Going Global in the Digital Era: How Digital Finance Affects Chinese OFDI

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ABSTRACT

This study investigates the effect of digital finance on Chinese OFDI using Probit and Logit models on A-share-listed Chinese enterprises and representative OFDI data from 2011 to 2020. It shows that digital finance has a heterogeneous impact on Chinese OFDI both in probability and scale depending on the enterprise digitalization level. That is, digital finance has a positive (negative) effect on the OFDI of high (low) digital enterprises. Mechanism analysis reveals that the digital divide, which causes credit resources to be squeezed and increased financing constraints for these enterprises, is the main cause of the negative impact of digital finance on the OFDI of low-digital enterprises while the negative impact of digital finance on the OFDI of low-digital enterprises while the negative impact of digital finance on the OFDI of low-digital enterprises is limited to greenfield investments and highly competitive industries. The findings highlight the importance of encouraging enterprise digital transformation when developing digital finance policies to effectively leverage the potential of digital finance to drive Chinese firms' OFDI.

KEYWORDS

Chinese OFDI, Digital Divide, Digital Finance, Digital Inequality

1. INTRODUCTION

Outward FDI (OFDI) is an effective way for developing countries to engage in global cooperation, acquire advanced technologies, and undergo industrial transformation (Jiang et al., 2020). China, the world's largest developing country, has experienced sizeable growth in OFDI since the implementation of the "Go Global" strategy at the turn of new millennium, becoming a major source of OFDI worldwide. According to the Statistical Bulletin of China's Outward Foreign Direct Investment, China's nonfinancial OFDI has increased approximately 55-fold in 20 years, from \$2.7 billion in 2002 to \$152.02 billion in 2021, making it the second-largest global outbound investor¹. This signifies the

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historic transition of Chinese corporations from global manufacturers to global investors. However, the rapid development of the digital economy, particularly in digital finance, has presented both opportunities and challenges for Chinese enterprises expanding globally (Feng & Chen, 2022). While digital technologies open up new avenues for Chinese enterprises to participate in global markets, they also present challenges, such as lack of innovation capacity and modest technological advantages when compared to developed counterparts (Huang and Khan, 2022). This divide is becoming increasingly apparent, with only 17% of enterprises achieving high digital transformation by 2022². This gap limits Chinese enterprises' long-term ability to enhance their global competitiveness, increase productivity, and maximize the benefits of OFDI (Deng et al., 2022). Therefore, bridging the digital divide is critical for Chinese enterprises to remail competitive in the global marketplace. This can be achieved by increasing their capacity for innovation, technological advancements, and operational efficiency, allowing them to maintain competitiveness, increase productivity, and maximize the benefits of their OFDI (Jiang et al., 2023).

The Chinese government has been actively encouraging Chinese enterprises to expand internationally in recent years, and has offered them strong support for their overseas endeavors. This support has manifested itself in a variety of policies aimed at encouraging and facilitating international investment, particularly in the digital economy (Li et al., 2023). A significant policy example was the Guidelines for Foreign Investment Cooperation in Digital Economy, which were published by the Chinese Ministry of Commerce in 2021. These guidelines underscore the significance of actively participating in the global industry chain of digital economy, and optimizing the "Go Global" strategic layout, as well as emphasizing the importance of digital technology in promoting firms' digital transformation and establishing globally competitive digital enterprises (Ge et al., 2022). In this light, studying the relationship between digital finance and China's OFDI can provide valuable insights into the nuanced mechanisms through which digital finance has influenced and shaped the patterns of outbound investment Chinese enterprises. This would help policymakers, researchers, and market participants understand the dynamics of China's international investment landscape. It will also aid policymakers in developing supportive policies and initiatives to encourage and facilitate digitalization among businesses, specifically targeting those with low digitization levels.

Digital finance is an important aspect of the digital economy that uses digital information technology to overcome the time and space constraints of traditional financial services (Cao et al., 2022). It has the potential to improve the efficiency of financial services while lowering associated costs (Gomber et al., 2017; Sun et al., 2023). It may play an important role in easing the financing constraints faced by multinational enterprises and their OFDI (Wang et al., 2022). However, on the flip side of the coin, such digital financial services are available and benefiting to firms that have already digitalized (Zeng et al., 2022). Consequently, firms that have a low level of digitalization (or those lacking digital production and operation practices) are likely to experience digital inequality because of digital divide (Selwyn, 2004; Mayer, 2018). As a result, the impact of digital finance on OFDI is proportional to the digitalization level of enterprises. Due to the high cost, lengthy cycle time, and difficulty of digital transformation projects the digital transformation of enterprises is unfortunately ongoing and expensive (Wen et al., 2022). While a large number of (particularly Chinese) enterprises have a low level of digitalization due to their high tax burden (Chen et al., 2023).

A considerable amount of empirical work has been conducted to assess the determinants of Chinese OFDI. These studies have considered a variety of factors such as human mobility (Gao et al., 2013), exchange rate (Liu & Deseatnicov, 2016), traditional financial supply (Yan et al., 2018), minimum wage (Fan et al., 2018), the Belt and Road Initiative (Du & Zhang, 2018), environmental regulation (Dong et al., 2021), public participation (Li et al., 2022) and so forth. However, the literature on the impact of digital finance on OFDI in the digital age is scarce. While most studies on the economic consequences of digital finance have overlooked the notion of digital divide or digital inequality. The majority of the existing literature only discussed the digital divide theoretically (Robinson, 2015; Lythreatis, 2022) with little empirical research on the topic. While some research

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