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China's Overseas Foreign Direct Investment Risk: 2008–2009

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ABSTRACT

Since the implementation of its 'going-out' strategy, China's outward foreign direct investment (FDI) has experienced a rapid development, which has already become an important part of its overseas interests. This paper briefly analyses the current situation and its main features, the losses suffered as well as the major risks that China's outward FDI faced during 2008 and 2009. The preliminary conclusions include: (1) China's overseas FDI has experienced rapid development, but is still low in absolute terms, while the concentration trend of geographical and industrial distribution is obvious. This indicates that the 'going-out' strategy has been faithfully implemented, but also contains high risks. (2) The risks of China's outward FDI emanate from four main aspects: breach of contract and unexpected transactional costs; exchange loss; premium-value transactions; and failure of integration. (3) Overseas FDI faces systemic risks. The internal causes from the Chinese side include a high concentration of investment, excessive government intervention, low international business management ability and a lack of overseas investment strategies. (4) Based on a country risk analysis of China's overseas FDI, the most important issues are the legal, political, social and other institutional differences and conflicts. Through interpretation of reports on *Outward FDI and Co-operation Country (region) Guide (2009 Edition)* issued by the Ministry of Commerce, this paper argues that the primary risk of China's overseas direct investment is the incompatibility of institutions.

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ABBREVIATIONS AND ACRONYMS

AUD	Australian dollar
BCG	Boston Consultancy Group
BIT	Bilateral Investment Treaty
CAD	Canadian dollars
DRC	Democratic Republic of Congo
FDI	foreign direct investment
IMF	International Monetary Fund
KRW	Korean won
M&A	mergers and acquisitions
OECD	Organisation for Economic Co-operation and Development
RMB	renminbi (Chinese currency)
RV	recreational vehicle
SAIC	Shanghai Automotive Industry Corporation
SOE	state-owned enterprise
SUV	sport utility vehicle
WTI	West Texas Intermediate

INTRODUCTION

Since 2000, when the 'going-out' strategy was officially made public, China's outward foreign direct investment (FDI) has expanded, exceeding $10 billion five years later and making China the largest outward FDI investor among developing countries. In the wake of the international financial crisis of 2008–2009, unlike most countries, Chinese outward FDI increased. This phenomenon has played an important role in facilitating the transfer of China's production capacity to other countries, deepening international reciprocal co-operation on natural resources, ensuring an effective response to crisis and even increasing Beijing's right to speak about improving the international economic order. As a crucial component of China's 'going-out' strategy, FDI is part of 'a grand strategy related to the overall situation and future of China's development'.[1] For China, the long-term strategic significance is that the rapid development of outward FDI can contribute to deepening domestic reform and the opening-up process, and lead to greater Chinese participation in fostering a more equitable form of economic globalisation. Outward FDI makes it possible for China to attain and safeguard its development interests. At the same time, as the pace of China's overseas investment continues to grow, this strategy carries certain risks, which will have significant implications for China's overseas and national development interests.

This paper reviews and analyses the risks of China's FDI from 2008 to 2009. It first looks at the current status and main features of China's FDI, giving a brief analysis of its risks. It then examines the cause of these risks, analysing the role of China's public and private sector in relation to these risks. Finally, it provides an interpretation of a series of reports in *China's Outward FDI and Co-operation Country (region) Guide (2009 Edition)*.

CHARACTERISTICS OF CHINA'S OVERSEAS FDI

Overseas FDI accounts for a small fraction of China's outward FDI

A striking feature of the statistical data for China's outward FDI is that 'outward' does not mean outside the border, but rather outside the customs boundary, which includes all regions outside mainland China.[2] Thus, separate customs territories such as Hong Kong, Macao and Taiwan, which fall under the jurisdiction of China's sovereignty, are included in China's outward FDI statistics. At the same time, the complexity and risks of the economic and trade exchanges among Mainland China, Hong Kong, Macao and Taiwan differ greatly from real 'outward' investment, due to the political, cultural and geographical proximity of these areas. According to the *Statistical Bulletin of China's Outward Foreign Direct Investment,* in recent years Hong Kong and Macao represented the largest share of China's total outward non-financial FDI, surging to 70.3% in 2008, while the FDI stock rose to 63.8% at end of 2008. This does not accurately reflect the real economic relations between China and the outside world, or give a true picture of the close relationship between China's overseas and national development interests.[3] Therefore, to understand the real pattern of China's investment beyond national boundaries, 'overseas' FDI will be

used as a measure to reflect investment in foreign countries and regions outside the scope of China's effective sovereignty and jurisdiction.

Another defect is that China's outward FDI statistics also include traditional international tax havens such as the Cayman Islands or British Virgin Islands, where inflow FDI does not usually mean real investment. According to historical data, the Cayman Islands and the British Virgin Islands represented 52.1% of China's outward FDI in 2005, and 16.7% in 2008. This aspect of China's outflow FDI is known as the 'virgin phenomenon'. While it is difficult to be sure of the final destination of the inflow FDI to those international tax heavens, most of these investments came back to China, enabling domestic investors to be treated as foreign companies and so acquire super-national treatment concessions. In other words, the 'virgin phenomenon' usually represents a 'fake FDI' phenomenon.[4] Therefore, for the purpose of this paper, China's investment in the Cayman and British Virgin Islands is excluded from the 'overseas FDI' and country risks discussed.

After eliminating the statistics for Hong Kong, Macao, Taiwan and the two tax havens, China's overseas FDI represented about 20% of outward FDI in recent years. For instance, in 2008, overseas FDI flows were $13 billion, while the stock reached $35.74 billion.

