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Chinese Outward Foreign Direct Investment in Developed
and Developing Countries: Converging Characteristics?

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Abstract

The spectacular surge in Chinese outward foreign direct investment (OFDI) has been reinforced by China's accession to the WTO (2001). The understanding of their determinants remains a key theoretical question, in particular whether they confirm the standard conceptual framework - 'ownership', 'location', 'internalisation' (OLI) and 'linkages' (augmenting competences by learning). The paper argues that the determinants of Chinese OFDI change over time and converge toward global strategies, via a comparison between Chinese OFDI in developed countries (based on an original database of 1800 investment operations in Europe from 2002 onwards) and in developing countries (Sub-Saharan Africa, Latin America). While their impacts indeed vary according to countries' contexts, Chinese OFDI in developed and developing countries converges toward complex and similar motives, become more mature through the combination of various modes of entry (greenfield and mergers-and-acquisitions), and exhibit more commonalities than differences. The comparison thus demonstrates that while the determinants of Chinese OFDI in developed countries were initially access to their markets, they now include efficiency-seeking motives (dispersing design, R&D and production) and assets-seeking (or augmenting assets) motives, the latter's prevalence in developed countries (e.g., patents, skills, brands) remaining a contrast with developing countries. Chinese OFDI in developing countries is mostly driven by resource-seeking motives (strategic inputs for China's growth), but also in resource-endowed developed countries (Australia, Canada). Large investments are driven by Chinese state-backed firms both in developed and developing countries. The growing number of Chinese small and medium private enterprises which invest in developing countries (e.g., Sub-Saharan Africa) shows that market access has increasingly become a determinant of OFDI, together with efficiency - and assets-seeking motives - rising labour costs in China being incentives for relocating abroad, in particular in labour-intensive sectors where competitiveness is driven by prices. Chinese firms often conduct these various strategies simultaneously.

Keywords: China; foreign direct investment, Europe; Sub-Saharan Africa

JEL Classification: F21; F23; O53; O55

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1. Introduction²

The surge in Chinese Outward Foreign Direct Investment (OFDI) flows began at the millennium after China entered the World Trade Organization (WTO) in December 2001, and was driven by the development of the Chinese economy - hence the importance of push factors - and the rise of Chinese firms, which became major investors abroad. A key theoretical question is therefore to understand whether Chinese OFDI confirms the OLI (‘ownership’, ‘location’, ‘internalisation’) standard conceptual framework regarding the determinants of foreign direct investment (FDI) (Dunning, 1981), and its extension through a resource-based view of the firm: the latter assumes that companies go overseas in order to get access to a resource that is not otherwise

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available at home, the objective being the enhancement of international competitiveness (Mathews, 2006; Kaplinsky and Morris, 2009a).

The paper argues that the determinants of Chinese OFDI change over time and converge towards global strategies, via a comparison between Chinese OFDI flows in developed countries (based on an original database covering about 700 Chinese groups in greater Europe, i.e. including non-EU countries, which have realised about 1800 operations of investment over 2002-2012) and in developing countries (mainly Sub-Saharan Africa). Indeed, while their impacts (positive and/or detrimental) always vary according to countries' contexts, the characteristics of Chinese OFDI in developed and developing countries over time exhibit an increasing convergence, and more commonalities than differences.

Differences may stem from differences in levels of development and assets that Chinese firms can pick up. An important difference is the prevalence in developed countries of the strategic asset-seeking motive (e.g., patents, codified and tacit knowledge, management capabilities, marketing skills, brands or goodwill), in contrast with developing countries. The resource-seeking motive that predominates in developing countries, however, also prevails in resources-endowed developed countries (e.g., Australia, Canada). Large investments are driven by Chinese state-backed firms both in developed and developing countries.

Indeed, commonalities increasingly appear across Chinese OFDI. Firstly, they rapidly converge from contrasted motives (e.g., access to markets in developed countries vs. access to natural resources in developing countries) to complex and similar motives.

Secondly, Chinese investments become more mature through the combination of various modes of entry (e.g., mergers-and-acquisitions), even if *greenfield* investments still predominate.

Thirdly, large state-backed enterprises, which were the first to secure official support to go abroad, are now outnumbered by private companies, notably small and medium enterprises that aim at escaping China's domestic constraints. In addition, while the impacts of Chinese OFDI on some developing countries are important at a macro scale due to their economies' small size and institutional weaknesses (and are crucial in such sectors as mining, energy or construction), such macro impacts are also significant in developed countries for some sectors (e.g., telecom equipment, solar panels) or regions (e.g., industrial parks), even if they are still limited.

The comparison thus demonstrates that the determinants of Chinese OFDI in developed countries were initially access to their markets along with the building of trade-supporting networks. They now include assets-seeking (or augmenting assets) motives, and increasingly efficiency-seeking motives by dispersing design, research-and-development (R&D) and production in Chinese global investments, with these motives being more and more interlinked.

For their part, the determinants of Chinese OFDI in developing countries mostly are the access to primary commodities that China views as strategic inputs for its growth, and they are mostly implemented by state-backed large enterprises. However, market access has increasingly become a driver of Chinese investment, as shown by the growing number of Chinese small and medium private enterprises that invest in developing countries, particularly Sub-Saharan Africa. The efficiency-seeking motive also

increases, as Chinese firms harness abroad assets that foster their expansion at home or overseas - rising labour costs in China being incentives for relocating abroad, in particular in labour-intensive sectors (e.g., textile-clothing) where prices still are core criteria of competitiveness. Chinese firms often conduct these various strategies simultaneously.

The paper is structured as follows. Firstly, it summarises the main elements of the theoretical literature on the determinants and characteristics of foreign direct investment. Secondly, it presents key facts regarding Chinese FDI in developed and developing economies, with a focus on Europe and Sub-Saharan Africa respectively. Finally, it analyses the differences and similarities between Chinese FDI and explains the increasing convergences of determinants and characteristics of Chinese investments.

2. The theories of determinants and characteristics of outward foreign direct investment

2.1. The difficulty in defining foreign direct investment

Foreign direct investment is not easy to define, and therefore is difficult to compute. There are different forms of international financial flows or development finance: e.g., direct investment; equity investment or portfolio flows; aid, and debt. Direct investment and equity investment confer on the investor the ownership of assets. Bond issues and loans produce a regular stream of payment obligations, while the return on direct and equity investment is determined by the financial performance of the investment. Direct investment refers to the purchase or construction of productive capacity in a country by a firm outside the country.

Defining a certain capital flow or asset as ‘investment’ bestows certain rights on foreign investors, which is supposed to facilitate foreign investment. However, the macroeconomic management of capital flows of magnitude beyond the control of national governments may be difficult. The volatility of capital flows may affect domestic financial stability; hence the definition of investment matters to national laws and international agreements regarding foreign direct investment: it delineates which assets or investment flows are covered by national laws.

At the global level, the term of ‘investment’ does not have a fully accepted meaning. The internationally accepted method for classifying and recording cross-border foreign investment flows for balance-of-payments statistics distinguishes direct investment, portfolio investment, financial derivatives and other investment. National laws and International Investment Agreements also provide definitions of ‘investment’ and ‘foreign investment’, which may differ from the balance-of-payments definition. It is therefore not easy to define investment, which create problems of homogeneity and comparability of FDI data, as highlighted each year by the UNCTAD World Investment Report (e.g., UNCTAD, 2005).

For data collection purposes, FDI has been defined as involving an equity stake of 10% or more in a foreign enterprise. According to the 2004 World Investment Report (UNCTAD, 2004), FDI is defined as “an investment involving a long-term relationship and reflecting a lasting interest and control by a resident entity in one economy (foreign

direct investor or parent enterprise) in an enterprise resident in an economy other than that of the foreign direct investor”.

FDI has three components: equity capital, reinvested earnings and intra-company loans. Equity capital is the “foreign direct investor’s purchase of shares of an enterprise in a country other than its own”. Reinvested earnings “comprise the direct investor’s share (in proportion to direct equity participation) of earnings not distributed as dividends by affiliates, or earnings not remitted to the direct investor”. Such retained profits by affiliates are reinvested. Intra-company loans or intra-company debt transactions refer to “short- or long-term borrowing and lending of funds between direct investors (parent enterprises) and affiliate enterprises”. UNCTAD also mentions non-equity forms of investment (e.g., subcontracting, management contracts, franchising, licensing and product-sharing).

There are various types of FDI: *greenfield* FDI (new investments, new assets), joint ventures, and cross-border mergers-and-acquisitions/M&As (the consolidation of different companies into one entity - a merger - or the acquisition of existing assets, e.g., via privatisations): FDI may imply the direct entry of foreign firms, or the acquisition of existing firms. Privatisations are foreign direct investment if they imply an acquisition of more than 10% equity share.

FDI flows are also to be distinguished from FDI stocks. According to the UNCTAD World Investment Reports (e.g., 2004), FDI flows comprise capital provided (either directly or through other related enterprises) by a foreign direct investor to an FDI enterprise, or capital received from an FDI enterprise by a foreign direct investor. FDI stocks refer to the value of the share of the capital and reserves (including retained profits) attributable to a parent enterprise, plus the net indebtedness of affiliates of parent enterprises. FDI stocks are often estimated by either cumulating FDI flows over a period of time or adding or subtracting flows to an FDI stock that has been obtained for a particular year from national official sources or the IMF data series on assets and liabilities of direct investment.

2.2. The various determinants of foreign direct investment

The literature distinguishes many motives that incite firms to invest across national borders.

Firstly, these determinants refer to characteristics of host countries, e.g., market-related characteristics such as their growth rate or the policies they conduct. Growth in the host country appears to be a positive determinant of FDI (Calderon *et al.*, 2004). For example, Ajayi (2004) identifies the following list of determinants: size of the market and growth; costs and skill of the labour force; availability of good infrastructure; country risk; openness of the economy; institutional environment; availability of natural resources; concentration of other investors (agglomeration effects); return on investment; enforceability of contracts and transparency of the judicial system; macroeconomic stability. In contrast, governance failures, problems of policy credibility, macroeconomic policy failures and poor liberalisation policies deter FDI flows.

The existence of regional arrangements (the European Union is here a prominent example), which increase the size of markets, may be a positive determinant of FDI.

