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THE IMPACT OF BUSINESS-GOVERNMENT RELATIONSHIP ON LOCATION CHOICE BY KOREAN FIRMS IN CHINA: A COMPARATIVE CASE STUDY

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ABSTRACT

Since China embarked on market-oriented reform in 1979, various kinds of economic zones have been set up to attract foreign direct investment (FDI). These economic zones often compete against each other for investment, offering better policies and creating more incentives. In most local economic zones, red tape is significantly reduced because of the establishment of local zone authorities with consolidated power to oversee FDI-related matters. Foreign invested enterprises (FIEs) need to deal with much less number of government agencies in these zones than outside these zones. But on the other hand, relationship with these zone authorities becomes crucial for FIEs targeting or operating in these zones. Prior research shows FIEs in China often make their location choices based on the preferential policies offered by different regions. But a neglected factor is that how the business-government relationship might affect foreign firms' location choice between these zones within the same locality. This paper studies the impact of the bilateral FIE-zone authority relationship on FIEs' location decisions. Drawing upon location literature and using data from case studies, the paper provides evidence on the impact of business-government relationship on two levels of location choice by Korean firms in China and advances propositions for future research.

Key words: Location choice, Business-government relationship, Korea, China

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INTRODUCTION

The establishment of business-government relations is a practical means by which firms (whether Chinese or foreign) have been able to reduce risk in operating in China. Foreign invested enterprises (FIEs) make their location decisions in China not only in response to the differences in policy and infrastructure development across different regions but also taking into account the relationship with local governments. While most of the existing research on the location choice of FIEs focused on the impact of traditional factors such as labour costs and market, how the relationships with Chinese governments affect location decision remain understudied for two major reasons. First, it is difficult to measure the business-government relationship and hence difficult to compare its impact with that of other easily measurable variables such as labour costs and market growth. Second, the Chinese bureaucracy is complex, and foreign firms often deal with multiple or many government agencies for different matters in one local area. Worse still, some FIEs may have to deal with multiple levels of governments (e.g. local, provincial, central) if they operate in a certain industry or their capital investment exceed a certain level. To reduce the complexity and allow the development of a conceptual model for studying the impact of business-government relationship, we focus our research on the dyadic relationships between FIEs and local government authorities with consolidated power in China's local economic zones.

The paper first provides a conceptual foundation, drawing on FDI location literature. Following a description of research design and background of target firms, the paper offers empirical case evidence on the impact of business-government relationship on the location choices by four Korean firms in the City of Suzhou in east China. Specifically, we study how the business-government relationship impacted on two levels of location decisions: first, Korean firms' choice of the city of Suzhou and second, their choice of one local economic zone over another within the same city. Based on the comparison of the case study data, the paper advances propositions and discusses the implications for future research.

CONCEPTUAL FOUNDATION

Studies on FDI location choice traditionally concentrated on four sets of variables, comprising of policy incentives, infrastructure development, market and factor endowments especially labour cost (Dunning 1993, 1998). There has been much research on policy variables as the locational determinants of FDI (Loree and Guisinger 1995, Nicholas et al. 2001, Zhou et al. 2002). Policy variables reflect governments' desire to alter the flows of FDI across different countries or regions through different tax regimes or non-tax incentives. Governments can also influence FDI spatial distribution within a country indirectly through infrastructure development. Previous research has shown the quality and cost of infrastructure as one of the most important factors influencing MNE location decision (Mody 1997, Zhou et al. 2002).

A salient feature of China's FDI inflows is the highly uneven regional distribution, with the FDI concentrated in coastal provinces where policies are more favourable to FIEs and infrastructures are better developed (Luo 1998, Zhang 1999). The Chinese government has adopted a region-based approach for FDI-related policies, aiming to channel FDI into different regions at different stages of economic reform (Ma 2000). Despite deregulation and privatisation, Chinese governments at multiple levels continue to play important roles in infrastructure projects, encompassing multiple roles of financier, supplier, customer and regulator (Ramamurti 2003). The government can therefore exert full control over both policy and infrastructure development and manipulate both variables to alter the flow of FDI across the country.

