

Hosting Chinese direct investment in Europe: Significance and implications

Daniel Van Den Bulcke
*University of Antwerp and
Antwerp Management School*
Macau, March 28, 2013



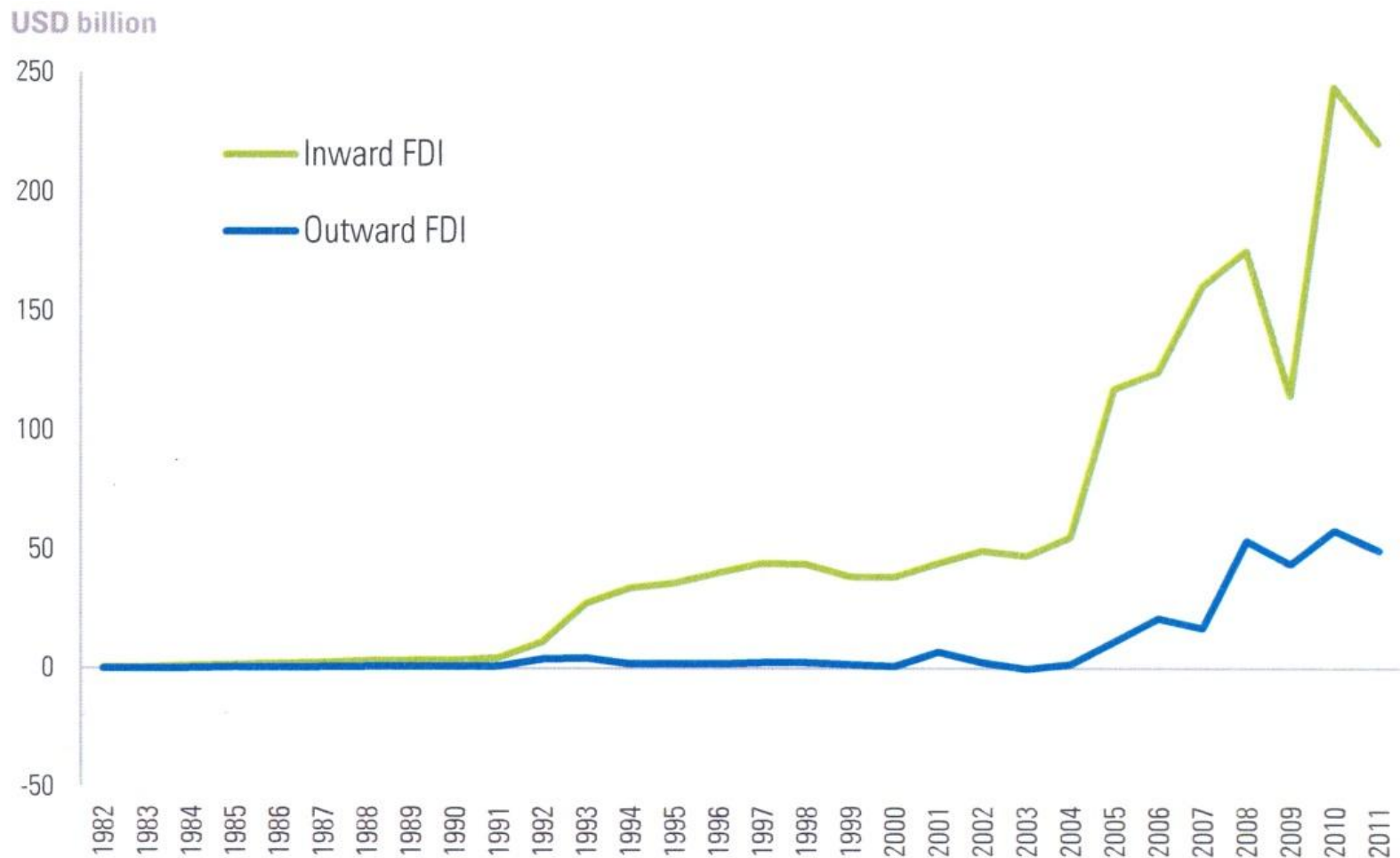
Outline

- **China's outward direct investment**
- **China's outward direct investment policy regime**
- **Chinese direct investment in the European Union**
- **China's outward investment in the EU as compared to the US**
- **Chinese investment presence in Europe: A more complete picture**
- **China's direct investment in the EU: Issues of concern**

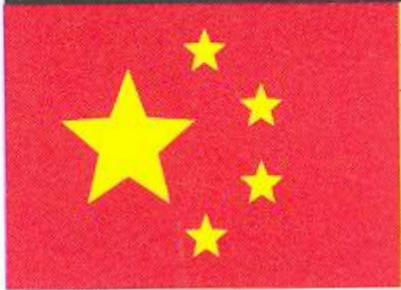
China's outward direct investment



China's inward and outward FDI flows (1982-2011)

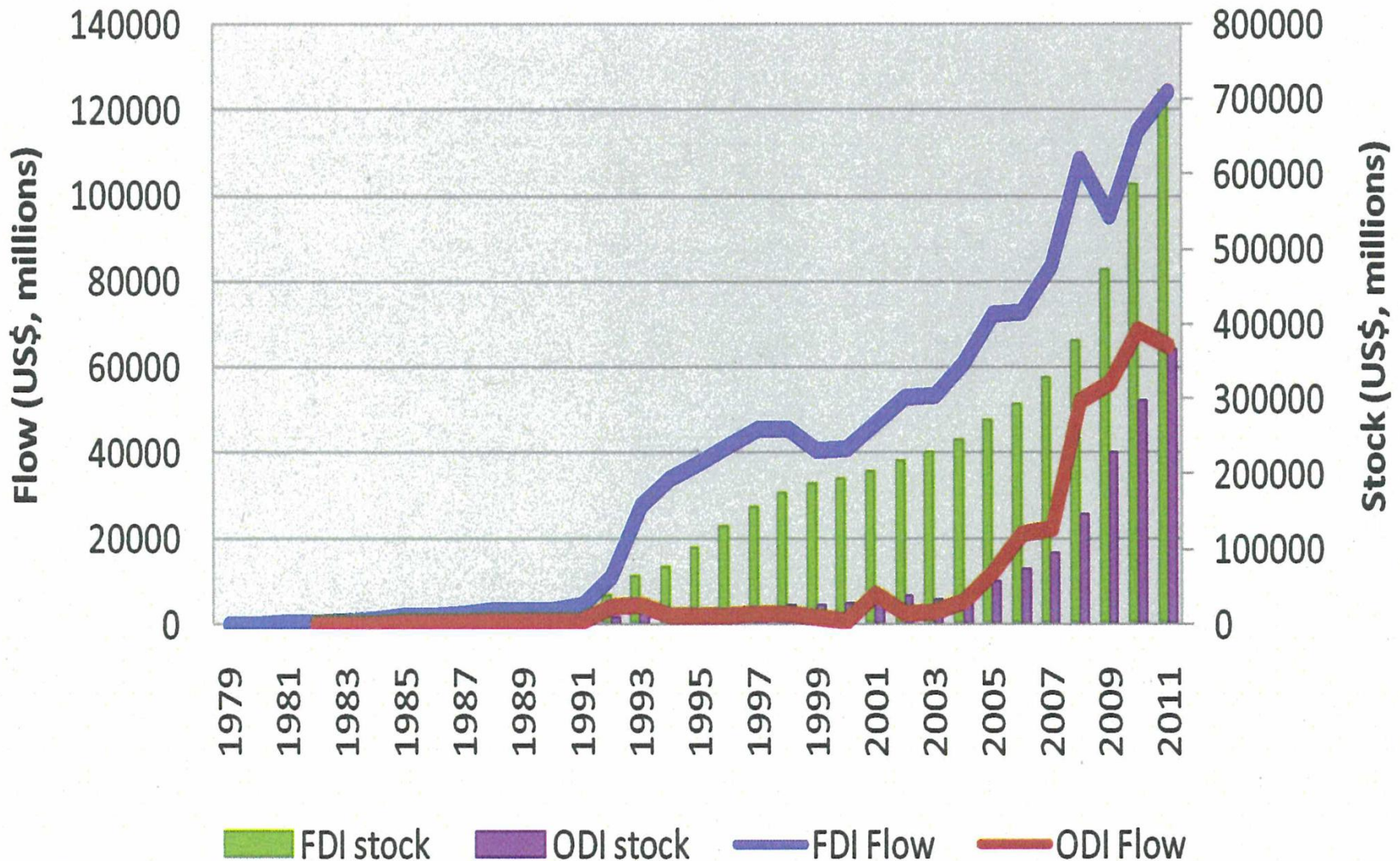


Fortune, October 26, 2009

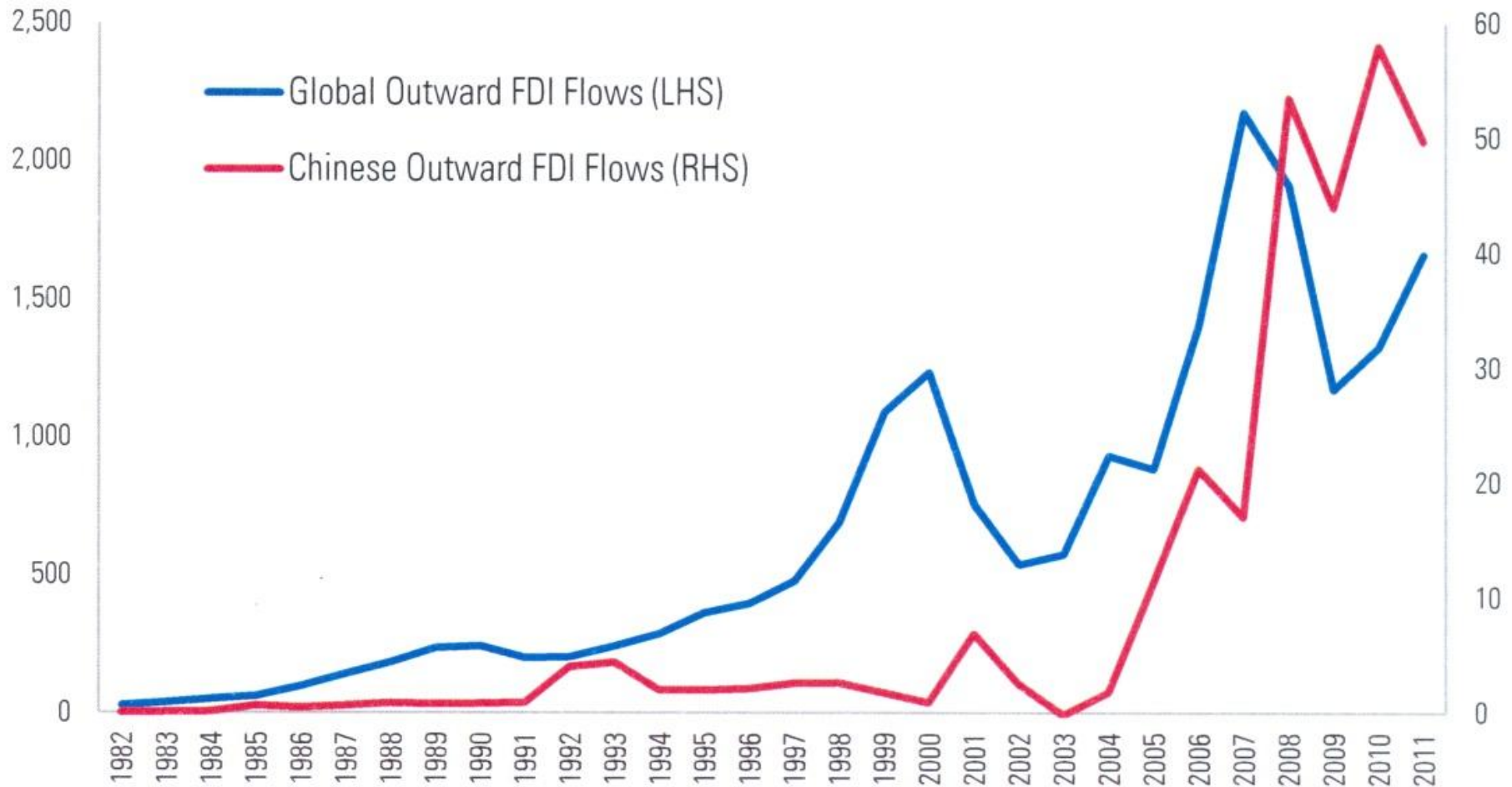


THE CHINESE HAVE LONG BEEN ON A SHOPPING SPREE FOR NATURAL RESOURCES. NOW, WITH \$2 TRILLION IN THEIR POCKETS, THEY ARE SHIFTING THEIR AIM TOWARD AUTO-MAKERS, HIGH-TECH FIRMS, AND REAL ESTATE. **WHERE WILL THEY STRIKE NEXT?**

