The impact of institutional distance on sustainable investment: evidence from China's Belt and Road Initiative

Heshan Sameera Kankanam Pathiranage and Huilin Xiao
School of Business Administration, Southwestern University of Finance and Economics, Chengdu, China, and
Weifeng Li
PBC School of Finance, Tsinghua University, Beijing, China

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Abstract

Purpose – In an attempt to satisfy the desire to become a global economic leader, China is working on a series of ambitious deals with several countries. As a major country in a region considered as an emerging market, the immense infrastructure gap that is curtailing trade and accessibility for economic growth has led to major changes in economic policy. The past few decades have seen China invest billions of dollars not only in the developing countries of Africa and Asia but also in other world economic giants of Europe and the USA. China has embarked on a rigorous global effort to close the infrastructure gap through the Belt and Road Initiative (BRI) in partnership with multilateral development banks. China's BRI brings together several countries in East Asia and the Eurasian mainland into close proximity with China, thereby promoting inland trade between the countries. The investments in this project are estimated to reach US$1tn over a span of ten years. However, the volume of outward foreign direct investments (OFDI) from China to the host countries is determined by several factors. Several previous researchers have studied various issues affecting the business activities of China and the given countries. First, the cultural organization, policy approaches and objectives of China as a country create trade barriers with countries involved in the BRI plan. This paper aims to provide a comparative overview of how the institutional distance of the Belt and Road countries from China affects their sustainable development.

Design/methodology/approach – Data on the nature, success and challenges of the BRI (such as the volume of bilateral trade and OFDIs and its financial implications) were extracted from various published studies. The impact of cultural distance and internationalization of the BRI enterprise was analyzed through a comparative research methodology.

Findings – A significant relationship exists between institutional distance and sustainable development of the Belt and Road countries. However, the barriers – for example, inhospitable culture and regulations for organizations in participating countries – could become pillars of success once resolved.

Originality/value – Previous studies lacked a standard framework to investigate how institutional distance is related to China's outbound trade with the Belt and Road countries. The comparative analysis methodology adopted in this study fills this gap.

Keywords Institutional distance, Sustainable investment, Belt and road countries, Comparative analysis, Outward FDI, Cultural distance

Paper type Research paper

1. Introduction

Chinese enterprises have picked pace in venturing into international markets despite China's late start in outbound investments. The 2018 Word Investment Report of the UN Conference

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on Trade and Investment (UNCTAD) ranked China as the second-highest exporter of capital, indicating that the outbound investments of China were higher than its inward foreign investments (UNCTAD, 2018). China's outbound investment channel not only reduces overcapacity in the home market but also benefits the host country economies (Seid, 2018). This channel provides a strong foundation for China and its partners to upgrade their industrial structure. However, despite the excitement over China's spreading economic roots, the inherent protectionism of global markets creates an obstacle for Chinese companies to grapple with. These firms are continually challenged by the institutional regulations of the host countries, some of which are too demanding, with the firms having to operate with narrow profit margins or sometimes no profit at all.

It is virtually impossible to examine the context of institutional distance and China's outbound investments before first analyzing the regional context within which these investments are concentrated (Tian, 2015). Unlike outbound investments of other countries (which mostly occur between developed countries), China directs its foreign investments not only to the developed but also to developing countries, as emphasized by Jiang and Jiang (2012). More than 60% of China's foreign investments target relatively poor countries (Deng, 2013). The diversified market targets imply that China continually encounters variations in institutional distance as compared to any other country engaged in outbound enterprise investments. Notably, a majority of the countries targeted by China's outbound investment happen to back the recently conceived Belt and Road Initiative (BRI). BRI comes at a prime stage when the global economy is undergoing gradual recovery from the frequent recessions of previous decades. However, the rate of economic development is not uniform, with some countries at the take-off stage, some driving to maturity and others such as the USA with one foot already into the age of mass consumption (Deng and Yang, 2015). China perceives BRI as a common point for cross-country cooperation toward uniform global economic growth. The initiative also provides Chinese enterprises with opportunities to open up to other countries through trade. This paper provides a comparative overview of how the institutional distance of the Belt and Road countries from China affects their sustainable development.

The rest of the paper is organized as follows. Section 2 provides an overview of the extant literature. Section 3 describes the methodology used in the study. Section 4 presents the results and Section 5 discusses the findings of the study. Section 6 summarizes our findings and concludes the paper.

2. Literature review and research

2.1 Literature review

Usually, business ventures involving multinational cooperation are aligned on an institutional basis in which host countries favor foreign countries that offer bilateral investments. In most cases, the venturing country seeks a country with institutional structures and an organizational culture similar to those of the home country, especially for immense outbound investments. However, cultural distance still exists even for countries with close formal institutional organization, but according to published research on international investments, state-owned enterprises invest in culturally different environments (Jiang and Jiang, 2012). For China, the investments serve both expansionist and imperialist purposes, while the host country accepts the Chinese organizational culture and cherishes the connection with a major world economy. Considering the benefits, the host countries adapt to organizational coordination through non-formal skills to reduce the barriers of trade between the two countries. Thus, despite the cultural distance, foreign enterprises operate without many barriers and make fast decisions to scale their investments and realize benefits. For example, European and African BRI countries and China have very different plans and the former's external environment is a critical contribution to the cultural distance both in terms of market and non-market aspects. For the BRI plan to succeed, the formal and informal sectors require incentives to realize a strategy to close the institutional organization gaps. For Asian partners in the BRI plan, the differences are minimal and China's investments in the region are higher and more successful than those in African and European counties. According to Peretiatko and D'Souza (2005), cultural differences can prevent firms from entering and succeeding in a host market. Thus, the implication of cultural dissimilarities is that different cultures have conflicting philosophies toward business. Therefore, the philosophical differences have to be addressed and a new management model suitable for the investment ventures of both the home and host countries needs to be created.