Common membership in a regional integration agreement of a host country with a source country may substantially increase FDI from that source. These positive impacts, however, are fragile, as multilateral or regional trade arrangements and policies, e.g. preferential trade policies or North-South agreements, may be put to an end, as underscored by UNCTAD (2006) regarding the ending in 2005 of the quotas established under the Multi-Fibre Arrangement (MFA), which contributed to divestment in the garments industry in some Sub-Saharan African countries: preferential market access is not in itself sufficient to retain manufacturing FDI in a context of global competition. The link between regional integration and outward FDI, however, is complex (Blomström and Kokko, 1997); it remains limited for the regional heavyweights such as Brazil, China, India and South Africa (Kubny *et al.*, 2008).

Also, among key determinants of FDI that refer to particular characteristics of the host countries are their structural or geographic conditions, e.g. the presence of natural resources, or locational advantages, such as the proximity with important markets. Landlocked countries are here particularly affected by geographical disadvantages, e.g. transportation (UNCTAD, 2003).

The existence of a skilled labour force in the FDI recipient country also favours the attraction of FDI. In contrast, the lack of these determinants may create low-equilibrium traps: a lack of human capital has a negative impact on FDI and a lack of FDI has a negative impact on the incentives to acquire education (Faini, 2004). Human capital and local skills in recipient countries are increasingly viewed as key determinants of FDI. Human capital also makes that host countries gain maximum benefits from FDI.

The policies implemented by host countries are essential determinants of FDI. Openness to FDI is an attractor of FDI (Agosin and Machado, 2007). Taxation policies are thus important drivers of FDIs, which are attracted by lower corporate taxes, as well as higher productivity (Razin and Sadka, 2007 for OECD countries). Likewise, trade policies, e.g., trade openness, play a crucial role in fostering FDI, or other policies such as the establishing of export processing zones. Trade liberalisation fosters inward investment: here trade and FDI may be viewed as complements.

The importance of policies in the recipient countries is also underscored by the international financial institutions (IFIs), the IMF and the World Bank. For the IFIs, 'good policies' and market-related determinants typically attract FDI, i.e. political and macroeconomic stability, firm commitment to economic reform, sound monetary and fiscal policies, appropriate exchange rate policies, lack of obstacles to private sector activities, trade openness, export-oriented trade strategies, open policies to international flows of services and knowledge. Privatisation is typically a policy that may attract FDI. The government policies that constitute positive determinants are, e.g., macroeconomic stability, efficient institutions, political stability or a 'good regulatory framework' (Asiedu, 2006). Monetary and exchange rate policies may foster FDI and poor monetary and exchange rate policies may hinder FDI, especially the recurrence of inflationary episodes, opaque monetary policies or the existence of parallel market as signals of distortions (Rogoff and Reinhart, 2003). In turn, macroeconomic instability, investment restrictions, a weak regulatory framework, underdeveloped financial systems, corruption and political instability, high country risk appear to have a negative impact on FDI (Ndikumana, 2003).

As for investment in general, uncertainty is indeed an important deterrent of FDI: risk is an important constraint on FDI, because it implies high premium. In such contexts, investors therefore exhibit a preference for the status quo (Fernandez and Rodrik, 1991). The ‘reputation’ of a country matters, and regions where investors have a negative perception of it tend to receive less investment, or investment only in specific sectors (such as primary commodities, e.g., oil). Corruption may therefore deter FDI, and it may even be argued that it influences the type of FDI and contractual arrangements: in countries with pervasive corruption, the value of having a local partner increases in order to bypass bureaucracy, while corruption decreases the protection of investor’s assets (Smarzynska and Wei, 1999). Sub-Saharan Africa global share of FDI has thus lagged behind other regions in the world due to perceptions of high corruption and weak governance, which have combined with poor infrastructure - poor infrastructure in recipient countries being typically detrimental to FDI.

Finally, in a context of global competition for the attraction of FDI, the determinants of FDI are not only absolute but relative to other regions, and they are to be distinguished according to absolute and relative terms: a country may improve infrastructure, institutions, regulatory framework, but FDI may remain stagnant if other regions are more attractive.

2.3. A key theory of the determinants of foreign direct investment: the ‘Ownership, Location and Internalisation’ (OLI) framework and its extensions

Secondly, the determinants of FDI are also related to characteristics and strategies of the investing firms. FDI can be viewed as the expression of a trade-off within the investing firms: firms choose between modes of entry, e.g., direct entry, or acquisition of existing domestic firms in the host country (Mattoo *et al.*, 2001). Distinctions between import-substituting and export-oriented FDI, or horizontally and vertically integrated FDI may be here viewed as canonical.

Import-substituting FDI may be motivated by trade barriers and tariff-jumping: trade and capital movements are here substitutable (Blomström and Kokko, 1997). Another motive for FDI is that in order to compete in a foreign market - which local firms know better - the firm must possess some intangible assets that provide it with a competitive edge (e.g., technological expertise). Multinational firms here ‘internalise’ their international operations by establishing foreign affiliates, which entail less transaction costs (Blomström and Kokko, 1997).

Four categories of determinants of FDI are widely used in the literature, in particular by UNCTAD (e.g., UNCTAD, 1998; see also Odenthal, 2001): 1) market-seeking investments refer to the access to new markets that are attractive, e.g., due to their size or growth; 2) efficiency-seeking investments aim at taking advantage of cost-efficient production conditions (cost and productivity of the local workforce, the cost and quality of infrastructure services - transport, telecommunication -, administrative costs, and focus on sectors where products are produced for regional and global markets, and competition is based on price (e.g., textiles and garments, electronic or electrical equipment, etc.) and not on quality differentiation; 3) resource seeking investments aim at exploiting endowments of natural resources, which firms usually choose on the basis of differences in production cost in different locations; 4) strategic-asset seeking investments are oriented towards man-made assets, as embodied in a highly-qualified

and specialised workforce, brand names, or shares in particular markets - e.g., cross-border M&As, whereby a foreign firm takes over the entire or part of a domestic company that is in possession of such assets.

For Kubny *et al.* (2008), market-seeking FDI aims at serving the local market of the host country and involves a horizontal replication of similar production lines in different locations. Efficiency-seeking vertical FDI is motivated by international cost differentials and segments the value chain through relocating specific stages of the production process to where they are most cost-effective. Horizontal FDIs predominate when relative factor endowments and relative prices are similar in the home and the host country, and vertical FDI predominate when relative factor endowments vary. Kubny *et al.* thus argue that trade and horizontal FDI are substitutes, while trade and vertical FDI are complements. It may be added that when multinational corporations are resource-seeking, such as in Sub-Saharan Africa, human capital seems less important for attracting FDI: human capital, however, remains an indirect determinant of FDI as it contributes to political stability, which is another determinant of FDI.

Among the most well-known framework regarding the determinants and characteristics of FDI, a special importance may be given to the one elaborated by Dunning (among many papers, Dunning, 2000; Dunning and Lundan, 2008). Dunning coined it the 'Ownership, Location and Internalisation' (OLI) framework, or the 'eclectic paradigm'.

Box 1: The OLI framework (excerpt from Dunning, 2000: 163-164).

The eclectic paradigm avers that the extent, geography and industrial composition of foreign production undertaken by multinational enterprises is determined by the interaction of three sets of interdependent variables - which, themselves, comprise the components of three sub-paradigms. The first is the competitive advantages of the enterprises seeking to engage in FDI (or increase their existing FDI), which are specific to the ownership of the investing enterprises, i.e. their ownership (O) specific advantages. This sub-paradigm asserts that, *ceteris paribus*, the greater the competitive advantages of the investing firms, *relative to those of other firms* - and particularly those domiciled in the country in which they are seeking to make their investments - the more they are likely to be able to engage in, or increase, their foreign production.

The second is the locational attractions (L) of alternative countries or regions, for undertaking the value adding activities of multinational enterprises. This sub-paradigm avers that the more the immobile, natural or created endowments, which firms need to use jointly with their own competitive advantages, favor a presence in a foreign, rather than a domestic, location, the more firms will choose to augment or exploit their O specific advantages by engaging in FDI.

The third sub-paradigm of the OLI tripod offers a framework for evaluating alternative ways in which firms may organize the creation and exploitation of their core competencies, given the locational attractions of different countries or regions. Such modalities range from buying and selling goods and services in the open market, through a variety of inter-firm non-equity agreements, to the integration of intermediate product markets, and an outright purchase of a foreign corporation. The eclectic paradigm avows that the greater the net benefits of internalising cross-border intermediate product markets, the more likely a firm will prefer to engage in foreign production itself, rather than license the right to do so, e.g. by a technical service or franchise agreement, to a foreign firm.

The eclectic paradigm further asserts that the precise configuration of the OLI parameters facing any particular firm, and the response of the firm to that configuration, is strongly contextual. In particular, it will reflect the economic and political features of the country or region of the investing firms, and of the country or region in which they are seeking to invest; the industry

and the nature of the value added activity in which the firms are engaged; the characteristics of the individual investing firms, including their objectives and strategies in pursuing these objectives; and the *raison d'être* for the FDI.

Regarding this last contextual variable, scholars have identified four main types of foreign based multinational enterprise activity: 1) that designed to satisfy a particular foreign market, or set of foreign markets, viz. market seeking, or demand oriented, FDI; 2) that designed to gain access to natural resources, e.g. minerals, agricultural products, unskilled labor, viz. resource seeking, or supply oriented FDI; 3) that designed to promote a more efficient division of labor or specialisation of an existing portfolio of foreign and domestic assets by multinational enterprises, i.e. rationalised or efficiency seeking FDI. This type of FDI, though related to the first or second kind, is usually sequential to it; 4) that designed to protect or augment the existing O specific advantages of the investing firms and/or to reduce those of their competitors, i.e. strategic asset seeking FDI.

