China’s FDI in Africa and the Role of Institutions: 
A Theoretical Analysis on the Explanatory Power of Conventional FDI Theories
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**LIST OF ABBREVIATIONS**

- CAD: China-Africa Development Fund
- DC: Developed Country
- DOTS: Direction of Trade Statistics
- FDI: Foreign Direct Investment
- FOFAC: Forum on China-Africa Cooperation
- FPI: Foreign Portfolio Investment
- GDP: Gross Domestic Product
- GNP: Gross National Product
- IB: International Business
- IBM: International Business Machines
- IDP: Investment Development Path
- IFDI: Inward Foreign Direct Investment
- IMF: International Monetary Fund
- LDCs: Least Developed Countries
- LLL: Linkage, Leverage, Learning
- MNEs: Multinational Enterprises
- MOFCOM: Ministry of Commerce People’s Republic of China
- MOFERT: China’s Ministry of Foreign Economy Relations and Trade
- NOI: Net Outward Investment
- Oa: Asset Specific Advantages
- OECD: Organization for Economic Co-operation and Development
- OFDI: Outward Foreign Direct Investment
- Oi: Institutional Assets
- OLI: Ownership, Location, Internalization
- Ot: Transaction-cost Minimizing Advantages
- SASAC: State-owned Asset Supervision and Administration Commission
- SEZ: Special Economic Zones
- SOE: State-owned Enterprise
- TAZARA: Tanzania-Zambia Railway
- UN: United Nations
- UNCTAD: United Nations Conference on Trade and Development
- WTO: World Trade Organization
Abstract

This thesis set out to explore the strength of conventional foreign direct investment theories in uncovering the motives of China’s investment in Africa. A case study approach was taken combining qualitative and quantitative sources. The motivation of outward foreign direct investment activity from China to Africa points to being dual. The resource-seeking motive drives state-owned enterprises. Private Chinese firm’s objective is of the market-seeking kind. The hypothesis of unconventional theories that exploration rather than exploitation of ownership advantages determine FDI was discovered to give an insufficient description of the case. Exploitation of ownership advantages has allowed for exploration. The relocation of low-end manufacturing to Africa is a result of China transforming towards more knowledge-based industries. Outward foreign direct investment from China to Africa flow to the industries which they are disadvantaged transferring capital, technology, and knowledge. Consistent with the theory of the Investment Development Path, China as a result of gaining experience from inward investment has reached a stage of increased focus on outward foreign direct investment. The transfer of network knowledge from the Chinese government, and private investors present in Africa substitutes experiential knowledge. Consequently, allowing for deviation from the Uppsala model. Psychic distance is eased through Chinese government initiatives, and Chinese business networks facilitating learning and understanding of the market. In addition, shared similarities in cultural characteristics bridge the gap. China’s ownership advantage in Africa was first of foremost found to be an institutional one.
1. Introduction

In International Business (IB) literature, foreign direct investment (FDI) is commonly theorized to be initiated based on organizations being capable of transferring a set of capabilities, or a country reaching a certain stage in development. In addition, knowledge of a market, geographical proximity, and the cost-saving motive are all factors that are believed to have an effect on the FDI decision. In recent years, some have taken the view including Buckley, et al. (2007), and Mathews (2006) that FDI theories are formulated to describe the internationalization process from developed countries. The opposing arguments to traditional theories are twofold in the case of China. The first is that China’s business environment encompasses characteristics that influence the FDI decision, which traditional theories might not have taken into account. The second is that China might be driven to outward foreign direct investment (OFDI) based on the search for exploring advantages, and not exploiting as predicted by traditional theories. An identified gap in existing research and literature was whether conventional FDI theories, or alternatively unconventional theory and hypotheses suggested for China can explain the country’s increased investment focus on Africa.

China’s choice of Africa as an investment destination has received extensive amounts of media and literature attention. The identified motive is frequently believed to be resource based, and many hold the idea that it resembles neo-colonialism. Compared to the existing attention and criticism China has received for its focus on Africa, official Chinese statistics on FDI reveal that the volumes of FDI to Africa are not massive relative to other regions. There are however, certain features of their investment relations that are distinctive and have caused additional interest for writing this thesis. Among others, the use of relationships to facilitate business, familiarity of being a developing country, and China’s non-interference policy towards African politics. In connection with FDI theory, the goal of this thesis is to investigate if these distinctive features reduce the value of conventional FDI theories. With my thesis, I hope to contribute with an overview of the collaboration and provide a different view on the existing literature by combining FDI theory, business history, and the effect of policy and institutions.
1.1 Problem Statement

What motivates Chinese outward FDI to Africa, and is it in accordance conventional FDI theory?

For each theory of the five selected theories in the literature review, propositions are constructed to identify the main idea of the theory. The propositions are further used in the discussion to examine the fit between theories, and the specific case of China’s FDI in Africa.

The Product Cycle

Proposition 1: China’s low-end manufacturing is being relocated to Africa because of cheaper factors of production.

Kojima’s Trade Theory

Proposition 2: China’s FDI in Africa is a strategy to compensate for disadvantaged industries.

Investment Development Path Theory

Proposition 3: China’s FDI in Africa is the outcome of reaching the latter stages of the Investment Development Path.

Uppsala Internationalization Theory

Proposition 4.1: Increased FDI in Africa is a result of increased knowledge of the market.

Proposition 4.2: The obstacle of psychic distance is manageable.

The OLI Paradigm

Proposition 5: China’s FDI in Africa is an outcome of existing OLI advantages.

Proposition 1, 2 and 3 relate to China’s economic development.

Proposition 4 and 5 will address the specific case of China-Africa.
1.2 Methodology

The methodology chosen when writing this thesis is qualitative. Within the qualitative methodology, a case study approach was taken. Case studies allow combining qualitative and quantitative evidence, and is not limited to a particular data collection method (Yin, 1981). In case studies, findings from the previous developed theories guide the data collection and analysis. The qualitative evidence leads to a discussion of the relevance of theory in relation to the case. The thesis is supplemented by quantitative statistical data conducted by institutional agencies, governments, and secondary empirical research to draw a conclusion. Yin (1981) distinguishes between types of case studies to be exploratory, descriptive, and explanatory. The explanatory method is the one adopted in this thesis, and involves using both qualitative and quantitative research to explore and describe a phenomenon. The case study approach is ideal when carrying out a holistic and in-depth analysis (Tellis, 1997).

The method gives me the opportunity to present a theoretical analysis, statistical data, and more than one finding in empirical studies when trying to answer my research propositions to investigate whether there is a fit between theories and reality. Criticism of case study methodology often focuses on generalization. Single-case studies especially are greatly criticized for lack of generalizability. (Stake, 1995) argues that generalization can take two forms, petite and grand. Petite generalization refers to generalization within the case. Certain petite generalization within this case occurs, for example by drawing conclusions based on analysis of OFDI activity from a country to a continent and not that of individual firms. Grand generalization refers to drawing general conclusions on the issues of the case, and applying to a different case. Grand generalization is not the objective of this thesis. A case study intention is finding the particularities of the specific case (Stake, 1995).
1.3 Research Approach

The first step has been creating a theoretical background for my analysis. To enhance the explanatory strength of theory, theoretical triangulation was used. Theoretical triangulation refers to using multiple theories simultaneously, to look at the same situation through different perspectives to support or refute findings. Theoretical triangulation has benefits as well as limitations. The benefits include an in-depth analysis, and decreasing alternative explanations. The limitations include the occurrence of confusion due to a poorly defined theoretical framework. The goal when writing the literature review was to provide an overview of FDI theories that are generally accepted as being the main theories. When doing this I was inspired by the selected leading theories in the book “Multinational enterprises and the global economy” by Dunning & Lundan (2008).

Secondly, I wanted to distinguish whether the unit of analysis of the theories was at the macro level, or micro level. The OLI paradigm is included because even though it is commonly referenced as a microeconomic theory, the paradigm intention is to describe the internationalization process of all firms from a particular country or group of countries (Dunning, 2001). Lastly, to create a structure and overview for the theoretical context of this thesis, Table 1.1: Selected Leading Theories, Frameworks and Hypotheses on FDI was created, and is presented in chapter 2.

The next step was to collect and examine statistical evidence. To answer my problem statement and research propositions, secondary sources of data were collected and analyzed from three sources. United Nations Conference on Trade and Development (UNCTAD) was established in 1964 to promote trade and integration of developing countries into the world economy. UNCTAD offers access to the institutions interactive database where data is collected through national sources such as central banks, ministries and statistical offices. Data from UNCTAD can be copied and distributed freely, as long as UNCTADstat is cited as a source. The database is one of the most inclusive databases of FDI activity, and covers almost all economies in the world.
Ministry of Commerce People’s Republic of China (MOFCOM) data is the second source of data. The reasoning for supplementing UNCTAD data with MOFCOM data is that MOFCOM data is a national source that contains more wide-ranging data on China, including regional and sectoral distribution. While UNCTAD data on China is available from the year 1982, MOFCOM data can only be used from 2003. “Before 2003, the method used by MOFCOM to collect OFDI statistics was inconsistent with international standards, and it is believed that the official statistics seriously underestimated the actual OFDI volumes from China” (OECD, 2008, p. 71). The international standard in question relates to OECD benchmark definition of foreign direct investment, which provide a detailed approach to which components constitute as FDI, and how the transactions should be measured and recorded. MOFCOM data is accessible through the statistical bulletin published yearly with data on the OFDI activity from China. The last source of secondary data is from the International Monetary Fund (IMF) Direction of Trade Statistics (DOTS). The database comprehends statistics on the value of merchandise exports and import between China and Africa aggregated at the national level.

1.4 Credibility of Data Sources

UNCTAD compiles data from national and international sources such as IMF and OECD when national data is not obtainable. UNCTAD figures on Chinese OFDI conform to the international standard definition of FDI, and are known to be an accurate and reliable source. UNCTAD reports figures that more comprehensively cover Chinese outward FDI flows (Kolstad & Wiig, 2012). Yet, UNCTAD data falls short in providing a detailed description of total outward FDI from China including a sectoral and regional overview. For these purposes, data from MOFCOM is used. From 2003, Organization for Economic Co-operation and Development (OECD) approved MOFCOM data to be of international standard. MOFCOM has set an approval process for enterprises wishing to engage in foreign investment, and is rationally only able to pick up investments that are reported to the ministry. Underestimation of the actual OFDI volumes might occur based on enterprises escaping the formal approval process (OECD, 2008) .
In addition to underreporting, ‘round tripping’ seems to be prevalent in China. Both Davies (2012), and Kolstad & Wiig (2010) claim that OFDI statistics from China includes ‘round-tripping’. Resulting in investment relocated for the sole purpose of taking advantage of favorable host country conditions such as tax avoidance. Alternatively, the possibility that China is the end stop for investment but ‘round-tripping’ allows for receiving favorable conditions as a foreign investor. This can lead to discrepancies between what is reported, and what is actually going on in reality. On one hand, Chinese official FDI statistics suffer from having flaws such as underreporting and ‘roundtripping’ that cast doubt to its validity. On the other hand, UNCTAD has used MOFCOM as its national source from 2003, and data from Chinese official reports is the most consistently used statistical evidence in academic research on China’s FDI activity. Ultimately, I am aware of the issues of validity yet I still find the data necessary for my analysis as it is the only wide-ranging source.