Another two sets of variables identified by Dunning (1993) are related to market opportunities and labour cost. In China, while most foreign companies entered during 1980s to take advantage of the abundant cheap labour, market-related variables like market size and market growth played a more significant role in attracting foreign investment since 1990s. The trajectory of FDI spatial distribution in China in the past two decades reflected the overall shift of FIEs' strategic mentality from cost-oriented towards market-oriented (Suh and Seo 1998). Throughout the 1980s the south China province of Guangdong took a disproportionately larger share of total inflow FDI, serving mainly as the low-cost manufacturing base for export-oriented Hong Kong companies (Sun 1998). Although Guangdong remained the largest recipient of FDI, other regions have gradually succeeded to attract more investment in the 1990s. Entering 2000, the gravity of China's economic growth has shifted to the Yangtze River Delta area, comprising Shanghai and major industrial cities of neighbouring Jiangsu and Zhejiang provinces. While FIEs used Guangdong and Pearl River Delta as a production base for exporting labour-intensive products, western MNEs favoured Shanghai and Yangtze River Delta for serving China's domestic market (Peng 2000a).

Apart from the traditional location factors, the development of economic zones played an important role in attracting FDI into China. The setting up of different economic zones over time mirrors the government's attempts to control the FDI geographic distribution, which has been generally proven a success (Hayter and Han 1997, Luo and O'Conno 1998). In 1979, four special economic zones (SEZs) were established in south China as economic laboratories in which policy experiments could be tried out on a geographically restricted area (Wall 1993). Since 1984, FDI was encouraged in 14 coastal open cities (COCs), including China's most important industrial cities such as Shanghai and Tianjin. They offered foreign investors an opportunity to gain access to China's most densely populated area with a relatively well-developed infrastructure and well-trained labour force. In 1985, three larger economic development zones (EDZs) were designated in Yangtze River Delta, Pearl River Delta and the Southern Fujian Triangle, and some of the special policies towards FIEs that had only been enjoyed by SEZs were made more widely available (Fukasaku et al. 1994).

Since late 1980s, to compensate the unbalanced development caused by the concentration of SEZs, COCs and EDZs in coastal regions, the central government allowed the creation of various types of economic zones by local authorities across the country (Hayter and Han 1997). Though appearing under different labels such as industrial parks, economic zones and export processing districts, these local zones are designated areas within cities or counties that offer a set of different policies for FIEs than the rest of the localities, compared to the city/region-wide coverage of FDI policies in SEZs, COCs and EDZs. It is the local not the central government who makes policies and regulations governing FDI in these local economic zones.

Many localities have more than one such zone, which often compete against each other for investment by creating better policy incentives. Prior research shows foreign firms often make their location choices based on the preferential policies offered by economic zones (Beamish and Wang 1989). But a neglected factor is how the business-government relationship might affect foreign firms' location choice between these zones within the same localities. Competition among local governments for FDI resulted in divergent regulatory regimes in local economic zones in the earlier stages of economic reform, when preferential policies were the most important consideration of FDI location choice. But there has been an increasing convergence of FDI policies since 1990s, particularly among the economic zones in the same provinces or cities, as local authorities realized that policy competition could only lead to a lose-lose situation. For the economic zones located within the same localities, therefore, policy incentives are no longer the major differentiation factor for their attractiveness. FIEs choose between different zones in the same localities based increasingly on non-policy considerations.

In most local economic zones, red tape is significantly reduced because of the administrative streamline with the establishment of a single powerful local authority to oversee all FDI-related matters. FIEs need to deal with much less numbers and diverse varieties of government agencies in these zones than outside these zones. But on the other hand, bilateral relationship between FIEs and these zone authorities becomes crucial for firms targeting or operating in these zones. The focus of this paper is the impact of FIE-zone authority relationships on FIEs' location choice of China's economic zones, as compared to the policy variable as well as traditional non-policy factors like infrastructure, labour and market.

RESEARCH DESIGN

A comparative case study approach (Yin 1989) has been employed to explore foreign firms' decision-making in choosing between China's economic zones within the same locality and build research propositions. This approach enables the researcher to explain a decision or set of decisions and the dynamics of change in these decisions (Schramn 1971) through the collection of detailed information from a range of sources about a particular institution or a number of organisations (Hammersley 1989). While it is impossible to generalise the findings from case studies to broader populations, multiple case study design can be used to achieve theoretical replication and assist in the process of testing theoretical propositions (Yin 1993). Previous research (Peng 2000b) has used this method to study the interaction between the Chinese state and the MNEs.