Table 1: Outward FDI versus overseas FDI, 2003–2008 ($ billions)

Category / Year	Outward FDI			Overseas FDI	
	Total value	Proportion of Hong Kong and Macao	Proportion of Cayman Islands and British Virgin Islands	Absolute value	Proportion of outward FDI (%)
2003 flows	2.85	1.18	1.02	0.66	23.1
2004 flows	5.50	2.66	1.67	1.16	21.2
2005 flows	12.26	3.43	6.39	2.45	20.0
2006 flows	17.63	6.89	8.37	2.37	13.5
2007 flows	24.84	13.78	4.48	6.58	26.5
2008 flows	55.91	39.28	3.63	13.00	23.2
2008 stock	183.97	117.41	30.80	35.76	19.4

Source: Annual *Statistical Bulletins of China's Outward Foreign Direct Investment*. In 2003–2007: Non-financial outward FDI data. In 2008, the flows and stock are all outward FDI

Overseas FDI is concentrated in certain regions

Under the 'going-out' strategy, China's outward FDI is rapidly expanding around the world. In recent years, China has invested in a growing number of economies: from 2003 to 2008, new investments reached 35 countries and regions. At the same time, Chinese investment

is concentrated in certain geographical areas, with the top ten countries/regions receiving over 60% of total investment in recent years, reaching a peak of 81.1% in 2008. Until the end of 2008, the investment stock in the top ten countries/regions accounted for 55.1% of the total. In addition, the number of the countries/regions increased sharply, from four to 21, representing investment flows of more than $100 million in 2007. As a proportion of overall overseas FDI, investment flows surged from less than 40% in 2004 to 80%, and even 90%, in 2008. These changes show not only the size of China' overseas FDI, but also imply a rapid increase in large-scale projects, which in turn means many investment projects focused on specific sectors that require huge funding.

Table 2: Concentration of China's overseas FDI

	Total flows of China's overseas FDI ($ billion)	Investment stock cover countries or regions	Investment flows more than $100 million in the country/region			Investment flows in the top ten countries/regions	
			Number of countries/regions	Investment ($ billion)	Proportion of overall overseas FDI (%)	Investment ($ billion)	Proportion of overall overseas FDI (%)
2003	0.66	135	1	0.15	23.6	0.51	77.2
2004	1.16	145	3	0.39	33.5	0.75	64.6
2005	2.45	159	6	1.45	59.3	1.78	72.5
2006	2.37	168	4	0.90	37.9	1.42	59.9
2007	8.25	169	21	6.86	83.1	5.28	64.0
2008	13.00	170	18	11.68	89.9	10.55	81.1

Source: Annual *Statistical Bulletins of China's Outward Foreign Direct Investment*. In 2003–2007: Non-financial outward FDI data. In 2008, the flows and stock are all outward FDI

In terms of flows and stock, the Asian region has enjoyed a major share of China's overseas FDI, although China's investment in Africa is growing rapidly. In 2008, flows to Africa surged to first place, in front of Asia, mainly because China's investments in South Africa were ten times greater than the previous year. In 2008, South Africa was China's top FDI destination, accounting for 87.6% of investment flows in Africa. As the demand for mineral resources rose, China's direct investment in Oceania also experienced rapid growth. Currently, Australia is the country that receives the largest stock of China's overseas FDI.

The priorities and trends of China's overseas FDI can be identified by examining the proportion of total inward FDI to host continents. In 2008, Africa and Oceania accounted for the biggest proportion of China's investment. China's overseas FDI in Africa and Oceania occupied 6.26% and 3.93% of their inward FDI, compared to only 1.01% in Asia and less than 1% in Latin America.[5] China's direct investment stock accounted for 1.53% and 1.14% of Africa and Oceania's inward FDI stocks. In Asia, the continent which owned

the highest absolute amount of China's investment stock, the proportion was only 0.49%,[6] while in Europe, China's investment accounted for only 0.07% of the total inward FDI stocks. This data therefore reflects more clearly the geographical distribution of China's overseas FDI and also (to some extent) the orientation of China's investment in the industry and the ease of access of recipient markets.

Table 3: Regional distribution of overseas FDI ($ billions)

	2003 flow	2004 flow	2005 flow	2006 flow	2007 flow	2008 flow	2008 stock
Asia	0.318	0.343	0.942	0.773	1.603	4.267	13.914
Africa	0.075	0.317	0.400	0.520	1.570	5.490	7.800
Europe	0.150	0.170	0.510	0.590	1.090	0.880	5.130
North America	0.058	0.126	0.320	0.260	1.130	0.360	3.660
Latin America	0.023	0.088	0.080	0.102	0.420	0.052	1.436
Oceania	0.034	0.120	0.200	0.130	0.770	1.950	3.820
Total amount	**0.658**	**1.164**	**2.452**	**2.375**	**6.583**	**12.999**	**35.760**

Source: Annual *Statistical Bulletins of China's Outward Foreign Direct Investment*. In 2003–2007: Non-financial outward FDI data. In 2008, the flows and stock are all outward FDI

Table 4: China's total inward FDI in all continents ($ billions)

	Chinese investment flows in the host continents	Local absorption of the total investment flows	China's investment flows accounted (%)	China's investment stocks in the host continents	Local absorption of the total investment stocks	Chinese investment stocks accounted (%)
Asia	4.27	421.89	1.01%	13.91	2,835.85	0.49%
Africa	5.49	87.65	6.26%	7.80	510.51	1.53%
Europe	0.88	632.70	0.14%	5.13	7,352.94	0.07%
North America	0.36	360.82	0.10%	3.66	2,691.16	0.14%
Latin America	0.05	144.38	0.04%	1.44	1,184.37	0.12%
Oceania	1.95	49.63	3.93%	3.82	334.45	1.14%
Total value	**13.00**	**1,697.35**	**0.77%**	**35.76**	**14,909.29**	**0.24%**

Source: The local absorption of the total investment data is from *World Investment Report 2009*, United Nations Conference on Trade and Development (UNCTAD). Author did the ratio

Target industries in the energy and mining sectors

Cross-border mergers and acquisitions (M&A) are concentrated in the energy and mineral industries, mainly because of China's long-term economic development strategy. In 2008 and 2009, Chinese enterprises took part in at least 34 cross-border M&A above $100 million, representing a total value of up to $57.13 billion.[7] Of these, 13 M&A were in the energy industry, accounting for $27.754 billion or 48.6% of the total $100 million, while 15 M&A were in the mining industry, worth $26.234 billion or 45.9% of total transactions. Utilities and business services each had one M&A worth $1.58 billion and $858 million respectively, while the three manufacturing M&A amounted to $704 million.[8]

The economy's rapid growth in recent years has put strong pressure on China's domestic reserves of natural resources, such as oil, non-ferrous metals and iron ore. China needs to ensure its energy supply security, price stability and an adequate supply of raw materials through co-ordinated arrangements around the world. These will not only be conducive to sustained economic development, but also enable China to enter and compete in commodity markets. China's inevitable choice is to seek to control as many oil and other resources by expanding its overseas investments, which are mainly conducted by China's large state-owned enterprises (SOEs) due to the capital-intensive nature of the resource sector.[9]

THE RISK OF CHINA'S OVERSEAS FDI: STATUS QUO

Studies have shown that, internationally, the success rate of large-scale enterprises M&A was less than 50%, while 67% of China's overseas acquisitions in the past 20 years did not succeed.[10] According to statistics of the Ministry of Commerce of the People's Republic of China in 2007, 65% of Chinese enterprises' overseas investments were in the red.[11] Another study estimated that, in 2008, cross-border M&A by Chinese enterprises lost more than RMB[12] 200 billion, which is equivalent to about $29.3 billion.[13] Based on recent case studies, M&A experience four categories of problems: breach of contract and delay to transactions; currency exchange losses; premium-value transactions; and integration failures.