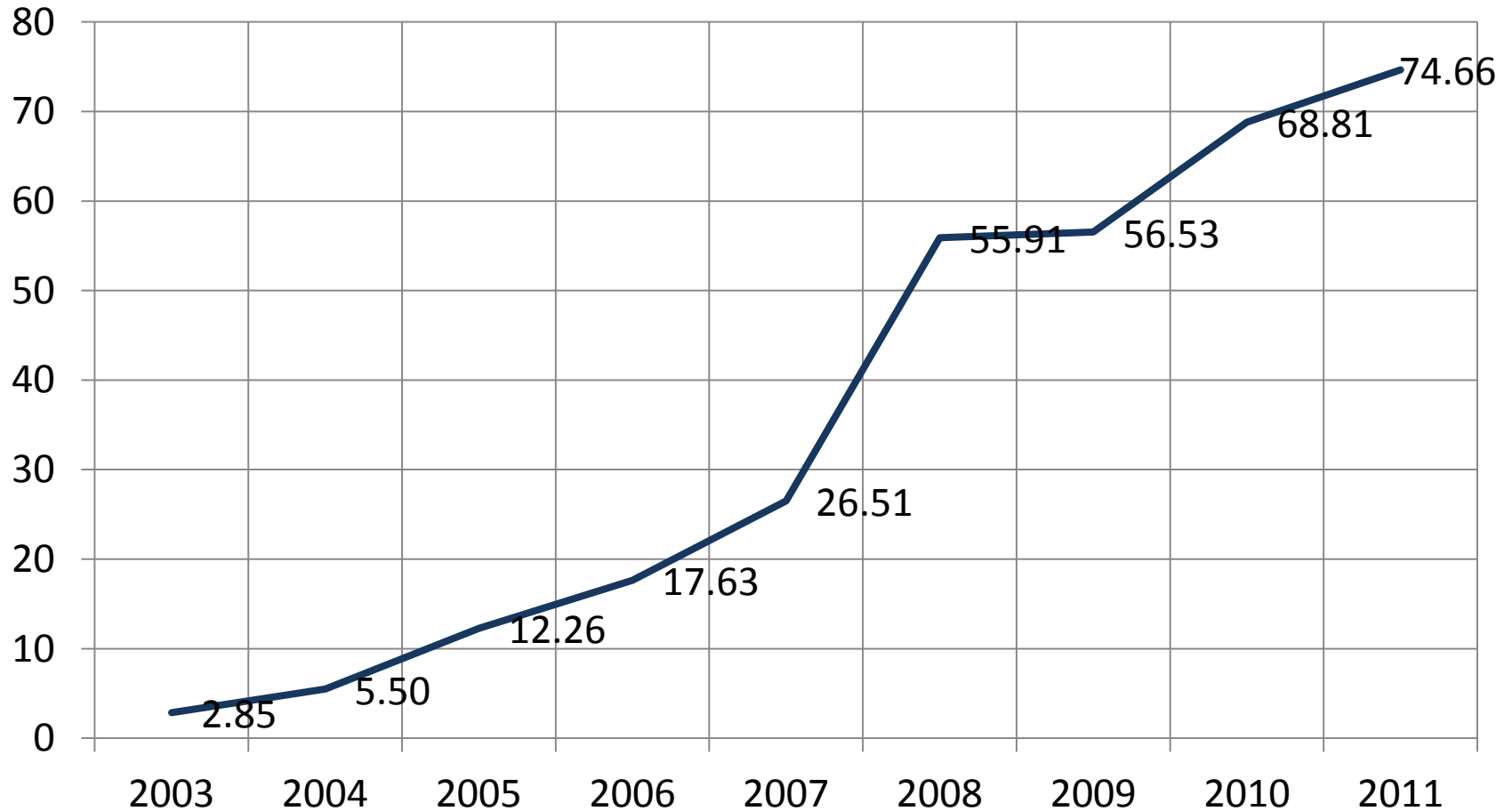
China's Outward FDI vs. Global Outward FDI Flows (1979-2011)



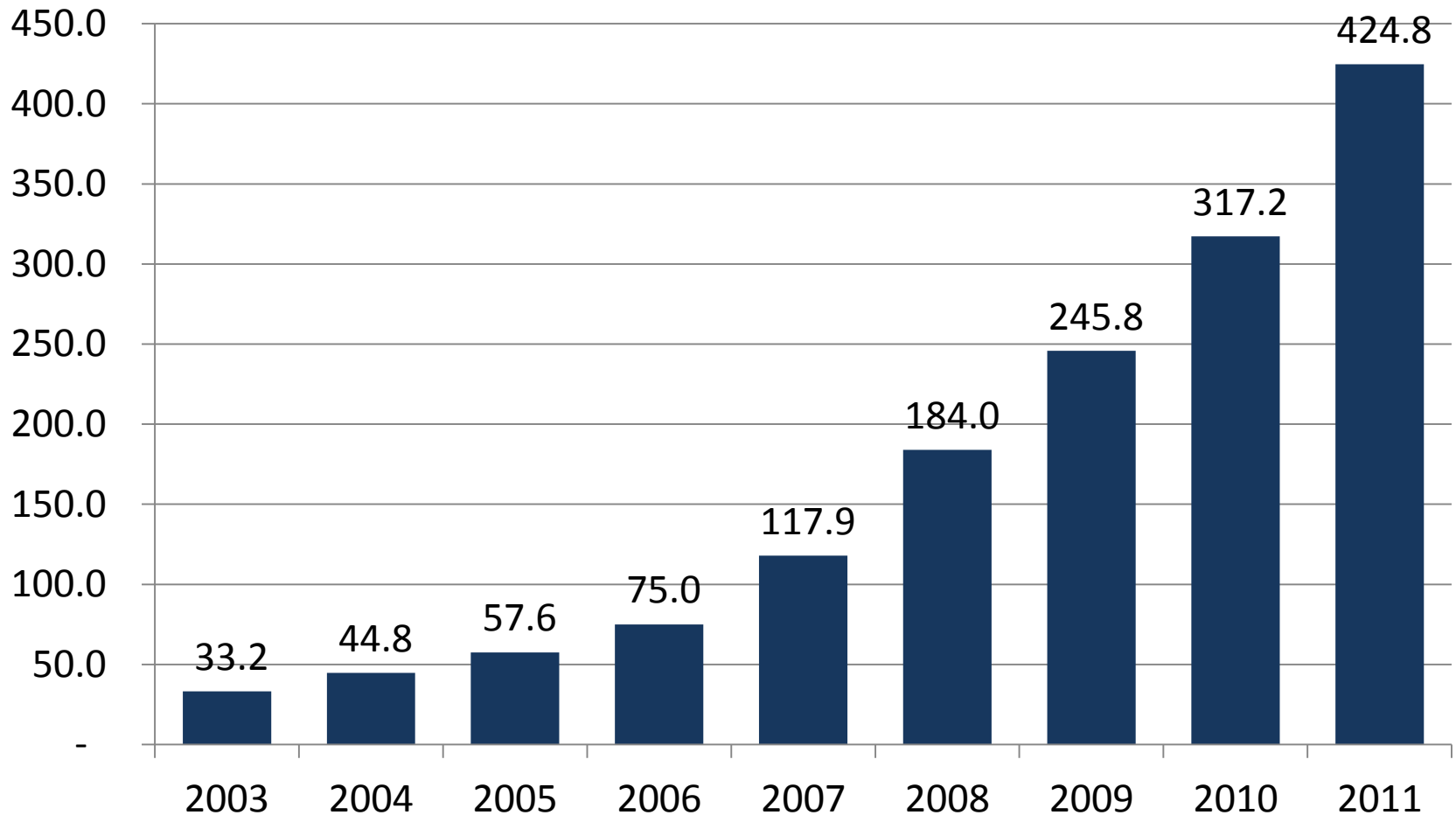
China's Outward FDI vs. Global Outward FDI Flows (1982-2011)



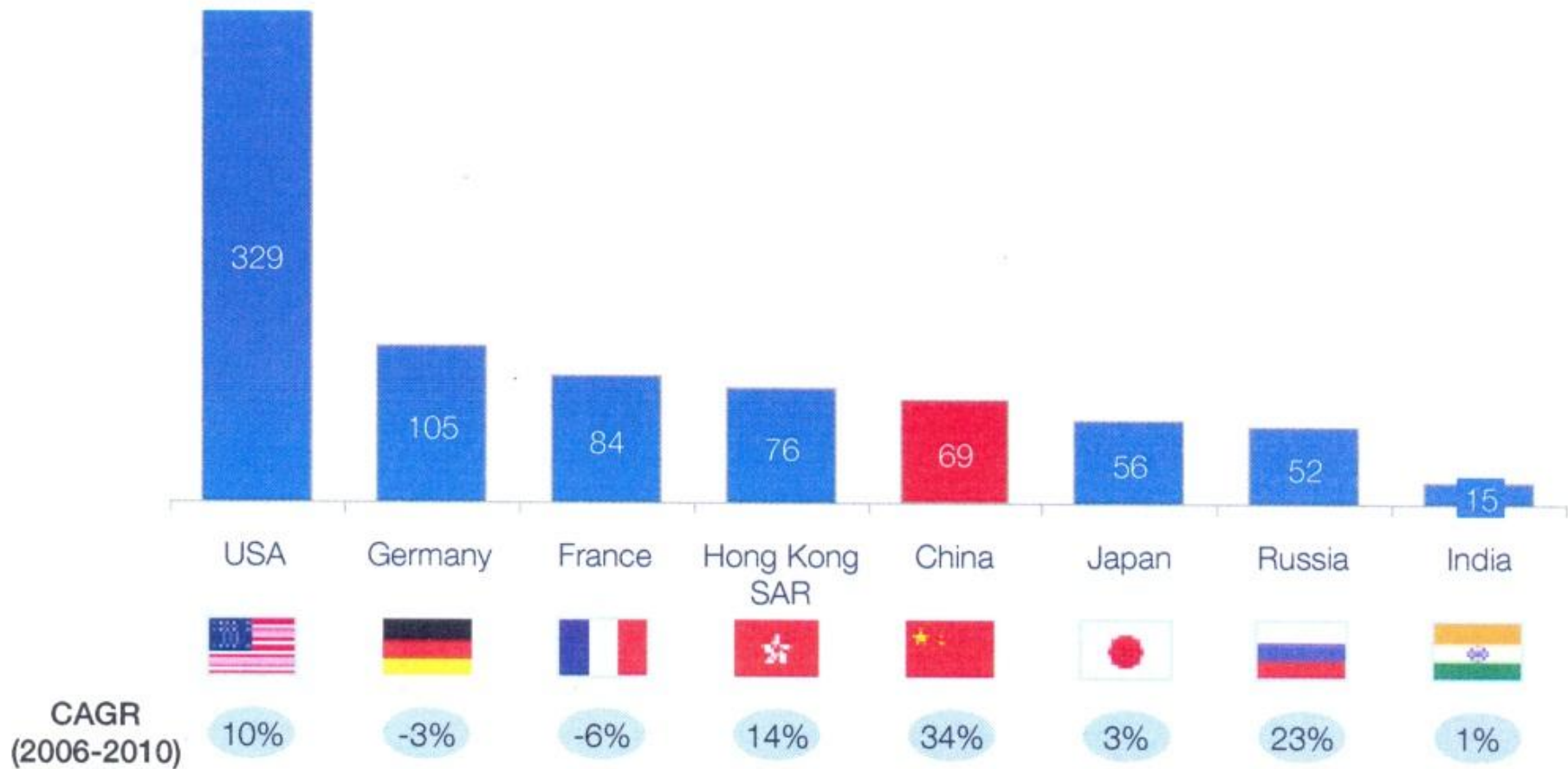
China's FDI outflows (2003-2011) (US\$ million)



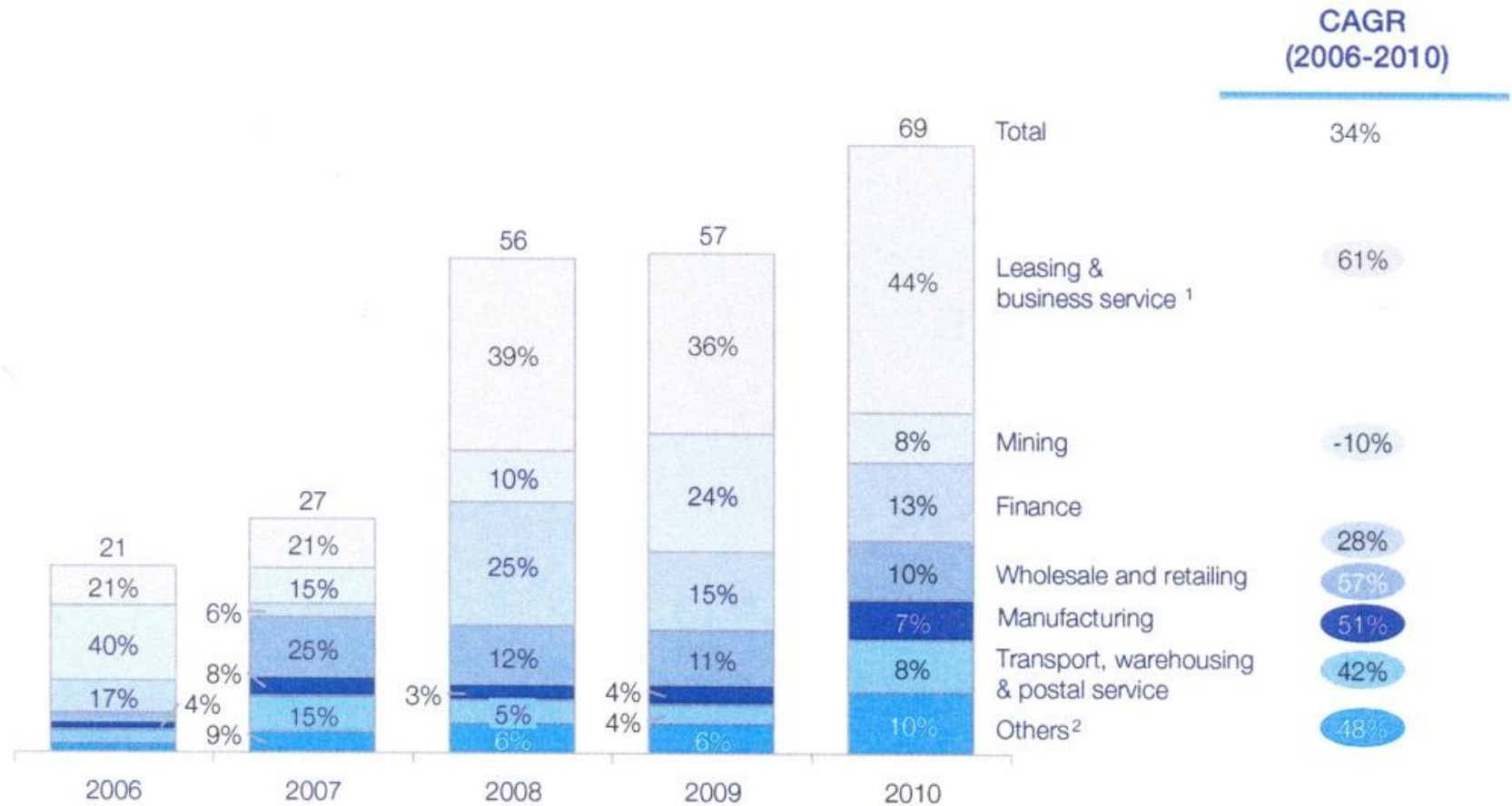
China's outward FDI stock (2003-2011) (US\$ million)