Dunning (2002) has underscored that during the 1990s, the behaviour of MNEs in developing countries has been driven by efficiency-seeking motives and/or subcontracting, and that globalisation has changed the locational determinants of FDI. Indeed, determinants of FDI change with the transformation of international trade and the increasing pre-eminence of global value chains and global production networks, where trade is not only a 'trade in goods' but a 'trade in tasks' (Grossman and Rossi-Hansberg, 2006; Baldwin, 2011a). For Dunning (2002), the geography of FDI is affected by the widening scope of the knowledge-based economy and regional integration schemes. For multinational firms, spatially related decisions - i.e. what and how much to sub-contract, what and how much to produce, and to whom and where to sell end products - increasingly constitute the core of competitive advantage. The specific strategies of investing firms are less driven by 'traditional' motives, and, in particular, the existence of high skilled labour is increasingly viewed as crucial.

There have been debates as to whether the OLI framework is adapted to multinational enterprises (MNEs) from developing countries, as the latter may exhibit specificities vis-à-vis MNEs from developed countries (Buckley *et al.*, 2007; Gu, 2011; Henley *et al.*, 2008; Metallinou, 2013). Developing countries MNEs may be driven by additional motives and China's MNEs suggest that the OLI framework should be extended.

Indeed, the OLI paradigm is challenged by the internationalisation of latecomer and newcomer firms from the periphery, which try to have access to specific resources in order to improve their competitiveness in global markets. Mathews (2006) thus elaborated the 'LLL' framework, for 'linkage', 'leverage' and 'learning'. He stresses three motives that are under-addressed by the OLI framework, i.e. the 'linkage' and 'leverage' motives, which are linked and result in 'learning' motives (see also Sanfilippo, 2010). 'Linkage' refers to collaborative strategies with foreign companies through asymmetric partnerships (Peng, 2001), whereas 'leverage' makes use of these connections and the strengths of partners (Melin, 1992). Reiterated practice of both 'linkage' and 'leverage' may result in firm's 'learning'. Mathews thus underscores that globalisation, global value chains, fragmentation of activities and external international sourcing all require explicit coordination (as coined by Gereffi *et al.*, 2005): therefore learning and accumulative know-how and competences become easier to acquire.

The strategies followed by Chinese firms when they venture abroad fit the 'LLL' scheme particularly well. A better understanding of Chinese firms' international

strategies, however, requires a deeper analysis of the combinations of the still dominant OLI framework with this new approach, together with the role of relational assets that are based on the sharing of common social norms.

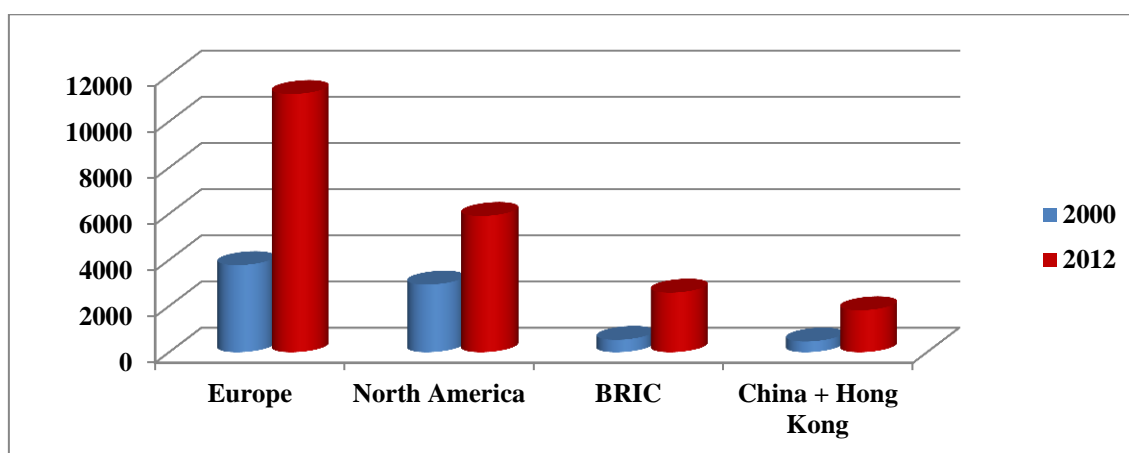
Kaplinsky and Morris (2009a) agree that the ‘linkage’, ‘leverage’ and ‘learning’ motives are particularly crucial. These combined factors may explain new forms of FDI from emerging countries, especially from Asia, regarding their investments in high-income economies: indeed, firms invest not so much to exploit their competences, but in order to augment these competences by learning from their overseas operations. For Kaplinsky and Morris, this ‘leveraging’ FDI may be a new type of outward FDI, which would characterise firms from low-income economies such as China, India and Brazil.

3. Chinese foreign direct investment in developed and developing economies: key facts

3.1. The global landscape of foreign direct investment

When considering global FDI outward stocks, Europe and North America are still the main regions of origin, even if their relative share decreased from 80% in 2000 to 72% in 2012. In contrast, the club of large emerging economies or BRIC (Brazil, Russian Federation, India and China) - driven by China with Hong Kong included - increased their position of global outward FDI stocks from 7.5% in 2000 to 11% in 2012 (figure 1). China was particularly active during this period to become, in 2012, the third largest investor globally, after the United States and Japan (UNCTAD, 2013). This result, however, is still modest even if it displayed a sharp increase during the 2000s.

Figure 1: Global Outward FDI stock for main regions and country, 2000 and 2012 (\$billions)



Source: computed by the authors from the series of UNCTAD World Investment Report, for the years 2000 and 2012.

A large part of FDI flows are composed of Mergers-and-Acquisitions (M&As), which involves developed economies both as countries of origin and destination. The

preference for M&As over *greenfield* investments as the dominant mode of entry has been observed since the 1990s. This inclination lies in part on asymmetric information regarding the value of M&As and *greenfield* projects, and the development of financial markets. Indeed, financial markets usually provide efficient mechanisms to set the value of M&A targets, while there is no comparable mechanism to assess the value of *greenfield* investment. Other causes include a favourable contractual environment and corporate restructuring needs. The importance of Europe is boosted by intra-Europe deals.

The rise of developing countries in FDI destination is also likely to weigh on the choice between *greenfield* projects and M&As, as developing country enterprises become more attractive target for acquisitions (UNCTAD, 2010). FDI in developing economies is, however, still mainly composed of *greenfield* investments, whereas FDI outflows from developing economies remain still lower than FDI inflows.

When looking at industrial patterns of FDI, it comes to light that manufacturing and services are the main sectors of destination for FDI projects at a global scale (table 1). However, the primary sector grew rapidly during the 2000s - to increase twofold its relative share from 2006 to 2011 - due to the interest of investors for mining, quarrying and petroleum. Interestingly, investment outlays in fossil energy were made to a large extent in developed economies (Canada and USA), and were largely driven by oil shale. On the contrary the effect of the global financial crisis on services, particularly on financial services and banking, is clearly visible: indeed, the global share of services fell from 50% in pre-crisis period to an estimated 40% in 2011 (UNCTAD, 2012).

Table 1: Global sectoral distribution of FDI projects, 2008-2011

Year	Primary	Manufacturing	Services
Average 2005-2007	8 %	41 %	50 %
2008	10 %	42 %	48 %
2011	14 %	46 %	40 %

Source: computed by the authors from the series of the UNCTAD World Investment Report for the years 2008 and 2011.

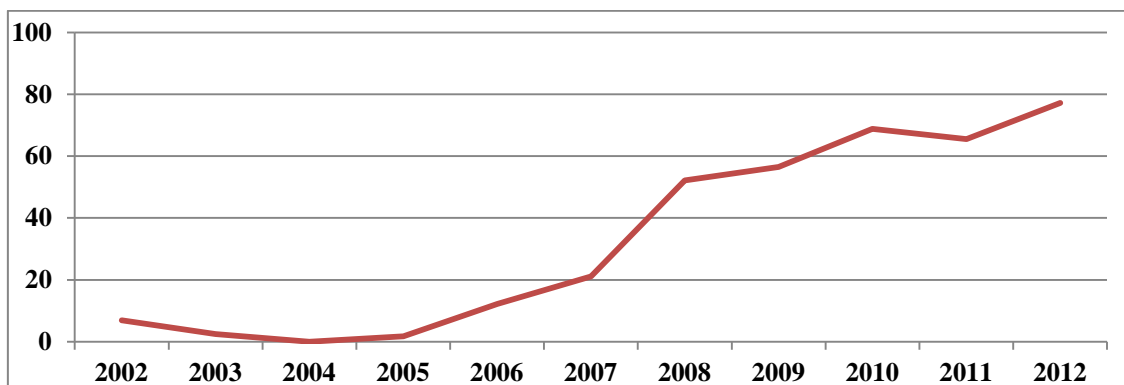
3.2. Chinese outward foreign direct investment

The growth of Chinese outward FDI flows began at the beginning of the millennium and accelerated in 2004. Outward FDI rose more than fortyfold - from 1.8 billions of dollars a year to \$77 billion a year - from 2004 to 2012, and is expected to reach 150 US\$ billions a year by 2015 (figure 2).

This dynamics was driven by two linked events: first, the adhesion of China to the World Trade Organization in 2001, after a decade of intense negotiations particularly with the US federal administration; second, the enactment by Chinese authorities, at the end of 1999, of the so-called 'go global' policy (*zou chu qu*) in order to support outbound investments in a broad spectrum of industries (Salidjanova, 2011). This policy was confirmed in 2004 when both the influential National Development and Reform Commission and the policy bank China ExIm Bank announced measures to support investments overseas in specific areas related to the basic needs of the booming Chinese economy.

Therefore, the following four key domains were put forward: i) natural resources-seeking investments where domestic resources are in short supply; ii) investment in manufacturing that promotes export of products, technology and equipment; iii) R&D collaborative projects, which could bring in advanced technologies, managerial experience and talents; and iv) mergers-and-acquisitions in order to enhance firms' international competitiveness and enlarge their market share (Andreff, 2013).

Figure 2: China outward FDI flows, 2002-2012 (US\$mn)



Source: computed by the authors from the series of the UNCTAD World Investment Report from 2002.

To deal with the data on FDI released by the Ministry of Commerce of the Popular Republic of China's (MOFCOM), however, is a genuine challenge (see Appendix). Two well-known limitations can be reminded.

On the one side, financial offshore centres are severely distorting the geographical distribution of Chinese OFDI (Schüller *et al.*, 2012). Three geographical areas of destination are particularly affected: Asia, Latin America and Europe.

