. Bush, he was not "centered only on promoting foreign investment, rather, it sought a balance between maintaining an open environment for investment and preserving important security interests" (P56). Although china is a new-comer in the United States market, the past experience of Chinese investments in the US tells us that Chinese FDI will present unique considerations with regulators and policymakers, especially in the area of national security, because china is not an ally of the US, U.S concerns over the unlicensed transfer of dual use technologies.

As to ongoing regulatory compliance considerations, Chinese investors should concern foreign trade control compliance and compliance with the Foreign Corrupt Practices Act of 1977. They also should comply with any "standard regulatory approvals or disclosures that are required for the transaction based on certain general characteristics and specific to certain industries" (P58).

As to the national security, the most relevant organs are president and Committee on Foreign Investment in the U.S (CFIUS). The president has authority to review "any merger, acquisition, or takeover….. by or with any foreign person which could result in foreign control of any person engaged in interstate commerce in the United States." (P61).

CFIUS is an affiliated branch of the Department of Treasury. The CFIUS is "comprised of eight other voting members (the Department of Commerce, Defense, Homeland Security, Justice, State, and Energy, the U.S. Trade Representative, and the White House Office of Science and Technology); two permanent non-voting members (the Director of National Intelligence and the Department of Labor); and several other White House offices that act as observers and, on a case-by-case basis, participate in CFIUS reviews" (P62). When the CFIUS conducts national security review, they generally ask three threshold questions: "first, whether there is foreign control over a U.S. business; second, if there is foreign control, whether the transaction may present any significant national security issues; third, if there are national security concerns, whether they can be mitigated through contractual commitments from the transaction parties or other permissible means." (P62).

4. Modes of Entry by Chinese Firms in the US

As to modes of entry, generally, we are talking about Greenfield investment and Merger& Acquisition (M&A). M&A is "the preferred mode of entry when the purpose of the FDI is not to exploit firm-specific proprietary advantages (such as technologies or brands), but rather to acquire them" (P25). One major motive of M&A is to "acquire assets that are complementary to those already possessed by the foreign investor in order to enhance the efficiency and competitiveness of the investor" (P25). "When the industry is fast-growing, the parent firm is highly R&D intensive and the aim of investment is seeking to acquire or protect firm-specific strategic assets, Greenfield mode will be chose and preferred" (P27).

When going abroad, "Chinese foreign investment is directed at acquiring assets and resources, including technology and managerial know-how" (P28). Therefore, it is not surprise that "majority of Chinese executives plan to make acquisitions the heart of their long-term global strategies"(P29).

Although there is no sufficient evidence to prove that Greenfield investment is superior than M&A, in host countries mind, Greenfield investment will have more spillover efficiency, capital investment and employment benefits. Moreover, most Chinese MNCs are state-owned corporations. National security concern, no political loyalty and lack of transparency all perplex Chinese investors. With these in mind, the author recommended joint venture and non-controlling ownership.

5. Socio-political Costs Facing Chinese Multinationals in the US

When Chinese investment enters into the United States, one of the biggest concerns for Chinese executives is liability of foreignness. The Liability of Foreignness refers to "the added costs, specifically Socio-political costs, faced by the foreign affiliate of a multinational enterprise (MNE) that are not incurred by domestic firms in the host country" (P122). According to the author, liability of foreignness includes formal constraints, which are shaped by regulatory institutions, and informal institutions, which are shaped by normative and cognitive institutions.

Regulatory pillar includes "codified and formalized in rules and procedures" (P123). Normative pillar consists of "social norms, values, beliefs, and assumptions about human nature and human behavior that are socially shared and are carried by individuals" (P124). Cognitive pillar affects the "schemas, frames, and inferential sets, which people use when selecting and interpreting information" (P124).

In order to familiar with these difficulties, author recommended several strategies. To regulatory liability of foreign, Chinese investors should conduct compliance training and cooperate with a local partner. To overcome normative and cognitive liability of foreign, Chinese MNCs should become an "insider", cluster with ethnically similar customers and competitors, contribute to the local community and learn from early entrants to the US market.

6. Comment and Learning from the Japan

In the 1980s, another Asia country, Japan, experienced almost the same difficulties when she decided to invest into the United States. Although, China, different from Japan, is not an ally of the United States. Chinese investors could learn a lot from Japanese investors.

Several authors attributed transforming of lobbying strategies to Japanese corporations' different entering mode and American anti-Japanese pressure. In 1970s, Japanese and American were trade partners, Japanese corporations entered American market by products export. In 1980s, Japanese corporations, especially Japanese automobiles corporations, set up

ISSN: 2688-9323

plants and factories there. And vehicles are consumer-oriented products, it is easy for Japanese vehicle corporations utilizing their own dealers, components suppliers, and their own huge manufacturing and assembly operations to pressure American policy-makers. More straightforward, Japanese corporations had to drop inefficient and ineffective "quiet, behind-the-scenes" non-confrontation lobbying strategy and adopted confrontation due to "domestic content".

Most authors analyzed the transforming of lobbying strategies only from the perspective of economic factors. However, foreign or international lobbying is sub-part of international relationship. The international lobbying or lobbying strategies should be analyzed below Japan-America relationship. Before 1980, America was responsible for Japanese national defense. America regarded Japan as his dependency, it is easy to understand that Japanese, even their Japanese corporations, could not resort to confrontation but non-confrontation lobbying strategies. However, in 1980s, America returned the national defense to Japan and asked her to shoulder more responsibility in resisting the Soviet Union and Socialism. At the same time, America attributed its economic depression to Japan and formulated several restrictions. On the contrary, Japanese economic reached almost same level or surpassed America. Therefore, Japanese dared to say "no" to American economic pressure. In this way, the transforming of bilateral relationship could also influence lobbying strategies, which was from non-confrontation to confrontation.

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