

INVESTMENT RISK MANGEMENT FOR CHINESE SMALL-MEDIUM ENTERPRISES INVESTING IN LAO PDR AGRICULTURAL SECTOR

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Abstract

The Chinese investment is currently one of the top three investment countries, besides Thailand and Vietnam, which came to invest their multi-million US dollars in Laos, and many projects are investing in the agricultural sector. The development of Chinese investment in Lao PDR is due to number of reasons. Although there is an increasing trend of investment from China as well as other neighbouring countries, many issues related to investment have also seen increasing.

The objectives of this research are to analyze Foreign direct investment (FDI) risks Chinese Agri-investment Small and Medium-sized Enterprises (SMEs) are facing. And formulate appropriate investment risk management suggestions to Chinese Agri-investment SMEs who are investing in Lao PDR. A lot of Chinese SMEs are attracted by both China's and Lao's FDI policies. and Lao's natural resource, its cheap production factors, and short geographical distance. However, while these Chinese SMEs arrived Lao, they find out there are very much different from what they thought before. 148 respondents repounded to the questionnaires launched during the meetings. Respondents were classified into four clusters. Data were analyzed by statistical program SPSS to show significant values and correlations. The study shows that Investment risk is no longer a general concept, and there are different definitions of different types of investment SMEs. And the formulated strategies can bring positive impact on Chinese SMEs who has investment in Lao agricultural sector, and who are going to invest in Lao agricultural sector. This important information can reflect both investors and communities' perspective on investment and will help suggesting solutions for the so call 'win-win solution' for sustainable agricultural development.

Keywords: Investment risk management, Chinese Small and Medium-sized Enterprises, Agri-investment, Lao PDR.

Introduction

Since the New Economic Mechanism (NEM) was introduced in 1986, Laos has been in transition from a centrally planned economy to a more market-oriented economy. Gradually, price controls were removed, socialist cooperative farming abandoned as farmers were allowed to work on their plots and take ownerships, the exchange rate system was unified, government's monopoly on trade removed, the number of state-enterprises reduced, and establishment of private firms allowed. Foreign capital inflows are important sources of investment finance for low income developing countries like Laos. However, massive foreign capital inflows also may have adverse economic effects (Kyophilavong, 2009).

Agriculture is a high priority area in triggering overall growth, reducing poverty, ensuring food security and meeting the environmental goals. Agricultural investment is the most important and most effective strategy for poverty reduction in rural areas, where the majority of the world's poorest people live (World Bank, 2008; APO, 2012). This increase in FDI inflows has been driven by integration with Laos' rapidly growing neighbors, Thailand, China and Vietnam. Through the 1990s and 2000s, the region has become better integrated, and demand has increased for raw materials and agricultural commodities, attracting foreign investors to the agriculture sector in Laos (Wright, 2007).

In most of the developing countries, performance of SMEs has always been one of the key issues since they are less productive and faces many constraints (Davidsson, 2004). And in many countries they face the constraints of technological backwardness, lack of human resource skills, weak management systems and entrepreneurial capabilities, unavailability of appropriate and timely information, insufficient use of information technology, poor product quality. As a result, there exists a low level of performance. Along with rapidly increased outward FDI from China, there are many risks rising also. In order to improve the quality of Chinese outward FDI, Chinese enterprises must understand what investment risks they are facing in hosting countries, especially, after commodities price dropped.

Most of Chinese outward FDI into agricultural sector are SMEs. SMEs are vulnerable to product, market and technological changes because they are not diversified and are often one product, one market companies (Buckley, 2007). In this case, the SMEs are going through a very difficulties time. Most of them are bankrupt, and only few are survived.

Objectives of Research

The objective of this research is to analyze Foreign direct investment (FDI) risks Chinese Agri-investment Small and Medium-sized Enterprises (SMEs) are facing. And formulate appropriate investment risk management suggestions to Chinese Agri-investment SMEs who are investing in Lao PDR.

Conceptual Model

There are 18 Independent variables regarding to the investment risk management, which namely as follow: Foreign direct investment-related policies of host countries, Level of corruption in the host Government, Social security in the host country, Is financing method single or multiple, Inflation and exchange management, cultural difference, language barrier, Technical level of workers, Whether the company's products have unique characteristics that can be distinguished from those of other companies, Investment size of the company, Relationship between the company and the local community, Length and educational background of senior management, Higher education and overseas experience of senior management, Staff training, High-level meetings, Sales markets and major competitors, Network of relations between the host country and the home country and between the various branches of the host country, Are there existing investment risk management strategies within the company.

