E-Brief

China: an emerging FDI outward investor

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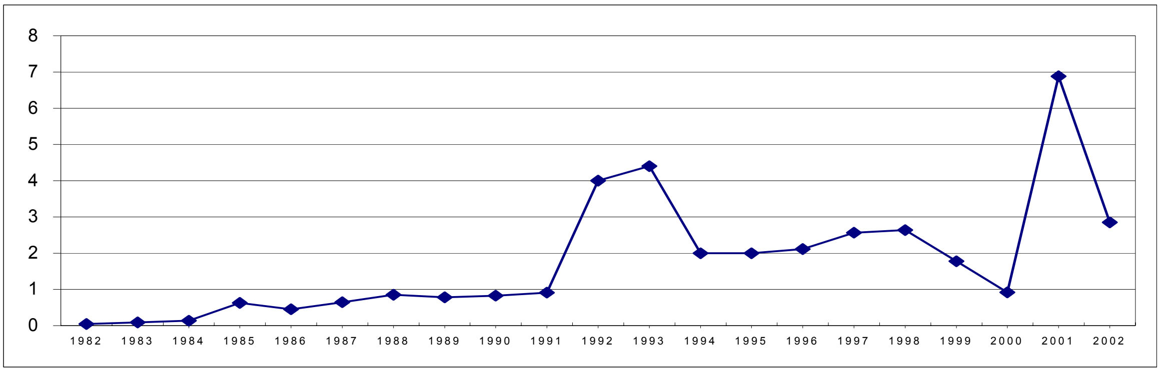
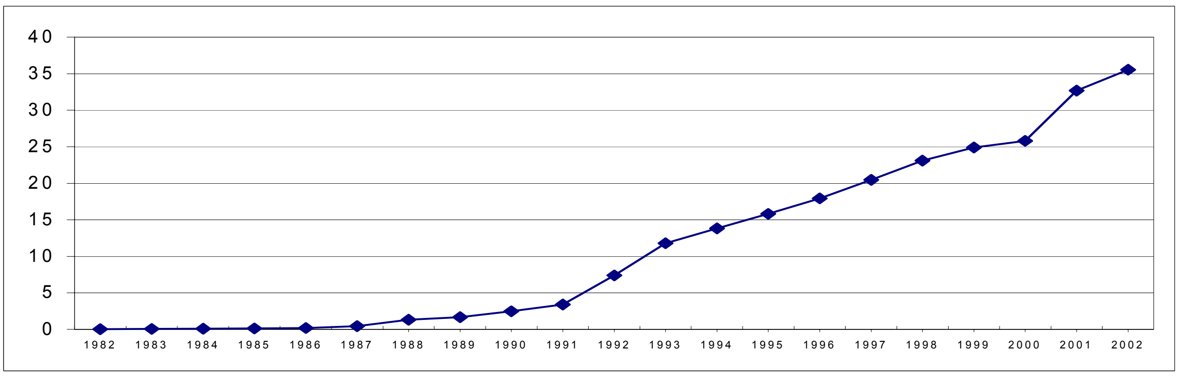
China is not just a magnet for foreign direct investment (FDI), but it is increasingly also a source of FDI, says UNCTAD in a note released today. The recent merger of the television and DVD operations of TCL (China) and Thomson (France), giving majority control to the former, highlights this trend. Average annual outward FDI flows have grown from $0.4 billion in the 1980s to $2.3 billion in the 1990s, contributing to an accumulated book value of at least $35 billion of Chinese outward FDI stock (on a balance-of-payments basis) at the end of 2002. Some 7,000 approved outward investment projects (foreign affiliates) of Chinese non-financial firms are associated with roughly $9 billion of this stock alone, covering trade, transportation, resources exploration, tourism, manufacturing and other activities in 160 countries. Chinese TNCs invest not only in neighbouring countries, but also in Africa, Latin America, North America and Europe. Access to natural resources, markets and the acquisition of strategic assets (including technology and brand names) are the main driving forces. Says Karl P. Sauvant, Director of UNCTAD's Investment Division: "Chinese enterprises are at the threshold of becoming major foreign direct investors in Asia and beyond."

Figure 1. China's outward FDI flows, 1982-2002
(Billions of dollars)



Source: UNCTAD, FDI/TNC database, based on IMF's balance-of-payments statistics.