Case study research provides a detailed examination of an event (or series of related events) that exhibits (or exhibit) some identified general theoretical principle (Mitchell 1983). Cases are chosen predominantly for their ability to test and build theory rather than on the basis of their typicality (Stoecker 1991). The selection of target firms, therefore, should be based on their explanatory potential and not on their typicality or representativeness (Mitchell 1983). Based on the four embedded cases, this research will identify the plausible hypotheses that explain the decision making of foreign companies in China and allow subsequent studies to test these hypotheses.

Korean subsidiaries in China are selected for this study for two reasons. First, there are some similarities in the institutional factors in Korea and those in China, reflected in the common heritages in tradition and culture. Due to these common cultural backgrounds, Korean firms tend to understand the Chinese social institutions (e.g. *Guanxi*) better than western MNEs, showing more sensitive response to the differences in the institutional factors.

Second, both large high-tech and small-to-medium low-tech companies from Korea invested in China. This differs from other major FDI source countries in China, with the majority of Hong Kong firms are small and concentrate in low-tech industries while firms from western countries tend to be large and high-tech. The analysis of both large and small firms from one source country helps to minimize the impact of control variables such as size and industry.

The case study design was administered through semi-structured interviews conducted at four Korean manufacturing firms in Suzhou, a major industrial city about 80 km east of Shanghai. The city has been experiencing economic boom in recent years, with its two major economic zones attracting large volume of FDI. Located in the east part of the city, Suzhou Industrial Park (Park hereafter) was a joint initiative by Chinese and Singaporean governments. Started in 1994 with a planned area 70 sq km, the Park's GDP increased from 1,132 to 36,150 million RMB in 2003.

The inflow FDI also grew rapidly, with realized value of $US 1,205 million in 2003 as compared to $US 70 million in 1994 (Suzhou Statistical Yearbook 2004).

Suzhou New and High-Tech Zone (Zone hereafter), located in the west part of the city, was started in 1990 and approved by the central government as a national high-tech industrial development zone. In 1997, the Zone was approved as one of the first four industrial parks open to APEC members. Between 1992 and 1999, the Zone's GDP expanded from less than 100 million to 12 billion RMB (Suzhou Statistical Yearbook 2004). By 2001, there were more than 360 foreign enterprises including some world-famous multinational companies such as Epson, Dulex, Motorola, TDK and Sanyo, with a total investment of $US 3.5 billion. Thirty-nine Fortune 500 companies are involved in some ten projects, with an investment of $US 100 million in each project (Suzhou New and High-Tech Zone Investment Guide 2004).

Interviewees include Korean expatriates and Chinese managers. In each case, the main formal interview was conducted with senior managerial staff, including general manager, deputy general manager, HR manager and plant manager (see Table 1 for interviewees' detail). The main interviews constitute the backbone of the research, and data obtained were coded on a five-point Likert scale allowing a quantitative comparison of variables impacting the decision-making. The informal interviews and discussions were conducted with other key informants ranging from president to lower rank managers and workers, providing valuable supplementary information for in-depth case studies (Nichols 1991).

When selecting target firms, we first obtained from Suzhou Industry and Commerce Bureau a list of Korean firms operating in Suzhou and then contacted the firms on the list by phone and by personal referral. We selected our sample firms based on two criterions: first they must be manufacturing firms to minimize the impact of industrial variation, and second they must be located either in the Park or the Zone. Among the eight companies accepting our interviews, three were excluded from our study as two of them were located outside the local economic zones and one was a trading company. That resulted in five firms meeting our selection criterion, three in the Zone and two in the Park. We further excluded one company in the Zone which was too small (a family-run factory with less than 50 workers) and had too short a presence in Suzhou (less than five months in operation). That leads to the four firms under study, two each from the two local zones.

AS Company

Located in the Zone, AS is a wholly owned subsidiary of a Korean firm in advanced technology system (ATM) manufacturing industry, producing key LCD components, such as back light units for mobile phone manufacturers. In 2004, the company exported all of its products to customers in Korea and imported 100 per cent of high value-added equipments such as Ion Blower, Measuring Microscope and Dust Collector. The company aims to sell 50 per cent of its products in China by 2005 and started to source its main production material plastic sheet from 3M in Shanghai from the end of 2004.

