

International Conference
**Performance of BRIC:
An Economic Analysis**

Centre for Economic Studies and
Planning, JNU, New Delhi

FMSH/EHESS, Paris

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Chinese FDI

Between Strategic Assets Seeking and Firms Multinationalisation

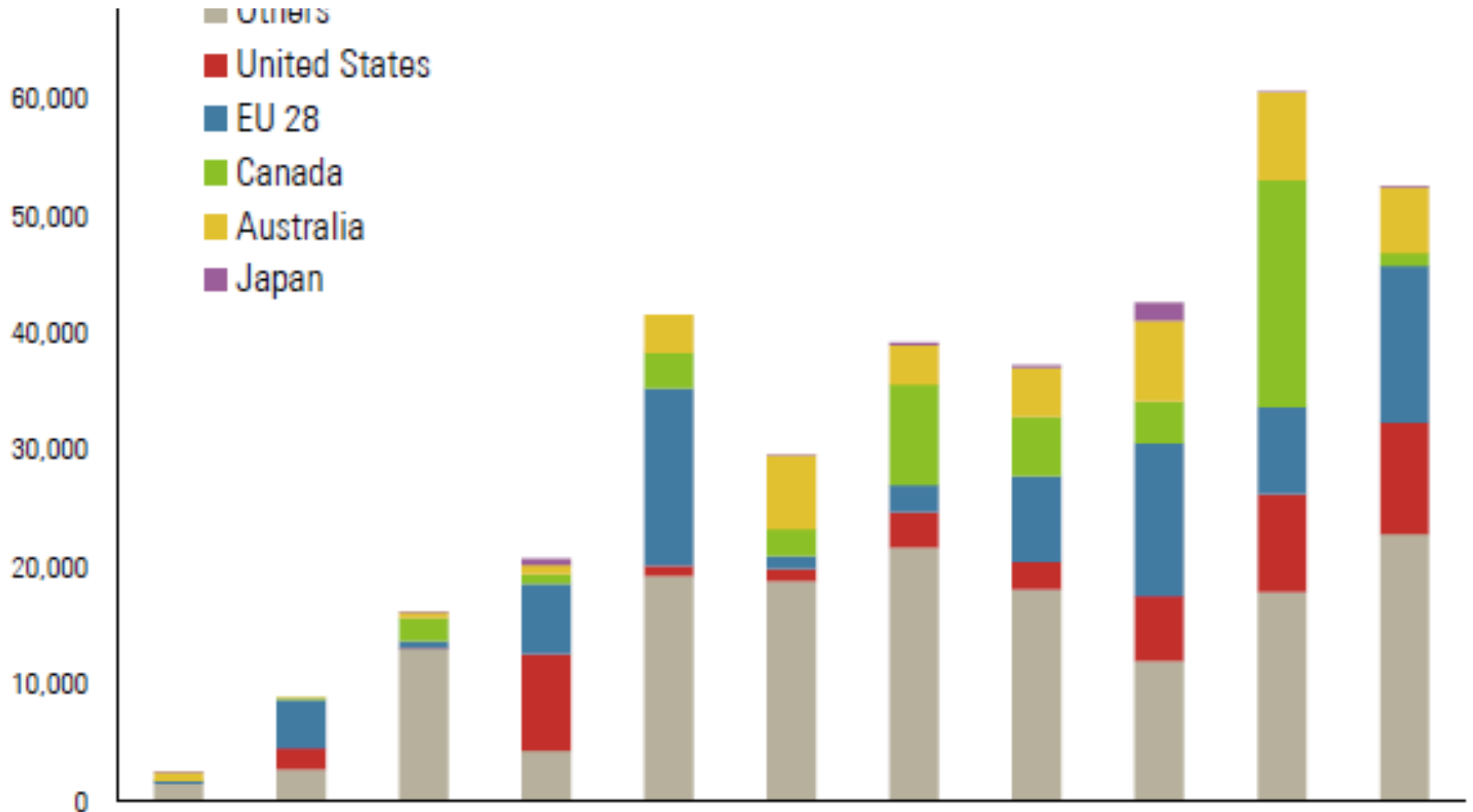
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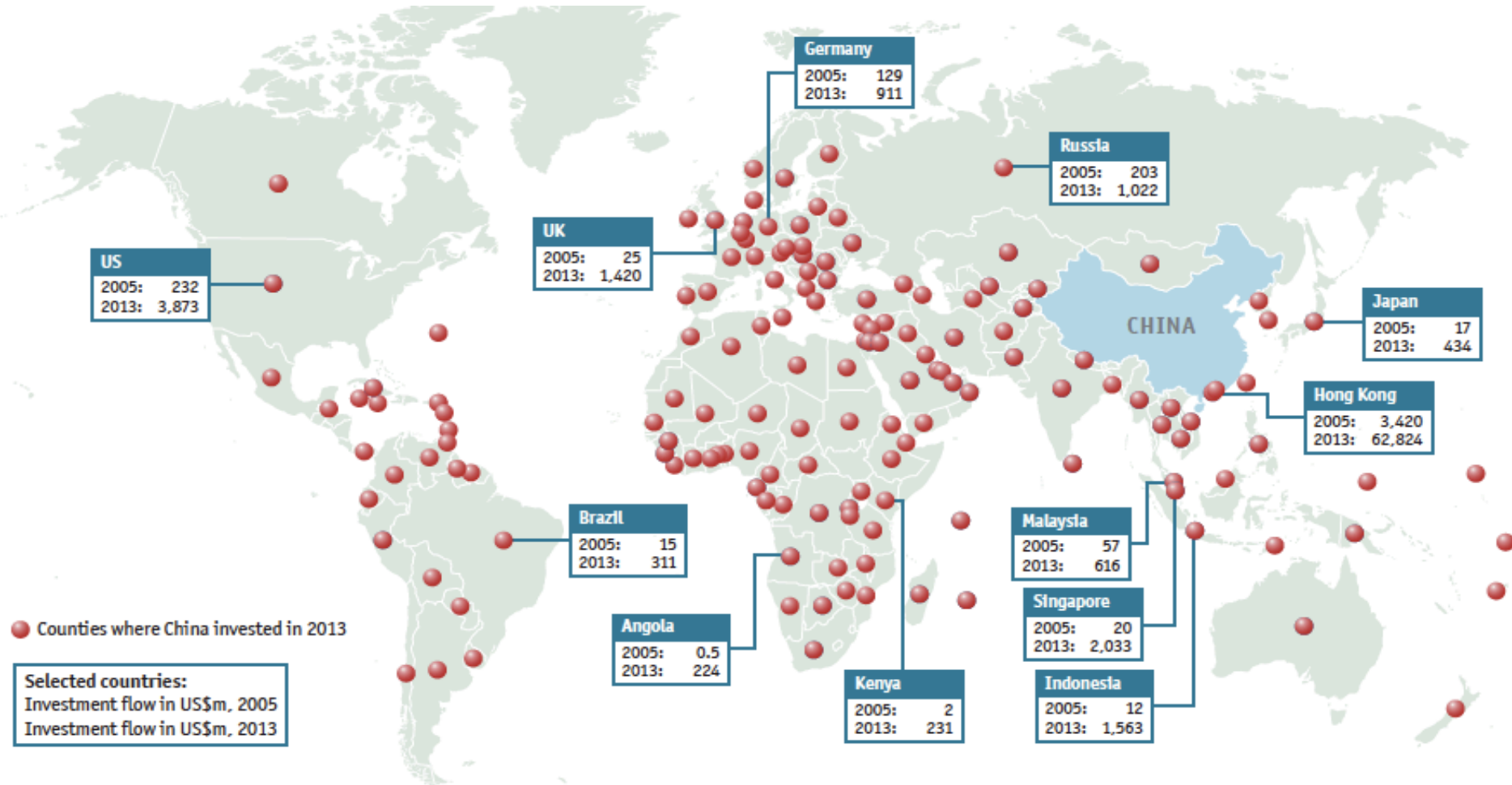
Main Points

- The internationalization of Chinese firms towards High Incomes Market Economies (HIME)
 - seeking strategic assets, multinationalisation, minority stakes?
 - A Threat for High Tech Western Companies?
- Is Catching-up Possible?
 - "Us and them" the technology gap, limited resources, expertise availability, Western constraints against take over
 - Entry modes: European Countries(EU-28) Specificity?
- Learning Curve, Markets Opening : an Accelerating Effect?

Chinese FDI World Distribution 2004-2014



Spreading Over the World



Asset Seeking or Multinationalisation?