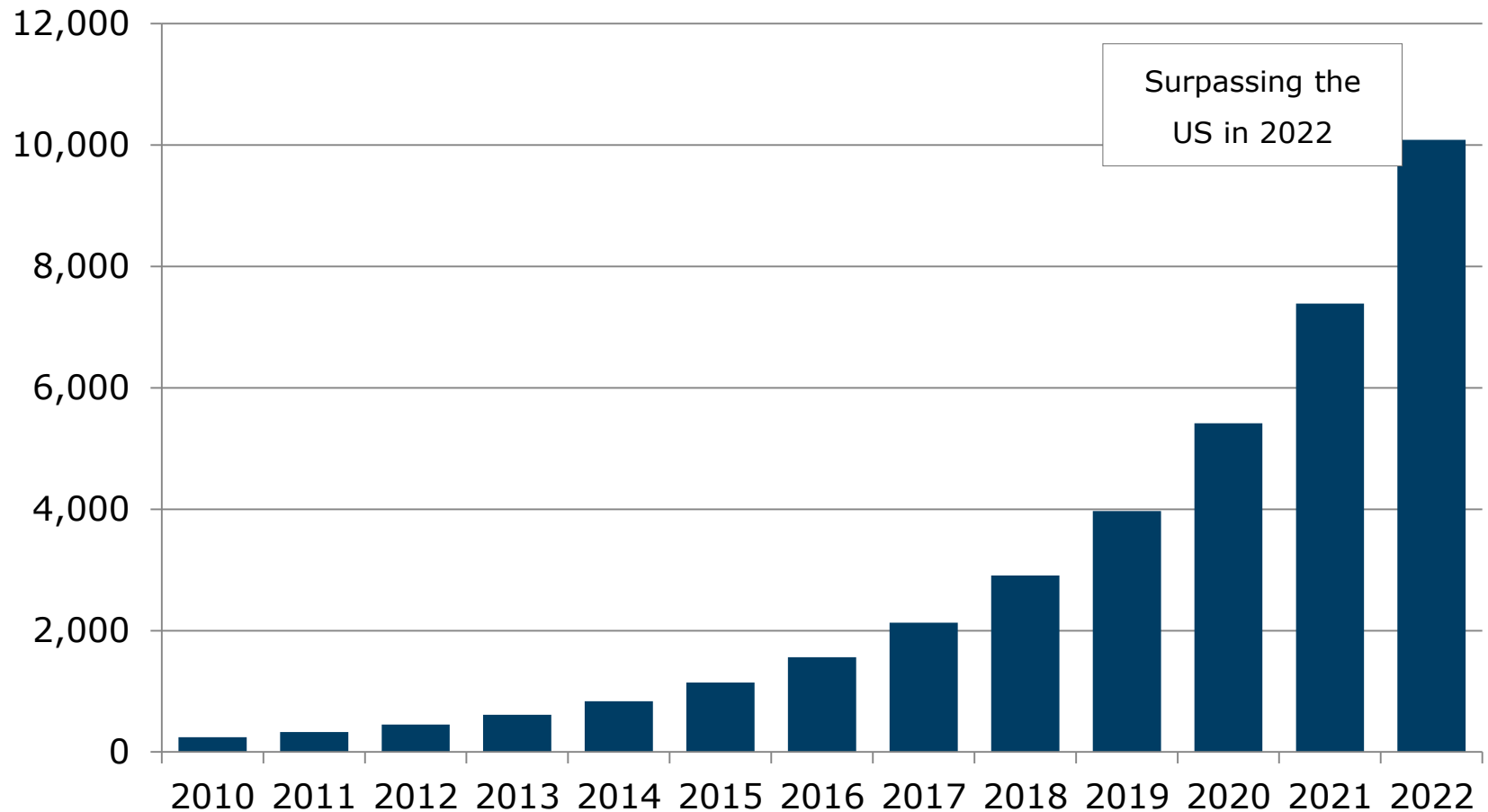
Outward FDI flows from major economies (2010) (bn US\$ and CAGR 2006-2010)



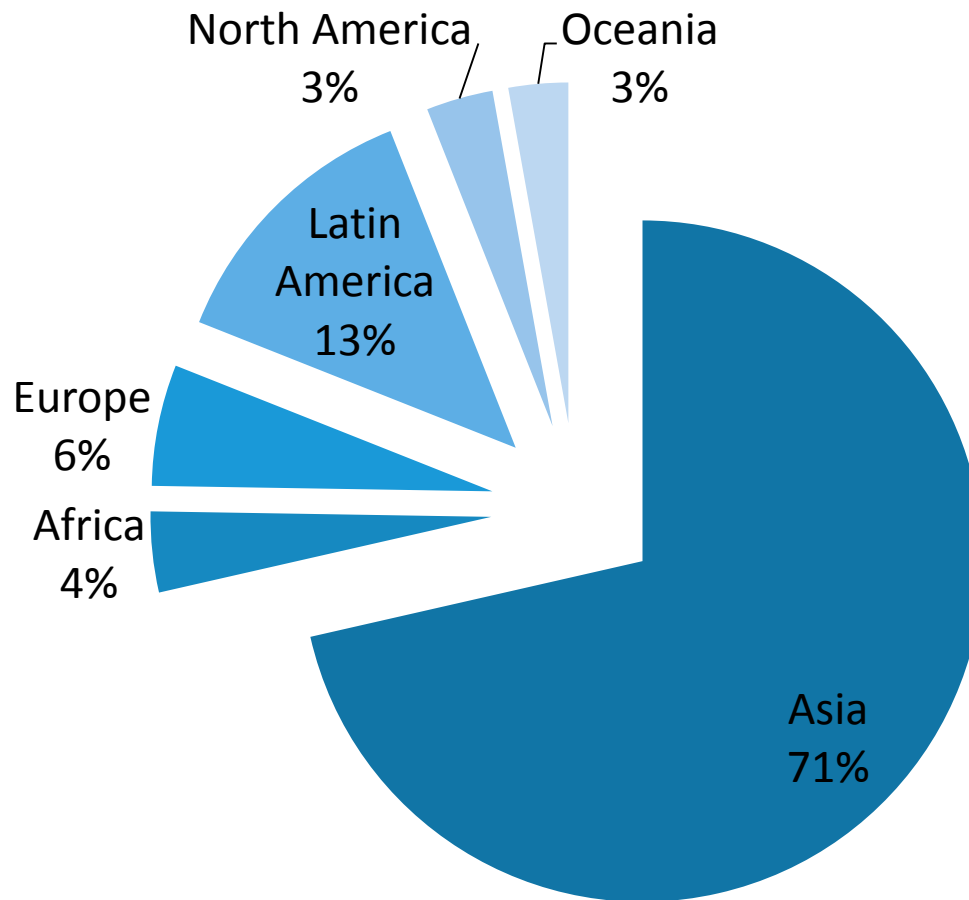
China's outward FDI by industry (2006-2010) (bn US\$ and CAGR 2006-2010)



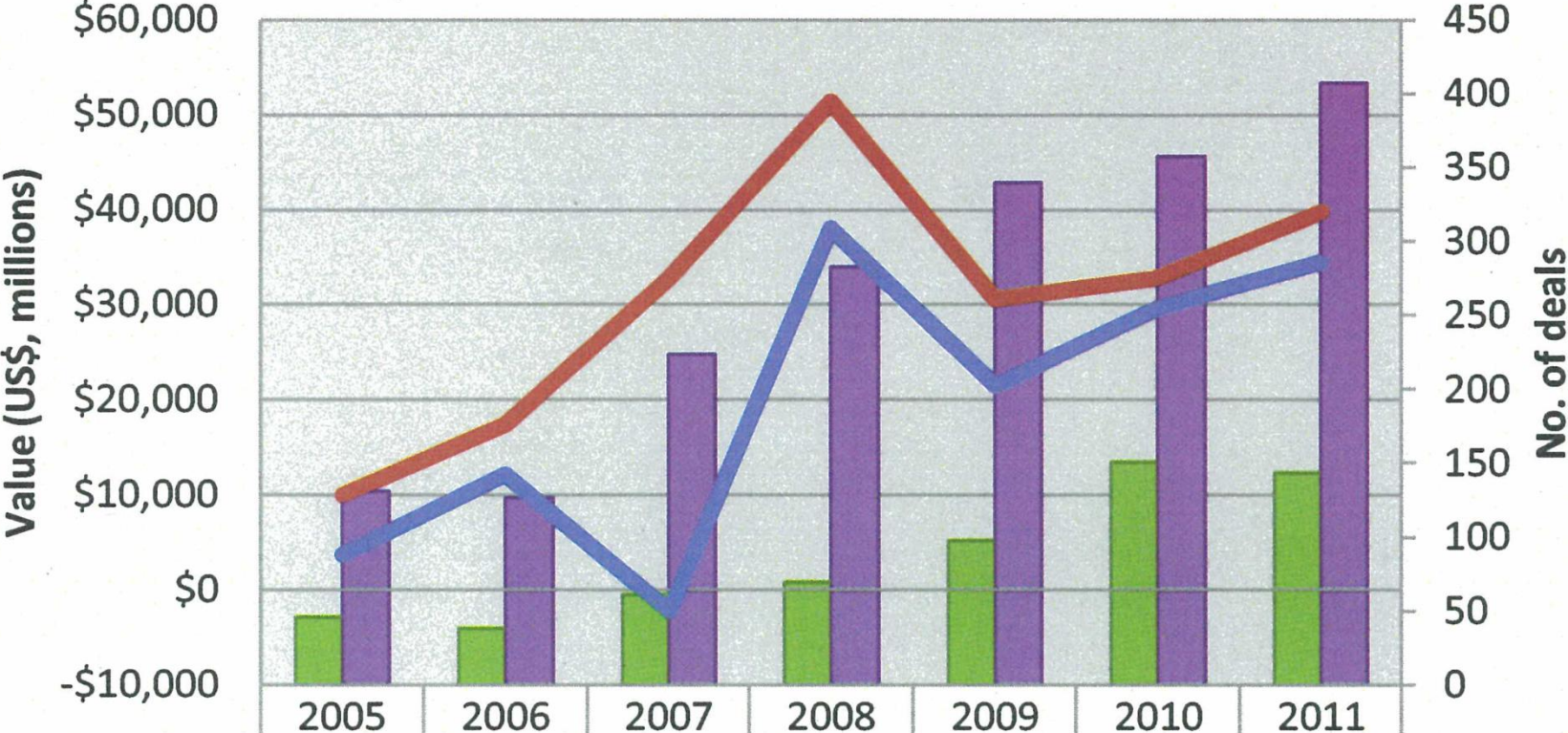
Projection of China's outward FDI stock (2010-2022)







Geographic distribution of China's outward FDI stock (2011)

