

This version: August 30, 2016

**Words vs. actions:  
International variation in the propensity to honor investment pledges in China**

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**ABSTRACT**

We examine whether companies from certain countries are more likely to honor investment pledges. Using data on contracted and utilized FDI in China, we find that firms honor an average of 59% of their pledges within two years. The propensity to honor pledges is lower for firms from countries with greater uncertainty avoidance, power distance, and egalitarianism; higher if the source country is more traditional; and is unaffected by popular attitudes towards China. Prior literature has found that these cultural characteristics are associated with higher levels of utilized FDI. We extend this to show that announcements of planned corporate activity may be more reliable for firms from countries with certain cultures.

JEL Code: F21, F23, G18, G31, Z13

Keywords: foreign direct investment (FDI); China; culture; institutions; policy

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Hornstein thanks Chi Lo for market insights and assistance with data; seminar participants at University of Connecticut, Wesleyan University, John Bonin, Joyce Jacobsen, David Kuenzel, Kanda Nadnoi, Elif Sisli Ciamarra and Minyuan Zhao for helpful comments; Tianyu (Rain) Xie, Raymond Wong and Christopher N. Nanda for excellent research assistance; and the Wesleyan University Quantitative Assistance Center for financial support. Hornstein conducted part of this work while visiting New York University's Stern School of Business. All errors remain our own.

## 1. Introduction

Firms often announce large investments publicly well before actual capital flows occur. As a result of this time lag, the monetary values of proposed and actual investments may differ non-trivially due to information received in the interim, or the belief that an investor is not bound by prior pledges. For example, we find that in China just 59% of all investment pledges are fulfilled in the same or following calendar years. Economic transactions involve elements of trust (Arrow, 1972) and trust can increase levels of foreign direct investment (FDI) and trade (Guiso et al., 2004). Trust is considered to be one of many elements of culture, and cultural characteristics such as egalitarianism also increase FDI flows (Siegel et al., 2011, 2012). Thus, we examine whether the propensity to honor investment pledges is related to national culture using data on contracted and utilized FDI flows into China.<sup>1</sup>

The propensity of investors to pre-announce investment plans has been studied previously through a focus on the *speed* with which investment pledges would be fulfilled. We explore a new dimension of this question by focusing on the *degree* to which investment pledges are fulfilled. Thus, we build upon the growing body of knowledge that national culture affects corporate activity through the managerial decision-making channels (Li et al., 2013) and FDI (Siegel et al., 2011, 2012). Roughly two-thirds of cross-border FDI occurs via mergers and acquisitions (Head and Ries, 2008), and the volume of cross-border mergers is inversely related to cultural distance between source and host countries (Ahern et al., 2015). Corporations from countries with

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<sup>1</sup> Since all investments examined in this paper are in China, the phrases “national culture”, “home country culture”, and cultural distance are used interchangeably. We note that this is in slight contrast to some of the papers we reference that use data for cross-border activities world-wide, and thus do not have a common base country.

higher levels of uncertainty avoidance hold more cash for precautionary purposes and make lower levels of corporate expenditures, acquisitions, and repurchases (Chen et al., 2015). These arguments suggest that cultural characteristics might systematically affect the propensity of investors from a country to honor investment pledges.

By examining only firms engaging in cross-border investments, we situate our analysis of the impact of culture on corporate activity in the context of FDI. The impact of national culture on bilateral FDI inflows has been studied previously in two different ways. First, the literature on FDI determinants has focused on common cultural values (Siegel et al., 2011 and 2012), and on the impact of coethnic trade and investment networks (Huang et al., 2013; Tong, 2005). Second, the corporate finance literature has examined how national culture affects corporate actions in general, oftentimes proxied by managerial decisions (e.g., Chen et al., 2015). Both literatures share a commonality in that they examine how national characteristics affect observed levels of investment.

We look one step earlier at pledged levels of investment to ascertain if ex post observed levels of investment (i.e., utilized FDI) are systematically related to ex ante pledged investment levels (i.e., contracted FDI). China is the only country that receives significant FDI inflows and systematically collects and, until 2005, released data on pledged levels of FDI.<sup>2</sup> We therefore examine this question in the China context as there is variation in the levels of contracted and utilized FDI received from different source countries. Moreover, throughout this period China was one of the largest recipients of FDI worldwide. We are thus able to reconcile the two literatures by proposing an

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<sup>2</sup> To the best of our knowledge, the only other countries that regularly collect and release some data on pledged FDI are Cambodia, India, Laos, the Philippines, Thailand, and Vietnam.

explanation for how national culture affects bilateral FDI flows: culture creates variation in the degree to which firms are expected to honor promises made previously.

The national culture of the source country may have different effects on the levels of pledged and actual FDI, particularly in the case of China. First, firms from countries with higher levels of uncertainty avoidance have higher levels of corporate cash holding due to precautionary motivation (Chen et al., 2015). Similarly, when the source country has a higher level of uncertainty avoidance, firms are significantly less likely to undertake risky actions (Li et al., 2013). As a result these firms may find it easier in general to make investments due to a reduced need to acquire external funding and yet have a preference to invest in better understood opportunities that may present reduced levels of risk through the presence of fewer unknowns. This would be consistent with the finding that firms are more likely to invest in locations that are more culturally familiar (Du et al., 2008, 2012) and where local partners are considered more trustworthy (Ang et al., 2015). These arguments suggest that home country cultural characteristics should have similar effects on both contracted and utilized FDI. This effect may be moderated, however, by the presence of shared linguistic ties (e.g., local usage of Chinese characters) or by popular sentiment towards China as China's role in the world economy has changed markedly, in reality and in perception, over the period studied herein.

Second, FDI flows reflect national aggregation of data generated by firm level activities. Whether firms make and fulfil investment pledges reflects managerial decision-making and is related to, but may be separate from, how the firm finances growth through usage of the external and internal capital markets. Glaser et al. (2013) show that multinational conglomerates do not always invest as planned due to managerial

hubris that generates investment inefficiencies. The Glaser et al. findings complement and extend the earlier findings of Wurgler (2000) that there is substantial variation in the efficiency of capital allocation across industries within countries.

Third, the Chinese data on contracted and utilized FDI represent national level analogues to the firm level data studied by Glaser et al. (2013). China requires many foreign investors to receive government approval for investments, and the government has thus long compiled data on contracted, or pledged, FDI. Utilized FDI data are verifiable as they represent cross-border capital flows and would therefore be visible on the national accounts of the host and source countries. In addition, until December 2005, the Ministry of Commerce reported monthly on the levels of contracted FDI. As the central Chinese government granted policy incentives to provinces based on the levels of pledged investments, it is possible that the announced values of contracted FDI were artificially inflated in response to local government officials' incentives (US-China Business Council, 2006). Alternatively, it is possible that that firms from certain source countries were more inclined to inflate investment pledges in order to extract greater rents from local government officials.

A source country's national culture might affect the willingness of firms to even consider investments in a particular country or the likelihood that a project might receive government approval. This is consistent with the prior findings that companies from source countries that are more culturally distant from China are more likely to invest only in parts of China with stronger economic institutions (Du et al., 2008, 2012; Ang et al., 2015). In order to examine whether cultural characteristics affect the propensity to fulfil pledged investments, we conduct empirical tests using a gravity model of international

trade to examine the impact of source country culture upon FDI. Since firms value quick fulfilment of investment pledges (Hawk et al., 2013), the propensity of firms from a country to honor their investment pledges can be proxied by use of the UC ratio, as developed by Hornstein (2011), and renamed the commitment ratio herein. The commitment ratio is the ratio of the level of utilized FDI in a year to the average value of contracted FDI announced in the current and prior years.

While the average country-year level of contracted FDI was \$186 mn and the average country-year level of utilized FDI was \$131 mn, on average just 59% of all investment pledges were fulfilled within two calendar years. We find that the commitment ratio is lower when the source country has greater uncertainty avoidance, although this effect is mitigated by the extent of past FDI into China. There is limited evidence that the commitment ratio may be lower for some countries with higher power distance indexes. The uncertainty avoidance and power distance data are obtained from Hofstede (2010). For robustness, an alternate measure of cross-country cultural values is used, the Schwartz Values Survey, to capture social, non-business culture. Local attitudes towards China, as captured by public opinion polls, are unrelated to the commitment ratio. Finally, our event study analysis shows that the commitment ratio was higher for Asian countries during the Asian financial crisis, and world-wide after China joined the WTO. These results show consistently that the commitment ratio is affected by home country cultural values.

We continue with a discussion in Section 2 of FDI and why variation is observed in the propensity to honor FDI commitments. How home country cultural and population characteristics might affect corporations honoring investment commitments are presented

in Section 3. Our data are presented in Section 4. In Section 5 we discuss empirical results from analysis of the commitment ratio. Finally, Section 6 concludes.

## **2. Foreign direct investment**

Companies routinely disclose skeletal details of planned investments ahead of time, particularly if the projects are large in value, might alter the firm's identity, or are in new locations. However, these ex ante announcements often are minimal in scope, covering location and general purpose of an investment, and thus often do not receive considerable attention.<sup>3</sup> As corporate announcements are not standardized, and firms may make disclosures at any step in the process, it is generally not possible for outsiders to track how actual and planned expenses compare within a firm.

Analysis of corporate investments generally proceeds in one of two ways: using ex post data at the firm-year level to identify how a firm invested, or using aggregated annual data at the country-year level to identify trends in total domestic or foreign investment. We follow a third path using FDI data from China as China has long collected data on contracted, or pledged, FDI. Our dataset permits us to accomplish two goals that we think are new to the literature on corporate investments. First, we document cross-country variation in the degree to which investment pledges are fulfilled; and second, we show that home country culture affects the observed investment patterns.

### **2.1 FDI in China**

Foreign investors in China are routinely required to obtain government approval for investments, although the regulations have been relaxed over the years. When a

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<sup>3</sup> There are exceptions such as the July 2014 Volkswagen announcement of a \$900mn investment in the U.S., which received considerable media attention (Boston and White, 2014).

project receives government approval, an anticipated monetary value is associated with the project. This is known as the ‘contracted value’ as it represents the monetary value that is stated in the relevant contracts or memorandums of understanding. Contracted FDI flows represent the total of all future expected cash flows associated with all investment projects funded by companies from the source country in all subsequent time periods. Contracted FDI has long been tracked carefully by various government agencies within China at both national and local levels. Contracted flows represent promised or planned investments that receive government approval in a calendar period.<sup>4</sup> By contrast, utilized FDI is the total of all actual cash flows associated with all investment projects from a source country in a calendar period. Both contracted and utilized FDI flows can be positive or negative depending on whether inflows exceed outflows.<sup>5</sup>

Until 2005 the Chinese central government released data on contracted and utilized FDI on a monthly basis, and routinely provided break-downs by source country and by destination within China. Many of the individual provinces and municipalities also reported this data. As of 2005, the central government stopped releasing this data even as the provinces and municipalities continued to release this data, albeit not on a

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<sup>4</sup> Although the Chinese government required advance approval from foreign investors prior to market entry, there were no penalties for firms that didn’t fulfil their commitments. These firms might face reputational problems that could affect future investment plans as local counterparts, particularly government authorities, might discount their credibility in subsequent periods.

<sup>5</sup> Contracted FDI could be negative if companies pre-announce plans to repatriate funds, and the total monetary value of such plans exceeds the value of planned investments announced during the same period. Similarly, utilized FDI could be negative if companies repatriate, or transfer out of the country, more funds than they invest in that same period. If quarterly FDI data are examined, a non-trivial number of country-quarter observations would have a negative value for contracted FDI. However, when we use annual FDI flows, net inflows almost always greatly exceed net outflows. While we use the terms “contracted FDI” and “utilized FDI” throughout this paper, they consistently are referencing net values as we do not have data only on inflows.



consistent basis.<sup>6</sup> The data that is used in this paper was obtained at a source country – calendar quarter level, with no information regarding the individual firms or projects.<sup>7</sup>

Contracted and utilized levels of FDI might differ for four reasons. First, in the interval between announcing and fulfilling investment plans, firms may acquire additional knowledge about the host country. For example, some managers may have cultural knowledge or intelligence that is not portable to new countries or environments (Earley and Mosakowski, 2004), which would cause their employers to make less effective investment estimates ex ante for more culturally distant locations. This would suggest social or business culture characteristics of the home country may explain variation in fulfilling investment pledges abroad.

