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**OUTWARD INVESTMENTS FROM CHINA
AND RUSSIA: MACROECONOMIC AND
INSTITUTIONAL PERSPECTIVE**

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Abstract: China is one of the strategic trade partners for Russia, and both countries are top investors among emerging economies. Surprisingly, this is not justified with the investigation of whether outward foreign direct investments (OFDI) from China and Russia differ from other economies and what are distinguishing characteristics of the OFDI originating from these two countries? Based on institutional theory we test the set of hypotheses concerning OFDI from China and Russia. We conduct panel regression analysis on the sample of Chinese and Russian OFDI for the period 2002-2012. The results show that informal institutions are more important for China than for Russia, whereas for Russian OFDI government plays guiding role. Moreover, our results contradict previous studies saying that less developed institutional environment is more attractive for firms from emerging markets; the rule of law variable shows positive significant coefficient for both countries. Nevertheless, traditional allocation of OFDI still remains important for China and Russia.

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CONTENT

Introduction.....	5
China-Russia context for OFDI.....	5
Outward FDI from China and Russia: institutional perspective	7
Literature analysis and hypotheses development	10
Research method.....	13
Discussion of results	15
Conclusions.....	16
References.....	16
Appendices	19

Outward Investments from China and Russia: Macroeconomic and Institutional Perspective

Introduction

Over the past two decades, IB research has been showing an increased interest in foreign direct investments (FDI) from emerging economies in general, and in the most prominent developing countries (also known as BRICS) as major players among developing economies, in particular. Discussion on how these countries invest internationally, with the focus on outward FDI (OFDI) from China (Buckley et al., 2007; Deng, 2009; Kotabe, Jiang, & Murray, 2010; Morck, Yeung, & Zhao, 2008) has led to an attempt in understanding the comparative features of OFDI from various emerging markets (Del Sol & Kogan, 2007; Tolentino, 2010). The key questions, however, remain relatively unchanged since initial scholarly attempts to describe and understand the phenomena of FDI within the narrow scope of emerging economies' investment: Can and should the Chinese and Russian outward FDI (OFDI) be treated similarly or separately to those from other economies, and, if there is a difference, what are the major distinguishing characteristics of the OFDI originating from these two countries? We aim to answer this question in this paper.

From the outset of large-scale international investments in the early 2000s, the two countries have remained among the few economies in the world still showing the highest figures in OFDI in spite of the global economic crisis (Panibratov & Kalotay, 2009). Behind the curtain of officially registered OFDI there are multiple rough estimations of the capital flows from both Russia and China, which exceed the official figures on OFDI since the systems of reporting, tracking and registering capital flows are at a developmental stage in both these two countries. The actual figures on FDI, both coming in and going out of Russia and China, are likely to be even higher than those that are stated.

Despite the lack of the long experience in the field of cross-border capital exchange between China and Russia, both the theoretical underpinning of their FDI and the local tools of keeping track of the capital flows are underdeveloped in comparison to those of developed economies. In fact, 2006 was the first year that Russia became a net capital importer, indicating a notably large amount of capital flow for Russian commercial entities and residents (Vahtra, 2009), while Chinese FDI outflow started to grow significantly in 2007 with the inflow being relatively high for a longer period (Cheng & Ma, 2010). Due to this, even less attention was attributed to the process of capital exchange between the two investing countries. It is of a particular focus for this paper to examine the drivers and determinants and to investigate the motives for Russian and Chinese FDI exchange.

China-Russia context for OFDI

Research on how FDI influences both home and host economies suggests a wide range of effects including impacts on domestic employment, trade flows, tax revenues, R&D and innovation expenditures, wages etc. FDI inflows to a developing country increase its capital stock and raise the host country's labor productivity, output, employment, and incomes (Blomström et al., 1998). Moreover, additionally to these outcomes the literature suggests that further efficiency gains in the host economy arise from the increased competition generated by foreign firms, from technological and managerial spillovers, and from learning-by-doing effects in local suppliers (Huang, 2004).

A rapidly changing environment and economic and social shifts have led many developing countries to become a significant source of FDI, particularly to other developing countries. Since the majority of developing countries are usually limited in capital resources, are endowed in labor but face shortcomings with foreign currency, some scholars argue that

developing countries are unable to participate in capital investment abroad. However, in aiming to build and sustain a competitive advantage for companies, many developing countries' governments provide a stimulus for supporting home-country firms' international operations.

Most of the literature concerning FDI from emerging economies focuses on China, India and Brazil, leaving Russia behind the scene; however, some researches dedicated to Russian FDI still exist. Different aspects of FDI theory and its implication in the Russian context have been discussed by Panibratov and Latukha (2014), Kalotay and Sulstarova (2010), Panibratov and Kalotay (2009), Vahtra and Liuhto (2006). Vahtra and Liuhto (2006) have examined Russian FDI activities with a focus on companies in the oil and gas industries and the motives for Russian international investment. Panibratov and Kalotay (2009) have investigated the political interference in Russia's OFDI. They state that Russia shows a significant difference in FDI patterns from other countries, including those in transition, since Russian companies seek to decrease the possible negative effects of domestic risks by means of establishing an immediate international presence. In other words, Russian outward investments can be generally described and explained within the traditional framework of FDI, although some extensions are needed to explain OFDI from Russia.