Figure 2. China's accumulated outward FDI flows, 1982-2002
(Billions of dollars)



Source: UNCTAD, FDI/TNC database.

Note: Data from 1985 to 1989 are from national sources. Data after 1989 are estimated by accumulating flows.

With an average of $2.3 billion, China's average annual outward FDI flows during the 1990s (figure 1) were only slightly lower than those of the Republic of Korea ($2.9 billion) during that period. Accumulated Chinese outward FDI flows exceeded $35 billion in 2002 (figure 2), which is, however, only about as much as the outward FDI stock of Ireland or Portugal.

As a result, an increasing number of Chinese firms are now among the largest TNCs from developing countries, in terms of foreign assets: in 1994, only seven Chinese enterprises were among the top 50 largest TNCs from developing economies and only one of them had foreign assets above $2 billion; by 2001, twelve Chinese TNCs were in the top 50 largest TNCs from developing economies, and as many as six had foreign assets of above $2 billion (table 1).

Table 1. The TNCs headquartered in China among the top 50 largest TNCs from developing countries, ranked by foreign assets, 1994 and 2001

(Millions of dollars, number of employees)

1994

Ranking by				Assets		Sales		Employment		TNI[a]
Foreign assets	TNI[a]	Corporation	Industry	Foreign	Total	Foreign	Total	Foreign	Total	(Per cent)
1	b	China State Construction	Construction	2 189	b	1 000	b	b	b	b
2	b	China Chemicals Imp and Exp Corp.	Trading	1 915	b	7 914	b	b	b	b
3	b	China Metals and Minerals Corp.	Trading	710	b	2 270	b	b	b	b
4	b	China Harbor Engineering Group	Construction	559	b	409	b	b	b	b
5	b	SHOUGANG Group	Metals	446	b	980	b	b	b	b
6	b	China National Cereal, Oils and Foodstuff Imp and Exp Corp.	Trading	440	b	6 200	b	b	b	b
7	b	China Iron and Steel Industrial and Trading Group	Metals	188	b	257	b	b	b	b

2001

Ranking by				Assets		Sales		Employment		TNI[a]
Foreign assets	TNI[a]	Corporation	Industry	Foreign	Total	Foreign	Total	Foreign	Total	(Per cent)
1	3	China Ocean Shipping (Group) Company	Transportation	9 382	16 926	2 149	6 757	4 124	74 669	30.9
2	4	China National Offshore Oil Corporation	Petroleum	4 814	8 635	976	3 669	13	24 406	27.5
3	5	China State Construction Engineering Corporation	Construction	3 739	8 099	1 818	5 790	6 833	236 464	26.8
4	1	China National Cereal, Oils and Foodstuff Imp and Exp Corp.	Trade	3 707	5 014	6 446	13 004	359	25 000	41.6
5	12	China National Petroleum Corporation	Petroleum	3 350	83 254	1 600	41 089	4 400	1 167 129	2.8
6	2	China National Chemicals Imp and Exp Corp.	Trade	2 788	4 928	9 148	16 011	350	7 950	39.4
7	9	SHOUGANG Group	Steel and iron	969	6 675	467	4 401	2 086	179 997	8.8
8	6	China National Metals and Minerals Imp and Exp Corp.	Trade	729	2 797	998	4 277	570	7 145	19.1
9	7	China Harbor Engineering Company	Construction	520	3 271	6 579	17 826	812	70 160	18
10	11	Shanghai Baosteel Group Corporation	Steel and iron	383	19 389	1 211	8 643	50	113 896	5.3
11	8	Haier Group Corporation	Refrigerator production	328	3 188	976	7 260	803	31 281	8.8
12	10	ZTE Corporation	Telecommunication equipment	17	1 205	260	1 685	120	12 961	5.9

Source: UNCTAD, *World Investment Report 1996,* pp. 34-35, and *World Investment Report 2002,* p.61.

[a] TNI stands for "transnationality index". The transnationality index is calculated as the average of the following three ratios: foreign assets to total assets, foreign sales to total sales and foreign employment to total employment.

[b] Data are not available.