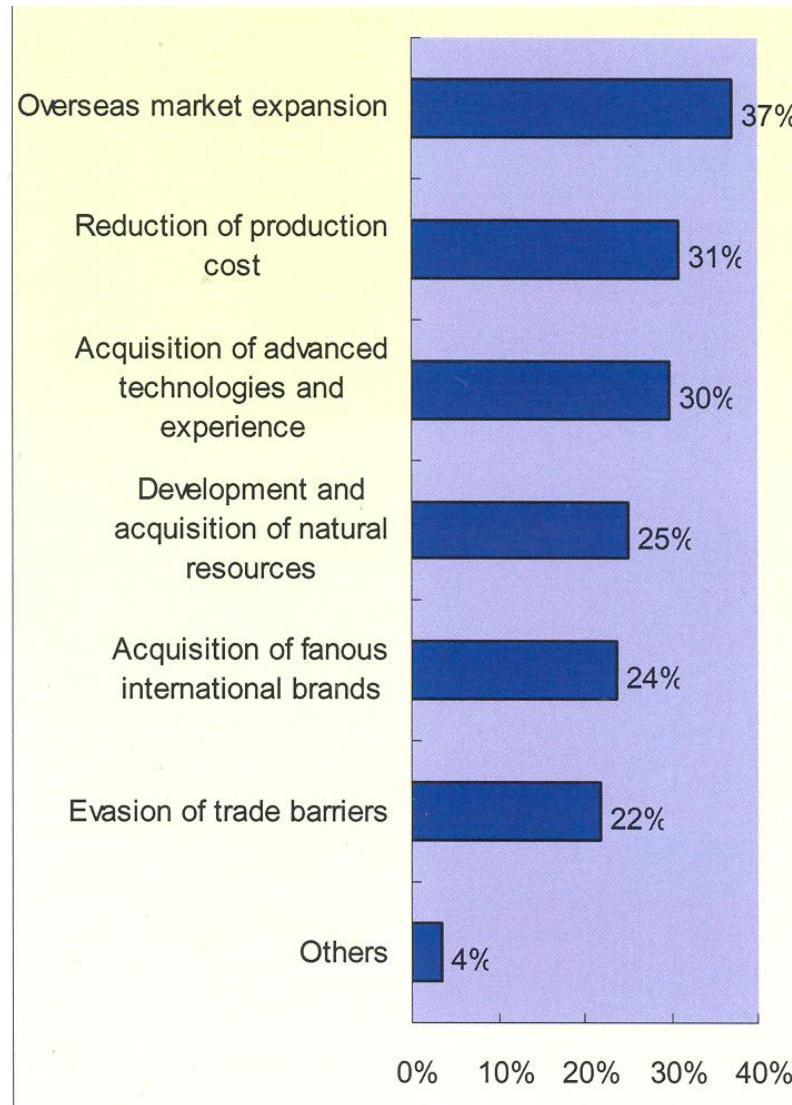


Chinese OFDI: Greenfield investments vs. M&As

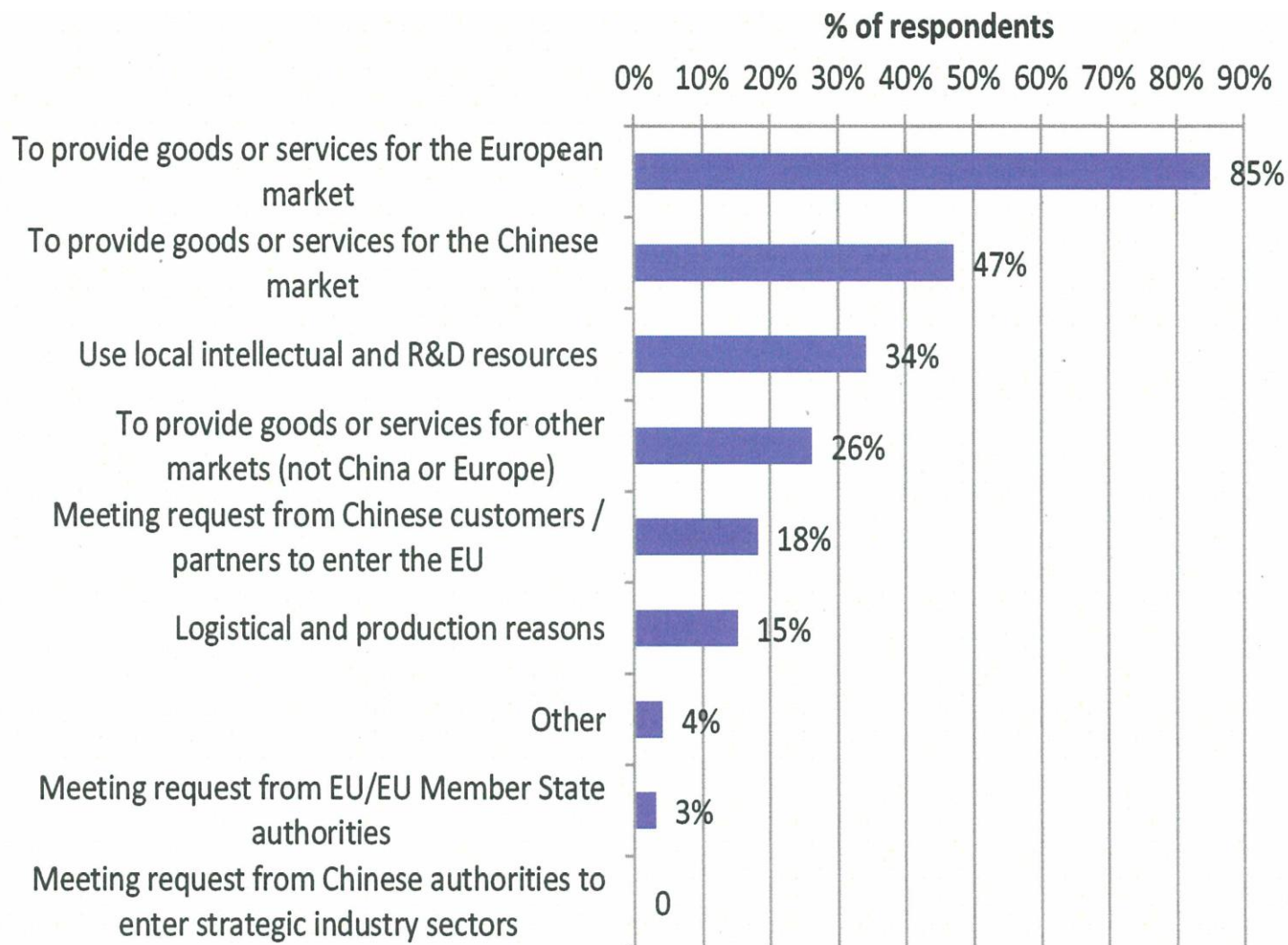


 M&A deals	45	38	61	69	97	150	143
 Greenfield investments	131	127	223	282	340	357	407
 M&A value	3653	12090	-2282	37941	21490	29578	34355
 Greenfield value	10009	17490	32765	51477	30512	32880	39718

Future investment motives of Chinese MNEs (CCPIT 2009)



Motivations for Chinese Firms to invest in Europe (EUCCC 2012)



China' Outward FDI: Conclusion

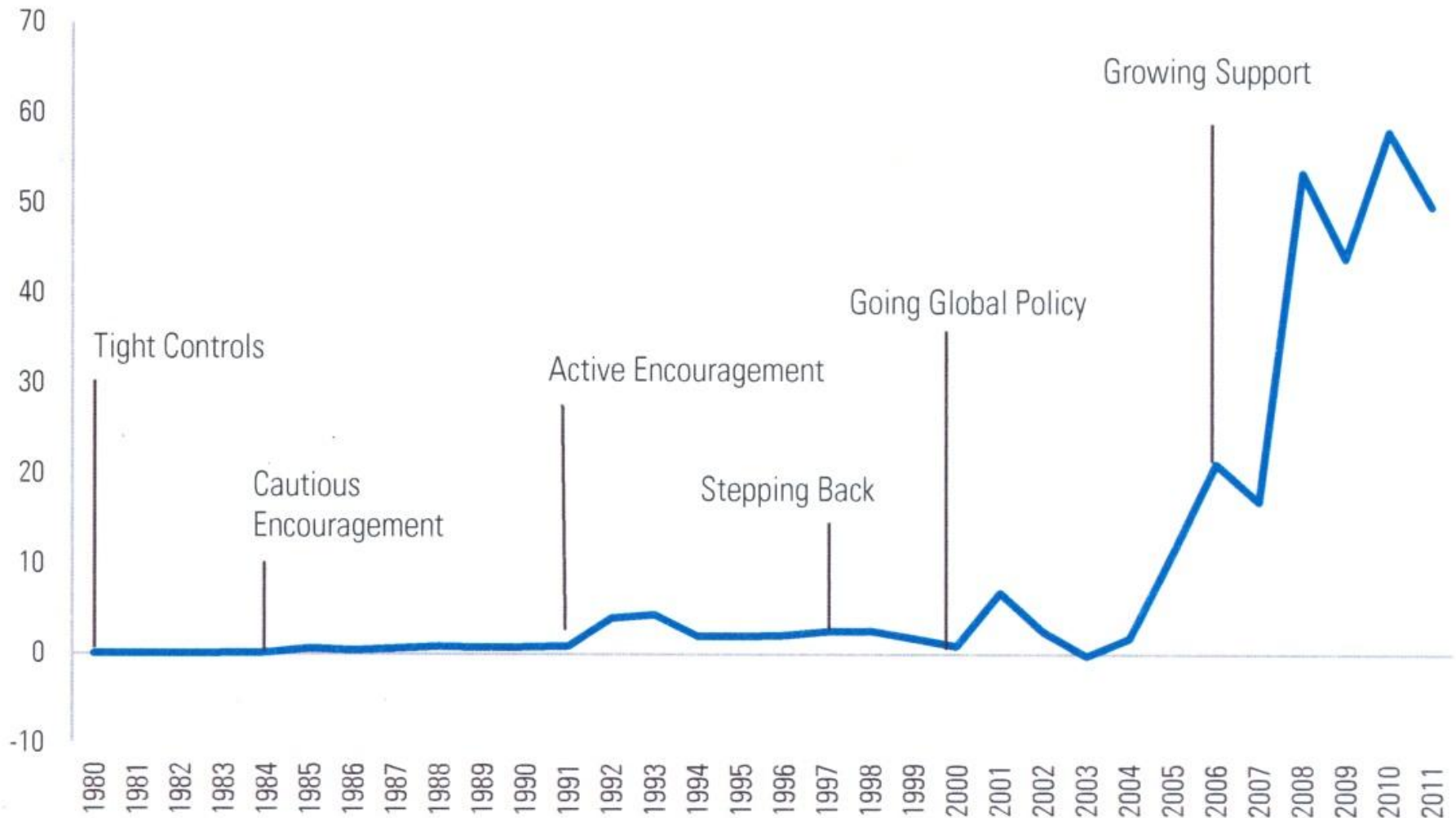
- China's outward FDI **suffered less from the credit crunch and the financial crisis**, while its competitors had to cut back their investment;
- **Market expansion was the dominant motive** to expand abroad for Chinese firms **but the search for advanced technology, know how and brands** is becoming more important;
- **Question** raised if China's OFDI expansion can be **explained by the usual economic forces** of the theory of FDI as it is strongly driven by SOEs and government policy and is searching for **ownership advantages** rather than the reverse (asset augmenting FDI).



China's Outward FDI Policy Regime



Stages in the Policy Liberalization and OFDI Flows (1980-2011)



Special impetus of China's outward FDI policy

1999-2005: "Go out" (GO) policy and creation of legal framework for OFDI (2000); WTO entry (2001)

- Trade processing activities by private companies
- Simplification of procedures and **increase of incentives for OFDI**

2006- : China started to relax and abolish the controls over OFDI. Also further increase of incentives and other promotional measures

2007- : Sovereign Wealth Funds engaging into FDI (e.g. CIC)

➤ **Wen Jiabao, Chinese Premier, March 5, 2006**

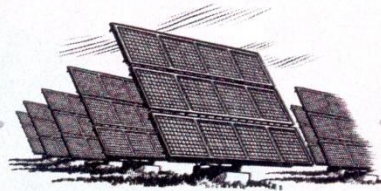
"We will support qualified enterprises in going global, making overseas investment..., establishing processing centres, marketing and service networks and R&D centres in other countries"



China's FDI in the European Union

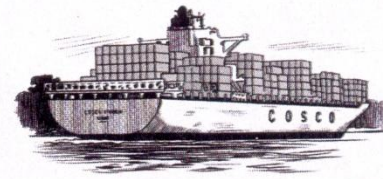


China's appetite for European firms: Some examples (2010-2011) (1)



Elkem

Norway/silicon materials
Bought for \$2 billion



Port of Piraeus

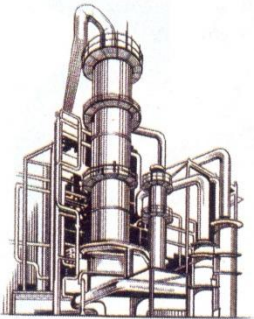
Greece/shipping
Leased for \$5 billion



Saab

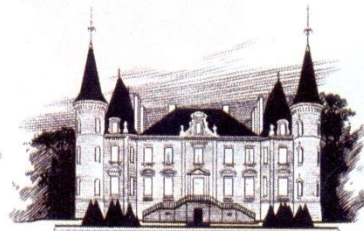
Sweden/auto
Bought for \$140 million

China's appetite for European firms: Some examples (2010-2011) (2)



BorsodChem

Hungary/chemicals
Bought a controlling stake
for \$1.6 billion



Chateau de Viaud

France/wine
Bought for \$15 million



Medion

Germany/computers
Bought a controlling stake
for \$670 million



Volvo

Sweden/auto
Bought for \$1.5 billion

Some more examples of Chinese acquisitions in EU

- 100% of German Putzmeister by **Sany** (€360 million)
- 21% of Portuguese Energias de Portugal by **China Three Gorges Project Corporation** (€800 million)
- 25% of Portugal's Redes Energeticas Nacionais by **China State Grid** (€387 million)
- 8.68% of Thames Water by **CIC** in UK (£600-£700 million)
- 60 % of Weetabix by **Bright Food** in UK (about \$ 2 billion)
- 48 % of France's Air Azur airline by **Hainan Airlines Group**
-

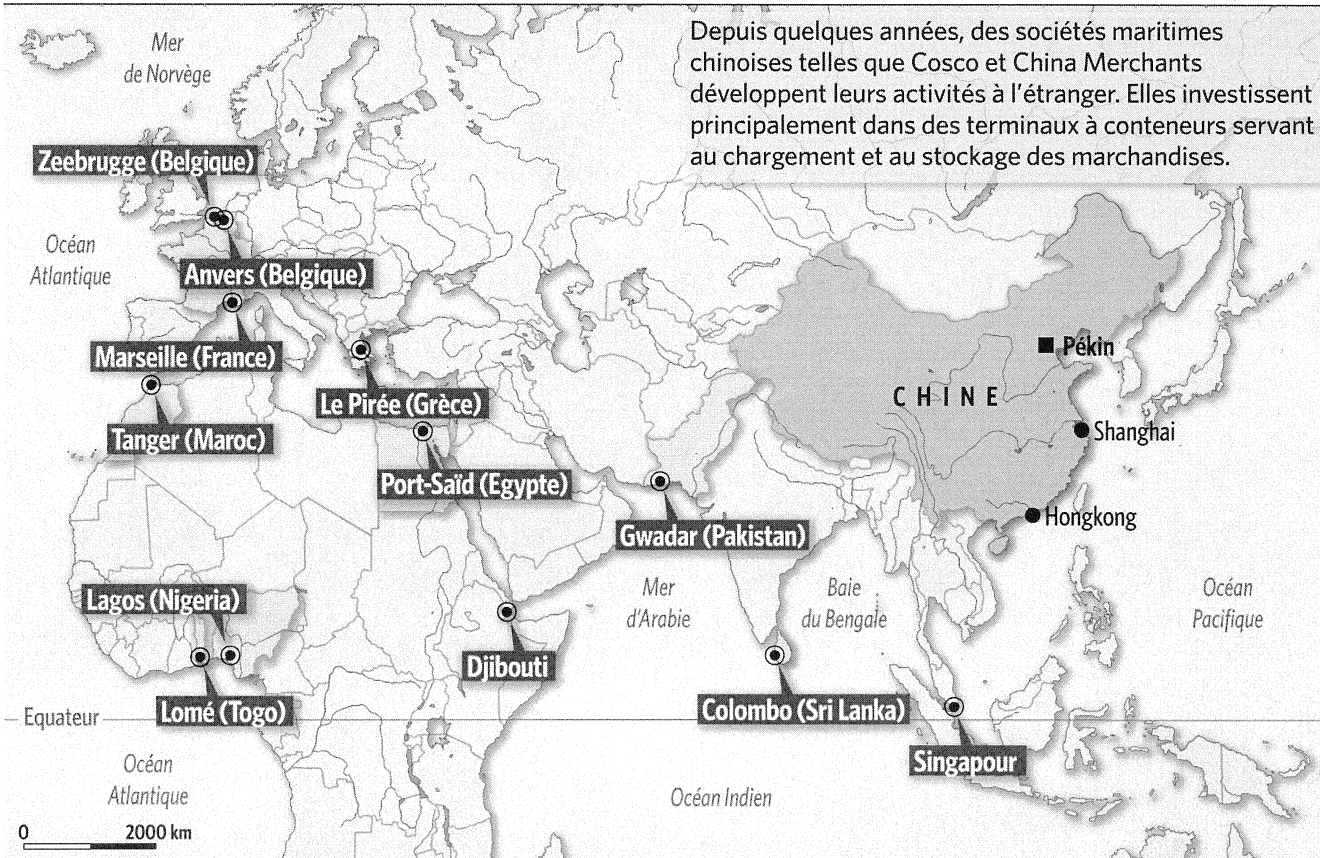
Weak financial position of European companies → Speeding up of Chinese companies to penetrate into the European market