While Russia's OFDI being a relatively minor focus within BRICS, most of the studies have been conducted in order to test and assess whether the FDI theory and frameworks are applicable for China's cases and whether they can fully explain China's OFDI (Buckley, 2007; Child & Rodrigues, 2005; Yang, 2003). Buckley (2007) suggests that despite the certain applicability of western theories elaborated for developed countries, slight changes and extensions should be considered when talking about China's FDI: namely, special ownership advantages and institutional factors are needed to be inbuilt within the general FDI theory to explain China's OFDI. Child and Rodrigues (2005) conclude that the study on China's interaction with FDI flows provides the opportunity to extend the existing FDI theory to four primary areas: the latecomer perspective; catch-up strategies; institutional analysis with reference to the role of government; and the relations between entrepreneurs and institutions. All these theoretical investigations' results reveal the conclusion that traditional FDI theory can explain China's OFDI to a certain degree; however, additional amendment, complementation and explanations are needed in the context of China.

Although both Chinese and Russian OFDI have generated considerable interest in recent years, few empirical studies have been conducted to investigate the determinants behind and consequences of the presence of Chinese and Russian MNCs in other countries. Moreover, as we are aware, there were no researches conducted to identify those motives and determinants for these two countries to invest in each other. There is a large literature on the host country determinants of FDI, which suggests that investment is attracted to countries with good institutions (Globerman & Shapiro, 2006). However this statement is applicable only for FDI outflow from developing countries, since the empirical research conducted by Cheng and Ma (2010) exposed the inverse situation, whereby Chinese OFDI is attracted by countries with weaker institutions.

Therefore, we may conclude that, to some extent, the models and results for OFDI from developed countries cannot be fully generalized and applied for a developing economy; and additional studies concerning OFDI from developing countries should be made. Since FDI in general is dominated by flows from developed countries, it is an open question whether existing FDI theories can explain Chinese and/or Russian OFDI. Moreover, there is an emerging literature on FDI flows from developing economies, which suggests that these flows may differ from those of developed economies (Filatotchev et al., 2007), however, most studies of FDI related to China and Russia, have focused on the countries as a location for FDI from other countries, rather than as a source of FDI.

Outward FDI from China and Russia: institutional perspective

Taking the changing nature of institutions in general, and the highly dynamic institutions in emerging economies (with China as an example), an institutional perspective is extremely important for emerging markets (Meyer et al., 2009). Scholars have recently been actively elaborating the questions of how institutional variables of a host country can influence the location choice of FDI, its correlation with location within the chosen country and its interaction with other strategic decisions such as mode choice (Shapiro, Tang, & Ma, 2007). The specific location of operations is a major concern for multinational firms (Cantwell & Iammarino, 2000) and is of particular importance for large decentralized emerging countries, where institutions, environment and policies may differ significantly across different regions. For example, in Russia FDI is concentrated not only in the traditional financial centers in Moscow and St Petersburg, but also in smaller provincial cities that are actively stimulating trade and capital flows by means of introducing reforms and regulations (Meyer & Pind, 1999). In China, institutional differences within the country influence corporate strategies and foreign investment inflow (Zhou, Li, & Tse, 2002).

Institutions also provide opportunities to learn about business partners, to better understand the background to their decisions and likely behavior, significantly reducing information asymmetry – a major source of market failure (Casson, 1997). In many emerging economies, weak networking may significantly increase information asymmetries so firms face higher transaction costs and partner-related risks (Meyer, 2001), and need to spend more resources searching for information (Tong, Reuer, & Peng, 2008).

Institutions are equally important when it comes to selecting an appropriate mode of entry (Brouthers, 2002). Formal institutions, such as the legal framework, and informal institutions, such as the practices of law enforcement, shape the transaction costs in pertinent markets and, consequently, an investor's preference for internalizing markets (Meyer, 2001). Furthermore, institutions may affect transaction costs, efficiency in resource exploitation and capabilities. For example, networking competences are most developed in those countries where transactions are commonly based on personal relationships and networks. The institutional environment thus shapes the key parameters determining FDI, and they are of particular importance when it comes to studying such emerging economies as Russia and China, where government regulations and specific social environments play crucial roles in various aspects of the economy.

Outward FDI from China

Although China's OFDI is still relatively small compared to the massive volumes of inward FDI, it has been picking up for several recent years with Chinese companies seeking momentum for moving internationally, acquiring capital abroad in a broad spectrum of sectors ranging from natural resources to manufacturing and telecoms, and in many others (Salidjanova, 2011). As China is integrating into the global economy, its national economy is growing at a high speed in order to catch up with the world and fulfill the role as a global production facility. China thereafter faces a severe shortage of resources in almost all types of raw materials including oil, uranium, iron ore, aluminum and many others, so the country is actively either building trade relations with natural resource-endowed countries such as Russia, Australia, Brazil and Central Asian countries, or acquiring needed resources through FDI activities.

China outbound investment jumped drastically and started to increase at an almost exponential-like pace starting in 2005, as did FDI inflow. With the announcement of a "go overseas" policy and the start of the 11th five-year plan stimulation and support for China's OFDI commenced. Along with the promotion of China as an investment plateau, performed by the Chinese government, which included the mitigation of legal and bureaucratic obstacles

for inward investment, several actions of promotion were made internally as well, which highly stimulated local firms to go abroad: to set up funds to support outbound investment, to increase the amount of subsidies, to facilitate investment approval procedures, to delegate the approvals from central to local authorities etc. (Cheng & Ma, 2010).

During the period between 1990 and 2000 China's OFDI was not showing any extraordinary growth, while between 2001 and 2005 Chinese firms started to turn their interest towards the idea of moving their interest and capital abroad. Currently, by 2013, China's FDI outflows increased dramatically. Compared with the beginning of 2000s, FDI outflow was more than tenfold, with US\$6.8bln in 2001 and US\$101bln in 2013. At the critical point of 2005-2006 FDI outflows were more than doubled, with a year-over-year change index of almost 100% in 2006 (US\$21bln) against 2005 (US\$12bln). The second two-fold change in outbound investment happened in 2008 compared to 2007, US\$52bln against US\$22bln respectively. Even the outburst of financial crisis did not affect that much the growth tendency of Chinese investment activity, which slowed down, but continued the ongoing escalation.

