Chapter 14
Understanding FDI in Socialist Nations:
A Comparative Study Between China and Vietnam

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ABSTRACT

The link between foreign direct investment and economic growth has been widely studied. The studies have provided insights into how developing nations enable growth by adjusting policies to entice investors. Foreign investors entering emerging markets have to make strategic decisions on how to set up their operations. Investors look for markets and countries that would maximize their returns and position themselves as leaders in the industry. Hence, understanding entry requirements and economic policies are vital to understanding FDI. Keeping this in mind, this chapter analyses FDI in socialist nations and how their policies have evolved over time. The chapter will analyze the motivations and trends in FDI and how institutional conditions have enabled or impeded growth. The chapter studies China and Vietnam and compares their approach to FDI. The chapter uses Eclectic Theory posited by Dunning to understand changes in policies and how socialist nations are evolving to accept FDIs. The chapter concludes with a comparison section and presents scope for further research.

INTRODUCTION

The 21st century world is characterized by globalization and an unprecedented fast-paced technological evolution. The world is currently in a shift from ICTs to a new, undefined technological paradigm spearheaded by Artificial Intelligence. On a parallel line, Global Production Networks (GPN) and Global Value Chain (GVC) have created a need for regional development to create a truly interdependent framework. Though the debate over FDI has subsided since the 1980s, its role in development has been heralded as

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a game changer. However, its role in development comes with impediments. Global income inequality is fuelled by FDI and more in developing nations than developed.

This chapter will analyse the motivation and trends in FDI and the development of GVCs in the initial segment the chapter will put forth clearly with help of data and research the FDI trends across geographies. This will help establish how and why nations choose to make FDI a strategic component of their economic policy. The chapter then moves on to detail "Eclectic Theory" a popular theory used to understand impact of FDI on countries. Using this theory the issues and impact of FDI on a nation's economy and its correlation with other policies will be assessed through two case studies. So as to provide a level playing ground for analysis countries with similar political ideology the key influencer in any foreign collaboration has been chosen – China and Vietnam. The chapter will conclude with takeaways and scope for further research.

FDI and Development: Motivation and Trends

FDI has proven to be a better option than trade for firms to leverage endowment factors between home and host nations. The primary reason for this is that FDI enables MNCs to own and control operations abroad. This enables them to control overseas profits and capture market that would have otherwise been taken by importers and exporters. Historically, companies have invested overseas to gain access to local natural resources. Locational advantages can be defined as "benefits arising from a host country's comparative advantages accrued to foreign direct investors" (Shenkar & Luo, 2008, p.63). FDI inflows tend to be influenced by business environment of host nation, infrastructure, policies of the countries and access to minerals (Popovici & Călin, 2014). The choice of location is also influenced by behaviour and motivations of the firm. For instance, a resource seeking firm's objectives to engage in FDI would differ from a market seeking firm.

Firms generally tend to invest abroad to acquire a particular resource at lower real costs than the cost they would have incurred in their home country. This makes the motivation of FDI for the MNC to become profit-oriented and competitive in the markets it serves or intends to serve (Shenkar & Luo, 2008). For instance, PepsiCo heavily invested in Brazil and Argentina (Madura, 2008; PepsiCo, 2018). The main reason for investment were benefits resulting from economic liberalization. Labour differentials, non-tariff barriers and tariff policies are important while choosing a country to invest. MNCs tend to use knowledge of market and information scanning abilities to select countries that would reap them the most profit.

MNCs are also motivated by policies taken by states. For instance, tax incentives, investing in greenfield projects, and subsidies on cross-border resources make FDIs a lucrative form of investment. Figure 1 provides an understanding of the number of national investment policy measures have affected the areas where companies invest. Other motivations for MNCs to invest in a nation include:

1. Reduced inventory costs
2. Efficient utilization of capacity
3. Access to domestic markets with specialized skills
4. Benefits from special tax privileges
5. Benefits from special tariff treatments between host nation and key trading partners (Abe, 2009).