Increasing concern in European countries

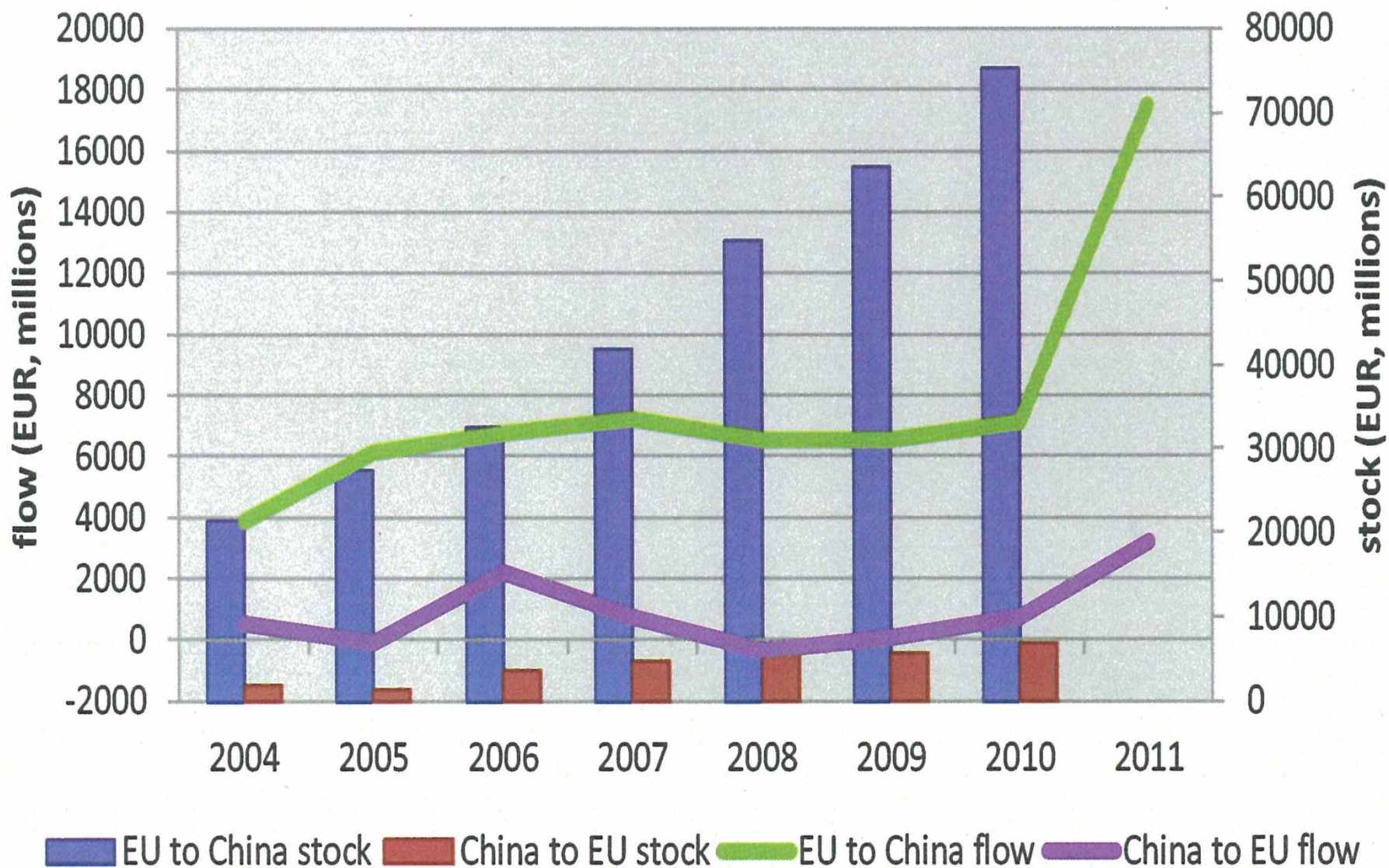
Global/European presence of Chinese maritime firms

Pékin multiplie les acquisitions aux quatre coins du globe

Depuis quelques années, des sociétés maritimes chinoises telles que Cosco et China Merchants développent leurs activités à l'étranger. Elles investissent principalement dans des terminaux à conteneurs servant au chargement et au stockage des marchandises.



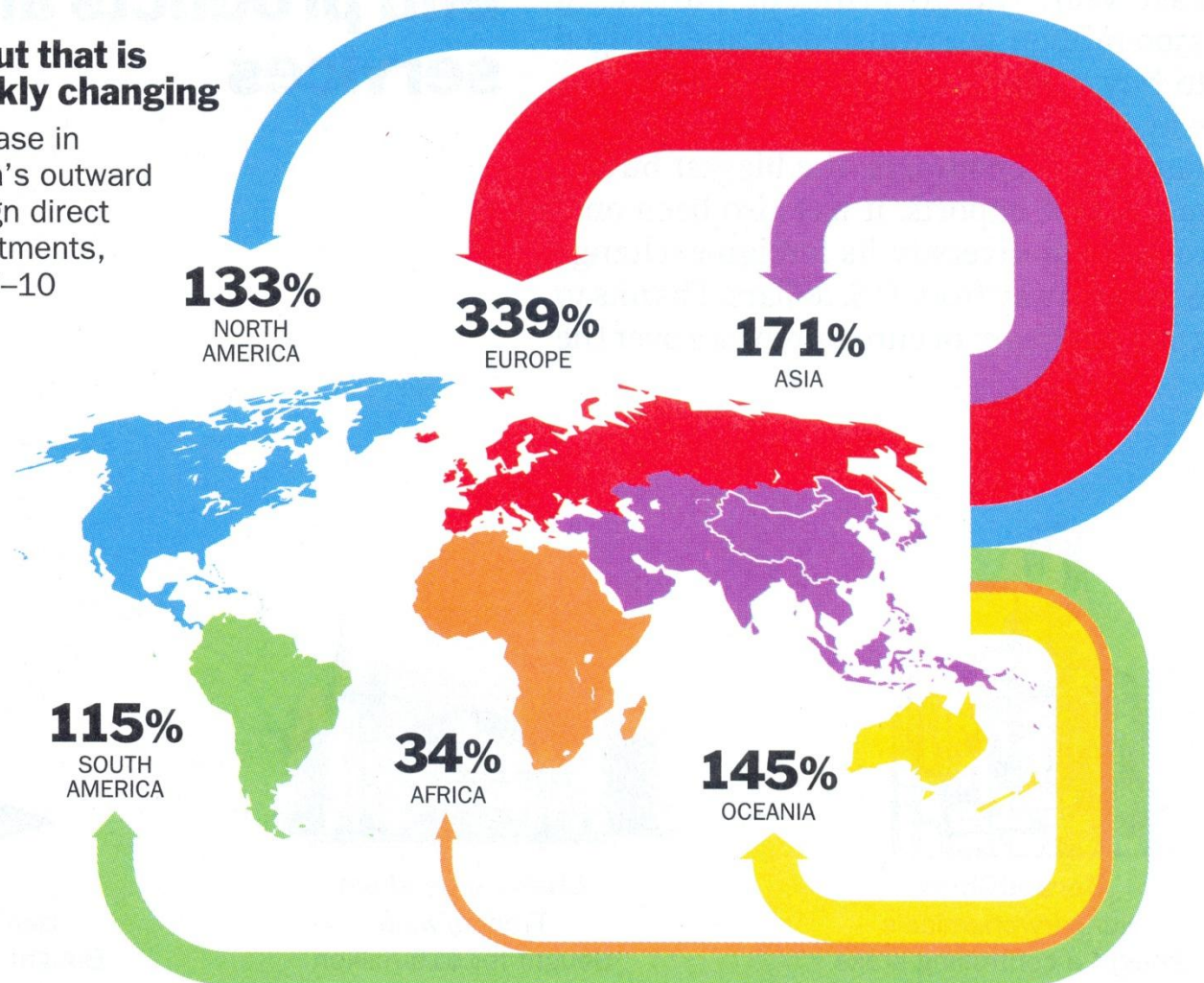
China-EU investment relationship: Flows and stocks IFDI and OFDI (2004-2011)



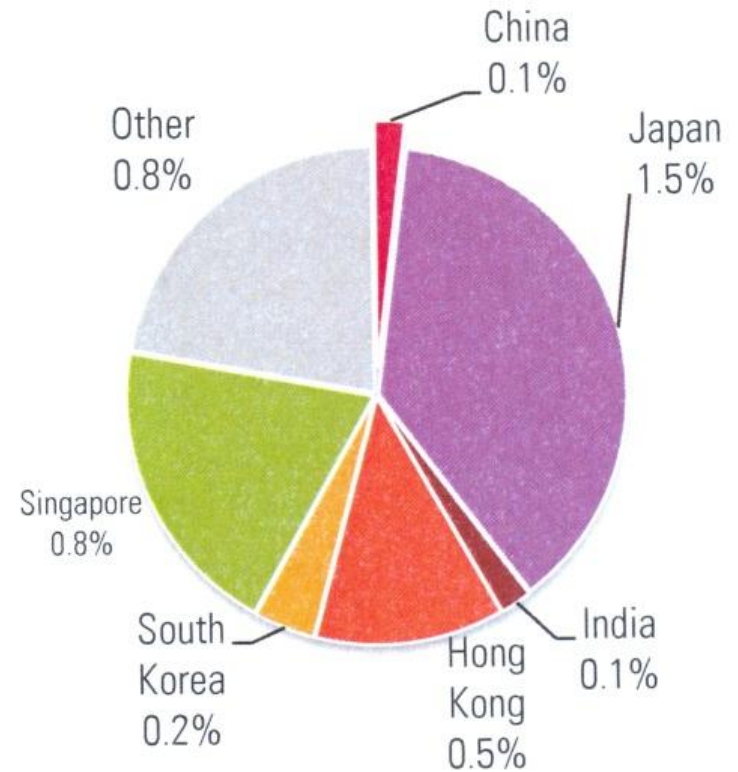
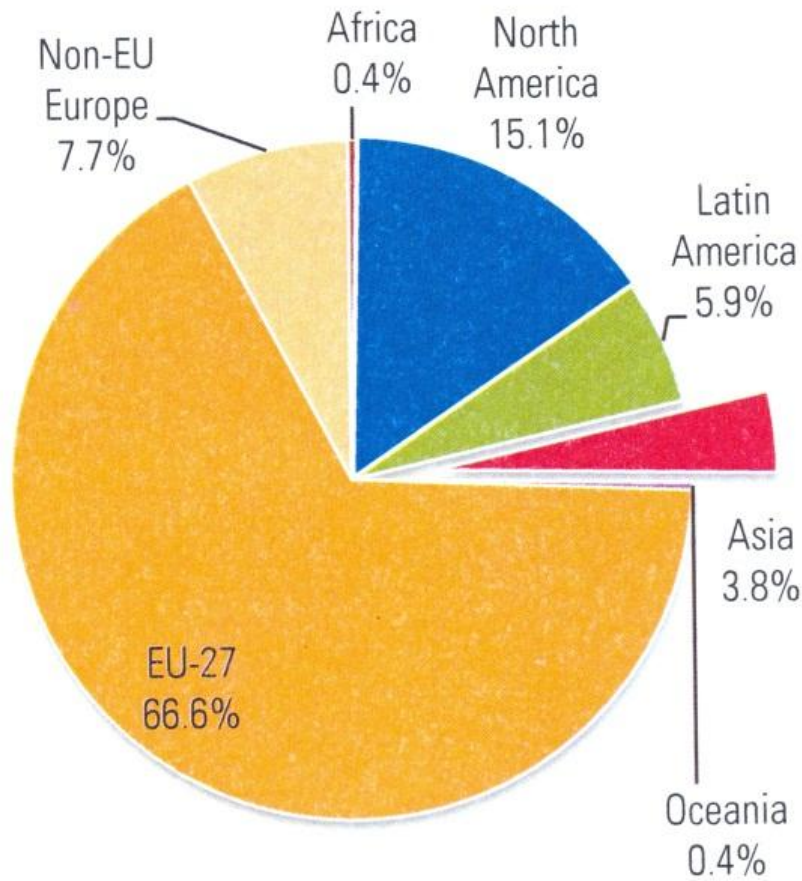
China's OFDI 2007-2010: Percentage increase by continent

... but that is
quickly changing

Increase in
China's outward
foreign direct
investments,
2007-10



Composition of the EU's inward FDI stock by source region (2010)