The launch of BRI has raised concerns over its potential to create unfair policies in the host nations, which would ultimately affect the institutional distance between the Belt and Road nations and China. Further, researchers have examined whether these impacts would in turn change China's investment scales, scopes, models and outcomes. Several studies have since been conducted to establish the extent to which the institutional dissimilarities between China and the BRI beneficiaries have affected China's decision-making paradigms and the results of large-scale outbound investments. A comparison by researchers has shown clear differences between investment flows from China to the European and African regions and to the Asian region. The comparisons have quantified cultural differences and the impacts of both the formal and informal institution differences on China's policy-making on large-scale outbound investments and the results of enterprise investments before and after the conception of the BRI. Table 1 presents the cultural distance scores of African countries versus China.

The extant research exhibits variability with respect to the type of institutional distance used to assess the impact of BRI on outbound investment. Some studies used formal institution differences (involving regulations by recognized entities and policymakers or the absence thereof) in the host countries while others relied on informal institution differences (involving sociocultural dissimilarities) (Ang *et al.*, 2015).

The studies reported as follows. First, formal institution dissimilarities define the scope of large-scale outbound investments by foreign enterprises, but do not significantly affect the scale of investments. In the same context, formal institution variances between China and the BRI countries have pushed enterprises to come up with full ownership structures for their businesses but do not significantly affect the investment models. Second, conversely, informal institution dissimilarities between China and the countries in the region significantly influence large-scale outbound investments (Buckley *et al.*, 2018). The influence of formal institutions includes expansion in the magnitude of enterprise investment, reduction in the room of enterprise investment and a push on the enterprises to come up with full ownership structures or merger and acquisition modes (Alon *et al.*, 2018). Third, collective institutional dissimilarities – entailing both formal and informal differences – have increased the probability that many enterprises would take on large-scale outward investments. Lastly, studies have found that the complementariness of China's BRI largely affect formal institution structures (Alon *et al.*, 2018). This indicates that the BRI's efforts to bridge the informal (cultural) distance between China and the Belt and Road countries remain inadequate.

Institutional distance is problematic for the outflow of foreign direct investment (FDI) recorded in China (Rani *et al.*, 2015). Researchers have identified China as the second-largest country for FDI inflow and outflow (Choi and Kim, 2003). Further, it is also an emerging

Table 1.
African countries and their cultural distance from China

African country	Power distance	Individualism vs Collectivism	Masculinity vs Feminity	Uncertainty avoidance	Cultural distance
Angola	0.2523	0.0516	14.9451	14.2451	7.3734
Benin	2.8035	0.3222	1.8081	9.8925	3.7067
Burkina Faso	2.8035	0.3222	1.8081	9.8925	3.7067
Burundi	2.8035	0.3222	0.2542	6.3312	2.4278
Cabo Verde	0.7009	0	18.3708	1.5828	5.1636
Cameroon	0	1.2890	0.2543	9.8925	2.8589
Central African Republic	2.8035	0.3222	1.8081	9.8925	3.7066
Chad	0	4.1765	1.3843	22.8555	7.1041
Congo, Dem. Rep. of the	2.8035	0.3222	1.8081	9.8925	3.7066
Congo, Republic of	2.8035	0.3222	1.8081	9.8925	3.7066
Cote d'Ivoire	2.8035	0.3222	1.8081	9.8925	3.7066
Djibouti	2.8035	0	0.0071	9.8925	3.1758
Egypt	2.8035	0.3222	3.1148	39.5698	11.4526
Equatorial Guinea	0	1.2890	0.2543	9.8925	2.8589
Ethiopia	2.8035	0	0.0071	9.8925	3.1758
Gabon	2.8035	0.3222	1.8081	9.8925	3.7066
Ghana	0	0.3222	4.7746	19.3892	6.1215
Guinea	2.8035	0.3222	3.1148	9.8925	4.0333
Guinea-Bissau	0.2523	0.0516	14.9452	14.2451	7.3736
Kenya	2.8035	0.3222	0.2543	6.3312	2.4278
Liberia	2.8035	0	4.7746	6.3312	3.4773
Libya	0	4.1765	1.3843	22.8555	7.1041
Madagascar	2.8035	0	0.0071	9.8925	3.1758
Malawi	2.8035	1.2890	4.7746	6.3312	3.7996
Mali	0	4.1765	1.3843	22.8555	7.1041
Mauritania	0	4.1765	1.3843	22.8555	7.1041
Mauritius	2.8035	0	0.0071	9.8925	3.1758
Morocco	2.8035	8.7139	1.1936	22.8555	8.8917
Mozambique	0.7009	0.3222	5.5373	3.1023	2.4157
Niger	0	4.1765	1.3843	22.8555	7.1041
Nigeria	0	1.2890	0.2543	9.8925	2.8589
Rwanda	2.8035	0.3222	0.2543	6.3312	2.4278
Senegal	2.8035	0.3222	3.1148	9.8925	4.0333
Sierra Leone	2.8035	0	4.7746	6.3312	3.4773

(continued)