The IMF DOTS database covers annual, quarterly, and monthly export and import data for a 187 countries from 1981-2013. Member countries of the IMF are required to report trade statistics. If a country does not report current trade statistics or trade statistics is not available for a country, partner country statistics make it possible to estimate trade. Because of differences in trade reporting methods, there can be discrepancies between a country's recorded exports and the trading partners recorded imports. Estimated trade statistics are not provided in the instances where both trading partners do not report data during a ten-year period. The benefits of IMF DOTS data include the high coverage of countries, and number of years of reporting. The disadvantages of the data include differences in reported trade methods.
1.5 Delimitations

The limitations of this thesis are resultant to the FDI theories chosen to be in described in-depth, the time horizon of the analysis of data, and the broad analysis of a continent and country. Table 1.1: Selected leading theories, frameworks and hypotheses on FDI, includes selected important contributions made on the theory of FDI. However much a number of these theories contributed to FDI theory in a historical context, the analysis of some of these will not shed light on my problem statement. To show my awareness of their contributions to FDI theory they are included in my table with author, year, and key argument. The time horizon chosen is an additional delimitation. The focus period of this thesis is from 2001-2010. In 2001, China went through a major liberalization reform through the ‘go global’ strategy and OFDI has grown significantly since.

The focus timeframe is continuous with one exception. China’s outward FDI is examined from 1982 and inward FDI from 1970, which is when UNCTAD started to collect data for China. This is done intentionally to show the effect of changes in policy, and the path of development. In addition, Africa being a continent there might be variations in the scale of Chinese FDI present in the different countries. My intention is to create an overall overview of Chinese presence in Africa, and not a country specific analysis. Lastly, there are many microeconomic effects of China’s investment in Africa that fall outside the scope of this thesis.

1.6 Structure

Chapter 2 will be focused on FDI theory, and lay the theoretical foundation for the analysis. The theoretical framework is further used to study the trends of China’s outward foreign direct investment (OFDI) in chapter 3. Chapter 4 will be exploring the relationship between China and Africa based on particularities of China found in the previous chapter. Chapter 5 will give room for a discussion, including newer theories suggested for China and dismiss or support the research propositions. Chapter 6 will conclude.
2. Theoretical framework

2.1 Definitions

There exists numerous of definitions of FDI, some more broad than others. I find that most appropriate for this thesis is to stick the definitions of the sources of data. “FDI can be defined as an investment made by a resident of one economy in another economy, and it is of a long-term nature or of ‘lasting interest’ ” (UNCTAD, 2009, p. 35). UNCTAD differentiates FDI from foreign portfolio investment (FPI) and other forms of international investments based on the element of control. The element of control relates to ownership, and is defined as 10 percent or over. MOFCOM does not provide an own definition of FDI. Following the reasoning that China from 2003 is following the OECD benchmark definition of FDI, OECD definition is used as substitute. “Foreign Direct Investment (FDI) occurs when a business located in one country (the direct investor) invests in a business located in another country (the direct investment enterprise) with the objective of creating a strategic and a lasting relationship” (OECD, 2008, p. 62). Correspondingly, to UNCTAD, lasting interest is defined as ownership of 10 percent or more.

The mentioning of multinational enterprises (MNEs) occurs through several stages of this thesis. The connection between FDI and MNEs is noticeably in the definition of MNEs. Dunning & Lundan (2008) describe an MNE as an enterprise that engages in FDI or controls value-added activities in more than one country. Moosa (2002) offers similar insight in his classification of MNEs, suggesting that a firm becomes an MNE when undertaking FDI. The terms multinational corporation, transnational enterprise and multinational enterprise are commonly used interchangeably. The latter term, multinational enterprise (MNE) will be used in this thesis.

2.2 Literature Review

Table 1.1: Selected Leading Theories, Frameworks, and Hypotheses on FDI underneath summarizes selected theories of FDI, name of researcher, key argument and which academic research field the theory belongs in. The theories highlighted in bold are the theories that are analyzed in- depth in this thesis. The reason why I chose these theories for my analysis is that I wish to focus on FDI from China to Africa on a macroeconomic level. The chosen theories seem suitable for achieving my purpose.


Table 1.1: Selected Leading Theories, Frameworks, and Hypotheses on FDI

<table>
<thead>
<tr>
<th>Macro Economic Theories</th>
<th>Micro Economic Theories</th>
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<tbody>
<tr>
<td>Theory</td>
<td>Author(s)</td>
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<td>Theory</td>
<td>Author(s)</td>
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<td></td>
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<tr>
<td>Industrial Organization Theory</td>
<td></td>
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<tr>
<td>Theories of the Firm</td>
<td></td>
</tr>
<tr>
<td>The product cycle</td>
<td>Vernon (1966)</td>
</tr>
<tr>
<td>Internationalization process</td>
<td>Johanson and Vahlne (1977, 1990), Eriksson, et al. (1997)</td>
</tr>
<tr>
<td>Theories of International Capital Movement</td>
<td></td>
</tr>
<tr>
<td>Currency area theory</td>
<td>Aliber (1970)</td>
</tr>
<tr>
<td>Theories of trade</td>
<td></td>
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<td>--------------------------------------------------------------------------------</td>
<td></td>
</tr>
<tr>
<td>Kojima (1973 to 1982)</td>
<td>FDI should be undertaken when the country has a comparative disadvantage but can generate value-adding activity in a different country</td>
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<table>
<thead>
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<th>The Eclectic Paradigm (OLI paradigm)</th>
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<tr>
<td>Dunning (1977, 1988, 1998)</td>
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<tr>
<th>The Investment Development Path</th>
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2.2.1 Conventional Theories

I have put forward the concept of conventional theory, which I wish to explain more carefully. Inspired by Moon & Roehl (2001) who suggest a dissimilarity between conventional and unconventional FDI theories, conventional theory is claimed to be covered through a large part of the existing litterature. Conventional theory has as its main argument that FDI is initiated as a response to the possession of one or more advantages. Moon & Roehl (2001) find that there is a variety of FDI activity that cannot be explained by such conventional theories. The authors suggest an imbalance theory, where firms enter markets without the ownership of advantages as predicted by existing theories. They do so to access resources necessary to restore the balance. Specifically, the authors identify two such cases which they label outside the scope of conventional theories: a) strategic investments, and b) investments from least developed countries (LDCs).

Strategic investments are not necessarily based on current advantages of the firm, and is initiated as a competitive response to secure future advantage. The second is investments made by LDCs into developed country (DC) markets. In the latter case, an advantage is seldom equal to the firms in the DC they compete however it is the lack of advantage that drives these investments. As China is not a LDC, consideration would be taken to explore if their strategy in Africa fits that of a strategic investments as described by Moon & Roehl (2001).

Kojima's macroeconomic FDI theory in the literature review can possibly seen as the theory that challenges the definition what is conventional. Kojima (1973) suggests that investement should flow from a relatively disadvantaged industry in the home market to an advantaged or potentially advantaged host nation, transferring knowledge and tecnology. The author states that ownership assets such as tecnological knowledge, machinery, and equipment is exchanged for the final products. However, it is not claimed that current ownership advantages are not present, but that resource endowments are scarce or not available in the source country. For that reason, I do not consider it contradictory to include a literature review that examines conventional theory.
2.2.1 The Product Cycle

The theory of the product cycle uses a micro economic theory to explain the macro-economic concept of FDI. The starting assumption is that entrepreneurs in industrialized countries must have access to scientific knowledge, but it is the application of knowledge in a specific way that leads to the innovative production. Furthermore, Vernon claims that each country’s entrepreneurs will know its market the best, and in the initial stage the competitive advantage lies at home. Secondly, he emphasizes that a country’s capability to innovate within industries of high-income and those that substitute capital for labor determines their trade position. Following this logic, Vernon builds on the concept of the product cycle and connects how involved a country is in foreign investment to where the product is in the cycle.

The introduction stage in the cycle involves production at home for a domestic market. The reasoning behind this according to Vernon is that inputs in the product might still be subject to change, and there is a need for ease of communication between different stakeholders in the value chain. The maturing stage is characterized by the need for flexibility declining. The cost of production and achieving economies of scale is given increased focus over distressing about product features. Demand for the product in its home market is likely to increase, and demand from other developed markets is likely to begin as well leading to exports activity. As an alternative, foreign production rather than exports is considered based on cost saving, imitation of the product in the foreign market, and restrictions on import place by foreign governments. The third phase is known as the standardized phase. Which translates into high capital intensity, and products needing less skilled labor. Cost reduction due to fear of imitation, and intensified competition are common in this stage. Production in a cost-saving location is a viable strategy at the stage. Shifting the balance of where the competitive advantage is now located, the innovating country will now become an importer of its own product.
The product cycle as a contemporary and general theory has received criticism. Including if the theory is capable to explain FDI activity other than that of US firms in the 1960s. Acknowledging the increased global scope of MNEs a decade later, Vernon revisited the concept of the product cycle. Stating that the theory has partly lost its descriptive value of explaining foreign activity of industrialized countries. However, he found that the theory is more suited to explain the foreign activity of developing countries. His arguments included that industrialized countries increasingly are becoming more similar in income, market size, and cost of production. Yet, there will be a gap in these factors compared to developing countries. When foreign activity takes place from an industrialized country to a less developed country, capabilities and innovations will transfer. This in turn leads to the less developed country initiating an own product cycle, undertaking FDI in other developing markets that lag behind in the ‘industrialized pecking order’ (Vernon, 1979).

2.2.2 Kojima’s Macroeconomic Theory of FDI

Kojima developed a trade oriented FDI theory that took a starting point in comparing the American economy to the Japanese economy, and more specifically their FDI decisions. Kojima put forward the idea that FDI should be carried out if investment flows from a comparatively disadvantageous industry in the investing country, to a comparatively advantageous industry in the host country transferring capital, technology, and knowledge. If FDI flows in this manner, Kojima argued that it would improve the industrial structure on both sides and facilitate trade.

Furthermore, he suggested that the American-type of FDI was anti-trade oriented because America would foreign produce in industries were the competitive advantage was at home. To explain the anti-trade oriented behavior of American FDI, Kojima used Hymer (1960, 1968) and Vernon (1966) theories as examples. Both Hymer and Vernon’s theories on FDI claim that the comparative advantage should be in the host country initially then transferred. Kojima on the other hand, meant that if FDI flows from an industry in which the comparative advantage is in the investing country it prevents upgrading of the industrial structure in both countries.
Kojima supported Japanese FDI as being trade-oriented or pro-trade because it took into consideration the industries were the country has lost comparative advantage. Japanese investment was concentrated towards natural resources, an industry which Japan was comparatively disadvantaged. Advocating for North-South trade, he highlights the efforts of Japan to invest in developing countries, including offering developing assistance for import. Developing assistance should be offered in those industries where Japan was losing its comparative advantage, but the developing country is gaining or is expected to gain. The industries chosen in the developing country should be export oriented, and not only serving the benefit of the investing country. To make cost similar, Kojima argued for a free trade policy stating that trade barriers such as tariffs should be liberalized. The limitations of the theory include the over focus on factor endowments in the FDI decision compared to other possible explanations such as product differentiation, or economies of scale (Dunning & Lundan, 2008).

2.2.3 The OLI Paradigm

The OLI paradigm is one of the most central theories of FDI and explaining the determinants of the internationalization process. Developed and empirically examined by John H. Dunning in his 1980 article” Towards an eclectic theory of international production”, the paradigm has been revisited and revised by himself and several other academics many times. The main propositions of the paradigm is that international production takes place because firms possess certain advantages. The eclectic paradigm explanation of firm’s foreign activities will depend on four conditions being satisfied (Dunning & Lundan, 2008).