China's outward FDI in the EU as compared to the US



Chinese FDI in the EU as compared to the US (2011)

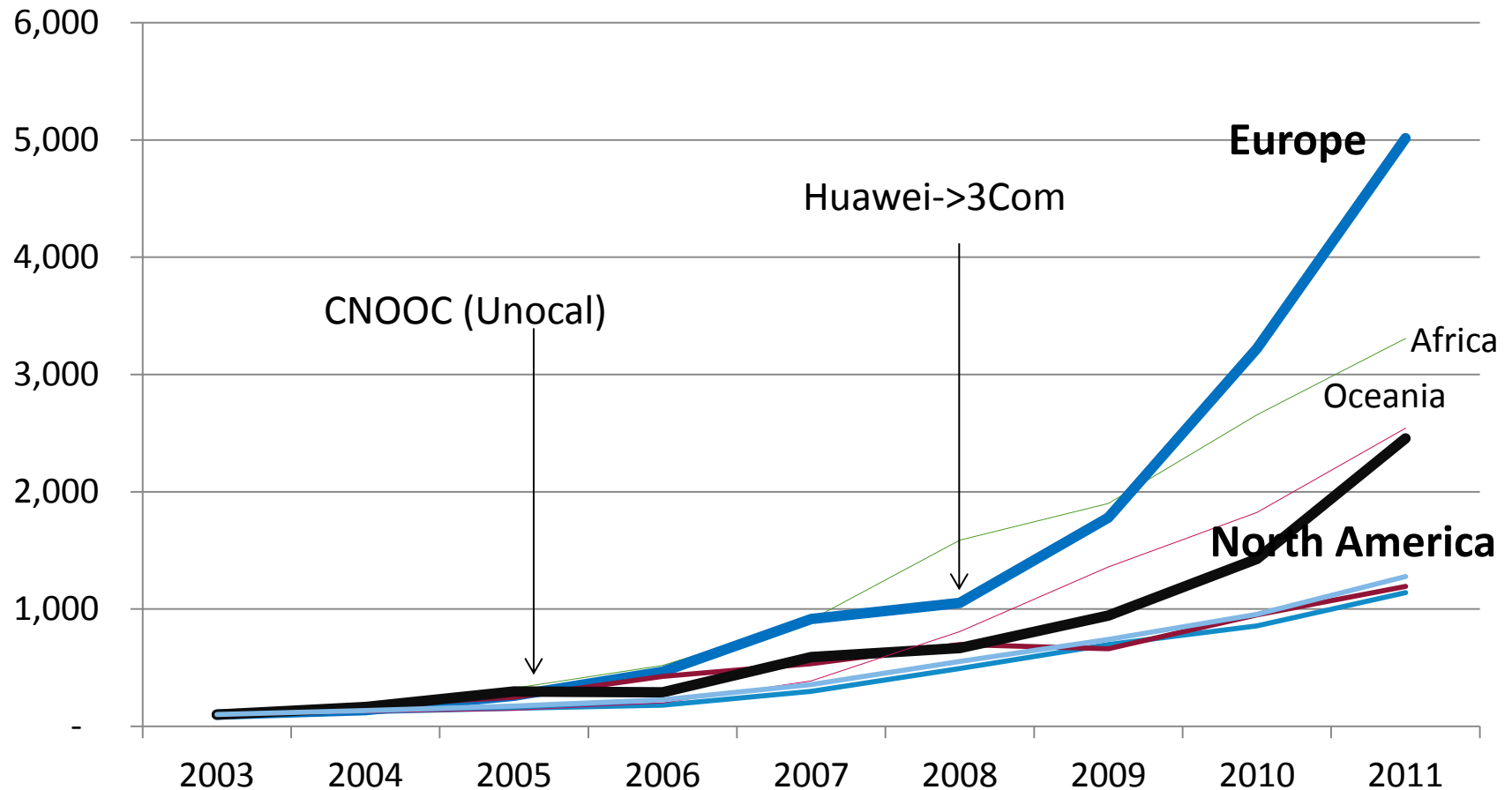
FDI flows 2011

- › US\$**7.56** billion vs. US\$**1.8** billion
- › **10.13%** vs. **2.4%** of Chinese total OFDI flows

FDI stock 2011

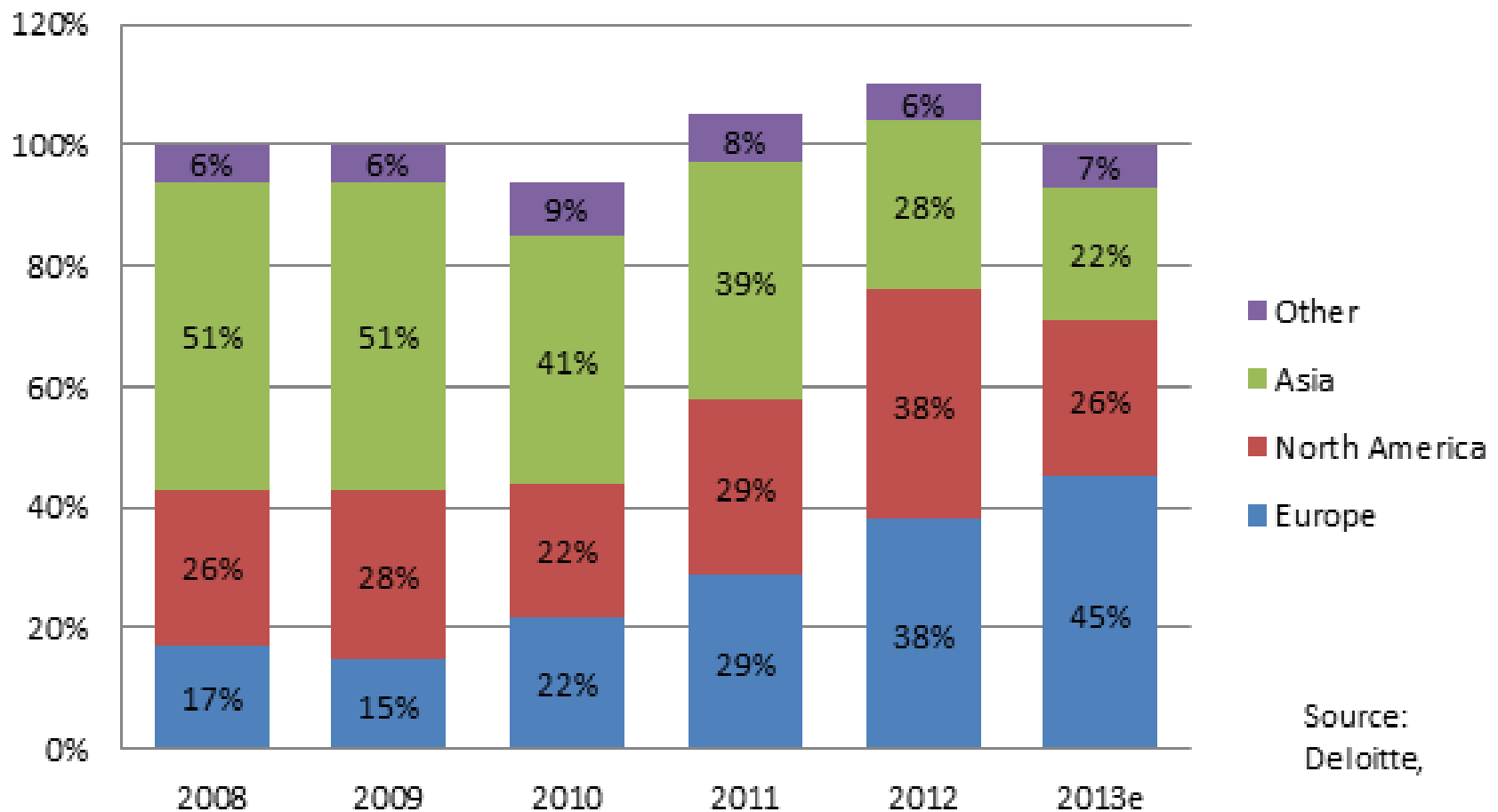
- › US\$**20.29** billion vs. US\$**8.99** billion
- › **4.78%** vs. **2.12%** of Chinese total OFDI stock

Evolution of China's outward FDI stock per region (2003-2010) (2003=100)



Europe's increasing share of China's OFDI (2008-2013)

China's Outbound Investment



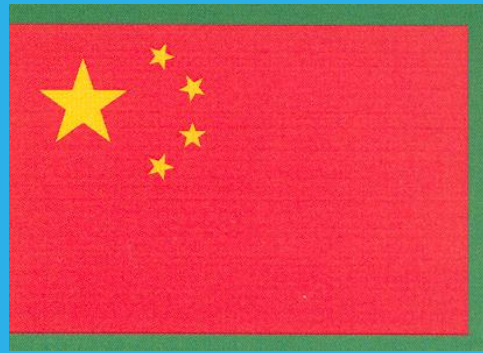
EU vs. US

The **EU** → the US

- ▶ Is becoming more of a **priority region** for Chinese firms among developed economies

Partly due to the suspicion and hostility that Chinese investors encounter in the US

- ▶ **CFIUS** --> **CNOOC** (Unocal) and **Huawei** (3Com)
- ▶ Discouragement for Chinese investors to enter into the American market via M&As in sensitive sectors



China's outward direct investment in Europe: A more complete picture



Euro-China Investment Report 2011-2012



European landscape of Chinese-owned enterprises

Carried out by the **Euro-China Centre** at the Antwerp Management School

- Haiyan Zhang
- Zhi Yang and
- Daniel Van Den Bulcke

As background study for TAF

(The Antwerp Forum, November 22-23, 2011)

- To be updated bi-annually

Identification method of Chinese enterprises in Europe (2009-2010)

