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THE COMPARISON OF THE CHINA AND JAPAN ON THE ATTRACTING FOREIGN DIRECT INVESTMENT

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Abstract

As Asia's two economic powers, the relation between China and Japan in the aspects of foreign direct investment is closer. In this paper, we through the date from 1988 to 2012 to study direct investment between China and Japan and the mode of direct investment on the empirical analysis. Results show that in the long run, Japan's foreign direct investment in China and export to the domestic economy has a promoting effect, while Japan's exports has inhibitory effect on China's economic growth, and imports have interaction with GDP. Japan's economic changes have a big impact on China's economic, but China's economic growth for the Japanese economy has obvious promoting effect.

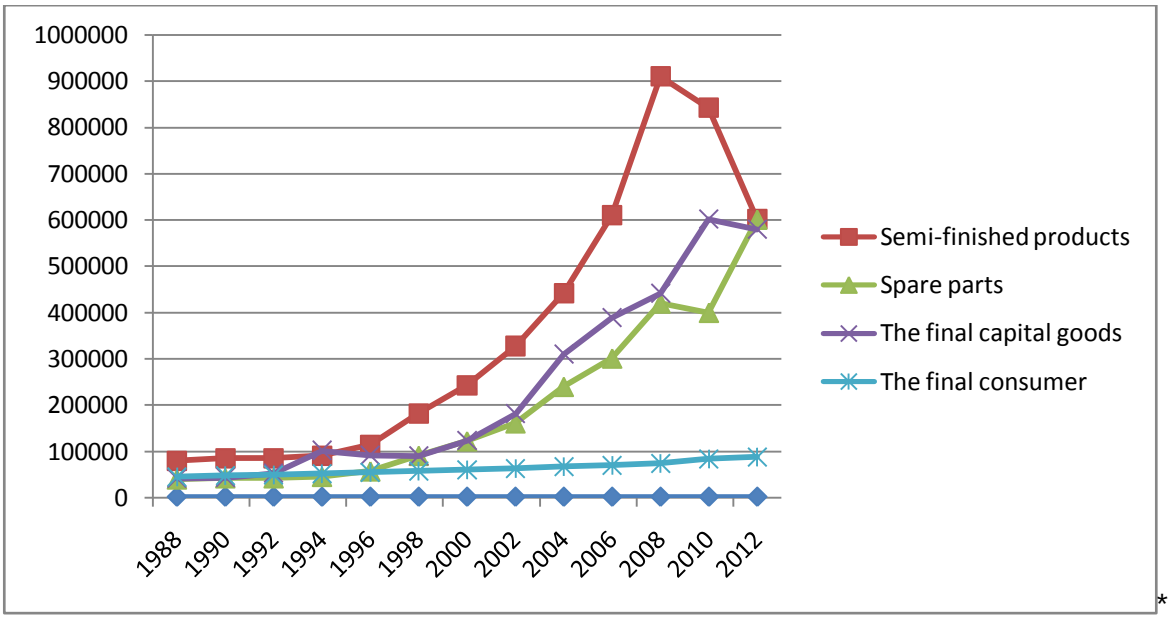
Keywords: FDI, China, Japan, similarities, difference, Investment

INTRODUCTION

According to Japan attractiveness survey 2008, China and Japan have become two of the popular international investment destination states in Asia in the early 21st century. After implementing the open-door policy in the early 1980s, China's economy was increasing rapidly in the 1990s and early 21st century. There was a rapid growth of FDI in China from 1983 to 1993 and the peak of FDI inflow was approximately 120 billion dollar in 1993, followed by 8-years restructuring of FDI flows, then only China keeps a growing trend of attracting FDI till now. Furthermore, China's GDP has ranked second in the world in the early 21st century. Compare with China, Japan, which is a developed country in East Asia as well as the important economy to the world, also has advantages to attract different kinds of foreign capitals. Even though the conditions to invest in Japan were relatively rigid in the past, the major limitations to investors have been gradually reduced since the 1980s, such as the Foreign Investment and Exchange