Given the country's rapid economic development and the Government's interest in encouraging outward FDI, Chinese investments abroad can be expected to increase further.[1] In his speech at the ASEAN Business and Investment Summit on 7 October 2003 in Bali, Indonesia, Mr. Wen Jiabao, Premier of the State Council of the People's Republic of China, announced that "the Chinese Government will encourage more of its companies to make investment and establish their businesses in Asian countries."[2] Added Vice-Premier Wu Yi one month later "…we will actively foster our own multinational companies ….We will create all kinds of (favourable) conditions to help our multinational companies further explore overseas markets and engage more strongly in global economic competition and co-operation".[3] Should the Chinese currency strengthen against other major currencies, more Chinese enterprises could be potentially pushed to invest abroad because of relatively lower investment cost and to avoid the disadvantage of less competitive export prices at home.

The Ministry of Commerce's statistics – which capture only a part of total outward FDI stock, namely $9 billion[4] – suggest that about 60% of the approved Chinese outward investment during 1979-2002 was destined to Asia (table 2). North America was the second most popular destination, followed by Africa and Latin America.

The lion's share of Chinese outward FDI flows went to Hong Kong, China (table 3). They are partly influenced by geo-cultural affinity and strategic reasons such as raising funds in the capital market there or using Hong Kong, China, as a springboard for channelling investment elsewhere. For instance, Fujian Enterprise (Holdings) Ltd., China International Trust and Investment Corporation and Guangdong Enterprise (Holdings) Ltd. invested in other countries through their affiliates in Hong Kong, China.[5] The United States is the second most popular destination for Chinese outward FDI flows (table 3). These two economies accounted for more than half of the cumulative approved Chinese outward FDI value during 1979-2002. Despite this concentration, Chinese outward FDI flows are reaching more and more countries.

Table 2. China's approved FDI outflows, by region, 1979-2002

Rank[a]	Region	1979-2002 Number of projects[b]	1979-2002 Cumulative investment value (Millions of dollars)
	Total	6 960	9 340.0
1	Asia	3 672	5 482.3
2	North America	847	1 270.5
3	Africa	585	818.1
4	Latin America	362	658.2
5	Europe	1 194	561.1
6	Oceania	300	549.8

Source: Ministry of Commerce of China, *The Almanac of China's Foreign Trade and Economic Cooperation*, 2003.

[a] Ranked by investment value.
[b] The number of projects refers to approved investment projects involving Chinese enterprises.

Table 3. China's approved FDI outflows, top 30 destinations, 1979-2002

(Millions of dollars)

Rank[a]	Economy	1999		2000		2001		2002		1979-2002	
		Number of projects[b]	Value	Number of projects[b]	Value	Number of projects[b]	Value	Number of projects[b]	Value	Cumulative number of projects[b]	Cumulative investment value
	Total	220	590.6	243	551.0	232	707.5	350	982.7	6 960	9 340.0
1	Hong Kong, China	24	24.5	15	17.5	26	200.7	40	355.6	2 025	4 074.3
2	United States	21	81.1	15	23.1	19	53.7	41	151.5	703	834.5
3	Canada	1	0.1	8	31.7	4	3.5	4	1.2	144	436.0
4	Australia	3	1.7	13	10.2	6	10.1	15	48.6	215	431.0
5	Thailand	3	2.0	6	3.3	9	121.3	5	3.9	234	214.7
6	Russian Federation	12	3.8	14	13.9	12	12.4	27	35.5	482	206.6
7	Peru	1	75.7	1	0.001	2	3.1	..	..	20	201.2
8	Macao, China	3	0.2	4	0.5	6	2.4	2	2.0	229	183.7
9	Mexico	2	97.0	1	19.8	1	0.2	1	2.0	45	167.4
10	Zambia	4	6.7	3	11.6	3	4.3	1	0.3	18	134.4
11	Cambodia	13	32.8	7	17.2	7	34.9	3	5.1	61	125.0
12	Brazil	1	0.5	3	21.1	4	31.8	8	9.3	67	119.7
13	South Africa	14	12.8	17	31.5	2	12.4	3	1.7	98	119.3
14	Republic of Korea	1	0.1	5	4.2	2	0.8	7	83.4	62	107.8
15	Viet Nam	2	6.6	17	17.6	12	26.8	20	27.2	73	85.0
16	Japan	1	0.5	2	0.3	6	1.7	11	18.2	236	82.1
17	Singapore	6	2.9	6	1.0	3	0.4	6	2.1	172	71.7
18	Myanmar	1	6.6	7	32.9	3	1.8	5	15.8	38	66.1
19	Indonesia	0	19.0	1	8.0	2	0.6	6	3.7	59	65.0
20	Mali	1	1.2	1	28.7	..	..	..	..	5	58.1
21	Mongolia	15	40.3	12	5.4	7	4.5	7	3.4	69	56.6
22	Germany	1	0.3	1	1.6	3	3.5	6	2.8	150	51.5
23	New Zealand	..	..	..	..	2	0.9	2	0.9	26	48.7
24	Egypt	5	3.8	3	9.7	2	1.4	3	16.3	27	48.5
25	Oman	..	..	..	..	..	..	1	17.5	70	47.2
26	Papua New Guinea	..	..	1	0.9	..	..	..	..	20	44.7
27	Nigeria	2	1.6	1	2.6	8	6.4	9	11.4	49	44.3
28	Tanzania	3	16.3	1	1.0	..	..	2	0.4	19	41.3
29	Kazakhstan	7	17.2	5	7.7	1	0.3	3	26.9	51	39.6
30	Lao PDR	1	2.0	2	24.4	1	1.2	2	61	18	36.6