Amadeus
database

18,225,135
companies
registered in **43**
European
countries

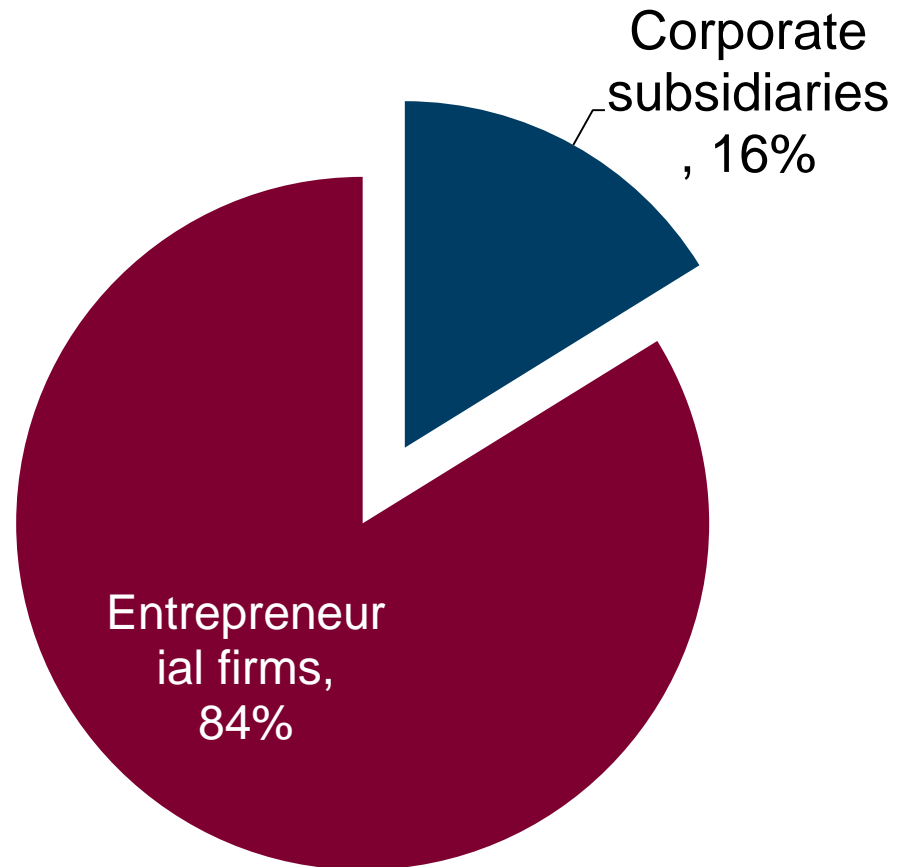
Dataset of this
study

4,676 Chinese
enterprises
registered in **28**
European
countries

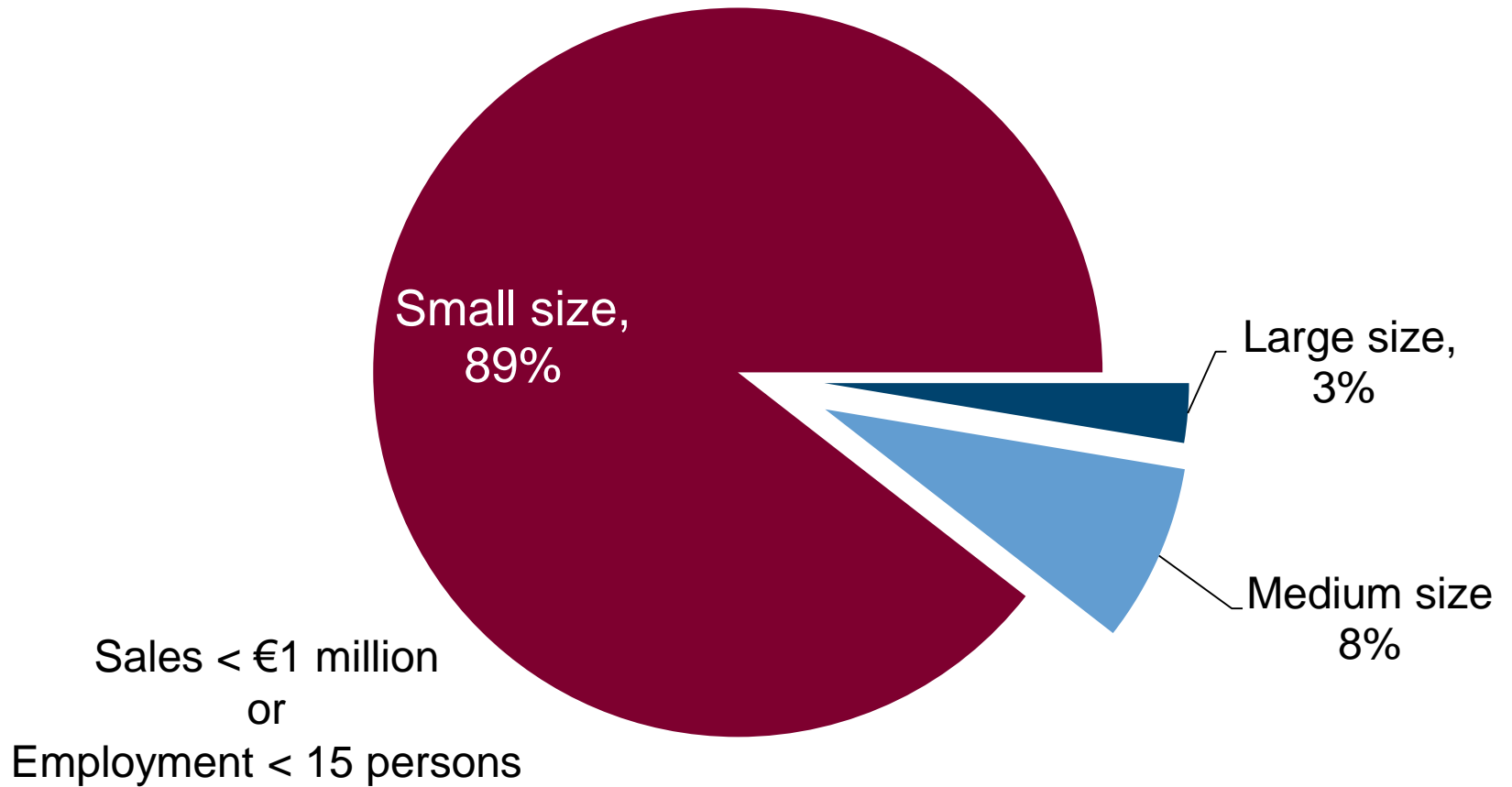
4,525 Chinese
FDI enterprises or
subsidiaries

151 Chinese
portfolio
investments

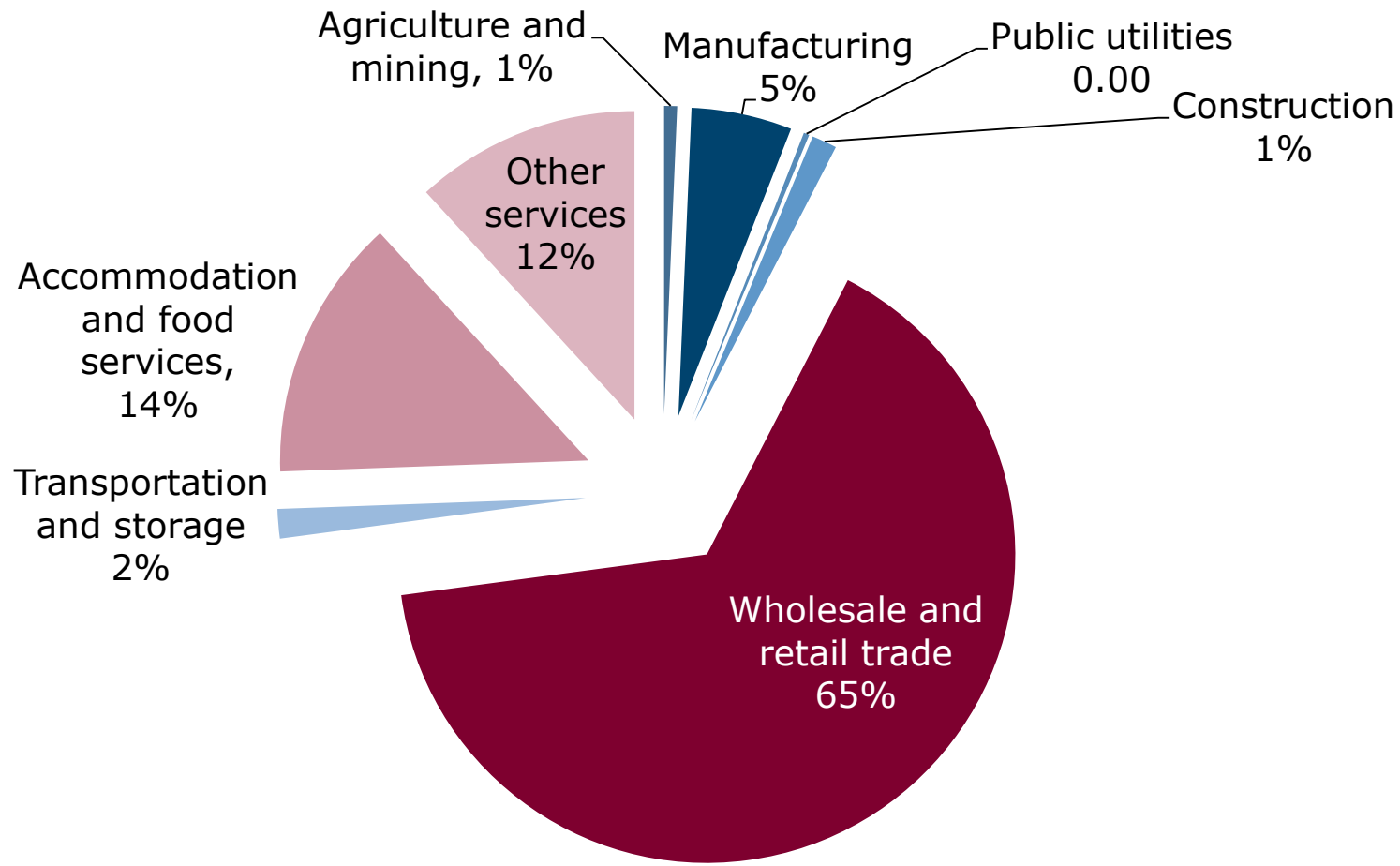
Mostly entrepreneurial firms



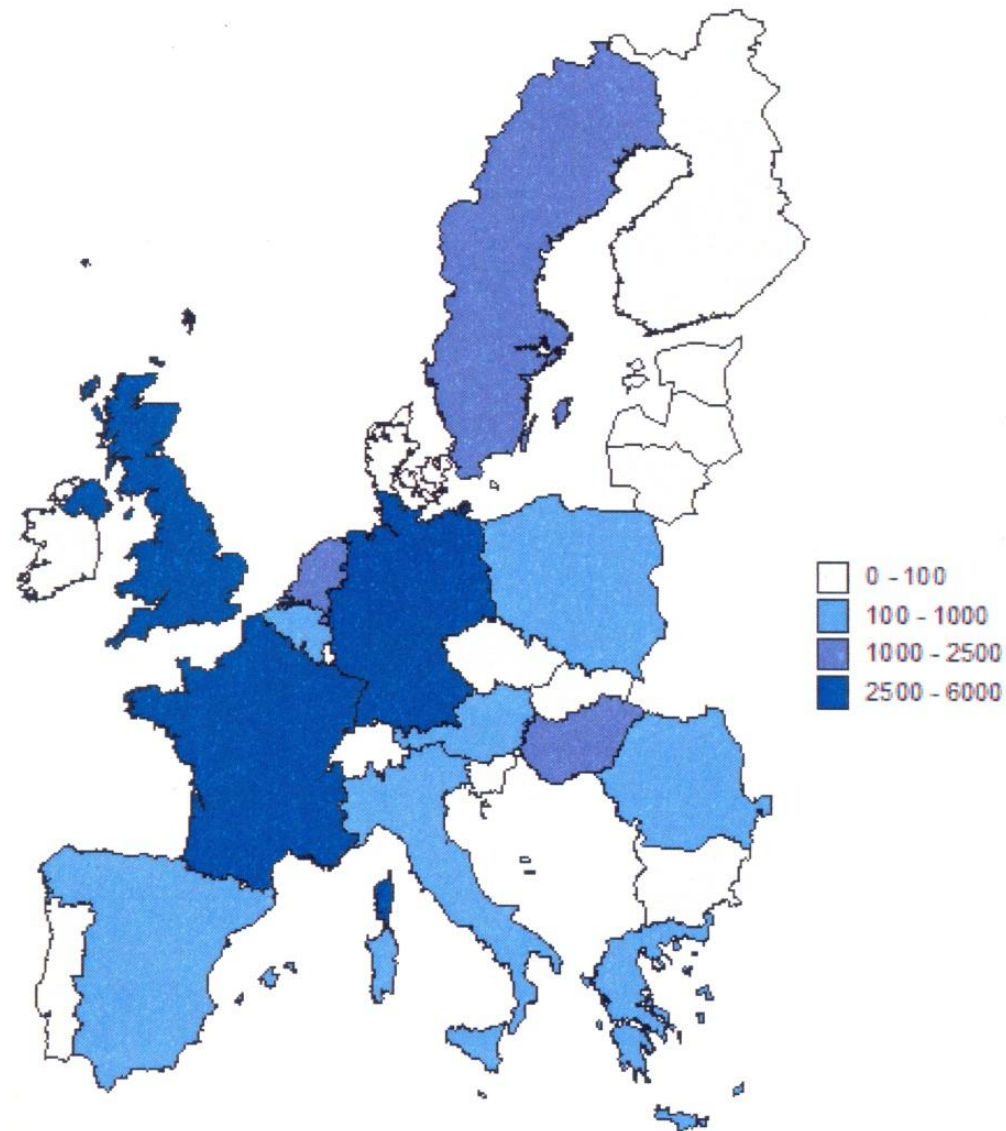
Mainly small sized companies



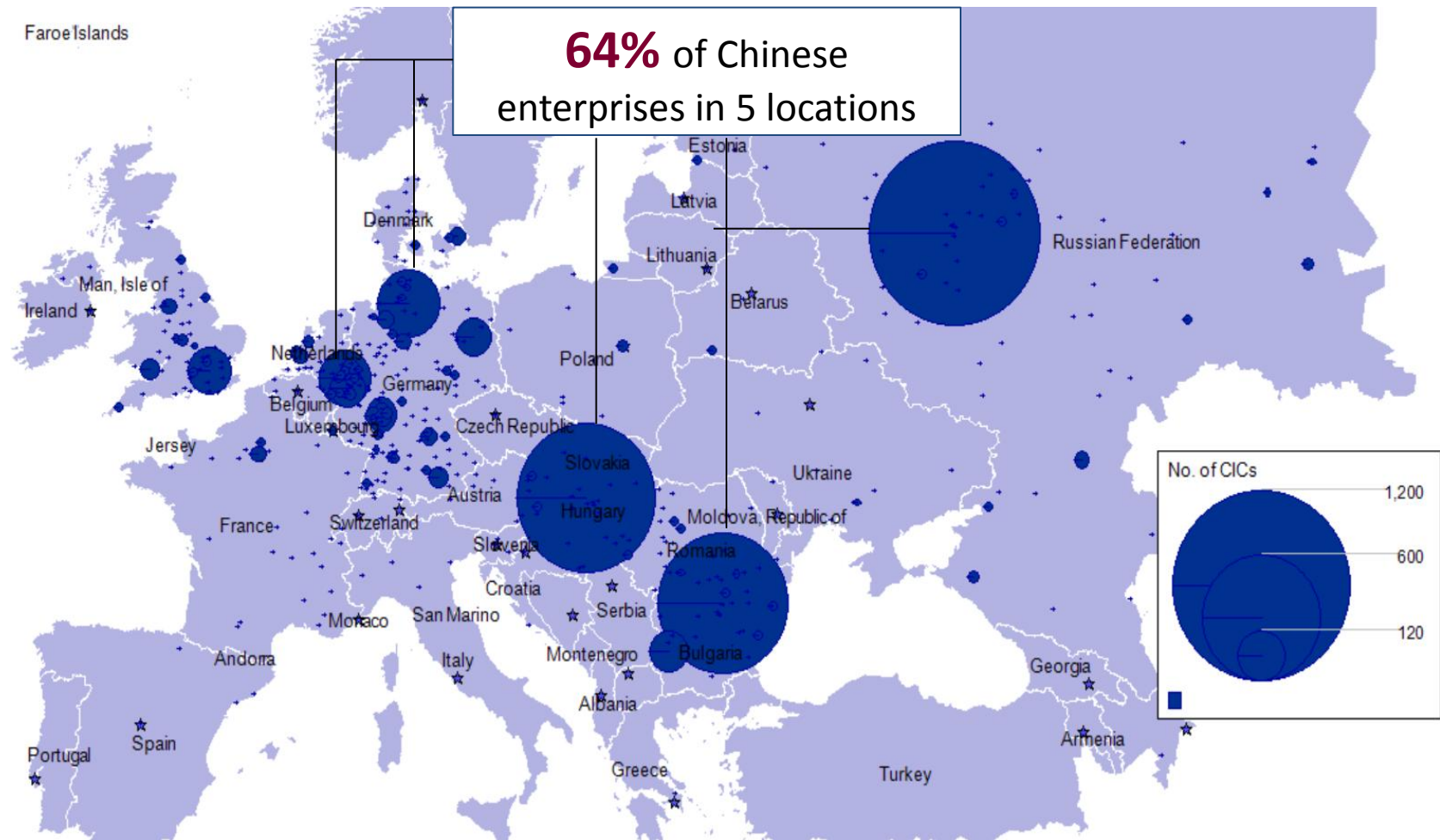
More than 90% in the service sector



Chinese direct investment in the EU-27 (2000-2011)(Rhodium Group)