First and foremost, Asia is impacted by the so-called 'round-tripping' flows through Hong Kong bound to mainland China in order to obtain preferential FDI treatment. Indeed, if in 2010³, 72% of China's outward FDI total stock was officially reported to have flown to Asia, the share of Hong Kong was 87% of total Asia.

Second, if for the same year, 14% of China's outward FDI total stock was reported to have flown to Latin America, the share of Caribbean tax havens, i.e. the British Virgin Islands and the Cayman Islands, was 92%!

Last, if for the same year, 5% of China's outward FDI total stock was reported to have flown to Europe, the share of Luxembourg was 37%. Furthermore, the Russian Federation which is included within the European area (with a share of 18%) has to be discarded in order to select Europe as a developed area.

By putting aside financial offshore centres (and the Russian Federation for Europe) due to the uncertainty of the final destination of FDI flows that went through - except for Hong Kong where around three-quarters of FDI outflows are directed towards mainland

³ The following data come from the 2010 Statistical Bulletin of China's Outward Foreign Direct Investment (MOFCOM).

China - the geographical distribution is more even, except Asia, which is still well ahead thanks to its spatial and cultural proximity (table 2).

When comparing OFDI stock for 2010 to 2005, Asia share is decreasing from 47.7% in 2005 to 41.7% in 2010, along with North America's share from 13.6% to 11.2% in 2010. On the contrary, Europe crossed over the symbolic threshold of 10% (table 2).

Table 2: Adjusted geographical distribution of Chinese OFDI stocks, 2010 (\$mns)

	Africa	Asia	Europe	Latin America	North America	Oceania
Value	13042	29089	7137	3377	7829	8607
Percentage	18.7	41.7	10.2	5.0	11.2	12.3

Source: authors estimates, using data from MOFCOM 2010 Statistical Bulletin of China's Outward Foreign Direct Investment.

On the other hand, Chinese firms do not report foreign earnings that are reinvested abroad as OFDI along with intra-company loans and non-financial and private sector transactions. If the risk of underreporting was negligible when Chinese OFDI was in its infancy, it is not the same when firms expand abroad beyond their first implantation, and re-incorporating foreign earnings may increase the share of developed countries presented in table 2.

Overall, MOFCOM data can be used when one wants to envision a general trend and orientations. If more details are needed, however, one has to deal with firm-level data and switch to commercial databases. Among the datasets available no single one reflects the different modes (*greenfield*, M&A, joint-venture or partnership) followed by the companies to go abroad. Therefore, one has to cautiously combine different datasets. There are again limitations: for example, it is difficult to pick up all the M&A deals as many Chinese companies use 'special purpose vehicles' from third countries as Caribbean tax havens (Rosen and Hanemann, 2009).

3.3. Chinese OFDI in developed countries, with a focus on Europe

When considering adjusted data on Chinese OFDI (table 2), developed countries, i.e. Europe and North America, ranked second in 2010 among destinations (with more than 20% of China's outward FDI total stock in 2010), behind Asia (particularly South Asia) but ahead of Africa, Latin America and Oceania.

Accordingly, Europe is an appropriate representative of the attractiveness of developed countries for Chinese companies when venturing abroad even if alternative destinations, such as North America or Japan to a lesser extent, have their own specificities and advantages. Moreover, Europe's share has expanded in the course of the 2000s.

The present analysis of Chinese investments made across Europe is based on firm-level data extracted from a proprietary database built by the authors with the support of the French Ministry of Economy⁴. In 2013, more than 700 Chinese companies have been

⁴ This database has been elaborated by Françoise Hay (University of Rennes-1) and Christian Milelli from

identified for Greater Europe, i.e. including non EU-countries except Russia, Ukraine and Belarus. These firms have realised over the 2002-2012 period around 1800 operations of investment (1200 operations from mainland China's firms, the remaining being from Hong Kong's firms). More fine-grained findings emerge from the pooling of several sources (see Appendix). The originality of the database not only stems from the continuous collection of information related to investments that are planned or effectively made but also from the monitoring of the life-cycle of these operations (extensions, relocation across Europe or in China, or closures).

Europe remains attractive: indeed, it still holds several advantages for Chinese investors. It is a highly-integrated geographical area in terms of institutions (European Union), economy (single market), currency (Eurozone) and movement of people (Schengen area). In addition, Europe has a population of around 500 million of high-income consumers, it is an area of outstanding political stability, it has an efficient transport infrastructure network, all this with a qualified labour force and first-class technologies and skills. This is particularly attractive for investors from emerging economies, which are embarked on an unabated catching-up move.

Regarding the types of Chinese firms that invest in Europe, this database suggests that most operations of investment are made by small and medium enterprises (SMEs). The most important investments in terms of value, however, are made by large state-backed and private firms.

The following features emerge from the dataset and analysed more in depth below:

- Chinese firms follow a learning process
- Motives are broadened and become more complex
- Steady increase of mergers-and-acquisitions with low level of risk
- Spatial polarisation
- Specialisation according to host country advantages
- Sectoral coverage is expanded

3.3.1. Chinese firms follow a learning process

Most Chinese investors are following long-term strategies. Thus, when they invest in Europe it is not to earn money at any price but first and foremost to gain a foothold in European markets, particularly in wholesale and retail trade, because the Chinese economy is still export-driven. Another reason lies in the still large cultural distance between China and Europe on how to conduct and succeed in business activities and reflects the insights of the 'Uppsala school' (Johanson and Wiedersheim-Paul, 1975). However, as there are largely backed by their state - be it directly and conspicuously, or indirectly and in a non-transparent way -, their investments are easier to finance and less risky. As a result, they can accept low-return in their operations contrary, for example, to Indian corporations, which are basically private entities.

The French manager of a Chinese subsidiary in Europe met by one of the authors made a revealing point: most Chinese firms do not have an expansionist spirit *per se*, they simply wish for their European acquisitions to serve their parent company. This

coincides with the observation made by several analysts on the so-called ‘light touch’ approach following the acquisition of foreign firms by Asian firms, mainly Chinese: corporate stability takes precedence over everything else (Cogman and Tan, 2010).

The Chinese investment projects initiated during the economic crisis are better prepared, with clearer geographical and sectoral targets. These investors also keep out of the public view, in order to avoid fuelling protectionist reflexes or even xenophobic feelings in a Europe that has been in crisis since 2008 (Hay *et al.*, 2011).

3.3.2. Broadened and more complex motives: seeking for strategic assets

The first motive for Chinese firms when investing in Europe was basically access to markets, either to secure new markets in Europe or expand already existing market shares, or to support exports to Europe, which is to date the first consumer market overseas for China. This motive is still important for Chinese companies coming into Europe and explains the importance of services compared to manufacturing activities when looking at the whole distribution of activities for Chinese companies in Europe. When looking in detail at the content of services, one can identify numerous commercial premises or representative offices.

The second motive is to search for strategic assets - i.e. R&D qualifications, managerial capabilities, organisational skills, marketing expertise, brands and reputation (Hay and Milelli, 2013). By doing so Chinese firms either acquire or augment their resources and capabilities, at home or/and abroad, in order to raise their competitive edge. Strategic assets are obtained either through cumulative experience or collaborative modalities, such as joint-ventures or partnerships, or even the takeover of distressed firms or non-core subdivisions. The former is a long lasting process and is often coupled with the search for specific resources outside the company in order to move up the value chain, whereas the latter is time-saving but requires firms to have substantial absorptive and learning capabilities. Such a quest corresponds either to the needs of Chinese firms or to the shortages of the Chinese economy (Deng, 2007). It is a new strategy for two reasons: first, this motive was rare for the incumbent multinational companies, which generally had ownership-specific advantages before investing abroad. Second, this motive came after the access to the market, which is still paramount.

The third motive, which is related to efficiency issues, is new. Usually, this motive concerns incumbent multinationals from developed economies that are confronted with increased costs, particularly wages. It is surprising to see this motive at play for companies from a country at this stage of development: indeed, China is still a developing economy. And even if Chinese wages rose rapidly during the last two years, particularly in coastal regions, i.e. around 20% per year, there is still a substantial gap with Western wages, particularly for low or middle qualifications.

When they expand across Europe Chinese firms are, in fact, looking for particular locations that are endowed with specific advantages, which match suitable locations for R&D centres, production or distribution facilities, or regional headquarters. The aim is to improve the efficiency and the competitiveness of Chinese companies (Hay *et al.*, 2011).

The previous three motives are increasingly pursued by Chinese firms in Europe in an integrated scheme. For example, market- and asset-seeking (or increasing assets)

motives, are pursued hand in hand in a growing number of sectors. The same is true with the efficiency-seeking motive, when Chinese companies are setting R&D centres in technological clusters not only to acquire directly (or indirectly through spillovers) strategic assets in order to sustain the ramping up of their technological ability, but also to entice talented people at affordable cost.

More generally, by dispersing design, R&D or manufacturing activities across Europe Chinese firms are following genuine regional strategies, which are part of a global design (Andreff, 2013).

3.3.3. Steady increase of mergers-and-acquisitions of firms with low level of risk

Chinese investment is increasingly taking the form of merger-and-acquisitions of foreign firms that are in difficulty but present a low level of risk, and with which Chinese investors already had business relationships.

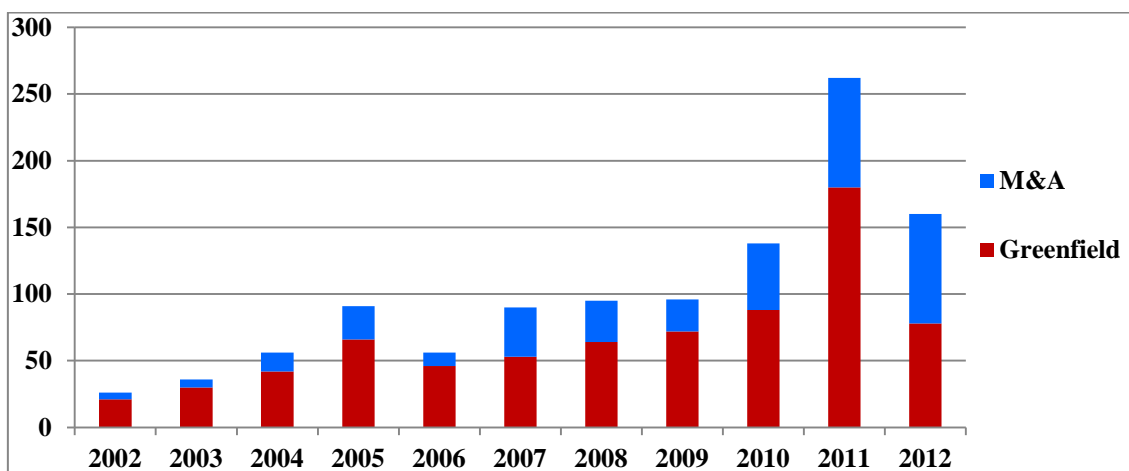
The number of Chinese acquisitions, i.e. from minority equity participations to mergers, has continuously increased over the period to overpass in 2012 the number of *greenfield* investments: 51% against 49% (figure 3).