1) Ownership (O) advantages: the ability to own distinctive and sustainable ownership advantages compared to firms of other nationalities in attending to a particular market, or group of markets.

2) Internalization (I) advantages: on the condition that the ownership advantages are fulfilled, the enterprises accesses whether it is beneficial to internalize capabilities rather than externalize to add value to the O advantages.
3) Location (L) advantages: If O and I advantages are fulfilled, the enterprise decides on whether it is in their best interest to utilizing their capabilities in a foreign location.

4) If the ownership, location, and internalization (OLI) advantages facing a particular firm are in place, the subsequent action is to evaluate if foreign production is consistent with the supporting institutions of the firms strategy and long-term objectives of stakeholders.

Ownership advantages are either tangible or intangible assets that are specific to the ownership of a firm, or the country in which it operates. There are three types of ownership-specific advantages. Asset specific advantages (Oa) which are property rights, and/or intangible assets. These include product innovation, noncodifiable knowledge, and production management. Transaction-cost minimizing advantages (Ot) which are advantages of common governance. These include obtaining inputs on favored terms, achieving productivity gains, and synergetic economies. Institutional assets (Oi) which are formal, and informal institutions that govern the value added activities within a firm and between the firm and its stakeholders. Such as norms, codes of conduct, and incentive systems.

Internalization advantages are related to the transaction cost theory by Williamson (1979), where the option of outsourcing value-adding activities versus completing them in-house is decided based on cost and ease of transaction. Without the advantages of internalization, much FDI would be replaced by international contracts between buyer and seller (Dunning, 1980). Location-specific advantages are such as resource endowments, institutional systems, transport costs, and cultural differences. These factors weigh the cost and difficulties of operating in a foreign country, and influence the decision of favoring the home or host country. The more immobile the locational advantages the firm needs are, the more likely it is that the firm will prefer FDI to exploit the ownership specific advantages.
Dunning has revisited the topic of the eclectic paradigm in numerous of his articles explaining in depth some of properties of the paradigm. Firstly, he states that the composition of the OLI paradigm is context specific. Meaning that home and host country economic and political features together with the industry entered will have an influence. Secondly, the three sub-paradigms are interrelated, and the focus is on the value of the whole being greater than the sum of parts. Thirdly, the paradigm is not prescriptive, but rather an explanation of how internalization is taking place. In addition, the OLI paradigm should not be viewed as being static, and any strategic action towards the current composition of OLI advantages can change them at later period.

In 1995, Dunning revisited the paradigm in light of changes due to the economic environment, and what he calls “alliance capitalism”. He found that the OLI advantages will be influenced by the relationship between firms, and that an individual firm is not necessarily the only source of its advantages but is influenced by the coalitions and cooperation’s it has entered into. Lastly, Dunning (2001) emphasizes that there exists many theories of FDI and MNE activity, and these explanations should be viewed as complementary rather than substitutes, thereof the alternative name the eclectic paradigm.

2.2.4 Investment Development Path (IDP)

The IDP theory was developed by Dunning (1981) as a dynamic view within the OLI paradigm. The connection with the OLI paradigm is that IDP analyzes changes in FDI patterns in connection with changes of the OLI advantages of both domestic, and foreign firms (Narula & Guimón, 2010). The theory describes five different stages in a country’s economic development, and how the stages relate to net foreign investment activity. Dunning and Narula introduced the fifth stage of the IDP in 1996 (Dunning & Lundan, 2008) As a country develops, the composition of the OLI advantages of the domestic firms investing overseas and foreign firms investing in that country changes. Through the IDP, it is possible to identify the determinants of change as well as its effect on the development. The conclusion put forward by IDP is that Gross National Product (GNP) per capita, and a country’s international investment position are correlated.
Furthermore, Dunning (1981) found that although the four stage grouping of countries was suggested to build on the properties of the OLI sub paradigms, deviations from the average existed due to specific country distinctions. Dunning (1986) shifted the focus to developing countries and their pattern to initiate in outward FDI. The arguments presented in this article were threefold. As a country develops, its investment activities change and it moves from being the receiver of inward FDI to initiating outward FDI. Secondly, the correlation between outward FDI and development of a country will depend on its own resources, economic, and political system. In addition, the country’s cultural, economic and political relations with other countries. Lastly, the distribution of outward FDI between industries will be dependent on the characteristics identified in the second argument.

Figure 2.1 is added to follow the explanation of the five stages visually. The line net outward investment (NOI) represents the difference between outward, and inward direct investment stock. GNP is increasing horizontally. The first stage of the IDP model a country’s outward, and inward FDI is likely to be minor. Several of the countries in this stage are the least developed countries; capital and technology inflow is limited and may take the form of aid for infrastructure. The ownership of natural resources is it main source of competitive advantage. Ownership and location advantages are absent commonly because of imperfect domestic market with shortage in infrastructure, inexperienced labor force, and underdeveloped or non-existent institutions (Narula & Guimón, 2010). In the second stage of the IDP, there is an increase in L advantages. The country becomes more attractive to MNEs, and inward FDI (IFDI) grows substantially. The net position (NOI) is however, still negative because the O advantages of the domestic firms are lacking resulting in limited outward FDI (OFDI). The focus on developing institutions is given additional attention at this stage.
In the third stage, countries will move towards being industrialized and focus shifts from growth based on investment to innovation. Domestic firms begin to create their O advantages. The government plays a key role in encouraging education and innovation at this stage. The increased O advantages firstly leads to exports, secondly to OFDI as sales in foreign locations increase, or the cost of home production rises (Dunning & Lundan, 2008). Outward FDI increases steadily, and inward FDI tends to slow down due to the competitive pressure it provides on in domestic firms. In sectors where the country has lost its comparative advantage, inward FDI is still needed. At stage four, the net position becomes positive as outward investment passes inward investment. In some industries, the O advantages of domestic firms begin to resemble those of developed countries. The stage is characterized by economies reaching a post-industrial stage of development. Efficiency of macro-institutional and macroeconomic systems is a source of comparative advantage. The fifth stage is characterized by countries receiving roughly the same amounts of inward and outward FDI. NOI tends to move fluctuate around zero, and these economies are most developed.

Figure 2.1. Graphical Representation of the Investment Development Path (not drawn to scale; for illustrative purpose only). Source: (Narula & Dunning, 2010, p. 265)
2.2.5 The Uppsala Internationalization Theory

The Uppsala internationalization theory is a behavioral and evolutionary theory that mainly explains two patterns in the internationalization process. Firstly, the researchers at the University of Uppsala found that firms seem to follow sequential steps in their internationalization process. Four different modes of entering a foreign market were identified; reaching a higher stage represents increased market commitment.

Stage 1: No export activity or infrequent export

Stage 2: Export via agent

Stage 3: Establishing a foreign sales subsidiary

Stage 4: Production in host country

Increased commitment to internationalization is a result of organizational knowledge about a foreign market gained through direct experience. A firm gains direct experience solely through operating in a foreign location. The theory predicts that a lack of direct experience will act as an obstacle to international operations. Inspired by Penrose (1995), the researchers classify knowledge about a market into objective knowledge and experiential knowledge. Claiming that objective knowledge only creates theoretical opportunities. Experiential knowledge on the other hand, allows for a concrete identification of opportunities and their fit with the activities of the firm. Increasing foreign commitment through knowledge of the market is shown in Figure 2.2. The model shows four concepts of internationalization divided into state and change aspects. The model is developed to be dynamic; the output of one concept influences the next. The state aspects affect the decision of whether, and in which way the change aspect will occur. In the same manner, the state aspects will be affected by the outcome of the change aspects.
The researchers do not see internationalization as a conscious strategy for optimum allocation of resources, but instead a process of adjustment to the changing conditions of the firm and its environment. Where investing more resources in a market is a function of market knowledge. The second pattern they found in the internationalization process is an effect of the concept ‘Psychic Distance’. “Psychic distance can be defined as the factors preventing or disturbing firms learning about and understanding about a foreign environment” (Dunning & Lundan, 2008, p. 92). Examples include business practices, culture, industrial development and language. Johanson & Vahlne (1977) found that in the early internationalization process geographical proximity is of importance because of lower perceived market uncertainty. The researchers identified dissimilarities in language and culture as important obstacles. Although the original research was conducted on an essentially homogenous group of Swedish manufacturing firms, other empirical studies have found support of the hypothesis (Dunning & Lundan, 2008).
In 2009, the model was revisited by the researchers in the article “The Uppsala internationalization process model revisited: From liability of foreignness to liability of outsidership” now with a focus on business networks. Acknowledging a changed economic and regulatory environment, the authors emphasized that learning and commitment could take place in relationships. The term ‘Liability of Foreignness’ is complications of internationalization resulting from being outside of a business network. The stages of the establishment chain was reconfirmed in the revised version however, with some modifications. The correlation between order of market entry mode and psychic distance was found to have weakened, and the focus was shifted to the relationship between business networks and psychic distance. If an international business network is established, that might reduce perceived psychic distance, which in turn means that the order of entry mode might not follow the original 1977 research. The classification of knowledge into objective, and experiential knowledge was also extended to include relationship-specific knowledge. Relationship-specific knowledge is knowledge about each other’s heterogeneous resources and capabilities, and is a result of the interaction between two parties.

2.3 FDI Motives

The problem statement refers to identifying China’s motives for investing in Africa. To identify the reasons for undertaking FDI, Dunning & Lundan(2008) build on a taxonomy used by Behrman (1972). The taxonomy distinguishes between four types of FDI flows.

1) Natural Resource Seekers

The drivers for investing abroad for natural resource seekers is taking advantage of the availability of acquiring resources at lower cost, obtaining a specific resource that might not be available in the home country, or that might be of higher quality if produced in the host country. Furthermore, the motivation of the firm is increasing its competitiveness or creating a more profitable firm. Resource seekers can be divided into three main groups. The first group is primary producers and manufacturing enterprises. This type of investment is usually location bound once investment is placed, and requires significant capital expenditure.
These firms seek resources that require complementary skills and markets that the firm is competent to serve. Resource-seeking investment of this type by Chinese investors in Africa has been noticeable in recent years (Dunning & Lundan, 2008). The second group is manufacturing and service MNEs with high labor cost, which undertake FDI to search for lower labor costs. Free trade or export processing zones are commonly set up to attract this kind. The type of labor that these MNEs seek is unskilled, or semi-skilled labor to supply labor-intensive intermediate or final products for export. The third group consists firms acquiring to fulfill needs such as capabilities and skills.

2) Market Seekers
Market seekers invest in a specific host country that in most cases might have been served through exports but wishes to be closer to its market, potentially because of increases in tariffs, or trade barriers imposed. Proximity to the market, protecting existing market, or size of the market possibly also increases the motives for local production. Dunning & Lundan (2008) identify four main reasons for market seekers to initiate FDI; 1)Following main suppliers or customers to retain their business. 2) Adapting to the host country’s taste and local resources and capabilities. 3) Costs of supplying product from a distance is higher than local production. 4) Strategic reasons to stay competitive.