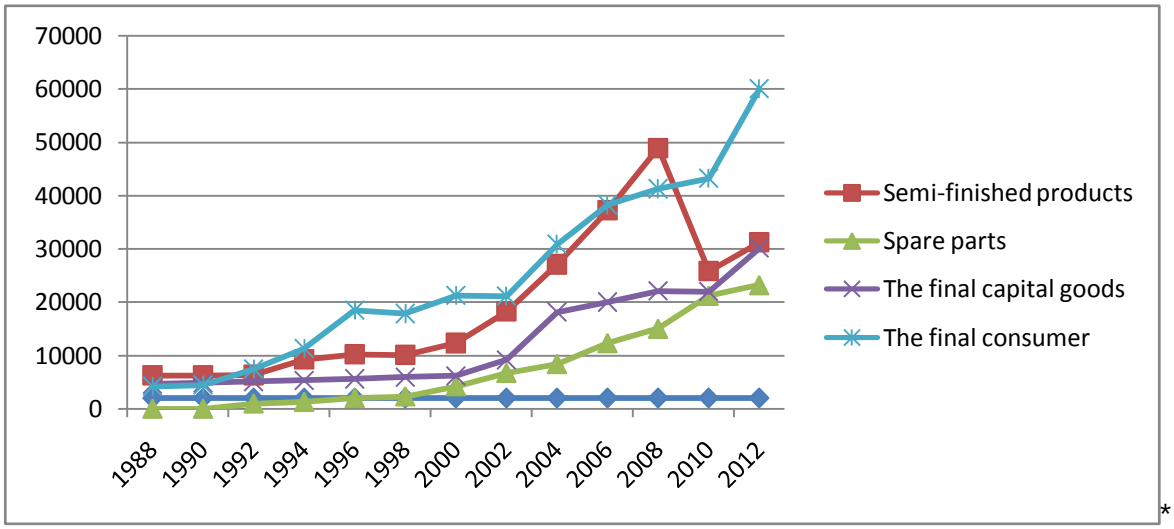
Control Law. At the same time, the trade between the two countries also rise as quickly and as the growth of the Japanese investment, based on the classification of BEC from 1988 to 2012, the two countries are divided into: semi-finished products, spare parts, final capital goods and final consumer goods so on four categories. The Table 1 and Table 2 show them in the following:

Table1. China's commodity classification of import from Japan



Source: Ministry of Commerce of the People's Republic of China (2013)

Table 2. China's various types of merchandise exports to Japan



Source: Ministry of Commerce of the People's Republic of China (2013)

INWARD FDI AS A PERCENTAGE OF GDP

According to the JETRO Global Trade and Investment Report 2013, Japan's GDP ratio of inward FDI is only 3.7%. Compared with Japan, inward FDI takes up 10.3 of China's GDP in 2013.

The reason why Japan's inward FDI remains at a low level could be ascribed to an array of contributors. To begin with, foreign enterprises in Japan face the issues of choosing the proper management method. Methe (2005, 35) indicates that the need of accommodate Japanese management approaches is still a puzzler to FDI. Besides, the recruitment of localization could be a problem. Methe (2005, 36) concluded that the ratio of Japanese who works for foreign companies remains very low at around 2% of the total employment. Usually, Japanese employees think that the job security of foreign enterprise is relatively low, in terms of the economic depression or the companies without good growth in profit (Mathe, 2005, 36). Moreover, potential restrictions are still existed. Hidden limitations might be the major barriers to foreign investment to entry Japan's market. For example, Schaede concludes that the Japanese market of many fields is still restricted though non tariff barrier to trade and the governance of direct import have been phased out since 1980s. He also suggests that Japan's regulation system in the post-war period is based on the hidden prohibition of foreign capital entry. Apart from the obstacles mentioned above, cross-holding and stable holding of shares could be contributors as well. Many Japanese companies take advantage of these approaches of holding share to fight against acquisition because the approaches can limit the influence and governance from the financial market (Methe, 2005, 27). At the same time, there are around 40% of the stocks can be dealt in the financial market because around 60% of them held by the stable stockholders (Methe, 2005, 35). Last but not least, the cost of doing business might also be the major obstacle to Japan's inward FDI. The biggest barrier to Japan's inward FDI is the business cost, followed by the uniqueness of Japan's domestic market, and the languages barrier in order.