African country	Power distance	Individualism vs Collectivism	Masculinity vs Feminity	Uncertainty avoidance	Cultural distance
Sudan	0	4.1765	1.3843	22.8555	7.1041
Tanzania	2.8035	0.3222	4.7746	6.3312	3.5579
Togo	2.8035	0.3222	1.8081	9.8925	3.7066
Uganda	2.8035	0.3222	0.2543	6.3312	2.4278
Zambia	11.2141	2.9003	4.7746	6.3312	6.305
Zimbabwe	11.2141	2.9003	4.7746	6.3312	6.305

Source: Gagne (2018)

Table 1.

market with a great institutional environment unlike other developing countries in Asia or Europe. It is also different from other emerging countries in regions with high FDI inflow and outflow (Fidrmuc and Korhonen, 2018), such as Hong Kong, The Netherlands, Japan, the USA and the UK. Empirical studies on institutional distance in the context of China's BRI have identified institutional patterns in China's outward foreign direct investment (OFDI) (Amighini *et al.*, 2013a). The analyzed differences reveal emerging patterns in the host countries. Social and political conditions in host countries are potential factors in FDI decisions (Fidrmuc and Korhonen, 2018). Policy issues related to corporate tax, openness, product market regulation, trade barriers concerning institutional distance and so on, have also been addressed (Liu and Yang, 2016). Other issues investigated include non-policy factors such as political stability and the economic ties between the BRI countries. Other research studies suggest that exchange of market regulations and businesses or even analysis of the trade investment culture are vital determinants of strong inward FDI flows. Liberalization and understanding political risks are the main factors that determine OFDI in China (Drogendijk and Blomkvist, 2013). Traditional studies show that the institutional distance of host countries influence Chinese OFDI.

Research findings indicate that institutional distance poses a challenge, as it limits Chinese bilateral trade with BRI countries. Therefore, China's bilateral trade with BRI countries is more sensitive to cultural distance than institutional distance changes. The impacts can be measured through a comparison of beta coefficients. The Asian BRI countries are first compared. The comparison results indicate that bilateral trade between the European countries and China are less sensitive to institutional distances. However, bilateral trade with each country differs because the institutional distance impact on the imports of China differs among its trading partners (Stahl and Voigt, 2008). The BRI has increased China's export sensitivity to institutional distance. Institutional distance has played a major role in increasing trade among the host countries in the BRI routes. Consequently, the BRI has drawn worldwide attention.

The current study adopts a quantitative approach to expand the BRI concept. Prior work largely relied on qualitative analyses to describe the effect of the BRI on countries that have so far benefitted from the initiative. Even quantitative studies failed to exclusively analyze how the BRI complements institutional differences at the enterprise level (Du and Boateng, 2015). Lastly, previous work used total amounts of outbound investments by Chinese enterprises, rendering an investigation into the structural properties of these outbound investments difficult (Cui and Jiang, 2009). Therefore, our study conducts a micro data analysis to shed light on the characteristics of Chinese enterprises' large-scale outward investments (Du and Boateng, 2015). Large-scale investments include those valued at US $100m or more. Large-scale investments are selected for the meta-analysis because they are subjected to stronger institutional regulation in host countries than small-scale investments (Buckley *et al.*, 2018). They are also more likely to drive significant economic changes among the BRI countries within a short time than small-scale outbound investments.

Research findings indicate that institutions are the rules of the game in any society. These institutions are identified as cognitive, regulative and normative structures in the society. Further, they also include activities that, when combined, help provide stability and meaning to social behavior (Buckley *et al.*, 2018, p. 3). Often, organizations are embedded in different institutional environments and later end up being influenced by the environment, hence confirming the rules as well as belief systems in the environment (Buckley *et al.*, 2018, p. 16). The influence creates conformity to rules and belief systems in the environment, making the organizations institutionally isomorphic. Institutional theory indicates that the institutional environment is a key determinant when dealing with firm structure and behavior (Buckley *et al.*, 2018, p. 12). Countries have different characteristics when handling the national and institutional environments, composed of various types of institutions such as value systems, policy, education system and regulations (Buckley *et al.*, 2018, p. 2). Institution theory, which underpins the facts of institutional distance, indicates that there exists variance in different countries as well as in the institutional environment. As countries and multinational corporations spread their operations in different countries, there is a need for an interface across the institutional environment. This is the reason institutional distance is selected for investigation in this research study.

2.2 Theoretical analysis and research hypotheses

Based on the literature presented by Buckley *et al.* (2018), Alon *et al.* (2018), Drogendijk and Blomkvist, (2013), Stahl and Voigt (2008) and Du and Boateng (2015), the study advances the following hypotheses.

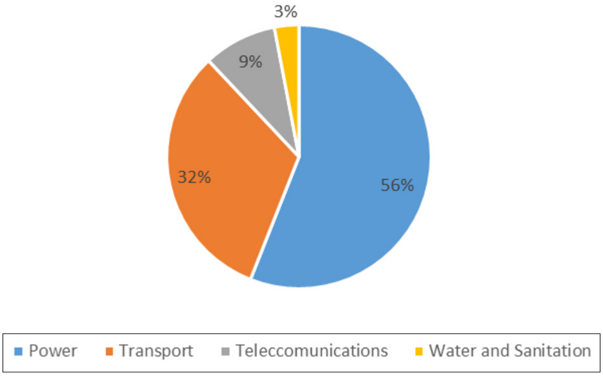
H1. Institutional distance affects the scope of trade significantly and constrains policy formulation and economic cooperation between countries but does not limit large-scale investments.

