Determinants of Foreign Subsidiary Exploring Location-Specific Advantages: Capability Transfer and Experience Accumulation

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Abstract
Concerning the increase of foreign investment activities and changes of global environment, performance of foreign subsidiaries has been a crucial issue. According to the classification of FDI (Foreign Direct Investment) motivation, we identify four types of location-specific advantages such as market advantage, resource advantage, efficiency advantage, and strategic asset advantage. Each advantage is complement with different ownership advantage of MNEs. For example, for those MNEs with R&D capabilities as core competence, FDI locations with resource, efficiency, and strategic asset advantages are preferred choices. On the other hand, MNEs with better marketing capabilities prefer FDI locations with market advantage. Therefore, the degree to which the foreign subsidiaries explore location-specific advantages depends on how well the parent firms transfer their core competence to them. For building the enduring enterprise, MNEs also try to use diversification strategies to enter new foreign markets. With accumulation of international and localized experience, foreign subsidiaries have more decision-making autonomy and higher operational efficiency. In this study, we think determinants of foreign subsidiaries exploring location-specific advantages includes the core competence of parent firms. It depends on whether related or unrelated diversification is executed and how much MNEs accumulate experience. To examine our hypotheses, we use Taiwan Economic Journal and China Statistical Yearbook as database source, tracking operating performance of Taiwanese subsidiaries in China from 2000 to 2013. Affirmative conclusion of interaction effects between foreign subsidiaries’ locational advantages and MNEs’ ownership advantages on the performance of foreign subsidiaries is made by empirical tests.

Keywords: Location-Specific Advantage, Ownership Advantage, International Experience, Diversification
Introduction

Foreign direct investment is an important growth strategy for firms (Chang & Rosenzweig, 2001). Most of previous research indicates that the FDI locations chosen by parent firms influence the operating performance of foreign subsidiary companies (Vanhonacker & Pan, 1997), competitive advantage in a global market (Dunning, 1998), and the globalization of value chains (Yamawaki, 2004). With the increase of international investment activities and the change the global environment, the location choice of FDI has been an important issue both in research and practice (Chadee et al., 2003). Demand patterns in local market as well as changes in resource endowment affect global marketing strategies and strategic resources allocation.

Companies choose to invest in foreign markets for a number of reasons. The eclectic theory proposed by Dunning (1980, 1988) has been one of the main frameworks which were widely applied in the past to explain and examine the FDI decisions of multinational firms over the past two decades. It corporates industrial organization theory, product lifecycle theory, and internalization theory to indicate that three potential sources of advantage that may underlie a firm’s decision to become a multinational. There first must be some ownership advantage to investment, which means that the firm controls some specific asset such as know-how, research and development capability, or marketing capability that are not generally available to its competitors which allows it to generate positive profits. Locational advantages focus on the question of where an MNE chooses to locate. There are four main types of benefits pursued by MNEs who decide to go global and enter international markets, including market seeking, resource seeking, efficiency seeking and strategic asset seeking. Market seeking factors of FDI such as market size, market growth, structure of domestic market, etc. aim at penetrating the local markets of host countries. While resource seeking investments are made in order to have access to cheap raw material, pool of labor, infrastructure, etc, new sources of competitiveness, economies of scope and specialization and low cost of production are some of the efficiency seeking factors of FDI (Faeth, 2009). Strategic asset seeking primarily motivates these strategies in advanced economies in the form of acquisitions of local firms (Luo and Tung 2007, Mathews 2006).

Dunning (1995) indicates that FDI location choice is a result of considering MNEs’ ownership advantage, their strategic purposes, and the FDI locational specific advantage evaluations. Resource-based view consider MNE’s ownership advantage is a combination of superior resource sets and management capability, which can be transferred into competitive advantages in host countries (Barney, 1991). Ownership advantages not only help MNEs to make good use of local resources, but also effectively absorbs and integrates local business knowledge and technology and builds new capabilities (Madhok, 1997). However, each MNE has different core competencies because of different resources, resulting in different motivation of FDI. For example, if MNEs have a leading technological capability, they may seek to diversify their investment in natural resources to reduce their production costs, or to seek market locations to build a leading market position.

Therefore, FDI is an important way to match the core competence of MNEs and the locational advantage of the host country. With different investment objectives, FDI
can be divided into two types: asset exploitation and asset seeking (Galan, González-Benito, & Zuñiga-Vincente, 2007). From the point of view of asset exploitation, MNEs want to transfer their competitive advantage in the home country to overseas markets through FDI, so they prefer to choose developing or emerging countries as FDI locations, for rich natural resources or the large market. From the perspective of asset seeking, MNEs want to learn from overseas markets to enhance their knowledge and technical ability, so the FDI locations tend to be the developed countries or mature capital markets, or as the upstream country (Makino, Lau, & Yeh, 2002). Although these two views appear to be two distinct FDI decision-making thoughts, they are complementary to each other (He & Wong, 2004; Nachum, Dunning, & Jones, 2000).