These 18 independent variables are defined from literature review. And they are all shown on the questionnaire as Characteristics of Chinese SMEs and Current investment practice. This aims to collect data and find out the correlations between these 18 independent variables and investment risk management.

Research Methodology

This research is both qualitative and quantitative. It is a result of triangulation of both qualitative and quantitative research methods that make possible the gathering of different kinds of data. The qualitative methods allow a deeper understanding of the research subject to formulate the appropriate investment risk management to Chinese Agri-investment SMEs who are investing in Lao. Quantitative methods will help to bring out empirical data that both complement and authenticate the qualitative analysis and conclusions. The basic assumption of all triangulation is that the weaknesses of each single method are compensated by the counter-balancing strengths of another. This being a case study research means that the research will be much more focused and limited in scope to be managing within the time allowed and resources available. The methods used intend to provide an objective, unbiased evaluation of data.

This research has been divided into three steps, the first step was pre-test questionnaire. To ensure content validity, the research questionnaire were reviewed and confirmed by three experts in the field of management specifically investment risk management. In order to ensure the reliability of the

survey results and the authenticity of the collected data, the reliability analysis and validity analysis of the questionnaire were carried out through the questionnaire pre-test before the formal survey, because the total sample size was 148 SMEs, so about one fifth, which is 30 SMEs were selected for the questionnaire prediction. The questionnaires were printed in Chinese as the interview are Chinese. The second step was conducted formal interview those 148 SMEs. There are the regular conference set up by Chinese government for those SMEs who has Agri-investment in Lao, Myanmar, and other south Asian countries. The questionnaires were distributed during the annual conference. The third step was to analysis the data collected by questionnaire.

Relevant data of 148 Chinese Small-Medium Enterprises (SMEs) Invest in Lao PDR Agricultural Sector from 236¹ SMEs were selected to analyze the main factors affecting agricultural investment in Lao PDR from the perspective of the enterprises. Preliminary investigations were made on characteristics of Chinese Agri-investment SMEs who are investing in Lao and their current investment practice. And then, followed by analyze what investment risks Chinese Agri-investment SMEs are facing. Cluster analysis is a statistical technique that sorts observations into similar sets or groups. Correlation analysis can be used to verify the linear relationship between two variables. From the correlation coefficient r , we can know whether the two variables are linear, the strength of the linear relationship, and whether it is positive correlation or negative correlation.

Descriptive research method was applied in this study using the interview schedule technique and focus group discussion to gather the data and other pertinent information needed. Multiple regression analysis was used in the presentation of results and discussion.

Research Results

Through two-step cluster analysis, the sample size is divided into four clusters. The proportion of valid samples in the first cluster was 25.7, the second cluster was 33.8%, the third cluster was 14.9% and the fourth cluster was 25.7% . The size of the four clusters of cases is not too large or too small, the distinction is good. It has not reached a good degree and needs to be further tested and optimized.

The first cluster, invest in single short-term cash crop. The second group, invest in single long-term cash crop, the third group, invest in multiple cash crops, and the fourth group, multiple types of investment which means not only invest in agriculture sector but also other sectors.

Table 1 Four cluster size and characteristics

	Numbers of SMEs	Characteristics
Cluster1	38	Invest in single short-term cash crop
Cluster2	36	invest in single long-term cash crop
Cluster3	39	invest in multiple cash crops
Cluster4	35	multiple types of investment which means not only invest in agriculture sector but also other sector
Total	148	

According to the correlation analysis, the first category, who are invested in a single short-term crop, the correlation between the independent variable **Sales markets and major competitors**, and the impact on the risk of agricultural investment in Laos (Pearson correlation) was 0.630**, with $P(\text{sig}) < 0.01$ was significant. As a result, SMEs that invest only in a single short-term crop, such as vegetables and fruits, have a relatively weak ability to resist risk, the Sales markets and major competitors have the greatest impact on their investment risk.

¹ According to Department of Commerce of Yunnan provincial, there are 236 Chinese Small-Medium Enterprises Invest in Lao PDR Agricultural Sector that are recorded on official list up to 2019.