Second, investors may believe their announced levels of FDI can serve as a bargaining chip to extract concessions from local governments such as a tax holiday or access to foreign exchange quotas (US-China Business Council, 2006). These firms might alter the final value of their investment later, possibly as a result of whether the concessions granted were in line with expectations. This would be consistent with a belief that legal regulations governing FDI and tax codes are a framework for negotiations and not a formal, fixed structure.

Third, it is possible that the firm has changed its world-wide strategy and thus has decided to complete a fraction of previously announced investments. Alternatively, a firm's investments may systematically differ from what is planned because the firm does

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<sup>6</sup> The data is analyzed herein at the source country-year level as other variables are available only at the annual level. We note that China's Ministry of Commerce continues to issue news releases that reference current values of utilized and contracted FDI data at the source country-month-province level (MOFCOM, 2015).

<sup>7</sup> Accordingly, it is not possible to test for whether firms are engaging in repeat transactions, and thus learning from their own past experiences in China.

not feel it is necessary to honor its commitments. If firms differ idiosyncratically in their propensity to honor investment contracts, then there would be no coordinated effect on all firms from a country. However, if this is common among firms from a single source country, then it could be a reflection on the source country's culture.

Finally, firms may fully honor the foreign currency value of investment pledges. However, the nominal US dollar value of the investment may appear to have changed due to intertemporal changes in the exchange rates causing a gap to emerge between the contracted and utilized values of FDI.

## **2.2 Propensity to honor FDI commitments**

If investors consistently implement investment plans as anticipated, then contracted and utilized FDI flows would be perfectly correlated, albeit with a potential time lag.<sup>8</sup> Similarly, if investors *on average* make similar adjustments to their plans after initial announcement, then contracted and utilized FDI inflows would remain perfectly correlated although they would differ in value. If investors vary in the degree to which they modify investment plans after announcements, then the contracted and utilized FDI values may vary in an unpredictable fashion. Consistent with real option theory, firms may announce investments in order to send public signals to competitors or authorities with no intention of fully honoring these public signals. Characteristics of the firm's management might thus be related to the likelihood that the firm carries out its investments as planned. As corporate leaders are shaped by their home country culture

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<sup>8</sup> In the absence of data on the average time gap between announcements of contracted FDI pledges and fulfilment, we follow the lead of Hornstein (2011) and assume pledges are likely to be fulfilled within the same or subsequent calendar year.

(Pan et al., 2014), we would then expect that home country culture may affect the propensity of investors from that country to honor their word.

The ratio of utilized to contracted FDI flows, the *UC* ratio, captures the relationship between utilized FDI flows and the previously announced contracted FDI flows, as introduced by Hornstein (2011). We interpret Hornstein's *UC* ratio as a proxy for the national average propensity to honor commitments and henceforth we refer to the *UC* ratio as the "commitment ratio". The utilized and contracted FDI flows may be observed contemporaneously if pledged FDI is delivered within the same calendar year. However, it is possible that some investments occur over a longer horizon, and it is probable that investments announced at year-end are not fulfilled that same calendar year. Accordingly, Hornstein (2011) modeled the *UC* ratio as the ratio of utilized FDI in a calendar year to the average value of contracted FDI in the preceding and contemporaneous calendar years, and we follow this framework.

The growing literature on determinants of project profitability informs that profitability is negatively affected by the length of time to fully set up a project except when there is real option value to delaying onset of investments (Hawk et al., 2013). Given the intensity of competition in all sectors in China, and the rapid rate of economic development, the real option value of delaying investments may be low in China. On the other hand, accelerating the pace of investments also increases the cost of such investments (Pacheco-de-Almeida et al., 2012). The growing mass of evidence regarding increasingly fast project establishment time lines in different industries world-wide suggests that firms are cognizant of these advantages and try to fulfill investment pledges as quickly as possible.

More important or powerful managers are most likely to increase investments when resources are available even as their investments are generally less efficient than the investments made by other managers (Glaser et al., 2013). Given the rising importance of China in the global economy, multinationals are increasingly placing better connected individuals in charge of their China operations. Thus, it is probable that pledged corporate investments in China are more likely to be fulfilled than planned corporate investments elsewhere. If this is true, it could lead to an upward bias in the estimated commitment ratio but measurement error in our dependent variable would not lead to biased coefficient estimates.

Whether culture affects the propensity of firms to honor their pledges is a precursor to many of the corporate governance questions that presume incentives can motivate managers to make the 'right' decisions. Here we are able to understand how culture can shape corporations' beliefs that decisions can be altered ex post to fit preferences. The actual size and timing of investments are decided by corporate executives who may have personal interests that are imperfectly aligned with those of their employer. If this is a greater problem in some countries, then it is reasonable to expect investments, both planned and actual, could be used to enable managerial entrenchment (Jensen, 1986; Shleifer and Vishny, 1989; and Morck and Yeung, 1992). This could lead to an upward bias in the commitment ratio through increased correlation of contracted and utilized FDI. Managerial career concerns may lead to pledged investments being implemented more quickly (Narayanan, 1985; Stein, 1989) or delayed longer than optimal (Grenadier and Wang, 2005). This could lead to a bias, upward or

downward, in the commitment ratio. Corporate executives world-wide may well face career and agency concerns such as these.

Similarly, Wurgler (2000) shows that there are profound and sustained differences in productivity across countries. More productive firms become multinationals (Raff et al., 2012), and multinational enterprises invest more efficiently (Greene et al., 2009). Thus, home country culture may affect the productivity of a firm and the pattern of the firm's subsequent investments. When firms from multiple countries invest side-by-side in a common destination, there may be profound and persistent source country effects on their investments. Thus, we will examine how the propensity to honor investment pledges varies across countries.

### **3. Cultural variation in propensity to honor commitments**

The core principles that unite a country are systems of values and beliefs that infuse the formal legal and political structures and the informal practices that evolve to supplement them (North, 1990; Williamson, 2000). These principles generate the first definition of what is commonly called culture by stressing the role of beliefs. The second definition of culture stresses the role of individuals' values and preferences in shaping decision-making rules that lead to the evolution of institutions (see Alesina and Giuliano (2015) for a detailed overview). These approaches are complementary as beliefs and preferences may evolve jointly (Alesina and Giuliano, 2015). Similarly, Guiso et al. (2006) define culture as “those customary beliefs and values that ethnic, religious, and social groups transmit fairly unchanged from generation to generation”.

Culture affects how individuals and firms operate, in particular how willing they are to assume risk and make potentially irrevocable decisions. For example, at one extreme individuals might seek out opportunities to interact primarily with similar individuals. A common example of this is the rise of coethnic trade and investment networks such as among overseas Chinese (Huang et al., 2013) or Gujarati Indians in the U.S. (Kalnins and Chung, 2006). Alternatively, individuals and firms may self-select into, and away from, different types of opportunities. Thus, companies from some countries might make similar investments in certain locales. For example, linguistic and cultural ties have led Hong Kong firms to dominate in Guangdong province while Taiwanese firms dominate in Fujian province. A growing literature has found that cultural connections explain the volume of foreign trade and investment flows (e.g., Rauch and Trindade, 2002; Siegel et al., 2011, 2012; Tong, 2005; etc.). One unresolved question is the extent to which culture affects these flows. To test for a causal link between culture and corporate activity, we follow the lead of Guiso et al. (2006) and focus primarily on those aspects of culture that appear to be time invariant (i.e., can be inherited from prior generations).

We distinguish between time invariant measures of culture such as those based on beliefs, discussed in Section 3.1, and time varying measures of culture such as changes in popular attitudes, discussed in Section 3.2. These measures of culture may be affected by the presence of shared linguistic ties, discussed in Section 3.3.

### **3.1 Cultural measures**

Specific components of home country culture that influence corporate behavior have been identified. For example, egalitarianism increases FDI (Siegel et al., 2011,

2012), individualism and uncertainty avoidance are associated with higher corporate cash holdings and lower levels of corporate expenditures (Chen et al., 2015), and trustworthiness affects choice of investment locations (Ang et al., 2015). Similarly, cultural distance also affects the quality of these actions. For example, Ahern et al. (2015) show that cross-border M&A announcement returns are lower for firms from more culturally distant countries while Shi and Tang (2015) present a domestic U.S. analogue with cultural distance measured using religious and ethnic similarities. Pan et al. (2014) find that CEOs corporate behavior is consistent with the cultural values embedded in their ethnic heritage, thus confirming that culture may be time invariant. These papers are part of a growing literature on cultural distance and economic activity that uses cross-country surveys on attitudes to capture elements of cultural beliefs.<sup>9</sup>

The earliest set of international surveys of cultural values that is widely used in this research area was first conducted by Hofstede in the 1960s and gradually updated and expanded to cover a larger number of countries. Hofstede's cross-country studies reveal that there is considerable international variation in cultural values among managers at large corporations worldwide. These individuals have a 'cultural sensitivity' that reflects their nationality and their work environment. More recently, the Schwartz Values Survey asked a common set of questions about beliefs to roughly 15,000 individuals world-wide in 2004. These two sets of surveys give complementary insights into the presence and variation of cultural values world-wide and thus how individuals in a country might view potential investments and vary in their propensity to honor

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<sup>9</sup> See Zingales (2015) for a thorough review.

commitments. The Hofstede measures are generally used to capture corporate culture while the Schwartz Values Survey are used as measures of social culture.

First, we begin with corporate culture to capture the mindset of managers who may be making the decisions regarding overseas investments. The FDI data we use represent multiple investment decisions made by managers at different corporations. Thus, we rely primarily upon the Hofstede measures as corporations are micro-societies with unique cultures (Guiso et al., 2015). We examine two of the Hofstede measures that capture values which might influence how individuals plan investments and the propensity of these individuals to honor subsequently their pledges: uncertainty avoidance and power distance.

Individuals vary in their willingness to tolerate unanticipated outcomes and their desire to ensure harmony by maintaining the status quo. Hofstede calls this phenomena “uncertainty avoidance”. Uncertainty avoidance is “the extent to which the members of a culture feel threatened by ambiguous or unknown situations” (Hofstede et al., 2010, 191). Uncertainty avoidance is distinct from risk avoidance as risk can be quantified whereas uncertainty cannot.<sup>10</sup> Countries with a higher degree of uncertainty avoidance have a lower tolerance for ambiguous situations and a clear preference for rules and order and a greater synchronicity of interests. Uncertainty avoidance is negatively associated with corporate risk taking (Li et al., 2013; Mihet, 2013) and capital expenditures and acquisitions (Chen et al., 2015), which would be consistent with companies engaging in more due diligence prior to announcing investments. As corporate cash holdings are

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<sup>10</sup> Risk avoidance is intrinsic to investment planning and would already be embedded in the values announced for contracted and utilized FDI. Uncertainty avoidance, on the other hand, affects whether investors would even announce the contracted plans and/or fulfill the pledges later (i.e., the utilized FDI).



positively associated with uncertainty avoidance (Chen et al., 2015), companies from countries with higher uncertainty avoidance would be able to honor investment pledges more easily. Cultures that have low uncertainty avoidance display a greater degree of innovation and exploration of new situations (Mihet, 2013; Shane, 1992).

The contracted FDI data may be more accurately estimated when the source country has more uncertainty avoidance, leading to a higher commitment ratio. However, the commitment ratio may be lower when the country has higher uncertainty avoidance as these firms are more likely to simply not enter a new market even if they have committed publicly to doing so. Thus, it is not clear how the commitment ratio will be systematically affected by the uncertainty avoidance of the source country.

Alternatively, firms may set expectations for the operating environment based on the structure and operation of the government in their home country. That is, if firms are from countries where members of a society accept and expect that power will be distributed unequally, then they may believe that they have the ability to negotiate with other governments to extract valuable concessions that may not be available to all investors. This concept is known as the power distance index as per Hofstede (2010). Countries with high degrees of power distance are more hierarchical while countries with low degrees of power distance are more egalitarian. Investors from countries with high degrees of power distance may thus make strategic announcements in the hope of gaining additional concessions from a government prior to actually fulfilling these investments. On the other hand, firms from countries with higher power distance may be more likely to honor investment pledges in order to increase their potential bargaining power in

subsequent periods. We thus conclude that it is unclear whether the commitment ratio and power distance index would be positively or negatively related.