- Chinese FDI
 - North: Asset Seeking, Brands, Markets for Acquiring Products with Higher Value Added
 - South: Raw Materials (minerals, agricultural products), Markets for low/ average VA Products
- Real Multinationalisation of Chinese Firms?
 - Real Chinese Globalized Groups? Only Few
 - Absorption of Technology Capabilities to Produce the Innovations Needed in China

Plan

- FDI from Emerging Economy: Reminders
- "Who are We, Who are They? "Two Distinct Trajectories in the » Wild Capitalist Globalization "(P. Nolan)
- A Constrained Offensive? Entry modes of Chinese companies in Europe (Ph. Le Corre and A. Sepulchre)
- Recent Data on Entry on HIME and issues
- Conclusions

The Big Divide

- Ownership: SOE, Non-SOE
- US vs. Europe?
- Technologies: low or high?
- Asset Seeking vs. Markets Expansion
- Hiding Capital, Round tripping, Valorisation
- Majority vs Minority Stakes
- Manufacturing vs. Finance, Real Estate
- Specialization, Deepening vs Diversification
- MNC and World Strategy or Skinning Up and Back to China?
- Market Growth: China or the World?

FDI Outflows from Emerging Economies

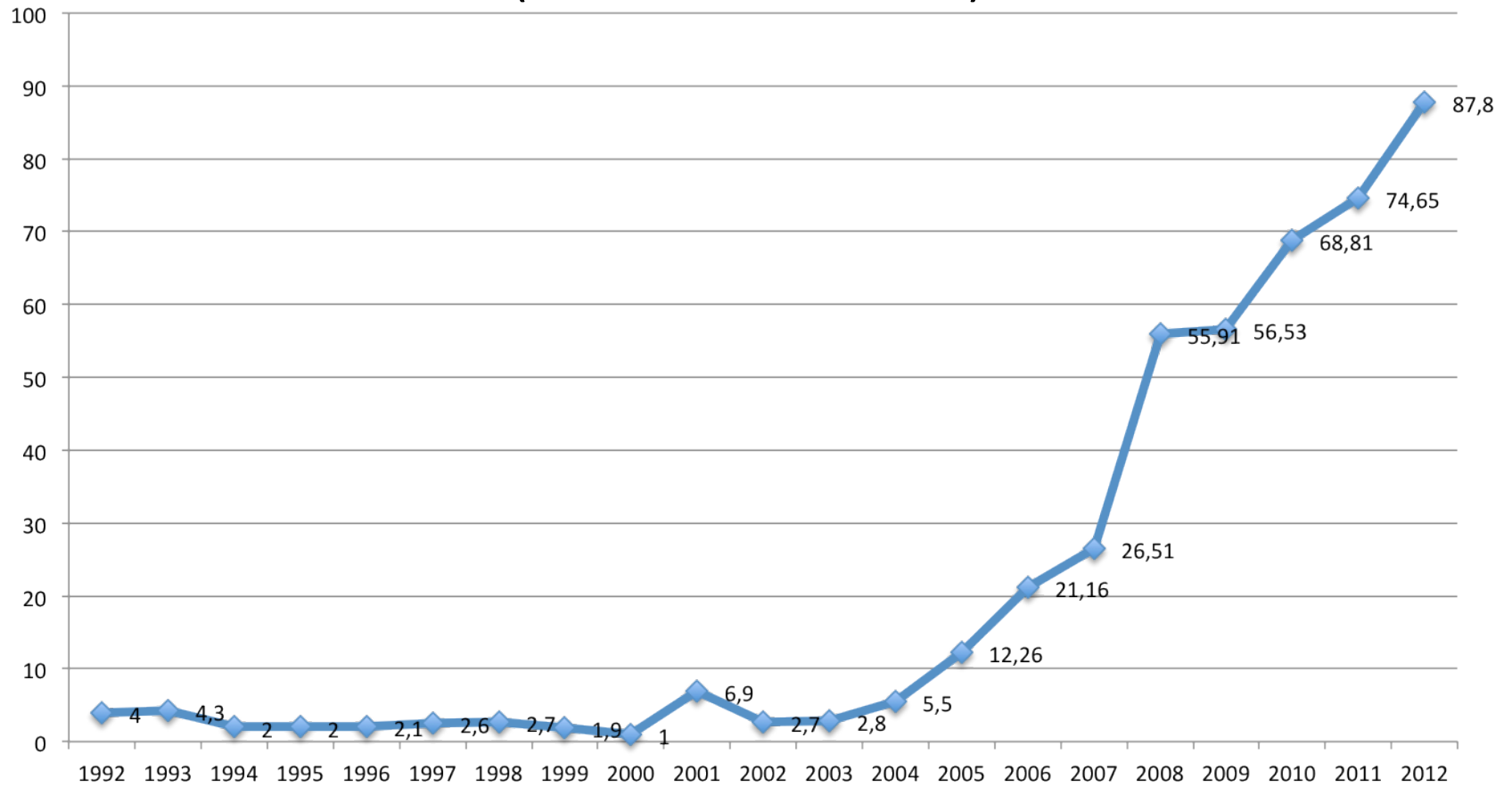
- South-South:
 - Horizontal FDI: market research, factors (raw materials)
 - Rise in internal costs (Chinese FDI -> Vietnam)
 - Low / medium VA. No value chain content: Lat Am, Africa ..
- South-North
 - More Vertical investment , focused on segments, access to higher technologies, brands, markets (more difficult): international value chain?

Outflows from China...

- A « Politique de la Grandeur »: *Going global*
- Circumvent Reluctance of Foreign Firms in China to Transfer Technology (Protection of Intellectual Property, WTO)
- Limitation of Chinese Stock Markets and HK (Alibaba goes to NYSE for IPO)
- Escaping the State Control: Circular Investment, Capital Flight
- Build Financial Platforms from Tax Havens: Cayman Islands, British Virgin Islands ...

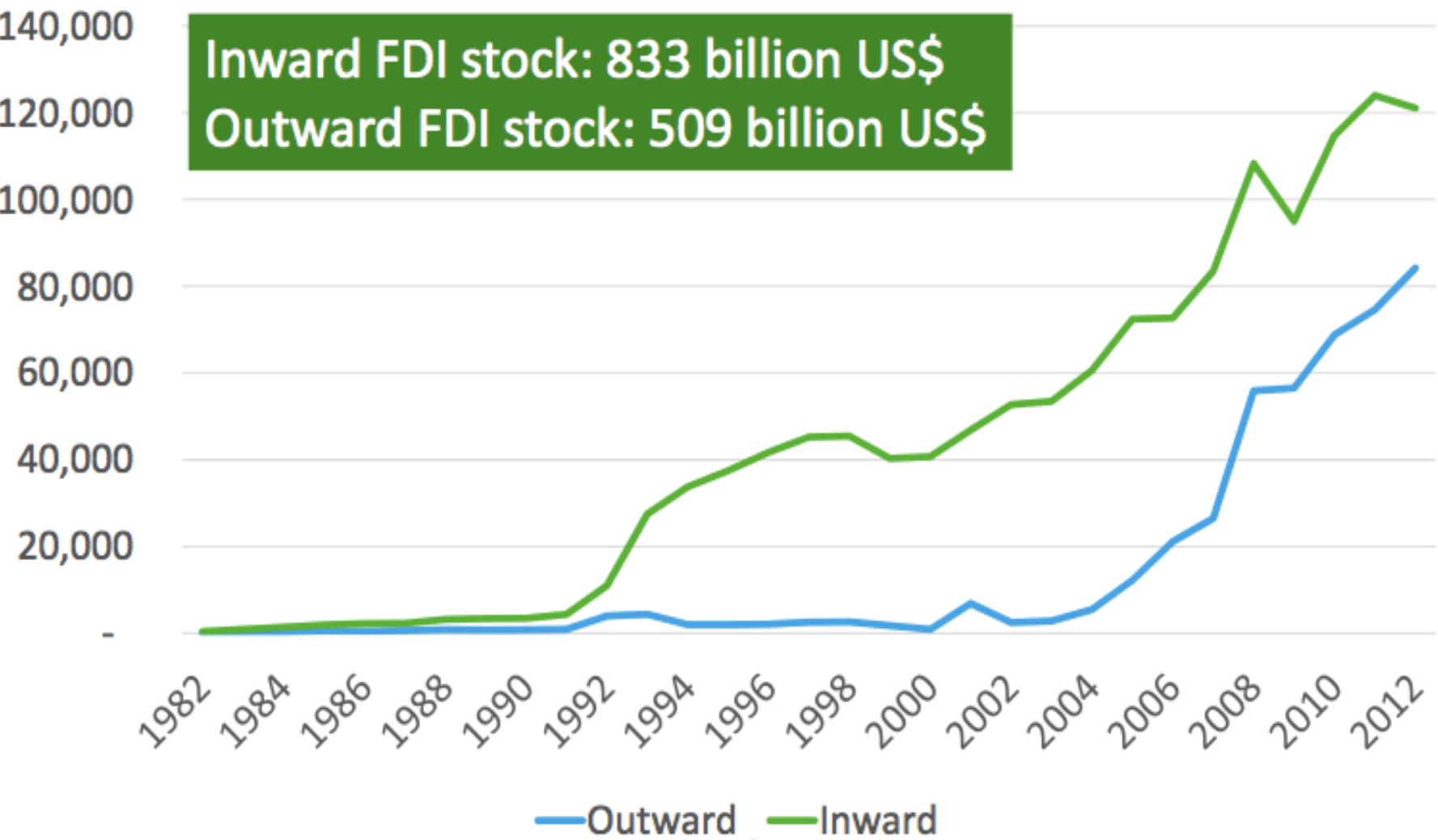
Flow of Chinese FDI

(Unit: 1 bn de USD)