KO Company

Also located in the Zone, KO is a wholly owned subsidiary of a Korean firm producing Hi-Fi for automobiles. The company was established in 2001 but spent the first two years in landscaping, building factory plants, installing and testing assembling lines. With all product and process technology transferred from Korean parent company, the company just started full-capacity operation at the time of interview in 2004. KO was confident in receiving 30 percent of its orders from parent firm and generating the rest 70 percent of sales in China.

SA Company

Located in the Park, SA is a wholly owned subsidiary of a Korean container component manufacturer, which is a part of SA Precisions and Industrial Group (a non-Chaebol affiliated industrial corporation) headquartered in Pusan. Established in 1996, SA's sales increased from $US 9.6 million in 1997 to $US 35 million in 2003, making it one of the largest suppliers of door hardware and door gasket for containers. Its major buyers include such Korean Chaebols as Jindo, Hyundai and Singamas, and major shipping lines in Western countries. SA's products have met industrial standards of countries like UK, US, France, Germany and Australia, making it difficult for rivals to compete in all major markets.

SU Company

Also located in the Park, SU Electronics Co. is the largest and the only Chaebol-affiliated company surveyed. Its Korean parent SU Group has nearly 70 years history and more than 40 affiliated companies around the world, covering a wide range of businesses including electronical industry, financial services, insurance services, trade, chemical and machinery industries. SU Electronics (Suzhou) Co. was set up in 1995 as a joint venture between SU Electronics Company and Suzhou Industrial Park Inc. By year 2003, the SU Suzhou company had nearly 3,000 employees and a total investment of US $153 million, of which Korean SU Electronics Company held 88 per cent. It is the only production base of white goods for SU Electronics Company in China, producing more than 100 products of various specifications in the four series of refrigerator, microwave oven, washing machine and air conditioner as well as their key spare parts. The Korean parent SU Group plans to turn SU Suzhou Company into the group's largest production base and R&D centre for white goods.

The four companies selected for the case study shows substantial differences in their history of operation in China, size of the workforce and investment capital. The history of the companies ranges from two to ten years, while the size of the investment capital ranges from US$1 million to US$ 153 millions. SU is the only joint venture while others are wholly owned subsidiaries. While AS and KO companies aim to sell most of their products in China, SA's major customers are more diversified in their regions, including US, Europe and Australia. SU both sells its products at the Chinese domestic market and exports to the rest of the world. Table 1 shows the major characteristics of the companies selected for the case study.

Table 1. Major Characteristics of Target Firms

	AS Company	KO Company	SA Company	SU Company
Year of Establishment in Suzhou	2003	2001	1996	1995
Member of Large Business Group or Chaebol	No	No	No	Yes
Number of employees as of 2004	about 150	about 100	about 250	about 2,000
Investment capital as of 2003	US$ 1 million	US$ 8 million	US$ 35 million	US$ 153 million
Main products	LCD components for mobile phone	Hi-Fi for automobile	container components	electronics home appliances
Main interviewee	Deputy General Manager Ms. Deng (Chinese)	Human Resource Manager Mr. Park (Korean)	General Manager Mr. Kim (Korean)	Plant Manager Mr. Tang (Chinese)
Key informants	General Manager (Korean); Sales Manager (Korean)	Plant Manager (Chinese); Deputy General Manager (Chinese)	Deputy General Manager (Chinese); President (Korean)	former Deputy General Manager (Chinese); Sales Manager (Korean)
Location	The Zone	The Zone	The Park	The Park

CASE ANAYSIS

Based on the field data, this section addresses the two research questions and advances two propositions. The first question examines why the target firms chose the city of Suzhou over other locations in China, comparing the role of business-government relationship with traditional location determinants. The second question investigates the impact of the same variables on the choice between the Zone and the Park in Suzhou.

Research question 1: the choice of the city of Suzhou

When asked about why the city of Suzhou was chosen over other locations in China, the interviews confirmed the importance of traditional factors like labour costs and market potential in the four target firms' location decision, though there were some variations in the weight of each variable (see Table 2). All the target firms established their operations in Suzhou mainly for the purpose of establishing a low cost production base for exporting, but the factor of labour costs intertwined with the consideration of local market potential in their choice of Suzhou. Neighbouring China's largest industrial and commercial centre of Shanghai, Suzhou offers easy access to overseas markets through Shanghai's airport and port facilities as well as to China's domestic market through the Yangtze River. The city is also endowed with skilled labour force, much better educated than the workers in southern province of Guangdong where the vast majority are migrant rural labours from inland provinces (Wei 1995). FIEs often chose Suzhou to exploit the cheap skilled labour as well as the easy access to the huge potential market of east China.