We also use the Schwartz Values Survey as the managers who make foreign investment decisions may be influenced by broader popular culture. The Schwartz Values Survey measures of egalitarianism, traditionalism, and harmony to capture aspects of how individuals may behave in business relationships. These data were collected from surveys administered to over 15,000 urban K-12 teachers in 55 countries in 2005. We look at popular culture as managers are raised by communities made up of individuals. If individuals believe they have a responsibility to treat others fairly and that all people should be treated similarly, then the society may be more egalitarian (Siegel et al., 2011, 2012). In such a society, individuals may be particularly cognizant of their dependencies upon others, and thus be more inclined to honor personal commitments. In egalitarian societies there is lower tolerance of individuals or organizations that abuse their power, whether it is market- or political-based.

By contrast, the concept most diametrically different from egalitarianism is hierarchy, which represents a society in which there is an unequal power structure and resource allocation. Egalitarianism and hierarchy share a common assumption that how individuals act towards one another would be constant across times and settings. Siegel et al. (2011 and 2012) show that more dissimilar levels of egalitarianism in a pair of countries is associated with lower levels of bilateral FDI. We thus hypothesize that the absolute level of egalitarianism in a society may be indicative of local firms' propensity to honor commitments elsewhere.

We also use the Schwartz Values Survey data on the concepts of traditionalism and harmony. Traditionalism is a preference for what has been done previously or the extent to which things are done because they are customary, and thus serves as a proxy for the degree to which change can cause discomfort. A preference for traditionalism may make firms from a country less likely to honor pledges unless they have previous experience investing in China. Finally, the concept of harmony captures the idea that groups and individuals should fit together peacefully, and avoid change and acrimony. Thus, a preference for harmony may lead firms from a country to make more accurate investment pledges and thus be more likely to honor commitments.

### **3.2 Attitude towards China**

If citizens of a country have a generally positive attitude towards China then firms from that country may treat Chinese counterparts more respectfully, and thus have a greater propensity to honor agreements made with Chinese counterparts. While the fraction of a country's population that is ethnic Chinese could proxy for the extent to which that country has positive attitudes towards China, this may be a biased estimator of positive sentiment. After all, ethnic Chinese citizens of a country may have less positive attitudes towards China than individuals who are not ethnic Chinese. Accordingly, Desmet et al. (2015) argue that ethnic and cultural diversity are unrelated. We therefore use popular sentiment to proxy for business attitudes towards China.

Citizens of many countries are routinely surveyed on many questions, including attitudes towards specific countries or issues. The Pew Global Attitudes Project routinely examines popular attitudes towards China. These surveys reveal considerable variation in how members of different countries view China and show that these attitudes vary over

time.<sup>11</sup> Our hypothesis is thus that the tone of popular attitudes towards China may affect the composition of FDI to China, and the propensity of local investors to honor commitments made in China. We note, however, that one limitation of using nationally aggregated data on popular sentiment is that it may mask domestic variation in attitudes towards China. For example, Che et al. (2015) show that Japanese firms are less likely to invest in the parts of China that were most affected by the Japanese invasion from 1937-1945. Thus, these attitudes would be reasonable proxies of domestic investor attitudes towards China if the sample population captured by the Pew surveys is representative of the population of corporate decision makers.

### **3.3 Linguistic ties**

Economic theory generally posits that ethnic ties enable relationships to develop more quickly and more deeply through more efficient transmission and creation of trust between individuals. The emphasis on ethnic ties is related to the sociological concept of ‘social capital’, which captures the idea that individuals who share a common community may have a higher common degree of trust and willingness to share resources. Ethnicity is associated with the provision of trade credit in developing countries (Fisman and Love, 2003), longer-term financial contracts (Guiso et al., 2004), international technology diffusion (Kerr, 2008), and with the global presence of firms (Foley and Kerr, 2011). The impact of ethnic ties has been examined in single-country studies such as that of Guiso et al. (2004) who look at intra-Italian links, Kalnins and Chung (2006) who examine the Gujarati population in the U.S., and Huang et al. (2013) who look at

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<sup>11</sup> In a similar vein, it is possible that Chinese routinely stereotype foreigners and thus make certain foreign investors feel more or less welcome in China. While this may occur, it is not possible to identify a standardized source of such data, and thus domestic attitudes are excluded from our analysis.

overseas Chinese investors in China, and also in the cross-country context by others such as Fisman and Love (2003).

Huang et al. (2013) show that overseas Chinese are more inclined to invest in China, and that this happens even when the overseas Chinese companies are less productive *ex ante*.<sup>12</sup> Because of their lower productivity ahead of time, the overseas Chinese-invested firms subsequently under-perform compared to those firms established by foreign investors who are not ethnically Chinese.<sup>13</sup> On the other hand, the beneficial effects of social capital due to shared ethnic ties is most profound for individuals with fewer resources (Kalnins and Chung, 2006). Thus, even as these overseas Chinese investors appear to create weaker investments in China, these investments may still be more successful than if these firms had instead invested in other countries.

Due to the presence of a large Chinese population worldwide, Chinese characters are routinely used in written communications in many countries (e.g., Japan). Investors from countries where Chinese characters are routinely used may exhibit a greater degree of comfort in China than investors from countries where Chinese characters are never, or almost never used in business (e.g., United States). We therefore use a Chinese character dummy variable to proxy for linguistic ties between the source country and China. We argue that investors from countries that use Chinese characters may make more informed investment estimates, as reflected in the contracted FDI data, and may feel a higher

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<sup>12</sup> While this phenomenon involves true FDI from abroad, we will later address a related concern: round-tripping whereby Chinese individuals or businesses send monies overseas that is then invested in China as “foreign” investment.

<sup>13</sup> This is reinforced by earlier findings presented in Tong (2005). This may also be related to a familiarity bias whereby overseas investors flock to the areas of China they know best. For example, Fujianese dominate the Taiwanese population, and Taiwan is the largest foreign investor in Fujian province.

comfort with fulfilling a greater proportion of these investments, as reflected in the utilized FDI data, and thus have a higher propensity to honor commitments.

#### **4. Foreign direct investment data and variable construction**

##### **4.1 Foreign direct investment data**

The key variables used in our analysis are the contracted and utilized FDI data reported by the Chinese government and obtained from the CEIC database. The utilized FDI data are available for 1995-2013 while the contracted FDI data are available for only 1994-2005. Accordingly, our key dependent variable, the commitment ratio, can be estimated for only 1995-2006.

While the FDI data is available at the quarterly basis, all other variables used in the analysis are available only at an annual basis. The quarterly FDI data reveal considerable variation with regards to the timing of investment pledges and fulfillments. First, we note that there does not appear to be a seasonal pattern to the data. That is important as it implies companies are making investment plans and fulfilling them in response to corporate needs, and not in response to artificial deadlines induced by calendars. Second, when we examine the quarterly utilized FDI data, there are many quarters in which a source country has net utilized FDI that is negative due to capital repatriation in that quarter.<sup>14</sup> The countries that have negative utilized FDI in calendar quarters are countries with low effective tax rates. Desai et al. (2007) show that firms are more likely to repatriate capital when the effective tax rate is higher abroad.

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<sup>14</sup> Note that if the planned repatriations are announced ahead of time, it is theoretically possible for contracted FDI to be negative in a quarter.

On the other hand, when we use the annual data we find that the utilized FDI data are non-negative for all source countries. In addition, when we rely upon the annual data then the possibility that a set of FDI projects were announced concurrently is removed from the data.<sup>15</sup> Moreover, by using annual data we do not need to worry about seasonal spikes such as a rush to complete deals before the end of a fiscal or calendar year, or distortions caused by the timing of Chinese New Year.

We report in Table 1 the summary statistics for our dataset in log form. Utilized FDI varies markedly over time, ranging from a minimum value of \$0 mn to \$73.4 bn, and contracted FDI varies even more markedly from -\$8.80 mn to \$75.2 bn. We show in Figure 1 six representative countries as there are three general patterns observed in the data. First, in some countries such as Japan and the United States contracted FDI appears to accurately forecast subsequent utilized FDI; second, in countries such as Canada and Malaysia we see contracted FDI consistently exceeds utilized FDI; and finally, in countries such as Sweden and Vietnam there appears to be no clear patterns in contracted or utilized FDI.

## **4.2 Commitment ratio**

The commitment ratio is based on the province-year level measure called the *UC* ratio, which was introduced by Hornstein (2011). This formulation is modified slightly to reflect our focus at the country-year, not province-year, level, and is also renamed the “commitment ratio”. The commitment ratio proxies for whether and how quickly investors from a source country honor their investment commitments. The concept of commitment is measured as

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<sup>15</sup> This often happens when government officials such as Ministers or Secretaries of Commerce visit China or host a delegation from China

$$Commitment_{c,t} = \frac{U_{c,t}}{\frac{1}{2}(C_{c,t} + C_{c,t-1})}, \quad [1]$$

where  $U_{c,t}$  and  $C_{c,t}$  are the utilized and contracted FDI flows, respectively, from source country  $c$  in year  $t$ .

While conventional theory long held that firms would gradually expand internationally as they learned from prior experience, firms are now increasingly likely to move quickly when expanding internationally. Firms move quickly to reach their optimal scale of production and also to create or overcome barriers to entry (Chang and Rhee, 2011). Firms with shorter time to build their new facilities or complete investment plans subsequently post higher performance metrics and achieve higher market valuations (Salomon and Martin, 2008; Hawk et al., 2010). We follow the lead of Hornstein (2011) and use the average of the preceding and current year values of contracted FDI in the denominator of the commitment ratio.<sup>16</sup> This accommodates calendar induced year-end spikes in the data, and allows for the possibility that firms fulfil investments gradually over a fiscal year, which may not correspond to the calendar year.

Our commitment ratio would have an average value of 1.0 if firms fully honored their investment pledges. Instead we report in Table 1 that the average value is 0.595, with a standard deviation of 0.517. The minimum value is -0.808 and the maximum observed value is 8.071. However, in empirical analyses we restrict the sample to country-year observations where the estimated commitment ratio is in the range of 0 to 4. This range was selected to mitigate the effect of larger, lumpier projects that are announced rarely, and to minimize the number of excluded observations (10 in total).

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<sup>16</sup> Hornstein (2011) showed that alternative constructions of this ratio employing up to three years of data in the numerator and/or denominator were all highly correlated. We obtained similar results with this dataset.



We observe that on average most firms over-state the value of their future investments, leading to a mismatch between contracted and utilized FDI data. This is illustrated in Figure 2 where we show the variation in the commitment ratio for the same representative six countries shown in Figure 1.

### **4.3 Impact of past FDI**

Due to the prevalence of co-location of compatriot firms in foreign countries, and the spillovers that can occur from the existence of similar firms in a host location, we need to control for the past FDI flows from the source country into China. Agglomeration has been a key focus of the large literature on how investors select locations, particularly in China. Drawing upon the agglomeration literature developed in the context of FDI in China such as Head and Ries (1996), Cheng and Kwan (2000), Chang and Park (2005), and Amiti and Javorcik (2008), it is clear that foreign investors consistently have a bias towards locating new investments in the same places that already have attracted firms from the same home country or in the same industry.

Two measures of past FDI flows are used separately in our empirical analyses: the stock and the scale of past FDI from the source country. First, the stock of past FDI from the source country proxies for the extensive margin of FDI as it captures the breadth of source country companies' total past investments in China. The stock is defined as the sum of all utilized FDI from the country in prior years. Second, the scale of FDI is measured as the ratio of utilized FDI to the count of investments in the prior year. The scale of FDI in the most recent year is used to capture the intensive margin of FDI. However, we note that the data on the count of newly established investments is available

for fewer years than the other FDI data, 2004-2006, and thus our scale measure of FDI is available for 2005-2006 only whereas our stock measure is available for 1996-2006.

#### **4.4 Home country cultural characteristics**

Two aspects of home country culture are examined: corporate work culture as captured through use of the Hofstede measures; and societal or popular culture as captured through the Schwartz Values Survey. Popular attitudes towards China were collected from the Pew Global Attitudes Project.<sup>17</sup> The number of countries for which data on these cultural proxies could be obtained varies markedly. The Hofstede and Schwartz Values Survey data were each available for nearly all countries in the sample while the Pew Global Studies popular attitudes variables were less widely available.

We report in Table 2 the average values of each cultural measure by country. Table 2 shows that there is considerable international variation in the time invariant cultural measures, uncertainty and power avoidance, and that the variation in these measures parallels that of the time variant cultural measures, egalitarianism and traditionalism. For example, Portugal has high uncertainty avoidance, egalitarianism and traditionalism while the U.S. has lower values for all of these measures. We note that countries with a long history of large-scale economic interaction with China such as Canada and the United Kingdom have lower frequency of positive opinions of China than countries that are economically developing such as Bangladesh, Malaysia and Pakistan even as the average attitude towards China of these experienced investor nations exceeds that of the international mean for this variable (43-59% vs. 74-82%).