3) Efficiency Seekers
There are two main kinds of efficiency-seeking FDI; 1) Taking advantage of relative cost and difference in factor endowment in different countries. 2) Reaping the benefits of differences in consumer tastes, supply competencies, and of economies of scale and scope in countries with similar economic structures and income levels. Cross border markets must be both well developed, and open for efficiency-seeking foreign production to occur. Efficiency motives frequently occurs following resource and market seeking investments.
4. Strategic Asset Seekers

Strategic assets seekers acquire assets of foreign corporations to enhance the acquiring firm’s human capital, and physical asset to stay or increase competitiveness. The goal is owning and utilizing the benefits of similar activities, or diversified capabilities through common governance in diverse economic and potential environments. The majority of strategic investment are initiated on the expectation that it will bring additional benefits to the organization.

A firm’s motive for investing abroad might change because of completing the establishment phase and experience. Initially most firms will be resource seekers, or will be driven by retaining or gaining new markets. When firms becomes more multinational, concerns of raising efficiency and gaining new sources of competitive advantage shift to be the primary motives. Dunning (1988) provided an extension of the original OLI paradigm connecting it to the framework of the three motives of foreign production. The category of strategic asset seeking was first introduced a few years later. Appendix 1: Types of international production adapted from Dunning & Lundan (2008) includes the four categories of motives and explains their linkage in connection with the OLI advantages. The ownership advantages are almost synonymous with motivation as they answer the question of why foreign production takes place. The locational advantages answer the question of where these ownership advantages are found. Internalization is by what means, or how the objective is being pursued to reduce uncertainty and limit transaction cost. Depending on the motive of foreign production, existing ownership advantages, the gains of the location, and reasons for internalization vary.
3. China's Outward FDI

China has gone through three significant transformations in the past century (Redding & Witt, 2010). The first period is from 1911 when the Manchu dynasty was overthrown, which led to decades of civil war. The second period started in 1949 with the communist revolution associated with Mao Zedong. The communist revolution led to the world’s largest collectivized state. The third period was initiated by Deng Xiaoping, the de facto leader of China in 1978 and began a fundamental shift in ideas of profit. By liberalizing the Chinese economy, a change in economic ideology was born. One that moved from protectionism and self-dependence to an aspiration for integration into the world economy.

Special economic zones (SEZs) was an initiative by the Chinese government to promote FDI and trade. The first SEZs in China was introduced in 1979. The purpose of SEZs was to encourage economic development utilizing resources that might be specific to that province, or testing international ideas and concepts before they were brought into the rest of the country. As a strategy to attract FDI, SEZs put in place tax and tariff reductions, flexible labor conditions, and preferential fees for property. The flexible conditions of the zones meant less risk and uncertainty to foreign investors in the influences from currency concerns and patent protection. SEZs have made a substantial contribution to China’s development through knowledge, technology, and skills spillovers (Zhihua Zeng, 2010).

China is today in a place where the country’s economy has gradually opened up, and a great deal of influences have been brought in since 1978. Redding & Witt (2010) among others identify acquiring technological capabilities, importing institutional structure, and FDI. China has developed in a path that is different from Western liberal market economies, and would run into obstacles in trying to imitate these markets. The radical change from a coordinated market would have to take the form of one that does not abandon culture. For that reason, China has developed business systems that is different from what is seen in many economies, one that is largely shaped by its culture, history and its institutional environment.
3.1 Changes in Policy and its Effect on FDI

Chinese business history led to changes in policy made by the state, which shaped the development and magnitude of FDI to a large extent. Buckley, et al. (2007) found five key stages in the development of Chinese outward foreign investment policy.

Characterized by the open door policy launched in 1978 by Deng Xiaoping. The intention was to integrate China in the world economy. Initially, it was predominantly only allowed for firms approved for state-owned trading corporations by China’s Ministry of Foreign Economy Relations and Trade (MOFERT) to invest abroad.

Because of government encouragement to liberalizing restrictive policies, additional corporations are allowed to establish foreign affiliates. Under the preconditions of necessary capital, technological and operational capabilities, and a suitable joint venture partner.

Internationalization is incorporated into the national economic development policy. The approval process was tighten because of the concerns of loss of control over state assets. Simultaneously, authorities promote international business activities especially to specific sectors in nearby locations such as Hong Kong.

Stage 4: “Implementation of the 'go global' policy” (1999-2001)
In 2001, China launched a ‘go global’ strategy as a part of its 10th five-year plan (2001-2005). Contradicting policies of regularization, and encouragement characterize this period. Restrictions were put in place to secure investment in genuinely productive purposes. However, investment in specific sectors such as exports of raw materials, machinery parts, and light industry was encouraged through reduction in export tax, financial support and foreign exchange assistance.
Stage 5: Post-WTO period (2001- )

In 2001, China joined the World Trade Organization (WTO). This meant for China that the country had to comply with the rules of the WTO both related to transparency, and opening up markets to foreign competitors.

Figures 3.1 and 3.2 show the evolution of China's FDI. See Appendix 2. for a table of yearly outflow, and Appendix 3. for the accumulated OFDI stock. Figure 3.1 shows that OFDI began to accelerate in 2001, from $ 915 million in 2000 to $6.8 billion in 2001. The immediate growth is the result of the intervention from the government to secure China’s growth in the future by encouraging the economy to ‘go global’. However, in the consequent years OFDI investment slowed done only to rise again in 2005 where in have keept on increasing until 2010 when it reached $ 68.8 billion.

Figure 3.1: OFDI Flow from China 1982-2010. Source: UNCTADstat (2013)
Figure 3.2 illustrates that IFDI to China began to accelerate prior to OFDI. In the 1980s when the first SEZs were launch, IFDI began to develop. By 1984, IFDI had reached $1 billion. In one year from 1991 to 1992, IFDI more than doubled from 4.3 billion to 11 billion in 1992. Following China’s entry to WTO in 2001, IFDI increased steadily until 2008. Because of the financial crisis, IFDI decreased from a $108 billion in 2008 to $95 billion in 2009. In 2010, IFDI flow picked up again and reached 114 billion.

![IFDI to China Flow 1970-2010](image)

**Figure 3.2: IFDI Flow to China 1970-2010.** Source: UNCTADstat (2013)

In relation to the IDP model, the beginning of the 1980s shows the first stage. Both OFDI and IFDI was in a development phase. In accordance with theory, China was in the process of opening up to internationalization and capital and technology was still limited. In the 1990s, China reached the second stage of the IDP. The dominant position of China was as net receiver of FDI, and OFDI was still limited. During the 2000s, increased attention was given to OFDI with the government taking an active role encouraging firms to ‘go global’, which characterizes the third stage in the model. In addition, IFDI has slowed down. Amounts of IFDI are still higher; however, the growth rate of OFDI has surpassed that of IFDI since 2001. The net position of FDI as of 2010 is still negative indicating that the fourth stage has yet to be reached.
3.2 Geographical and Sectoral Distribution of Chinese OFDI

The largest share of accumulated FDI flow in 2010 went to Asia, and amounted to $44.8 billion. When analyzing yearly FDI flow from 2003-2010, it is visibly that this pattern has been consistent with exception of the years 2005 and 2006. In 2005 and 2006, FDI flow to Latin America was higher (see appendix 4). Latin-America received $ 10.5 billion in 2010. Davis (2012) suggests a possible explanation for the sudden increase in flow to Latin America. 92 percent of the share of OFDI to Latin America goes to the Cayman Islands and British Virgin Islands. Two countries that are known for being tax havens. Following Asia and Latin-America, Europe was the third largest recipient with $ 6.7 billion in 2010. North-America received the fourth highest FDI flow of $2.6 billion. Africa received $2.1 billion. Lastly, Oceania received $ 1.8 billion in 2010.

When looking at the OFDI flow from 2004-2010 it is visible that there has been a change in the industries most invested in, see Appendix 5. An identified trend for the last three consecutive years is that the leasing and business services industry has received the largest stake of investment. Leasing and business services contains support functions such as information, and communication technology. Davies(2012) suggest that the figures for leasing and business services might be misleading, and are ultimatly target at manufacturing. His argument is that the industry does not seem consistent with the industries of the Chinese firms that invest overseas. When observing 2010 solely, the banking industry with a total of $8.6 billion is the second most popular industry. Wholesale and retail industry with $6. 7 billion follows in third place. When observing the OFDI stock in 2010, the picture is somewhat different, see Appendix 6. The leasing and business services has an accumulated flow of almost double the second place, which is banking. Different from the statistics on OFDI flow, mining had the third largest stock in 2010. One possible reason why mining is more visible in stock data then flow data is that FDI flow shows a static picture of investment activity within a year. While investment activities in natural resources tend to be large and can be carried out for more than one year this might result in data on FDI flow to be less well-informed than stock.
3.3 Investing Actors

There are two investing actors in China that primarily engage in OFDI activity, state-owned enterprises (SOEs) and private enterprises. In 2003, the state-owned asset supervision and administration commission (SASAC) was established. SASAC manages the assets of the state by performing the responsibilities of investors. These assets include companies that deem strategic to be under the ownership of the state. Currently, 117 companies are recorded as central SOEs under the management of SASAC including firms in the sectors of petroleum, shipping, and telecommunications. Chinese OFDI is dominated by SOEs according to Chinese official figures. The 2010 statistical bulletin from MOFCOM shows that the majority of the top 50 non-financial transnational corporations ranked by FDI asset, stock, and revenues are indeed state-owned or partly state-owned enterprises. See Appendix 7 for the top 10 companies.

There exists some criticism whether the regulation for SOEs to invest overseas is more lenient than that for private firms. With economic and political interest being so closely interlinked there is also the issue of preferential treatment for SOEs, allowing them to be the frontrunners in OFDI by fulfilling national interest. SASAC has set an approval process on OFDI from all state-owned enterprises. Some decentralization of power exists regarding approval of OFDI for private entities, allowing local provincial governments to approve investment. Luo, et al. (2010) claims it demands no more than 15 working days for both private and state-owned businesses. While Voss, et al. (2008) suggest a restrictive approval process for private firms. Their argument is that the business environment in China were well established relations of high importance discourages private firms to perform FDI. Alon (2010) examined how the institutional environment of China triggers OFDI from state and private sector separately. He found that private companies when engaging in OFDI seek open economies where they can offset the institutional disadvantage of the home market and, rely in these markets on networks as a substitute for government support. While the state sector utilizes what he calls institution specific advantages, including regulatory, financial and ownership factors which results in state sector investments being of a more costly and complex nature.
3.4 The Influence of Institutions on Investment

The role of institutions and its effect on FDI has received increased attention in the last decade or so. Whether home country institutions and regulatory framework are developed or not affects strongly on OFDI from a developing country (Voss, et al., 2008). The definition of institutions is “institutions are the rules of the game in a society or, more formally, the humanly devised constraints that structure human interaction” (Mantzavinos, et al., 2004, p. 77). Institutions can be referring to formal institutions such as constitutions, law and regulation, or otherwise informal institutions such as conventions, moral rules and social norms. Institutions facilitate in easing or complicating market transactions or put differently, institutions can decrease or increase transaction costs.

An inherent characteristic of many emerging markets is the shortage or unavailability of formal institutions (Khanna, 2010). According to the World Bank, an emerging economy is one that has an average per capita income of less than $9000, and simultaneously experiencing rapid growth and economic transformation (Enderwick, 2007). China’s gross national income per capita in 2011 was $4,940 (World Bank, 2012). China as an emerging market inevitable possesses some institutional flaws, or as Khanna(2010) labels it ‘institutional voids’. These institutional voids create a gap in the intermediaries available in easing market transations. Khanna (2010) suggests an alternative definition of emerging markets “...emerging markets as those where these specialized intermediaries are absent or poorly functioning” (Khanna, 2010, p. 24).