Table 2. The Importance of Different Factors in the Choice of the City of Suzhou

	AS	KO	SA	SU
Labour costs	5	5	5	4
Local market	5	4	4	5
Infrastructure	5	5	4	4
Policy	4	4	5	5
Relationship with local government agencies	3	3	3	3

Note: the interviewees were asked to rank the importance of each factor from low (1) to high (5)

AS, for example, generated all of its sales from selling the products (key LCD components) back to its customers in Korea in 2003, but the company was targeting at least 50 per cent sales within China by 2005. The company considered developing local market as important as exploiting cheap labour when locating in Suzhou. There has been significant increase of the demand within China, as the country's major shipping lines are no longer required to source from state owned enterprises. In the case of SU, it is the only Chaebol-affiliated company and much larger in size, with a stronger market-orientation than the other three firms in its choice of Suzhou. Since its establishment in 1995, SU had increased its sales in China from US$ 54 million in 1996 to US$ 1.2 billion in 2001. It has set up 12 sales agencies in China, five of which were in Yangtze River Delta. To better serve Chinese customers, SU has set up a 24 hours quick-to-doorstep service network and a toll-free hotline, pioneering the industry's after-sale service in China.

Policy and infrastructure were ranked as of high importance in all the four companies' location choice of Suzhou. The two local economic zones in which the four companies are located generally offer similar preferential policies to FIEs with the Park places more emphasis on attracting firms with advanced technology. Table 3 summarizes major policies offered by the two economic zones. A significant policy advantage for locating in the two zones in Suzhou is the management mode of customs clearance, known as 'one time declaration, one time documents checking, one time inspection'. Both zones have their own customs offices linking directly with the port and airport customs in Shanghai through an electronic logbook management system. The normal customs procedures for import and export at Shanghai ports do not apply to in-and-out cargos shuttling between the two local economic zones in Suzhou and abroad. With the ability to have import materials and export products declared at, inspected and released by the local economic zones, the location of Suzhou contributed significantly to the efficiency of logistics for these companies. The extensive and convenient transportation network Suzhou enjoys further enhanced the policy advantage. About 80 km away from Shanghai, Suzhou is within two hours' reach to Shanghai's ports and airports. It is close to National Highway No. 312, Shanghai-Nanjing Expressway and Shanghai-Beijing Railway. For FIEs targeting China's inland market, the city also provides easy access to one of the largest freight stations in Jiangsu province, Baiyangwan freight station, only 3 km away.

In comparison, all the interviewees did not think the relationship with local government as important as other factors. All stated that Suzhou government policies and procedures were transparent, streamlined and Suzhou officials were efficient. 'Perhaps because of 2, 500 years' of splendid culture and civilization, Suzhou people are much better educated and government officials are also much cleaner than places like Guangdong…' according to the deputy General Manager Deng of AS, who had previously worked in Guangdong for five years. This view of Suzhou's government agencies was concurred by the General Manager and Chairman Kim of SA, 'I came to Suzhou since 1996 and surprisingly you can hardly hear of serious corruption cases or charges involving Suzhou officials, this is not easy given the extent of corruptions these days in China…'. As compared to operating in other places, 'you do not need to spend too much time and efforts in relationship-building with governments here, because the policies are relatively clear and the officials are relatively clean', stated the HR Manager Mr. Park of KO Company. Consequently, compared to other factors, all the four companies did not take relationship with the local government as an important determinant in their choice of Suzhou (ranked 3 in Table 2).