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<sup>17</sup> These surveys were conducted at varying time intervals in different countries. We assumed that the attitudes expressed in one survey remained unchanged until the next survey occurred. That is, the assumption is that while the surveys were conducted at non-constant time intervals, events had occurred that motivated the Pew Global Studies Project to undertake surveys at particular times.

#### 4.5 Economic control variables

The vector of variables,  $X$ , includes economic characteristics of the source country and of the relationship between the source country and China as motivated by the trade literature which has shown that bilateral trade flows are affected by trade regulations, real economic activity, and cultural proximity. Thus, we begin with one measure of trade regulations: the tariff rate (favored nation status) as reported by the World Bank.<sup>18</sup> To capture home country economic conditions that might affect corporate investment activity we include real GDP per capita to proxy resource constraints that might affect any firm from that country. Firms may delay or modify investment plans if there are unexpected currency shocks although currency shocks often are associated with changes in GDP. Accordingly, average annual exchange rates or foreign exchange volatility, proxied by the standard deviation of daily exchange rates, are used in robustness tests.<sup>19</sup>

Finally, we also include a proxy for whether the source country shares a language with our host country, China. If we used the literal definition of common language, then this variable would be observed for only three source countries: Hong Kong, Singapore, and Taiwan.<sup>20</sup> Instead, we use a looser measure suggested by an Asian native: whether a

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<sup>18</sup> We cannot use simultaneously the preferential trade agreement index from the Database on Economic Integration Agreements (obtained from Jeffrey Bergstrand's website, <http://www3.nd.edu/~jbergstr/>) as it is highly correlated with the tariff rates. However, this index was used in robustness tests and generated qualitatively similar results.

<sup>19</sup> Daily exchange rate data could be obtained for only a subset of the countries analyzed in our paper. As the two exchange rate measures are highly correlated with one another (0.92) and each is also highly correlated with real GDP (0.48-0.49), we are unable to use simultaneously an exchange rate measure and real GDP. All results reported in this paper are qualitatively similar to those obtained with usage of either exchange rate variable in lieu of real GDP.

<sup>20</sup> As will be discussed later in Section 6.7, all results reported herein are qualitatively unchanged if we exclude from our sample the countries that constitute "Greater China", defined socially as either Hong Kong and Taiwan or Hong Kong, Singapore and Taiwan. This is done to control for the possibility of round-tripping of investment funds from China. Data is not available for Macau and thus it is excluded from all analyses reported in this paper.

source country's language or media regularly uses Chinese characters. The rationale behind this measure is that such citizens would feel more comfortable in China as they would be at least semi-literate. We thus code the variable "Chinese characters" to take the value of 1 for the following countries: Hong Kong, Japan, Singapore, South Korea, Taiwan, and Vietnam.

We also include a measure of the source country's external orientation: total trade or trade openness. As the two variables are highly correlated, we use these measures separately. Total trade is the logarithm of total exports plus imports while trade openness is total trade scaled by nominal GDP. This data was obtained from the World Bank and the Taiwanese National Statistics Bureau.<sup>21</sup>

Year fixed effects are included to capture global economic and political trends such as exchange rate volatility.<sup>22</sup> Country fixed effects are not included as nearly all regressions include the time-invariant country level Hofstede cultural measures. The error term is assumed to be clustered by source country.

## 5. Propensity to honor promises

To identify how national characteristics affect the likelihood that investors will honor their pledges, we estimate this empirical model:

$$Commitment_{c,t} = \beta_0 + \beta_1 Culture_c + \beta_2 FDI_{c,t} + \beta_3 X_{c,t} + \gamma_t + \varepsilon_{c,t}. \quad [2]$$

In this model, an independent variable will be statistically significantly different from zero only if it has different effects on utilized and contracted FDI flows. The focal variable,

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<sup>21</sup> Bilateral trade data between source countries and China was obtained from the OECD statistical database but we could not use this data as bilateral trade and utilized FDI flows are highly correlated.

<sup>22</sup> Because the FDI data is collected at the country-year level, we are unable to include industry fixed effects.

*Culture*, is measured as a characteristic of the country that would affect local firms' probability of planning and/or fulfilling investments in China. In the models discussed in Sections 5.1 and 5.4, we use only time invariant cultural measures, and thus culture is captured as  $Culture_c$ . However, in the models shown in Sections 5.2 and 5.3 we use time-varying cultural measures, and culture is included in the model as  $Culture_{c,t}$  instead. Past FDI is alternatively captured through stock and scale measures (the extensive and intensive margins). The vector  $X$  contains economic characteristics of the source country. Year fixed effects are included to capture global economic and political trends. Finally, the error terms are clustered by source country.

### **5.1 Impact of corporate culture**

Since the propensity to honor investment pledges is a business decision, our baseline model shown in Table 3 uses separately two measures of work culture from Hofstede. While all models control for the source country's past FDI into China, past FDI is measured as the stock of utilized FDI, extensive margin, in Models 1-4 and as the scale of utilized FDI, intensive margin, in Models 5-8. Two sets of results are presented side-by-side in this table: baseline results with culture proxied by uncertainty avoidance (Models 1-2 and 5-6) and power distance (Models 3-4 and 7-8).

First, the propensity for firms to honor commitments is significantly lower when firms come from countries with a greater degree of uncertainty avoidance. This suggests these firms make upward biased investment commitments. We observe that this effect is somewhat moderated by the types of past experiences investors from the source country have had in China as the interactive effect of uncertainty and FDI margin is positive. This suggests that the effect of uncertainty avoidance is greater among firms from

countries with more China knowledge, and thus less uncertainty to overcome. In other words, intrinsically greater knowledge about how to operate in China may offset the effects of home country culture.

Second, we find that the propensity to honor commitments is unrelated to the power distance index. This indicates that firms are not leveraging relationships to change investment costs after making commitments. However, when we interact the power distance index and scale of FDI (Models 7-8), we observe that the countries with greater power distance and larger recent investments in China are less likely to honor investments. This suggests investment pledges may be used to extract concessions from local parties before investments are actually made. Firms from countries with higher levels of power distance index may negotiate greater benefits after signing preliminary contracts, and thus be more willing to honor investment promises in China. However, the converse may also hold: companies from countries with lower power distance index scores may learn more about China after making their investment pledges. What these firms learn may make them feel uncomfortable operating in China and thus be less likely to honor prior investment pledges.

Whether companies from a country honor investment pledges appears to be completely unrelated to the stock of past FDI from the source country to China (Models 1-4). Agglomeration theories suggest investors prefer to collocate with other investors from the common home country. That the stock of past FDI is insignificant suggests that firms may already have incorporated the benefits of agglomeration into more effective investment valuations. Thus, there is a symmetric effect of stock of FDI on utilized and contracted FDI inflows and no resultant effect on the commitment ratio.

On the other hand, the propensity to honor commitments is significantly affected by the scale of past FDI from the source country (Models 5-8). This relationship is negative when we control for the uncertainty avoidance (Models 5-6), and positive when we control for the power distance index (Models 7-8). As the uncertainty and power distance indexes are only weakly correlated (0.105) and neither variable is highly correlated with the scale of FDI (-0.175 and 0.078, respectively), it is hard to identify a clear story for why the scale variable would flip signs depending upon which aspect of culture is included in a model. Thus, we are left with a clear story that the scale of past FDI matters but with some ambiguity regarding *how* it matters. At the bottom of Table 3 we report that the cultural measure, uncertainty avoidance or power distance, and the interactive term of this cultural measure with a margin of FDI is jointly statistically significantly different from zero in six of our eight models.

Turning now to the control variables, we find that tariffs have no effect on the commitment ratio. This suggests that while tariffs affect the levels of trade of investment, as shown previously in the trade literature, they affect the propensity of investors to make FDI but not whether FDI commitments are honored. The commitment ratio appears unrelated to the source country's level of wealth (captured by real GDP per capita) or regular usage of Chinese characters. When a source country has a larger level of foreign trade or has a more open economy, companies are more likely to honor investments. The unifying story obtained from the control variables is that variables that are well known to affect levels of trade and FDI do not have similar effects on the propensity of investors to honor commitments.

## 5.2 Impact of social culture

The most common criticism of the Hofstede measures of culture is that the sample surveyed, IBM executives or their peers, may not be representative of the workforce in each country. However, we argue that corporate executives are the people who would be making corporate investment decisions that could lead to FDI, and thus this criticism is inapplicable in the framework analyzed herein. Nonetheless, an alternative source of cultural data is now used: the Schwartz Values Survey. The Schwartz Values Survey measures may be appropriate as all decision makers for corporate investments will, at minimum, have completed at least some years of K-12 schooling. We use three measures of popular culture: the average degrees of egalitarianism, traditionalism, and harmony in a country. These results are shown in Table 4.

First, we examine egalitarianism to capture how managers might treat colleagues, employees, and regulators. We observe that the propensity to honor commitments is significantly lower when the source country is more egalitarian (Models 1-2 and 7-8). This may indicate that the effects of egalitarianism are embedded at an earlier stage: that is, whether a firm even makes investment pledges in China, which is consistent with the findings of Siegel et al. (2011, 2012) and our findings on the levels of contracted and utilized FDI (as discussed earlier in Section 5). The interactive term of egalitarianism and the intensity of past FDI, stock or scale, is positive and statistically significant, which suggests that when companies have greater knowledge of actual operating conditions in China, they are more inclined to honor investments. We note that when we control for the scale of past FDI (Models 7-8), the magnitude of the coefficient on the interactive term is significantly larger than that of the level of egalitarianism, suggesting that firms from



more egalitarian countries may be *more* likely to honor their investment commitments. This is confirmed by the F-test for joint significance of both terms involving egalitarianism as these results are statistically significantly different from zero.

Next, we examine the effect of traditionalism (Models 3-4 and 9-10). In countries that have greater respect for tradition, there may be greater pressure to act consistently across time and thus be more inclined to honor investment commitments. We obtain limited support for this hypothesis as the commitment ratio is insignificantly related to traditionalism. However, we find that the interactive term for traditionalism and the margin of FDI is negative (Models 9-10). This suggests that while firms from traditional cultures may be more inclined to honor their pledges, they may feel less obligated to do so when they have more knowledge of local operating conditions.

Finally, we look at the effects of harmony (Models 5-6 and 11-12). The propensity to honor commitments appears largely unrelated to the average value of harmony. However, it is slightly greater when there is more knowledge of China operating conditions (extensive or intensive margins). These results suggest that when investors care more about preserving harmony, they will want to do so when they have more at stake (i.e., past investments).

These results suggest that popular cultural attitudes do affect the commitment ratio. Also, as companies learn more about China, investors are less likely to act in a manner that is consistent with their home country culture. The effects vary markedly depending upon how the investors acquire prior knowledge regarding China. That is, when we control for the totality of past investments in China (Models 1-6) we obtain

results that are not fully consistent with the impact of the most recent past investments in China (Models 7-12).

### **5.3 Public opinion towards China**

We now modify the model so that we include the percent of the population with a positive opinion of China as an additional independent variables. These results are shown in Table 5. We find that public opinion is consistently unrelated to the propensity of firms to honor their pledges. This suggests that corporate investment activity is not driven by intertemporal variation in popular sentiment.

Once again we find that the commitment ratio is negatively associated with uncertainty avoidance but this effect is slightly reversed by the source country's past FDI into China (Models 1-2 and 5-6). While the power distance per se is not associated with the commitment ratio, the commitment ratio is lower when power distance is higher and past FDI is larger (Models 7-8). The joint statistical significance of the Hofstede cultural measure and the interactive term with FDI margin is now less statistically significantly different from zero than was observed in our baseline model (Table 3). This suggests that while public opinion per se is not significantly associated with the commitment ratio, it is nonetheless changing the effect of home country culture.

### **5.4 Events**

The Asian Financial Crisis occurred in 1997-1998 and China joined the World Trade Organization (WTO) in 2001. It is possible that these two events affected the pool of potential investors in China and/or the willingness of these investors to honor their investment pledges. Accordingly, we now estimate an expanded model that includes measures of these two events, reported in Table 6. While we were earlier able to use two

measures of the margin of FDI, we are now able to use only the extensive margin as the intensive margin can be estimated only for the years 2004-2006, which is well after both events occurred.