China: Inward & Outward Flow

Inward FDI stock: 833 billion US\$
Outward FDI stock: 509 billion US\$



Among MNC from Emerging Economies

- Of the 100 most Advanced and Internationalized Companies from Emerging Economies (BCG Index)
 - > 40 are Chinese, almost from all sectors, mostly state enterprises: high leverage, access to credit, implicit subsidies
 - India > 24: mainly high technology, more value-added products. private conglomerates
 - Russia, Brazil, Mexico: < 10 per country

Theories: Traditional

- Since Vernon (1979), Multinational Third World and the product life cycle (Lall Wells)
- The Localized Technological Change and the Theory of Technological Accumulation (Cantwell and Tolentino)
- The Eclectic Paradigm and the Investment Development Path (Dunning)

Recent Theories

- Matthews, Moon and Roehl, Luo Tung
- Key elements:
 - Motivated by specific assets seeking
 - Ex-ante comparative disadvantages
 - Partnerships are essential: Leverage effects
Limitation, Learning
 - Accelerated Multinational Growth
- Schumpeterian theories, evolutionists

From Emerging Economy, a Variety of Companies Operate Internationally

- **Totally multinationalized: MNC from DE: Bharat Forge, Tata Group and CEMEX. Baby born MNC (China)**
- **Regional actors: want to internationalize, but various limitations: VinaCapital (VN) PKO (PL) CEZ (R. Tch)**
- **Global providers: seek resources lacking in their country of origin: CNOOC (China), Reliance Petroleum Limited (India)**
- **Global sellers: produce and supply at home, also sold outside: Gazprom (Russia)**
- **Actors on multi-regional niches: smaller companies operating in several regions in niche sectors, based on the technology or innovative processes (Israel).**

"Who are we, who are they? »

- Peter Nolan: *Is China Buying the World ?*, 2012
- Two distinct trajectories in the "wild capitalist globalization »
 - In HIME: at the heart of globalization, deep restructuring of firms
 - M & A, concentration in the industry, finance
 - Advance, breakthrough in many areas of innovation, R & D, organization, infrastructures
 - In China:
 - Strong economic growth, accumulation of financial resources (export.) restructuring but technological gap increases,
 - limited financial resources, weak multinationalisation

« Who Are We? »

- In HIME, strong movement of M&A
 - In industry, banks, finance.
 - Generated significant amount capital In the last 15 years
 - Inward FDI stock in developed economies: 10795 bns of \$ (69% global stock) against 4368 bns (28%)
 - outbound FDI stock respectively \$ 14,000 bns (84%) against 2546 bns (15%)
- Biggest Western groups:
 - > 50% -> 80% of their business abroad
 - Capitalization: Exxon + Apple = Chinese Sovereign Fund

Increasing Domination of Developing economies?

- A new industrial and financial system
 - nesting firms between developed countries at the heart of each national productive system(more Europe FDI -> US than Asia)
- Companies of EE in FT, Forbes rankings
 - Companies operating in traditional industries (mining, metallurgy), protected (banks), usually firms States
- -> Western MNCs in globalization:
 - Actors / beneficiaries in terms of products, volumes, innovation, profitability, market domination

«Who Are They » (Chinese Companies)

- A complex ecosystem, dualistic (Zhao Wei)
- A state sector that is largely restructured
 - 80 "national champions" in traditional sectors, medium and high technologies,
 - Direct and indirect support of the State: RD, credit, subsidies.
- A « non-state" sector with many entrants (Geely)
 - Bear the risk, no access to R & D nor public funding from the state.
 - Mainly original equipment manufacturing (OEM)
 - Less constrained, more entrepreneurship
- Hybrid firms at the frontier: Lenovo, Haier,

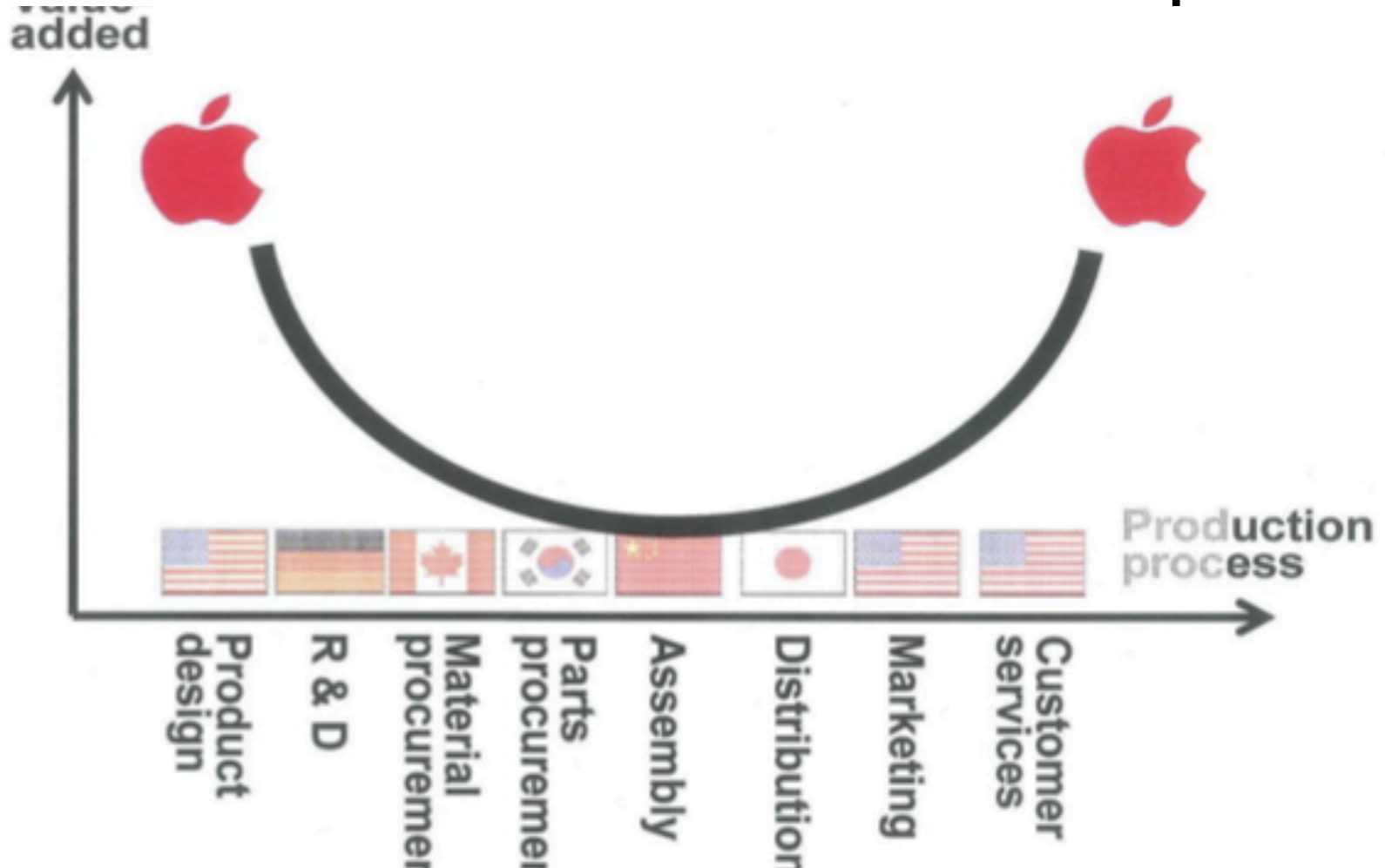
Asymmetric cooperation?

"Chinese firms are facing global companies that carry the competitive struggle deep into the Chinese economy, with their international production systems. In terms of military strategy, large multinational companies conduct the "war" in the camp of the enemy, enter China in order to weaken local businesses, combat capability before they can build capacity outside the country "P. Nolan

A limited cooperation?

- The facts:
 - Domestic innovations still weak, dependent on foreign patents, no major technological breakthroughs
 - Foreign products dominate the market (8 of 10 cars of foreign brands in China ..)
- Recent move
 - Increase of spending on national research and development (level of Japan),
 - accelerate technology transfer, pushing Foreign invested Firms to Cooperate
 - *Going global*: The way to overcome this

Asset Seeking: Toward the End of China as the « World Workshop »?



A Limited Multinationalisation?