Source: Ministry of Commerce of China, *The Almanac of China's Foreign Trade and Economic Cooperation, 2000-2003.*

[a] Ranked by cumulative investment value.
[b] The number of projects refers to approved investment projects involving Chinese enterprises.

A number of factors have contributed to China's outward FDI:

- Chinese firms that are exporting are investing abroad to support their exports, to service their markets also through FDI or to expand their market presence. In markets with which Chinese has considerable trade surpluses (e.g. the United States), FDI may increasingly become an alternative vehicle to supply those markets. As part of such a strategy, Chinese firms are also buying local distribution networks. In addition, sluggish domestic demand in China and excess industrial productive capacity since the late 1990s in certain industries (especially in machinery and electronic appliances) have encouraged Chinese firms to look for growth opportunities abroad. These companies include Chinese TV producers such as Konka Electronics, Skyworth and Changhong Electronic Groups, and household appliances manufacturers like Haier and Guangdong Midea Group. The recent merger of the television and DVD operations of TCL (China) and Thomson (France), with the former having a 67% stake in the joint-venture entity known as "TCL-Thomson Electronics", is an example.[6]

- Growing financial strength and exposure to international business have played a part in encouraging Chinese firms to venture aboard. The success of China in attracting FDI flows induces Chinese outward FDI through demonstration and spillover effects on domestic firms. Growing competition at home also encourages Chinese firms to go abroad, adopting a diversification strategy in generating revenues and transferring matured industries to low-income countries (e.g. bicycle production in Ghana and video players in South-East Asia). Once abroad, Chinese TNCs begin to acquire advantages related to "transnationality" – confidence in, and knowledge of, operating in a foreign environment. More Chinese firms are aspiring to become global players by investing and operating abroad.

- Chinese FDI in developed countries is rising. The motives for such investment include access to technology and other strategic assets such as brand names, as well as access to markets. The aspiration to go abroad to build or acquire international brand and advance product development has also become a major factor. With growing financial reserves, Chinese TNCs have gone on a buying spree abroad to acquire assets whose prices may have been depressed by the current international economic downturn. For instance, TCL bought the bankrupt Schneider Electronics (Germany) in 2002, for $8 million; Huayi Group of Shanghai bought the bankrupt Moltech Power Systems (United States) for an estimated $20 million; BOE Technology acquired Hynix Semiconductor's flat panel display unit (Republic of Korea) for $380 million in February 2003 and is buying a 26.4% stake in TPV (a PC monitors manufacturer) for about $135 million; Shanghai Haixing Group bought Glenoit Corp-Specialty Fabrics in United States for $14 million; Shanghai Electric Group bought the financially troubled Akiyama Publishing Machinery Company in Japan; D' long Group acquired Fairchild Dornier 728 passenger jet programme in Germany; and China Telecom is negotiating to buy Excelcomindo (a cellular operator) in Indonesia. M&As and alliances are also a strategy used by Chinese firms to enhance their competitiveness. For instance, the merger of TCL's television and DVD operations with Thomson (France) will give the former the brand name of Thomson in Europe and RCA in the United States; and Huawei Technologies has joint-venture agreements with Siemens, NEC, Matshushita and Infineon.