It is of crucial importance to mention one of the major initiatives of Chinese government to initiate and stimulate a country's capital outflow. In 2006 China began to explore the ideas of setting up "overseas China economic and trade cooperation zones" in host countries. These zones were supposed to fulfill the following several purposes: to expand exports through the host economies in order to decrease bilateral trade frictions caused by the rapid increase in Chinese exports; develop Chinese firms and build Chinese brands in the global market place; to reduce the overflowing foreign reserves; and to create a cluster of Chinese companies abroad, which would be easier to support.

The target countries for these zones were those, who, firstly, maintained good political bilateral relationships with China and, secondly, could bring trade and FDI benefits in return back to China by means of economy specialization (mainly natural resources, which are lacking in China), namely: Russia (Ussuriysk economic and trade zone, approved in 2006; Transbaikal zone), North Korea, Pakistan, (Haier-Ruba zone, 2006), Nigeria, Kazakhstan, and Cambodia (Lake Tai zone) (Cheng & Ma, 2010).

This initiative of the government succeeded in attracting Chinese firms to invest abroad, and highly facilitated the investment process and activity of Chinese companies. Provided with substantial financial support, firms have adjusted to the understanding of opportunities lying outside the borders of China.

According to many studies of Chinese investments (Luo, Xue, & Han, 2010; Wang et al., 2012), a higher degree of state ownership increases OFDI. The biggest sources of China's OFDI are profitable and listed state-owned companies. According to Cheng and Ma (2010), the share of OFDI made by SOEs in the first decade of the 20th century was approximately 83%. However, most of these companies are listed on domestic and foreign stock exchanges and are obliged to meet certain transparency and corporate governance requirements, while private-owned companies are not so transparent and usually keep internal information closed. It is hard to reveal the political motives and influences on the decision-making processes of these large enterprises and it may vary across sectors and regions. However, apparently, there are clear political motives and effects in the natural resources sector, while in other sectors, investment decisions appear to be on a commercial basis and only limited political involvement has been observed.

In 2013, Chinese outward investment flowed to more than 165 countries across all regions of the world. The Asian region represents the major share in China's OFDI, constituting 70% of total outflow, with one dominant destination being Hong Kong. Hong Kong was the top destination since the very beginning of China's expansion abroad and it remains the absolute leader in China's ODI, with a stand-alone 83% of the region share and making an outstanding 58% of total outward investment. Other newly industrialized countries

of Asia (Singapore, Indonesia) also represent a specific interest for China's investment; however, shaded by the giant share taken by Hong Kong, altogether they stand for only 3%.

There are three major distinctive features driving China's OFDI: proximity (both territorial and cultural), market size and growth, and natural resource endowment (Buckley et al., 2007). All investment activities and the spread of Chinese investment flows are predetermined by one or several of these factors, meanwhile Australia and Central Asia are appealing for natural resource investment, Europe and US are attractive for their market size and opportunities, and Hong Kong and Singapore are close in terms of culture and business management environment.

Outward FDI from Russia

OFDI from Russia has significantly increased over the past few years (Panibratov, 2012a). With more than US\$95bln of FDI outflow in 2013 Russian Federation appears to be one of the leading countries in terms of direct investment abroad, followed only by the USA, Japan and China (UNCTAD, 2014). The speed of growth of Russian OFDI is one of the highest in the world.

Russian companies are sharply abandoning simplistic import-export activities and are beginning to use a broad variety of more sophisticated investment tools in the cross-country value exchange. As one of the examples – OFDI stock has risen dramatically from US\$20bln in 2000 up to more than US\$370bln in 2007 and almost US\$390bln in 2012. The significant drop in outward investment escalation in 2008 was definitely the result of the breakout of the world financial crisis, when the investment climate throughout the world became very unpredictable, but by 2009 OFDI recovered its trail of growth.

Sourcing OFDI from Russia indicates a growing interest by Russian companies to seek newer and better opportunities for their business expansion outside the borders of its home country, a readiness to increase their international competitiveness and to strengthen their international position in the global market by means of gaining access to resources, strategic assets and new markets worldwide. The outstanding growth of OFDI performed by Russian companies shows that in some cases companies find investment opportunities abroad more attractive than domestic ones. This fact derives from drawbacks in the business environment, an underdevelopment of policy regulations and pitfalls with governmental practices (Vahtra & Liuhto, 2006). In other words, companies seek to escape the unfavorable system of the home country environment and safeguard their business from domestic risks by establishing an immediate international presence (Settles, 2008).

The key features of the recent trends in OFDI from Russia are that companies start to expand from both the traditional investment direction of the neighborhood (CIS and Eastern Europe) and developed countries (Western Europe and USA) towards totally new regions with vast opportunities – Latin America and Asia-Pacific.

Another distinctive characteristic of Russian OFDI is so-called round-tripping, when investment occurs through companies located in third countries. This explains why Cyprus has always been traditionally one of leading destinations of Russian OFDI flows – it provides an offshore platform for further investment activities or trans-shipping of investment. There are some assumptions (Kalotay, 2010) – that to a significant degree inward FDI into Russia consists of the capital that has been already transferred out of the country in order to get tax reductions and other benefits provided to external investors.