- Weakness:
 - Of operations carried out in Europe, the United States
 - Of capitalization of multinational firms
 - Of Methods of financing: limited capacity of banks
 - Of Integrating via the multiplication of sites: pb international management, intercultural
- Acquisition
 - of bankrupt companies: IBM, Volvo, McCormick, Club Med ..
 - Of segments of companies with low or average value added
- Many barriers to entry: Protection (US)

Acquisitions, Domestic Competition

- Paradox of acquisitions strategies
 - In part, acquire strategic assets (high technology) to repatriate technology in the domestic market
- Geely / Volvo (Sweden)
 - Buying a Ford bankrupt firm at a good price
 - Development in China: to enter upmarket
- YTO / McCormick (France)
 - Competition between Chinese state firms and private firm
 - Skinning up?: take the knowledge, back to China

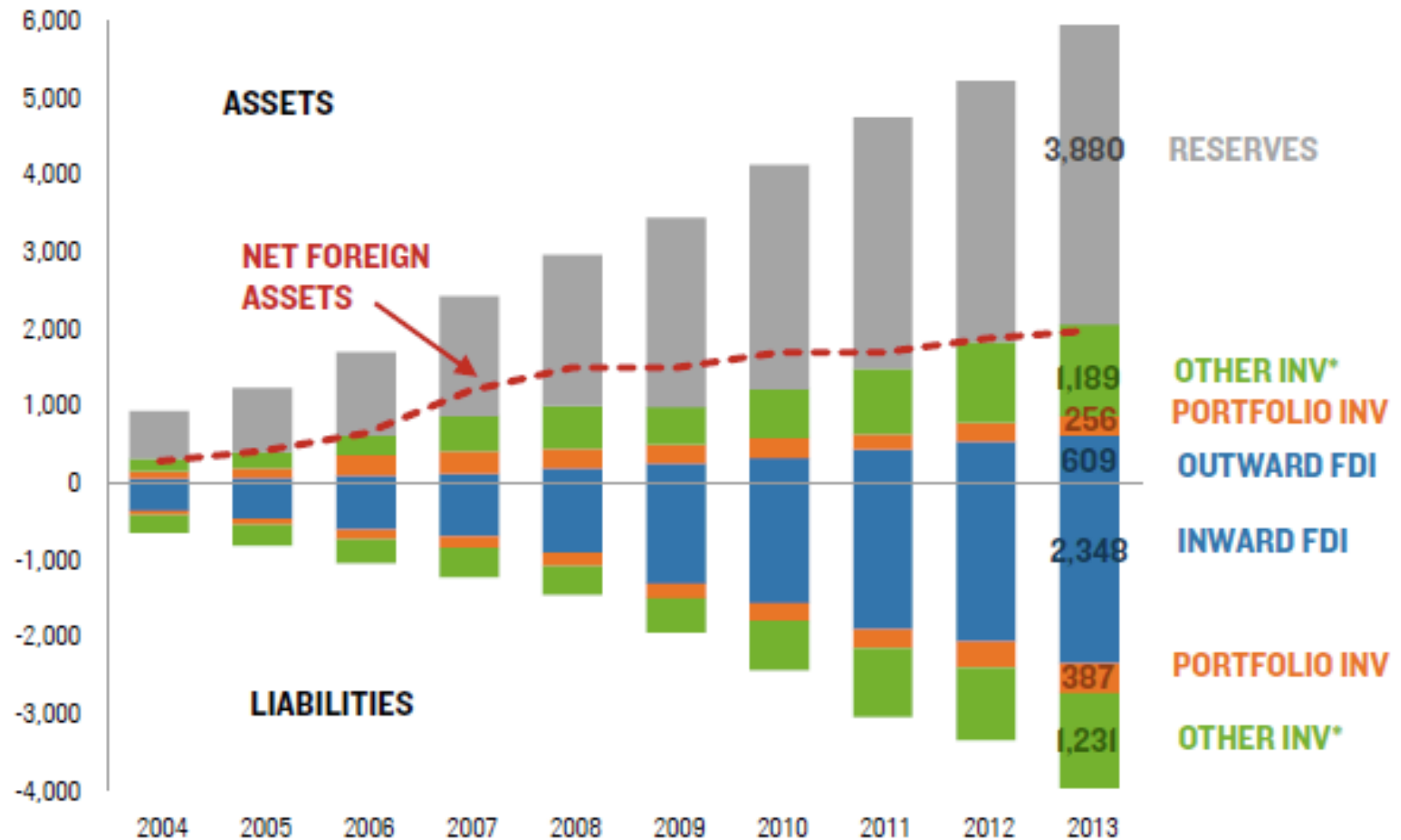
A Limited Internationalisation?

- South-South: limited levels in terms of multinationalization,
 - no integration, no formation of regional value chains (Lat. America, Africa)
 - Difficult to acquire firms in targeted strategic sectors (petroleum): biggest oil companies in Develop. Economies are public owned
- Insufficient financial resources:
 - Chinese financial surpluses for the protection of the domestic financial system in crisis
 - Underdeveloped domestic financial market
 - Difficult trade off on the capital markets: issuing shares / bonds, credit vs using firms's cash flow

Financial Position , 2004-2013

Figure I: China's International Investment Position, 2004-2013

USD billion, total stock, assets (+) and liabilities (-)



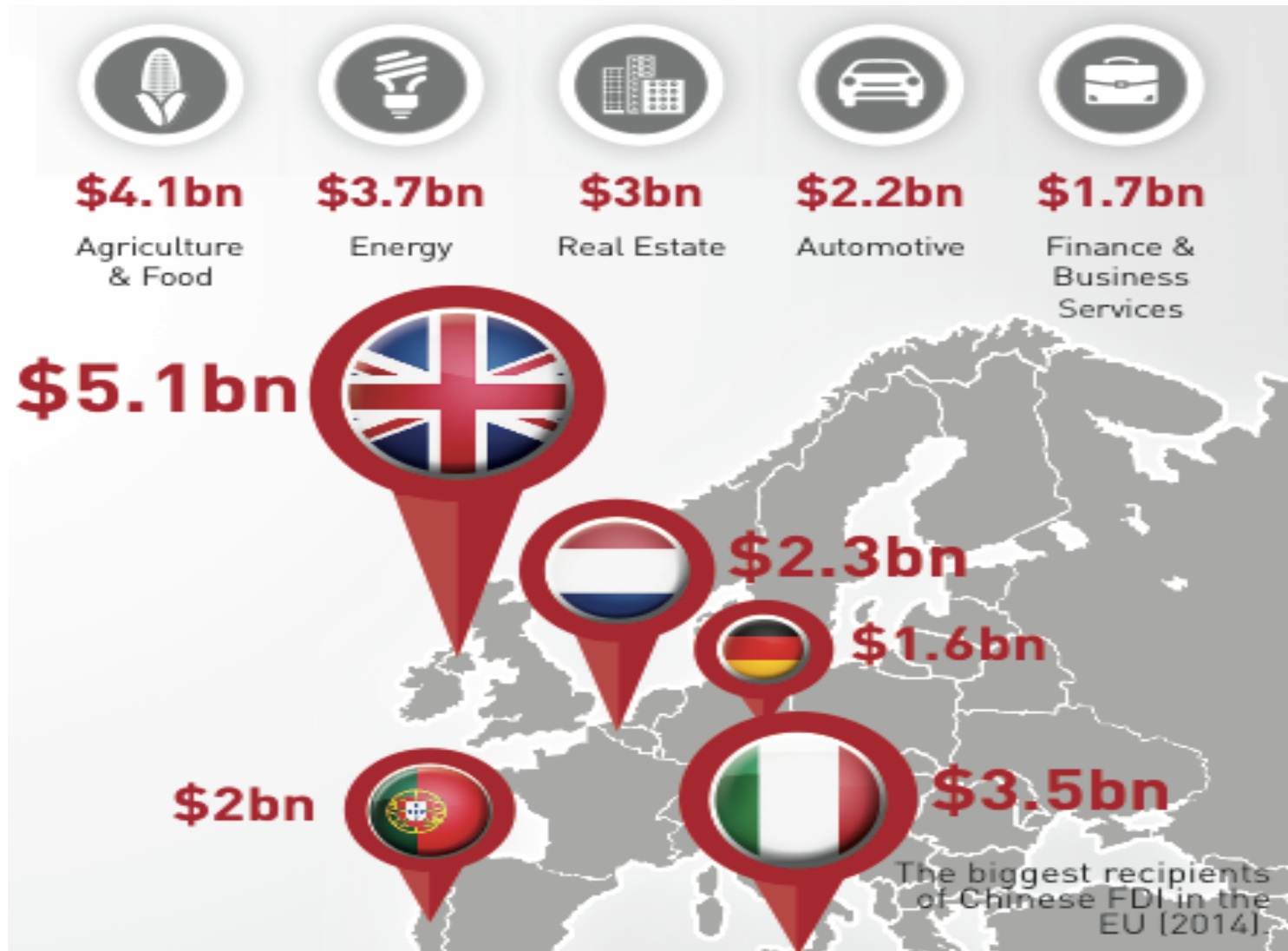
How to Catch Up?

