Motivations for Outward FDI from Emerging Economies to Advanced Economies: A Literature Review

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***Abstract* - Outward Foreign Direct Investment (FDI) from emerging economies in recent years has experienced rapid growth, especially from the BRIC (Brazil, Russia, India, and China) economies. This has gained much attention from international business researchers. The present study assessed the motivations for the outward FDI from emerging economies to advanced economies based on literature review. The paper revealed that market seeking, natural resource seeking, strategic asset seeking, efficiency seeking, and home government support motivate firms from emerging economies to invest in advanced economies. However, efficiency seeking least motivates China's outward FDI due to its low labour cost. The study also made an evaluation of the existing theories of FDI to determine whether they adequately explain such investments. Based on the evaluation, the OLI Paradigm and the Resource-Based View do not adequately provide a plausible explanation for such investments. However, emerging economies outward FDI to advanced economies seemed to be adequately explained by the Institutional Theory.**

***Keywords* -** *Outward FDI, Emerging Economies, Advanced Economies, FDI Theories*

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I. Introduction

Foreign Direct Investment (FDI) has become a significant factor in contemporary globalization (Almsafir et al., 2011). FDI is seen as an essential instrument for economic growth in both developed and developing economies (Ross, 2015; Yakubu & Mikhail, 2019). Over the years, emerging economies have been the major zones for foreign direct investment from advanced economies (Zhang & Daly, 2011). According to the World Bank, Outward FDI includes "transfer of assets and liabilities between residents and non-residents' fellow enterprises, if the ultimate controlling parent is resident" (Datahelpdesk.worldbank.org, 2016). The growth and motivations for outward FDI from emerging economies have gained much attention from international business researchers (Buckley et al., 2007). Several studies (for example Lin, 2010; Labes, 2015) have examined the drivers of FDI inflows in emerging economies. However, the motives regarding outward FDI from emerging economies need much clarification. This paper will therefore outline the motivations for outward FDI from emerging economies, and at the same time evaluate whether existing theories of FDI clearly and adequately explain such investments. The study is organized in two sections. The first section assesses the motivations for outward FDI from emerging economies, and the second part outlines whether existing theories of FDI adequately explain such investments from emerging economies.

II. Motivations for Outward FDI from Emerging Economies

Several studies have been conducted on the motivations of Outward FDI from emerging economies. Such motivations are discussed below.

2.1 Foreign Market Seeking

Market seeking has been one of the major reasons why emerging economies undertake outward FDI to advance economies (Buckley et al., 2007). As argued by Chakrabarti (2001), firms are motivated to invest in foreign markets with greater growth potentials which gives them the opportunity to maximize returns as well as enjoy economies of scale. A study by Holtbrugge and Kreppel (2012) in determining the outward FDI of BRIC (Brazil, Russia, India, and China) countries revealed that outward FDI from Brazilian firms is motivated by market seeking reasons. They argued that domestic competition among firms in Brazil and foreign companies in Brazil has increased due to the openness of the Brazilian economy. As a result, firms are pressured to expand to new markets in both neighbouring and developed economies. Holtbrugge and Kreppel also found Russia, China and India outward FDI to be influenced by market seeking. China's membership with the World Trade Organisation has allowed more MNCs to invest in the country creating more competition in the local market, hence forcing most Chinese firms to engage in outward FDI to advance economies in order to increase their presence in the foreign market. Kalotay and Sulstarova (2010) argued that the size of foreign markets greatly influences Russian firms’ decision to make investments in the international markets. They explained that the acquisition of companies in the EU by oil and gas companies in Russia indicates the extent of Russia outward FDI in advance economies. According to Das and Banik (2015), Indian firms have increased their outward FDI to advanced economies through joint ventures and wholly-owned subsidiaries, which accounts for their market seeking outward FDI. For example, Infosys BPO (an Indian company) established wholly-owned subsidiaries in USA and Australia.