Formal institutions are present in a market to support and enforce rules for interaction. In the case of China, few independent formal institutions exist, but state-owned institutions are present to a large extent. Market institutions are absent because of political properties. When the entities that are governing and facilitating the market are also have a large strategic interest in performing profitable investments, this creates a conflict of interest or a competition for resources. SOEs play a key role as investing companies initiating FDI and simultaneously being controlled by SASAC. Institutions that are relevant in foreign investment are suspected to be present to give SOEs support or, give them an advantage over private firms.
The Economist (2011) reports that ‘the government quietly obstruct market forces’, ‘enforces rules selectively to keep private-sectors rivals in their place’, and ‘state firms such as China Telecom can dominate local markets without running afoul of antitrust authorities’. The article suggests that some of the economic coordination needed in institutions is established in the political arena instead of independent institutions. The state in China has actively been involved in taking on the role of market institutions. The government has to a large extent in history been solely responsible governing the magnitude, and ease of with business transactions are conducted. Even though the Chinese market possess some of traits of a market economy, its full emergence to a market economy is not yet realized. In many ways, it still possess the characteristics of a coordinated market run by political actors. The absence of market institutions allows this political coordination to exist. This is visible through the policy framework that had to be in place before OFDI accelerated, but also the presence of actors on the market such as SASAC.

Changes in formal institutions led to changes in policy, but the outcome is a result of changes in both formal and informal rules (Mantzavinos, et al., 2004). The role of informal institutions play an important role in China. Geert Hofstede, a Dutch academic performed a study on IBM (International Business Machines) employees in 40 different countries, later extended to 50 countries between the years 1967 and 1973. The study is has been extensively cited in academic literature, yet it has received much criticism. Because all respondents of the study worked for the same firm, some critics claim that it generalizes by assuming homogenous behavior of a whole nation. Nevertheless, more arguments that are favorable supporting Hofstede’s work exist that criticism (Jones, 2007). Measuring culture on five dimensions, Hofstede found that China is a highly collectivistic country in contrast to many western societies, which were found to be individualistic societies. Collectivism is defined as “…a society in which people from birth onwards are integrated into strong, cohesive in-groups, which throughout their lifetime continue to protect them, in exchange for unquestioning loyalty” (Hofstede, 2007 , p. 417).
Collectivism is visible in the Chinese business culture through the importance of ‘Guanxi’ and social capital, that both are forms of informal institutions since they are social norms. ‘Guanxi’ has been attempted to be translated into English as relationships, connections, and networks. Often business in China is not conducted with strangers, one has to be a part of an inner circle and a relationship can take substantial time to cultivate. Redding&Witt (2010) identify two major forms of social capital: the first is the personal form, which is between individuals based on reciprocity and obligation; the other is the institutional form, based on a system of stable order such as law, high quality information, professional standards and bureaucracy. The authors argue that the institutional form is hardly present in China, and personal form is of higher importance. Informal institutions can act as substitutes, or complements to formal institutions. Boisot & Child (1996) examined the substitution of the personal form of social capital versus the institutional form in China. The researchers found that information in China is shared in informal relationships, which develop legitimacy from embedded social practices rather that formalized systems. This has resulted in ‘network capitalism’ as an alternative form of to market capitalism, were trust and interpersonal accommodation are key characteristics.

The importance of networking as an institutionalized practice has historical roots, and is widely practiced in China. In situations where there is an unavailability of codification and diffusion of information, there is less dependence of formal institutions and more dependence on informal institutions like network. Codification refers to how information systematized, and if information is comprehensible. Diffusion relates to whether information is shared without difficulty in a society. The Western path to modernization in contrast, developed towards bureaucracies as information became more codified and diffused. Subsequently, leading to the creation of institutions and market capitalism. A common empirical finding in locational choices of countries that undertake FDI show that institutional development has a positive effect on inward FDI. Globerman & Shapiro (2002) found that good governance hereunder open transparent legal and regulatory regime, and policies promoting domestic and international competition increases FDI inflows. Bénassy-Quéré, et al., (2007) found that the quality of institutions have a significant effect on FDI inflow particularly identifying bureaucracy and corruption.
4. The China-Africa Relationship

China’s involvement in Africa dates back to as far as 618 A.D (Ncube & Fairbanks, 2012). The historical presence of China in Africa can be divided into three periods. The period up to 1949 where the relationship consisted of trade of goods and slaves, labeled the ‘episodic’ phase. The second phase begun in 1960 and lasted until 1989. This period was considered the “symbolic” phase, and was characterized by open conflict and competition with the West and Soviet Union and the beginning of the Cultural Revolution. The third period is labeled the “symbiotic” phase begun in 1990 and is ongoing to the present. Key characteristics of this phase is the modernization of the People's Liberation Army, development of the "Socialist Market Economy” and the restructuring of state-owned Enterprises.

4.1 The Development Path of China’s OFDI to Africa

To understand the presence of China in Africa today, it is valuable to go back to the ideological phase because this is the era where the much emphasized motto of the present ‘mutual benefit’ was born. Led by Mao Zedong, China was socialist country from 1949. When colonialism began to come to end in Africa, China offered assistance to take a stand against imperialism and support African countries in functioning as independent nations. In an era when the West and Soviet Union were seen as enemies of China, Africa was viewed as a possible ally. The cooperation between the two was entered into based on shared ideological beliefs in socialism. China’s interest in this period was primarily development aid, infrastructure, and political interest. Following their shared ideological beliefs, Africa was to an extent inspired by China’s attempt to transform out of poverty and tried to emulate a Chinese model of development. An example of this was collective farming in the agricultural sector. The political interest included China only keeping diplomatic ties and granting development aid with African nations that supported the One-China policy, and did not acknowledge Taiwan as an independent country.
Based on ideology, one of China’s first investment in Africa was initiated only this time around the intention served were also economic in addition to political. Between 1970 and 1975, Tanzania-Zambia railway (TAZARA) railway project came to life. The railway connected landlocked Zambia to Tanzania’s ports. Funding was first sought from the World Bank who rejected the proposal, because it was considered unprofitable based on the trade benefits of the project not justifying the costs. Still, China took on this investment and funded the TAZARA railway with a 30-year interest free loan of close to $400 million. The TAZARA railway is symbolic for the FDI that was to come from China in the future, not always profitable in the eyes of other investing actors, but one of several components in China’s Africa strategy.

In the 21st century, China’s involvement in Africa has been more commercial in nature but the characteristics of the ideological phase remain including soft loans and non-interference in Africa’s self-autonomy. A turning point in serving the growing commercial interest of China came in 2000, when the Forum on China-Africa Cooperation (FOFAC) was established. The first conference held in Beijing, gathered more than 80 ministers from China and 44 from African countries to discuss the direction of economic cooperation including bilateral trade. The aim of the FOFAC was to encourage long-term partnership though mutual benefit and equality. “In 2000, China was starting to harvest the fruits of nearly two decades of reform in its aid and economic relations with Africa” (Brautigam, 2009, p. 77).
Following the ‘go global’ policy of 2001, China OFDI in Africa has grown at a high rate. Figure 4.1 shows that in 2003 China’s OFDI flow to Africa was $74.8 million; by 2004, the value was more than four times as much. It has kept on accelerating rapidly with reaching its peak in 2008, and declining in 2009 due to the financial crisis (FOFAC, 2011). In 2006, during the third ministerial conference of FOFAC president Hu Jintao of China announced an action plan for China’s Africa policy from 2007-2009, possibly explaining the 2008 peak.

In the economic field, the action plan assurance:

- Facilitate and balance bilateral trade by duty free trade with least developed African nations.
- Encourage investments from Chinese enterprises to Africa by providing preferential loans and buyer credits.
- Promote, increase and facilitate cooperation in the fields of agriculture, Infrastructure and resource extraction.
- Debt reduction and relief.
- Economic assistance with no political strings attached.

![China's OFDI Flow to Africa 2003-2010](image)

**Figure 4.1: China’s OFDI Flow to Africa 2003-2010.** Source: MOFCOM (2009, 2010)
A FOFAC initiative that has seen results is the increase in bilateral trade. By 2009, China was Africa’s largest trading partner (OECD, 2011). Figure 4.2 shows the progress of trade patterns. Offering similar insight as OFDI figures, there has been a significant increase of bilateral trade until 2008 when there was a decrease in 2009 due to the economic recession. The balance of trade between the two has been alternating however, China has been running trade deficit since 2005. Although being of similar size, the trend indicates that the need from imports from Africa has been greater than the demand for exports the last couple of years. China-Africa Trade and Economic Relationship Annual Report 2010 issued by FOFAC highlights the bilateral trade relationship of China and Africa through the decades. The main patterns of trade in the 21st century include imports to China from Africa being predominantly in the primary sector. Energy and mineral products are the main imports, oil imports has also increased accounting for 13 percent of Africa’s oil export. China’s main exports to Africa are mechanic and electronic products accounting for over 50 percent of the total exports to Africa in 2010.

![Bilateral Trade China-Africa](image)

**Figure 4.2: Bilateral Trade China-Africa.** Source: International Monetary Fund Direction of Trade Statistics (2013)
4.2 Chinese Investing Actors in Africa

Over the last decade, the structure of the majority of projects initiated by Chinese government enterprises (SOEs) and private enterprises in Africa has shifted. Prior to the year 2000, there were no private enterprises reporting OFDI to Africa (Shen, 2013). In 2002, the figure increased to 2 out of 18 active projects. In 2005, private projects saw a large increase to 52 projects amounting to 35 percent of the total OFDI. In 2012, this figure was 923 projects, which equaled 55 percent of the active OFDI projects from China to Africa surpassing SOE investments. Figure 4.3 below compares active Chinese government-led projects in Africa to private-led projects by the end of 2011. Active being the key word, an assumption made when using the late 2011 data on investment is that the investments were conducted over a time period overlapping with the focus timeframe. What is evident from this figure is that the two actors tend to invest in different industries. SOEs predominantly invest in the primary sector and secondary sector, including resource extraction and construction in Africa. Private enterprises invest in the tertiary and secondary sector, including services and manufacturing.

![Figure 4.3: Comparing Active Chinese Government-led Projects in Africa to Private-led Projects](image)

Source: (Shen, 2013, p. 4) calculated based on figures from MOFCOM
The motives of OFDI from SOEs and private investors contrast. The strategic needs of SOEs are primarily in securing the both present and future need for energy, and other raw material. Private firms on the other hand, are securing their competitiveness to survive. Shen(2013) investegated the motives of a sample of private enterprises operating in Africa and found these belong to mature industries escaping the domestic enviornment to secure growth and survival. Brautigam(2009) agrees with this view and claims that the Chinese state is encouraging the move of the low-end manufacturing industry. The author specifically point to the China- Africa Development Fund(CAD) initiated at the FOFAC Summit in 2006. The equity fund is expected to provide $5 billion in economic support for Chinese ventures in Africa, and intends to fullfill the purpose of facilitating the move of mature industries.