The third major feature of Russian OFDI is its unequal distribution between huge industrial companies and firms of a lesser scale, including SMEs. Large enterprises exercise control over the OFDI flows and combined together make up the absolute majority of investment activities, however recent trends show growth in the interest of small- and medium-sized Russian firms investing abroad (e.g., Latukha et al., 2011; Panibratov, 2012b), which is, nevertheless, quite an exception in the overall investment activity of Russian firms.

Principally, this gap takes root from the different financing capabilities and objectives for investment. SMEs are limited in resources; therefore, their OFDI activities are mostly encompassed by seeking for market niches and technologies, and rarely on acquiring assets (Vahtra & Liuhto, 2006).

The other reason behind the inequality of FDI amounts between MNCs and SMEs is the lack of information and publications on OFDI produced by the latter. While industrial giants are eager to show their international presence and raise their image for potential investors inside the home country and abroad, SMEs are not announcing their expansion, thus the analyzing and estimating of the scope of their international activities becomes very complex.

The CIS and EU countries are still the main recipients of Russian investment. The share of the European Union is about 40%, mainly due to Cyprus and Netherlands – countries with favorable legislative and taxation policies for foreign investment. The CIS still represents a major destination for OFDI (UNCTAD, cross-border M&A database) including approximately one fifth of Russian OFDI with more than 80% spread amongst neighboring countries (Ukraine, Belarus, Kazakhstan).

The new destinations of Latin America and the Asia-Pacific region mainly comprise developing countries, which have become increasingly attractive for Russian companies together with a better understanding of the opportunities they can provide. Giving broad scope for those who seek new markets, greater efficiency or resources, countries like China, India, Brazil and Chile provide an opportunity to enhance their business, meanwhile Australia, Hong Kong and Singapore, being developed countries, could become substantial in terms of strategic assets and technologies. Even though these countries altogether only make up no more than 10% of current OFDI their significance is steadily growing.

China is one of the main trade partners of the Russian Federation (firmly supporting this statement is the simple fact that many corporate portals of Russian firms, especially in the natural resource sectors, have a version in Chinese language). China also has one of the highest index of growth for goods exchange, and FDI as a new commonly used tool of moving capital across borders, should theoretically follow the same flow and trends as export does. However, despite the significance of China for Russian international trade, its attractiveness as a platform for Russian outward investment leaves a lot to be desired. The first OFDI activities targeted in China took place only in 2005, and by 2007 the total OFDI forwarded to China was approximately US\$54mln, which accounts for about 1.2% of the total Russian OFDI value. In 2008, based upon the fall-outs of the financial crisis, the amount of Russian investment into China declined up to less than the half of this value standing for mere 0.4%, 0.5% in 2009, and begun recovering back in 2010 reaching 0.6% of the total. However, many Russian companies still announce a strong interest in investing in China, considering this country to provide a broad variety of opportunities for the expansion and the development of their business.

Literature analysis and hypotheses development

Determinants of Russian and Chinese OFDI

Home-country GDP

The home-country environment, including GDP growth, can be perceived as a macro-level extension of the ownership advantage of local MNCs and, therefore, is expected to play an important role in determining OFDI flows from a particular country (Kalotay & Sulstarova, 2010). It is expected to be of particularly high importance in the case of Russian and Chinese OFDI, since the largest values in the share of the total OFDI are perceived to be carried out by large multinational companies that contribute the most to the GDP growth.

Host-country GDP

As a proxy for market-seeking motivation for the internationalization of the companies and, therefore, determinants for market-seeking investments host-country GDP and GDP per-capita are introduced in this research as a measure of absolute the market size and market attractiveness of the host-country (Dunning, 1979; Chakrabarti & Basu, 2002). Host country market size is expected to be a significant determinant and have a positive impact on FDI flow: as the market grows, so do the opportunities for investors for achieving better results in profit generation. Market size is estimated to be one of the major determinants for Russian and Chinese OFDI and explicators of both countries' continuous investments in production facilities and distribution networks in developed regions.

Natural resource endowments of host country

The previous research has also widely considered resource-seeking investment in multiple empirical tests (Buckley, 2007; Cheung & Qian, 2008). Recent trends in China's OFDI demonstrate that Chinese investments are strongly motivated by the need to satisfy their growing demand for primary resources and this is especially true for investments in developing countries (Buckley, 2007), while for Russia resource-seeking investment motives are strong in metal mining and metallurgical industries, which continuously face trade barriers imposed by other countries and growing production costs in the home country and at the same time they are eager to diversify their resource base (Kalotay & Sulstarova, 2010). However China's ODI is expected to have a positive correlation to the resource endowment of the host country, whereas Russia's ODI is not expected so. In order to explain this correlation we introduce the *natural resource endowment* as a variable showing relative resource endowment across countries.

Geographic distance

Market-seeking companies are more likely to serve geographically proximate locations through export, while more distant markets through FDI (Buckley & Casson, 1981). This would suggest a substitution of FDI for other modes of serving markets as distance increases. On the other hand, the correlation between FDI and distance could be negative, since according to the gravity model the increase in distance could result in growth in transaction costs (Kolstad & Wiig, 2012). However, the overview of recent trends in Russia and China OFDI activity shows an inverse correlation, meaning that the majority of FDI flows into nearby countries. The predictions over the interdependence between FDI and distance from an investing economy are to be open and discussed in line with the further results.

Hypothesis 1: Market size of both home and host country are important arguments for Chinese and Russian OFDI.

Hypothesis 2: While investing abroad China and Russia choose amongst countries with high market potential and endowment in natural resources

Hypothesis 2a: with Russia seeking energy-demanding countries;

Hypothesis 2b: and China seeking energy-rich countries.