Breach of contract and delay to transactions

A common problem was unexpected delays to transactions or breaches of contract, due to both commercial and non-commercial factors, which increased the investment costs and risks of overseas FDI.

In recent years, the largest commercial breach of contract was when Rio Tinto tore up the capital injection agreement with Aluminum Corporation of China (Chinalco). In 2008, Chinalco held 9.3% of Rio Tinto shares and was the largest single shareholder. On 12 February 2009, Chinalco and Rio Tinto announced the signing of a strategic co-operation agreement, which included a cash injection provision of $19.5 billion by Chinalco. If this transaction had been completed, Chinalco would have owned 18% of Rio Tinto's total shares, 19% of Rio Tinto plc (UK) and 14.9% of Rio Tinto Limited (Australia). On 5 June 2008, Rio Tinto announced a unilateral breach of contract, of what could have

been China's largest cross-border M&A. However, Chinalco only received $195 million in final compensation. Although Rio Tinto's rejection of Chinalco's huge capital injection was not surprising, what was amazing was that the final penalty for the liquidated damages was only 1% of the total contract. Afterwards, in order to remain Rio Tinto's single largest shareholder, Chinalco was forced to acquire shares on the open market at a cost of about $15 billion.

The unforeseen risks facing Chinese enterprises' overseas FDI are mainly in the energy, mineral and other strategic resources sectors, and come from increased protectionism. One example was in February 2009, when PetroChina Company Limited bid CAD[14] 499 million ($460 million) to acquire a small Canadian oil company, Verenex Energy, Inc., whose main business was in Libya. According to Libyan government regulations, any change in control of the foreign assets requires the Libyan National Oil Company's written consent. Initially, in May 2009, the Libyan National Oil Company expressed an interest in the offer, but did not approve the deal or exercise the right of preemption until announcing, in June, that Verenex's acquisition of the exploitation concession in Libya was illegal. On 22 June, Verenex denounced the Libyan National Oil Company in a public notice, noting that the real motive of its reluctance to approve the transaction was to 'cut off price [to buy on their own], or to raise the approved fee'. Following months of continued efforts, PetroChina and Verenex decided to terminate the acquisition on 7 September because Libya was blocking the deal.[15] Verenex was eventually sold to a Libyan sovereign wealth fund for only $340 million, 30% lower than the PetroChina offer.[16]

In addition to direct involvement by stakeholders in Chinese overseas FDI transactions, third parties have also interfered for international political reasons. For example, on 22 April 2008, the government of the Democratic Republic of Congo (DRC) signed a package of co-operation agreements with Chinese companies, including the China Railway Group Limited and the Sinohydro Corporation.[17] The agreements centred on investment in copper and cobalt ore projects and infrastructure construction projects in the DRC, based on the 'project for resources' mode (as it is characterised by the World Bank), worth $9.25 billion. Chinese enterprises committed to build hundreds of clinics, hospitals and schools, two hydroelectric dams, 3 300 kilometres of highways and 3 000 kilometres of railways in the DRC, in return for obtaining rights to develop copper and cobalt mines.[18] At that juncture, the DRC was finding it very difficult to obtain large amounts of capital through other channels and, although the financing agreements were 'win–win' and conformed to commercial principles, some international forces were uneasy. At the time, Kinshasa and foreign donors were discussing how to relieve the country's huge foreign debt, and negotiations were at a delicate stage.[19] The 'Paris Club' creditors and the International Monetary Fund (IMF) were opposed to some provisions of the agreements.[20] The IMF stated: 'Just co-operation agreements of China and the DRC should be consistent with the requirements of debt sustainability',[21] and requested that the agreements be amended.[22] Under pressure, as large debt relief was being linked to Chinese commercial loans, the agreements were drastically revised: the $3 billion infrastructure projects in the second phase and $3 billion of government guarantees for mining projects were removed, reducing the overall size of the agreements to $6 billion.[23] On the surface, the IMF intervention was motivated by concerns that the agreements could aggravate the debt burden of the DRC. However, the media in the DRC believed that the true reason for the IMF's fierce opposition was to obstruct the expansion of Chinese 'resources for infrastructure' or 'loans

for energy' into other fields in Africa. This expansion was believed to pose a threat to the old colonial mode of acquiring resources by Europe and the US.[24]

Exchange loss

Overseas FDI necessarily involves foreign currency assets, which inevitably leads to exchange risks caused by the uncertainty of exchange rates. Traditionally, China's overseas investment enterprises sell products denominated in dollars, and have product costs denominated in the host countries' currencies, while their credit at home relies mainly on renminbi loans from Chinese state-owned banks. In recent years, with the appreciation of the renminbi and the depreciation trend of foreign currencies, especially the dollar,[25] the overseas FDI of Chinese enterprises have faced more and more serious exchange risks. Since 2008, traditional hedging instruments have had difficulty dealing effectively with the tumultuous financial system, furthering the prospects of uncertainty due to systemic risk. Moreover, Chinese overseas enterprises have suffered enormous losses due to exchange rate movements.