2.2 Natural Resource Seeking

According to Dunning (1993), acquiring natural resources motivates firms to make investments in other countries. Natural resource accessibility has been a motivator for Chinese firms' outward FDI (Kang & Jiang, 2012). Deng (2004) posits that though China possesses some natural resources, in terms of per capita availability, such resources are quite low especially in areas of petroleum, aluminum, timber which demand is on the increase. As a result, Chinese firms are driven to engage in outward FDI to developed economies in search for such natural resources. Kalotay and Sulstarova (2010) explained that obtaining quality natural resources from advanced economies has been a major motivator of Russian mining firms to engage in outward FDI. According to the World Investment Report (2006), access to natural resources accounts for most Indian firms' outward FDI. As explained by Beerannavar (2013), there has been an increase in the acquisition of mining and oil companies by Indian firms in order to get access to mining and oil resources in the advanced economies which are relatively scarce in India (Example; Hindalco (an Indian company) acquiring most Australian copper mines). Also, Reliance Industries Ltd (an Indian firm) acquisition of Pioneer Natural Resources Co. (in the USA) demonstrates the natural resource seeking outward FDI of Indian firms to the advanced economies (Das & Banik, 2015). Natural resource acquisition by emerging economies from advanced economies has gain the attention of national governments from emerging economies, as most of them (example; China) have made efforts to establish relations with other countries to facilitate easy access to natural resources by firms from emerging economies (Morck et al., 2008; Duanmu & Guney, 2009).

2.3 Strategic Asset Seeking

According to Dunning (1998), strategic asset seeking has been a significant motive for firms to engage in outward FDI in different countries. Strategic assets such as advanced technology, managerial skills, superior brands, etc. are necessary for firms to compete globally (Ye, 1992; Deng, 2004). Taylor (2002) argued that over the years, China’s motive for outward FDI has been primarily to obtain strategic assets in areas such as advanced technology, research and development as well as superior brands. Similarly, Kalotay and Sulstarova (2010) explained that the investment motives of transnational corporations in Russia especially those in the automotive telecommunication industries are driven by access to technology and strategic assets such as local distribution outlets and quality brands, typically in the developed countries. Holtbrugge and Kreppel (2012) also found that strategic asset (managerial skills, technological know-how, and brands) seeking is a significant driver of outward FDI from firms in Brazil, India, and China to advanced economies. Holtbrugge and Kreppel illustrated the strategic asset seeking motive of these firms by using some selected firms in Brazil, China, and India. For example, building a superior global brand and technology were the key motivators behind the acquisition of the personal computing division of IBM by Lenovo. Also, another example is the acquisition of 5% share of EADS (European aerospace firm) by VTB (a Russian bank), which was motivated by access to modern technology and managerial skills (Holtbrugge & Kreppel, 2012). Das and Banik (2015) argued that technological seeking has been a major driver of Indian pharmaceutical industry outward FDI to advance economies, especially in the USA and Germany.

2.4 Efficiency Seeking

Outward FDI from emerging economies to advanced economies is also motivated by efficiency seeking though this varies across countries (Gugler & Boie, 2008). Low labour cost in developing countries usually serves as a motive for advanced economies to invest in developing economies (Ross, 2015). As a result, some studies (for example, Buckley et al., 2008; Deng, 2004; Kang and Jiang, 2012) argued that outward FDI from emerging economies is unlikely to be motivated by efficiency seeking due to efficient cost of labour (for example; China). However, De Mello (1997) posited that emerging economies are still motivated to invest in advanced economies due to labour conditions and labour quality. Holtbrugge and Kreppel (2012) argued that the recent investment by Russian oil and gas companies to the advanced economies has been motivated by efficiency seeking due to increase in oil and gas prices. Similarly, Holtbrugge and Kreppel explained that Russian banks (example; VTB, a Russian state-owned bank) have increased their investment worldwide including investment into major advanced economies such as the UK, Germany, and France in order to minimize cost.