Equity participations are still the main vehicle due to the ‘liability of foreignness’, i.e. uncertainty related to the context they are not familiar with, but mergers are also rising, particularly in the case of transactions involving former Chinese sub-contractors, suppliers or partners of European firms in joint-ventures or partnerships. Thus, internal workings, know-how and the manufacturing lines hold no more secrets for them. They can provide liquidity and take over their debt. However, it could be challenging as it often entails companies, which seasoned Western managers have been unable to turn around. These buyouts usually keep the activity in place with, in some cases, a duplication activity in China, or a relocation of all the firm’s manufacturing lines combined with sales offices or outlets maintained in Europe. This may be a contrast with OFDI from other emerging countries, such as India, which tend to focus on highly-visible firms in host countries.

Investments that aim to extend capacity are also rising, which is a sign that Chinese companies are integrating within European economies and local communities. At the end of the cycle, closure is a possible contingency but still in modest magnitude: basically, it concerns small and medium enterprises, except some large firms such as TCL, a TV manufacturer, which closed all its European plants in 2006.

Lastly, joint-ventures are so far not a valued entry mode for Chinese investors into Europe. As mentioned previously, due the ‘liability of foreignness’ this choice is not specific to Chinese companies but concerns all companies from emerging economies when they come in developed countries; Chinese companies, however, are more aggressive and want to capture more activity along the value chain. For example, when firms from China or Hong Kong operating to the textile-clothing sector come to or expand in Europe they move upstream, in particular by buying renowned brands, or downstream, by setting up retail chain (the Esprit group being an example).

Figure 3: Chinese investments in Europe, 2002-2012: *Greenfield* investments and Mergers-and-Acquisitions (vertical axis: number of transactions)



Source: computed by the authors from a proprietary database on Chinese firms in Europe.

3.3.4. An ongoing spatial polarisation

When looking at the geographical distribution of the number of Chinese firms in Europe, two opposed results emerge. A first one consists of a growing polarisation on the three largest countries, i.e. the United Kingdom, France and Germany: 56% during the whole period (2002-2010), and 60% for 2011-12.

On the contrary, a second outcome consists of a lesser polarisation in five countries - Belgium, Italy, Netherlands, Spain and Poland: 21% during the whole period, 17% for the two last years, 2011-12.

It is worth mentioning that these trends go hand in hand with an extensive approach initiated in the early 2000s with more European countries being targeted by Chinese companies to set up commercial premises, export-support activities or plants.

But what comes out from the post-2008 crisis period is that the country (market) size matters along with the geographical position in relation with Continental Europe: indeed, France and Germany have increased their relative share during the last two years. Another factor plays against the United Kingdom, which was previously the main destination, i.e. the fact it does not belong to the Schengen area. Indeed, Chinese citizens willing to travel from the UK to Continental Europe have to get a visa. Thus, one cannot infer that the last trend is only related to the market-seeking motive. Indeed, these countries have also been the destination of the majority of the R&D facilities set up by Chinese companies across Europe (Hay and Milelli, 2013).

Lastly, a marked interest by Chinese investors for Central or Eastern European countries up to 2007 has apparently not been able to withstand the financial crisis: decisions to invest there made before the outburst of the crisis have seen the lowest rate of effective achievement when compared to other European countries.

3.3.5. A specialisation according to host country advantages

When Chinese companies select Europe for their investment projects they have increasingly in mind a strategic map of the host country advantages, not only at the country level but also at the micro level, be a province or a cluster. This move is in large part of a mimetic or herding nature: first-movers, however, are common and successful in a large spectrum of activities, and they are basically market-driven. French vineyards are an example, particularly those from Bordeaux label origin; experts know that if they produce renowned agricultural products they are also a valued reserve with the opportunity to realise substantial capital gains by selling them. When foreign investors bought vineyards at the end of the 20th century, North-American investors had the lead, whereas since the 2000s investors from emerging economies with ‘deep pockets’, i.e. China or Persian Gulf countries, or at a lesser extent, Brazil or India, are much more active.

By locating in London or Luxembourg for financial or banking activities, in Italy for design, in France for the acquisition of prestigious brands in luxury activities, or in Germany for automotive or engineering activities, Chinese investors are demonstrating a rational behaviour, which is similar to that of other foreign investors. It is surprising, however, to observe the rapidity of their acquisition of this extensive knowledge, and their maturity when they carry out their investment projects.

3.3.6. The expansion of sectoral coverage

Chinese investors have continuously expanded their sectoral coverage at a global level as well as in Europe. In the latter the expansion was particularly impressive from 2002 to 2012 (figures 4a-4b). It extends beyond manufacturing sectors and includes transport companies (particularly shipping companies, Cosco and China Shipping Containers Lines), which generated numerous investments in 2002 (figure 4a). Banks (e.g., Bank of China or ICBC) were also a growing sector. The share of medium-high technology sectors (e.g., electrical machinery or transport equipment) is also rising rapidly, which reflects that China is moving up the technology ladder due to its integration into global production networks (Ma and Van Assche, 2012).

The prominent place of the equipment sector (i.e. 30% of all the numbers of Chinese investments made in Europe for 2002-2012) was driven by car manufacture, with one third of investments going into the United Kingdom, electrical-electronic equipment (mainly into France, Italy and Spain), and mechanical engineering (Germany, France and Italy). In addition, there is substantial investment in the telecommunications sector, with Germany receiving nearly one third. For example, Huawei Technologies moved its European headquarters from London to Düsseldorf along with the setting-up of R&D facilities.

The current economic crisis has been viewed by Chinese companies as a genuine source of opportunity either to acquire ailing European companies or divisions, or start investing from scratch in new sectors or reinforce their presence.

The authors collected empirical evidence on the following sectors. First, in relation with the surge of the Chinese automobile market and its crowded and competitive nature - more than 150 automakers - Chinese companies have continued to make investments -

plants, R&D facilities or commercial premises - in the European automotive industry. Indeed, independent Chinese firms searched for overseas automotive companies or auto-parts makers, which were for sale. For example, Geely bought Volvo cars from the US firm Ford Co. in 2010 and thus harnessed a global brand and technological assets.

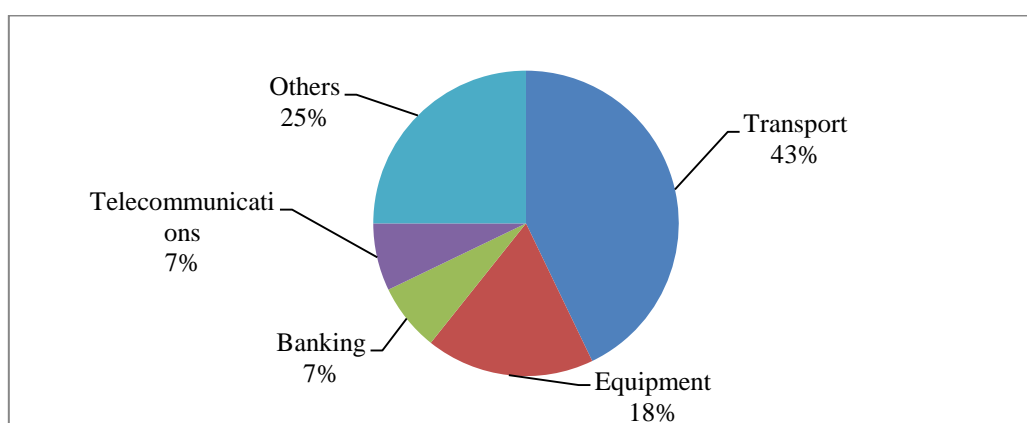
Second, due to the intensity of the 2008 financial crisis it is surprising that Chinese financial institutions have set up numerous branches and other units. This result is at odd with the previous result based on MOFCOM data on global sectoral distribution (table 1). The discrepancy could be explained either by an expansion process from re-investing earnings or by so limited amounts that authorisations are not required.

Third, Chinese investments in information technologies and telecommunications are significant. This is a new trend, as these activities were previously more of an Indian domain. This is due to new investments in software and related services by Chinese firms, with nearly half focusing on the United Kingdom.

Another salient point is the interest in utilities and transport infrastructures. For example, during the 2000s, Chinese companies invested in the sectors of water in the United Kingdom or electricity energy in Portugal. All these investments were not successful, as was the case of the construction of a highway in Poland in 2011⁵.

Lastly, investments made in renewable energies, which were practically non-existent before the crisis, have since accounted for a significant proportion. Indeed, for the 2008-2012 period, they represent more than 10% of investments made in Europe. The importance of these investments, however, must be tempered by the fact that they relate mainly to sales activities. They have been stimulated by the effects of the crisis in both China and the rest of the world. Germany has received around 40% of these new investments and France more than 22%. Suntech Power and Yingli Green are the most active investors and some Chinese companies were considering setting up assembly units in Europe before the industry was plagued by overcapacity in Europe and China.

