

The Non-linear Effect of Institutional Distance on the Location Selection of China's Outward Foreign Direct Investment

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Abstract. With panel data of 46 countries from 2003 to 2016, the author set up a static panel data model to investigate the relationship between the location selection of China's outward foreign direct investment and the institutional distances of different dimensions. The empirical results showed that there is a significant negative relationship between formal institutional distance, informal institutional distance and the location selection of China's outward foreign direct investment. In addition, the formal institutional distance cannot show its negative effect on location selection of China's outward foreign direct investment unless it was within a certain range, that is to say, there exists a non-linear effect of formal institutional distance on China's outward foreign direct investment. Meanwhile, in the case of formal institutional deficit, the negative effects played by the formal institutional distance on China's outward direct investment will be weakened.

1. Introduction

Since the 21st century, China has witnessed rapid development in outward foreign direct investment activities. In terms of investment amount, with the outward foreign direct investment flow reaching 145.67 billion dollars in 2015, China jumped to the second place in the world for the first time, with an 18.3% rise on year-on-year basis. In 2016, global economic growth was slow, which, however, did not affect China's outward foreign direct investment activities. China's outward foreign direct investment flow reached 196.15 billion dollars, accounting for 13.5% globally with a 34.7% increase on a year-on-year basis. From the perspective of location distribution, it was extremely uneven. In 2016, China's outward foreign direct investment emerged in 190 countries or regions around the world, with capital flow mainly to Asia, Latin America, North America and Europe, which accounted for 66.4%, 13.9%, 10.4% and 5.4% of China's total outward foreign direct investment respectively. China's outward foreign direct investment mainly flowed to Hong Kong, China in Asia, to tax havens such as the Cayman Islands and the British Virgin Islands in Latin America, to the United States, Canada and Bermuda in North America and to Germany in Europe.

The location selection of outward foreign direct investment has been a hot topic that has attracted special attention of experts in the field of foreign trade research and scholars have conducted various studies from different perspectives (Peng et al., 2008; Zong Fangyu et al., 2012; Chi Jianyu and Fang Ying, 2014; Wang Yongqin, etc., 2014). It has drawn much attention to study the investment activities of overseas multinational enterprises in emerging markets based on the institutional perspective. For a long time, scholars have held the belief that the good institutional quality in the host country not only reduces the risk of overseas investment, but attracts investment from multinational enterprises (Busse and Hefeker, 2005, Zhou Jian, 2010). However, the results of some studies on the location selection of China's outward foreign direct investment in recent years have shown that China's outward foreign direct investment has not flown to developed countries with higher institutional quality such as Europe and the United States (Cuervo-Cazurra and Genc, 2008; Kolstad and Wiig, 2012), but countries with lower institutional quality or similar to that in China in Latin America and Asia, indicating that the host country with high institutional quality does not necessarily attract China's outward foreign direct investment, but countries with institutional quality similar to that in China succeeds in attracting overseas investment from China's multinationals. The reason is that the larger differences in the institutional quality between the home

country and the host country, the higher costs and risks multinational enterprises take to adapt to the local environment. Similarly, the closer the institutional quality between the two countries, the faster multinational companies can adapt to the local environment and the lower the disadvantages will be. In this way, they manage to obtain legitimacy (Cuervo-Cazurra and Genc, 2008).

China is an emerging market country, whose motives of outward foreign direct investment are bound by its own specific institutional environment and factors affecting the location selection of OFDI are different from those in developed countries such as the United States and Japan. Compared with the institutional quality of the host country, institutional distance can better explain the location selection of outward foreign direct investment (Habib and Zurawicki, 2002; Du, 2009). Therefore, under the background of international trade liberalization and the Belt and Road, it is of great practical significance to analyze the effects of institutional differences between the two countries on the location choice of outward foreign direct investment of Chinese enterprises and provide scientific and effective decision-making and basis for enterprises in terms of foreign investment. As a result, does the institutional distance have the ability to affect the location selection of China's outward foreign direct investment? How does the institutional distance affect the foreign direct investment of China's enterprises? How serious is the effect? All of them are problems to be studied in depth in this paper.