H2. The greater the formal and informal distance, the more the risk that a large-scale investment will fail.

H3. Institutional distance makes cross-border mergers more unlikely and forces firms to adopt a full ownership structure in the host countries to retain control of operations.

Research on China's outbound enterprise investments in the international markets narrows down to three key areas (Amighini *et al.*, 2013a; Liu *et al.*, 2017; Morck *et al.*, 2008). First, a group of researchers focused on the characteristics of Chinese enterprises as determinants of the country's outbound investment level. These researchers have demonstrated that enterprises and firms with superior competitive advantages are more productive and have a higher likelihood of making large-scale investments abroad. Larger companies are also more likely to maintain their overseas investments at a solid level despite shifts in international market dynamics (Amighini *et al.*, 2013a). Larger Chinese multinational firms are also adept risk takers and are cautious in their approach to foreign investments, especially in emerging and frontier Belt and Road markets. A second strand of literature focuses more on the outcome of Chinese outbound investments. Amighini *et al.* (2013a) noted that Chinese enterprises often generate reverse technology spillover in their immediate regions. The target areas witnessing the reverse spillover are technology, agriculture, energy and mineral resources. More to the point, Chinese firms see the BRI as a clear sign that the respective governments want them to look overseas and revolutionize the areas of their investments. Junrong and Yuan (2017) state that China accounts for 50%–60% of the total FDI in the Asian region, as shown in Figure 1. Table 2 presents the data of investments in BRI and non-BRI countries.

These financial aspects are important considering the global financial crisis of 2008. Regardless, China also provides 10%–15% of the direct investments in all the four regions it operates in at the BRI routes. Generally, China's OFDI flows and BRI investments have shown an upward trend. Data from 2003 through 2014 indicate that direct investment by China in the BRI regions has been rising gradually, as shown in Figure 2, in line with strengthening international economic cooperation (Steenkamp, 2001). Furthermore, research findings indicate that bilateral economic cooperation has continued to improve gradually. Consequently, direct investments in the BRI regions, especially by China, suggest that countries in these regions enjoy industry and consumer market advantages. Large-scale



Power	56%
Transport	32%
Telecommunications	9%
Water and Sanitation	3%

Figure 1.
Infrastructure investment needs in Asia by sector, 2017

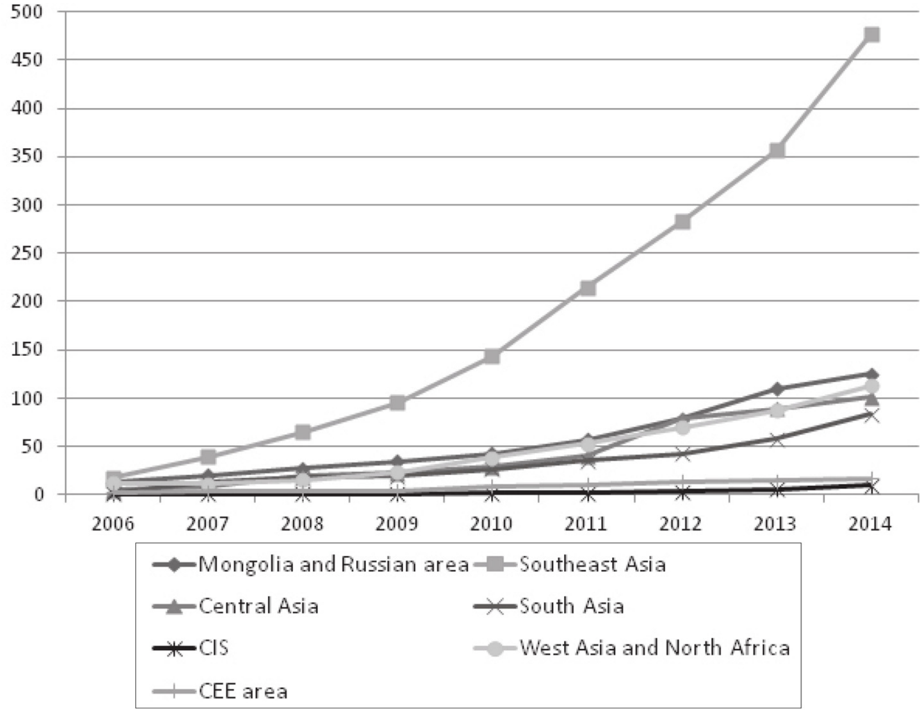
Table 2.
Descriptive statistics: Tabular data on economic investments in BRI and non-BRI regions

DP (US$tn)	Maximum		Minimum		Average	
BRI	9.61	CHN	0.003	MDV	0.68	
EU	3.75	DEU	0.01	MLT	0.65	
Other countries	16.69	USA	0.00	SYC	0.81	
Trade values (US$)						
BRI	0.37	CHN	–	–	–	
EU	0.14	NLD	–	–	–	
Other countries	0.30	USA	–	–	–	
Tariff (US$)						
BRI	579.74	EGY	4.97	–	–	
EU	18.44	AUT	3.28	–	–	
Other countries	1,358.42	ISL	6.16	–	–	

Notes: BRI: Belt and Road Initiative; EU: European Union; CHN: China; DEU: Deutsche Eislauf Union; USA: United States of America

mutual direct investments will increase these advantages. In brief, 11 countries in Southeast Asia are among the leading investors in China (Sartor and Beamish, 2014). These are followed by 19 countries in West Asia and Eastern Europe, which together account for the second largest amount of investments in China. The other regions have relatively low investment in China.