  Accessing foreign technology also takes the form of establishing R&D centres in developed countries. Huawei Technologies and ZTE Corporation have each established an R&D centre in Sweden;[7] Guangdong Glanz Group Co. an R&D centre in Seattle, Konka (an electronics company) an R&D facility in Silicon Valley; Haier an R&D centre in Germany and a design centre in Boston, United States; and Kelon a design centre in Japan. In 2002, eight Chinese companies formed technological alliances with or acquired Danish firms, mostly for accessing technology.[8]

- The need to access natural resources abroad has encouraged Chinese firms to invest in oil, gas and mining activities in resource rich countries (table 4). Most of them are state-owned enterprises that acquired minority or majority stakes in foreign companies. Sinopec, Petrochina and China National Offshore Oil Corporation (CNOOC) have invested in 14 countries, including Indonesia, Kazakhstan, Myanmar, Sudan and Yemen. Baosteel entered into a joint-venture with Hamersley Iron

(Australia) and is negotiating a joint-venture with Companhia Vale do Rio Doce (Brazil) in iron ore production involving a $8 billion steel plant in Brazil. Firms such as COFCO, China National Chemicals Export and Import Corporation, and China Metals and Minerals have invested in Africa, and China National Petroleum Company in Sudan (box 1).

Table 4. Selected Chinese resource-seeking FDI, 2002

Acquiring firm	Target firm/activity	Industry	Host location	Equity interest and acquisition value
Huaguang Forest Co. Ltd.	Rayonier Inc. (East Coast Timberland operations)	Timber tracts	New Zealand	100% equity stake for $ 7.7 million
China Petroleum & Chemical Corporation	Oil field	Oil	North Africa	75% equity share for $394 million
Petro China Co. Ltd	Devon Energy-Indonesian Oil	Oil	Indonesia	100% stake for $262 million
Baosteel	Joint venture with Rio Tinto's Hamersley Iron Unit in iron ore mining	Iron ore	Australia	46% stake for $30 million
CNODC and CNPC	Salyan Oil Ltd	Oil	Azerbaijan	30% stake for $52 million in 2 oil fields
China National Offshore Oil Company Ltd	Repsol-YPF SA	Oil	Indonesia	Nine subsidiaries in five oil and gas fields for $585 million
CNOOC	Tangguh Gas Fields	Gas	Indonesia	12.5% stake from BP for $275 million
China National Chemical Import and Export Corporation	Atlantis subsidiary	Oil field service	Norway	$105 million

Source: UNCTAD, cross-border M&A database.

Box 1. China National Petroleum Company's (CNPC) investment in Sudan

In 1995, CNPC reached an agreement to form a joint-venture with the Government of Sudan and other partners to produce oil jointly. CNPC invested $757 million in the $1.7 billion project and has a 40% share in the joint-venture known as Greater Nile Petroleum Operating Company. Talisman Energy, a Canadian company, as well as Sudanese and Malaysian companies are partners of the joint-venture entity. The company began operation in 1999.

Source: UNCTAD.

- Avoiding trade quotas for exports to developed countries has prompted some Chinese firms to invest abroad. For instance, some Chinese textile companies invested in Cambodia to take advantage of quota-free access for exporting to the United States and the European Union. Guanda Import and Export Co. Ltd. invested in Cambodia for "the reason that the United States and members of the European Union have no quotas on the great majority of textiles imported from the Kingdom of Cambodia".[9] Other Chinese textile companies have also invested in Africa to utilize advantages of host countries (box 2).

Box 2. Shanghai Huayuan Group Corporation's investment in Nigeria

In 1997, Shanghai Huayuan Group Corporation (SHGC), together with a Nigerian company, acquired a textile company owned by a French company. SHGC invested $2.4 million and owned 80% of the company. Production was restored in August 1997 with an annual production capacity of 1,500 metres of printed and dyed cloth. In 2000, the partners expanded the operation with an additional capital injection of $6 million for building a cotton mill with a production capacity of 13,000 spindles. In the same year, the joint-venture operation made a net profit of $0.76 million and became one of the largest taxpayers in Nigeria and employing about 1,000 people.

Source: UNCTAD.

- Aside from "push" factors, Chinese outward FDI is also motivated by "pull" factors such as a host country's favourable investment policies, including incentives and other location-specific advantages (table 5). For example, a number of Chinese companies are reported to have chosen the United Kingdom to take advantage of investment grants.[10]

More generally, the more China becomes integrated in the world economy and Chinese firms become subject to international competition through imports and inward FDI, the more these firms will invest abroad – to acquire a portfolio of locational assets that helps them to improve their international competitiveness.

