Comments on “Does Bank FDI Promote Firm FDI? Evidence from China's Outbound Multinational Activity” by Chor, Li and Kikuchi

Toshihiro Okubo

Keio University

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This paper

- Investigate whether banking FDI leads to Manufacturing FDI.
  - Using the Chinese outward FDI micro-level data in banking sector and manufacturing sectors
  - Basic mechanism is in the line of Melitz/Manova.
    - Reducing FDI costs by Chinese banks promotes FDI
- Results are clear.
  - Chinese Big 5 banks' FDI (at t-1) promotes entry of Chinese manufacturing FDI (at t).
  - c.f. Chinese Big 5 banks' FDI (at t+1) is not significant
- Several sensitivity tests
  - Timing issue (placebo test)
  - Carefully dealing with causality issue
  - Spillover issues
  - Collocation of other countries' banks FDI.
  - Main bank relationship

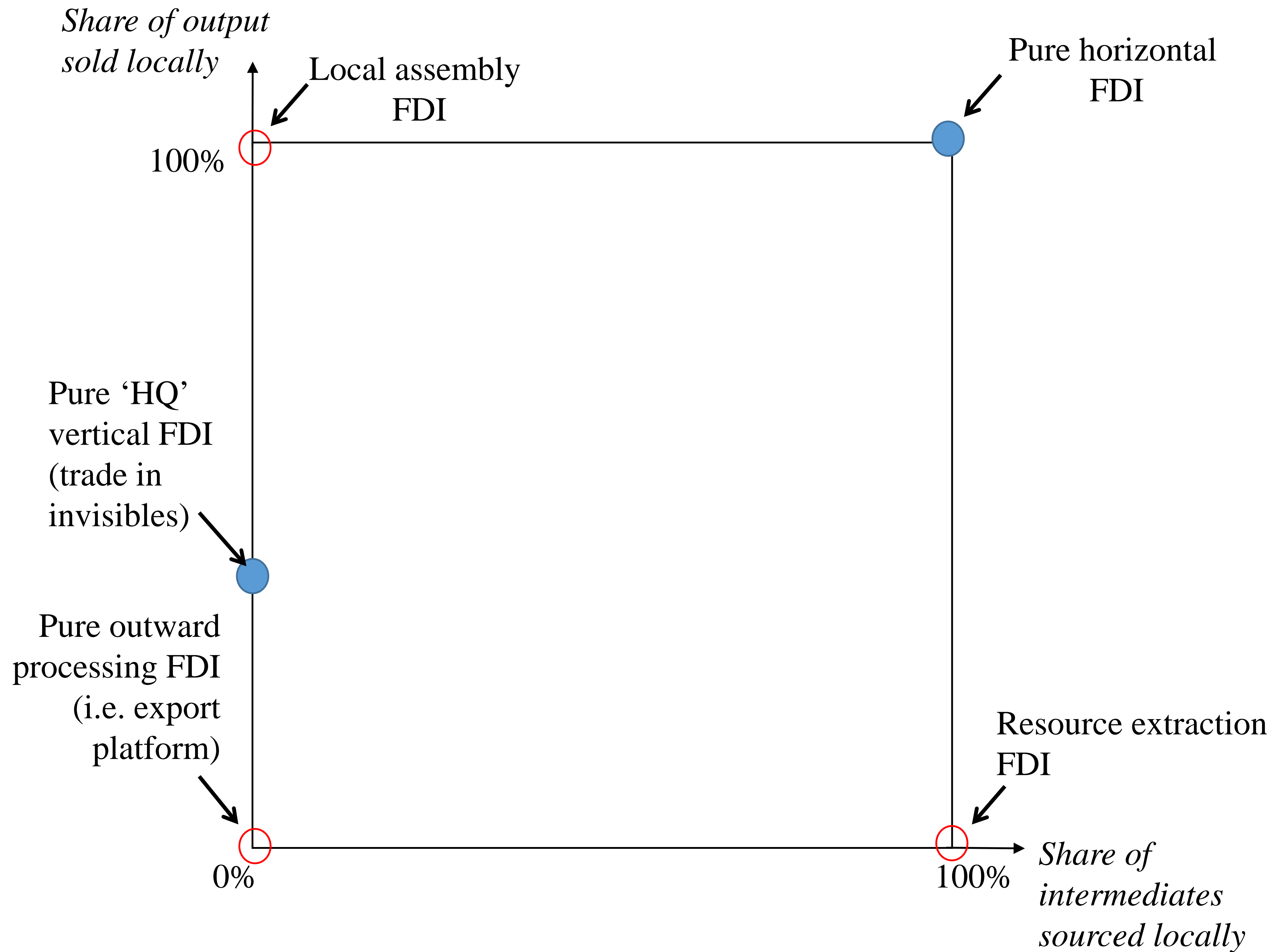
Back to FDI literature