2. Literature Review

In fact, institutional quality refers to a set of social norms that can be adopted to regulate behaviors of enterprises, and institutional distance refers to the degree of difference between the host country and the home country in institutional quality (Xu and Shenkar, 2002). In existing researches, scholars mainly choose to analyze the influence of institutional distance on the location selection of enterprises' outward foreign direct investment from the perspective of liability of foreignness. Therefore, in time of outward foreign direct investment enterprises not only seek the host countries with high institutional quality or large market size for investment, but also obtain their legitimacy by finding their comparative advantages. When making outward foreign direct investment, developing countries need take the lack of their own institutional environment into consideration. In this way, enterprises from these countries will obtain more comparative advantages from investing in countries with similar institutional quality than investing in developed countries (Cuervo-Cazurra and Genc, 2008; Dixit, 2009). Bénassy-Quéré and other expects (2007) confirmed through empirical studies the relationship between similarity in institutional quality between host countries and home countries and the location selection for outward foreign direct investment by use of panel data from 52 countries. The results showed that the more similarity in political and legal systems between two countries would attract outward foreign direct investment more easily. Deng Ming (2012) divided the institutional distance into economic institutional distance, legal institutional distance and cultural institutional distance, explored the influence of economic institutional distance, legal institutional distance and cultural institutional distance on the location selection of China's outward foreign direct investment by adopting the spatial panel data model and found that all these three types of Institutional distance had obvious hindrance effect and spatial demonstration effect on China's outward foreign direct investment. Namely, with greater hindrance effect of the economic institutional distance comes greater institutional distance, and China's enterprises will be unwilling to invest in regions with huge difference in domestic system due to a lack of the desire for transnational investment. Qi Chunling and Zou Chao (2013) pointed out that the greater difference the host country and the home country have in economic institutional distance and legal institutional distance, the more outward foreign direct investment flow it will be. However, with greater cultural distance comes less outward foreign direct investment flow. Liu Jing and Zhu Caihong (2012) divided the institutional distance into the regulatory institutional distance and normative institutional distance and analyzed the influence of the institutional distance of countries in the South and North on the location selection of enterprises' outward foreign investment, results of which showed that greater normative institutional distance between countries in the South and North often resulted into smaller outward foreign direct investment flow. However, in the outward

foreign direct investment activities of countries in the South and the North, there was obvious difference in the influence of the regulatory institutional distance on outward foreign direct investment. To be specific, the regulatory institutional distance can promote the transnational investment of enterprises when making foreign direct investment in southern countries but restrained the transnational investment of enterprises when making foreign direct investment in northern countries. Aleksynska and Havrylchyk (2013) argued that there was an obvious asymmetric relationship between institutional distance and OFDI flows.

It is not difficult to find that scholars have not reached a consensus on the relationship between institutional distance and the location selection for outward foreign direct investment of enterprises, the majority of whom only studied the relationship between them from the perspective of certain institutional dimensions, but failed to conduct classification studies on institutional distance from the aspect of institutional distance as a whole. At the same time, while few attempt to analyze the asymmetric, non-linear relationship of the influence of institutional distance on the location selection of outward foreign direct investment with the institutional distance itself as the starting point. Therefore, based on North's classification of institutions, the author in this paper divides institutional distance into formal institutional distance and informal institutional distance (Estrin and Baghdasaryan, 2009), gives directionality to formal institutional distance and brings in the concept of directional institutional distance, which is difference between the institutional distance of the home country and that of the host country. Studied the nonlinear relationship of institutional distance, directional institutional distance and location selection for China's outward foreign direct investment by use of the panel threshold model.