2.5 Home Government Support

Governments from emerging economies have been a major source of motivation for outward FDI by emerging economies into both developing and developed economies (Luo & Tung, 2007). The crucial role played by home governments in emerging economies in promoting outward FDI has been examined by Cheung and Qian (2009), Morck et al. (2008) and Holtbrugge and Kreppel (2012). They explained that firms from emerging economies especially Russia and China receive strong motivations by their home governments to invest overseas through the provision of support in terms of financial and technical support, and at policy making. Dunning and Narula (1999) argued that the growth in outward FDI from emerging economies has been as a result of policy liberalization by home governments to support firms to invest abroad. According to Gammeltoft et al. (2010), through the "going global" policy which was adopted by China in 1999, the Chinese government has increased its support for outward FDI in China. This has led to a sharp growth in China's outward FDI in both developed and developing economies (Kolstad & Wiig, 2012). China has also increased its support for outward FDI through its Sovereign Wealth Fund, China Investment Corporation (Hu & Cui, 2014). Mowla et al. (2004) posited that due to favourable government policy support such as tax breaks, outward FDI for Indian pharmaceutical companies has increased dramatically. Similarly, Holtbrugge and Kreppel (2012) explained that strategic industries in Russia such as oil and gas industries have received support from the home government to invest abroad.

III. Evaluation of FDI Theories in Explaining the Outward FDI From Emerging Economies

Among the existing theories of FDI include the OLI framework or the Eclectic paradigm developed by John Dunning, the Resource-Based-View theory, and the Institutional theory. These theories are outlined below to consider whether they explain the outward FDI from emerging economies.

3.1 The OLI paradigm and Outward FDI from Emerging Economies

This indicates three sources of advantages that firms may possess to become competitive as multinationals. The OLI represents Ownership, Location and Internalization advantages. The OLI paradigm provides the most comprehensive explanation to the emergence of FDI. As outlined by Dunning, FDI is as a result of ownership, location and internalization advantages. However, the OLI framework may not adequately explain the current trend of outward FDI from emerging economies into advanced economies. Firms from emerging economies may not have ownership advantages such as advanced technology, quality brands, and managerial know-how as in the case of firms from advanced economies. As argued in the study, emerging markets are motivated to acquire these strategic assets in the advanced economies which they lack. Hence, the ownership advantage of the OLI falls short in providing a vivid explanation to such investments from emerging economies. In addition, considering the high cost of labour, manufacturing cost and high transaction costs in the advanced economies compared to developing economies, the locational and internalization advantages may not also provide a comprehensive explanation for the outward FDI from emerging economies into advanced economies.

3.2 The Resource-Based Theory and Outward FDI from Emerging Economies

The resource-based view suggests that scarce, valuable, and non-substitutable resources serve as a major source of competitive advantage for a firm which results in superior performance (Peteraf, 1993). As argued by the resource-based view, a firm is able to engage in FDI through the use of its valuable and unique brands, and advanced technology (Hsu & Pereira, 2008). However, as indicated in this study, firms from emerging economies lack these scarce resources, which they rather seek from advanced economies. Therefore, the resource-based view does not explain the outward FDI from emerging economies to advanced economies.

3.3 The Institutional Theory and Outward FDI from Emerging Economies

The institutional framework or system of a firm's home country affects the internationalization strategies of the firm (Peng et al., 2008). Favourable home country policies will motivate firms to invest overseas (Buckley et al., 2007). On the other hand, countries with poor institutional systems lead to high transaction costs (Meyer, 2001). As evidenced in this study, governments from the emerging economies provide support in the form of finance and policy formulation to motivate firms to invest in overseas markets. Therefore, the institutional theory in a way provides some explanation to outward FDI from emerging economies.

V. Conclusion

In conclusion, the paper assessed the motivations for outward FDI from emerging economies into advanced economies, and also considered whether existing theories of FDI adequately explain such investments. The study revealed that market seeking, natural resource seeking, efficiency seeking, and support from home country government forms the major motivations for the outward FDI from emerging economies. Efficiency seeking in terms of labour cost seems to be the least motivator for some emerging economies (example, China) due to low labour cost. The study also revealed that the OLI paradigm which forms the most comprehensive FDI theory does not adequately explain the outward FDI from emerging economies. The Resource-Based View also falls short in explaining such investments. However, the Institutional theory which considered home country government policies seems to provide an explanation to the outward FDI from emerging economies, due to the favourable policies and support received from the home governments.

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