In addition to expanding the benefits of self-reliance through FDI, MNEs also try to diversify their reach by pursuing growth through new business ventures. However, the international diversification involves the expansion of professional management, diversification and geographical scope. The core competence of the enterprise itself and the subsidiaries' operation projects are crucial to whether the international diversified enterprises can achieve diversified operational risks and make effective use of the overseas geographical advantages so as to improve the financial performance of the subsidiaries.

The accumulation of international experience also affect the subsidiary's decision-making autonomy and operational efficiency. In the early stages of market entry, foreign affiliates face not only the impact of language and cultural differences (Hirsch, 1976) but also the limitations of the local governments. In order to reduce the uncertainty of the local environment, MNEs hope to make full use of their accumulated research and development capabilities, marketing capabilities, management experience, the development of overseas markets or to seek strategic resources to maintain their competitive advantage. With the accumulation of international experience and knowledge, and with a certain degree of understanding of the local market, the autonomy of foreign subsidiaries will be increasingly high, less and less leaning on their parent company. Foreign subsidiaries have the ability to accumulate the local market-related knowledge back to the parent company, and help their diversification and innovation.

In order to validate the above-mentioned points, we must track the location characteristics and management performance faced by foreign subsidiaries, and combine MNEs' self-supporting and international experience to explore the advantages of subsidiaries. Most of past studies use cross-sectional research methods such as case studies (Hannula, 2005) or questionnaires (Makino et al., 2002; Tseng, 2007; Tahir & Larimo, 2004), which show respondents' subjective perception rather than effectively examine the operation of foreign subsidiaries. The literatures of FDI location decision often use the location choice or investment amount as the response variables and clarify which are the most critical locational advantages by testing the effects of location characteristics on firms' performance. This study examines whether these local advantages can be harnessed by foreign subsidiaries from the perspective of business performance of subsidiaries and discusses some moderators such as the parent company's ownership advantage, the degree of international diversification, the accumulation of international experience. It is hoped that the
research results can provide MNEs important information and decision-making environment and ability to make good use of locational advantages.

This study use the Taiwanese firms’ investment in the China China market as an example, to explore how the foreign subsidiaries adept in using locational advantages. Dunning (1998) divides FDI motivations into four categories: market seeking, resource seeking, efficiency seeking, and strategic asset seeking, and listing the relevant location characteristics respectively. Therefore, we divide the locational advantage into four categories: market advantage, resource advantage, efficiency advantage, and strategic asset advantage, and examines the extent of the subsidiary well utilizing locational advantage. This is our first research purpose.

The benefit of internationalization comes from MNEs’ ownership advantages such as R&D intensity, advertising intensity, and capital intensity (Jung, 1991; Dess, Gupta, Hennart, & Hitt, 1995). Yip et al. (2000) have also found that MNEs' FDI strategy presents a combination of the firm's specific assets and capabilities with local resources to maximize the value of the particular assets and capabilities it possesses, overtake or catch up with local competitors. This study aims to measure the Taiwanese firms’ ownership advantages from the aspects of technological capability, marketing capability and firm size, and discuss which locational advantage can complement with as to explain the extent to which foreign subsidiaries can make full use of various locational advantage. This is our second research purpose.

The relationship between MNEs' international diversification and business performance has not been consistent. This is because international diversification, while making overseas subsidiaries more complex business environment, but also increase its ability to develop and import new products. Most studies suggest that the direct effect of international diversification on firm performance is a nonlinear relationship of decreasing U positive linearity (Daniels & Bracker, 1989; Mathur et al., 2001). In contrast to this view, this study argues that international diversification affects the extent to which parent companies' ownership advantages and managerial experience can be successfully transferred to overseas subsidiaries, thereby influencing the extent to which subsidiaries can take advantage of local advantages. If there is a large difference in operating items between parent companies and foreign subsidiaries, the diversification may results in difficulty in transferring operating experience, and then the subsidiaries may not be able to make good use of the locational advantage. To study whether the degree of diversification will weaken the benefits of operating experience from parent companies to foreign subsidiaries is our third research purpose.