3. Theoretical Basis and Relevant Hypotheses

The neo- institutional economics school points out that the institutional factors refer to the social environment in which enterprises conduct various activities, which in turn will have direct or indirect effects on the various activities of enterprises. When conducting foreign investment, transnational enterprises should take into account not only their own resources and structure, but also the external institutional environment in order to achieve higher benefits from outward foreign direct investment with internal and external legalization at the same time. The greater the institutional distance between the host country and the home country system, the greater the difference between them in the institutional environment, in which case transnational enterprises need to spend more time and capital costs to solve various risks caused by mechanism and contract when conducting outward foreign direct investment. In the meantime, it takes more time for them to familiarize with the local market environment, build up interpersonal relationships and social networks and reduce the uncertainty risks brought by institutional differences.

Assuming that in an OFDI project, there is no institutional distance between the host country and the home country (ie, the two countries have basically similar political constraints, corruption, efficiency of legal system, social customs and interpersonal relationships). In order to facilitate the analysis, it is assumed that the project does not have a termination term, the net present value of the profits from outward foreign direct investment in the project should be:

$$NPV_{sh} = \sum_{t=1}^{\infty} \frac{V}{(1+\delta)^t} - TC = \frac{V}{\delta} - TC \quad (1)$$

Among them, V stands for the profit of the project in period t , with TC as the total economic costs of the project and δ as the discount rate. According to the investment decision theories, enterprises are willing to make outward foreign direct investment only when $NPV_{sh} \geq 0$. In other words, the criteria on which enterprises determine whether to make outward foreign direct investment is:

$$V > \delta TC, \text{ accept}; V \leq \delta TC, \text{ refuse} \quad (2)$$

Assuming that there is an institutional distance between the two countries in this outward foreign direct investment project, $C(\Delta dis)$ stands for the operating cost added to the project due to institutional distance in each period is and the term of termination for this project will be relatively short, with N duration. Therefore, formula (1) can be rewritten as:

$$NPV_{sh} = \sum_{t=1}^N \frac{V}{(1+\delta)^t} - TC - \sum_{t=1}^N \frac{C(\Delta dis)}{(1+\delta)^t} = \frac{V}{\delta} - TC - \frac{C(\Delta dis)}{\delta} \quad (3)$$

According to the investment decision theories, enterprises are willing to conduct outward foreign direct investment only when $NPV_{sh} \geq 0$. That is to say, with the presence of institutional distance, the criteria on which enterprises determine whether to make outward foreign direct investment is:

$$V > \delta(TC + \delta C(\Delta dis)), \text{accept}; V \leq \delta(TC + \delta C(\Delta dis)), \text{refuse} \quad (4)$$

According to formula (2) and (4), under the condition of institutional distance, the criteria for outward foreign direct investment of enterprises changes from $V > \delta TC$ to $V > \delta(TC + \delta C(\Delta dis))$. Since the risks in outward foreign direct investment projects may increase because of institutional distance, what come with greater difference in the institutional quality are greater risks and greater costs. That is, if $\frac{\partial C(\Delta dis)}{\partial \Delta dis} > 0$, function $C(\Delta dis)$ is an increasing function with function value above zero. That is to say, in the case of the existence of institutional distance, the criteria for determining outward foreign direct investment of enterprises have risen, namely, $\delta(TC + \delta C(\Delta dis)) > \delta TC$. At this point, enterprises hope to get outward foreign direct investment projects with higher expected profits.

The institutional distance includes formal institutional distance and informal institutional distance, of which the formal institutional distance refers to differences in expressly stated institutions such as political efficiency, laws and regulations and rules among countries or regions, while informal institutional distance refers to differences in cultural traditions, customs and cognition among countries or regions. Usually informal institutions have something to do with the cultural elements of a country, which can be replaced by the cultural distances between two countries. The cultural distance puts enterprises in liability of foreignness when conducting outward foreign investment, making it harder for them to establish interpersonal network and information network in the local area and causing greater resistance in communication and management between the parent enterprises and subsidiaries. Therefore, the liability of foreignness brought by the cultural distance has a great hindrance to the outward foreign investment of enterprises. On this basis, the following hypotheses are proposed:

Hypothesis H1: The formal institutional distance has a negative impact on China's outward foreign direct investment.