In first half of 2008, exchange losses of overseas FDI came mainly from the appreciation of the renminbi and the continued depreciation of the dollar. Of the 745 Chinese listed companies that incurred exchange gains and losses in the first half of 2008, 488 companies suffered net exchange losses of up to 65%, a total loss of more than RMB 5.2 billion – PetroChina ranked number one with more than RMB 1 billion in exchange losses.[26] The second half of 2008 saw a dramatic fall in the value of the pound sterling, the euro and the Australian dollar (AUD), one after another. In the third quarter, in less than two months, the pound sterling depreciated by about 25% and the euro by about 21% against the RMB. In September and October, the Reserve Bank of Australia cut interest rates twice and the Australian dollar declined by nearly 40% against the dollar, which resulted in a number of Chinese companies in Australia suffering huge exchange losses. According to information publicly available, at least 12 large Chinese SOEs suffered exchange losses related to the depreciation of the Australian dollar.[27] A typical example of the effect of the Australian dollar's depreciation was Chinalco, which suffered total exchange losses of RMB 2.351 billion in the first three quarters of 2008.[28] The most dramatic was the fate of Chinalco's investment in the Aurukun bauxite project in Australia, for which Chinalco paid AUD 2.92 billion in March 2007, when the exchange rate was about AUD 1 for $0.68. However, over a year later in July 2008, the rate reached $0.9848, a 40% appreciation, which meant that Chinalco also had to pay more than 40% for its main foreign currency assets that were in dollars. Furthermore, after the Australian dollar's sharp decline in July 2008, equipment ordered previously in Australian dollars faced the risk of substantial depreciation. As China currently lacks hedging tools, especially financial derivatives, some companies have chosen to use the corresponding country's derivatives as hedging instruments to avoid foreign exchange losses. In a period of extreme currency fluctuations, this strategy can lead to more serious losses. Such was the case in 2008 for CITIC Pacific, which experienced huge losses pursuing this risk-offset strategy. Seeking to reduce the currency risk associated with acquiring an iron ore project in western Australia, the company leveraged foreign exchange contracts, which led to losses of more than HKD[29] 14.6 billion as the Australian dollar plummeted.[30]

Losses from premium-value transactions

Between 2002 and 2009, China more than doubled its number of enterprises established overseas, an average annual increase of 10.8%.[31] During the same period, the stock of China's outward FDI increased by 5.4 times, an average annual growth rate of 30.3%. The investment growth rate greatly exceeded the growth rate of the number of companies,[32] which inferred an expansion of the scale of investment projects and greater concentration. However, the gap between the two numbers was much higher than similar Chinese domestic data,[33] which suggests that other factors were in play.

In recent years, for many high-value overseas FDI transactions by Chinese enterprises, the actual purchase price was not only much higher than the domestic price, but also higher than similar deals between other foreign firms. Even after the financial crisis in 2008, when the overall global economy went into recession and many foreign enterprises suffered financial difficulties, several overseas 'bargain-hunting' M&A by Chinese enterprises were unsuccessful. The popular image of making acquisitions at a low price did not come true as expected. On the contrary, the outbreak and continuation of the financial crisis led to many Chinese enterprises' overseas FDI projects suffering a huge discount due to financial losses.

One source of premium loss was the dramatic fluctuation of prices in the international market: in 2008 and 2009, the prices of oil, ores and other commodities in international markets were volatile. In 2008, the average price of US West Texas Intermediate (WTI) and North Sea Brent crude oil (Brent) was respectively $100.06 and $97.26 per barrel, up 38.66 % and 34.37 % compared to the same period in the previous year. On 11 July 2008, the WTI price reached a record high of $147.27 per barrel. However, from the beginning of August, as the financial crisis and global economic recession spread, the demand for oil declined and international oil prices began to fall sharply. On 19 December 2008, WTI prices fell to $33.87 per barrel, the lowest level in nearly five years, a fall of more than 70% compared to July's record highs.[34] Moreover, in 2009, the international oil price trend rose to $80 per barrel by the end of the year. However, the annual average price of WTI and Brent fell respectively 38.2% and 36.5% compared to the previous year.[35] As the oil prices fell, many Chinese enterprises, which were involved in cross-border M&A when the international oil prices were high, suffered losses. For example, China Oilfield Services Limited acquired Awilco Offshore ASA of Norway for RMB 17.1 billion (about $2.5 billion) when the international price of oil reached a record peak in July 2008, after which the international oil price slumped. One year later, the company announced that the acquisition had resulted in a value loss of RMB 820 million.[36] It is not surprising that, in its acquisition of Rio Tinto shares, Chinalco suffered a paper loss of more than $8 billion (equivalent to about RMB 54.4 billion) during one year, as in 2008, the international price of primary aluminum dropped from $3,260 to $1,471 per ton (the London Metal Exchange aluminum spot price).[37]

Another type of premium loss is obvious when analysing some of the actual deals negotiated. For example, in May 2008, Chinalco entered into a joint venture agreement with foreign enterprises to build a million-ton electrolytic aluminum plant in Saudi Arabia and a 1 860 megawatts captive power plant, investing a total of $4.5 billion. Chinalco would hold 40% shares in the aluminum factory (becoming the largest shareholder) and 20% shares in the power plant (making it the third-largest shareholder).[38] At that time in

China, investments in electrolytic aluminum production was RMB 40–70 million per ten thousand tons and in power, RMB 4–6 million per megawatt. Based on this, investing in similar projects in China would have required up to RMB 18.1 billion (only about $2.65 billion).[39]

Integration failure

The greatest challenge of M&A comes from the post-acquisition integration, as making a deal (whether successful or not) is only the beginning. The post-merger company has to change the management structure and the internal and external environment of the company. Indeed, the best measurement of a successful takeover is the ability of the 'new' company to continue stable operations under the new framework.

In cross-border acquisitions, integration involves not only product lines, sales channels and business strategies, but also corporate culture, which is arguably more important. A survey by Deloitte found that 60% of M&A do not achieve the desired business value. Of these, two-thirds fail to integrate cultures after the merger. In the M&A business, a major challenge is bridging the culture gap and blending both corporate cultures into a new corporate culture.[40] Many of China's overseas M&A that were considered as 'successful' ultimately failed because of ineffective integration, which led to more losses.

In October 2004, the Shanghai Automotive Industry Corporation (SAIC) contributed KRW[41] 90 billion ($500 million, or about RMB 4.1 billion at the time) to buy 48.92% of the South Korean Ssangyong Motor Company (Ssangyong), becoming its largest shareholder. This first acquisition by a Chinese enterprise of a foreign vehicle manufacturer was considered a landmark event for the Chinese auto industry to compete internationally. Although SAIC injected huge funds, the already troubled Ssangyong's operational difficulties were not reversed, and the 2008 sales were 30% lower than expected. By the end of 2008, Ssangyong suffered a serious liquidity crisis, which led to its financial situation deteriorating further, affecting SAIC's financials, which declined sharply. SAIC then went on to accrue long-term equity investments to offset the depreciation of about RMB 3.076 billion for Ssangyong.[42] The financial difficulties caused a further crisis of confidence on both sides. SAIC's proposed reorganisation plan included high job cuts, which were ill-received by the Ssangyong union. The breakdown of the Ssangyong labour negotiations, at the end of 2008, was followed by a bankruptcy crisis. On 9 January 2009, Ssangyong attempted to restore control over the management of the firm, which subsequently led to SAIC losing control of the company. On 22 May 2009, the Ssangyong union began a strike, which lasted 76 days and resulted in further deterioration; SAIC made a RMB 1.182 billion provision for impairment of long-term equity investment,[43] which meant that the SAIC asset investment losses caused by Ssangyong were more than its initial investment. At the end of 2009 the South Korean court approved the reorganisation plan, which diluted SAIC's share in Ssangyong from 51.33% to 11.2%. Thus, the SAIC investment in Ssangyong appears to have been a complete waste of human and material resources.