However, with the accumulation of international experience, MNEs not only get more and more familiar with the business environment and cultural customs in host countries, but also accumulated a certain amount of resources and contacts. At this point, the MNEs are looking to acquire new knowledge from the host country and to evolve their capabilities into new products and services (Luo, 2000). As a result, subsidiaries operating in the old business are more autonomous and less dependent on the parent company, while subsidiaries engaged in new businesses are more able to absorb the support of the parent company because of their familiarity with the local environment. Therefore, after the overseas subsidiaries accumulate some local experiences, it is the fourth research purpose to explore whether the degree of
diversification will strengthen the capacity transfer of the parent company. The conceptual framework for this study is shown in Figure 1.

![Conceptual Framework of this Research](image)

Figure 1: Conceptual Framework of this Research

Taken as a whole, the objectives of this study are to examine how the ownership advantages, diversification strategies, and internalization experience influences MNEs to take advantage of FDI-location antecedents. To this end, this study analyzes a sequence of FDI cases of Taiwanese manufacturing firms in China. According to the latest report of the United Nations Conference of Trade and Development (UNCTAD, 2010), China has become the second largest recipient of FDI after the U.S. and received investments valued at US$95 billion in 2009. Of the numerous countries investing in China, Taiwan, which officially opened investment in China in 1991, accounts for a large portion of FDI in China in spite of the political hostility between these two parties.

Notably, this paper delves into the FDI patterns of Taiwanese-listed firms (TLFs) in China at the provincial level and explicitly focuses on the economic incentives, like market size and labor cost, each province offers (Buckley, Devinney, & Louviere, 2007; Coviello & McAuley, 1999). Though China is a unitary nation with a uniform legal system, the institutions that contribute to a well operating market economy (e.g., property rights protection and contract enforcement) can vary across provinces and influence a MNE's location choice (Du, Lu, & Tao, 2008). The structure of this paper is as follows. Section two begins with a review of literature on MNEs' FDI motives with their preferred locational advantages. The remainder of this section introduces some major location antecedents that MNEs consider for FDI decisions in China. The final two sections present the empirical results and discussion.

**Literature Review**

1. International Motivations and Locational Advantages

Compared with exporting, licensing, and non-equity alliances, FDI is an important scope-growing strategy and an entry mode with high commitment (Chang & Rosenzweig, 2001). Although FDI involves higher operational risk and liability for MNEs, they can benefit from this investment through effective management control, communication; and, more importantly, decision autonomy (Zaheer, 1995). Of the FDI-related decisions that MNEs make, location choice has a crucial impact on the probability of success and profits. In his prominent article, Dunning (1998) identifies four FDI motives for MNEs that comprise resource-seeking, market-seeking, efficiency-seeking, and strategic asset-seeking. Following Dunning's classification, Makino et al. (2002) distinguish FDI motives into asset-exploitation and assetexploration, either of which leads firms to choose different location patterns.
Firms with asset-exploitation motives are those that intend to transfer their specialty to a host country and extend their existing asset advantages (e.g., production know-how). Exploitation-oriented investments mostly occur in less developed countries (LDCs) or in a downstream direction.

Conversely, firms with asset-exploitation motives expect to acquire/upgrade essential assets (e.g., technology) through FDI, and exploration-oriented investments usually take place in developed countries (DCs) or in an upstream direction. Dunning and Narula (1996) propose similar arguments in their investment development path (IDP) framework. In fact, these two streams are not independent but interrelated (He & Wong, 2004). Nachum, Dunning, and Jones (2000) claim that they are complementary and that an FDI decision is the result of the harmonization of motives of MNEs and the locational advantages of the host country. Galan, González-Benito, and Zuñiga-Vincente (2007) further recognize that the FDI motive of MNEs is the prerequisite of location choice, and MNEs make decisions by linking the evaluation of advantages (characteristics) of a destination with specific motives. MNEs with asset-exploitation mindsets have primarily resource-, efficiency-, and market-seeking motives and prioritize factors such as labor cost and market size and potential; but those with asset exploration mindsets seek strategic assets and emphasize factors such as R&D capability and human capital. All four FDI motives and the correspondent FDI location characteristics are illustrated as table 1.

### Table 1: FDI motives and FDI location characteristics

<table>
<thead>
<tr>
<th>FDI motive</th>
<th>Definition</th>
<th>Location characteristics</th>
<th>Wadhwa &amp; Reddy (2011)</th>
<th>UNCTAD (1998)</th>
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<tbody>
<tr>
<td>Market seeking</td>
<td>Focus on local market size or potential of growth.</td>
<td>GDP, natural growth rate, import/output</td>
<td>Market size, income per capita, market growth rate, proximity to global market, preference of local market, market structure.</td>
<td></td>
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<tr>
<td>Resource Seeking</td>
<td>Seek lower cost and more stable supply of materials and resources</td>
<td>Import amount, number of people who use internet, number of people who use cell phones, density of traffic network</td>
<td>Cost of materials, number of low-wage blue-collar workers, infrastructure such as convenience of traffic, telecommunication</td>
<td></td>
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<tr>
<td>Efficiency Seeking</td>
<td>Global allocation of enterprise’s value chain activities based on specialization</td>
<td>Consumer price index</td>
<td>The adjustment of resources through labor productivity Other intermediate material costs A member of the Regional Cooperative Network</td>
<td></td>
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<tr>
<td>Strategic Asset Seeking</td>
<td>Seek a source of technology, marketing and management expertise.</td>
<td></td>
<td>Number of white-collar workers Technology, innovation, brand equity</td>
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</table>