We begin with a model that includes two additional terms relevant to the Asian financial crisis: a dummy variable to capture Asian countries as Asian firms were the most liquidity constrained at this time and an interactive term to capture Asian firms during the Asian financial crisis. These results, which are shown in Models 1-4, indicate that firms from Asian countries do not differ in their propensity to honor commitments except during the financial crisis. That is, Asian firms were more likely to honor commitments made during the financial crisis. An alternate interpretation of this framework is that Asian firms may have always had a greater knowledge of China and thus were more inclined to invest in China at a time of regional crisis.

Next, we examine how China's accession to the WTO affected the commitment ratio. We find that firms were less likely to honor investment pledges after China joined the WTO (Models 5-8). It is possible that local Chinese officials' ability to offer idiosyncratic investment incentives to foreign firms was decreased after China joined the WTO, which may have led to both a change in the pool of firms willing to invest in China and the accuracy of their initial investment pledges.

Earlier results regarding home country cultural measures were found once again. That is, the commitment ratio is negatively associated with uncertainty avoidance although the effect is moderated slightly for countries with greater experience in China (Models 1-2 and 5-6). In addition, the commitment ratio is unaffected by the power

distance index irrespective of the degree of the source country's prior FDI in China (Models 3-4 and 7-8).

## **6. Conclusion**

We contribute to three overlapping areas of the literature. First, there is a long literature on how companies expand internationally through a lifecycle that often begins with foreign trade before moving to overseas investments, and how firms decide where to invest overseas (e.g., Blonigen, 2005; Raff et al., 2012). Second, a growing body of research has shown that national cultural differences affect the types of individuals who become corporate decision makers (e.g., Liu, 2013; Pan et al., 2014), and the levels of corporate risk taking (Li et al., 2013), corporate cash holdings and investments (Chen et al., 2015), foreign direct investment (Siegel et al., 2011, 2012), and cross-border mergers and acquisitions (Ahern et al., 2015). Finally, there is a literature that examines how firms implement decisions regarding investments, chiefly by focusing on internal managerial power (Glaser et al., 2013) and the speed of investments (Pacheco-de-Almeida et al., 2012; Hawk et al., 2013).

Our contribution to these literatures is showing that national culture affects the propensity of corporations to honor commitments abroad, and thus the pattern of FDI, through usage of Chinese data. Corporations seek to reduce informational asymmetries within and across firm boundaries in order to reduce the cost of capital and increase profitability. Cultural distance increases transaction costs (Guiso et al., 2006), which decreases the profitability of investments, and cultural values persist strongly across generations (Giavazzi et al., 2015). Thus, cultural attitudes affect the composition and

scale of corporate investments, particularly overseas. Our results suggest that there is persistent cross-country variation in the ability to plan and implement corporate investments, which is related to the efficiency of past investments (Wurgler, 2000).

National culture may be measured using proxies for corporate culture such as the Hofstede measures, or social culture such as the Schwartz Values Survey measures. Irrespective of which set of proxies is used, we obtain a consistent result: the likelihood that investors honor previously announced pledges, as captured by our commitment ratio, is related to the culture of the investors' home country. For example, we find that greater uncertainty avoidance may lead a corporation to front load their due diligence and produce more accurate investment pledges, or estimates, ex ante and these estimates are generally lower in monetary value. Firms from these countries also invest less subsequently. This suggests that even after engaging in greater knowledge acquisition up front companies from these countries are still more reluctant to honor investment pledges.

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## **Appendix 1. Culture affects FDI**

Culture is known to affect the level of utilized FDI (e.g., Siegel et al., 2011, 2012) with the effects greater among differentiated products (Rauch and Trindade, 2002). We begin by examining whether the precursor to actual investments – contracted FDI – is systematically related to these cultural characteristics. Next, we examine whether the earlier findings persist in our sample through analysis of utilized FDI. Finally, it is possible that companies are simultaneously announcing and fulfilling investment pledges. Accordingly, contracted and utilized FDI may be better modeled jointly using simultaneous equations. These three sets of results tell a consistent story: the level of investments is related to the culture of the source country.



### A1.1 Separate analyses of Contracted and Utilized FDI

Our first empirical model relates the level of FDI to source country culture as:

$$FDI_{c,t} = \beta_0 + \beta_1 Culture_c + \beta_2 FDI_{c,t-1} + \beta_3 X_{c,t} + \gamma_t + \varepsilon_{c,t}. \quad [2]$$

The dependent variable is contracted FDI or utilized FDI. Our focal independent variable is culture, which we capture in two ways. First, culture may affect the value of contracted FDI if investors from a particular country are likely to engage in more or more accurate due diligence to better estimate associated costs due to a desire to avoid uncertainty (uncertainty avoidance). Alternatively, investors from a particular country may believe that they have greater power to win concessions from local leaders or businesses prior to announcing investments and thus the power distance index (power distance) may be systematically related to the level of contracted FDI. We estimate this model using two different measures of FDI – the extensive margin or stock of past FDI (Models 1-4) and the intensive margin or scale of past FDI (Models 5-8).

The vector of variables,  $X$ , includes economic characteristics of the source country and of the relationship between the source country and China. Year fixed effects are included, and the error term is assumed to be clustered by source country.

We report in Table A1 the results for analysis of contracted FDI (Panel A) and utilized FDI (Panel B). We find mixed evidence regarding whether FDI flows are related to home country cultural values. When we control for the total stock of past FDI from a source country we find that there is no relationship between FDI flows, contracted or utilized, and home country cultural values. However, when we control for the scale of past FDI (intensive margin), countries that have higher preferences for harmony and

egalitarianism are making lower levels of investment pledges and actual investments. These results are similar to those obtained previously by others with respect to only utilized FDI (e.g., Siegel, 2011, 2012).

### **A1.2 Simultaneous equations modeling of Contracted and Utilized FDI**

It is possible that firms are simultaneously pledging and fulfilling investments. This could happen if firms announce planned investments early in a calendar year and begin fulfilling them later that same year. Alternatively, firms may make a constant stream of investments – either a series of new investments or regular improvements to existing investments. In both instances, separate estimation of contracted and utilized FDI may suffer simultaneity bias. This might, for example, explain why the effect of power distance on FDI varies based on whether FDI is defined as contracted or utilized. Thus, we now use simultaneous equations to model the two series.

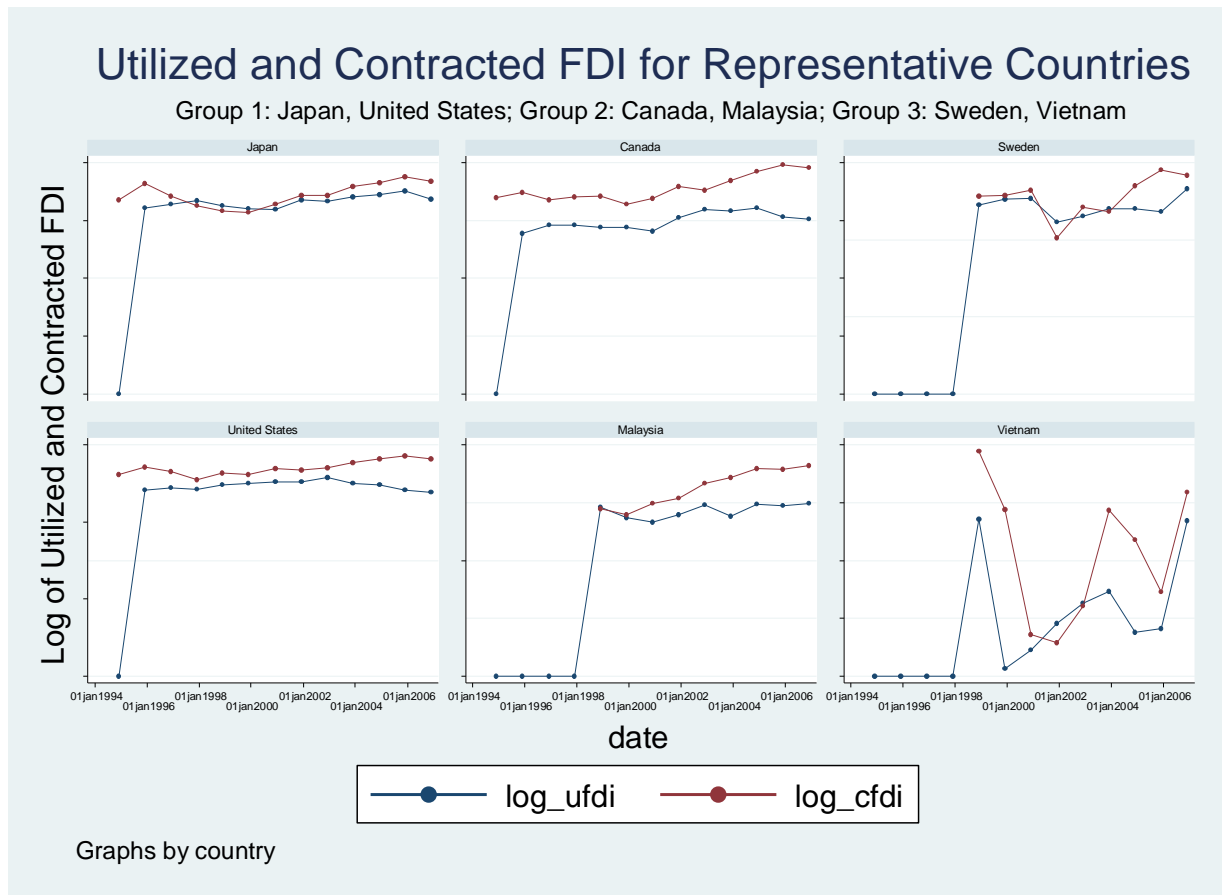
When we use a simultaneous equations framework, we obtain the results shown in Table A2. We find that the level of contracted FDI is consistently not associated with those two characteristics while utilized FDI is negatively correlated with uncertainty avoidance and positively correlated with power distance. Thus, the effect of national culture appears to show up *after* investments are announced publicly. This is consistent with the widely held belief that Chinese officials were seeking to attract as much investment as possible from as many countries as possible.

### **Appendix 2. Greater China**

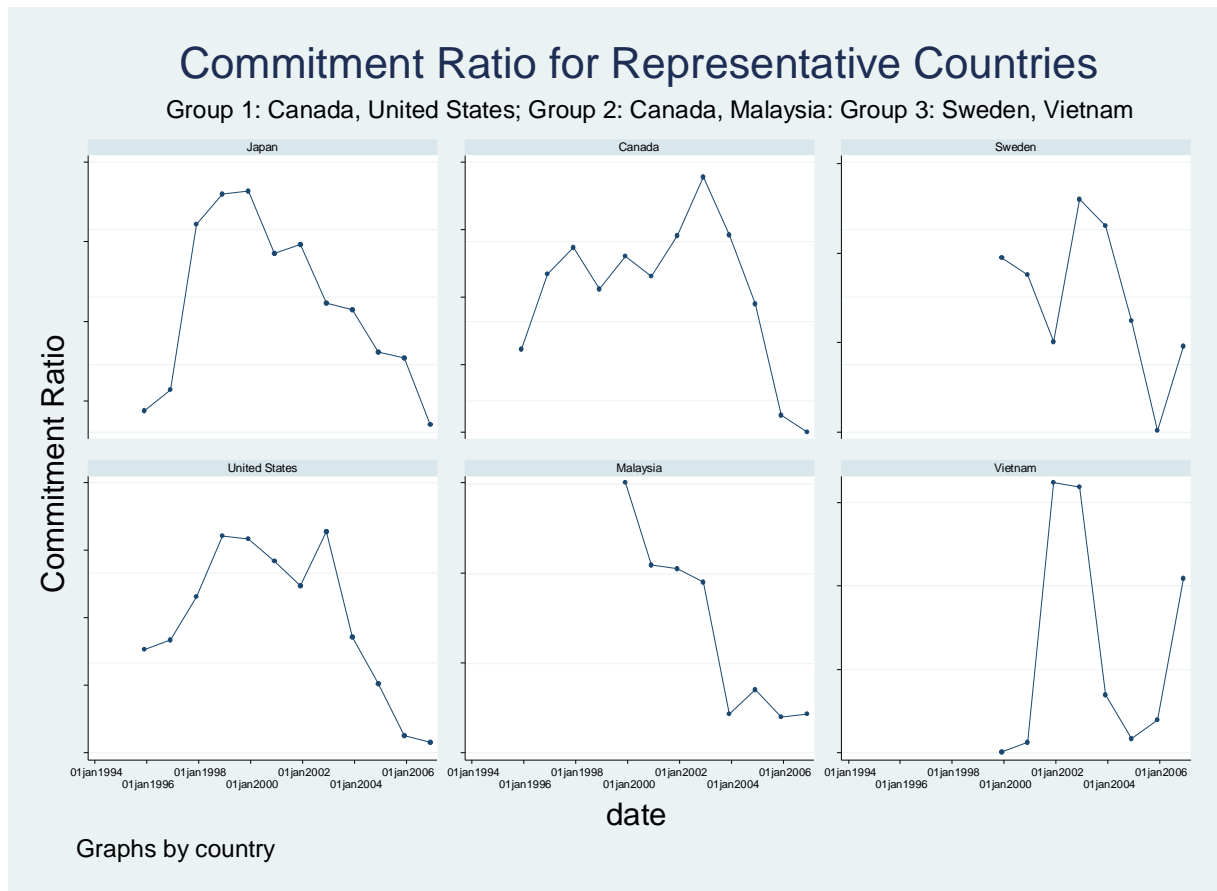
Many people contend that some, if not much, of the FDI from Hong Kong and Taiwan is misclassified and is actually mainland Chinese monies that have been routed via foreign companies in order to obtain FDI incentives. This phenomenon is oftentimes

called “round-tripping”. If round-tripping were indeed commonplace, then FDI from Hong Kong and Taiwan would effectively be domestic investment, not FDI. Accordingly, we re-estimate all models after excluding data from Hong Kong and Taiwan. The results of this estimation are qualitatively similar to those reported herein. A representative table is presented as Table A3 to illustrate how the results shown earlier (in Table 3) remain qualitatively unchanged when the countries that constitute “Greater China” are excluded from the estimation sample.