Hypothesis 3: Russia and China invest more in geographically closed countries

Apart from the macroeconomic indexes embedded in this research, our study will also encapsulate the investigation of institutional development and governance factors determining Russian and Chinese OFDI and derive institutional variables.

It is likely that institutions and governance are important determinants of FDI, especially in case of less-developed countries (Blonigen, 2005). Poor legal protection leads to

increasing costs of business operations, decreasing FDI motives, while poor institutions result in underdevelopment of infrastructure, hence, negatively influencing FDI inflows into countries. There is empirical evidence that diverse corruption indices strongly and negatively influence FDI (Wei, 2000).

However, a number of studies on China's OFDI have generated empirically supported conclusions that Chinese companies have competitive advantage in countries with poor institutions. The level of corruption in China is much higher than in developed countries, so Chinese multinational companies are much more experienced in operating in an opaque business environment and bribery (Kolstad & Wiig, 2012). Despite the absence of researches dedicated to the institutional impact of Russia's OFDI, it is clear that the same, or more or less similar, situation can be observed in the case of the Russian business environment and Russian companies, so one may conclude a general similarity from this perspective. Thus we derive following hypothesis concerning institutional distance:

Hypothesis 4: Institutional distance between Russia, China and host country negatively affects the volume of OFDI.

Regulatory quality

Regulatory quality captures perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development. It encapsulates such aspects as price control, tax policy, antimonopoly policy, protectionism, competition, subsidies and many others. Based on common sense the quality of governmental regulations should have a positive impact on FDI, however, taking into consideration the above-mentioned relationship between institutional underdevelopment in host and home countries and investment performance of Chinese firms, we suppose a negative correlation between regulatory quality in the host country and OFDI specifically for Russian and Chinese companies.

Hypothesis 5: Chinese and Russian OFDI are associated negatively with host government regulatory quality.

Cultural distance

According to North (1991) informal institutions define the rules of the game as formal ones. Many scholars argue that in emerging markets informal institutions often substitute formal because of their underdevelopment (Peng, 2013). Therefore we suggest that for Russian and Chinese firms similar cultural environment plays important role while choosing allocation of OFDI.

Hypothesis 6: Russian and Chinese OFDI are positively associated with smaller cultural distance.

Formal and informal involvement of the State

While trying to explain the role of the State in OFDI, prior research argues that this role of state ownership (Sun, Xu, & Zhou, 2011) and of organizational linkages through measures such as politicians serving as members of boards and as part of the top management team (Lester, Hillman, Zardkoohi, & Cannella, 2008; Hillman, Zardkoohi, & Bierman, 1999). As for interpersonal relationships – such as the personal relations of CEOs with Parliament members or even the President – they are hidden and uneven, in the literature as well as in the real life. Yet, Boddewyn and Brewer (1994) consider these 'political' relationships or ties as

an efficient tool that provide better access to decision makers, and better bargaining skills. Both China and Russia are the most frequent context in which to study the informal role of the State and politics in the process of international investments of domestic firms, with Russia, it can be argued, being the most controversial case (Panibratov, 2013; 2014). This informal role of the government affects OFDI from China and Russia at least to the same extent as instruments that are more formal.

Nevertheless formal state engagement in overseas investments of Russian and Chinese companies should not be overlooked. Recently bilateral investment treaties (BIT) got significant attention from the scholars. BITs legitimize the host market in the eyes of foreign investors; reduce the ambiguity of the host government's obligations; offer the prospect of international arbitration (Trevino et al, 2008; Garcia-Bolivar and Schmidt, 2004; Kerner, 2009). Therefore we assume that there is a direct effect of signed BIT between two governments and volume of OFDI to the partner country.

Hypothesis 7: OFDI from China and Russia are largely driven and supported by state initiatives and political mechanisms, which may both promote or prevent outward investments.

Research method

Data collection

We collected data on Chinese OFDI from Chinese Statistical Yearbook publishing annually by National Bureau of Statistics of China. Data on Russian OFDI we derived from Russian Central Bank website where this data has been published since 2007. Thus we limit our time period for seven years: 2007 – 2013. All macro data were collected from secondary sources such as Thomson Reuters Database, World Bank database, Unctad. In order to avoid biased results we eliminated tax heaven countries from the sample. Consequently we got 411 observations for Russia and 154 observations for China.

Table 1.

Variable	Name	Description
Dependent	OFDI	Volume of OFDI from China and Russia at certain year. Statistical yearbook for China; Rosstat (before 2007), Central Bank data (since 2007) for Russia
Independents: Macroeconomic factors	GDP _{hc} GDP _{home} Natres RD	GDP host country GDP home country Natural resources endowments host country R&D expenditure, % of GDP host country
formal institutions	WGI: Rulelaw _{hc} Corruption control	World Government Indicators Rule of law host country Corruption control of home country
informal institutions	cultdist	Cultural distance calculated by Hofstede indexes.

Regions	CIS Geodist	Commonwealth of independent States Asian region
Institutional distance	instdist	Coefficient calculated as a root of squared sum of four world governance indicator: rule of law, political instability, control of corruption and government effectiveness. (absolute value)
Role of the State	BIT	Bilateral Investment Treaties

Our *empirical model* looks as follows:

$$FDI_{it} = \alpha + \beta_1 BIT_i + \beta_2 HGDP_{it} + \beta_3 HGDP_{pcit} + \beta_4 RULE_{it} + \beta_5 CORCONTR_t + \beta_6 CDIST_i + \beta_7 CI_{Si} + \beta_8 GEO_i + \epsilon_{it}$$

where dependent variable OFDI_{it}, represents Russia/China OFDI in country i in year t and is a function of the following home-country explanatory variables: BIT_i – dummy variable reflecting whether there is bilateral investment contract with host country or not; HGDP_{it}, HGDP_{homeit} – GDP of host and home country at certain year respectively; RULE_{it} – rule of law indicator in host country, CORCONTR – the control of corruption in home country at certain year; CDIST_i – cultural distance with host country; CIS_i – membership in CIS; GEO_i – country's belonging to Asian region.