If the overseas subsidiaries can make good use of the locational advantages, then their operating performance must be improved. According to Table 1, we classify the locational advantages of the locations in China as market advantage, resource advantage, efficiency advantage, and strategy asset advantage, and we propose the following research hypotheses:
H1-1: The better the local market advantage is, the better operating performance the China subsidiaries have.
H1-2: The better the local resource advantage is, the better operating performance the China subsidiaries have.
H1-3: The better the local efficiency advantage is, the better operating performance the China subsidiaries have.
H1-4: The better the local strategic asset advantage is, the better operating performance the China subsidiaries have.

2. Ownership Advantage of MNEs

International business and strategic management scholars believe that companies must have some unique advantages or ability to be able to create a competitive advantage, thereby enhancing organizational performance. The eclectic theory (Dunning, 1988) proposes that ownership advantage is divided into asset advantages and trading advantages. The former is the manufacturer itself has the advantages of intangible assets, including technical capacity, management capacity; the latter refers to manufacturers have economies of scale resulting from co-management by international operations. Manufacturers who have intangible assets in the home country have the motivation to the overseas market development. Because the host market and the home market are in different geographical locations, it helps to expand the market, rather than snatch markets from different access channels (Delios & Beamish, 2001; Morck & Yeung, 1998).

For MNEs, appropriate FDI locations help them not only reduce additional costs required for the transfer and application of intangible assets from the home country to the host country, but the expected benefits will not depreciate too much (Delios & Beamish, 2001). Cave (1976) argues that technical competence and marketing expertise are the dominant monopoly advantages of firms. Jung (1991) argues that MNEs must have unique knowledge, such as product differentiation, R&D intensity, and capital intensity, to maintain a competitive advantage in a transnational operating environment. Luo (2002), respectively, to measure the density of ownership of proprietary technology knowledge, the density of advertising spending to measure the ownership of proprietary marketing assets. He found that when two companies have complement resources or consistent target, there is a strong positive relationship between product association and performance.

(1) Technical Capability and R&D Expenditure Density

The investment in research and development is the basis for the development of technological capabilities. By continually updating product-related knowledge, manufacturers are better able to provide superior products and improve their manufacturing processes to gain competitive advantage (Baily, 1972; 1974). R&D investment as a globally undervalued value chain activity, driven by globalization and technological convergence, it is common for MNEs to set up different R&D centers in different countries. In the past, R&D activities of multinational enterprises have been focused on developed countries, but in recent years there are indications that they are gradually shifting from developed to developing countries (UNCTAD, 2005). The R&D activities of multinationals in East Asia are not just technology transfer, but also new forms such as R&D outsourcing, technology search and R&D network.
cooperation (Reddy, 2000; Howells, James, & Malik, 2003). In the past, some studies have found that Taiwanese firms’ FDI location choices are significantly related to their technological capabilities (Chen and Chen, 1998; Makino et al., 2002; Liu and Liu, 2007).

From the perspective of asset exploitation, MNEs want to transfer their competitive advantages to their overseas markets through FDI, so they tend to set up subsidiaries in developing countries or emerging countries, making full use of abundant natural resources or low R&D cost (Makino et al., 2002). MNEs also hope that the investment in the host country will help to well use their technical capacity, or to avoid the technology being imitated. FDI is believed to help foreign subsidiaries to make good use of local R&D human quality and intellectual property rights. Therefore, we propose the following research hypotheses:

H2-1: Taiwanese parent company's technical capacity helps to enhance the positive effect of local resource advantages on China subsidiaries’ performance.

H2-2: Taiwanese parent company's technical capacity helps to enhance the positive effect of local strategic asset advantages on China subsidiaries’ performance.