**Figure 1. Utilized and contracted FDI by country.** In this figure we report the logarithm of contracted and utilized FDI by country over time for six representative countries. Group 1 is Japan and the United States as contracted FDI appears to track subsequent utilized FDI. Group 2 is Canada and Malaysia as contracted FDI consistently exceeds utilized FDI. Group 3 is Sweden and Vietnam as no clear patterns in contracted and utilized FDI are observed.



**Figure 2. The commitment ratio by country.** In this figure we report the variation of the commitment ratio, measured as the ratio of current year utilized FDI flows to the average of current and preceding year contracted FDI flows, for six representative countries. Group 1 is Japan and the United States as contracted FDI appears to track subsequent utilized FDI. Group 2 is Canada and Malaysia as contracted FDI consistently exceeds utilized FDI. Group 3 is Sweden and Vietnam as no clear patterns in contracted and utilized FDI are observed.



**Table 1. Summary statistics.** In this table we report the mean, standard deviation, minimum and maximum values, and count of observations for each variable used in our empirical analyses. The definition of each variable is reported in the second column of this table, and the source is reported in the third column.

Variable	Definition	Source	Mean	Std. Dev.	Min.	Max.	Count
U_FDI	Utilized FDI, log US\$m	CEIC	5.098	2.324	0.077	11.204	579
C_FDI	Contracted FDI, log US\$ mn	CEIC	5.447	2.428	-0.128	11.228	386
Commitment ratio	Commitment ratio as defined in Equation 1. The ratio is estimated as the ratio of a country's utilized FDI in a given year to the average level of contracted FDI in the preceding and current year.	Authors' estimates	0.595	0.517	-0.808	8.071	387
Stock FDI	Sum of all utilized FDI through end of prior year, log US\$m	Authors' estimates	1.831	0.487	-1.465	2.589	577
N_FDI	Count of FDI projects receiving utilized FDI from a source country in a year	CEIC	693.101	2150.759	1	1.60E+04	238
Scale FDI	Ratio of utilized FDI to count of FDI projects receiving utilized FDI in the same year	Authors' estimates	5.286	36.177	0.015	403.208	238
Uncertainty avoidance	The uncertainty avoidance index captures the degree to which members of a population feel uncomfortable with uncertainty and ambiguity.	Hofstede (2010)	61.912	23.521	8	112	579
Power distance	The power distance index reflects whether less powerful members of a population accept and expect that power will be distributed unequally.	Hofstede (2010)	54.325	22.317	11	104	579
Egalitarianism	A measure of the degree to which people view themselves as being egalitarian. Egalitarian individuals view others as moral equals with shared human interests and welfare.	Schwartz Values Survey	4.72	0.282	4.309	5.214	523
Traditionalism	A measure of the degree to which people prioritize respect for what has been done previously or for carrying out actions because it is customary.	Schwartz Values Survey	2.803	0.405	2.038	3.733	523
Harmony	A measure of the degree to which people expect groups and individuals to fit together peacefully and to avoid conflict.	Schwartz Values Survey	4.012	0.33	3.242	4.557	523
Attitude	Percent of population that has a positive attitude towards China according to surveys.	Pew Research Center	50.14	14.886	5	83	356
Tariff	Weighted average tariff rate, most favored nation status	World Bank	5.278	11.924	0	255.79	493
GDP	GDP per capita, log US\$	World Bank	11.435	2.074	6.970	17.13	579
Exchange rate	Average exchange rate of local currency to the USD per year	World Bank	527.43	2192.884	0.421	1.60E+04	579
Chinese characters	Dummy variable that takes the value of 1 if the country's main language uses Chinese characters, and is 0 otherwise	Authors' estimates	0.143	0.351	0	1	579
Total trade	Total exports plus imports, log US\$m	World Bank	25.972	2.728	12.289	29.247	579

Openness	Ratio of total trade to nominal GDP	World Bank	0.581	0.79	0	5.103	579
Asian crisis	Dummy variable that takes the value of 1 during the Asian crisis (1997-1998), and is 0 otherwise		0.035	0.183	0	1	579

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**Table 2. Cultural values by country.** In this table we list the values of the Hofstede measures of corporate culture (uncertainty avoidance, power distance index), Schwartz values of popular culture (egalitarianism, traditionalism, harmony), and percent of population reporting positive attitudes towards China. We report at the bottom the average value of each series for each country.

Data source  Country	Hofstede		Schwartz Social Values Survey			Pew Research Center
	Uncertainty Avoidance	Power distance	Egalitarianism	Traditionalism	Harmony	Positive attitude towards China
Argentina	86	49	4.844	2.836	4.191	32.2
Australia	51	36	4.740	2.722	4.011	53.765
Austria	70	11	4.934	2.445	4.391	
Bangladesh	60	80				74
Belgium	94	65	5.025	2.438	4.075	
Brazil	76	69	4.861	3.185	4.221	52
Canada	48	39	4.741	2.404	3.700	53.684
Costa Rica	86	35	4.759	3.106	3.997	
Czech	74	57				34.778
Denmark	23	18	5.029	2.038	4.216	
Egypt			4.699	4.447	4.034	62.5
Finland	59	33	4.931	2.366	4.292	
France	86	68	5.153	3.116	4.507	49.857
Germany	65	35	4.975	2.185	4.557	40.632
Greece	112	60	4.821	2.439	4.366	56
Hong Kong	29	68	4.463	3.009	3.468	
Hungary	82	46	4.515	2.344	4.338	
India	40	77	4.458	3.189	3.938	35
Indonesia	48	78	4.332	3.382	3.821	69.6
Iran	59	58	4.432	3.444	3.619	
Ireland	35	28	4.873	2.637	3.722	
Israel	81	13	4.625	3.129	3.242	46.1
Italy	75	50	5.109	2.454	4.325	28.143
Japan	92	54	4.309	2.752	4.198	36.684
Korea	85	60	4.422	3.307	3.573	55.421
Luxembourg	70	40				
Malaysia	36	104	4.396	3.324	3.630	82.2
Netherlands	53	38	5.018	2.467	4.019	56
New Zealand	49	22	4.949	2.432	4.161	
Norway	50	31	5.075	2.170	4.333	
Pakistan	70	55				77.889
Panama	86	95				
Philippines	44	94	4.579	3.641	4.013	52
Poland	93	68	4.474	2.862	4.024	37
Portugal	104	63	5.129	2.557	4.330	
Romania	90	90	4.376	2.338	3.971	
Russia	95	93	4.360	2.675	4.099	63.467
Singapore	8	74	4.492	3.207	3.547	



South Africa	49	49	4.447	3.212	3.874	37
Spain	86	57	5.214	2.969	4.421	50.2
Sweden	29	31	4.953	2.569	4.397	43
Switzerland	58	34	5.109	2.596	4.315	
Taiwan	69	58	4.345	2.868	4.167	
Thailand	64	64	4.504	3.733	3.659	
Turkey	85	66	4.656	2.650	4.065	35.778
United Kingdom	35	35	4.925	2.525	3.904	59.474
United States	46	40	4.709	3.002	3.528	43.895
Vietnam	30	70				
<b>Mean</b>	64	54	4.732	2.837	4.030	50.652
<b>Count</b>	47	47	42	42	42	28

**Table 3. Hofstede measures of corporate culture.** In this table we report results from the regression of the commitment ratio on the stock of past FDI (Models 1-6) or scale of recent FDI (Models 7-12); uncertainty avoidance index (Columns 3-4 and 9-10) or power distance index (Columns 5-6 and 11-12); the interaction of the stock or scale of FDI with the Hofstede cultural measure (uncertainty avoidance or power distance); economic control variables; and a measure of the economy's external orientation (total trade or trade openness). We report at the bottom the p-value of the F-test for joint significance of the cultural measure and the interactive term of that cultural measure with the margin of FDI. Standard errors are reported in parentheses. \* denotes significance at the 10% level; \*\*, 5%; and \*\*\*, 1%.

	Extensive Margin of FDI - stock				Intensive Margin of FDI - scale			
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
FDI Margin (t-1)	-0.168 (0.111)	-0.148 (0.110)	0.222 (0.170)	0.272 (0.171)	-0.082*** (0.030)	-0.068*** (0.025)	0.164*** (0.042)	0.154*** (0.043)
Uncertainty avoidance	-0.007** (0.003)	-0.007** (0.003)			-0.003*** (0.001)	-0.003** (0.001)		
Uncertainty avoidance * FDI Margin (t-1)	0.003** (0.001)	0.003** (0.002)			0.002*** (0.001)	0.002** (0.001)		
Power distance			0.004 (0.006)	0.006 (0.006)			0.001 (0.001)	0.001 (0.001)
Power distance * FDI Margin (t-1)			-0.003 (0.003)	-0.004 (0.003)			-0.002*** (0.000)	-0.002*** (0.000)
Tariff	0.000 (0.001)	0.001 (0.001)	0.000 (0.001)	0.000 (0.001)	-0.007** (0.003)	-0.005 (0.004)	-0.004 (0.002)	-0.003 (0.003)
GDP	0.007 (0.011)	0.011 (0.012)	0.015 (0.012)	0.022* (0.013)	-0.013* (0.008)	-0.004 (0.009)	-0.014** (0.006)	-0.008 (0.006)
Chinese characters	0.071 (0.069)	0.021 (0.070)	0.092 (0.070)	0.037 (0.071)	0.029 (0.063)	-0.016 (0.063)	0.069 (0.043)	0.032 (0.046)
Total trade	0.011** (0.004)		0.010** (0.004)		0.009 (0.006)		0.008* (0.005)	
Openness		0.018 (0.038)		0.038 (0.045)		0.056** (0.024)		0.036* (0.019)
Constant	0.770*** (0.286)	0.958*** (0.289)	-0.028 (0.340)	0.056 (0.363)	0.443** (0.191)	0.516*** (0.132)	0.164 (0.135)	0.297*** (0.082)
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
R <sup>2</sup>	0.273	0.268	0.265	0.263	0.197	0.224	0.381	0.386
Adjusted R <sup>2</sup>	0.231	0.226	0.222	0.220	0.110	0.140	0.314	0.320
N	312	312	312	312	83	83	83	83
F-test of joint significance	0.042**	0.049**	0.190	0.157	0.015**	0.020**	0.000***	0.000***

**Table 4. Schwartz measures of social culture.** In this table we report results from the regression of the commitment ratio on the stock of past FDI (Models 1-6) or scale of recent FDI (Models 7-12); egalitarianism (Columns 1-2 and 7-8), traditionalism (Columns 3-4 and 9-10), or harmony (Columns 5-6 and 11-12); the interaction of the stock or scale of FDI with the social cultural measure (egalitarianism, traditionalism, or harmony); economic control variables; and a measure of the economy's external orientation (total trade or trade openness). We report at the bottom the p-value of the F-test for joint significance of the cultural measure and the interactive term of that cultural measure with the margin of FDI. Standard errors are reported in parentheses. \* denotes significance at the 10% level; \*\*, 5%; and \*\*\*, 1%.