- Strong ideas of P. Nolan:
 - Put into perspective the breakthrough of the Chinese economy with the changes of the productive and world financial system induced by large firms and national innovation systems in HIME: Increase the gap
 - The conditions for the emergence of Chinese firms to become genuine multinationals far from being met
 - National technology base, managing the complexity of advanced technologies still missing in China today

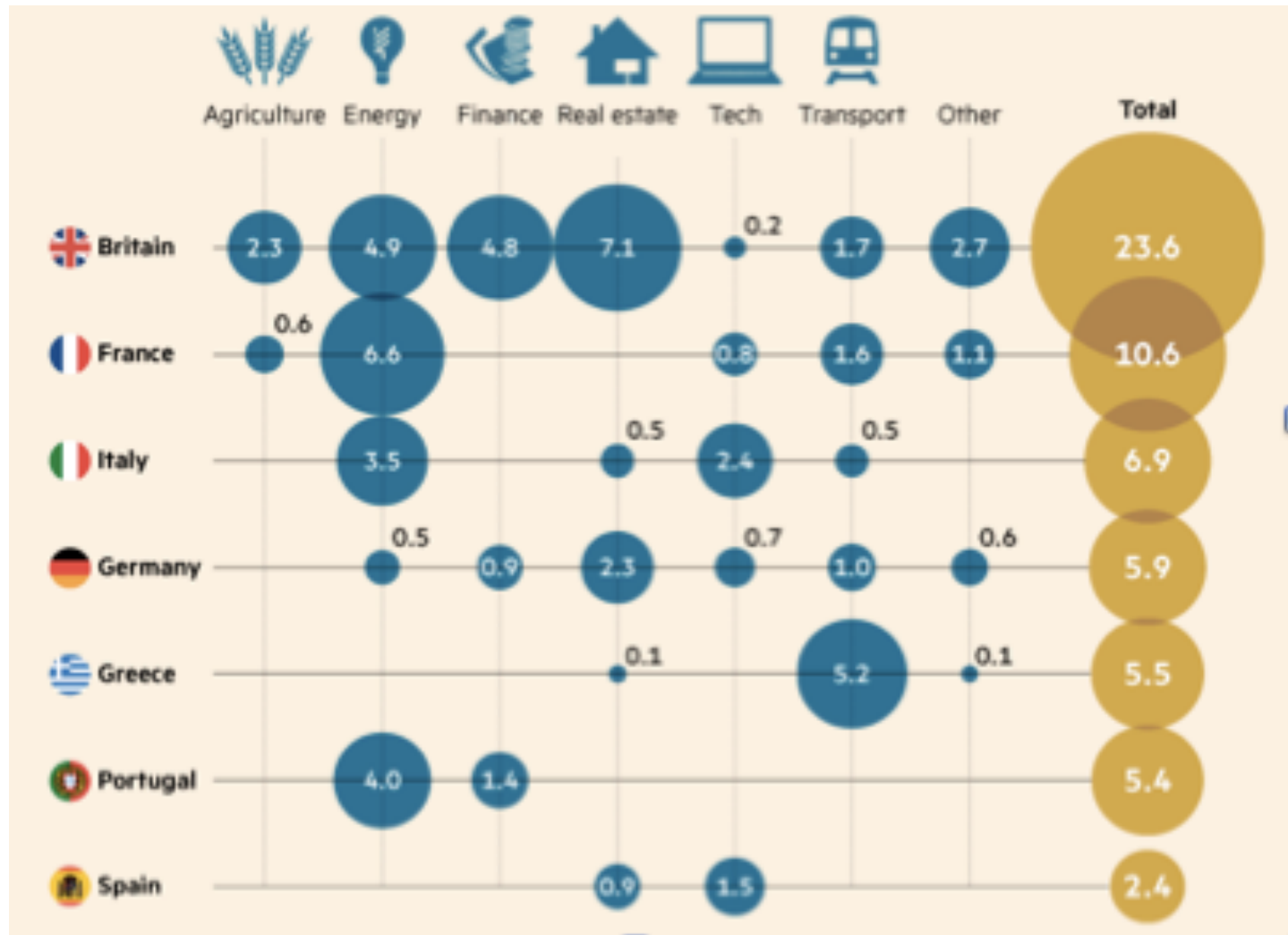
Europe: a New Era for the Development of Chinese FDI?

- Le Corre and Sepulchre Analysis
 - Confirm P. Nolan developments
 - Provides insights on the entry modes and arbitration between acquisitions / multinationalisation
- Chinese FDI in Europe
 - Easier to entry: European and national regulations, still fragmented markets crisis, investment needs
 - Attractive acquisitions (Volvo, ..)
 - Variety of opportunities, of chinese investors

Chinese FDI flows in 2014 in Europe



Stock of Chinese FDI in Europe, 2005-2014



A typology of Chinese FDI

- Specialization and diversification resulting in the purchase of different types of assets by Chinese investors
 - ***Specialization*** for emerging companies in technology, progress successfully in foreign markets, including advanced Lenovo, Haier, Huwaie
 - ***Diversification*** by capital companies in different sectors: real estate, food, insurance .

A Spatial Distribution Related to Opportunities

- EU-15 and NMS
 - EU 15: acquisitions, NMS: virgin investments
- Majority or minority of firms control
 - Limited capital available,
 - Complexity of asset management:
 - Fight against corruption in China -> preference for minority controls? Dangerous to gain competencies abroad..
- Industry or real estate?
 - Today, the first destination, UK (London): Estate, Germany: 4th ..

A Variety of Entrants

Ownership

State owned

Private

Organizational form



Corporate investor

State-owned corporations

Non-state owned corporations

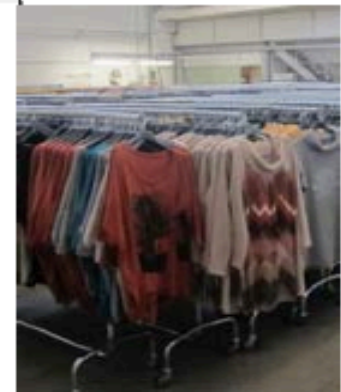
- National champions

- World-stage aspirants
- Global niche players

Entrepreneurial investor

Entrepreneurial and family businesses

- Entrepreneurial cluster participants
- International entrepreneurs



Investments Characteristics in Europe (China + other MNC from E.E.)

- China (21%) India (29%) most important Inv in Europe from EE. Russia 3rd
- UK 1st destination, followed by Germany, and at some isitance France and Spain, recently Portugal
- Target Sectors
 - Services at the top (financial services)
 - Pharmaceutical and metal: Top in manufacturing
- High Income Countries: attract more Technology Driven FDI
- Low & Middle-Income Countries: FDI in relation with market or resource-motivation seeking

Investments in Europe ...

- Main finding of a recent research: ***Technology-Driven FDI by Emerging Multinationals in Europe*** (Lund University)
- Technology Driven FDI: distribution within Europe reflects existing technological hubs:
 - Automobile in Germany, Wind Energy in Denmark, ITC: more spread
- Most Investment in Europe: Green fields rather than M&A. 80% of Chinese Investment, 50% of Indian and Brazil are Green fields
- Regarding acquisition: less control if objective is to acquire technology competencies than a customer base. Indian maintain the European company as a separate entity to preserve the brand value
- Companies with high level of intangible assets: conduct TDFDI
- High diversity of the impact of TDFDI, no generalized predatory behaviour. In some case: positive impact on the European subsidiaries

Geographical distribution (% of firms), 2013

Western Europe	29%
Southern Europe	12%
Northen Europe	4%
Northen Europe	55%

Entry Form

Whilly owned subsidiary	47%
Majority Joint Ventures	18%
50-50 Joint Ventures	15%
Minority Joint Ventures	14%
Other Joint Ventures	6%

Entry Form per Type of Firms

	SOEs	Private firms	Ind. & family business
Minority JV	10,88%	9,60%	15,81%
50:50 JV	2,51%	5,39%	18,46%
Majority JV	18,83%	15,48%	19,82%
Wholly owned subsid.	67,78%	69,54%	45,91%