The network theory of outward investment suggests that FDI is an approach for firms seeking assets such as management, technology and marketing expertise to reinforce, supplement or create new ownership advantages (Buckley & Ghauri, 1989). Chen & Chen (1998) found that Taiwanese investment in Southeast Asia and China is dominated by relational linkages. Firms, while being separate entities, are networked with many other firms to reduce costs, diversify risks, and gain access to key resources through network relationships. A manufacturer of foreign investment, often lead the other upstream and downstream manufacturers together action. So the network will result in the manufacturer of the phenomenon of collective foreign direct investment. After the manufacturers of the finished products assembly factories in certain industries invest in China China, the upstream parts suppliers will naturally go to invest in order to maintain the network relationship, timely supply and finished assembly, and save the transportation cost and tariff. In the Chinese China. Therefore, the following research hypothesis is listed:

H2-3: Taiwanese parent company's technical capacity helps to enhance the positive effect of local efficiency advantages on China subsidiaries’ performance.

(2) Marketing capabilities and advertising spending density

Marketing is the ability to make the value of innovation created by R&D activities exclusive to the firms' investment activities. Firms use advertising, promotions, and promotions in marketing strategies to influence consumers' perceptions to increase the value of the brand, as competitors' imitation and competition barriers help manufacturers increase their market share and generate better profit (Bunch & Smiley, 1992; Kessides, 1990). Because of the heterogeneity of consumer reactions and the dynamics of the market (Dickson, 1992), firms must have the marketing ability to understand the needs of the target market and give consumers a good brand reputation and corporate image. The ability of such assets to allow manufacturers to be convertible between different markets, so that manufacturers can more effectively use
lower cost and potential buyers to communicate in order to create new market segments (Hall, 1992, 1993; Jain, 2001).

Because Taiwan domestic market is limited, if manufacturers do not focus on international strategies such as foreign trade or foreign direct investment, they will be limited by the domestic market and reduce its growth. Therefore, MNEs focus on the overseas investment location of the market advantages, including market growth, market size and so on. Moreover, they hope that the foreign subsidiary can effectively undertake the parent company's marketing capabilities, make good use of the local market advantage. Accordingly, the following research hypothesis is listed:

H2-4: Taiwanese parent company's marketing capacity helps to enhance the positive effect of local market advantages on China subsidiaries’ performance.

3. Degree of diversification and international experience

Enterprises develop new markets or operate new businesses to pursue growth or to improve synergy (Ansoff, 1965). MNEs' overseas subsidiaries can not only increase the utilization rate of resources, but also share new technologies or resources with the existing businesses, or combine the resources of the enterprises with existing resources or make good use of the remaining resources, so as to seek diversification of new markets. A number of studies have also suggested that performance in international related diversification is superior to international unrelated diversification (Berger & Ofek, 1995; Varadarajan & Ramanujam, 1987). Therefore, if the degree of diversification of MNEs is lower, or the overseas subsidiaries are engaged in the original business or related diversification, they can make the subsidiaries more effective use of local resources, or more effectively absorb the original parent company from the application of Advantages. Accordingly, the following research hypothesis is listed:

H3-1: China subsidiaries who are engaged in related diversification have better absorbing ownership advantages from Taiwan parent firm so that the effect of locational advantages on these China subsidiaries’ performance are better.

Although the international diversification makes MNEs in a more complex environment, but by the stimulation of external environment, MNEs get a lot of learning opportunities. Bartlett & Ghoshal (1989) propose that international diversification can make MNEs not only avoid the risks associated with the operation of a single industry, but also avoid the ups and downs of the industry, which cause large fluctuations in corporate earnings. However, in the early stages of internationalization, MNEs are not yet familiar with the overseas markets they enter. As the uncertainty faced by managers increases, the complexity of decision-making increases, and management costs increase, the risk of overseas operations is increased, offsetting the benefits of diversification.

However, with the accumulation of international experience, MNEs are more and more able to adapt to the economic, political, legal and cultural environment of the host country and reduce the unfamiliar and unfamiliarity with the market of the host country (Beamish, 1988). Johanson & Vahlne (1977) defines international experience as international market knowledge which is a unique resource embedded in the internal human resources of an organization and is an important source of information
about the operation of an enterprise's overseas markets. With experience in overseas markets increasing, MNEs can gain market-specific knowledge, including the structure of the market mechanism, the cultural patterns and the characteristics of the downstream companies. Increased knowledge of MNEs' experience of customers, markets and needs in the host country will confirm opportunities in overseas markets and reduce the risk of developing local markets. Even if the undertaking is not the same or unrelated to the parent company, the overseas subsidiaries may, with experience, know how to re-apply the seemingly unrelated parent company's ownership advantage. MNEs can also increase internal knowledge, such as skills and experience, by promoting and coordinating the flow of knowledge within the organization (Gupta & Govindarajan, 1994), thereby increasing tacit knowledge, enhancing the innovation capacity of MNEs (Subramaniam & Venkatraman, 2001). Accordingly, the following research hypothesis is listed:

H3-2: Even if Taiwanese firms engaged in non-related diversification in China, with the increase of international experience, the China subsidiaries also have better absorbing ownership advantages from Taiwan parent firm so that the effect of locational advantages on these China subsidiaries’ performance are better.

