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Transnational Corporations
Volume 20, Number 3, December 2011

Contents

ARTICLES

- | | | |
|--|---|----|
| Kazuo Kadokawa | Determinants of foreign direct investment:
Evidence from a questionnaire survey in
the Japanese manufacturing sector | 1 |
| Frederico Rocha and
Ana Urraca Ruiz | The role of the network coordinator in the
attraction of foreign investments in R&D:
The case of the Brazilian oil and gas industry | 33 |

PAPER SERIES

Commemorative papers on the work of John H. Dunning

- | | | |
|---|--|----|
| Sarianna M. Lundan,
Hafiz Mirza and
James Zhan | | 61 |
| Sarianna M. Lundan | An institutional perspective on the social
responsibility of TNCs | 69 |
| Seev Hirsch | Making globalization moral? | 87 |

Determinants of foreign direct investment: evidence from a questionnaire survey in the Japanese manufacturing sector

Kazuo Kadokawa*

This paper explores the results of a questionnaire survey investigating the determinants of foreign direct investment (FDI) by Japanese manufacturing firms from 1994 to 2009. Specifically, the questionnaire asked the respondent firms their reasons for considering foreign rather than home country locations, as well as major obstacles to undertaking FDI. Although labour availability and proximity to markets, supplier firms and raw materials are key determinants, this study reveals that there are significant variations among manufacturing industries. The analysis also reveals differences among industries with regard to obstacles to undertaking FDI and reasons for preferring a home country location.

1. Introduction

This study examines the reasons for which Japanese manufacturers consider offshore production and also explores the advantages of the home country that discourage foreign direct investment (FDI). It also highlights cross-industry variations in the determinants of FDI in the Japanese manufacturing sector. Compared with other large, developed economies, Japanese outward FDI relative to its economic size is exceptionally small (OECD, 1998). Although recent Japanese manufacturing has been increasingly globalized, only 5.3 per cent of the owners of new plants, surveyed from 1994 to 2009, responded that they had considered offshore production. The cause of this idiosyncrasy of the Japanese manufacturing sector has not been sufficiently studied.¹ This study, therefore, investigates the mystery of Japanese firms' exceptional level of preference for the home country.²

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¹ The present study follows the line of empirical studies based on the home country of investing firms (e.g. Schroath et al., 1997; Zhao and Zhu, 2000; He, 2003).

² This survey study offers more policy-relevant evidence on the actual location decisions than do econometric studies. The "policy-turn" of research has recently been advocated by several economic geographers (Lambooy and Boschma, 2001; Markusen, 2001, 2003; Martin, 2001; Massey, 2001), a resurgence of interest stimulated by the controversial findings of the World Development Report 2009: Reshaping Economic Geography.

This study explores the questionnaire survey data collected by an affiliated organization of the Ministry of Economy, Trade and Industry (METI). The subject of the survey were newly built or relocated manufacturing plants in Japan from 1994 to 2009.³ This questionnaire first asked why firms considered foreign rather than domestic locations.⁴ Second, it asked why firms remained in the home country.

The questionnaire survey also assessed the impact of policy incentives. Recent empirical studies on FDI are increasingly oriented towards the impact of policies to promote FDI inflows.⁵ For instance, many studies note that intra-firm exchange rate management is one of the most important reasons for FDI decisions. Froot and Stein (1991) observed increasing inward FDI during the period of exchange rate depreciation in United States. Klein and Rosengren (1994) confirmed that currency depreciation accelerated FDI inflows through an analysis of various United States data, categorized by the country and type of FDI. The studies of Grubert and Mutti (1991), Swenson (1994) and Kogut and Chang (1996) highlighted M&A cases. Lipesey (2001) and Desai, Goley and Forbes (2004) focused on the period of currency crises in Latin America. Blonigen (1997) demonstrated that real US dollar depreciation against the Japanese yen encouraged Japanese FDI to the United States; Blonigen and Feenstra (1997) indicated that the threat of United States market protection and trade barriers stimulated Japanese FDI to the United States.

Several studies have suggested that the foreign tax rate is an alternative explanation for changes in FDI flows. Hartman (1984, 1985) originally investigated the impact of tax controls on FDI. Slemrod (1990) focused upon double taxation issues. Scholes and Wolfson (1990),

³ The questionnaire survey has been a popular tool in location study (Hoover, 1948;

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