Table 5. Summary of survey results for 100 Chinese TNCs, 2000[a]

(Per cent of responding firms)

Why invest overseas?	What is most attractive factor in host country?	Where is your priority region?
47.1%: expanding overseas markets	32.0%: host country's privileged policies	32.0%: Africa
16.9%: better profits		20.0%: Southeast Asia
14.5%: sluggish demand in China	28.7%: requiring relatively small amount of investment	18.0%: Latin America
12.1%: export to third country		9.3%: Middle East
9.3%: competition with export from China	22.5%: cheap labour	8.7%: Eastern Europe
		8.0%: Central Asia
	8.4%: cheap land and proximity to raw materials	4.0%: Others

Source: Research Team of MOFTEC's Offshore Plant Project, "Inward flow should be accompanied by outward flow: policy analysis of China's offshore plant operations," *International Trade*, 5 (2000), pp. 9-13 (in Chinese), cited in Mark Yaolin Wang, "The motivations behind China's Government-initiated industrial investment overseas", *Pacific Affairs*, 75 (2002), 2, p. 187-206.

[a] 100 out of the 170 enterprises surveyed replied.

The Government has encouraged Chinese firms to invest abroad, in particular to secure the supply of resources to meet the growing demand at home and transferring matured technologies in which Chinese firms have a comparative advantage (e.g. electronics, textile and garment processing industries). It has also supported Chinese small and medium-sized enterprises to expand in international markets. Provincial administrations such as Guangdong and Shanghai have also actively encouraged their domestic enterprises to invest abroad. The Ministry of Commerce has already implemented policy measures, including a relaxed approval system for outward FDI. China has signed bilateral investment treaties with 103 countries and double taxation treaties with 68 countries as of December 2002 to facilitate its FDI abroad. The Export-Import Bank of China, through its financing facilities, has also played a role in supporting Chinese outward investment. Other measures to encourage Chinese firms to invest abroad include easier access to loans from commercial banks, foreign exchange and preferential policies such as corporate income tax exemption.

Increased Chinese FDI flows to various countries underline China's role as an emerging home country of TNCs. Recognizing the potential for China's outward FDI to grow further, various investment promotion agencies[11] have set up offices in China to court Chinese firms that are potential outward investors. They include agencies from Denmark, Malaysia, Scotland, Singapore, Sweden, Thailand and Wales.

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[1] The Ministry of Commerce (Mofcom) is working on a set of detailed policy measures to implement a "go out" strategy. Some measures are already being implemented.

[2] See the speech of Mr. Wen Jiabao, Premier of the State Council of the People's Republic of China entitled "China's Development and Asia's Rejuvenation", presented at the ASEAN Business and Investment Summit on 7 October 2003, Bali, Indonesia.

[3] Quoted in *China Daily* (World Economic Development Declaration Conference, Express, supplement), 7 November 2003.

[4] The Mofcom data refer to approved outward FDI flows and are based on cumulative basis from 1979 up to the end of 2002. These data do not include, for the period 1979-2002, reinvested earnings, intra-company loans and non-financial and private sector transactions. (Approval is required to obtain foreign currency.) These data, as the data based on the balance-of-payments, underestimate the size of the outward FDI stock of Chinese firms as they do not capture the amounts invested abroad by those firms using for example earnings from exports or loans raised in foreign capital markets.

[5] FDI by the various ministries of the Government of China or provincial and municipal authorities have also contributed to the concentration of Chinese investment in Hong Kong, China. They include, for instance, FDI made by the Ministry of Communication, Mofcom (previously known as Ministry of Foreign Trade and Economic Cooperation) and the Bank of China.

[6] Thomson will have the option to exchange its share within 18 months for an undisclosed stake in TCL International, which would then wholly own TCL-Thomson Electronics.

[7] There are currently 12 Chinese companies in Sweden, with most investment being in the information and communication industry.

[8] Encouraged by Chinese interest in Denmark, Invest in Denmark seeks to promote the telecommunication and biotechnology industries to Chinese investors.

[9] See http://www.chinapages.com/zhejiang/shaoxing/IE.

[10] See "PRC investment in the United Kingdom", *China Focus*, March 2003 (http://fiduciachina.com/Information/ Newsletter/904-1600.html/view).

[11] Some of these agencies also assist their national firms to invest in China.