Empirical testing

We conducted random effects panel regression analysis for both models (Chinese and Russian) using Stata 13 software.

We tested the models for multicollinearity, thus we had to run different models separating institutional distance variable and rule of law and corruption control variables. Results of both models regression are presented in the table below.

Independent variables	Russia model1	China model1	Russia model2	Chinese model2
GDP host country	-.0500125 (-1.63)	.0788838** (2.08)	-.062221 (-1.44)	.1095287*** (4.75)
GDP home country	.0414795** (2.25)	1.663826*** (5.03)	.0434737** (2.36)	1.792456*** (5.66)
Cultural distance	-.0062214 (-0.64)	-.0716407** (-2.09)	.0014188 (0.07)	-.057845* (-1.77)
BITs	.681624** (2.26)	-.076487 (-0.19)	.7661529** (2.32)	-.8989313* (-1.79)
Rule of law host country	.0532424*** (4.30)	.0249457* (1.69)	-	-
Control of corruption home country	.021042 (0.40)	-.0534165 (-1.51)	-	-
Institutional distance	-	-	.0159974** (2.04)	.0108633 (1.20)
Natural resources endowments	-.0132972 (-1.23)	.0266659 (1.18)	.0050194 (0.35)	.0182382 (0.80)
R&D expenditure, % of GDP host country	.0386058 (0.25)	.2725065 (1.14)	.5180091** (2.06)	.5056399** (2.11)

CIS	2.87536*** (3.77)	-	1.707314** (2.37)	-
GEO	-	.3452722 (0.62)	-	.5037419 (0.97)
_cons	-.3231701 (-0.23)	-39.6377** (-4.43)	1.642821 (1.30)	-45.5605*** (-4.87)
R-sq overall:	0.2492	0.3535	0.1848	0.3553
Prob>chi	0.0000	0.0000	0.0000	0.0000
Sample size	411	154	411	154

Discussion of results

Empirical testing partly confirmed our hypothesis but partly disapproved some, what encourages future investigation. Thus among macroeconomic factors neither R&D expenditure nor natural resources endowment showed significant results in both Chinese and Russian models. However in models including institutional distance variable R&D reveals positive significant coefficient for Russia and for China confirming the technology seeking motive of emerging markets firms. GDP of host country (market size) positively correlates with volume of OFDI for China, but doesn't confirm this hypothesis for Russia. At the same time home country GDP turns significant in each model for both countries, confirming that economic growth at home positively affects outward direct investments.

The guiding role of the state was confirmed for Russia in both models. Signed BIT with host country stimulates outward investment to this country, however for China we got opposite negative result in the model capturing institutional distance. There might be following explanation: the study covers 7 years period of time, while companies need time to react on government actions. In the short run signed BITs might not have immediate positive effect on OFDI, moreover companies may wait for further explicit signals especially if the host market is unfamiliar.

As for institutional factors we observe significance of the rule of the law indicator in host country. Better rule of law leads to more investment to this market from Russia and China. Therefore our hypothesis that Chinese and Russian OFDI are attracted by weak institution environment doesn't get any support. Moreover institutional distance in case of Russia positively associates with volume of outward investment. This means that Russian firms prefer to invest into markets either with strong formal institutions or very weak institutions (the variable is in absolute value). In Chinese model this variable was not significant.

In regards to informal institutions we observe difference between two countries. Cultural distance negatively affects OFDI from China showing significant results in both models whereas for Russia this variable insignificant. Nevertheless regional variable such as membership in CIS positively associates with volume of OFDI form Russia. Countries belonging to CIS might be very distant from Russia culturally, but common past provide firms with understanding of economic, institutional and political environment. Furthermore in majority of those countries people still speak Russian what facilitates cooperation. Surprisingly in Chinese case geographical proximity didn't reveal significant result.

Conclusions

Our study shows that institutional factors can affect outward investment from Russia and China. However we observe certain differences: for China informal institutions are more important whereas for Russia governmental support plays crucial role. Furthermore both countries tend to invest in countries with high level of formal institution's development, what contradict previous studies. Thus we can observe institutional change in both countries which affects internationalization strategies – now they aim to invest safe, relying on formal rules and regulations as it will lead to long-term business development.

Limitations of the study

The first and the most significant problem in this and other similar studies is the availability and reliability of the data to be collected. The two countries still lack a developed system of reporting and gathering information about macroeconomic activities, therefore there were data discrepancies between figures that were reported by worldwide and local databases.

Both Russia and China experience a state of things whereby companies are sometimes not eager to disclose information about their operations and international activities in particular, which makes the analysis of FDI flows an uneasy task. Furthermore, given the shortness of the time series available for analysis – both countries became significant capital investors in the mid-2000s – a short period for observation does not necessarily properly reflect actual trends and patterns of OFDI.

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Appendices

Annex 1. Major recipient economies of China's ODI by region, 2007-2013, US\$ 100 million.