Third, the literature extensively focuses on the factors influencing Chinese firms' performance following their outbound investments. The factors highlighted in this context mainly concern the institutional environment in the countries in which they operate and how the institutional differences between them and the home markets affect the investments.



Source: Statistical Bulletin (2015)

Figure 2. China's outward FDI stock in the OBOR initiative area (US $100m)

Among them, the influence of institutional differences on location choice and the performance index of the foreign investments have received the greatest attention from authors. Some of these authors have attributed the recent growth of Chinese overseas investments to the boost given by the government's BRI policy programs. BRI has turned out to be a bid by the Chinese Government to widen its influence on the institutions of the countries benefiting from the initiative because it enables China to fund and take on major infrastructure projects in the developing countries. China has embarked on a rigorous global effort to close the infrastructure gap through the BRI in partnership with multilateral development banks (Table 3 for the global infrastructure investment needs).

Demir (2016) and Szulanski (1996) revealed that enterprises usually attempt to avoid risks by choosing to invest in nations whose institutional environments are similar to those of their home countries. The closer the institutional gap between any two countries, the higher is the scale of outbound enterprise investments (Demir, 2016; Steenkamp, 2001). However, current evidence indicates that this theory applies mainly to international investments among developed nations, but not to China's outbound investments. Chinese enterprises making outbound investments are state-owned and the ownership advantage sustains their investments even in countries with a wider institutional gap from China's institutions. Furthermore, when trading with nations with similar formal institutions, Chinese enterprises tend to swap the formality of the institutions with "connections," which would enable them to reap considerable benefits from the home country's "market skills"

Table 3.
Comparison of estimates of global infrastructure investment needs

Source	Sectoral scope	Actual/expected annual investment (US$tn)[1]	Investment need (US$tn)		
			Time frame	Total	Per annum
Bhattacharya *et al.* (2016)	Including power generation, transmission and distribution, primary energy supply, energy demand and efficiency, transport, water and sanitation and telecommunication	3.4 (2015)	2015–2030	75–86	5–6
NCE (2014)		–	2015–2030	96	6.4
OECD (2017a)		3.4–4.4 (2017)	2016–2030	95	6.3 (or 6.9 under a 2°C scenario)
GI Hub (2017)	Including roads, railways, airports, electricity generation, transmission and distribution, water and telecommunication	2.3 (2015) growing to 3.8 (2040)	2015–2040	94	2.9 (2015)–4.6 (2040)
McKinsey (2016)	Including transport (roads, railways, airports and ports), water, power and telecommunication	2.5	2016–2030	49	3.3

Notes: The approaches to estimating actual and expected investment trends vary widely among studies. See also OECD (2017b). NCE: New Climate Economy; and OECD: Organization for Economic Co-operation and Development without having to contend with institutional adaptation and other forms of organizational protocols, as has been the case with several African trade partners. Further, multinational Chinese companies investing in countries with similar formal institutions are at ease with these foreign environments and any additional market or non-market investment derivatives.

López-Duarte and Vidal-Suárez (2013) also examined the role of informal institution difference in enterprises' outbound investments. Specifically, the authors noted that cultural similarities between the host and the home country promote outbound enterprise investments while cultural dissimilarities hinder expansion to a particular country. Peretiakto and D'Souza (2005) illustrated this trend with the case of Australia. Australia is the only country in the Asia-Pacific with significant cultural similarities to the USA. For this reason, there have been more outbound enterprise investments between the two countries than any other country in Southeast Asia. Further investigations indicate that different cultures inspire different business philosophies and practices (Cozza *et al.*, 2015; Meyer *et al.*, 2018). Thus, multinational enterprises with different home cultures will often encounter a slow response from host clients, especially because their original management models and business strategies clash with the purchase behavior informed by the cultural background of the host countries (Choi and Kim, 2003; Jiang and Jiang, 2012). The social culture of the host institutions may even reduce the effectiveness of similar formal institutions between a host and a home country, thereby hiding more resistance to outbound investments (Beugelsdijk *et al.*, 2018; Cui and Jiang, 2009; Smith, 2006). To overcome the cultural difference challenge, foreign enterprises make large-scale investments that will stand out and strengthen the culture of the home country, thereby reducing the cultural conflict with the home country.

According to the literature studied, institutional differences between nations increase the risk of failure of outbound enterprise investments. The current market place is highly competitive and companies entering into foreign territories may not always receive the best welcome (Rani *et al.*, 2015; Stahl and Voigt, 2008). Enterprises could be barred from continuing their investments in a foreign country because of conflicting interests, which may ultimately cause diplomatic tensions. Considering that expropriation and nationalization of outbound enterprise investments are rare in the modern global environment, the host country may transfer the weight of its political interests, driven by institutional differences, onto the foreign enterprise by implementing discriminatory policies and other measures that would raise the likelihood of outbound investment failure (Jiang and Jiang, 2014; Zhang and Jiang, 2012). Multinational companies would suffer the impact of cultural differences when they face public criticism in the wake of protection, increasing their operational risks.

3. Methodology

3.1 Comparative analysis

In an attempt to arrive at a conclusive interpretation of the impact of institutional distance in the context of China and the host countries on the relative scale of outbound investments, a comparative analysis to model the extent BRI is outlined.