Hypothesis H2: The informal institutional distance has a negative impact on China's outward foreign direct investment.

The formal institutional distance is related to the political stability, efficiency of the legal system and other aspects between two countries. The formal institutional quality is clearly defined and therefore has a strong learning effect. As a result, transnational enterprises will try their best to reduce the non-legality brought by institutional distance in the face of formal institutional distance when making overseas investment. At the same time, there will be less experience for mutual learning and greater hindrance of formal institutional distance to the overseas investment of enterprises with the presence of greater formal institutional distance. Namely, the degree of negative impact of formal institutional distance on overseas investment by enterprises will also change along with changes in the absolute value of formal institutional distance and the influence of formal institutional distance on the overseas investment of enterprises is not stable. On this basis, the following hypotheses are proposed:

Hypothesis H3: There is a non-linear effect existing in the influence of formal institutional

distance on China's outward foreign direct investment.

Yan Chunling and Zou Chao (2013) proposed that the institutional environment of the host country can regulate the influence of institutional distance on enterprises' overseas investment. Host countries with high institutional quality, due to higher political stability and efficiency of legal system, are more conducive for foreign enterprises' access to fairness and legitimacy. On the contrary, it is harder for foreign enterprises to guarantee legitimacy in host countries with poor formal institutional quality, due to social corruption and turbulence. In other words, there is certain relationship between the influences of formal institutional distance on enterprises' outward foreign direct investment and the institutional quality of the home country. At the same time, the directional formal institutional distance is divided into formal institutional surplus (the formal institutional quality in the home country is higher than that in the host country) and formal system deficit (the formal institutional quality in the home country is lower than that in the host country). In the case of formal institutional surplus and formal institutional deficit, there is difference in the influence of formal institutional distance on enterprises' foreign direct investment. Based on the above analysis, the following hypotheses are proposed:

Hypothesis H4: There is a threshold effect on the influence of formal institutional distance on China's outward foreign direct investment.

Hypothesis H5: In the case of a formal institutional deficit, the inhibition effect of formal institutional distance on China's outward foreign direct investment is weakened.

4. Description of Model Construction, Variables and Data

4.1. Model Construction and Variables Description

The investment gravity models have been widely adopted to explain enterprises' outward foreign direct investment activities, but the institutional distance factor is not included in traditional investment gravity models. In order to study the relationship between institutional distance and enterprises' overseas investment activities, Li Ping (2014) added the institutional distance factor into the traditional investment gravity models. The static panel data model is set up as follows based on models proposed by Li Ping (2014) in order to verify hypothesis H1 and hypothesis H2:

$$ofdi_{it} = \alpha_0 + \alpha_1 \Delta disf_{it} + \alpha_2 disi_i + \sum \beta_i x_{it} + v_i + u_t + \varepsilon_{it} \quad (5)$$

$$ofdi_{it} = \alpha_0 + \alpha_1 disf_{it} + \alpha_2 disi_i + \sum \beta_i x_{it} + v_i + u_t + \varepsilon_{it} \quad (6)$$

Among them, with α_0 as intercept term, $ofdi_{it}$ refers to China's direct investment flow in the host country i in year t and $\Delta disf_{it}$ refers to the formal institutional distance with the host country i in year t . The absolute value should be taken due to the lack of directionality. $\Delta disi_i$ stands for the informal institutional distance between China and host country i , while informal institutional distance consists of cultural dimensions. There is no time dimension because cultural factors do not change in a short period of time. $disf_{it}$ refers to the difference in the formal institutional quality between China and the host country i in year t , which indeed comes with plus or minus signs and therefore is called directional formal institutional distance; x_{it} refers to control variables, v_i, u_t stands for individual effects and time effects and ε_{it} is random interference term.