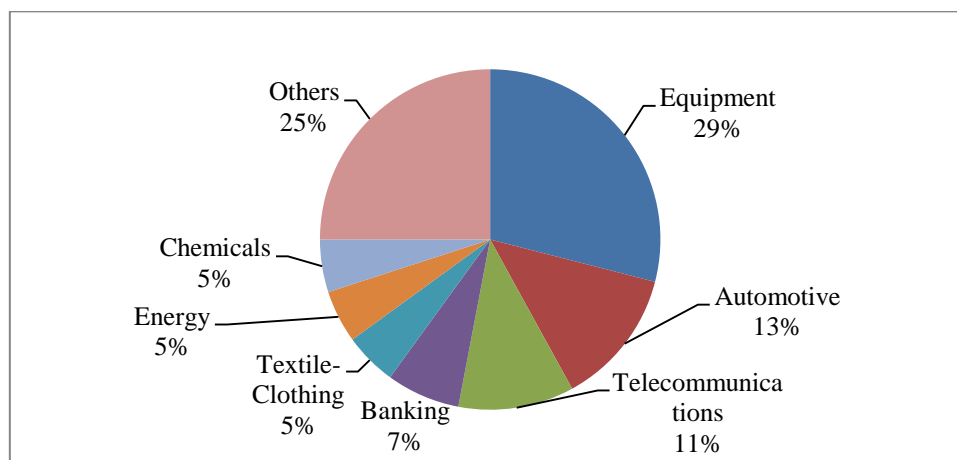
Figure 4a: Chinese foreign direct investment in Europe: sector breakdown for 2002



Source: computed by the authors from a proprietary database on Chinese firms in Europe.

⁵ COVEC stops Polish highway construction: http://www.china.org.cn/business/2011-06/18/content_22811134.htm

Figure 4b: Chinese foreign direct investment in Europe: sector breakdown for 2012



Source: computed by the authors from a proprietary database on Chinese firms in Europe.

3.4. Chinese outward foreign direct investment in developing countries, with a focus on Sub-Saharan Africa

China invests in developing countries, firstly in Asia, but also in Latin America and Sub-Saharan Africa (SSA). The case of SSA is here examined in detail, as it has given rise to an increasing literature, which aims at demonstrating that China's FDI is driven by its quest for natural resources as inputs for its own growth (Sindzingre, 2011; 2013).

China's FDIs in SSA, however, also focus on the manufacturing and service sectors: they are not only driven by resource-seeking motives, but also by motives of improving their access to markets, either the domestic markets of host countries or other markets; they are also driven by motives of improving efficiency, mainly in labour-intensive sectors (not in capital-intensive sectors), in harnessing the lower production costs that prevail in some SSA countries when those are not erased by infrastructure deficiencies (outages, transportation and the like).

A key point is that while it is very difficult to compute the exact volume and value of Chinese FDI, it must be underscored that it is even more the case for Chinese FDI in developing countries, and particularly FDI in SSA.

3.4.1. The evolution of Chinese foreign direct investment in developing countries

China's OFDI targets less the developing countries than it does Asia, the US and the EU. According to the Heritage Foundation⁶, China's OFDI still increased in 2012, with Chinese enterprises moving as a group from region to region. The main sectors were energy and metals, with the leading recipient of new Chinese investment being the U.S. (especially in energy and transportation construction).

⁶ <http://www.heritage.org/research/projects/china-global-investment-tracker-interactive-map>

China's OFDI, however, is increasingly important for the recipient developing countries. This is the case for Latin America, although, as for the other developing countries, there is no reliable database of Chinese investment in the region. As for SSA, Chinese financial flows in Latin America tend to target the commodity sectors, and Chinese companies have started in the 2010s to arrange new types of loan packages that exchange finance for commodities, typically loans-for-oil (e.g., in Venezuela, Brazil, Ecuador) (Gallagher *et al.*, 2012).

3.4.2. The pre-eminence of the resource-seeking motive: the example of Sub-Saharan Africa

China's FDI in SSA is similarly very difficult to compute. The Chinese presence may be overestimated by official statistics, as the latter sometimes include in the category of FDI the activities of Chinese services providers in the construction and infrastructure sectors (Pairault, 2013).

Figures regarding the share of China's FDI into Africa (not SSA) vary according to sources. According to UNCTAD (2013), Chinese FDI stock in Africa represented \$16 billion at the end of 2011, with South Africa being the leading recipient of Chinese FDI, followed by the Sudan, Nigeria, Zambia. China is a top investor in countries such as Sudan and Zambia. China's FDI flows would amount to around US\$20bn, which is modest in absolute terms and compared with trade flows⁷. For Standard Bank research, "China's FDI stock in Africa is almost always conflated with the estimated US\$35 billion in concessional loans from China Development Bank and China ExIm Bank which have been extended to various African governments over the course of the past decade"⁸. These loans are often treated as fully-realised cash flows even though they will be drawn over a number of years, may not be fully utilised, and are often used to pay for purchases of materials and equipment from a Chinese contractor.

As underscored by Mlachila and Takebe (2011), FDI flows are driven by two types of factors: pull factors (domestic conditions of recipient countries, e.g., macroeconomic conditions attracting inward FDI - size of the economy, growth, inflation, fiscal and external balances, and openness of the economy -, and structural factors such as infrastructure) and push factors (external conditions encouraging outward FDI, e.g., world interest rates and world growth). For Chinese FDI to SSA countries, push factors include: 1) abundant foreign reserves, which are compounded by the growing incentives for China to invest in emerging markets and low-income countries, including Africa; 2) increasing natural resource security concerns; 3) Chinese government support for outward FDI; 4) rising labour costs in China; 5) more acceptance of risk.

For SSA countries, Mlachila and Takebe (2011) list as pull factors: 1) abundant natural resources, which usually offer a high rate of return - e.g., oil, copper, iron ore; 2) investment climate; 3) better macroeconomic conditions; 4) liberalisation and deregulation; 5) privatisation; 6) preferential trade agreements (e.g., the EU's Everything but Arms initiative, the U.S. African Growth and Opportunity Act (AGOA), which provide foreign firms incentives to invest in SSA countries as a base for

⁷ Source: http://www.southerntimesafrica.com/news_article.php?id=8393. Felix Njini, 3 June 2013.

⁸ Ibidem, http://www.southerntimesafrica.com/news_article.php?id=8393. Felix Njini, 3 June 2013

exporting to Europe and the US, especially in sectors where low-costs matter, e.g. apparel. China's moving up the industrial value chain is an incentive for lower cost destinations for its lower end industries, e.g., SSA.

China's 'first movers' multinational firms were driven by the quest for securing the country's energy needs (Alden and Davies, 2006). Alves (2013a) lists some major investments of China in the commodity sector in SSA, with most of them being above one \$billion: e.g., Sinopec in Nigeria and Gabon (oil); Minmetals in DR Congo (copper); CNOOC in Uganda (oil); CNMC in Zambia (copper); Sichuan Hanlong in Cameroon and Congo (iron ore), and the like. Standard Bank research considers that China's future investments across Africa will be driven by ensuring resource security and this include hard and soft commodities, growing domestic consumption, shifting manufacturing to a higher value-added chain⁹.

A key characteristic of Chinese OFDI in SSA is the fact that a significant share of it is backed by the central government, i.e. it is driven by enterprises that are supported by the government, in particular public enterprises, and within this category, firms that are directly supervised by the government: indeed, as shown by Pairault (2013), this latter category would represent on average 80% of the stock of Chinese foreign direct investment: although they enjoy a genuine autonomy, such enterprises therefore can be said to express China's investment policy in SSA.

Kaplinsky and Morris (2009a), along with Gu (2009) and Corkin (2011), emphasize that China's investment in SSA may be divided in two types. The first one are investments that are driven by predominantly state-owned companies - belonging either to the central state, e.g., very large MNEs such as China National Petroleum Company (CNPC) and China Petroleum and Chemical Corporation (Sinopec), or to the provincial states levels. Such investment is typically resource-seeking; such firms typically invest in the resource sector, in infrastructure and construction projects, and focus on the long-term. The second type are investments that are driven by privately-owned firms: they typically invest in manufacturing and services sectors, act independently from the Chinese government and are self-financed; they may also be incorporated in SSA only, and in this case they rather invest in petty manufacturing and services.

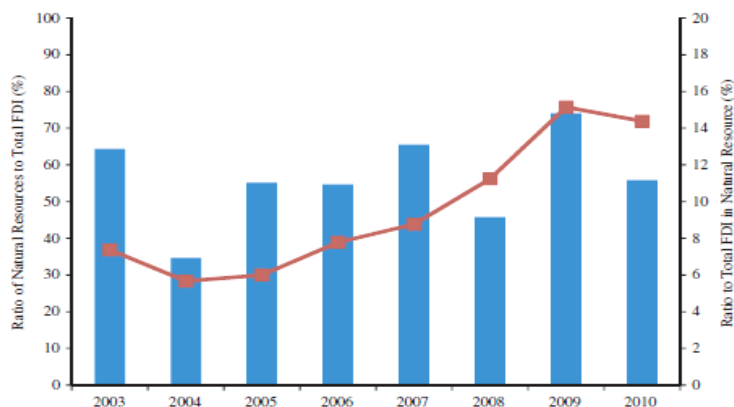
In volume, Chinese OFDI in SSA is driven by government-backed and large firms, and they focus on the commodity sector. The sectors are those of 'hard commodities', in particular oil and metals. In terms of number of firms, Chinese OFDI is driven by private firms.

According to Mlachila and Takebe (2011), based on the World Bank-Public-Private Infrastructure Advisory Facility/PPIAF Chinese Project Database and IMF staff surveys, during 2003-2007, 40% of Chinese OFDI was in the oil sector, 55% in mining, and 5% in natural gas. In terms of value, more than 70% of the total commitment cumulatively was in the oil sector. In the oil sector, most investments were initiated under bilateral agreements and run by one or more of three state-owned enterprises: China National Petroleum Corporation (CNPC), China Petroleum & Chemical Corporation (Sinopec), and China National Offshore Oil Corporation (CNOOC). In the mining sector, both Chinese state-owned and private companies are active in mining

⁹ Ibidem, http://www.southerntimesafrica.com/news_article.php?id=8393. Felix Njini, 3 June 2013.

projects. Such investing in the commodity sector has entailed some political risks (Moreira, 2013).

Figure 5: China's FDI in natural resources [share of China's total FDI (left scale); share of global FDI in natural resources (right scale)]



Source: Mattoo and Subramanian (2012).