The study compares the volume of China's BRI investments in the host countries across Africa and Europe versus the countries in the Asian region.

China's investments in the host countries are analyzed from two perspectives, institutional ownership (whether the firm is fully or partially owned) and mode of operation (whether market entry is through a merger and acquisition or a greenfield investment).

3.2 Variables

To conduct the comparative analysis, a comprehensive research was developed for several databases and search engines, such as Google Scholar. The comprehensive search identified literature that focused on the growth of investments in the BRI plan. These identified articles formed the basis for conducting the comparative analysis. Based on the identified literature, the analysis first compared the outward flow of investment in host countries by China under the BRI plan. First, the comparative analysis was conducted by reviewing the impact of cultural distance between host countries and the resulting flow of investments in the BRI plan. The analysis then focused on the influence of institutional distance between China and the host countries. Lastly, the analysis explored the impact of BRI on institutional differences between the Chinese and the nations along the Belt and Road with respect to cultural.

3.2.1 Dependent variables.

The variables are of two types: scale of investment and investment modes.

3.2.1.1 Investment margin. Following Liu and Yang (2016), this study delves into the large-scale outbound investment margins, described as the quantitative outflow of investments specific to a BRI country, measured as volume per year.

3.2.1.2 Mode of entry. Chinese state-owned enterprises' mode of entry into host country markets, especially in infrastructure projects, is influenced by the organizational structure of the firms. In an attempt to internationalize the enterprises, investments are based on fully owned structures because of the cultural distance. Fully state-owned enterprises venture into host countries with greenfield investments under the BRI plan.

3.2.2 Independent variables.

Cultural distances influence the organization of institutions, both formal and informal.

3.2.2.1 Cultural differences between formal institutions. Kolstad and Wiig (2012) and Zhang and Jiang (2012) investigated the institutional differences between various countries based on governance indicators. The results reveal the degree of difference between these countries and China. Comparing the mean of the indicators for each country with that of China indicates whether the country's economic and institutional organization is suitable for China. Similarly, comparing the average of the institutional governance indicators between China and the host country provides an insight into the impact of institutional distance on outbound investments under the BRI plan. If a country has a better governance index compared to that of China, investments by Chinese state-owned enterprises are positively affected; if not, they are negatively affected.

3.2.2.2 Cultural differences between informal institutions. The culture of a country is a key aspect in the organization of its informal institutions. Thus, cultural difference plays a critical role in shaping the investment and trade partnership between countries participating in the BRI plan. Cultural difference is measured as a dimension of power distance, the individualism or collectivism ideology, masculinity and femininity perspectives and risk avoidance. Cultural differences between countries manifest in terms of cultural and diplomatic relations on both a historic scale and an ongoing cultural exchange through trade and diplomacy (Hofstede, 2005).

3.3 Data sample and analysis

The existing literature has focused primarily on location selection and performance levels of outbound enterprise investment. Even attempts to analyze outbound enterprise investment decisions are not satisfactory as they miss out on key elements of investments, including scale, scope, model and ownership structure (Kolstad and Wiig, 2012; Zhang and Jiang, 2012). These studies lack a standard framework governing discussion on the scale and scope of investment, the mode of investments and the ownership structure and how these aspects are affected by institutional distance. Following this analysis, this paper attempts to construct a comparative review of institutional distance and all aspects of outbound enterprise investments, particularly focusing on China and the nations traversed by the BRI (Zhang and Daly, 2011). The comparative analysis can be considered a comprehensive framework to examine how institutional distance affects all aspects of outbound investments decisions and performance. It seeks to answer the following questions: To what extent do the differences in formal and informal institutions affect the scope and scale of large-scale outbound enterprise? How is the formal or informal institution distance related to the performance and failure of large-scale outbound investment?

This study used two search methods to identify the research published between January 2000 and January 2018. First, we conducted an electronic search on databases such as Business Source Premier, Business Source Complete, Academic Search Premier, ABI Inform Global and the Economic Intelligence Unit for empirical articles. We used keywords such as "prevalence," "impact" and "incidence" along with one or more of the following terms: "institutional distance," "outbound enterprise/China/BRI/country" and "factors." We also included articles containing terms such as "economic growth" and/or "decline," "international trade" and "Belt and Road countries" to investigate the relationship between institutional distance and trade with China. Second, we checked the references of the collected articles, dissertations and book chapters for studies related to our topic. We also skimmed through other literature reviews and comparative analyses on international trade involving China. We further retrieved and scrutinized the abstracts of these studies to ascertain their fit for our comparative analysis.

The retrieved articles were included, if at least one of the following was discussed with sufficient data and sample sizes:

- institutional distance and trade with China prior to the conception of the BRI;
- institutional distance and trade with China in the BRI era;
- China's trade with countries along the Belt and Road; and
- China's outbound enterprise investments.

For studies with the same or overlapping samples, the article with maximum findings was selected for the comparative analysis. This would assure the independence of the articles concerning participant inclusion.

3.3.1 Data analysis. We analyzed data from published studies mentioned in the literature review that focused on the growth and inflow of investments under the BRI plan. A qualitative approach was adopted to analyze the findings presented in previous literature. This approach involves an interplay between theory and analysis. As such, qualitative data was analyzed to discover patterns of the influence of BRI on the host country over a given time frame. The data analysis also sought to establish casual links between the variables that were being measured.