When exploring whether there exists a nonlinear relationship between the formal institutional distance and China's outward foreign direct investment, ordinary panel data regression models have no longer been applicable. Therefore, the panel threshold model is adopted in order to test hypothesis H3, hypothesis H4 and hypothesis H5. The core of threshold regression of panel data lies in determining the threshold variables and taking absolute value of formal institutional distance as the threshold variables to test hypothesis H3, whose threshold regression model is:

$$ofdi_{it} = \alpha_0 + \alpha_1 \Delta dis_{it} \times I(\Delta dis_{it} \leq r) + \alpha_2 \Delta dis_{it} \times I(\Delta dis_{it} > r) + \alpha_3 \Delta dis_i + \sum \beta_1 x_{it} + v_i + u_i + \varepsilon_{it} \quad (7)$$

The directional formal institutional distance is taken as threshold variables to test hypothesis H4 and H5, whose threshold regression model is:

$$ofdi_{it} = \alpha_0 + \alpha_1 \Delta dis_{it} \times I(dis_{it} \leq r) + \alpha_2 \Delta dis_{it} \times I(dis_{it} > r) + \alpha_3 \Delta dis_i + \sum \beta_1 x_{it} + v_i + u_i + \varepsilon_{it} \quad (8)$$

Where, $I(\cdot)$ is the indicative function in threshold regression and the value is 1 when the expression in parentheses is true and the value is 0 when it is not. r stands for the threshold value of threshold regression.

4.2. Description of Variable Source and Measure

4.2.1. Explained Variables

Outward foreign direct investment flows (Δdis_{it}). This variable comes from the statistical bulletin of China's outward foreign direct investment over the years, with the unit of 10,000 US dollars. Logarithm is taken in this variable in order to eliminate the heteroscedasticity in the model.

4.2.2. Explanatory Variable

Institutional distance (Δdis_{it}) contains formal institutional distance (Δdis_{it}) and informal institutional distance (Δdis_i), of which the formal institutional distance is measured by the World Governance Indicators released by the World Bank, which contains six indicators, corruption control, government effectiveness, political stability, regulatory quality, legal system effectiveness and discourse power and responsibility. In this paper, the principal component analysis is adopted to obtain a score measuring the formal institutional quality of a country and the difference between the formal institutional quality in China minus that in the host country can be used to represent the directional formal institutional distance dis_{it} , where the formal institutional distance should be the absolute value of directional formal institutional distance.

Informal institutional distance Δdis_i can be expressed according to Hofstede's cultural distance, which contains six dimensions: power distance, uncertainty avoidance, individualism and collectivism, rigid temperament, long-term orientation and tolerance, whose formula is:

$$CD_i = \sum_{h=1}^6 \left[\frac{(I_{hi} - I_{hc})^2}{V_h} \right] / 6 \quad (9)$$

Where, CD_i stands for the cultural distance between China and the host country i , which indicates the informal institutional distance in this paper; I_{ih} is the index value of the host country i at dimension h related to the cultural distance while I_{hc} is the index value of China at dimension h related to cultural distance, with V_h as the variance of the dimension h . (The data mentioned above comes from the "cultural dimensions" on the website <https://www.geert-hofstede.com>.)

In fact, in addition to institutional distance, there are also factors that influence the location selection of China's outward foreign direct investment, including the macroeconomic development level of the host country, natural resources, trade openness between the two countries and geographical distance. These factors are taken as control variables. For example, the macroeconomic development level of the host country ($pgdp$) is expressed with the GDP per capita in the US dollar system in logarithm; the supply and demand capacity of enterprise's outward foreign direct investment ($sgdp$) is expressed with the sum of GDP in the host country and China in

logarithm, with unit of 10,000 US dollars; natural resources (*omf*) are expressed by the peroration taken by the fuel, ore and metal exports in the total exports of goods of the host country. The bilateral trade openness of the host country and the home country (*btrade*) is expressed with the total import and export volume between China and the host country in logarithm; the geographical distance (*cd*) is expressed with the distance between the capital of the China and the host country logarithm, with unit of kilometers. (The control variable data comes from National Bureau of Statistics of the People's Republic of China, World Economic Development Database in the EPS Data Platform and the website: <http://www.indo.com>.)