Sector Distribution of Chinese Enterprises in Europe

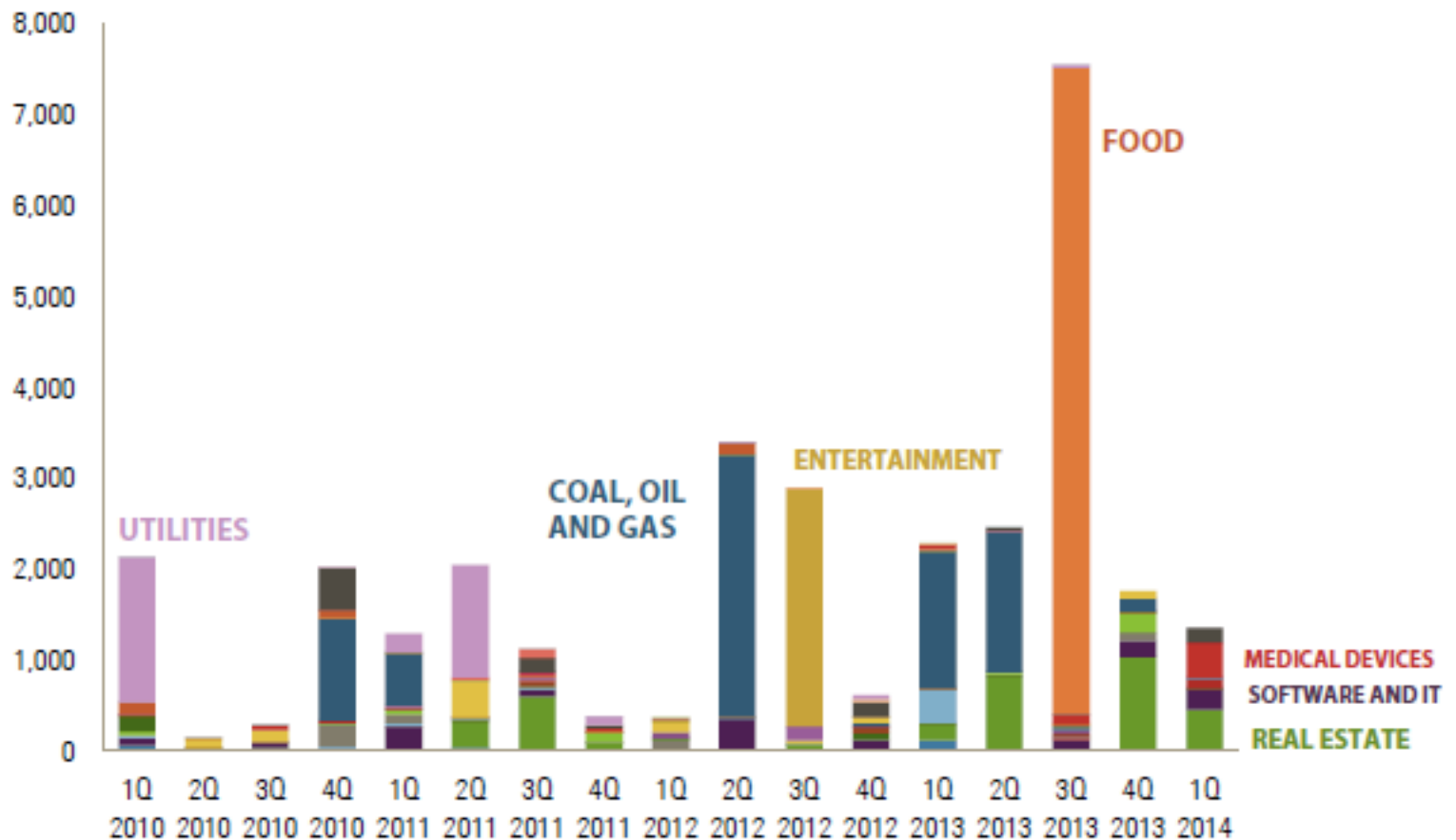
High Tech Manufacturing	3%
Low Tech Manufacturing	3%
Knowledge Intensive Service	8%
Less Knowledge Intensive Services	86%

China's M&As in Europe

- Privately owned enterprises > SOEs to become most important
- Central & Eastern Europe: a new Frontier
- Targeting sectors European reputed corporations with world class operation, management innovation competencies
- Growing role of individuals or families investments in Europe