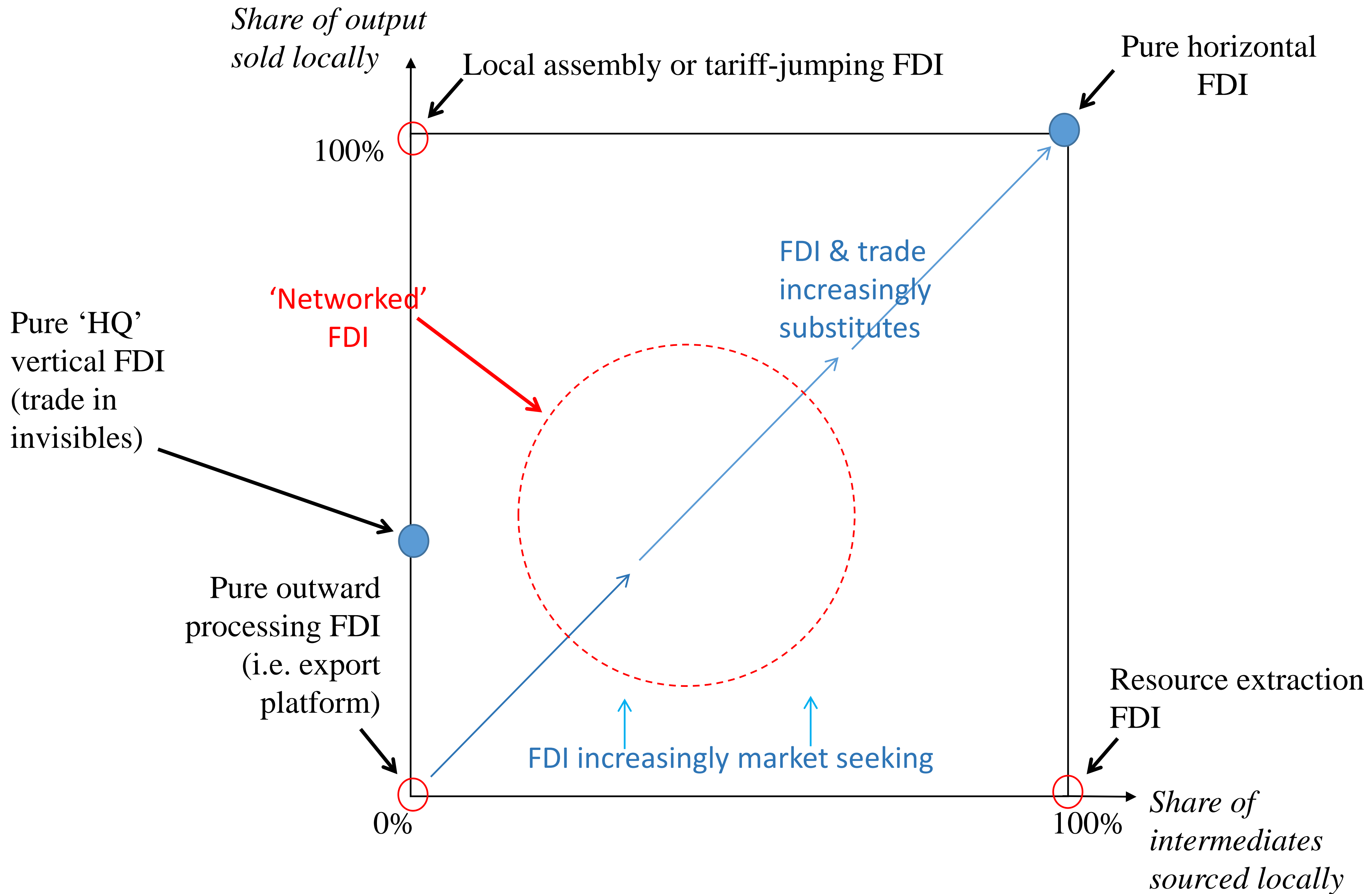
- Most studies study manufacturing FDI
  - The contribution of this paper is to shed light on the role of banking FDI
- FDI literature has classified FDI as horizontal and vertical FDI.
  - Horizontal FDI: Market seeking
  - Vertical FDI: Cost seeking
  - Complex FDI (Yeaple, 2003), fragmentation (Ando and Kimura, 2003,2005), platform FDI (Ekholm et al, 2005), network FDI (Baldwin and Okubo, 2014)
- Questions arise.
  - 1. Only new establishment of Chinese firms (entrant) need credit lending?
    - Greenfield FDI might be costly and M&A might be less costly
    - Local purchase by foreign affiliates might need more long-term credits.
    - Expand business might need more credits.
  - 2. Different FDI types might need different credit demands?
  - 3. Many other ways of finance? Short-term/long-term lending, support by trading companies, bond, stock market, etc