	Extensive Margin of FDI - stock						Intensive Margin of FDI - scale					
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
FDI Margin (t-1)	-2.463**	-2.445**	0.219	0.252	-1.232**	-0.829	-1.095***	-1.061***	0.363***	0.369***	-0.808**	-0.964**
	(0.998)	(0.964)	(0.196)	(0.187)	(0.547)	(0.518)	(0.176)	(0.186)	(0.081)	(0.085)	(0.389)	(0.371)
Egalitarianism	-0.679*	-0.710**					-0.172*	-0.166*				
	(0.356)	(0.346)					(0.089)	(0.090)				
Egalitarianism * FDI Margin (t-1)	0.533**	0.530**					0.239***	0.232***				
	(0.209)	(0.201)					(0.038)	(0.041)				
Traditionalism			0.005	0.041					0.054	0.067		
			(0.093)	(0.091)					(0.052)	(0.050)		
Traditionalism * FDI Margin (t-1)			-0.043	-0.050					-0.100***	-0.101***		
			(0.060)	(0.059)					(0.022)	(0.023)		
Harmony					-0.433	-0.261					-0.046	-0.108
					(0.274)	(0.265)					(0.108)	(0.106)
Harmony * FDI Margin (t-1)					0.331**	0.234*					0.201**	0.240**
					(0.138)	(0.132)					(0.097)	(0.092)
Tariff	-0.000	0.000	-0.000	0.000	-0.001	0.000	0.001	-0.001	0.002	0.001	-0.003	-0.000
	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)	(0.007)	(0.007)	(0.005)	(0.005)	(0.006)	(0.007)
GDP	0.032**	0.039***	0.021*	0.033***	0.018*	0.033***	-0.005	-0.001	-0.008	-0.004	-0.010	-0.000
	(0.013)	(0.012)	(0.011)	(0.010)	(0.011)	(0.009)	(0.010)	(0.010)	(0.007)	(0.009)	(0.007)	(0.009)
Chinese characters	0.221**	0.155*	0.048	-0.037	0.091	-0.026	0.114	0.064	0.070	0.028	0.141***	0.065
	(0.095)	(0.090)	(0.066)	(0.064)	(0.081)	(0.072)	(0.069)	(0.082)	(0.047)	(0.052)	(0.048)	(0.068)
Total trade	0.007		0.011***		0.017***		0.014**		0.011**		0.018***	
	(0.005)		(0.004)		(0.004)		(0.006)		(0.004)		(0.004)	
Openness		0.062*		0.087***		0.101***		0.024		0.026		0.080*
		(0.032)		(0.028)		(0.031)		(0.027)		(0.022)		(0.041)
Constant	3.305**	3.522**	0.029	0.032	1.669	1.198	0.768	1.069**	-0.122	0.074	0.136	0.702
	(1.631)	(1.567)	(0.355)	(0.348)	(1.043)	(1.025)	(0.506)	(0.472)	(0.180)	(0.180)	(0.451)	(0.427)
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
R <sup>2</sup>	0.338	0.342	0.310	0.317	0.346	0.349	0.307	0.276	0.357	0.344	0.231	0.233
Adjusted R <sup>2</sup>	0.296	0.300	0.265	0.273	0.304	0.307	0.222	0.186	0.278	0.263	0.136	0.139
N	274	274	274	274	274	274	72	72	72	72	72	72
F-test of joint significance	0.004***	0.009***	0.279	0.503	0.001***	0.003***	0.000***	0.000***	0.000***	0.000***	0.002***	0.003***

**Table 5. Popular attitudes and Hofstede measures of corporate culture.** In this table we report results from the regression of the commitment ratio on the stock of past FDI (Columns 1-4) or scale of recent FDI (Columns 5-8); the proportion of the population holding positive attitudes towards China; uncertainty avoidance index (Columns 1-2 and 5-6) or power distance index (Columns 3-4 and 7-8); the interaction of the stock or scale of FDI with the Hofstede cultural measure (uncertainty avoidance or power distance); economic control variables; and a measure of the economy's external orientation (total trade or trade openness). We report at the bottom the p-value of the F-test for joint significance of the cultural measure and the interactive term of that cultural measure with the margin of FDI. Standard errors are reported in parentheses. \* denotes significance at the 10% level; \*\*, 5%; and \*\*\*, 1%.

	Extensive Margin of FDI - stock				Intensive Margin of FDI - scale			
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
FDI Margin (t-1)	-0.697 (0.414)	-0.569* (0.312)	0.356 (0.267)	0.387 (0.254)	-0.085** (0.035)	-0.075*** (0.024)	0.149*** (0.053)	0.140** (0.059)
Uncertainty avoidance	-0.015* (0.008)	-0.014* (0.007)			-0.004** (0.002)	-0.003* (0.002)		
Uncertainty avoidance * FDI Margin (t-1)	0.008* (0.004)	0.007* (0.004)			0.002** (0.001)	0.002*** (0.001)		
Power distance			0.011 (0.009)	0.012 (0.009)			0.000 (0.001)	0.000 (0.001)
Power distance * FDI Margin (t-1)			-0.007 (0.005)	-0.007 (0.005)			-0.002*** (0.001)	-0.001** (0.001)
Positive attitude	0.003 (0.002)	0.001 (0.002)	0.003 (0.002)	0.002 (0.002)	0.000 (0.002)	-0.001 (0.002)	0.001 (0.001)	0.001 (0.001)
Tariff	0.000 (0.001)	0.000 (0.001)	0.000 (0.001)	0.000 (0.001)	-0.005 (0.006)	0.001 (0.005)	-0.002 (0.005)	-0.003 (0.004)
GDP	0.018 (0.015)	0.025 (0.015)	0.025 (0.016)	0.034** (0.016)	-0.025*** (0.009)	-0.012 (0.010)	-0.018* (0.009)	-0.015* (0.008)
Chinese characters	0.061 (0.139)	0.125 (0.156)	0.090 (0.121)	0.107 (0.127)	0.200* (0.103)	0.217** (0.084)	0.170* (0.095)	0.196** (0.088)
Total trade	0.080 (0.054)		0.019 (0.045)		0.021 (0.034)		0.020 (0.026)	
Openness		0.210*** (0.071)		0.123 (0.091)		0.188** (0.071)		0.060 (0.075)
Constant	-0.853 (1.100)	0.994 (0.601)	-1.224 (1.317)	-0.870 (0.553)	0.241 (0.962)	0.598** (0.222)	-0.168 (0.718)	0.339*** (0.098)
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
R <sup>2</sup>	0.338	0.342	0.326	0.332	0.290	0.384	0.455	0.453
Adjusted R <sup>2</sup>	0.268	0.272	0.254	0.261	0.131	0.246	0.332	0.330
N	187	187	187	187	50	50	50	50
F-test of joint significance	0.199	0.166	0.275	0.273	0.049**	0.017**	0.000***	0.020**

**Table 6. Impact of events - Asian financial crisis and China's accession to the WTO.** In this table we report results from the regression of the commitment ratio on the stock of past FDI; uncertainty avoidance index (Columns 1-2 and 5-6) or power distance index (Columns 3-4 and 7-8); the interaction of the stock of FDI with the Hofstede cultural measure (uncertainty avoidance or power distance); event variables (Asian country and Asian country during Asian financial crisis dummies in Columns 1-4; China member of WTO dummy in Columns 5-8); economic control variables; and a measure of the economy's external orientation (total trade or trade openness). We report at the bottom the p-value of the F-test for joint significance of the cultural measure and the interactive term of that cultural measure with the margin of FDI, and for the tests of the Asian financial crisis we also test for joint significance of the two Asian terms. Standard errors are reported in parentheses. \* denotes significance at the 10% level; \*\*, 5%; and \*\*\*, 1%.

Event	Asian financial crisis				China's accession to the WTO			
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
FDI Margin (t-1)	-0.152 (0.114)	-0.141 (0.115)	0.266 (0.199)	0.316* (0.181)	-0.168 (0.111)	-0.148 (0.110)	0.222 (0.170)	0.272 (0.171)
Uncertainty avoidance	-0.007** (0.003)	-0.007** (0.003)			-0.007** (0.003)	-0.007** (0.003)		
Uncertainty avoidance * FDI Margin (t-1)	0.003* (0.002)	0.003* (0.002)			0.003** (0.001)	0.003** (0.002)		
Power distance			0.005 (0.006)	0.007 (0.006)			0.004 (0.006)	0.006 (0.006)
Power distance * FDI Margin (t-1)			-0.004 (0.004)	-0.005 (0.004)			-0.003 (0.003)	-0.004 (0.003)
Asian source country	-0.064 (0.061)	-0.028 (0.062)	0.064 (0.111)	0.087 (0.071)				
Asian source country * Asian financial crisis	0.326*** (0.108)	0.374*** (0.094)	0.293*** (0.108)	0.320*** (0.105)				
China member of WTO					0.195*** (0.070)	0.196*** (0.066)	0.203*** (0.070)	0.201*** (0.067)
Tariff	0.001 (0.001)	0.001 (0.001)	0.000 (0.001)	0.000 (0.001)	0.000 (0.001)	0.001 (0.001)	0.000 (0.001)	0.000 (0.001)
GDP	0.011 (0.012)	0.012 (0.013)	0.010 (0.013)	0.015 (0.013)	0.007 (0.011)	0.011 (0.012)	0.015 (0.012)	0.022* (0.013)
Chinese characters	0.082 (0.081)	0.012 (0.070)	0.044 (0.079)	0.007 (0.056)	0.071 (0.069)	0.021 (0.070)	0.092 (0.070)	0.037 (0.071)
Total trade	0.011* (0.006)		0.005 (0.009)		0.011** (0.004)		0.010** (0.004)	
Openness		0.018 (0.039)		0.037 (0.044)		0.018 (0.038)		0.038 (0.045)
Constant	0.659** (0.312)	0.895*** (0.300)	0.077 (0.347)	0.055 (0.348)	0.375 (0.293)	0.563** (0.275)	-0.420 (0.353)	-0.337 (0.364)
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
R <sup>2</sup>	0.281	0.276	0.271	0.273	0.273	0.268	0.265	0.263
Adjusted R <sup>2</sup>	0.234	0.229	0.223	0.226	0.231	0.226	0.222	0.220
N	312	312	312	312	312	312	312	312
F-test of joint significance - culture	0.029**	0.037**	0.399	0.171	0.042**	0.049**	0.190	0.157
F-test of joint significance - Asia	0.011**	0.000***	0.030***	0.001***				

**Table A1. Contracted and utilized FDI.** In this table we report results from regression of level of contracted FDI (Panel A) and utilized FDI (Panel B) on the stock of past FDI (Columns 1-4) or scale of recent FDI (Columns 5-8); uncertainty avoidance index (Columns 1-2 and 5-6) or power distance index (Columns 3-4 and 7-8); the interaction of the stock or scale of FDI with the Hofstede cultural measure (uncertainty avoidance or power distance); economic control variables; and a measure of the economy's external orientation (total trade or trade openness). We report at the bottom the p-value of the F-test for joint significance of the cultural measure and the interactive term of that cultural measure with the margin of FDI. Standard errors are reported in parentheses. \* denotes significance at the 10% level; \*\*, 5%; and \*\*\*, 1%.