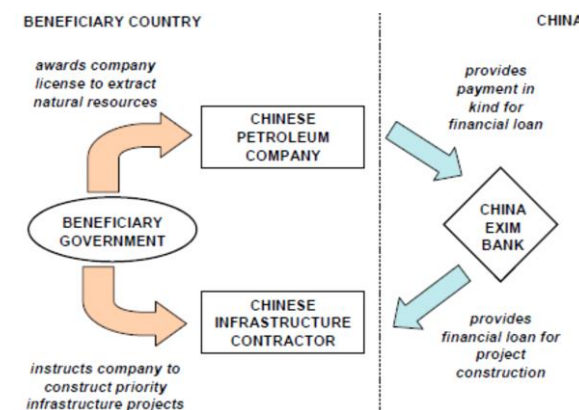
In terms of modes of financing, China's ExIm Bank, which plays a key role in financing global trade and investment, is the principal source of debt financing, with most of its loans targeted at infrastructure developments (Mlachila and Takebe, 2011), while the China-Africa Development Fund (or CAD Fund) established in 2006 to encourage Chinese private enterprises to invest in Africa, has been increasingly facilitating equity financing. Its priorities are agriculture and manufacturing, infrastructure, natural resources and industrial parks run by Chinese companies (Mlachika and Takebe, 2011, based on the China-Africa Business Council and China-Africa Development Fund¹⁰).

Another key dimension of the resource-seeking motive is its association with the development of infrastructure in SSA. A well-known mode of Chinese investment refers to the so-called 'Angola mode': this type of contract links trade, investment and aid, and is a 'packaged' contract of 'commodity-for-infrastructure financing', where a SSA country exports a commodity to China in exchange for the financing of an infrastructure project (Orr and Kennedy, 2008; Davies, 2010).

SSA infrastructure is very poor, which has made such contracts particularly attractive for SSA governments. The natural resource part is equity-financed by Chinese entities as FDI and the infrastructure part is debt-financed usually by China's ExIm Bank on concessional terms (Mlachila and Takebe, 2011; Christensen, 2010).

Such contracts, which aim at securing the long-term supply of a natural resource and accessing exploration rights, appear to be more effective in Africa than in South America (Alves, 2013a). These are associated, however, with little linkages with local economies in the sense of Hirschman (1958), as shown by the case of Angola (Corkin, 2011).

¹⁰ <http://www.cabc.org.cn>, and <http://www.cadfund.com>

Figure 6: Structure of the ‘Angola mode’ arrangement

Source: Foster *et al.* (2008).

Alves (2013b) thus lists the major ‘resource-for-infrastructure’ concessional loans (from 2\$bn to \$6bn pledged) in SSA over 2006-12: four are in the oil sector (Nigeria, Ghana, and Angola), and two others in the mining sectors (cobalt in DRC and iron ore in Gabon). Such contracts and loans have triggered controversy, regarding their opacity and the risks they involve (Jansson, 2013).

China also invests in Special Economic Zones (SEZs) with the objective of promoting manufacturing - which may be viewed as a duplication of one of the ingredients of their success at the initial stages of China’s growth, when foreign investors were confined within SEZs, such as Shenzhen. Among the 19 SEZs initially planned by China in the world, 6 are in SSA - in Zambia, Nigeria, Ethiopia and Mauritius (Bräutigam and Tang, 2012; 2011; OECD, 2001, table 6.10).

Foreign direct investment also includes investment in agriculture, and in particular land. There has been a widely publicised increase of such investment in SSA since the early-2000s (sometimes coined as ‘land grabs’), which are often implemented by investors from emerging countries - motives usually being the improvement of food security for the investing country. Chinese firms have achieved such investments, which appear to have the characteristics that are similar to other countries’ investments in large-scale acquisitions of land (on Senegal, Buckley, 2013).

3.4.3. The increasing orientation of Chinese foreign direct investment in Sub-Saharan Africa towards manufacturing sectors

China FDI is not only driven by the resource-seeking motives but also by market-seeking ones (Cheung *et al.*, 2011). Chinese firms are also driven by the motives of linkages and learning.

The natural resource and infrastructure sectors attract the biggest share of Chinese FDI to SSA, but investment in manufacturing is increasing (IMF, 2011): in addition to resource-seeking FDI, the rapid industrial upgrading currently taking place in China provides opportunities for these countries to attract FDI in manufacturing (UNCTAD, 2013). It should be noted, however, that SSA local manufacturing firms may be threatened by imports of cheaper manufactured goods (Kaplinsky and Morris, 2009b).

In Zambia, for example, Chinese firms have invested in the textile and clothing sectors, and have also supported this sector via an improved infrastructural development, which indirectly benefit the textile industry: however, their investments have remained limited, and Zambia's needs are covered by imports low-priced textile and clothing items, which highlights the difficulties in fostering industrialisation - difficulties facing both SSA governments and Chinese investors (Eliassen, 2012, on the example of Zambia).

The investing firms, however, differ from the firms that invest in the commodity sector: they tend to be medium and small private enterprises. As underscored by the IMF (2011), large state-owned firms tend to focus on resources and infrastructure, whereas private firms tend to concentrate on manufacturing and service industries. Therefore, although resource and infrastructure investment may be the largest sector in value, the number of private projects in other sectors is high and growing, driven by private small and medium enterprises, which target local and regional markets¹¹. Yet, as underscored by Mthembu-Salter (2012) in the case of the DR Congo, the Chinese government facilitates access by Chinese state-owned companies to large mining deposits in the DR Congo through loans from the state-owned ExIm Bank.

In Ethiopia for example, China's financing is driven by market size and low labour costs (as well as attractive public policies, such as facilitation of large land-leases), as Ethiopia has no significant natural resources: the manufacturing sector accounts for the largest amount of Chinese FDI, and one of the largest shoe exporters in China has started an important investment in Ethiopia in 2013: Chinese manufacturers increasingly invest in SSA in order to benefit from preferential trade tariffs and lower labour costs¹² (Dinh *et al.*, 2012). Even in resource-rich countries, Chinese FDI is not necessarily concentrated solely in the resource sector. Similarly, Zambia is another example where Chinese FDI targets all sectors of the economy (Kragelund, 2009).

Chinese firms also harness the preferential trade agreements that some SSA countries have with developed countries. Regional trade agreement may reinforce the market-seeking motives. According to the IMF (2011), some southern SSA countries have attracted FDI in the apparel sector from China thanks to the U.S. Africa Growth and Opportunity Act (AGOA), which gives eligible sub-Saharan African countries duty-free access to the U.S. market.

The survey made by Shen (2013a) thus underscores the growing visibility of Chinese private-sector investment in the manufacturing sector in some parts of SSA (Ethiopia, Ghana, Liberia, Nigeria, Rwanda, Zambia), which may be explained by the increased pressure of industrial restructuring in coastal China, a force that drives some labour-intensive firms to relocate to other parts of the developing world, including SSA. The comparison of government- and private-led outward FDI made by Shen (2013b) in 2011 shows that the latter focuses more on manufacturing sectors, and less on contracting and mining.

¹¹ And even large firms: a major non-natural-resource-related Chinese investment in SSA is the US\$5.4 billion purchase of a 20% stake in South Africa's Standard Bank by the Chinese Industrial and Commercial Bank (IMF, 2011).

¹² William Wallis, China plans multimillion Ethiopian investment, *Financial Times*, 3 June 2013.

4. Differences and similarities: increasing convergences of determinants and characteristics of Chinese foreign investments

If the steady increase of Chinese outward FDI since early 2000s concerned more countries and areas, and was driven by different motives in order to benefit from comparative advantages, commonalities are also expanding rapidly due to sizable underlying forces both domestically and globally.

4.1. Less differences than commonalities

Differences in motives of FDI may stem from variations in the level of development of recipient countries, as well as differences in the assets that Chinese firms can pick up abroad. Similarly, differences in motives of FDI also stem from variations in the level of development of Chinese firms: successful transfers of technological or intellectual assets require a certain level of ‘social capability’ (Abramovitz, 1986): Chinese firms willing to embark in this strategy must have achieved a critical stage of development.

An important difference in developed countries relative to developing countries lies in the prevalence in developed countries of the strategic asset-seeking motive for FDI to harness patents, codified and tacit knowledge, management capabilities, marketing skills, brands or goodwill.

Chinese OFDI flows, however, rapidly converge from contrasted motives - e.g., access to markets in developed countries *vs.* access to natural resources in developing countries - to more integrated motives.

A first commonality refers to the typology of Chinese firms: in both Europe and Sub-Saharan Africa, small and medium enterprises prevail in terms of numbers of investment operations, while large state-backed and private firms prevail in terms of value of investments.

A second commonality refers to the resource-seeking motive. As underscored by a large literature (e.g., World Bank, 2012), it is still the prevailing motive of Chinese FDI in developing countries, notably Sub-Saharan Africa, and could represent a key difference with developed countries, and Europe in particular. Nevertheless, the resource-seeking motive is also a significant driver of Chinese FDI in developed countries, as shown by Chinese FDI in a country that is endowed in abundant natural resources, such as Australia. Large investments in natural resources are mainly achieved by Chinese state-backed firms - for example, Sinopec or Petrofina in oil, or China Minmetals or Baosteel in metal ores. As a result, and this is a difference with Chinese FDI in developed countries, Chinese state-owned enterprises are more present in developing countries, whereas private firms tend to take the lead in developed countries.

Another commonality across developed and developing countries is the market-seeking motive. This motive historically prevailed in developed countries: yet Chinese firms increasingly invest in developing countries in order to produce intermediary or final goods for local and regional markets.

Several underlying factors can explain the increasingly common motives of Chinese FDI across recipient countries - developed and developing. On aggregated terms there is no convincing evidence of a Chinese exception as far as outward FDI is concerned, even if at an early stage there was some specificity. Buckley *et al.* (2007) identified three potential domains of distinctiveness: capital market imperfection, special

ownership advantages of Chinese multinationals, and institutional factors, particularly the high levels of government support. Nowadays, the pattern of Chinese investment abroad is converging toward the profile of investment that is exhibited by the U.S. or EU countries – yet with a greater share in natural resources for Chinese FDI relatively to the US and EU countries (World Bank, 2012): in particular, M&A deals are expanding rapidly, services are gaining in importance, especially if the many construction and engineering projects are taken into account, with both developed and developing countries being targeted.