Sales-Sourcing box diagram

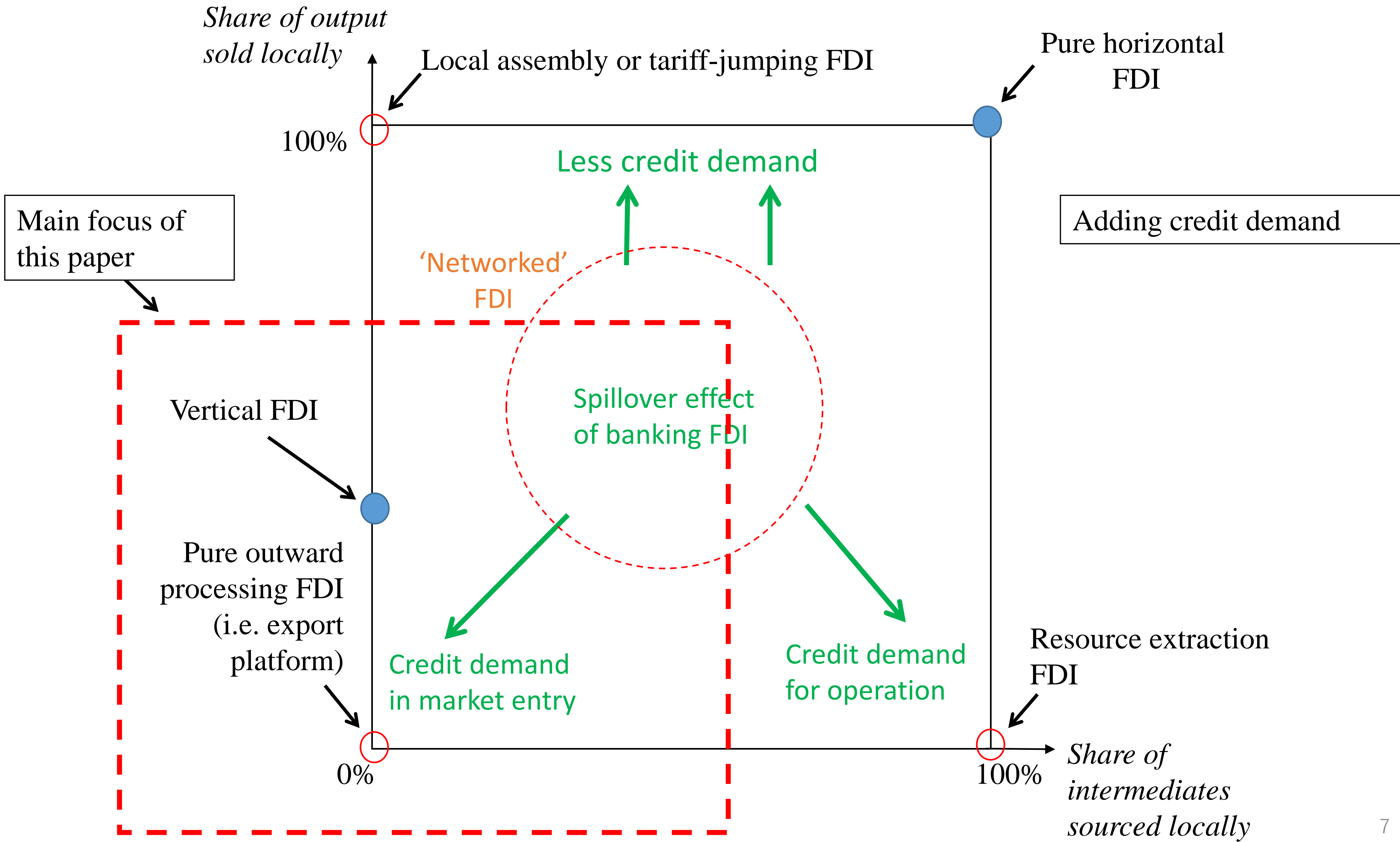
- Baldwin and Okubo(2014)
  - All FDI types are in one box diagram.