3.3.2 Comparative research methodology. Comparative analysis is a methodology to arrive at a conclusion about data through comparison of various groups. The research identifies and analyzes similarities as well as differences between the groups. Thus, the comparative analysis deployed for this study allowed comparison of outward investment flows from China to host countries under the BRI plan. It sheds light on the impact of cultural distance on collaboration between the BRI countries. The study focuses on a quantitative evaluation of the impact of cultural distance between China and the host countries and the resulting flow of investments under the BRI plan. The study also analyzed the influence of institutional distance between China and the host countries.

The hypotheses were then tested to ascertain whether the BRI had affected the institutional differences between China and the Belt and Road nations with respect to cultural distance.

This analysis examines the influence of BRI on the host country in a specific time frame. Both intensive and extensive investment margins were factored into the analysis of outbound investments. Intensive margins referenced the average outbound investments in one year whereas the extensive margins depicted the ideal quantity of these investments in the same year.

4. Results

The study investigated the investment mode from two perspectives, ownership structure and entry mode. The differences in formal institutions were examined according to the guidelines provided by Wang *et al.* (2012) and Kolstad and Wiig (2012). The differences evaluated in this study are based on the World Bank's Worldwide Governance Indicators (Drogendijk and Blomkvist, 2013). These indicators were calculated from difference scores comparing China and the Belt and Road countries. A positive difference between the two shows that the formal institutions in the host country are better organized than the Chinese market institutions, whereas a negative difference indicates poor formalism in the host countries compared to China. The difference in informal institutions, denoted by, underscores the impact of cultural differences on Chinese enterprises' investment indices for the neighboring Belt and Road countries. The indicators of informal differences include power distance, avoidance of uncertainty, collectivism or individualism and gender preferences. Informal and formal differences between China and the countries which host its outward FDIs.

The difference in cultural values is an indicator of the variations in diplomatic relations. Thus, countries with longstanding diplomatic relations are likely to have a narrow informal institution gap. On the other hand, the natural resource endowment of the host country was determined by the quantity of ores and metals as a proportion of the total exports and trade agreements signed by China and the host countries or the absence thereof. The study used secondary data on the regions and countries along the China Belt and Road.

5. Discussion

The comparative analysis fills the gap in previous studies caused by the absence of a standard framework to investigate how institutional distance is related to outbound trade for the Belt and Road countries. An analysis of micro-data of 2,400 large-scale outward investments from 600 Chinese enterprises has demonstrated that institutional distance undeniably affects investment decisions and outcomes. Also, the functional setting of the BRI, from the viewpoint of the differences in formal and informal institutions, has a role in defining the scope, scale and outcome of outbound investments.

Table 1 indicates that similar institutional characteristics are likely to attract large outbound investments from multinational enterprises (Ramamurti and Hillemann, 2018; Rani *et al.*, 2015). The more the institutional similarities between China and the Belt and Road countries, the fewer would be the policy conflicts and the higher the chances of enterprise adaptation and coordination. An upsurge in Chinese companies' investments in the host countries would be the end result of this relationship (Ramasamy *et al.*, 2012). The results further reveal that differences in informal institutions negatively affect the extensive margin more than the intensive margin (Sartor and Beamish, 2014). It is therefore more difficult for multinational companies to bridge the psychological gaps between countries than to embrace the formal regulations, such as the laws and policies in the host nations (Table 4).

The analysis has concluded that both formal and informal institution differences have diverse effects on enterprises' large-scale outward investments (Seid, 2018; Shirodkar and Konara, 2017). Primarily, the differences in these two types of institutions define investment decisions in two ways. Differences in formal institutions limit the scope of large-scale outbound investment more significantly than those in informal institutions (Sutherland and Anderson, 2015). However, the impact of formal institution differences does not significantly determine the scale of outbound investments (Du and Boateng, 2015). In the face of formal institution gaps, most companies involved in outbound investments mainly consider full ownership structures. Conversely, differences in informal institutions mainly affect the scale of investments, where enterprises are likely to expand their investments to mitigate the potential derailing effects of rigid informal institution differences (van Hoorn and Maseland, 2016; Wang *et al.*, 2012). Importantly, both formal and informal institution differences increase the risk of failure for outbound investments in foreign markets. The comparative analysis findings further reveal that the complementariness of the BRI is mostly felt at the level of formal institutions (Wei *et al.*, 2014). This indicates that the BRI potentially limits the scope of outbound foreign investments from Chinese markets but may not have the same impact on the scale of outbound investments. Therefore, the BRI is yet to bridge the culture gap between China and the Belt and Road countries, indicating that it still has a limited role in expanding the scale of investments in these countries.

On a different note, the analysis revealed considerable heterogeneity among the institutions and industries that underlie the abovementioned inferences. First, formal institution differences positively affect the scale of outbound investment in service industries more than they do in manufacturing industries (Zhao-Lin, 2011). Notably, however, the negative implication of the informal institution differences on the diversification of outbound investments from China is one-sided. These implications only apply to countries with formal institutions inferior to those of China. Therefore, Chinese enterprises' outbound investments targeted at countries with weaker institutional structures are less likely to be drawn back by informal institution differences. This is the case with China and most of the Belt and Road countries, including Myanmar.

Regarding the estimates for different industries and institutions, the comparative analysis findings show that the institutional difference between China and the other countries involved have significantly hindered the rise of outbound investments in the manufacturing sector. Informal institution differences significantly reduce the probability that an enterprise would make greenfield investments to enter into a host country's manufacturing industry. The institutional complementariness of the BRI to the institutional gap is more conspicuous in service industries than in the manufacturing sector.