Moreover, as mentioned above, the integration of Chinese companies into global value chains at different steps induces new motives, or combinations of different motives, to invest or globally streamline operations through non-equity forms.

4.2. The determinants of convergence in Dunning's OLI and Mathews' 'LLL' frameworks

Two dimensions - ownership advantages (O) and internalisation (I) - of the tripod elaborated by Dunning's 'eclectic theory' can be used here (Dunning, 2000). First, the greater the competitive advantages of the investing firms relative to those of other firms - particularly those domiciled in the country in which they are seeking to invest — the more they are likely to be able to engage in, or increase, their foreign production. Second, the greater the benefits of internalising cross-border intermediate product markets, the more a firm will prefer to engage in foreign production.

When matching these two trade-off with Chinese OFDI flows and corresponding strategies followed by Chinese multinational firms, there is growing evidence that both phenomena are in line with the theory. This result, however, is not enough to explain the growing convergence between the determinants of Chinese FDI towards developed countries and developing countries. Both aspects must therefore be deepened.

On the one hand, as private Chinese firms are increasingly venturing abroad due to push factors at home (particularly, over-competition in several industrial sectors resulting from highly subsidised state-backed enterprises; Nolan, 2001) along with pull factors (more favourable business environment and many opportunities in host countries), the competitive advantages of these firms, which are based on internal strength and often relational assets, entails similar strategies and motives.

On the other hand, Chinese firms from sectors where contracting and sourcing have been developed on a large extent (e.g. textile and clothing, consumer electronics, home appliances) have no choice but to capture more value and more profit, upward or downward, along the value chain (Lardy 2012; Beardson, 2013). This propensity to control more tasks and functions, i.e. internalise, is driven either by technical reasons (to better coordinate activities) or financial reasons in order to secure more profitable segments. Further, global value chains have accelerated this trend with numerous dispersed units where determinants are similar wherever they are located. If motives are still depending on an appropriate fit of ownership advantages and internalisation requirements, the development of external international sourcing requires a high level of explicit coordination. The transaction theory shows that this aim is more efficiently achieved through in-house procedures and routines (Gereffi *et al.*, 2005).

Table 3a provides an overview of the current distribution of motives according to Dunning's conceptual framework whereas table 3b highlights the distribution of the different processes at play according to Mathews' approach.

Table 3a: Motives of Chinese FDI: Europe versus Sub-Saharan Africa

Motive	Europe	Sub-Saharan Africa
Resource-seeking		Main motive due to abundant natural resources
Market-seeking	Still first motive	New motive but rapidly expanding in order to supply local markets, often in relation with exports
Asset-seeking	Rapidly expanding, particularly since the 2008 global financial crisis	
Efficiency-seeking	New motive, in order to acquire highly-qualified people, still scarce in China; and streamline operations regionally	Relocation of Chinese firms, particularly small and medium enterprises, in labour-intensive industries

Source: the authors, using Dunning' conceptual framework.

Table 3b: Processes underlying Chinese FDI: Europe versus Sub-Saharan Africa

Process	Europe	Sub-Saharan Africa
Linkage		Inter-relations with Chinese ethnic communities, or Chinese officials and state support institutions
Leverage	Large financial resources	Large financial resources Political connections
Learning	From previous joint ventures and partnerships in China with Western companies Insights from Chinese failures that occurred in Europe (e.g., TCL)	

Source: the authors, using Mathews' conceptual framework.

4.3. Convergence driven both by global forces and China's internal transformation

Two other arguments can be put forward to explain why determinants and patterns of Chinese OFDI change over time and converge towards global strategies.

4.3.1. Convergence pushed by connected global production and supply chains

As revealed by Baldwin (2012a, b), until the late 1980s, globalisation was associated with a 'first unbundling', which referred to lower trade and transportation costs. From

the early 1990s onwards, globalisation's 'second unbundling' has referred to lower communications and transmission costs: it involves both fractionalisation of stages of production and geographic dispersion of the unbundled stages, all these stages being connected by global supply chains.

Global supply chains work as a force of convergence for firms from developing countries: as shown by Baldwin (2012a, b), developing countries could join supply chains, thus avoiding to spend time in building up their own: latecomers and their multinationals join supply chains and grow because off-shored production brings elements, which Korea and Taiwan took decades to develop (Baldwin, 2011b). The internal logic of global value chains, i.e. fragmentation and geographical dispersion according to tasks to be performed ('research, design and product development activities' upward or 'marketing, sales, distribution, and after-sales services' activities downward), indeed favours uniformity (Sturgeon, 2013).

China's growth was driven by developed country multinationals that invested in developing countries due to low-wages in the sectors of production or assembling components and final goods, along with favourable export promotion policies - i.e. China's processing trade regime (Ma and Van Assche, 2012). Baldwin (2012a, b) emphasises that with the rise of Chinese wages, Chinese firms have a similar behaviour with poorer developing countries and firms, according to the classic Akamatsu (1962) 'flying geese' pattern where early developers move up the value chain and enables countries with lower wages to step in them.

Overall, diversifying and globalising through creeping external international sourcing, which is at the core of global value chains, fosters the road to convergence and commonalities of the motives of Chinese OFDI.

4.3.2 Convergence pulled by the transformation of the Chinese growth model

The transformation of the Chinese growth model from a regime that is driven by inward investment and exporting impetus towards a pattern that is spurred by domestic consumption and imports also fosters commonalities in Chinese firms' FDI projects.

The Chinese growth regime has indeed been driven over a long period of time by exports and investment outlays in manufacturing capacities and economic infrastructures at home. Several converging factors - which are confirmed by historical experience and empirical research -, show that this path is no longer sustainable (Lardy, 2012), and since the early-2010s China's government policies aim at reorienting the Chinese growth model towards a regime that is more driven by domestic consumption and imports. The outburst of the *subprime* financial crisis in 2008 has accelerated this orientation, although it may take time to switch to a new direction due to institutional and political constraints and inertia (Beardson, 2013).

One channel of causality between the transformation of the Chinese growth model and converging motives for Chinese outward FDI refers to the level of development and maturity of the Chinese economy, which is characterised by a continuous increase in living standards. Forces at play are rising urbanisation and educational levels, particularly tertiary education, and a growing middle class that generate a burgeoning and diversified domestic demand (World Bank, 2012) These changes encourage

Chinese multinationals to produce for the domestic market and also to provide overseas markets with more sophisticated goods and services.

Another causality stems from the rapid increase in numbers of privately-owned small and large firms, both in absolute terms and relatively to the numbers of state-owned enterprises, and their increasing move to overseas markets. Indeed, according to official sources (the National Bureau of Statistics of China), the number of registered private companies grew by around 30% for the period 2000-2009 and reached 40 million at the end of 2012.

Chinese private firms share several commonalities. First, they are basically market-oriented and their main goal is to maximise profit. Second, they have in common a family management system. Third, these private firms share the common constraint of securing the financial resources that are required for their development: it is another cause of a more standardised behaviour (Beardson, 2013). Furthermore, private firms are more attracted by large markets and host-country strategic assets. Moreover, contrary to large Chinese state-owned enterprises, they are averse to economic and political risks when choosing investment locations abroad (Amighini *et al.*, 2012).

5. Conclusion

This paper has investigated the determinants and characteristics of Chinese OFDI according to Dunning's framework, both in developed and developing countries, with a particular focus on Europe and Sub-Saharan Africa respectively.

It has shown that Chinese outward investment in Europe follows a learning curve, driven by the initial distance of Chinese investors vis-à-vis host countries. It has also revealed that investment motives have become more complex, i.e. including strategic assets-seeking: the initial motives of market-seeking and export-support increasingly combine with asset-seeking motives. Efficiency-seeking motives, although increasing, remain limited. Chinese investments therefore increasingly engage in merger-and-acquisitions of foreign firms or units of them, which display a certain level of security and on which Chinese investors already have some knowledge.

In contrast, the paper has also revealed that Chinese investment in a developing region such as Sub-Saharan Africa is more driven by resource-seeking motives, and increasingly by motives of improving access to markets, either local or international, as well as efficiency-seeking motives, mainly in labour-intensive sectors.

The comparison of both regions has shown that Chinese OFDI exhibits more commonalities than differences, and converge toward global strategies: Chinese OFDI in the 2010s combine a variety of motives and integrate geographical spaces; they are also shaped by constraints that stem from the transformation of the domestic Chinese growth path towards a more domestic consumption-led model.

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Appendixes

Appendix 1: Chinese official sources for data on outward foreign direct investment

The primary and the most used source, notably by UNCTAD for its annual *World Investment Report*, is the *Annual Statistical Bulletin on China's Outward Direct Investment*, which is compiled by the Ministry of Commerce/MOFCOM. It is co-published by the State Administration of Foreign Exchange/SAFE (People's Bank of China) and the National Bureau of Statistics. Data include OFDI flows and stocks based on investment approvals in the respective year and up to 2006 it only included non-financial OFDI flows. All overseas investments exceeding 10000 US\$ are required to register and obtain approval, but in 2003 the MOFCOM and SAFE introduced a programme that enabled overseas investments of less than \$3 million to be approved by local governments.

Secondary official sources are the *Balance of Payments* and the *International Investment Position* both published by the SAFE. These data are based on actual recorded outflows on a yearly basis.

Source: Rosen and Hanemann (2009).

Appendix 2: Note on the proprietary database on the presence and activity of Chinese firms in Europe

The data used come from several sources but two sources provide the main contributions: Thomson Reuters database for equity investments or mergers-acquisitions (Thomson One), and fDi Markets from the Financial Times for *greenfield* investments. Complementary sources have been used, such as European Investment Promotion Agencies, especially the 'Invest in France Agency', French and foreign press, specialised magazines, corporate websites, along with interviews conducted by the authors.

The data relate to Chinese groups that operate in the industry and services sectors, and which have invested in Europe. They exclude family and individual businesses - e.g., restaurants, small retail businesses or independent import and export offices. The resulting subsidiaries are mainly dedicated to sales or manufacturing activities, with R&D and regional coordination (European headquarters) functions taking off. Apart from the standard threshold of 10% for equity participation, a cut-off is put at 10 employees. The scope includes *greenfield* investments, extensions, equity participations, M&As, joint ventures and also closures.