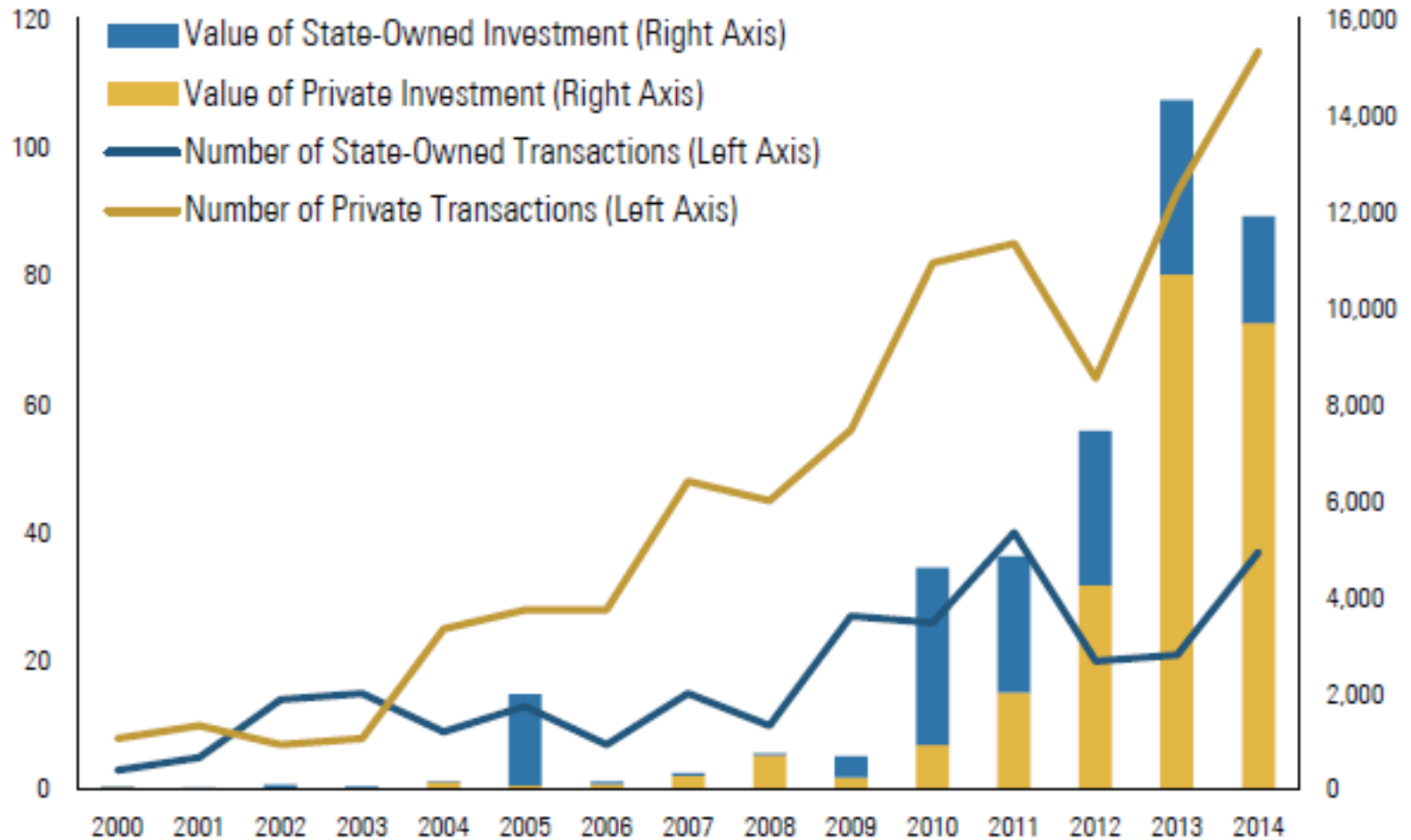
FDI in the US by Industries, 2005-2014

Annual figures, USD million



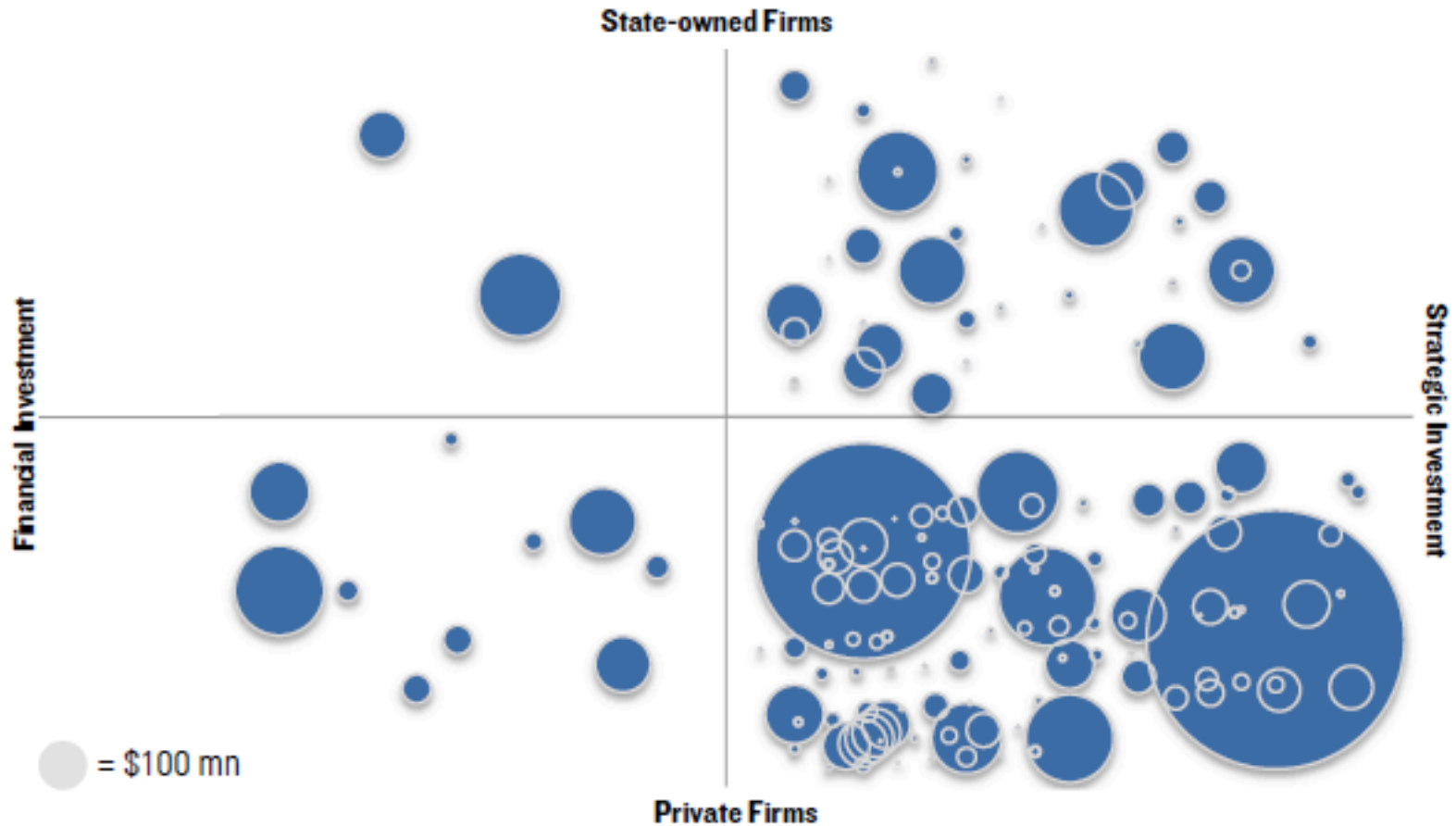
FDI in the US by Ownership

Number of deals, USD million



FDI in the US by Types, 2014

Bubble size indicates total investment value



Source: Rhodium Group. *Data are preliminary and subject to adjustment. A detailed explanation of sources and methodology can be

Conclusion

- Strong disability from the start to internationalize
- Domestic accumulation of resources, expertise, new forms of competition: push multinationalization
- But multinationalisation stammering and hesitant, still low amounts of capital
- Learning Curve: Fast
- Varieties of investment, Operators, Entry mode: not only strategic assets..
- Main Problem: Strengthening the technological base in China to succeed abroad and to compete one day the big MNCs from developed countries.

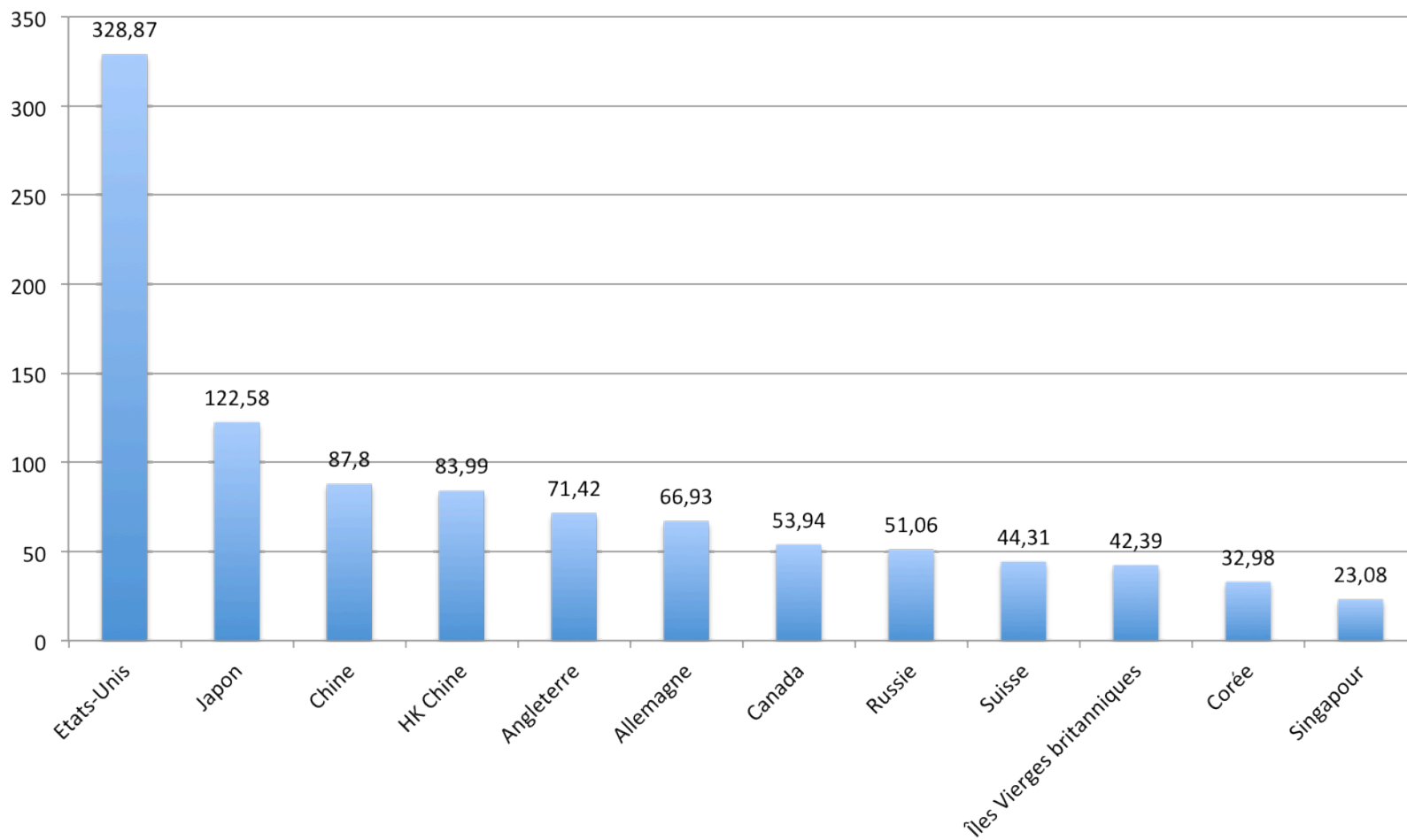
Annexes

- Data on Chinese FDI
- Sources:
 - Euro-China Investment Report 2013/2014, The Antwerp Forum 26.09.2013
 - Chinese Investment into Europe hits Record High in 2014, Baker & McKinzie
 - China's Global Outbound M&A in 2014
 - China's outward FDI, Economic Watch, BBVA
 - China-EU Relations, Deutsch Bank, July 31, 2014
 - Technology-Driven FDI by Emerging Multinationals in Europe. Project Report. Editor: Cristina Chaminade, CIRCLE, Lund University