The failure of SAIC's integration of Ssangyong demonstrates some fundamental mistakes made before and after M&A. Firstly, there was the lack of an adequate pre-merger investigation. SAIC thought that Ssangyong, as Korea's largest manufacturer of sports utility and recreational vehicles (SUV/RV), had developed the original diesel power technology through its longstanding co-operation agreement with the German company,

Mercedes-Benz, and therefore expected Ssangyong to have a good level of production management, technical equipment and research and development. However, after the merger, Ssangyong's viability turned out to be largely dependent on Mercedes-Benz's technical support, especially for diesel-powered technologies and accessories.

Secondly, as the management capacity of the combined enterprises was inadequate, the market situation did not improve. Ssangyong's traditional markets were in Korea and its main models were the high fuel-consumption SUVs. With the rising international oil prices in recent years, the competitiveness of the company's products declined, while new models were delayed. Not only did Ssangyong's product lines remain fundamentally the same, but also new international markets were limited. SAIC helped Ssangyong to export its cars to China and to establish the appropriate sales channels. However, Ssangyong's brand communications, image and customer satisfaction did not performed well in China, and the company failed to achieve the desired market share. Ssangyong sales did not improve after the acquisition, with the exception of 2007, annual earnings from 2004 to 2008 showed a deficit.

Most importantly, the key reason for the failure of M&A is the inability of both sides to achieve successful cultural integration. At Ssangyong, the most serious shortcoming was the relationship between management and the unions. During the five years after the acquisition, the trade union did not support any of the company's major decisions. The main conflicts were to do with technology transfer contracts and layoff programmes to reduce production costs, which have yet to be implemented because of strong resistance from trade unions. Under the banner of 'to prevent technology leakage, to fulfill investment commitments, to crush restructuring plan and for full employment', Ssangyong's labour union accused SAIC of not being sincere about long-term investment in Korea and launched a number of demonstrations and strikes. The two sides' sharp opposition caused a significant loss of business. The last straw was the collapse of the talks between employers and employees, which led to bankruptcy and reorganisation.

After acquiring Ssangyong, SAIC replaced the head of the company with a successor (who was also Korean). Concerned with personnel changes and layoffs, the Ssangyong labour union threatened to strike. Eight months later, another personnel change saw the arrival of a new director who proposed structural adjustment programmes that would lead to 550 job cuts. The Ssangyong labour union's 'die strike' lasted 20 days, caused about 16 000 motor vehicles to be cut, and a loss of about KRW 370 billion (RMB 3 billion). Despite a slight improvement in 2007, with the international financial crisis from 2008, the Ssangyong business was once again in deep trouble, requiring a capital injection from SAIC in order to develop a new vehicle model. In return for a $200 million capital injection, SAIC asked Ssangyong to carry out a structural adjustment, which included laying off 2 000 production line workers. Labour unions resisted the plan and, when negotiations between employers and employees broke down, Ssangyong went into bankruptcy and reorganisation to save the company. During the labour negotiations, before and after the bankruptcy proceedings, the labour union accused SAIC of 'steal[ing] Korea Automotive Technology, contradict[ing] the original investment agreements'. Labour union members even besieged the Chinese Embassy in South Korea, asking Chinese business groups to leave, and seized Chinese management personnel.

INTERNAL FACTORS AFFECTING OVERSEAS FDI RISK

The Tenth Five-Year Planning Outline in 2000 first proposed the 'going out' strategy and made clear the need to 'regulate foreign investment through supervision'. This shows that, from the outset, the 'going out' strategy was conscious of overseas FDI risks. Five years later, the Eleventh Five-Year Planning Outline was even more emphatic about the need 'to strengthen co-ordination of overseas investment, risks management and supervision of state-owned assets abroad'. In 2009, the government work report adopted by the Second Session of the Eleventh National People's Congress emphasised 'strengthening risks control and supervision of enterprises investment abroad'. The government work report approved by the National People's Congress in 2010 again suggested that the enterprises implementing 'going out' needed to avoid risks. At present, losses in overseas FDI, especially cross-border M&A, have far exceeded the normal level of losses in the domestic market. Accordingly, in addition to normal business risks and specific company risks, the more serious problems facing overseas FDI of Chinese enterprises come from the systemic external risks. These cross-border investment systemic risks come from both domestic factors of host countries or differences between countries (often called country risks), and the behaviour of Chinese enterprises caused by their own investment objectives, means and processes.

Investment over-concentrated in a few industries

China's overseas FDI has focused on a few industries such as energy and mining, where the largest M&A transactions have been concentrated in a few host countries. The focus on investing in large financial transactions has, in some cases, produced tensions and concerns within host countries, which probably exacerbated the potential economic and political risks. As a result, China's overseas investments face greater risks than its share of world investment warrants. For example, when Chinalco acquired $14 billion of Rio Tinto shares in early 2008, the Australian government had been encouraging the management to look for foreign investment. However, in 2009, Australia's Foreign Investment Review Board said that foreign investment in Australian mining companies would be limited to 15% of the shares, and new investment in mining projects should be less than 50%. These provisions are generally aimed at China's overseas FDI. Such problems cannot simply be attributed to the economic nationalism of host countries or protectionism. In fact, China is in real danger of becoming over dependent on imported resources, which will weaken any obligation to upgrade the Chinese industrial structure and enforce the existing 'backward' mode of economic growth and the irrational economic structure that still prevails in some industries. Therefore, to reduce overseas FDI risks, the most effective measures would be to change China's economic growth pattern, improve industry structure, increase economic efficiency and effectively co-ordinate international and domestic markets and resources. For a long time, China's overseas FDI will continue to be mostly in energy and raw materials,[44] which means that the concerns and possible frictions of host countries will not be rapidly eliminated.