In the case of China, inward FDI plays an important role in its economy. It can be ascribed to an array of contributors. Firstly, the incentive policies implemented by the government have a positive influence on the inflow of FDI to China. Zhang (2002, 54) concludes that the Chinese government adopts a series of incentive policies to improve the commercial environment for attracting FDI, including the establishment of special economy zones, several cities opened for attracting FDI, tax reduction, relatively cheap land price and rent, and the flexibility and convenience of foreign currency swap in the special costal cities. Secondly, China's market size is also a vital factor. As Schwab (2013) concluded, China's market scale is the second in the world which means it is a strong advantage. It is without doubt that the GDP

growth of China has kept an increase trend at around 8% annually since 1980s. Apart from the GDP growth, Ali and Guo also indicate that market scale can be associated with the GDP growth, which means a large market can receive more foreign enterprises' investments. According to this point of view, China's huge market scale is an apparent advantage to attracting a great amount of foreign capital. Thirdly, the business expenditure could be the factor as well. China's relatively competitive workforce wage and its population can affect the growth of inward FDI, to some extent. Compared with Japan and other regional countries, China is the most competitive leader in the region in terms of the commercial costs. According to the Global Competitiveness Report 2013-2014, China's pay and productivity, which is ranked 17 among 148 economies, is still relatively competitive. Nevertheless, it seems that this advantage is not as strong as before, because China is facing challenges from countries with lower workforce price, such as India, Vietnam and Laos.

SOURCE OF INWARD FDI

In comparison, the major source of inward FDI into China comes from neighbour countries or regions before 2002, particularly from Hong Kong, Macau and Taiwan (Whalley and Xin, 2010, 3). Ali and Guo indicate that a great amount of China's inward FDI comes from the Asian states and round-tripping foreign capitals, which are mainly from Hong Kong, Macao and Taiwan, plays an important role in this economy activity. After 2002, FDI inflow in China has become more diversified, because there is a growth of the investments from America and other developed states (Whalley and Xin, 2010, 3). Hence, the reason why the resource of FDI inflows is different between China and Japan can be ascribed to a host of factors.

Generally speaking, China and Japan are driven by different kind of factors in terms of their economic pattern. According to Japan attractiveness survey 2008, China now is a labour-intensive economy while Japan is knowledge-intensive. On the one hand, it means that investments in Japan mainly focus on knowledge-intensive industries, such as technology and high-value added product, for the business cost is high. According to JETRO survey on foreign company in Japan , there is not significant improvements of Japan's commercial environment, such as land price, the expenditure of using utility, tax rate and labour cost. The Japan attractiveness survey stresses that around 50% of investors asked for tax reduction, and 38% of them expected for reduction of labour price. Beside, one feature of knowledge-intensive economy is that a large amount of capital is used in research and development. According to Japan attractiveness survey 2008, Japan's commercial competitiveness in terms of research and development centre was ranked No.1 while China ranked No.2. Moreover, according to the Global Competitiveness Report 2013-2014, Japan's economy is driven by innovation and its

competitive strengths are the ability to innovate new and competitive goods and the level of commence sophistication. At the same time, training and higher education of Japan, ranked 21 among 148 economies, are considered as relatively competitive advantages. So it is apparent that the employees with higher education and professional skills and the mature research environment have a positive impact on Japan's economy. According to the research, two of Japan's merits are including the constant supply of skilled and competent workers, the information and technology environment. Therefore, heavy tax burden and high labour price are main obstacles for Japan to attract FDI of manufacturing, except for investments in high technology and innovation areas.