Table 3. A Comparison of Major FDI-related Policies Offered by the Zone and the Park

	The Zone	The Park
Corporate Income tax	Tax rate 15% applicable for all FIEs. In addition two year's exemption from first profit-making year and half reduction (7.5%) for the following three years	Tax rate 15% applicable for all FIEs. Foreign-invested advanced technology enterprises certified by relevant authority can enjoy additional three years' preferential corporate income tax rate of 10%. FIEs who re-invest profits to increase the registered capital or to open up new FIEs with an operation period of no less than 5 years can be refunded 40% of the corporate income tax already paid for the re-invested amount. Those who re-invest in export-oriented or advanced technology enterprises with an operation period of no less than 5 years can be refunded all corporate income tax already paid for the re-invested part.
Value-added tax	Exempted	Exempted
Import tax and tariff	Machines, equipment, moulds and spare parts as necessary for production, equipments and building materials as necessary for construction, office items for self-use are exempted from tariff and import tax	Machines, equipment, moulds and spare parts as necessary for production, building materials as necessary for construction, office items for self-use are exempted from tariff and import tax
Foreign exchange	Foreign currency settlement system not required; Capital account can be integrated with general account; company can fully retain foreign currency in bank account	Capital account can be integrated with general account; company can fully retain foreign currency in bank account
Customs clearance	Cargoes declared, inspected and released at the Zone Customs, no need to go through customs procedure at Shanghai ports	Cargoes declared, inspected and released at the Zone Customs, no need to go through customs procedure at Shanghai ports

Research question 2: the choice of the local economic zone

The relative importance of the location factors discussed above changed, however, when the interviewees were asked why their companies chose one economic zone over another within Suzhou city. All the four companies singled out their relationships with respective zone authorities as a key determinant.

The choice of the Zone over the Park: the cases of AS and KO

For AS and KO companies, labour costs, infrastructure and policy were far less differentiation factors than their relationships with the Zone authority in their choice of the Zone over the Park in Suzhou (see Table 4). The two local zones were equally attractive in terms of infrastructure and policy. Labour costs were slightly more an important issue for AS (ranked 3) because it is engaged in high-tech advanced technology system manufacturing which requires hiring of skilled workers and engineers. The Park was set up earlier than the Zone and many Fortune 500 manufacturing MNEs have established their presence there, pushing the average wage for skilled labour higher in the Park than in the Zone, which had more labour-intensive projects. AS Company could not compete with giant MNEs in offering comparable wages in the Park, and therefore it chose to locate in the Zone where the wage was competitive. According to the deputy General Manager Deng of AS, although the workers can move freely between the two zones, the cheaper housing and living expenses in the suburbs surrounding the Zone made it less likely for the employees to move across the city to find a job with better pay in the Park. 'If we located in the Park, then we will have to pay a higher wage to compensate the higher housing expenses for the key employees or we face losing them', Deng explained.

Table 4. The Importance of Different Factors in the Choice between the Zone and the Park

	The choice of the Zone over the Park		The choice of the Park over the Zone	
	AS	KO	SA	SU
Labour costs	3	2	1	1
Local market	N/A	N/A	N/A	N/A
Infrastructure	2	2	2	2
Policy	2	2	2	1
Relationship with local zone authority	5	5	5	4

Note: the interviewees were asked to rank the importance of each factor from low (1) to high (5)

Nevertheless, in comparison to the firm-specific relationship with the Zone authority, all of these considerations were not important. Both AS and KO have had previous connections with the Zone Administrative Committee, the highest authority of the Zone administering all the FIE-related matters from utilities supply to customs clearance. Headquarter of AS Company set up its first wholly owned plant in Shenzhen SEZ in January 2002. The current deputy General Manager Deng, a native of Suzhou, was recruited into a managerial position of the Shenzhen plant at the start of the company. Deng quickly rose to the deputy GM position because of her superb performance and trust she earned from the Korean GM. In June 2002, Deng was sent to Korean HQ for a three month 'leadership training', during which time she convinced the HQ to target the rapidly developing market of Yangtze River Delta area in east China. Upon returning to Shenzhen, Deng paid a number of visits to her hometown Suzhou, where she discussed the Korean company's investment plan with her high school classmate Mr. Li, the Director of Office of the Zone Administrative Committee. Deng subsequently organized two visits by the current AS GM Mr. Kim to Suzhou, more specifically, to the Zone. Attracted by Suzhou's investment environment and convinced by the solid relationship between his trusted deputy Deng and Mr. Li, the Korean GM convinced the HQ to take a quick decision to establish the second wholly owned subsidiary, AS, in the Zone of Suzhou.