Country or Region	2007	2008	2009	2010	2011	2012	2013
Total	2650609	5590717	5652899	6881131	7465404	8780353	10784371
Asia	1659315	4354750	4040759	4489046	4549445	6478494	7560426
Hong Kong, China	1373235	3864030	3560057	3850521	3565484	5123844	6282378
Indonesia	9909	17398	22609	20131	59219	136129	156338
Japan	3903	5862	8410	33799	14942	21065	43405
Macao, China	4731	64338	45634	9604	20288	1660	39477
Singapore	39773	155095	141425	111850	326896	151875	203267
Republic of Korea	5667	9691	26512	-72168	34172	94240	26875
Thailand	7641	4547	4977	69987	23011	47860	75519
Vietnam	11088	11984	11239	30513	18919	34943	48050
Africa	157431	549055	143887	211199	317314	251666	337064
Algeria	14592	4225	22876	18600	11434	24588	19130
Sudan	6540	-6314	1930	3096	91186	-169	14091
Guinea	1320	832	2698	974	2455	6444	10013
Madagascar	1324	6116	4256	3358	2310	843	1551
Nigeria	39035	16256	17186	18489	19742	33305	20913
South Africa	45441	480786	4159	41117	-1417	-81491	-8919
Europe	154043	87579	335272	676019	825108	703509	594853
United Kingdom	56654	1671	19217	33033	141970	277473	141958
Germany	23866	18341	17921	41235	51238	79933	91081
France	962	3105	4519	2641	348232	15393	26044
Russia	47761	39523	34822	56772	71581	78462	102225
Latin America	490241	367725	732790	1053827	1193582	616974	1435895
Bahamas	3899	-5591	100	-	-	-	-
Cayman Islands	260159	152401	536630	349613	493646	82743	925340
Mexico	1716	563	82	2673	4154	10042	4973
Virgin Is. (E)	187614	210433	161205	611976	620833	223928	322156
North America	112571	36421	152193	262144	248132	488200	490101
Canada	103257	703	61313	114229	55407	79516	100865

United States	19573	46203	90874	130829	181142	404785	387343
Oceania	77008	195187	247998	188896	331823	241510	366032
Australia	53159	189215	243643	170170	316529	217298	345798
New Zealand	-160	646	902	6375	2789	9406	19040

Source: China Statistical Yearbook

Annex 2. Geographical distribution of Russian OFDI flows, US\$ millions, percentage.

Country	2007	2008	2009	2010	2011	2012	2013
Total by countries	44 801	55 663	43 281	52 616	66 851	48 822	86 712
CIS countries	3 642	3 563	3 890	1 338	4 430	2 340	2 238
incl.:							
ARMENIA	277	266	179	5	69	130	94
AZERBAIJAN	5	104	5	9	9	-6	37
BELARUS	813	1 032	1 370	934	2 819	593	867
KAZAKHSTAN	107	326	1 028	-225	674	845	671
KYRGYSTAN	-11	0	0	11	20	-2	11
REPUBLIC OF MOLDOVA	43	15	110	21	-5	131	43
TANZANIA	45	23	14	8	48	38	-42
TURKMENIA	7	25	55	-60	0	2	23
UKRAINE	1 667	146	678	485	703	600	496
UZBEKISTAN	355	414	217	151	92	9	-12
<i>Not classified by countries</i>	231	1 150	232	0	0	0	52
Far-abroad countries	41 159	52 100	39 392	51 277	62 421	46 482	84 474
Eastern Europe							
ALBANIA	230	253	458	847	512	1 035	5 265
ABKHAZIA	...	0	2	44	30	23	6
BOSNIA AND HERZEGOVINA	125	441	261	319	522	716	554
BULGARIA	2 734	1 306	854	1 056	1 072	1 136	571
CZECH REPUBLIC	248	319	142	360	337	265	340
GEORGIA	33	58	32	318	88	63	98
HUNGARY	0	0	2	1	1	3	1
POLAND	28	-50	13	-2	30	-2	73
ROMANIA	1	25	39	196	-96	-1	-101
SLOVAKIA	13	29	7	11	19	49	32
Total Eastern Europe	3 413	2 381	1 809	3 150	2 515	3 288	6 839
Western Europe							
AUSTRIA	230	253	458	847	512	1 035	5 265
BELGIUM	-10	50	235	2 842	-2 032	-1 030	100
CROATIA	95	75	13	23	103	31	71
DENMARK	...	0	-9	47	60	56	33
ESTONIA	13	29	11	21	30	85	130
FINLAND	110	154	186	236	63	271	91
FRANCE	257	217	386	334	656	1 430	449
FRENCH GUIANA	0	2	0	0	0	0	0

GERMANY	0	0	0	3	0	0	0
GREECE	2	0	3	85	26	9	244
IRELAND	0	0	0	112	0	1	0
ISLE OF MAN	-107	-65	-14	527	21	-1	-18
ITALY	258	458	375	490	812	980	1 356
LATVIA	79	166	78	147	328	348	568
LICHTENSTEIN	16	11	4	0	7	130	-121
LITUANIA	57	57	64	49	66	28	46
LUXEMBOURG	497	2 633	765	2 483	2 005	-504	1 314
MAKEDONIA	0	0	0	0	1	3	1
MALTA	9	32	-1	8	-1	-10	2
MONAKO	81	82	52	79	362	116	281
MONTENEGRO	188	173	85	117	160	185	173
NORWAY	-10	2	22	144	26	80	39
PORTUGAL	3	25	24	25	24	30	45
SERBIA	44	11	609	208	372	63	-39
SLOVENIA	49	9	2	3	10	18	29
SPAIN	230	299	-438	1 185	527	512	264
SWEDEN	-55	177	256	203	489	390	-720
SWITZERLAND	1 404	2 426	1 806	1 750	3 719	76	1 358
THE NETHERLANDS	11 991	4 684	3 376	7 035	9 901	2 599	-3 022
UNITED KINGDOM	2 454	3 886	1 997	1 232	1 474	632	1 294
Total Western Europe	17 885	15 848	10 345	20 239	19 724	7 562	9 231
North America							
CANADA	87	295	158	315	387	403	538
USA	973	7 264	1 634	1 060	1 625	688	739
Total North America	1 060	7 560	1 791	1 375	2 011	1 091	1 277
Asia							
AFGANISTAN	0	218	3	1	5	5	1
CHINA	0	54	0	0	0	0	0
HONG KONG	886	1 311	2 178	-533	1 186	93	206
INDIA	50	42	25	59	88	86	158
INDONESIA	13	401	2	597	17	275	1
JAPAN	19	5	-2	-1	1	0	1
LAOS	0	0	1	3	5	0	0
NORTH KOREA	0	0	4	2	0	0	0
SEYSELLES	4	6	9	13	-24	42	41
SINGAPORE	1	0	0	18	155	1 262	304
SOUTH KOREA	1	28	0	1	70	113	2
TAIWAN (CHINA)	0	0	0	0	0	-1	-1
THAILAND	7	24	15	31	56	79	132
THE PHILIPPINES	0	0	0	0	4	0	0
TIMOR-LESTE	0	28	7	-5	-17	-37	-38
VIETNAM	1 345	3 962	2 301	1 834	3 861	7 395	62 266
Total Asia	2 325	6 078	4 543	2 021	5 407	9 312	63 075
Central and South America							