On the other hand, it means that inward FDI in China prefers labour-intensive industries. It can be attributed to an array of advantages, including the constant supply of qualified and cheap wage, inexpensive commercial cost, such as letting and land price, the significant market for services and production . Furthermore, among 6 Asian states or regions, including China, Japan, South Korea, India, Singapore and Hong Kong, China was ranked No.1 in terms of the business competitiveness in the manufacturing area, whereas Japan only ranked No.6. Besides, China now is an efficiency-driven economy. If the state continues to attract FDI, it needs to maintain the competitive strength in the following areas, including training and high education, the efficiency of labour market, market size including foreign and domestic market, the growth of merchandise market, financial market reforms. Hence, China is more suitable to those FDI which is efficiency-pursing.

FDI ENTRY MODE

There are different kinds of way for foreign investments to entry Japan and China. In the case of Japan, green field, joint venture and mergers and acquisitions (M&A) could be the common ways, In terms of the FDI entry model. Meanwhile, foreign investors might be more likely to select Equity Joint Venture (EJV), Wholly Foreign owned Enterprise (WFOE), Contractual Joint Venture (CJV) as their approaches to entry China's market.

As mentioned above, there are three major market entry patterns for FDI in terms of Japan, including mergers and acquisitions (M&A), joint venture and Greenfield. Firstly, M&A could be the primary entry approach to invest in Japan. For example, Fukao indicates that M&A is the major way to invest in Japan as well as other developed states. This could be ascribed to Japan's business environment after the bubble economy. Fukao suggests that the Japan's relatively weak stock market after the bubble economy and the domestic recession offer FDI a chance to acquire Japanese companies at a relatively affordable price. Moreover, the restriction from cross shareholding has been reduced. After the bubble economy, the proportion of cross-

holding share is declining, which means that it gives inward FDI growing opportunities to enter Japan's domestic commercial market. In addition, reform could also be an important contributor. The responsibility of issuing important and precise company information has become popularity since the second half of 1990s. It means that foreign investors can understand more about Japanese company's actual finance situation. Thus, M&A could be an effective way to directly invest in Japan, according to the commercial environment, the reducing obstacles from Japanese enterprises and the positive influence of reforms.

Secondly, joint venture, compared with M&A, sometimes cannot achieve consensus, ranging from decision-making and problem-solving, because it might be uneasy for foreign investors to operate the company. The business strategy of Japanese company could be one of the causes. As Methe (2005, 29) mentioned, Japanese decision makers are more likely to pursue larger market share, instead of focusing on current profit. However, unceasing pursuing market share has been an important cause of the decline of Japanese enterprise (Methe, 2005). Therefore, joint venture might not be the most effective way to invest in Japan.

Thirdly, Greenfield Investment might not be the best choice to foreign investors, especially to those who lack of any experience of Japan and their culture are largely different from this country. It could be attributed to a series of reasons, such as land price and supplier network. Not only can high land price negatively influence FDI, but also the difficult participation in the networks. For example, long-term work for establishing a certain reputation is essential to new company in Japan before being acknowledged by local companies (Methe, 2005, 34). More importantly, Japan's unique nature, which has been mentioned above, is one of the major entry barriers. And it could be a great challenge to foreign investors, especially those who lack local experience. In other words, it could be a huge work for foreign investors to do previous preparation, which might lose the best time to enter the market. Hence, Greenfield Investment is not the best way to entry Japan's market, compared with other two entry mode.

The major market entry modes in China, including Equity Joint Venture (EJV), Wholly Foreign owned Enterprise (WFOE), Contractual Joint Venture (CJV), are quite different from Japan (Ali and Guo, 2005).

In terms of the WFOE, it has been the most common way to invest in China. Poncet.S (2009,4) indicates that WFOE, which takes up more than 60% of China's total inward FDI, has been the most popular inward FDI into China since 2005. WFOE has an array of advantages, compared with joint venture. For example, it allows foreign investors to have more flexibility on corporate control and management strategies . Besides, it could avoid issues caused by a Chinese partner. For example, foreign investors might prefer profit and market share while Chinese partners are more likely to pursue technology as well as foreign advanced skills.