5. Empirical Study Results and Analysis

5.1. Static Panel Estimation Results and Analysis

In time of the panel data regression, the Hansman test should be first conducted to determine fixed effect or random effect for the model. The test results show that the fixed effect model is more effective. However, it is difficult to estimate variable coefficients that do not change with time by use of the fixed effect model, and the informal institutional distance and geographic distance do not change with time. Therefore, the Hausmann Taylor model is adopted to estimate variable coefficients, whose estimated regression results are shown in Table 1.

Table 1. Estimated Regression Results of Static Panel Models

	(5)	(6)
<i>Δdisf</i>	-0.2472 (0.0190)**	—
<i>disf</i>	—	-0.2476 (0.0110)**
<i>Δdisi</i>	-0.3339 (0.0397)**	-1.6359 (0.0009)***
<i>pgdp</i>	0.2341 (0.0020)***	0.1637 (0.0400)**
<i>sgdp</i>	0.9934 (0.0000)***	1.2928 (0.0000)***
<i>omf</i>	0.0080 (0.0250)**	0.0118 (0.0130)**
<i>btrade</i>	0.3178 (0.0510)*	0.0505 (0.8210)
<i>cd</i>	0.3626 (0.6880)	2.6104 (0.061)*
constant term	-15.0884 (0.0000)***	-24.5495 (0.0000)***

Note:***, **, *stands for the significant levels of 1%, 5%, and 10%, respectively and the numbers in parentheses are P value.

It can be seen from the regression results in Table 3 that whether the model is constructed by using expression (5) or (6), namely regardless of the absolute value or direction of formal institutional distance, the parameter estimates of the formal institutional distance significantly negative at the 5% significant level, which means that the formal institutional distance has a significant negative impact on China's outward foreign direct investment. Therefore, the results mentioned above support the hypothesis H1. The parameter estimates of informal institutional distance are significantly negative at the 5% significant level, which means that informal institutional distance has a significant negative impact on China's outward foreign direct investment. Therefore, the results mentioned above support the hypothesis H2.

What's more, the parameter estimates of GDP per capita of the host country are significantly positive at the 5% significant level in both models, indicating that China is more inclined to host countries with higher economic development level. The parameter estimates of the sum of GDP in

the host country and China are significantly positive at the 1% significant level, indicating that stronger supply and demand ability of outward foreign direct investment can better promote the foreign direct investment of enterprises. However, there is no significant relationship between geographic distance and bilateral trade openness and China's outward foreign direct investment in the model. The reason is probably that with the rapid development of global economy as well as complete transportation facilities, the inhibition effect of geographical distance on overseas investment by transnational enterprises has been weakened.

5.2. Panel Threshold Regression Results and Analysis

The panel threshold model is adopted in this paper to verify the nonlinear relationship between institutional distance and China's outward foreign direct investment. The STATASE panel threshold regression procedure is used to obtain the threshold regression results as shown in Table 2.

Table 2. Panel Threshold Regression Results

	(7)	(8)
<i>pgdp</i>	0.1760 (0.0317)**	0.1631 (0.0426)**
<i>sgdp</i>	1.0993 (0.0000)***	1.2795 (0.0000)***
<i>omf</i>	0.0111 (0.0520)*	0.0096 (0.0875)*
<i>btrade</i>	0.2894 (0.2309)	0.2115 (0.3732)
$\Delta dis_{it} \times I(\Delta dis_{it} \leq r)$	-0.1757 (0.1699)	0.1490 (0.3023)
$\Delta dis_{it} \times I(\Delta dis_{it} > r)$	-0.3689 (0.0015)***	-0.8099 (0.0000)***
Threshold Value	3.0895	-0.6987
Significance	6.5412 (0.0133)***	26.9346 (0.0000)***

Note:***, **, *stands for the significant levels of 1%, 5%, and 10%, respectively and the numbers in parentheses are P value.