ARGENTINA	0	0	0	1	9	17	10
BRAZIL	1	55	287	94	104	149	78
COSTA RICA	11	6	-1	8	-3	19	8
CUBA	0	0	0	0	1	1	1
DOMINICAN REPUBLIC	14	6	-57	11	5	2	5
GUATEMALA	0	0	41	173	91	99	16
MEXICA	0	0	0	0	-1	0	1
PANAMA	1	2	1	24	5	6	4
PERU	4	0	0	0	3	0	1
URUGUAY	0	0	0	0	2	1	2
Total Central and South America	31	70	271	310	216	295	125
Tax heavens							
ANDORRA	0	0	0	88	8	-5	-21
ANGUILLA	0	0	0	0	0	0	1
BAHAMAS	0	0	0	0	-1	-1	0
BELIZE	0	0	0	259	-115	-144	0
BERMUDA ISLANDS	80	49	36	36	61	536	-450
CAYMAN ISLANDS	53	718	296	74	-226	-13	507
CYPRUS	14 700	15 524	15 288	18 309	22 930	20 920	7 689
DOMINICA	14	6	-57	11	5	2	5
GIBRALTAR	14	13	0	1	33	-7	91
GUERNSEY	673	1 860	1 488	1 880	971	1 118	1 334
ISLE OF MAN	-107	-65	-14	527	21	-1	-18
JERSEY	-15	16	48	-4	389	215	752
LIBERIA	39	34	10	0	0	0	0
LIECHTENSTEIN	16	11	4	0	7	130	-121
MALTA	9	32	-1	8	-1	-10	2
MAURITIUS	0	0	0	0	0	0	5
NETHERLANDS ANTILLES	0	10	0	0	0
PANAMA	1	2	1	24	5	6	4
SEYSELLES	4	6	9	13	-24	42	41
ST.KITTS & NEVIS	172	22	1	1	4 617	-3 064	-3 612
ST.VINCENT & THE GRENADINES	0	121	0	0	0	0	-4
VIRGIN ISLANDS, BRITISH	51	542	1 789	48	-2 724	67	155
Total Tax Heaven	15 704	18 902	18 898	21 276	25 957	19 792	6 361
Middle East and Africa							
CONGO	48	25	22	30	20	63	14
CYPRUS	0	0	0	0	0	0	1
EGYPT	0	0	0	1	5	6	6
ETHIOPIA	0	0	1	0	0	0	0
IRAQ	0	0	0	0	0	5	32
ISRAEL	2	23	11	12	8	7	4
JORDAN	0	0	0	0	3	2	3
KENIA	181	123	20	863	279	1 105	177

LEBANON	0	0	3	90	1	0	0
LIBERIA	39	34	10	0	0	0	0
LIBIA	30	0	2	0	0	0	0
MAROCCO	0	0	0	0	0	4	-11
MAURITIUS	0	0	0	0	0	0	5
MONGOLIA	1	25	49	2	33	87	-19
NAMIBIA	0	0	0	2	0	1	1
PALESTINE	0	0	0	0	0	0	9
SAUDI ARABIA	0	0	0	2	-1	-1	-2
SOUTH AFRICA	1	1	33	0	0	2	1
TUNISIA	0	0	0	1	0	1	1
TURKEY	183	272	106	143	1 685	4 105	1 447
UAE	902	240	60	81	61	93	169
Total Middle East and Africa	1 386	742	317	1 226	2 094	5 476	1 838
Others							
AUSTRALIA	42	47	14	36	1 104	-64	122
CAIMAN ISLANDS	53	718	296	74	-226	-13	507
CURASAO	0	0	1	0	-3	0	116
DOMINICA	5	5	86	-25	919	388	-16
NETHERLANDS ANTILLES	0	10	0	0	0
NEW ZELAND	1	0	99	7	54	30	32
SAINT KITTIS AND NEVIS	172	22	1	1	4 617	-3 064	-3 612
SAINT VINCENT AND THE GRENADINES	0	121	0	0	0	0	-4
SOUTH OSSETIA	...	0	0	1	-6	0	0
Total Others	272	924	498	94	6 458	-2 723	-2 855
<i>Other countries</i>	213	-57	37	626	23	110	52
<i>Not classified by countries</i>	-543	869	1 256	2 001	2 481	-38	40

Source: Bank of Russia