The analysis further shows that institutional differences have both positive and negative research implications. Outbound investment did not scale up even when institutional differences increased in host countries with superior formal institutions. This led to a new revelation that formal institution differences do not universally hinder the diversification of outbound investments. Therefore, relatively strong institutional environments have a positive effect in moderating the impact of formal institution differences on outward investments. In contrast, strong institutional environments do not successfully moderate the impact of informal institution differences on outbound investments. Informal institution differences still have a considerable effect on the diversification of outbound investments.

Table 4.
African countries and their cultural distance from China

African country	Power distance	Individualism vs Collectivism	Masculinity vs Feminity	Uncertainty avoidance	Cultural distance
Angola	0.2523	0.0516	14.9451	14.2451	7.3734
Benin	2.8035	0.3222	1.8081	9.8925	3.7067
Burkina Faso	2.8035	0.3222	1.8081	9.8925	3.7067
Burundi	2.8035	0.3222	0.2542	6.3312	2.4278
Cabo Verde	0.7009	0	18.3708	1.5828	5.1636
Cameroon	0	1.2890	0.2543	9.8925	2.8589
Central African Republic	2.8035	0.3222	1.8081	9.8925	3.7066
Chad	0	4.1765	1.3843	22.8555	7.1041
Congo, Dem. Rep. of the	2.8035	0.3222	1.8081	9.8925	3.7066
Congo, Republic of	2.8035	0.3222	1.8081	9.8925	3.7066
Cote d'Ivoire	2.8035	0.3222	1.8081	9.8925	3.7066
Djibouti	2.8035	0	0.0071	9.8925	3.1758
Egypt	2.8035	0.3222	3.1148	39.5698	11.4526
Equatorial Guinea	0	1.2890	0.2543	9.8925	2.8589
Ethiopia	2.8035	0	0.0071	9.8925	3.1758
Gabon	2.8035	0.3222	1.8081	9.8925	3.7066
Ghana	0	0.3222	4.7746	19.3892	6.1215
Guinea	2.8035	0.3222	3.1148	9.8925	4.0333
Guinea-Bissau	0.2523	0.0516	14.9452	14.2451	7.3736
Kenya	2.8035	0.3222	0.2543	6.3312	2.4278
Liberia	2.8035	0	4.7746	6.3312	3.4773
Libya	0	4.1765	1.3843	22.8555	7.1041
Madagascar	2.8035	0	0.0071	9.8925	3.1758
Malawi	2.8035	1.2890	4.7746	6.3312	3.7996
Mali	0	4.1765	1.3843	22.8555	7.1041
Mauritania	0	4.1765	1.3843	22.8555	7.1041
Mauritius	2.8035	0	0.0071	9.8925	3.1758
Morocco	2.8035	8.7139	1.1936	22.8555	8.8917
Mozambique	0.7009	0.3222	5.5373	3.1023	2.4157
Niger	0	4.1765	1.3843	22.8555	7.1041
Nigeria	0	1.2890	0.2543	9.8925	2.8589
Rwanda	2.8035	0.3222	0.2543	6.3312	2.4278
Senegal	2.8035	0.3222	3.1148	9.8925	4.0333
Sierra Leone	2.8035	0	4.7746	6.3312	3.4773

(continued)

African country	Power distance	Individualism vs Collectivism	Masculinity vs Feminity	Uncertainty avoidance	Cultural distance
Sudan	0	4.1765	1.3843	22.8555	7.1041
Tanzania	2.8035	0.3222	4.7746	6.3312	3.5579
Togo	2.8035	0.3222	1.8081	9.8925	3.7066
Uganda	2.8035	0.3222	0.2543	6.3312	2.4278
Zambia	11.2141	2.9003	4.7746	6.3312	6.305
Zimbabwe	11.2141	2.9003	4.7746	6.3312	6.305

Table 4.

6. Conclusions and implications

In the context of the impact of cultural distance on BRI, countries are wary of the domination by a foreign power, especially China. In particular, countries fear foreign control and see it as a threat to their sovereignty. However, trade dominance by a foreign country is not a serious threat to the sovereignty of a modern republic and the BRI initiative has progressed despite cultural differences, though its implementation has been quite slow paced. In an attempt to bridge the cultural distance, China has revived the Silk Road and with it the ability to create a vision for the future – of mega trade projects in a long-term, strategic positioning in the global economy. In the interaction with countries with diverse cultural values, trade agreements and cooperation are different and such endeavors succeed only if the relationships can be sustained. As a result, the BRI has been formulated in such a manner that it marries the cultural values of both host countries and China to achieve a grand vision and strategy although it has had minimal success at best. China has made progress with ongoing efforts to limit the cultural difference between its partners in the BRI plan, which implies that cultural dimension in the relationship will continue to influence the partnership, but will reduce over time. Cultural distance is a major factor in the success of trade and its long-term outcome in the global economy. The initiative will strengthen with the facilitation of an organized cooperative framework among countries. The BRI by China has managed to promote sustainable development, especially in the economic aspect. It also promotes sustainable development of the environment, mechanisms and infrastructure. In this process, all the BRI countries have indicated an overall improvement in sustainability. The crux of the matter is that in the short period since its launch, the BRI has caused a positive effect on sustainability and development.

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Corresponding author
Heshan Sameera Kankanam Pathiranage can be contacted at: heshan.sameera@gmail.com