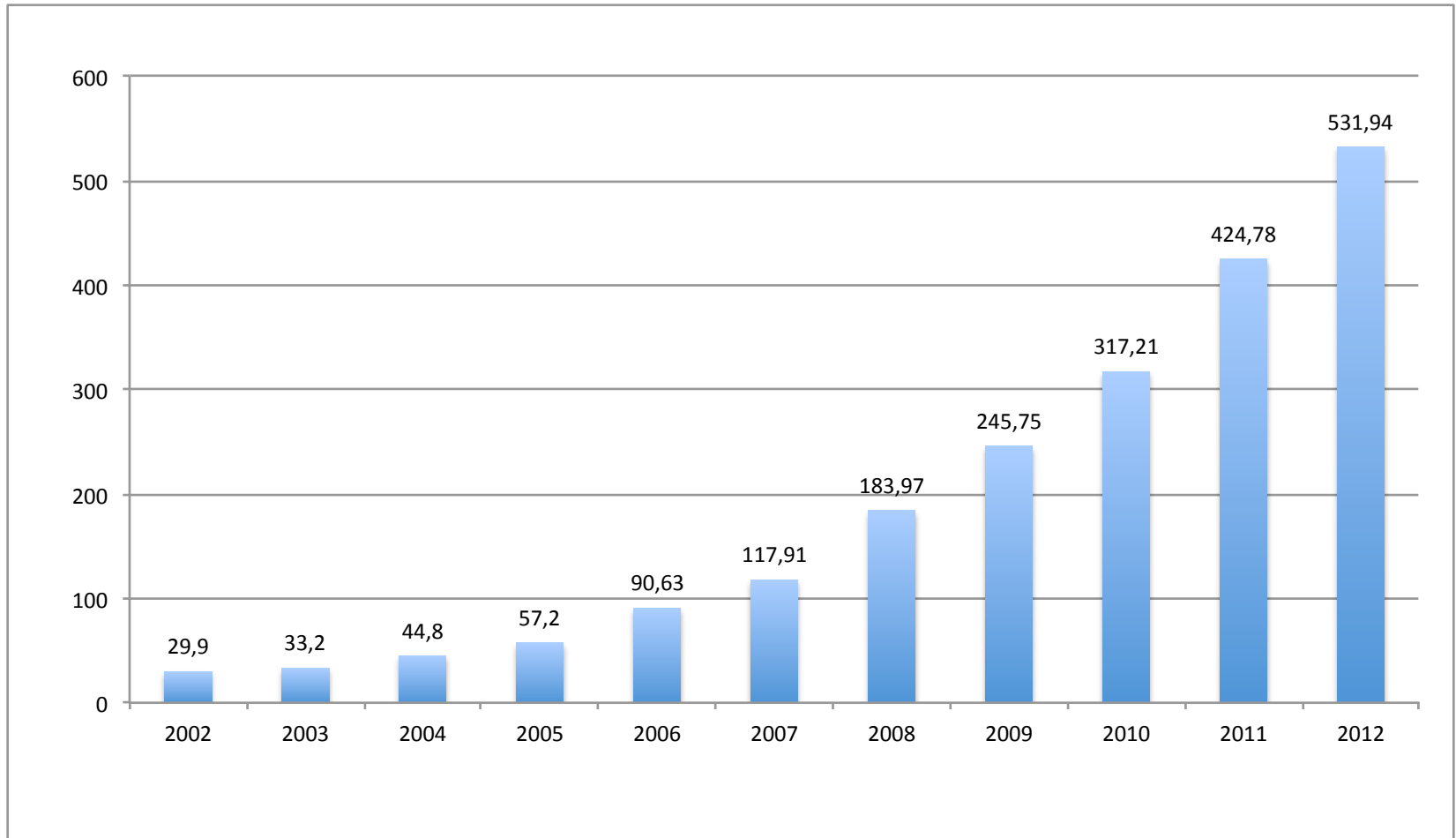
Sectoral Distribution



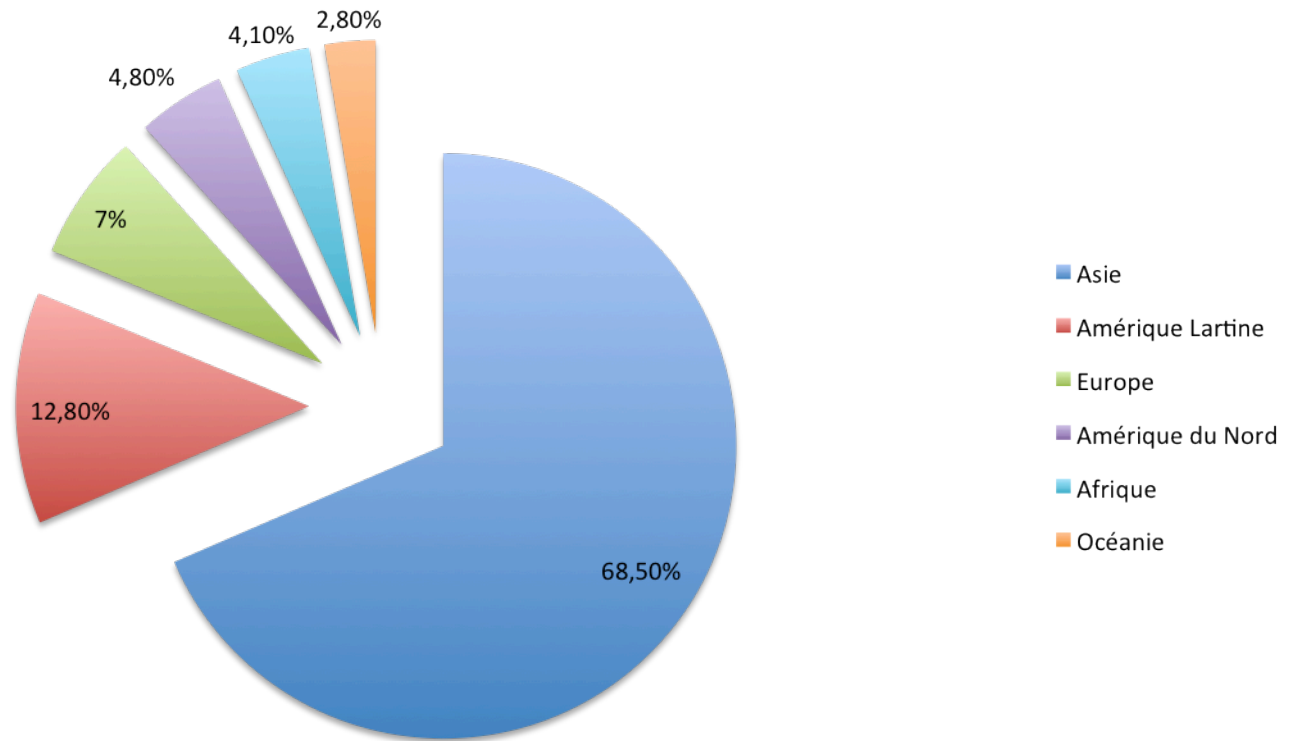
Chinese FDI Flows Compared to other countries in 2012 (bns USD)



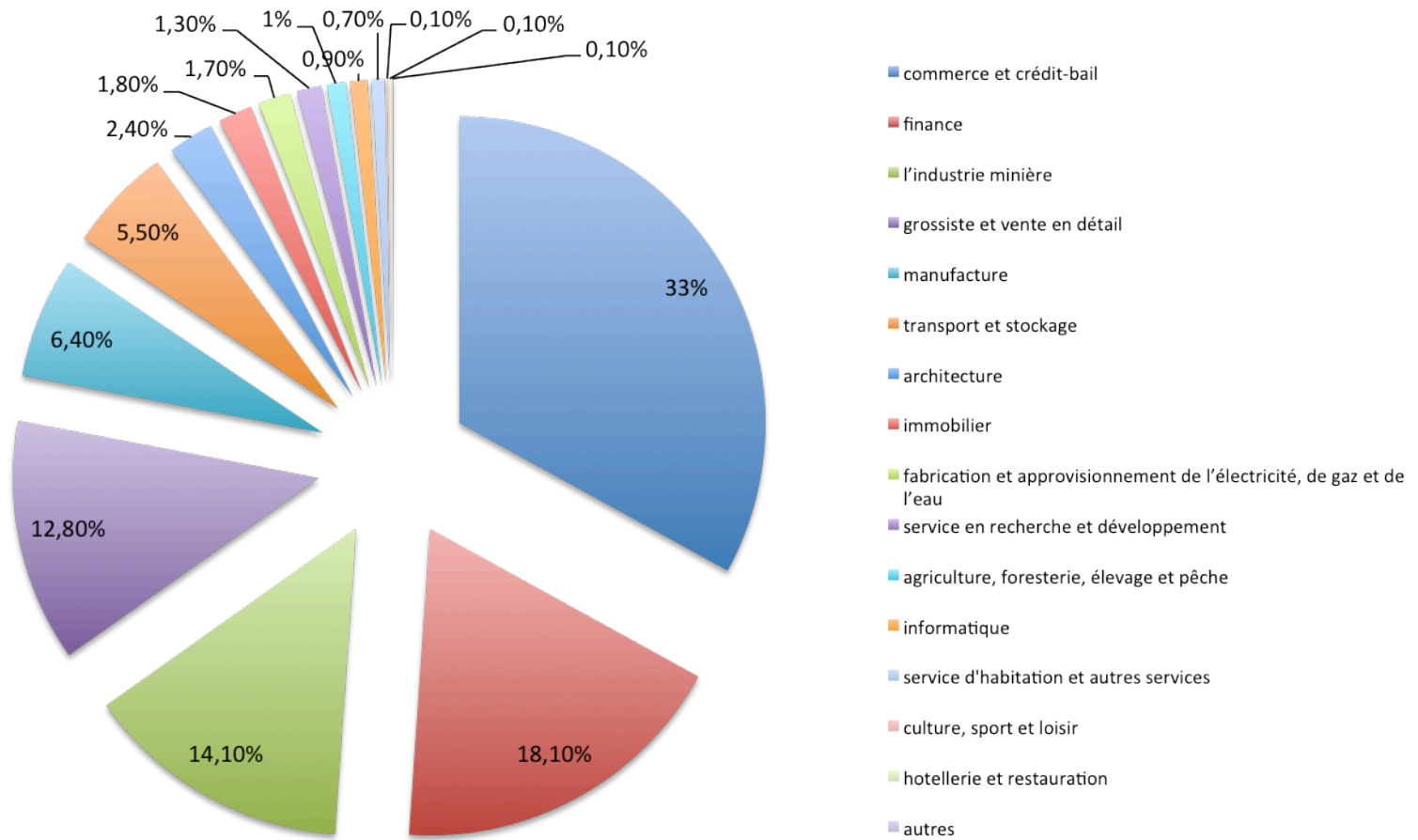
Chinese FDI Stock 2002-2012 (bns USD)



Geographical Distribution of Chinese Stock of FDI (2012)



Chinese FDI Sectoral Distribution of 2012 (in %)



Chinese FDI Stock by Ownership 2012