Excessive government involvement and intervention

China's overseas FDI relies to a great extent on large SOEs for cross-border M&A. Although the advantages of large SOEs are evident, this approach is not without its problems. In no matter what industry, business strategy needs to reflect the nature of capital expansion, both within and outside its borders. However, Chinese cross-border M&A are often said to be motivated by the interests of the Chinese government, although the majority of the Chinese people consider this belief to be the product of anti-Chinese prejudice. However, in view of the general rules of the global market, an objective attitude to such opinions is necessary. The opaque relations between government and SOEs will inevitably make expansion overseas more expensive and even, at times, act as a fatal obstacle. In early 2008, the Australian government issued a foreign investment review, based on six principles, that would examine 'whether the operation of the investor is independent of the relevant foreign government' and its corporate governance and financing arrangements. In essence, foreign investment (including M&A) should be a commercial activity, enterprises should be the main force, and government should only provide external institutions to protect business. At present, the Chinese government has done much to promote outward FDI by building mechanisms to guarantee its effectiveness. As of mid-2009, China had established bilateral economic and trade agreements with over 100 countries and regions all over the world and signed at least 127 Bilateral Investment Treaties (BITs),[45] making China number two in the world for BITs.[46] Nevertheless, for the 'going out' strategy to be truly effective and more efficient, the government will have to let market forces play a more important role in the future, so that SOEs can follow commercial principles independently when making investment decisions. And it is particularly important to create fairer competition mechanisms, which would allow private enterprises that are driven by economic self-interest to participate, along with institutions, and in the long run promote healthy and sustainable development of China's economy.

'GOING OUT' ENTERPRISES LACK MANAGEMENT CAPACITY FOR INTERNATIONAL BUSINESS

For many Chinese enterprises, their understanding of M&A integration seems to be stuck in a mode that emphasises purchasing hard assets – equipment and plants – and acquiring technology. The current financial crisis has exacerbated this approach, with Chinese SOEs searching for 'bargains'. Many Chinese entrepreneurs think that money can buy everything, whereas the cross-border M&A miscarriages of the last two years show that capital is not the most important consideration prior to an acquisition. Furthermore, after the acquisition, Chinese enterprises find it difficult to add value other than financial. These two issues show that China's overseas FDI capacity is seriously flawed. For enterprises, the ultimate purpose of cross-border M&A should be to optimise resources and industrial, technological and market structures, not just to achieve economies of scale. Chinese enterprises currently implementing the 'going out' strategy suffer from a severe shortage of international management capacity, which is reflected in the problems related to integrating organisational culture and human capital. A substantial gap exists between Chinese enterprises and international competitors, who are better able to handle the

problems of integration in M&A. This underscores the fact that Chinese enterprises need to exert more effort and take risks in order to achieve the aims of the 'going out' strategy.

CHINESE ENTERPRISES LACK AN OVERSEAS FDI STRATEGY

From 2005 to 2008, the renminbi–dollar exchange rate increased by more than 20%, which could be seen as a significant advantage for Chinese enterprises 'going out'. In 2008, the international financial crisis led to declining economic growth in many countries and a lack of demand, depressing international prices of staple products and resulting in a serious shortage of capital mobility. In contrast, the crisis encouraged many Chinese enterprises, especially large SOEs with relatively adequate cash in-hand, to 'bargain-hunt'. However, overall, Chinese enterprises investing overseas seem to lack a clear and long-term strategy, especially in acquisition and integration.

An investment opportunity and potential benefits will not automatically produce genuine profits. Comprehensive and clear strategic planning is a key factor to realising this fundamental aim. Chinese enterprises have strategic planning flaws in their use of overseas FDI: first, they usually only consider price and accessibility, not investment objectives that are consistent with their overall development goals; second, they do not have a long-term business plan or a clear picture of the acquisition's future direction; third, their due diligence is inadequate for the investment objectives, resulting in a failure to discover the risks; fourth, they do not have a fully considered integration plan before the transaction.[47]

One of the reasons for this lack of strategic planning is that the enterprises do not have a clear knowledge of their own business. The purpose of overseas FDI is to optimise resource allocation, introduce advanced technology, achieve economies of scale and promote the rapid expansion of production and capital. Corporate investors must correctly assess their competitive and strategic position and integrate human resources, which is something that many Chinese enterprises seem ill-prepared for. As Vice-Premier Wang Qishan pointed out, in relation to the Chinese entrepreneurs' impulse for overseas acquisition after the 2008 financial crisis, overseas M&A is not just about the money. He warned of the need to answer these questions first: 'Can you buy out? Can you manage it? Do you have confidence about your own management ability? Have you analysed the cultural differences between the two sides yet? Have you ever studied the local labour union relations?'[48]

The lack of strategic planning is closely related to the external institutional environment in which enterprises operate. Currently, enterprises that invest or are planning to invest overseas are subject to Chinese overseas investment policy. The Chinese government's legal protection of outward FDI is characterised by the lack of a unified, stable and authoritative legislation and overlapping or conflicting policies from different management sectors, which substantially reduces the efficiency of Chinese overseas FDI. In particular, the Chinese government has few policies in place that encourage and support entrepreneurs overseas. The Chinese government cannot take full advantage of mobilising the requisite resources under its auspices to address the market failures of information, and is not involved in the development of international rules for cross-border investment either.[49] More fundamentally, the government's industrial policies in the relevant enterprises cannot provide the correct incentives. The ultimate purpose of overseas FDI is

to co-ordinate domestic and international markets and resources, which means in essence importing resources for use in China rather than simply exporting goods, services, or soft power.[50] Overseas FDI can play an important role in promoting enterprise reform, improving governance and building multinational corporations. However, in recent years, the 'going out' strategy emphasised securing resources, focusing on investment in energy and mineral resources, an approach that does not take into account issues such as brand or sales channel development and innovation. As a result, enterprises inevitably see overseas FDI as involving quick successes and shortsighted behaviour, not strategic thinking and investment planning.

FDI IN COUNTRY RISK ASSESSMENT

Although in recent years more studies have appeared on the environments and risks of China's overseas FDI, few comprehensive studies focus specifically on the country risks of China's overseas FDI around the world. In 2009, the *Outward FDI and Co-operation Country (region) Guide* (hereinafter referred to as the report) was jointly published by the Chinese Academy of International Trade and Economic Co-operation, the Investment Promotion Agency of Ministry of Commerce (People's Republic of China) and Chinese embassies business sectors. The report gives a complete and objective description of the investment environments in host countries and/or regions, noting which types of investment risks exist. The report appears to reflect the local data, uses consistent standards when comparing countries and regions, and can be regarded as the authority on country risks of overseas FDI.

