Location Choice in Low Income Countries: Evidence from Japanese Investments in East Asia

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**Extended Abstract**

The emergence of China has given other developing countries a threat of multinational enterprises’ (MNEs’) concentration in China. China has attracted a vast volume of foreign direct investment (FDI). Since 1979, the country has attracted foreign firms as part of her export promotion policy. Afterwards, the increase of inward FDI has been outstanding since 1990. In particular, it expanded rapidly after Xiao-Ping Deng’s “Southern Tour Speech” in 1992. Furthermore, the rate of its increase seems to have been steadier since the country joined the WTO. As a result, in 2008, according to FDISTAT (UNCTAD), the inward FDI stock is ranked 1st among developing countries (10th in the world). Based on this fact on the large inward FDI in China, policy makers in developing countries particularly in ASEAN countries have worried about the decrease of inward FDI in those countries by replacing it with FDI in China. In short, China has been perceived as a potential absorber of world’s FDI to developing countries.

The purpose of this paper is to investigate the location choice of Japanese MNEs in East Asian developing countries at the subnational-level: China, Cambodia, Laos, Myanmar, Vietnam, the Philippines, Thailand, Malaysia, and Indonesia. Specifically, we call the basis of our analysis the province-level though it is not exactly province in some countries. In our sample host countries, the province-level analysis is necessary because there seem to be relevant differences not only across countries but also across provinces within a nation. For example, the target provinces of the open-door policy have been concentrated in the coastal region of China and thus there may be qualitative differences in policy treatment between coastal and non-coastal regions. In order to take care of subnational-level differences, we choose provinces as an analytical unit of our model.

In this setting, we conduct two kinds of analyses. First, by examining the location choice with the nested-logit model, we seek the appropriate nested structure of Japanese MNEs’ location choice in East Asian countries, i.e., their substitution patterns among those countries. For example, we intend to investigate empirically whether Japanese MNEs consider China and ASEAN countries as two distinct groups of potential host countries by examining the inclusive value parameters in the nested-logit estimation. This analysis is expected to give us some insights on the above-mentioned policy makers’ concern on whether or not, for foreign investors, China is substitute or complement to ASEAN countries. In particular, unlike the previous studies in the location choice literature, we estimate four-stage nested-logit model rather than simple two-stage nested-logit model. Second, the paper quantifies the importance of host country’s tariff rates against investing country’s products, compared with that of investing country’s tariff rates against host country’s products. While the former type of tariffs matters in MNEs’ importing parts and components from home, the latter type of tariffs becomes crucial in their exporting finished products to home. By introducing these two types of tariffs into our model, we examine those relative importance in the location choice of MNEs.

***Keywords*:** Location Choice, Multinational Firms, Nested-logit Model

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