  - Local sourcing vs local sales in host country
    - We can measure credit demand by FDI in host country
      - Newly established FDI needs credits (as FC).
      - More local sourcing needs more credit in host country
      - More local sales reduce credit demand in host country


Share of output sold locally
Local assembly FDI
Pure horizontal FDI
100%
Pure 'HQ' vertical FDI (trade in invisibles)
Pure outward processing FDI (i.e. export platform)
Resource extraction FDI
0%
100%
Share of intermediates sourced locally



Share of output sold locally
Local assembly or tariff-jumping FDI
Pure horizontal FDI
100%
FDI & trade increasingly substitutes
'Networked' FDI
Pure 'HQ' vertical FDI (trade in invisibles)
Pure outward processing FDI (i.e. export platform)
Resource extraction FDI
FDI increasingly market seeking
0%
100%
Share of intermediates sourced locally



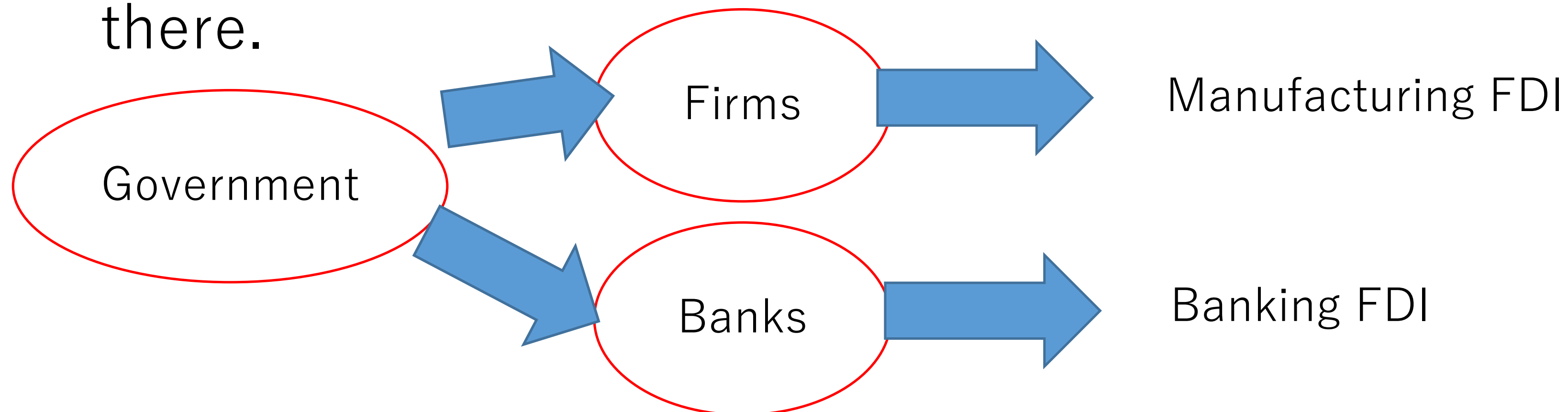
Share of output sold locally
Local assembly or tariff-jumping FDI
Pure horizontal FDI
100%
Less credit demand
Main focus of this paper
Adding credit demand
'Networked' FDI
Spillover effect of banking FDI
Vertical FDI
Pure outward processing FDI (i.e. export platform)
Credit demand in market entry
Credit demand for operation
Resource extraction FDI
0%
100%
Share of intermediates sourced locally

Back to banking literature

- This paper hinges on FDI mechanism a la Melitz and Manova.
  - However, the banking literature provides much richer insights and interpretations
- (1)Sectoral heterogeneity (credit-dependence)
  - High credit-dependence in some sectors
  - Rajan and Zingales index
  - High exposure to host country risks in high credit dependent sectors
    - Chinese bank protects Chinese FDI firms in host countries
- (2)SME Chinese firms
  - SME faces credit constraint and less access to local financial market
  - High exposure to host country risks in SME
    - Chinese bank protects Chinese SME FDI firms in host countries
- (3) Various channels for financing
  - Long-term/short-term bank lending, bond, stock, etc.
  - Finance by parent firms and affiliated firms

Still some concerns in causality issues

- There are some possible scenarios
- Scenario 1: Chinese government policies
  - Target destination countries (correlate with political relationship and diplomatic strategy)
  - Chinese government authorities put some high pressure (or tax/ subsidy schemes) on banking sectors as well as manufacturing firms (in particular SOE)
  - Banks go to the targeted country and then firms subsequently go there.



Some other possibilities

- Scenario 2: Conglomerate of bank and manufacturing sectors
  - Big 5 banks have ownership of some manufacturing firms
  - Big 5 banks FDI results in manufacturing sectors
- Scenario 3: Trade association, regional associations, semi-government organizations
  - The organizations provide some local meetings. Big 5 banks do “pre-play communication” with some manufacturing firms. Big5 promotes their FDI by promising credit assistance a priori.