The report includes a total of 160 countries and regions in the world, distributed over six continents (Asia: 36; Africa: 47; Europe: 46; North America: 2 (US and Canada); Latin America: 21; Oceania: 8).

A text-based interpretation of quantitative analysis was used to analyse the report. The main external risks faced by Chinese overseas FDI were divided into seven categories:

1 political risk, including political stability and administrative efficiency;
2 sovereign risk, including national treatment and market openness;
3 security risk, the threat of terrorism, epidemics and other physical threats;
4 legal risks, the integrity of the legal systems, Chinese enterprises' familiarity with legal systems and litigation costs in host countries (regions);
5 cultural risk, mainly cultural integration and the extent of friendliness towards China's overseas FDI;
6 risks of labour unions and stakeholders, the influence of main labour union forces and other external stakeholders, employment convenience and labour costs; and
7 environmental risk, the responsibility of environmental protection required by the host country.

The overall risk index of an individual country or region was achieved by averaging the seven types of risk. The qualitative and quantitative analyses of risks were based on the content analysis method. First, the nature of risk was identified, according to the text language. Then, the strength of these various types of risks was manually evaluated

using a 5-point Likert-scale, whose grades depended on words frequency extraction and language characterisation.

The geographical distribution of the overall risk index

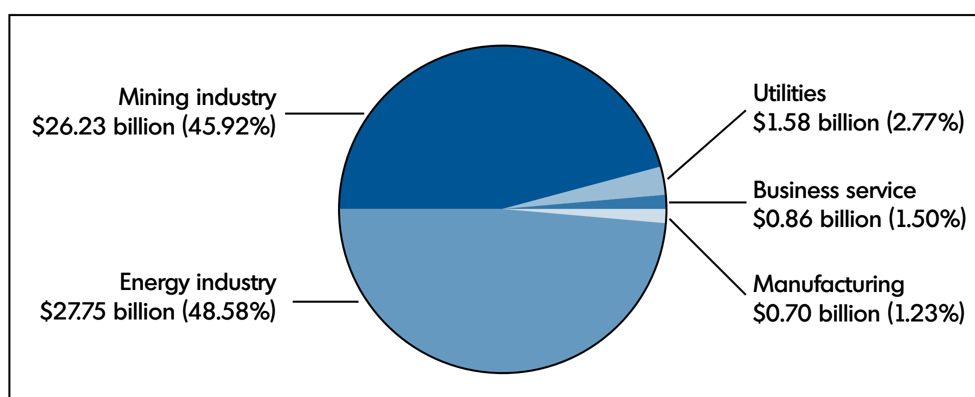
After estimating the risk index of China's overseas FDI in all continents (see Table 5), a cross analysis was conducted by combining the data of non-financial overseas FDI stocks and flows in 2008. A BCG matrix[51] was generated by combining the risk index with the geographical distribution of China's overseas FDI. Being similar to a SWOT analysis, the matrix was analysed using similar methods.[52]

Table 5: The risk index of China's overseas FDI in six continents

	Asia	Africa	Europe	US & Canada	Latin America	Oceania
Risk index	3.49	3.61	3.78	3.65	3.37	3.67

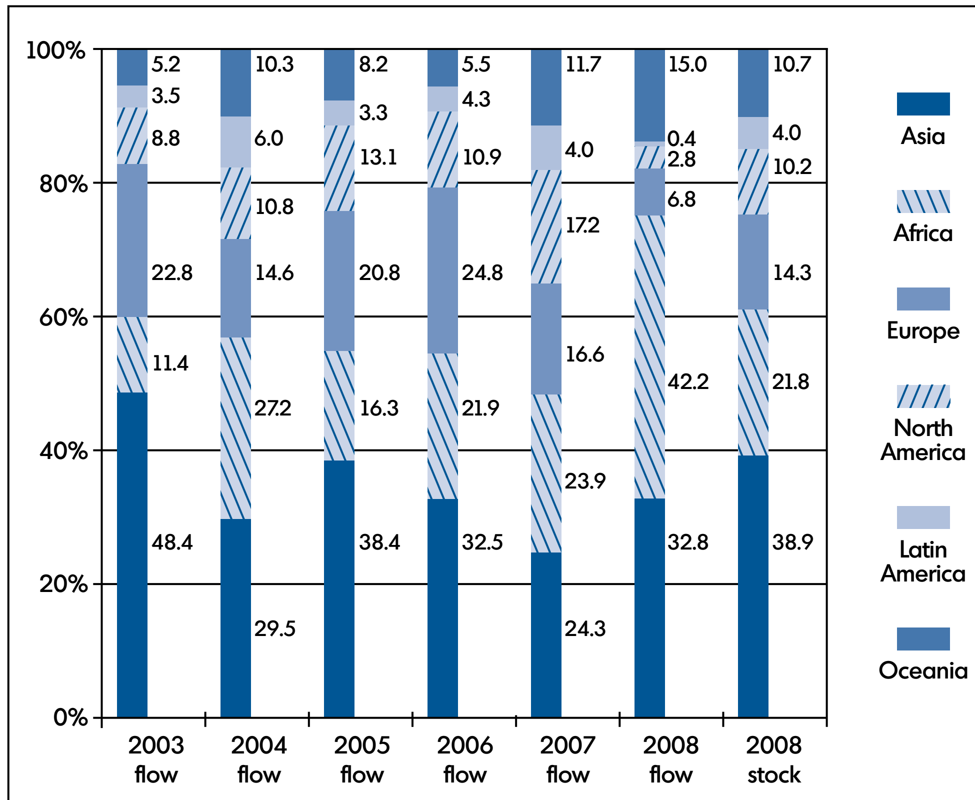
Based on the geographical distribution of the total overseas FDI stocks to the end of 2008, China's non-financial overseas FDI is at high risk in four of the six continents. The share of FDI stocks in Asia is the highest of the six continents (see Figure 2). The extent of investment is lower in Europe, Latin America and Oceania respectively, but the risks are ranked comparatively higher, making them more difficult areas for investment. Moreover, special attention should be given to Australia, as the country has absorbed most of China's overseas FDI for years. The US and Canada share a lower distribution ratio and the least risk, which makes them potential destinations (long-term) for China's overseas FDI. At present, China's investment in Africa represents a higher proportion of China's overseas FDI and seems to carry fewer risks, making the continent a unique and high-quality investment area.