Methodology and methods

In order to obtain the openness and objectivity of the data, this study uses the official database as the empirical data to verify the hypothesis. First, the Taiwan Economic Journal (TEJ) database provides basic information on Taiwan-listed and OTC companies as well as various public financial statements such as research and development (R&D) expenditures, advertising and promotional expenses, total assets and net sales, Business investment in the China subsidiary of the operating details of the situation, such as business projects, such as operating profit margins. Second, the official China Statistical Yearbook of the China contains information on the socio-economic characteristics of the provinces and municipalities directly under the central government. The China Electricity Yearbook provides information on electricity production statistics and the preferential policies on foreign investment provided by China's special economic zones.

1. Study the definition of variables

(1) Response Variables: The performance of China subsidiaries

In this study, the financial performance indicators of China subsidiaries of Taiwan firms provided by TEJ database are used to measure the performance of subsidiaries. Variables provided by the database include operating earnings, income before tax margin, earnings per share (EPS), and rate of net income before tax margin (NIBT). Because EPS and NIBRT are more informative and standardization, they are the response variables in this study. The formula for calculating these two indicators in the TEJ Database is as follows:

\[
\text{EPS contribution} = \frac{\text{(NIBT of China subsidiary x shareholding ratio of Taiwan parent company)}}{\text{stock shares of Taiwan parent company}}
\]
NIBT rate = (NIBT of China subsidiary x shareholding ratio of Taiwan parent company) / NIBT of Taiwan parent company

In addition, we convert these two variables into dummy variables. If the data is positive, it is encoded as 1, the data is 0 or the negative value is encoded as 0.

2. Location-specific advantages

According to the type of FDI motive, this study divides the locational advantages into four categories (Wadhwa & Reddy, 2011).

<table>
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<th>Table 2: Types of Locational Advantages</th>
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<tr>
<td>Location-specific Advantage</td>
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<td>Market Advantages</td>
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<td>Resource Advantages</td>
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<td>Strategic Asset Advantages</td>
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(1) Market advantage

In order to seek the motive of the market-oriented FDI, tend to choose a large market size and market growth rate with the market area advantage of the location. The large market size facilitate manufacturers reduce the cost of entry and reach economies of scale. China is often viewed as a huge investment potential for development because of its large population and territory. However, individual spending power is the key factor in determining the size of the market, can form an effective demand. Zhao and Zhu, 2000), local exports (Wadhwa & Reddy, 2011), the average gross domestic product per capita (Wolhwa & Reddy, 2007) Are common market size measure. In addition, the high market growth rate on behalf of the product market is booming, manufacturers should enter early to gain first-mover advantage. Population growth rate and growth rate of income per person and other economic indicators are commonly used proxy variables.

(2) Resource advantages

FDI with resource-based motivations tends to choose labor costs, raw materials or capital as low capital, that is, sites with resource advantages (Dunning, 1993). For example, Taiwan's traditional industries set up factories in Southeast Asia or the China to seek low-cost labor, raw materials and land. According to the theory of classical international division of labor, manufacturers in different regions through the production of FDI, trying to reduce production costs around to achieve the purpose of maximizing profits. Past studies have found that labor costs account for the majority
of firms' operating costs (Bajo-Rubio & Sosvilla-Rivero, 1994). Too high labor costs will affect the profitability of manufacturers, so manufacturers tend to choose a relatively low labor environment to invest (Coughlin et al., 1991; Zhang, 2001). In the past, labor cost per worker was often used as a measure of labor costs, but high salaries may also reflect a higher quality of local labor while producing a better gross output. Therefore, this study increases the rate of change in labor remuneration per employee as a proxy for labor resources.

Investment location of the basic equipment, the better, the more can reduce the logistics cost of the product. Regional infrastructure can include local transport facilities and electrical equipment. In this study, a standardized total index was established based on railway density (Zhang, 2001), highway density (Zhang, 2001), water density (Broadman & Sun, 1997), water supply and power supply (Li, 2004) Measure the quality of basic equipment around, as a proxy variable for equipment resources.