**Panel A: Contracted FDI**

	Extensive Margin of FDI - stock				Intensive Margin of FDI - scale			
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
FDI Margin (t-1)	4.600*** (1.040)	4.641*** (1.049)	2.715*** (0.824)	2.671*** (0.826)	-0.365 (0.234)	-0.517 (0.315)	0.601* (0.345)	0.794* (0.405)
Uncertainty avoidance	0.026 (0.028)	0.025 (0.028)			-0.029** (0.012)	-0.037*** (0.013)		
Uncertainty avoidance * FDI Margin (t-1)	-0.017 (0.016)	-0.017 (0.016)			0.008 (0.005)	0.012 (0.007)		
Power distance			-0.027 (0.022)	-0.031 (0.023)			0.011 (0.012)	0.013 (0.012)
Power distance * FDI Margin (t-1)			0.016 (0.013)	0.018 (0.013)			-0.006* (0.004)	-0.008* (0.004)
Tariff	0.000 (0.003)	0.000 (0.002)	-0.000 (0.002)	-0.000 (0.002)	-0.217** (0.089)	-0.263*** (0.089)	-0.221** (0.092)	-0.263*** (0.094)
GDP	-0.061 (0.049)	-0.066 (0.045)	-0.098* (0.050)	-0.112* (0.056)	-0.041 (0.128)	-0.110 (0.146)	0.008 (0.126)	-0.037 (0.156)
Chinese characters	1.175** (0.549)	1.086** (0.432)	1.143** (0.480)	1.058*** (0.373)	3.050*** (0.936)	2.995*** (0.742)	3.205*** (0.876)	3.095*** (0.702)
Total trade	0.025 (0.044)		0.030 (0.042)		0.087 (0.161)		0.110 (0.163)	
Openness		-0.049 (0.152)		-0.117 (0.140)		-0.448 (0.318)		-0.344 (0.293)
Constant	-0.987 (2.255)	-0.311 (2.048)	2.381 (1.903)	3.486* (1.776)	6.376 (4.869)	10.361*** (2.109)	2.607 (4.791)	6.213*** (2.201)
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
R <sup>2</sup>	0.809	0.808	0.805	0.804	0.500	0.508	0.468	0.465
Adjusted R <sup>2</sup>	0.798	0.797	0.793	0.793	0.446	0.455	0.411	0.407
N	311	311	311	311	83	83	83	83
F-test of joint significance	0.472	0.454	0.464	0.394	0.059*	0.018**	0.234	0.160

**Panel B: Utilized FDI**

	Extensive Margin of FDI - stock				Intensive Margin of FDI - scale			
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
FDI Margin (t-1)	4.842*** (1.146)	5.004*** (1.142)	3.118*** (0.804)	3.215*** (0.847)	-0.008*** (0.003)	-0.006** (0.002)	0.019 (0.019)	-0.001 (0.008)
Uncertainty avoidance	0.024 (0.030)	0.026 (0.030)			-0.020** (0.009)	-0.021** (0.009)		
Uncertainty avoidance * FDI Margin (t-1)	-0.016 (0.015)	-0.017 (0.016)			0.000* (0.000)	0.000** (0.000)		
Power distance			-0.028 (0.025)	-0.029 (0.026)			-0.005 (0.008)	-0.006 (0.009)
Power distance * FDI Margin (t-1)			0.013 (0.014)	0.013 (0.014)			-0.000 (0.000)	-0.000 (0.000)
Tariff	-0.001 (0.002)	0.000 (0.002)	-0.001 (0.002)	-0.000 (0.002)	-0.178*** (0.052)	-0.211*** (0.052)	-0.181*** (0.054)	-0.216*** (0.056)
GDP	-0.049 (0.049)	-0.036 (0.042)	-0.100* (0.057)	-0.093 (0.058)	-0.059 (0.106)	-0.042 (0.107)	-0.054 (0.112)	-0.028 (0.120)
Chinese characters	1.499*** (0.534)	1.251*** (0.454)	1.687*** (0.523)	1.428*** (0.457)	3.278*** (0.791)	2.876*** (0.682)	3.506*** (0.700)	3.068*** (0.601)
Total trade	0.065 (0.043)		0.074* (0.039)		0.150 (0.139)		0.164 (0.130)	
Openness		0.031 (0.086)		0.001 (0.078)		-0.026 (0.159)		0.015 (0.171)
Constant	-3.521 (2.421)	-2.268 (2.378)	-0.201 (1.964)	1.465 (1.938)	4.183 (3.966)	8.379*** (1.409)	2.771 (3.893)	7.143*** (1.642)
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
R <sup>2</sup>	0.867	0.862	0.862	0.856	0.563	0.538	0.518	0.488
Adjusted R <sup>2</sup>	0.860	0.855	0.855	0.848	0.535	0.509	0.488	0.456
N	479	479	479	479	205	205	205	205
F-test of joint significance	0.229	0.234	0.220	0.234	0.051*	0.042**	0.401	0.725

**Table A2. Simultaneous equations modeling of contracted FDI and utilized FDI.** In this table we report results from simultaneous equations modeling of contracted and utilized FDI as a function of the stock of past FDI (Columns 1-4) or scale of recent FDI (Columns 5-8); uncertainty avoidance index (Columns 1-2 and 5-6) or power distance index (Columns 3-4 and 7-8); the interaction of the stock or scale of FDI with the Hofstede cultural measure (uncertainty avoidance or power distance); economic control variables; and a measure of the economy's external orientation (total trade or trade openness). We report at the bottom the p-value of the F-test for joint significance of the cultural measure and the interactive term of that cultural measure with the margin of FDI. Standard errors are reported in parentheses. \* denotes significance at the 10% level; \*\*, 5%; and \*\*\*, 1%.

	Extensive Margin of FDI - stock								Intensive Margin of FDI - scale								
	(1) C_FDI	U_FDI	(2) C_FDI	U_FDI	(3) C_FDI	U_FDI	(4) C_FDI	U_FDI	(5) C_FDI	U_FDI	(6) C_FDI	U_FDI	(7) C_FDI	U_FDI	(8) C_FDI	U_FDI	
U_FDI (t-1)	0.778*** (0.050)		0.779*** (0.050)		0.791*** (0.049)		0.790*** (0.049)		0.949*** (0.042)		0.943*** (0.042)		0.967*** (0.041)		0.969*** (0.041)		
C_FDI (t-1)		0.621*** (0.036)		0.637*** (0.036)		0.623*** (0.034)		0.638*** (0.035)		0.851*** (0.041)		0.879*** (0.041)		0.868*** (0.036)		0.888*** (0.036)	
FDI Margin (t-1)	0.955*** (0.343)	1.560*** (0.275)	0.934*** (0.343)	1.535*** (0.277)	0.125 (0.308)	1.190*** (0.247)	0.053 (0.313)	1.235*** (0.250)	0.158 (0.096)	-0.590*** (0.100)	0.161 (0.103)	-0.539*** (0.102)	-0.251** (0.124)	0.907*** (0.114)	-0.290** (0.133)	0.848*** (0.117)	
Uncertainty avoidance	0.007 (0.006)	0.001 (0.006)	0.007 (0.006)	0.001 (0.006)					-0.001 (0.004)	-0.023*** (0.004)	-0.000 (0.004)	-0.021*** (0.004)					
Uncertainty avoidance * FDI Margin (t-1)	-0.005 (0.004)	-0.002 (0.003)	-0.005 (0.004)	-0.002 (0.003)					-0.004* (0.002)	0.013*** (0.002)	-0.004 (0.002)	0.012*** (0.002)					
Power distance					-0.014* (0.008)	-0.011 (0.007)	-0.017** (0.009)	-0.009 (0.007)					0.000 (0.003)	0.007** (0.003)	0.000 (0.003)	0.006** (0.003)	
Power distance * FDI Margin (t-1)					0.009* (0.005)	0.005 (0.004)	0.011** (0.005)	0.004 (0.004)					0.003** (0.001)	-0.010*** (0.001)	0.003** (0.001)	-0.009*** (0.001)	
Tariff	0.000 (0.003)	0.001 (0.003)	-0.000 (0.003)	0.001 (0.003)	0.000 (0.003)	0.001 (0.002)	-0.000 (0.003)	0.001 (0.003)	-0.031 (0.019)	-0.050** (0.020)	-0.027 (0.021)	-0.035* (0.021)	-0.037* (0.020)	-0.033* (0.019)	-0.029 (0.021)	-0.022 (0.019)	
GDP	-0.018 (0.025)	-0.034 (0.022)	-0.027 (0.027)	-0.019 (0.024)	-0.025 (0.024)	-0.040* (0.021)	-0.038 (0.027)	-0.028 (0.023)	0.009 (0.036)	-0.050 (0.038)	0.007 (0.040)	-0.012 (0.041)	0.025 (0.036)	-0.041 (0.035)	0.035 (0.040)	-0.012 (0.038)	
Chinese characters	0.171 (0.175)	0.515*** (0.146)	0.224 (0.159)	0.359*** (0.135)	0.092 (0.179)	0.548*** (0.149)	0.144 (0.165)	0.402*** (0.140)	-0.098 (0.264)	0.462* (0.275)	-0.013 (0.256)	0.231 (0.262)	-0.172 (0.273)	0.575** (0.256)	-0.168 (0.265)	0.371 (0.245)	
Total trade	-0.008 (0.016)	0.027** (0.014)			-0.006 (0.016)	0.028** (0.014)			-0.026 (0.029)	0.025 (0.031)			-0.018 (0.029)	0.023 (0.028)			
Openness			-0.054 (0.071)	0.072 (0.061)			-0.080 (0.073)	0.049 (0.064)			-0.003 (0.106)	0.223** (0.111)			0.071 (0.105)	0.181* (0.100)	
Constant	0.929 (0.747)	-1.980*** (0.623)	0.890 (0.668)	-1.527*** (0.558)	2.120*** (0.656)	-1.281** (0.557)	2.310*** (0.620)	-0.873 (0.539)	2.221** (0.964)	1.029 (1.016)	1.527** (0.714)	0.775 (0.741)	1.769** (0.883)	-1.265 (0.851)	1.141** (0.575)	-1.208** (0.572)	
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	
R <sup>2</sup>	0.903	0.929	0.903	0.928	0.904	0.930	0.904	0.929	0.933	0.924	0.932	0.927	0.933	0.937	0.933	0.939	
N	310		310		310		310		82		82		82		82		
F-test of joint significance		0.540	0.743	0.601	0.767	0.194	0.039**	0.144	0.095*	0.143	0.001***	0.191	0.005***	0.309	0.324	0.304	0.356



**Table A3. Hofstede measures of corporate culture excluding Greater China.** In this table we report results from the regression of the commitment ratio on the stock of past FDI (Models 1-6) or scale of recent FDI (Models 7-12); uncertainty avoidance index (Columns 3-4 and 9-10) or power distance index (Columns 5-6 and 11-12); the interaction of the stock or scale of FDI with the Hofstede cultural measure (uncertainty avoidance or power distance); economic control variables; and a measure of the economy's external orientation (total trade or trade openness). We report at the bottom the p-value of the F-tests for joint significance of the cultural measure and the interaction of that term with the margin of FDI. Standard errors are reported in parentheses. \* denotes significance at the 10% level; \*\*, 5%; and \*\*\*, 1%.

	Extensive Margin of FDI - stock				Intensive Margin of FDI - scale			
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
FDI Margin (t-1)	-0.192 (0.129)	-0.145 (0.113)	0.208 (0.167)	0.277 (0.177)	-0.082*** (0.029)	-0.069*** (0.026)	0.165*** (0.043)	0.155*** (0.043)
Uncertainty avoidance	-0.007** (0.003)	-0.007** (0.003)			-0.003*** (0.001)	-0.003** (0.001)		
Uncertainty avoidance * FDI Margin (t-1)	0.003* (0.002)	0.003** (0.002)			0.002*** (0.001)	0.002*** (0.001)		
Power distance			0.004 (0.006)	0.005 (0.006)			0.001 (0.001)	0.001 (0.001)
Power distance * FDI Margin (t-1)			-0.003 (0.003)	-0.004 (0.003)			-0.002*** (0.000)	-0.002*** (0.000)
Tariff	0.001 (0.001)	0.001 (0.001)	0.001 (0.001)	0.001 (0.001)	-0.007* (0.004)	-0.006 (0.004)	-0.005 (0.004)	-0.004 (0.003)
GDP	0.009 (0.011)	0.009 (0.012)	0.017 (0.012)	0.020 (0.014)	-0.015** (0.007)	-0.007 (0.009)	-0.015** (0.006)	-0.011* (0.006)
Chinese characters	0.058 (0.075)	0.056 (0.079)	0.084 (0.078)	0.075 (0.081)	0.064 (0.063)	0.038 (0.087)	0.112*** (0.042)	0.090 (0.055)
Total trade	0.031 (0.021)		0.023 (0.027)		0.016 (0.024)		0.001 (0.020)	
Openness		0.011 (0.037)		0.029 (0.046)		0.047* (0.027)		0.027 (0.020)
Constant	0.073 (0.595)	0.823*** (0.297)	-0.542 (0.807)	-0.076 (0.407)	0.304 (0.611)	0.568*** (0.150)	0.375 (0.533)	0.343*** (0.079)
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
R <sup>2</sup>	0.270	0.266	0.261	0.261	0.203	0.222	0.381	0.390
Adjusted R <sup>2</sup>	0.226	0.221	0.217	0.216	0.112	0.133	0.310	0.320
N	298	298	298	298	79	79	79	79
F-test of joint significance	0.042**	0.049**	0.190	0.157	0.015**	0.020**	0.000***	0.001***