In the interview with Deng, the GM Kim joined briefly and said 'I did not even visit the Park, I just looked at the policy manuals of the two zones, and listened to her (Deng) report, plus four dinners with Mr. Li, …and then I decided this (the Zone) is the place we are going to stay… I trust her and she told me she trust Mr. Li and the Zone authority…it was just that simple.' Deng added. 'apart from a slightly nicer environment, the Park does not really offer much better policy, besides, we know the people (the Zone authority officials and officers) very well which made us feel comfortable, so we thought the Zone was a better choice…' The GM Kim's words represented much of the decision-making for the choice of the Zone, 'She (Deng) knows everybody, when she walked me into the Zone Administrative Committee building for the first time, I knew instantly she is bringing our company to her home, (she knows) not just Mr. Li there but her senior high school classmates, junior high school classmates and former colleagues… I trust she will make AS successful at her home.' Interestingly, 'investing at home' became a single most important reason for the company's choice, and it was the relationship with the Zone authority which made the deputy GM as well as the company feel like 'investing at home'.

For KO, it had established a good relationship with the officials from the Investment Promotion Bureau of the Zone when they were on a promotion tour to Korea. The Zone authority later invited the management of KO to visit Suzhou. During their stay in Suzhou, the Korean managers also visited the Park and talked to the officials of the Park authority about the company's investment plan. 'But we received much warmer welcome by the Zone authority perhaps because we did not have any previous connections with the Park authority', said the HR manager Mr. Park from Korea. After comparing the policy, costs, and business environment of the Park and the Zone, KO company did not find significant difference, which actually made it easier for the company management to reach a decision. 'It would be difficult to make a choice if the Park offered clearly better policies than the Zone', Mr. Park explained, 'because they (the KO company management) already favoured the Zone over the Park before visiting the Park.' The prior relationship with the Zone authority thus accounted much for KO's final choice of the Zone.

The choice of the Park over the Zone: the cases of SA and SU

The cases of SA and SU provide further evidence that the firm-zone authority relationship was much more important than other factors in the choice of local economic zones within the same city. Labour costs, especially the costs of skilled workers, are higher in the Park than in the Zone. A joint initiative of Chinese and Singaporean government, the Park's infrastructure was better developed than the Zone as it was set up earlier and received huge investment from Singaporean government. But in recent years the Singaporean government has stopped its investment in the Park and the Suzhou municipal government has invested more than 100 billion RMB in the Zone, which reduced significantly the disparity between the two local zones. At the time of the fieldwork, the infrastructure and environment of both the Zone and the Park were regarded as the first class among China's many economic zones, and both SA and SU did not view the infrastructure difference between the two as a major factor in their choice (see Table 4). As discussed above, policies offered by the Park and the Zone are similar (see Table 3), and they were not important consideration in the both SA's and SU's location choice. But both companies took their relationship with the Park authority seriously in their decision-making, which was given the highest ranking (5) in Table 4.

SA Company's relationship with the Park authority was developed through two channels. SA Group started its investment with two companies producing sport shoes and components in Dalian and Fushun, the two major industrial cities in northeast China province of Liaoning. The two plants were closed down after a few years' loss. But during its operation in Liaoning, SA Group's management developed a close relationship with some provincial officials, including Mr. Gao who is of Suzhou origin. When the company was looking for other places to invest, Mr. Gao introduced its chairman and GM to the Suzhou Industrial Park authority from his hometown.

SA management also learned about the Park from one of its major clients in container manufacturing business. This client firm has once considered investing in Suzhou and has had extensive contacts with the Park authority. Though the company eventually chose Shanghai, its managers felt they owed the Park authority of Suzhou because they received very warm welcome during their visit to Suzhou and continuously received assistance from the Park authority in seeking reliable local component suppliers. When SA was planing to move out of Liaoning, the client firm referred it to the Park authority and facilitated the relationship building between the two sides.

As the chairman and GM Kim of SA put it, 'we would perhaps never invest in the Park were it not facilitated by Mr. Gao and our client firm in Shanghai. We could have gone to Shanghai, Kunshan (a town about 40 km away from Shanghai, famous of the concentration of Korean investment projects) or even Jiaxin (a city of Zhejiang province about 100 km away from Shanghai).' Of course, Suzhou's investment environment is much better than Liaoning, according to Mr. Kim, 'but Chinese government officials' and our own client's referral made a lot difference in our choice of the Park over the Zone.' In 2004, SA Suzhou plant reached a capacity of producing 500,000 sets of door hardware and door gasket, making it one of the largest container components manufacturers for shipping lines around the world.