4.3 Regional Distribution
Table 4.1 shows the top recipients of Chinese OFDI in Africa from 2003-2010. Consistent with trade patterns, and sectoral distribution is the interest in nations that are rich in natural resources. Sub-Saharan Africa points to being of higher importance than North Africa. A trend that separates China from other investing nations, as North-Africa is the most popular destination for FDI flows in Africa from 2004-2008 and again in 2010 (OECD, 2011). In connection to Dunning’s taxonomy of FDI motives, academics seem to be undecided between classifying China’s motives in Africa. The majority of literature points to the resource-seeking motive to dominate. In accordance with theory, obtaining a specific resource that is not available at home is a characteristic of resource-seeking FDI. What is certain is that China has a challenge of securing outside sources of energy because demand has outgrown supply. China went from a net exporter of petroleum to a net importer in 1993. Supporting the necessity to secure sources of energy is the figures on OFDI. Mineral and hydrocarbon rich countries accounted for 76% of Chinese OFDI in Africa by 2009 (OECD, 2011). Among academics that have found support for the dominate motive being securing natural resources are Alden & Martyn(2006), Adisu, et al. (2010), and Koldstad & Wiig (2011).
Table 4.1. Top Five Recipients of Chinese OFDI to Africa 2003-2010 (all figures are in US mill)

<table>
<thead>
<tr>
<th>Rank</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
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Distinctive in China’s resource involvement in Africa, and contributing to the increased focus on natural resources is accepting resources as a guarantee for payment. Resource-backed credit lines involve a country using its natural resources to guarantee a loan that can be intended most commonly for infrastructure. Resource-backed credit highlights that resource security is an important consideration for China (Carike, et al., 2012). Cheung, et al. (2012) found the resource-seeking motive to be present in the dataset from 2000s, and drew the conclusion that it is most likely in connection with the ‘go global’ policy. Furthermore the study found support for market seeking motives by using the variable Gross domestic product(GDP). Both the current GDP, and the real growth rate of GDP affected the destination for Chinese OFDI in Africa. Market-seeking motive seems to be connected to this case through Africa being a large market that is relatively untapped offering a strategic location for growth. Carike, et al. (2012) found similar results. The variable oil was found significant on the determinant of Chinese OFDI in Africa. However, market size seem to also be important as the top ten largest economies in Africa receive more OFDI than smaller economies.
Less attention has been given to the possibility the efficiency-seeking motive. Efficiency-seeking investments are performed to take advantage of relative cost differences in factors of production. The efficiency-seeking motive commonly occurs subsequent resource and market-seeking motive. As wage rates are increasing in China together with focus shifting to higher-value goods, a new market for low-skilled manufacturing might be pursued. OECD(2008) found that efficiency-seeking motive is present for China’s manufacturing enterprises investing in developing countries. The report finds that with industrial upgrading, low-tech and labor-intense manufacturing will be moved abroad. The current wave of Chinese firms relocating to Africa are labor-intens and of relatively low technology (Shen, 2013). However, there exists contradictions that this is is related to the search of cost differences in Africa. The first is that average labor productivity in Africa is lower than workers in China, Vietnam, or in other Asian countries(Brautigam, 2009). The second is that although there exists exceptions, labor costs in Africa is similar to Chinese labor cost (Bräutigam, 2008). Therefore, the efficiency-seeking motive does not directly apply to this case.

The strategic asset-seeking FDI motive is neither relevant for this case. The reasoning behind the realization, is that the motive involves seeking outside assets and competences of higher value in operations to stay or increase competitiveness. Strategic asset seeking does not occur very often for emerging economies, and when it does it is targeted towards the developed markets, where possibilities of acquiring innovative knowledge and improving technology exists.
4.4 Policies Encouraging Investment to Africa

Following the establishment of FOFAC, a number of initiatives have been put into place to encourage and simultaneously facilitate Chinese enterprise move into Africa. SEZs have been put in place to ease the obstacles and lower the costs of doing business. In 2006, at the third FOFAC conference China committed to establish three to five SEZs in Africa. The intentions of the zones were twofold. The first is, contributing to relocating labor intense mature industries abroad. The second is, that they were intended to fulfill political goals such as demonstrating and sharing the efficiency of the Chinese model (Bräutigam & Xiaoyang, 2011). More than ten African governments showed interest in hosting zones. By 2010, six zones were under development in Africa and a seventh was scheduled, see Appendix 8.

There was three parties collaborating on the zones, the Chinese government, African governments, and Chinese developers. However, the roles taken were different. Chinese developers took the lead. The African governments provided ideas for the activity taken place in the zones, and in some instances partnered with the Chinese firms on development. The Chinese government provided assistance in terms of material, network support, and promoting zones to companies planning to invest in Africa. Also, the state offered reimbursement of up to 30 percent of the the development costs, and several subsidies including tax rebates on imports and exports all depending on performance. The motives of the zones is primarily utilizing the zones to enter new markets, and expanding processing capacity of natural resources. Six of seven zones are focused on manufacturing with the exception of one zone that concentrates on mineal processing. Bräutigam & Xiaoyang (2011) claim that this provides evidence that China’s involvement in Africa goes beyond natural resource extraction.
CAD is a second initiative brought up at the FOFAC meeting in 2006. The Chinese government allocated $5 billion to support the establishment of Chinese business ventures in Africa. By the end of 2009, $700 million was assigned to over 30 projects in various areas including agriculture, manufacturing, and mining (FOFAC, 2011). The purpose of the fund is to encourage joint projects between state-owned or private Chinese firms, and African companies. The fund operates strictly on common project criteria’s, the goal being to earn a return and not incur losses. The investment horizon of CAD is longer than most equity funds ranging from five to eight years, but also longer if necessary. Serving the purpose of a private equity fund, it allows risk to be shared among several investors. A trait that is important for Chinese companies as they are not either familiar with the African market, or have much experience in risk management (Brautigam, 2009). More recently, the fund has granted funding to proposals by African entrepreneurs without Chinese participation.

Belonging to a group of more informal initiatives are business networks. Business networks have also played a role in facilitating the ease of conducting business in Africa for Chinese investors. In accordance with the predictions of the revisited Uppsala model, the correlation between business networks and perceived psychic distance appears to be stronger than market entry mode. Song (2011) identified two patterns among private Chinese firm’s overseas investment in Africa. Ethnic Chinese networks assist in information sharing of possible investment opportunities overseas. In addition, the networks share information of the possible operational risks of conducting business overseas. The role of the networks are stronger in a location such as Africa because it is a market that is far in terms of psychic distance, and before entry unknown territory to many Chinese firms. Business networks is primarily a phenomenon for private enterprises, as these firms do not have as strong government ties as SOEs.
Chinese business networks present in Africa can be divided into three groups (Song, 2011). The first group were businesspersons that came from Taiwan and Hong Kong in 1950s and 1960s. This group is mainly engaged in the textile and ceramic industry. The second group came from 1960s to the end of the 1990s. There was mainly two activities taken place at this time. The first was government aid and infrastructure projects. The second was state-owned trading companies. The communities from this period consist of remaining workers from the aid and infrastructure projects, and sales personal from state-owned trading companies. The experience workers had from SOEs was a great help to later established businesses in Africa. The third group came in the late 1990s, and involved private enterprises and business people that escaped the competitive business environment in China. He further distinguishes between the cooperative value of collaborating with the first and second group, compared to the third. The two first have developed stronger relationships and have more influence in leading business in Africa.

The entry modes of Chinese businesses in Africa have shifted over time (FOFAC, 2011). In the 1980s the entry modes were equity joint ventures, cooperative joint ventures, and leasing. However, differentiating it from the linear pattern of the Uppsala model, simultaneously companies that already had experience from trade were establishing factories. In the 1990s, entry modes took the form of solely funded enterprises, and joint ventures. The entry modes of the last decade are not included in the report. However, a study by Song (2011) investigated the entry mode pattern of private Chinese firms that have made real investments in Africa from 2006-2008. He found that 70 percent were wholly-owned manufacturing investments, 19 percent joint ventures. The remaining 11 percent were indirect product or service selling modes following the stage model. The reasoning for the increased commitment at an early stage was the existence of networks. When a business opportunity was identified overseas, Chinese networks or government sponsored aid projects were depended upon. At a later stage, cooperation or joint ventures with ethnic Chinese communities overseas could possibly be formed.
4.5 China’s Approach to the Institutional Environment in Africa

The attractiveness of a nation as a host for MNE activity is influenced by whether institutions are developed or not (Dunning & Lundan, 2008). The definition of institutions covers both formal and informal institutions. Formal institutions such as good governance in host nations is known to have a positive effect on FDI inflow. Informal institutions such as norms and social rules can also ease or complicate business interaction. The relevance of institutions in FDI are connected to OLI paradigm. Institutions affects the eclectic paradigm as a whole, see Appendix 9 adapted from Dunning & Lundan (2008). Appendix 9. gives examples of institutional mechanisms within each of the OLI components. To cope with the situation of institutional dysfunction, formal and informal instruments are suggested. Africa as a continent makes it more challenging to discuss nations individually it terms of how institutionally developed they are. To cover the presence of formal institutions, and to analyze whether instructional dysfunction discourages China’s investment in Africa as expected by theory, indexes covering safety and rule of law and corruption were used as tools.

Higher risk in a host nation is usually correlated with higher returns and use of an index without measuring return would be insufficient (Buckley, et al., 2007). However, the primary aim of the indexes is not measuring the relationship between risk and return. The aim is to prove institutional dysfunction in connection with similarity in host and home country institutions. The top receiving host nations of Chinese OFDI in Africa from 2003-2010 was used to evaluate the indexes. Namely Nigeria, Sudan, Algeria, and South Africa. The Ibrahim index is the most comprehensive source of data of African governance and measured based on four categories. The one found most appropriate to use, as it is closest to institutional dysfunction as Dunning & Lundan (2008) describe it, is safety and rule of law. The category measures judicial process, corruption, conflicts and crime. Transparency International publishes worldwide statistics on perceived corruption in the public sector. The transparency index is interesting to investigate as well, as it provides the opportunity to compare the host nations to the perceived levels of corruption in China.
Table 4.2 shows that the nations that China has invested the most in Africa rank notoriously low on governance and corruption indexes with the exception of South Africa. South Africa also ranked higher than China in transparency. A possible explanation for this could be renowned reporting and auditing standards, an advanced legal system, and the establishment of The Directorate of Special Operations in 2001. The directorate investigated and prosecuted corruption in government. China is increasingly working towards becoming more transparent. Initiatives taken include international and national efforts. China signed the United Nations (UN) convention against corruption in 2006 criminalizing bribery abroad. The Central Committee of the Chinese Communist Party issued a prohibition of entering commercial bribery overseas in 2008. Yet, corruption is still widespread in China.


<table>
<thead>
<tr>
<th>Year</th>
<th>Country</th>
<th>Score Ibrahim Index(Given from 0-100)</th>
<th>Transparency International score(Given from 1-10)</th>
<th>Transparency International score</th>
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</thead>
<tbody>
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<td>41</td>
<td>1.4</td>
<td>3.4</td>
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<tr>
<td>2004</td>
<td>Sudan</td>
<td>25</td>
<td>2.2</td>
<td>3.4</td>
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<td>25</td>
<td>2.1</td>
<td>3.2</td>
</tr>
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<td>Algeria</td>
<td>49</td>
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<td>3.3</td>
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<td>2010</td>
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<td>70</td>
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</table>
China’s view on corruption is largely shaped by the home environment, and it has yet disrupted economic development in China. Consequently, their view on combating corruption might be that it is harmful to growth (Brautigam, 2009). Several researchers have suggest that China is attracted to countries with weak institutions including Morck, et al. (2008), Buckley, et al. (2007), and Kolstad & Wiig (2012). The latter investigated the joint effect of institutions and ownership of natural resources, hypothesizing that Chinese OFDI is attracted to countries that possess natural resources together with underdeveloped institutions. Findings included that several of Chinese OFDI recipients in Africa have underdeveloped institutions. Highlighting Sudan as an example pointing to the country’s high corruption rate, and lack of democracy. In addition, the researchers discovered that Chinese OFDI is discouraged by natural resources when good institutions are in place. By rerunning the data and splitting the sample, attraction to poor institutions coupled with ownership of natural resources did not hold for OECD countries. Consistent with theory, suggesting that total FDI is attracted to countries with good institutions.

