

Firm Level Decision of FDI in China: Taiwanese Electronics Producers

Daniel Xu

Abstract

China has experienced extremely rapid growth in productivity and exports during the past few decades. Its relatively low wage rate has made it an attractive destination for foreign firms to offshore part of their production. It has long been the largest FDI recipient among developing economies.

Taiwan is one of the most important source countries of FDI in China. It is the second largest sender, right after Hongkong. If we take into account the fact that large portion of Hongkong FDI involves Taiwanese firm “diversion”, Taiwan plays an even more important role.

Despite the dramatic increase of Taiwanese production in China during 1990s, there were strong regulations of FDI before 2001. There were 316 manufacturing products prohibited from production in China. In addition, for those allowed to invest, there was a maximum “accumulated” investment limit of 50 million USD and a maximum annual investment limit of 2 million USD. As a result, the earlier stage Taiwanese FDI has concentrated in small and medium enterprises which are “low tech” manufacturers.

With China’s accession into WTO, Taiwanese government significantly deregulated FDI. Large electronics producers, including computer and semiconductor, were permitted to invest and produce their “core” products starting 2002. Furthermore, there was no restriction on the accumulated investment amount anymore.

Our study takes the sample of 406 large Taiwanese electronics producers and tracks their investment and production decisions in China from 1998 (before deregulation) to 2007 (after deregulation). Using unique administrative records from Taiwanese Ministry of Commerce, we were able to collect data of 933 affiliates of Taiwanese Electronics Producers in China.

We then ask the following questions. First, how do Taiwanese parent firm allocate its production activities among its Taiwanese production facilities and Chinese affiliates? Second, do Chinese manufacturing affiliates “inherit” production knowledge from its parent? Finally, how do Taiwanese producers choose potential production locations within China?

Our study will shed some light on each of these questions.