Moreover, WFOE does not have to go through special investigations, such as anti-monopoly review. Nevertheless, there are also some limits to WFOE. Chinese government now still does not allow foreign capitals to enter certain sensitive industries, such as telecommunication and military areas.

In comparison with Japan, joint venture is also a common entry mode into China. Usually, EJV and CJV are other common way to entry China's market. Ali and Guo concludes that CJV was the most common entry mode of FDI into China in the 1980s, and then WFOE and EJV has become more popular than CJV since the early 21st century. On the one hand, EJV is the entry mode that greatly encouraged by Chinese government. This can be attributed to two reasons. Firstly, the Chinese government largely supports this entry mode, for it believes that EJV can actually help local enterprises to promote their management skills, technology, and to solve the problem of developmental capital. Secondly, EJV could help foreign investors to understand more about China's market with the help of Chinese partners. On the other hand, CJV is a more expensive entry mode in terms of the business cost, such as the cost of maintaining the contract, compared with EJV and WFOE (Liu, 2004).

Nevertheless, CJV also has advantages, such as using future service as investment, in comparison with EJV which must prepare certain money for asset injection. Hence, WFOE and EJV and CJV are still the popular FDI entry modes into China through they have some disadvantages respectively.

Moreover, M&A in China is facing a variety of challenges, compared with Japan, such as the law restriction on share holding. It is also confronted with blocks or conditional approvals towards foreign investors, in terms of the Anti-Monopoly Law 2008. For example, the unsuccessful takeover on Huiyuan Juice Group by Coca-Cola is the classic case. Besides, Greenfield Investment in China is more popular, because China is still a developing country. In other words, there are a large number of investment opportunities, in terms of China's infrastructure development.

CONCLUSION AND DISCUSSIONS

The main research conclusion

In conclusion, there are some similarities between Japan and China, in terms of their performance of encouraging Inward FDI. Both Japan and China has similar size of market in the world, and joint venture is also one of the common FDI entry modes in two states. However, the differences between two nations are more than the similarities, in terms of the inward FDI as a percentage of GDP, source of inward FDI and the general FDI entry mode. Beside, flows of

inward FDI into Japan prefer high technology and innovation areas because it is a knowledge-intensive economy. Meanwhile, China inward FDI is more likely to invest in manufacturing, for it is a labour-intensive economy.

Discussions

China encourages foreign investment last a long time, on the one hand, China driving the development of the local economic development and keep up with the world pace, on the other hand ,China improve the domestic industrial structure that the introduction of advanced technology. China puts forward that adjusting and optimizing the investment structure to improve the level of the opening for the outside world that raise the level of utilization of foreign capital. The 18 the third plenary session put forward, in order to adapt to the new situation of economic globalization, must promote internal opening to the outside world and promote each other to go out and better for the combination to promote the international and domestic factors. It accelerates the speed of foreign investment into especially area which will attract more foreign investment.

The characteristics of Japanese investment in China is following: products will through China for processing and packaging, and then the final product will sold to all over the world, of which a large part of domestic products to Japan. Originally it is a sunset industry in Japan, but they transferring them to China makes it has the competitive advantage of industry, result from using China's cheap labor market at a low cost of production and processing after China's huge potential market demand. At the same time, the final product which after processing in China will sold to domestic ,it also can meet the needs of domestic. Under the framework of production networks in east Asia, Japan's investment and trade is the complementary relationship and Japan the marginal characteristics of industry transfer of foreign direct investment in China all will provide a reference for China's foreign investment.

WAY FORWARD

The structure of all kinds of trade relations between the two countries, we need to be further in-depth study. Because Japan is important source of investment in China, the study of the problem will also help China optimize adjustment of trade structure ,and will be more reasonable for the introduction of foreign capital and foreign capital utilization policy.

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