China’s ability to handle risky business environments is an outcome of its own distinctive institutional environment. Kolstad & Wiig (2012) suggest it reflects the institutional context of China with higher corruption levels than other developed countries that carry out FDI. The researchers go as far as to suggest that Chinese firms specialize in countries with poor institutions. In addition, they put forward that multinational investment activity performed by SOEs could result in excessive risk taking, unprofitable investments, and an attraction to countries with poor institutions. Chinese firms compared with firms from highly developed countries are more experienced and probably more capable with dealing with complex institutional features, which in turn can result to a competitive advantage (Morck, et al., 2008).
4.5.1 Informal Institutions and Psychic Distance

China and Africa are geographically distant; however, the two are closer in psychic distance such as business practices and culture. Using Hofstede’s research on cultural distance (see section 3.5) as a descriptive tool to examine comparisons in business practices, similarities are discovered. Cultural distance can be applied synonymously to psychic distance (Kogut & Singh, 1988). The dimensions measure in terms of culture the psychic distance between China, East African countries, West African countries, and South Africa. An alternative would be to add the African regions into one, but South Africa should discrepancies that were interesting to show. These discrepancies likely reflect that during the time of the study apartheid had not yet been abolished. Therefore, the results might reflect the culture of European descendants and are more similar to Western cultures. Countries are ranked from zero to 100 on four dimensions, with the exception of long-term orientation that stretches to 120. Figure 4.4 is added to analyze what possible differences, or similarities exist between Chinese and African business cultures.

Figure 4.4 Cultural Distance as a Proxy for Psychic Distance.

Source: (The Hofstede Center, 2013)
Power distance measures the acceptance of a hierarchical division of society. Acceptance of a power inequality is above 50 percent for China and the African regions with the exception of South-Africa that scored 49, which interprets that a flatter hierarchy in society is ideal. Individualism versus collectivism measures whether individuals in society value interdependence. South Africa scores high in individuality while China, East-Africa and West-Africa value collectivism. Masculinity versus femininity measures what kind of aspirations and goals the society encourages. Masculine traits include more focus on competition, success, and achievement. China and South Africa seem to value masculine traits compared to West and East- Africa .Uncertainty avoidance measures the actions a society takes to deal with ambiguity and risk. Uncertainty avoidance is of higher importance to African regions than China.

The last dimension was added in 1991 by researcher Michael Bond at the Chinese University in Hong Kong. The fifth dimension relates specifically to the case of China-Africa. The dimension was designed by Chinese academics to oppose western formulation of the measurements (Hofstede, 2007 ). The dimension relates to whether a long-term view versus a short time view is taken on achieving results. Long-term orientation is of much higher importance for the Chinese society compared to the African regions, with a value of 118 out of 120. Data on South Africa’s long-term orientation was not available.

In the context of the research proposition if physic distance is manageable, three dimensions are more interesting to go into depth with. The first is that collectivism is a characteristic of the Chinese way of doing business. Collectivism is also important for African regions with the exception of South Africa. It is evident that China is putting emphasize on the similarity in culture when it comes to relationship building. The report by FOFAC (2011) underlines arguments such as friendship, mutual trust, and solidarity. The second is uncertainty avoidance. China has a low score concerning to uncertainty avoidance compared to the African nations. In a business context, this can be seen as being able to handle a great deal of ambiguity. Which in terms can mean flexibility in accessing and adapting to the African market.
The third is that long-term orientation has been an important consideration for the Chinese when doing business in Africa. Indications of this is visible through commercial interest coming at quite late stage in their involvement and the long investment horizon of CAD. China’s strategy in Africa is well thought, long-term and still unfolding (Brautigam, 2009). The historical duration of their involvement gives them trustworthiness among African governments. The common trust they have built translates to an asset, namely relational capital. Relational capital limits the distance of being involved in a business relationship as counterparts have accumulated knowledge and trust.

In addition, there are other relational practices present in the cooperation such as China’s non-interference position to Africa’s internal affairs. China from a very early stage in their involvement made clear that they respect Africa’s autonomy to deal with political matters themselves. This differentiates China from most Western investors that together with the international community attempt to boycott economic activity, or sanction government leaders that violate human rights or are engaged in war crimes. China does not to the same extent as the West impose conditionality when financing projects. An illustration is the Darfur conflict in Sudan.

In 2004, the international community through the UN Security Council endorsed the first resolution drafted on economically sanctioning Sudan based on violation of human rights, and international humanitarian law. China on the other hand, abstained from sanctioning Sudan and continued investments together with sale of arms (Brautigam, 2009). The author makes two sound argument when shedding light on China’s behavior in Sudan conflict. The first is that China has been under criticism for violating human rights. Therefore, it is problematic for Chinese government to address a topic they have been criticized on themselves. Secondly, there is a fit in approach as Africa does have options regarding investors, not being solely dependent on those that impose conditionality on human rights. Consequently, China has consciously taken a noninterference position on ethical matters.
5. Discussion and Compatibility with Theory

In connection with Moon & Roehl (2001) notion of conventional FDI theories, several researchers have deliberated on the idea that Chinese OFDI cannot be explained by conventional theory. Buckley, et al. (2007) argue that open markets and industries together with increased competition forced some Chinese firms to seek new markets. Chinese OFDI has increasingly widened its reach, especially among developing countries with an offensive strategy to seek new markets. Brautigam (2009) suggests the same outlook. Her view is that tough competition in China has driven profit margins down because of the ability to create new firms, which in turn leads to overcapacity. Therefore, the Chinese government encourages labor-intensive mature industries to move to foreign locations because of fierce competition, and’ creative destruction’. Intensified competition encouraging the search for new locations illustrates the standardization phase in Vernon’s product cycle. Vernon suggested that once the home market reached the standardization phase, the factors of production can be obtained at a lower price in a foreign country and new markets for production facilities will be explored.

In accordance with Vernon’s revised application of the product cycle, evidence points to Chinese IFDI occurring prior to OFDI. Foreign MNEs investing in China resulted in a transfer of knowledge, and technology facilitating China’s transformation from a recipient of FDI to an initiator (Pedersen, et al., 2009). China’s increased focus on investing in emerging economies represents the view that China is starting their own product cycle, were Africa is an example of a continent that is behind in the ‘industrialized pecking order’. However, there are some opposing facts to this case in relation to Vernon’s hypothesis. The first is that average labor productivity was found to be lower in Africa than China. The second is that with exception, labor cost in Africa are similar to Chinese labor cost. Which suggest a motive that is not related to cost of production being lower, but rather an industrial upgrading leading to relocation. Proposition 1. that the relocation of low-end manufacturing from China to Africa is based on cheaper factors of production is found to be incorrect. Alternatively, it is found to be based on China’s change towards high technology production and the search for new markets to produce low-end manufacturing products.
Closely related to Vernon’s product cycle, and more suitable to describe the case of China-Africa is the ‘flying geese’ model. Developed by Japanese economist Akamatsu in the 1930s, the “flying geese” model attempts to explain the industrial development of Asian countries with Japan as the main focus. Akamatsu put forward the idea that the countries of the world form a flying geese pattern, where developed countries lead and less developed countries follow their technological innovations. One of the patterns he identified was that when a less developed country enters into an economic cooperation with a developed country, capabilities for economic growth transfer. Most relevantly, production will shift from what he terms ‘crude goods’ to ‘elaborate goods’, from labor intensive to capital and knowledge intense. Therefore, leading to relocation of production from the now advanced country to a less advanced. China has previously been known as the low-cost producer of the world however, recent literature suggest that the current domestic business environment has changed. China’s growth towards an emerging economy has stirred where the ‘economic weight’ lies in the world as China has graduated from low-skilled labor production to ‘leading dragon’ (Lin, 2012).

Due to transition in policy, China has become a market increasingly opening up to foreign firms. China does not only face increased domestic competition between national firms, but there is also a vast presence of foreign MNEs operating there. Foreign MNEs operating in China were the objects of a report written by KPMG (2012). A number of senior executives over a range of sectors were asked to clarify and predict the challenges, and opportunities of operating in China. Opinions expressed included: ‘growth slowing’, ‘costs rising’, and ‘China being an increasingly expensive place to do business’. The reports puts forward the idea that a ‘shift in the world’s production chain’ might be seen, with China moving up the hierarchy.
Consistent with the upgrading of China’s industrial development and SEZs opening up the possibility for a transfer of knowledge, Kojima’s trade theory enters. According to Kojima, a country should initiate FDI in disadvantaged industry allowing for a transfer of knowledge and technology. The market and resource-seeking motive of China in Africa is an approach to compensate for disadvantaged industries. The objectives being relocating mature industries to secure new markets and access to natural resources. Furthermore, China is applying the methods predicted by Kojima’s theory in Africa such as mixing investment with developing assistance for imports. Most notably, infrastructure development assistance, and offering resource-backed lines of credit. In addition, Kojima suggested that investment should be export oriented, which has been one of the specific characteristics of China’s involvement in Africa as China has been running a trade deficit since 2005. Lastly, Kojima argued for liberalizing trade tariffs, an effort that is partly realized through China developing SEZs in Africa providing tariff reliefs. Proposition 2, is found to be correct. OFDI from China to Africa flows in a manner that is correct with Kojima’s predictions. The disadvantaged industries consist of mining and manufacturing. Capital, technology and knowledge are transferred aimed at the advantage of obtaining natural resources and new markets. In addition, the Japanese model of development has further inspired China’s action of offering developing assistance, and limiting trade barriers by setting up SEZs.

The development of China’s FDI policy following the reasoning of IDP theory points to China having passed the first two stages. China is found to have reached the third stage of the IDP model. The first stage characterized by capital and technology inflow being limited, was surpassed when China launched its open door policy. Gradually more and more countries have opened their eyes up for the investment possibilities in China. In 2010, China was the second largest recipient of global inward FDI (UNCTAD, 2011). Neither is it a least developed country as GDP level correspond to that of an emerging economy. The second stage of the IDP is identified by the increasing location specific advantages. Attracting many MNEs, the locational advantages of China include producing at low cost together with being a highly populated market with an increasing middleclass.
Outward FDI is nevertheless not limited, and was higher than ever in 2010 indicating that the second stage is passed. The year 2001 seemed to have marked the beginning of China moving towards the third stage with active government intervention to increase China’s global presence. The Chinese economy is beginning to make its transition from imitator to innovator, as a result of exposure to new technology and knowledge from inward FDI. Although the amount of inward FDI is still higher consistent with the third stage, the growth levels of outward FDI has exceeded inward FDI. The fourth stage identified by outward FDI volumes passing inward FDI, concludes that the fourth stage has not yet been fulfilled. **Proposition 3**, that China has reached the latter stages of IDP is correct. Increased OFDI is a natural step following the IDP logic.