(3) Efficiency advantage

FDI-oriented, efficiency-oriented motives, low barriers to trade choices, free and mobile MNEs inputs and outputs, or high corporate network densities, where external economies are available, with an efficiency advantage. With the aim of economic growth, the China authorities are planning to invest in a variety of special economic zones at the national or provincial level to promote investment in attracting foreign investment. Special Economic Zones (SEZs) are areas in which the China government allows foreign enterprises or individuals and overseas Chinese, Hong Kong and Macao compatriots to carry out investment activities and implement special policies. The special economic zones are Shenzhen, Zhuhai, Shantou, Xiamen and Hainan. Open Coastal Cities Plan the region and focus on building infrastructure to create an investment environment that is world-class in order to attract foreign investment. Both the New and High-tech Industrial Development Zones and the Economic and Technology Development Zones are aimed at creating knowledge-intensive and open conditions, attracting foreign advanced technology and capital, Local R&D capabilities, and to encourage local higher education and business cooperation. Free trade zones (Free Trade Zones) and tax-free zones (Tax Protection Zones) and more in the port, the development of international trade, export processing, bonded warehousing, allowing foreign investment in international trade (Cheng & Stough, 2006; Zhou, Delios, & Yang, 2002). In this study, the number of local special economic zones, as an alternative variable of foreign preferential policies.

In the early stages of Taiwanese businessmen setting up factories in the China, they often had to purchase large quantities of machinery and equipment, raw materials and semi-finished products from Taiwan because of the shortage of local supporting industries, thus driving Taiwan's exports to the China. The higher the volume of imports, the greater the local government's desire for local development to meet foreign investment expectations, thus encouraging local imports. Sun, Tong, & Yu (2002) use the ratio of local imports divided by gross domestic product as proxy variables for the degree of openness of the local government to foreign investment. The higher the degree of opening to the outside world, the more conducive to foreign investment through common management control over local investment activities, such as respectively in the home country and the host country were concentrated in
research and development activities and production activities, to obtain economies of scale.

Taiwan firms may set up factories in China to follow the upstream manufacturers, or industry-related suppliers or customers have moved to China, had to invest in China. After the formation of local manufacturers' cluster networks, newcomers are more likely to have access to high-quality labor, local information, and convenient transportation, leading to positive vendor aggregation (Chen & Chen, 1998). Wei et al. (1999) pointed out that Chinese firms choose to invest heavily in local FDI. Zhang (2001) study also found that manufacturers are more willing to choose the density of the manufacturing sector in the province. Therefore, this study uses the number of local foreign businessmen (logarithmic value) as a measure of the degree of aggregation economy (Hong, 2007).

(4) Strategic asset seeking

Oriented FDI with efficiency, the tendency to choose R&D knowledge, technology and management and other strategic capital is rich, with Gang strategic assets of the location. Human capital comes from the local people's educational level. (Cheng et al., 2002), or the adult literacy rate (He, 2006), which is higher than the number of local scientists or engineers (Cheng and Stough, 2006). More universal and representative. The measurement of R&D capacity is set to the number of patent rights registered in each local year (Sun et al., 2002).

3. Moderators

(1) Technical capacity and marketing capability of parent firms

Firms must have some unique advantages or capabilities to create competitive advantage and thus improve organizational performance, such as vendor-owned technology assets and marketing assets (Delios & Beamish, 1999; Morck & Yeung, 1991). Firms' investment in R & D is the foundation of product value innovation, enabling manufacturers to gain knowledge of the product, enabling it to provide superior products and improve its own manufacturing processes, enabling Firms to better match their customers' (Baily, 1972; Branch, 1974; Tsai & Wang, 2004; McAlister et al., 2007). In addition, by advertising and promotion activities, changing consumer perceptions to create brand value (Aaker, 1996; Keller, 1998), allows manufacturers to differentiate their products in the minds of customers to prevent competitors from imitating competition barriers and creating firm value (Joshi & Hanssens, 2004; Kirmani & Zeithaml, 1993). In this study, we use TEJ database to collect the annual research rate and the advertising expenditure rate of the Taiwanese parent company, that is, the ratio of R&D or advertising expenditure divided by net sales, as the proxy of technological capability and marketing capability respectively.

(2) Diversification

We classify divides international diversification into relevant and unrelated diversification (Mansi and Reeb, 2002; Rosenthal and Sullivan, 1985). The TEJ database is only available for China subsidiaries and does not provide industry classification codes. Therefore, this study uses the content analysis, the China
subsidiary of the business item literally dismantling, calculated with Taiwan business parent company's business project content consistent with the formula is as follows:
Percentage of related diversification = the number of same words in operating items of Parent company’s and subsidiaries / the number of words in operating items of subsidiaries.
For the sake of simplicity, it is assumed that subsidiaries with a percentage greater than 0.3 are set to be related to diversification; and those with a percentage less than 0.3 are non-correlated.