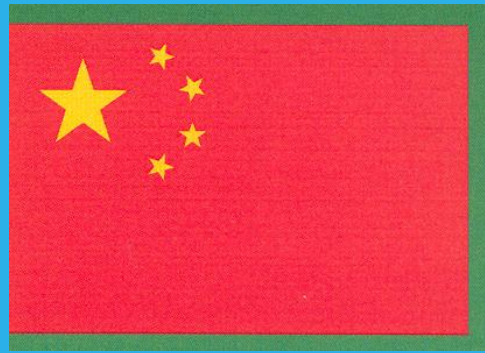
Mapping of Chinese enterprises in Europe (TAF)



Strong presence (about 2/3) in 5 European cities/urban centres

City/urban centre	No. of firms	%*
Moscow region	1,151	24.62
Budapest	812	17.37
Bucharest	715	15.29
Hamburg	188	4.02
London Inner	114	2.44
Düsseldorf	108	2.31
Grand Sofiya	88	1.88
Berlin	75	1.60
Köln	68	1.45
St Petersburg region	62	1.33
Frankfurt	52	1.11
Nordrhein-Westfalen	47	1.01

**High
concentration:
64%**



China's direct investment in the EU : Issues of concern



Challenges about China's OFDI in Europe (1)

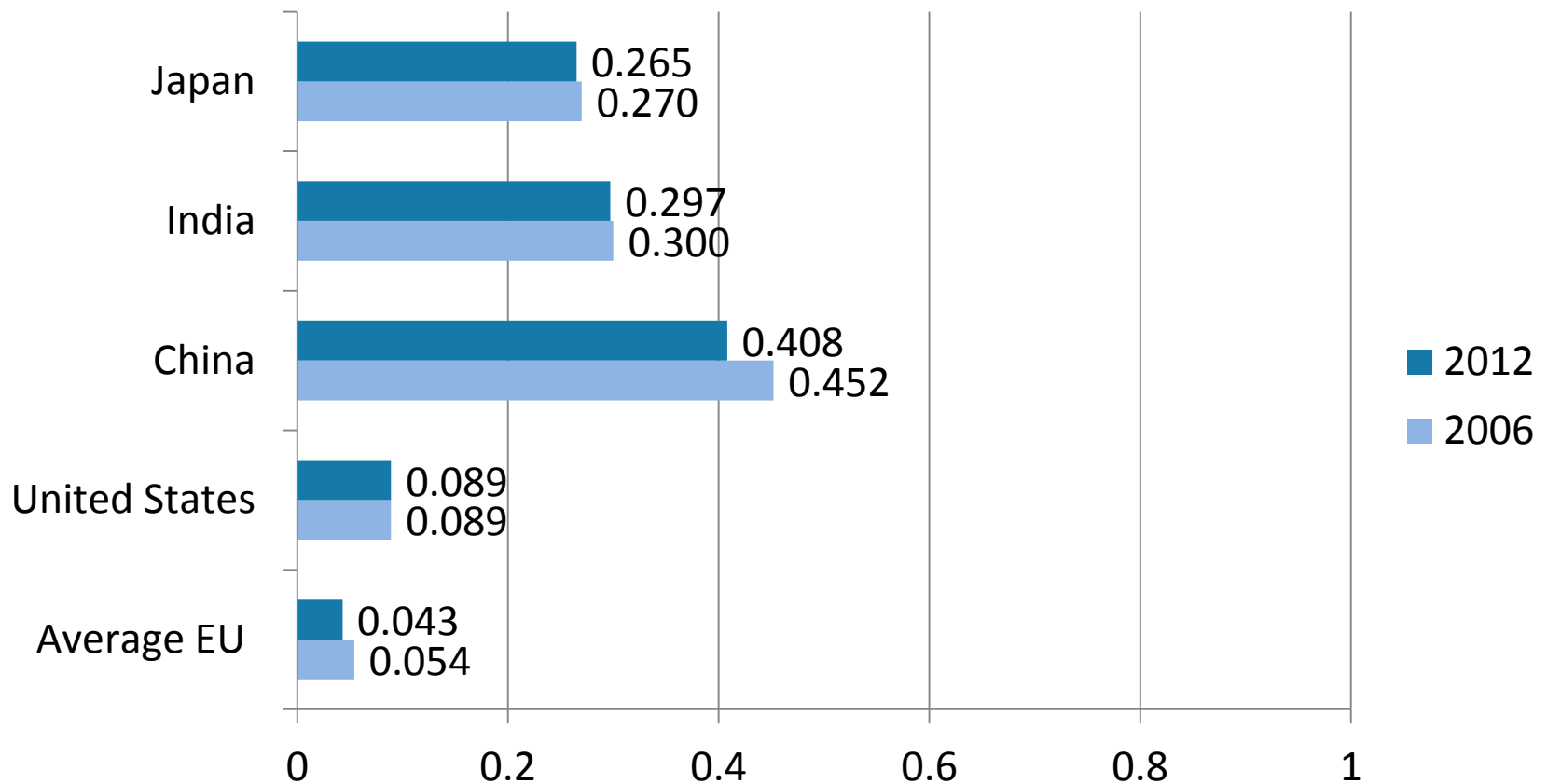
Chinese OFDI different from other countries? To a large extent yes! Why?

- Still strong elements of a **planned economy**: direct and indirect influence (e.g. Five year plans)
- Continuation of prominent **role of SOEs**
- Strong government **support of OFDI: GO!**
- Relatively more **asset augmenting** and strategic oriented motives than profit-maximizing
- **Imbalanced access** between EU and China in certain sectors: Reciprocity issue

Challenges about China's OFDI in Europe (2)

- China becoming the largest economy in the world: **changes in bargaining relationship**
- **National security** issues and Europe's fragmented approach, e.g. in telecommunications sector
- **Asymmetry in opening towards FDI**: China much more restrictive than EU countries (cfr. OECD's FDI Regulatory Restrictiveness Index China 0.4 vs. EU 0.04)

FDI regulatory restrictiveness index (2006-2012)



Other considerations about Chinese OFDI challenges in Europe

- Several **weaknesses of Chinese investors** about understanding European issues such as legal systems, labour law, intellectual property, diligence, role of NGOs, ...
- **Weak interfirm connections** with local firms (inter-firm) and intrafirm linkages (e.g. between headquarters and subsidiaries)
- **Neglect of intangibles** such as systems, people and processes resulting in difficulties in integrating across borders and cultures (cfr. TCL-Thomson failure)

Some conclusions about China's OFDI

- China's outward direct investment is still **small** at the world and European level, **but** is **growing fast** and is expected to expand further;
- Most Chinese outbound investors are **market seekers or are looking for technology, skills and brands** (also in Europe) and looking increasingly for natural resources in countries with weak institutions;
- **Europe increasingly ranks as a high priority region** for the larger Chinese firms since the middle of the last decade;
- **Within the EU, Germany and the UK score high** in attractiveness for large Chinese companies, while **East and Central Europe** host many small entrepreneurial firms;

....

Policy implications and recommendations about hosting China's OFDI (1)

- It makes sense to welcome OFDI from Emerging/BRIC, countries, including China, **to diversify the sources of FDI**;
- OFDI from emerging markets should be placed in a larger framework and **take into account immigration policy** (visa and work permits), preferably in an EU context;
- European countries and the EU should renegotiate the **Bilateral Investment Treaties** (BITs) with China and other emerging economies to make sure that the agreement is a **two-way street** (example of Germany);
- The **EU Lisbon Treaty** makes this possible as the authority of the European Commission has been extended to FDI;

Policy Implications and recommendations about China's OFDI (2)

- Danger of China and other emerging countries for **overextending** their OFDI through **incentives and government support**;
- The EU countries should insist on sufficient transparency in the investments of the **Sovereign Wealth Funds (SWFs)** from China and other emerging countries on the basis of guidelines or other supervisory measures;
- Special attention should be devoted to the strong **active governmental support** as part of China's industrial policy: especially SOEs, 'national champions' and the indigenous innovation;

Policy Implications and recommendations about China's OFDI (3)

- Efforts needed to capture the **entrepreneurial spirit of the small entrepreneurial Chinese firms** to integrate them better into the European project;
 - Need for better and more complete **data collection** about FDI both in the EU (e.g. Eurostat) and China (MOFCOM);
 - **General regulatory measures** to be preferred to specific measures with respect to the OFDI from China and other emerging economies;
 -

An European CFIUS?

In December 2010, the EU Commissioner responsible for industry voiced

- **concern** about increasing China's growing outward FDI and
- pleaded for the need to **establish a new authority** with the power:
 - to block foreign **takeovers** of strategic European businesses
 - to protect Europe's **advanced technology**
- In an interview, he referred to the 'Committee on Foreign Investment of the United States' (**CFIUS**) as a possible model

Lisbon treaty – Regulatory challenges

Pre-establishment market access -> Post-establishment protection

- › Changing FDI position of China
- › State-investor dispute settlement (international standard)

BITs: 26 BITs -> EU-China BIT

- › Diversity/difficulty
- › New elements to be included, e.g. human rights and sustainable development

Common EU FDI policy

- › Hardware without the software

Case illustration No. 1

EU Merger Regulations facing Chinese SOEs

- Understanding Chinese SOEs and their “boundaries”



Key challenges for the EU Commission for competition assessment

SOEs → SASAC

› 'China Inc'

Central SASAC → local SASACs

› Political control

Procedure:

- › Combination of turnover (thresholds at EU and national level)
- › Presence in at least three member States

Substance:

- › Independence in decision making
- › Competition assessment

Five FDI projects involving Chinese SOEs subject to EU merger control

Involved Chinese companies (Ranking in the 2011 Fortune Global 500)	Characteristics of the acquisition
China National Bluestar of ChemChina (475)	All shares and sole control in Elkem from Orkla ASA
Huaneng (275)	50% of shares held by GMR Netherlands in InterGen
Sinochem (168)	To establish a joint venture, owned 50% by DSM and 50% by Sinochem
China National Agrochemical Corporation (168)	To acquire 60% of Israeli agrochemical company Makhteshim Agan Industries Ltd. (MAI) by CNAC from Koor (part of the IDB group)
PetroChina (6)	To create three joint ventures jointly controlled by Ineos and PetroChina as part of a single transaction..

Results

All of 5 cases were **cleared in Phase I**

- › four cases cleared under the normal procedure
- › one case cleared according to the simplified procedure
- › ‘two thirds rule’ was not met: the transaction does not have a EU dimension

Yet

All questions about Chinese SOEs are still open

- › The European Commission took a ‘**wait and see**’ position
- › **Time bomb !?**

Case illustration No. 2

COVEC in Poland

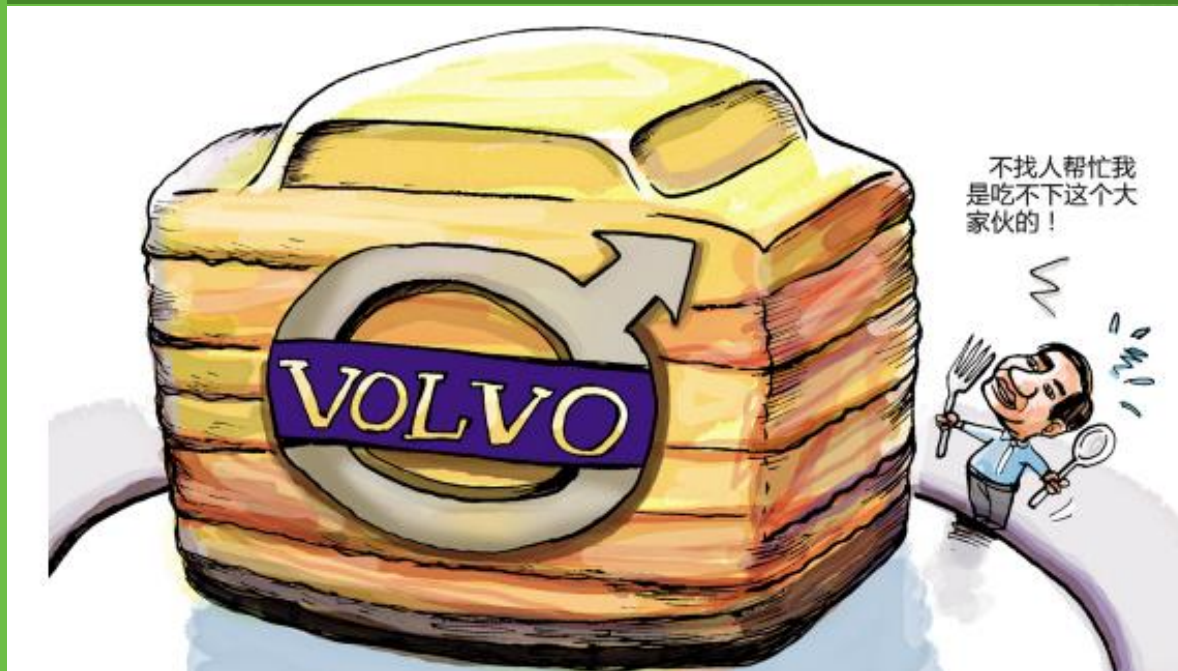
- Understanding Chinese SOEs and their “low-cost leadership strategy”



Case illustration No. 3

Geely's Volvo acquisition: Will it be successful ?

Post-acquisition integration



Case illustration No. 4

China in Prato

- Ethnic entrepreneurs



OECD FDI regulatory restrictiveness index

Pre-establishment conditions

- › Foreign equity limits (foreign share in the equity capital)
- › Screening and approval requirements for new FDI/acquisitions

Post-establishment protection (operational aspects)

- › Restrictions on key foreign personnel/directors
 - › Nationality/time/financial requirements
- › Other operational restrictions
 - › Establishment of branches/local incorporation required
 - › Reciprocity requirements
 - › Restrictions on profit/capital repatriation
 - › Access to local finance
 - › Land ownership

Key challenges for the EC in assessment

SOEs → SASAC

› 'China Inc'

Central SASAC → local SASACs

› Political control

Procedure: Combination of turnover

Substance: Independence in decision making

› Competition assessment

On the basis of the same regulation applied to European SOEs