The case of SU also reflects the importance of the path-dependency in relationship-building with local governments. SU was invited by Chinese government to joint venture with a local state-owned refrigerator manufacturing firm in Suzhou, which was one of the largest in China during the early 1990s located on the site of the latter-established Park. Later the local partner went nearly bankruptcy and was arranged by the government to be taken over by the Suzhou Industrial Park Co., an asset management company of the Park authority. Although the Park authority was not existent when the company entered China, the current Chinese partner (Suzhou Industrial Park Co.) had extensive connection with many of the officials in the Park authority, and according to the Plant Manager Mr. Tang of SU, some senior managers of the Chinese partner held concurrently positions in the Park authority. 'Moreover, many of these people (senior managers of the current local partner) are the same people managing the former bankrupted refrigerator producer. So the Korean SU Company's relationship with the Park authority should really be dated back to the beginning of the JV.' Thus, a good relationship with its long-term JV partner, in this case, also contributed to the SU's close ties with the Park authority.

When the Zone was set up, SU management did consider relocating across the city to save costs on labour and production, given its large workforce of nearly 3,000 workers. But the relocation will incur significant costs. First, the large co-investment made by the Park authority and the company in establishing direct electric and water links between local utility companies and the SU plants will be lost. Second, relocation to a competing local economic zone will not only break up the established ties with the Park authority but also seriously damage the JV partnership because some top managers of the current JV partner are also the key personnel of the Park authority. 'The costs of losing a long-term JV partner (though the identity of the local partner changed, key managers remained intact) at this time cannot be worse, as the company is significantly increasing its sales in China's domestic market and needs a reliable local partner to help establishing the distribution network', according to Mr. Tang. Consequently, the company decided to stay in the Park and not to relocate.

Both the Zone and the Park authorities have consolidated power over various kinds of state enterprises like utility supply companies and government agencies including customs house. The purpose of setting up such a single authority for local economic zones is to achieve administrative streamline and cut the red tape to the minimum. The establishment of such zone authorities with a consolidated power facilitates the foreign investment, reducing the number of government agencies foreign firms have to deal with and the complexity of the procedures investors have to go through. But on the other hand, it also implies the relationship with these zone authorities can be an important factor in FIEs' location choice. Case studies from the four Korean firms revealed while traditional location factors attracted Korean investment to the city of Suzhou, it was the relationships between these firms and respective local authorities that played a much more significant role in their location choice of one local economic zone over another within the Suzhou city. Thus, we advance two propositions as follows:

Proposition 1:
Foreign firms make their choice of location in China at the city level based more on traditional location factors such as local policy, market, and infrastructure and labour costs than their relationships with local governments.

Proposition 2:
Foreign firms make their choice between local economic zones within the same localities in China based more on their relationships with local zone authorities than traditional locational factors.

CONCLUSION

The development of China's economic zones has become a crucial locational determinant of FDI. But it also resulted in a constantly changing institutional environment and uneven development of various economic zones across regions. To reap the policy benefits offered by these zones, FIEs need to rely on close ties with local zone authorities, which can be an important factor in their choice of one local zone over another within the same localities. There have been few empirical studies focusing on the location choice between local economic zones by FIEs in China. Particularly, there has been a lack of research on how the firm specific ties with local zone authorities might impact on the FIEs' location decision, as compared to traditional policy variables as well as non-policy factors such as labour costs, infrastructure and market.

Based on case studies of four Korean manufacturing firms in eastern China, this paper compared the importance of business-government relationship with other factors in four Korean firms' location decisions at two levels. While we found traditional factors like policy and infrastructure attracted the four target firms to the city of Suzhou, it was the relationships between these firms and zone authorities that played a more significant role in these firms' choice of one local zone over another within the same city. Future research should specify the levels of FDI location choice, whether it's a country, a region, a city or an economic zone with a city.

Second, we found a significant impact of business-government relationship, as compared to traditional location factors of market, policy and infrastructure. Future research using large sample database should explicitly incorporate the business-government relationship as a variable in location studies and test the propositions advanced above.

Finally, as a limitation of this study and a suggestion for future research, a comparative analysis of multinational firms from East Asia, North America and European countries will shed more light on the generalisability of the hypothesis. A comparative analysis of FDI from different economies in East Asia, i.e. from Japan, Korea, Hong Kong and Taiwan will also show the differences within a broad category of East Asian culture.

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