(3) Internationalization experience

The accumulation of international experience and knowledge of local markets in the internationalization process is an important determinant of MNEs' future investment. Johanson & Valne (1977) argues that in the process of internationalization, firms need general knowledge as well as Market-Specific Knowledge. Among them, market-related knowledge is mainly derived from the local market operating experience, not easy to transfer to other FDI locations; and the production of knowledge due to more standardized, it is easier to different locations in the transfer of technology or knowledge. The measure of international experience can be divided into depth and breadth (Ogasavara & Hoshino, 2009). Depth refers to the number of years of experience, such as the number of years of overseas operations; breadth refers to the number of experience, such as the number of product lines or industries, or the number of overseas subsidiaries or overseas investment in the number of countries. However, most of the China subsidiaries in the TEJ database were not in existence for years, so this study only calculates the number of subsidiaries in China for each data year, as the index of China experience of MNEs.

4. Research model

For the sake of clarity, a simplified regression model is presented without adding control variables and explanatory variables that are not expected to have a significant impact. First, under the assumption that only four regional advantages are considered, the regression model is as follows:
Financial Performance = β₀ + β₁Markets + β₂Resources + β₃Efficiency + β₄Strategic Assets
Based on the hypotheses H1-1 ~ H1-4, the regression coefficients (β₁, β₂, β₃, β₄) are expected to be positive. Secondly, under the assumptions of adding two ownership advantages, technical capability (TC) and marketing capability (MC) as moderators in our models, the regression model is as follows:
Financial Performance = β₀ + β₁Markets×MC + β₂Resources×TC + β₃Efficiency×TC + β₄Strategic Assets×TC
According to the hypotheses H2-1 ~ H2-4, the regression coefficients (β₁, β₂, β₃, β₄) are expected to be positive. Then, we also use related diversification (RD) as a moderator as follows:
Financial Performance = β₀ + β₁Markets×RD + β₂Resources×RD + β₃Efficiency×RD + β₄Strategic Assets×RD
According to the hypothesis H3-1, the regression coefficients (β₁, β₂, β₃, β₄) are expected to be positive. If we consider both ownership advantages and related diversification as moderators, then the model is set as follows:
Financial Performance =
\[ \beta_0 + \beta_1 \text{Markets} \times MC \times \text{RD} + \beta_2 \text{Resources} \times TC \times \text{RD} + \beta_3 \text{Efficiency} \times TC \times \text{RD} + \beta_4 \text{Strategic Assets} \times TC \times \text{RD} \]

According to the hypothesis H3-2, the regression coefficients (\(\beta_1, \beta_2, \beta_3, \beta_4\)) are expected to be positive. At last, we add international experience (IE) of MNEs as moderators as follows:

Financial Performance =
\[ \beta_0 + \beta_1 \text{Markets} \times MC \times \text{RD} \times IE + \beta_2 \text{Resources} \times TC \times \text{RD} \times IE + \beta_3 \text{Efficiency} \times TC \times \text{RD} \times IE + \beta_4 \text{Strategic Assets} \times TC \times \text{RD} \times IE \]

According to the hypothesis H3-3, the regression coefficients (\(\beta_1, \beta_2, \beta_3, \beta_4\)) are expected to be negative.

**Discussion**

First, the results show all four kinds of location specific advantages partly have positive effects on China subsidiaries’ performance, which means H1 is partly supported. Second, only marketing capacity of Taiwan firms is successfully transferred to China subsidiaries which take advantage of income of local consumers better to generate more EPS contribution. So, H2 is also partly supported. Third, the results also show both the similarity of operating items between parent companies and subsidiaries (related diversification) and accumulated FDI experience in China make marketing capacity be better transferred from parent companies to subsidiaries so the income of local consumers have more positive effects on EPS contribution of subsidiaries. Therefore, H3-1 and H3-2 are also partly supported.

<table>
<thead>
<tr>
<th>Table 3: Types of Locational Advantages</th>
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<td><strong>m = market seeking</strong></td>
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<td>----------------------------------------</td>
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<tr>
<td><strong>H1</strong></td>
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<tr>
<td><strong>m ln(income)</strong></td>
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<tr>
<td><strong>m ln(population)</strong></td>
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<td><strong>m natral growth rate</strong></td>
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<td><strong>r traffic convenience</strong></td>
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<td><strong>r ln(water usage)</strong></td>
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<td><strong>e ln(# of foreign firms)</strong></td>
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<td><strong>e consumer price index</strong></td>
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<td><strong>s rate of first quality</strong></td>
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<tr>
<td><strong>m ln(income) X marketing capacity</strong></td>
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<td><strong>m growth rate X marketing capacity</strong></td>
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<td><strong>r traffic density X R&amp;D capacity</strong></td>
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<td><strong>s rate first quality X R&amp;D capacity</strong></td>
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<td><strong>constant</strong></td>
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<td><strong>Number of observations</strong></td>
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<td><strong>Number of subsidiaries</strong></td>
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References