The second category, who are invested in a single long-term crop. The correlation between the relevant investment policy, the degree of corruption of the host government, the way of financing, the technical level of workers and the degree of impact of the relationship with the local community on the risk of agricultural investment in Laos and the p (sig) values are (0.708, 0.000); (0.579, 0.000); (0.362, 0.030); (0.718, 0.000); (0.589, 0.000); respectively. Where P value is less than 0.01 is the significant correlation level, P value less than 0.05 is greater than 0.01 is the correlation level. For such single long-term crop investment SMEs, rubber and coffee for example, **the host country's foreign direct investment policy, the degree of corruption of host government officials, the financial chain, the diversity of financing, the skills of workers and their relationships with local communities** have the greatest impact on their investment risk.

The third category, who are invested in multiple crop. Among them, the correlation of the relationship network between the host country and the home country and the influence of the relationship network between the various branches of the host country on the risk of Lao agricultural investment was 0.882, and $P < 0.001$ was the significant correlation level. Thus, for such companies, the more stable the **sales network between the host country and the home country**, and the better the network establishment between the host country branches, the greater the profit they will make.

For the fourth category, who are having multiple investment, the correlation between **the time of high-level performance, the level of high-level education, and the degree of influence of high-level meetings and staff training** on the risk of Lao agricultural investment were (0.538, 0.001); (0.553, 0.001); (0.543, 0.001); (0.744, 0.000); respectively. where P value less than 0.01 was the significant correlation level. Therefore, for such SMEs, the longer the senior level performs its duties, the more the overseas background senior level have, the more frequent the senior level meetings, and the stronger the staff training mechanism is, the more profitable will be.

In summary, the 18 independent variables having different impact on investment risk management for each SMEs cluster.

Table 2 Comparison of Investment Risk Impact on Each SMEs

	IDV 1	IDV 2	IDV 3	IDV 4	IDV 5	IDV 6	IDV 7	IDV 8	IDV 9	IDV 10	IDV 11	IDV 12	IDV 13	IDV 14	IDV 15	IDV 16	IDV 17	IDV 18
1 st categories																√		
2 nd categories	√	√		√				√			√							
3 rd categories																	√	
4 th categories												√	√	√	√			

Conclusion and Discussion

Investment risk is no longer a general concept, and there are more specific definition of different types of investment enterprises. At the micro-level, the investment risks are defined more specifically. For the SMEs invested in a single short-term crop, market and the main competitors are their biggest risk of Lao agricultural investment. For the SMEs invested in a single long-term crop, FDI-related policies of host countries, Level of corruption in the host Government, Technical level of workers and Relationship between the company and the local community are their risks of Lao agricultural investment. For the SMEs invested in multiple crop, Network of relations between the host country and the home country and between the various branches of the host country are their risks of Lao agricultural investment. For the SMEs having multiple investment, Length and educational background of senior management, Higher education and overseas experience of senior management, Staff training and High-level meetings are their risks of Lao agricultural investment.

Implications and Recommendations

Chinese agricultural enterprises cannot only get cheap land lease from the local government, but also get alternative planting subsidy from the government in the process of investment in Laos, which are all the factors that attract many agricultural enterprises to invest. However, because of the backward economy and weak infrastructure construction in the investment areas, enterprises need to invest a lot of funds in the construction and improvement of infrastructure such as road repair, wiring and electricity and water supply in agricultural farming areas in order to ensure normal agricultural production and life, thus greatly increasing the operating costs of enterprises.

In recent years, agricultural prices have remained low, with the vast majority of Chinese companies that have invested in long-term crops, such as rubber, coffee and tea, especially in agricultural production. Many enterprises, because of the lack of understanding of the two countries' agricultural products export and loan application system, blindly expand the scale of production and operation, resulting in a serious shortage of funds, business operation is difficult, but also affect the business performance of enterprises.

According to the World Bank, performance of Chinese FDI is low rank, which is considered as ineffective investment, and it is getting worse since the commodities price dropped. They cannot distinguish among investment risks which are more important for them, which is part of reasons of poor performance.

Therefore, according to this research, even there are many risks for investing in Lao agricultural sector. It does not mean one company has to face them all, in another words, some risks are important to certain companies, and some risks are less important. Adopting the formulated strategies, the Chinese SMEs would understand their situations more specifically.

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