According to regression results shown in Table 4, the threshold value passes the significance test at the 5% significant level and the threshold model in this paper is relatively reasonable. In the expression (7), the threshold variable is the formal institutional distance without directionality, whose threshold value is 3.0895. In time of $\Delta dis_{it} \leq 3.0895$, the parameter estimates of formal institutional distance are not significantly negative at the 10% significant level; in time of $\Delta dis_{it} > 3.0895$, the parameter estimates of formal institutional distance are significantly negative at the 1% significant level, which shows that the formal institutional distance will have a significant inhibition effect on China's outward foreign direct investment only when it exceeds 3.0895. In other words, there is a non-linear effect of formal institutional distance on China's outward foreign direct investment. What is mentioned above supports the hypothesis H3.

In the expression (8), the threshold variable is the directional formal institutional distance, with the threshold value as -0.6987. In time of $dis_{it} \leq -0.6987$, the parameter estimates of directional formal institutional distance are not significant at the 10% significant level; in time of $dis_{it} > -0.6987$, the parameter estimates for directional formal institutional distance are significantly negative at the 1% significant level, which shows that the directional formal institutional distance will have a significant inhibition effect on China's outward foreign direct investment only when it exceeds the threshold -0.6987, which is to say that there is a threshold effect in the directional formal institutional distance on China's outward foreign direct investment,

with threshold close to 0. What is mentioned above supports the hypothesis H4. At the same time, since the threshold is almost 0, the asymmetry in the influence of directional institutional distance on China's outward foreign direct investment can be analyzed from the perspective of formal institutional deficit and formal institutional surplus. When $disf_{it} \leq 0$, there is a formal institutional deficit existing between China and the host country, without significant influence of the directional formal institutional distance on China's outward foreign direct investment; in time of $disf_{it} > 0$, there is a formal institutional surplus between China and the host country, with significantly negative influence of directional formal system on China's outward foreign direct investment. That is to say, with the presence of formal institutional deficit, the inhibition effect of the formal institutional distance on China's outward foreign direct investment is weakened. what is mentioned above supports the hypothesis H5.

In addition, as shown in Table 4, there is a significant positive correlation among the GDP per capita, the supply and demand ability of outward foreign direct investment as well as the natural resources of the host country and China's outward foreign direct investment, indicating that the economic development level, the supply and demand ability of foreign direct investment and the abundance of natural resources of the host country can all contribute to China's outward foreign direct investment. However, there is no significant positive relationship between trade openness between the two countries and China's outward foreign direct investment, which may be related to the substitution effect between investment and trade.

6. Summary

With the launch of the Belt and Road initiative in 2013, Chinese enterprises have been increasingly active in overseas investment so it is increasingly important to figure out factors affecting the location selection for enterprises' outward foreign direct investment and of great practical significance to understand the influence of institutional distance on the location selection of China's outward foreign direct investment. In this paper, the static panel model and the panel threshold model are adopted to analyze the influence of institutional distance on China's outward foreign direct investment and the nonlinear effect. Finally, the following conclusions are drawn. (1) Chinese enterprises should select host countries with institutional quality close to that in China for outward foreign investments to avoid the risks brought by liability of foreignness in outward foreign direct investment activities. (2) The inhibition effect of institutional distance on China's outward foreign direct investment will be weakened when the institutional quality of the host country is greater than that of China. Therefore, when making foreign direct investment, Chinese enterprises should carefully analyze the direction of institutional distance and compare the institutional quality between China and the host country. (3) The economic costs for overseas operations of Chinese enterprises may rise due to cultural differences between China and the host country. Therefore, when conducting outward foreign direct investment, transnational enterprises should try to invest in projects with relevant experience so as to avoid various risks caused by unfamiliar cultural environment.

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