The entry modes of both SOEs and private firms in Africa seem to contradict the stage model. It is important to distinguish between SOEs, and private firms because SOEs have been present longer and have more resources through government backing. SOEs invested through high commitment modes such as wholly own subsidiaries in the 1990s, as a consecutive step to trade. Before the year 2000, there was no registered OFDI activity in Africa registered by Chinese private firms. A significant part of private firms enter through high commitment modes such as wholly owned subsidiaries, and joint ventures at a relatively early stage (Song, 2011). The case does not seem to reflect learning through the original stage model, but rather supports the revised version highlighting business networks and national efforts to encourage and also assist investment in Africa. Starting with SOEs taking the first step and gradually transferring knowledge through business networks to private firms. The business networks consist among others of individuals that have been involved in government projects. This also points to learning being transferred from one generation of Chinese workers to another. SOEs and the Chinese government have paved the way for private firms, and especially in the 21st century put in place incentives to stimulate investment in Africa. Emerging countries can offset ownership and location disadvantages abroad through high levels of government support (Buckley, et al., 2007).
The experiential knowledge Johnson & Valhlne mention in their theory seems to have been transferred through networks, and government efforts to promote the market. Contradictory to the state and change mechanism describing the behavior a firm to commit to a market, Chinese firm’s market knowledge about Africa comes from national efforts to increase knowledge and commitment. Instead of following the linear model, accessed entry modes of different degrees of commitment have occurred simultaneously. Certain stages appear to have been leaped by private enterprises because of previous efforts made by SOEs and the Chinese government. **Proposition 4.1** Increased commitment based on increased learning is correct. Experiential knowledge is substituted by the transfer of knowledge from the Chinese government and business networks.

The psychic distance between China and Africa is mitigated through sharing cultural characteristics, and shared institutional imperfections. Hofstede’s dimensions of cultural distance indicate that China, East Africa and West Africa share some cultural traits, most importantly collectivism. Building an investment relationship based on cultivating an alliance symbolizes much of China’s investment in Africa, ranging from the TANZAM project to FOFAC initiatives such as debt relief and economic assistance. China has accumulated social capital in Africa through relational accommodation to achieve reciprocity. This reciprocity takes the form of cooperation on a government level. Chinese FDI in countries that record high levels of political risk commonly involves the Chinese government and the host country government (Buckley, et al., 2007). The long-term view Hofstede found to be true for China fits in the African investment context, as investment became commercial in nature quite late in the involvement. The importance of geographical proximity in the original version of the Uppsala model has been alleviated through policy backing and business networks. In support with the revised version of the Uppsala model, business networks and its connection with psychic distance is of higher importance to Chinese private firms operating in Africa. For SOEs, the government functions as a network. In addition, initiatives such as SEZs and CAD have contributed to bridging the gap of psychic distance.
The Ibrahim safety and rule of law index revealed that the most popular investment locations for China in Africa between 2003-2010 rank low on the index. Institutional dysfunction in a host country is expected to discourage FDI activity. The reason why China is not discouraged, I believe is revealed in the transparency index. The perceived corruption transparency index exposes that both China, and its popular investment locations have a low corruption index scores. This in turn translates into one of China’s ownership advantages in Africa. Discouragement is less present because of the knowledge of operating in an environment that has institutional flaws. Proposition 4.2 That the psychic distance between China and Africa is a barrier that is manageable is correct. Both through similarities in institutions and culture. In addition, government efforts and networks ease the distance.

Mathews (2006) represents the view of the need for unconventional theory to explain China’s internationalization. Commenting on a number of conventional theories inconsideration for globalization, he claims that in a time of relatively closed markets the common practice was FDI based on exploiting ownership advantages. Labelling firms from the Asia Pacific region ‘Dragon Multinationals’, he suggests that the stages of internationalization of these firms differ from what is predicted by theory. He argues that firms from developed countries as incumbents internationalize to exploit their resources. While ‘Dragon Multinationals’ as newcomers internationalize to seek resources that might otherwise be unavailable. Consequently, he challenges the OLI framework suitability for ‘Dragon Multinationals’. Suggesting that the existing OLI framework is focused on the’ push factors’ rather than the ‘pull-factors’. Push factors are existing capabilities that trigger FDI. While, pull factors are desired capabilities existing in different location. He presents an alternative framework, the LLL (Linkage, Leverage, and Learning) framework. The main idea being that internationalization is motivated by resource linkage, leverage, and learning. Linkage meaning that ‘Dragon Multinational’ have a tendency to link up to international business networks through joint ventures and strategic alliances, to gain their advantage. Linkage allows for increased cost efficiency within the networks namely Leveraging. Learning is a transfer of competencies occurring within the networks through repeated Linkage and Leverage.
As an alternative framework to explain the specific case of China-Africa, the \textbf{LLL framework} offers little new insight. In accordance with the \textit{LLL framework}, the international expansion of Chinese firms in Africa is based on requiring assets that would otherwise be unavailable. The OLI framework integrates the search for unavailable assets. The L component in the OLI framework incorporates resource endowment asserting that immobile the resource, the more likely foreign activity occurs. The O component answering the \textit{why} of internationalization incorporates the market-seeking motivation. In addition, Mathews (2006) claims that ‘Dragon Multinationals’ do not depend on prior possession of ownership advantages. Chinese investing actors in Africa possession of ownership advantages include being more industrially advanced, capital, and knowledge of operating in institutionally difficult environments. Without being able to exploit these resources, much of the investment taking place appears unmanageable.

The case of China-Africa does however agree with the increased importance of networks. Networks allow firms to develop flexibility quite early in foreign activity, allowing for certain stage in the Uppsala model to be leaped. Chinese business networks in Africa have permitted private firms to accelerate the internationalization process through a form of \textit{Linkage} and \textit{Learning}. Nevertheless, the importance of networks in FDI was brought up by Dunning (1995) in a revisit to the OLI paradigm. ‘Alliance capital’ as he called it can constitute as an ownership advantage by widening the scope of the O component. In addition, the revised version of the Uppsala model presented the increased importance of business networks resulting in deviations from the stage model.

The ownership advantages of Chinese investors in Africa include similarities is business culture and understanding of institutional uncertainties, which establish the Oi advantages. Furthermore, Oa advantages such as production management are present through China being more industrially advanced and possessing more technology and knowledge. If ownership advantages are existing, internalizing capabilities is the next step in the OLI framework. In the Case of China-Africa, the ownership advantages are present because of the particularities of the Chinese business system.
These O advantages are put best to use through internalizing the experience-based knowledge of operating in institutional uncertainty. In addition, the existence of Chinese labor intense industries move to Africa being a recent phenomenon, one can assume that the expertise on how to manage the production is in Chinese companies. The locational advantages in the case arise for the reason that they are complements. China has the capital, technology and management skills. Africa offers a large, relatively unexploited market.

**Proposition 5.** Is correct, increased FDI is an outcome of existing OLI advantages.

Buckley, et al. (2007) suggest that general FDI theory is not well suited for China’s OFDI. They put forward three arguments they believe should be incorporated in OFDI theory for China. The first is *Capital Market Imperfections*, which possibly contribute to acquisition being a normal entry mode for Chinese firms. The second is *Ownership Advantages*, incorporating social capital through Chinese business networks overseas. Lastly, *Institutional factors*, meaning that the institutional environment of China shapes Chinese firms FDI strategy. The findings of this case point to being more in line with the argumentation of Buckley, et al. (2007) in that deviations from conventional theories exist.

Still, a new theory in the lines of the *strategic investment* or the *LLL framework* as an alternative explanation in the case of China-Africa demonstrate inadequacy. The strength of Chinese investing actors in Africa points to being exploitation of ownership capabilities arising from China’s distinctive business environment. The case suggests a situation where the exploitation of push factors allow for the exploration of pull factors.

The institutional advantage is higher when adapting to the the institutional context of the host country (Dunning & Lundan, 2008). In the case of China and Africa, that is exactly what China is doing; in addition evidence such as a cultural similarities and the transparency index points to less adaption being needed. This is particularly attributable to the fact that China has knowledge of being a developing country. In addition, their ownership capabilities are possibly novel to host nations in Africa. Therefore, the findings of this thesis do not dismiss the explanatory power of conventional theory. China is exploring for new resources, but simultaneously Africa offers the ideal market to exploit present capabilities.
6. Conclusion

The objective of this thesis was to determine the motivations behind China’s increased investment to Africa. The findings suggest that the drivers of increased FDI activity to Africa by Chinese investors is twofold. Chinese SOEs are driven by the resource-seeking motive, as the objective is to secure present and future needs of China for natural resources. Private Chinese firms pursue market-seeking investments aimed primarily at the manufacturing sector to secure growth and survival. The case of China’s investment in Africa represents determination on a government level unlike something that would be expected from traditional FDI theories. Therefore, it allows deviations from conventional theory, yet the unconventional theory of strategic investment or the LLL framework prove inadequacies as alternative explanations. There are strong ownership advantages in the case that allow for the resource and market seeking motive to be explored. The propositions of conventional theory are mostly supported with some nonconformities. Which contradicts the view that traditional FDI theory does not fit the internationalization process of emerging countries. Yet, the theories require modification to fit the distinct features of emerging economies. These distinctive characteristics lead to deviance from the common criteria of FDI.

In the case of China-Africa, such abnormalities arise from China’s distinctive business system. The Chinese government undeniably plays an active role in putting in place policy for foreign investment when they see necessary. From China’s ‘open door’ policy in 1978 to the ‘go global’ policy of 2001, the Chinese state vigorously encouraged FDI. The existence of SOEs further the argument that government interest are at stake. The geographical distribution revealed that Africa is not amongst the top regional destinations for Chinese OFDI. In that respect, Africa did not stand out as the destination being singled out. At that point, the analysis took a turn in connection with FDI theory to examine China as a source country of FDI. Contradictory to the expectations of FDI theory, findings included an attraction towards host countries that have institutional deficiencies. An examination of the institutional environment of China revealed that informal institutions has to a large extent substituted formal institutions. Resulting in a familiarity with circumventing the barrier of underdeveloped institutions.
Through governance and corruption transparency indexes, China’s top FDI destinations in Africa exhibited low rankings. The same corruption transparency index on behalf of China similarly exposed low scores. Leading me to believe, that the attraction towards institutionally underdeveloped host nations arises from knowledge of operating in uncertain business environments. Consistent with China’s practice of using informal institutions to facilitate business, China’s standpoint in Africa includes much emphasis on relational capital and highlighting historical ties. Hofstede’s cultural dimensions in the instance of China and Africa indicate shared similarities in cultural characteristics. Signifying that China drawing attention to collaboration, reciprocity, and relations as their business strategy is suitable. In addition, China offers an alternative investment approach in comparison with many Western countries, one that offers a high degree of flexibility. By both means and methods such as offering natural resource-backed credit lines and the non-interference policy within the political affairs of Africa, China distinguishes itself as an investor.

The implications of this thesis are that though Africa can seem like an unlikely market for China, investment relations between the two is not a rapid phenomenon and historical ties do exist. Still, the resource-based opinion dominates literature and headlines thus leading to the view many have of neo-colonialism. I believe there is more to it. I think they resemble each other more than a Western counterpart does, and it happens to be that their needs complement one another. I consider the present literature and research on China’s FDI in Africa too immersed on the resource-seeking motive. Such much that it underestimate the advantage of institutional similarities. Differentiating my thesis from previous findings, I believe that China’s strongest ownership advantage in Africa is institutional. A resemblance in home and host country institutions would mean that institutional flaws not only represent constraints, but also possibly an ownership advantage itself that contributes to enabling FDI. I encourage a more nuanced exploration, and investigation on China’s presence in Africa. One that examines what effect the presence of similarity in home and host country institutions has on the FDI decision.
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