Figure 1: Distribution of China's overseas industrial M&A transactions, 2008–2009



Source: Calculated by the author from existing statistics

Figure 2: China's overseas FDI per continent



Source: Annual *Statistical Bulletins of China's Outward Foreign Direct Investment*. In 2003–2007: Non-financial outward FDI data. In 2008, the flows and stock are all outward FDI

As Figure 2 shows, Africa occupied the largest share of investment flows in 2008, a sign of its prominent position as an investment location. Oceania (actually Australia) is obviously also a valuable investment destination, while attention should be paid to the full potential of the US and Canada, whose regional advantages are weakening. Although higher investment risk has always been a factor in Europe and Latin America, their share decreased in 2008.

The overall coverage of seven types of risks

The seven types of risk have different exposure in the 162 countries and regions, and so a cross analysis was carried out that combined the coverage and the degree of risk. According to the report, the highest coverage related to labour unions and stakeholders risk (85.6%) and political risk (85%) in 137 and 136 countries and regions respectively, followed by legal risk (76.9%) and environmental risk (76.3%). Cultural risk had a coverage rate of 71.3%, while security risk and sovereign risk carried the lowest risk, at 46.9%.

Table 6: The coverage rate and risk index of seven types of risks

	Political risk	Sovereign risk	Security risk	Legal risk	Cultural risk	Labour union risk	Environmental risk
Coverage rate of risk (%)	85.00	46.90	46.90	76.90	71.30	85.60	76.30
Risk index	3.45	3.71	3.37	3.70	3.11	3.87	3.94

Based on the matrix that combined the index of seven risk types with risk coverage rates, the most common and severe risks for China's overseas FDI are: labour unions and stakeholders, legal risk and environmental risk. Although political risk and cultural risk are common, the problem is not serious. Security risk always has a large influence, but the probability and severity of the problems are not obvious. Finally, the effect of sovereign risk will be more serious but this risk only appears in certain countries and is not a universal phenomenon.

The distribution of various types of risk in different countries/regions

An investment risk analysis was created for different levels of economic and social development of countries and regions, using the World Bank's income classification. According to the World Bank, the 160 countries and regions in the report are divided into five categories: high income (OECD[53]), high income (non-OECD), upper-middle income, lower-middle income and low income. The overall index values of seven types of risks were calculated in the five categories of countries and regions (economies), which were sorted in ascending order for every type of risk.

1 Political risk

In general, high-income economies would be expected to have the lowest political risk, as their economic and political systems are more mature, their societies more stable, and the administrative efficiency of their governments more satisfactory. As such, the lower the economy's income is, the higher its expected risks. However, according to the statistical results, the highest political risk was not carried by lower-income economies, but by lower-middle income economies and upper-middle income economies, which are mainly from South-East Asia, South Asia, West Asia, Latin America, West Africa, Southern Africa and transition economies, where political stability and corruption are major issues.

2 Sovereign risk

The least-developed, low-income economies have a lower level of sovereign risk, which is in some respects counter-intuitive. A possible explanation for this result is that such economies are mainly from sub-Saharan Africa and South Asia, where leaders are less likely to be replaced and favourable conditions are offered to attract foreign investment. So, low-income economies have a lower probability of risks such as nationalisation.

3 Security risk

The severity of risks (such as public order, terrorism, epidemic diseases and other causes of personal security risks) is in inverse proportion to the per capital income level. This reflects the relationship between the level of economic and social development and the investment environment. The strength of such a risk is the same for investment from any country, including China.

4 Legal risk

Interestingly, although both groups belong to high-income economies, the legal risk faced by China's overseas FDI was not the same in OECD and non-OECD countries. As most of the non-OECD high-income economies have smaller economic aggregates, they cannot attract or retain real direct investment. Instead they may simply develop offshore financial business, becoming international tax havens. The OECD economies are advanced countries with basically sound legal systems. Many of these OECD countries have a common law system that differs from China's legal system, which means that Chinese companies often have to pay higher legal adaptation and litigation costs.

5 Cultural risk

Most of the low-income economies, mainly in sub-Saharan Africa and South Asia, maintain friendly diplomatic relations and traditional friendship with China and have a higher degree of acceptance of Chinese overseas FDI.

6 Labour unions and other stakeholder risks

Generally the labour union movement and labour costs are highly correlated to the extent of local economic development and income levels. As mentioned earlier, non-OECD high-income economies have lower economic aggregates and small real investment projects, but provide registration services, which makes labour union intervention and labour costs meaningless.

7 Environmental risk

In general, there is a trade-off between environmental protection and economic development in many countries or regions. Local environmental protection requirements are therefore in line with development and income levels. Lower-middle income economies are mainly from less advanced industrialised countries in Asia and Africa, where the industrial model is labour and resource-intensive. Therefore, the required environmental responsibilities are relatively lenient.

The main risks of Chinese overseas FDI were analysed in greater depth by submitting the seven types of risk to a factor analysis. The number of factors was decided according to whether their respective eigenvalue was greater than one. Three factors were extracted whose cumulative variance contribution rate was 76.798%. The maximum variance orthogonal rotation determined that factor 1 consisted of political, legal and cultural risks; factor 2 comprised union, security and sovereign risks; while factor 3 was environmental protection risk. The three factors were named: system risk, interest groups and majeure risk, and environmental liability risk. Therefore, generally speaking, the main barriers to Chinese overseas FDI are caused by incompatible legal, political and social systems. This

means that a lot of painstaking work remains if China is to improve its understanding and integration into the international formal and informal systems. Moreover, China's 'going out' strategy must be a process of integrating into the international system, and adequate attention must be paid to the interest groups, social and political movements and the supply chain in host countries. Chinese overseas FDI should also be committed to following the international trend of responsible environmental protection, in order to avoid social and political risk arising from ecological problems.

Table 7: Index of seven types of risks in five categories of economies

	Political risk	Sovereign risk	Security risk	Legal risk	Cultural risk	Labour union risk	Environmental risk
High income: OECD	2.46	3.58	2.12	3.91	3.59	4.04	4.64
High income: non-OECD	3.20	3.50	3.00	3.29	3.46	3.41	3.93
Upper–middle income	3.71	4.06	3.45	3.61	2.89	4.06	4.15
Lower–middle income	3.84	3.70	3.50	3.92	3.18	4.03	3.48
Low income	3.56	3.56	3.70	3.69	2.62	3.56	3.61

Figure 3: Geographic distribution and risk index of China's overseas FDI stocks in 2008

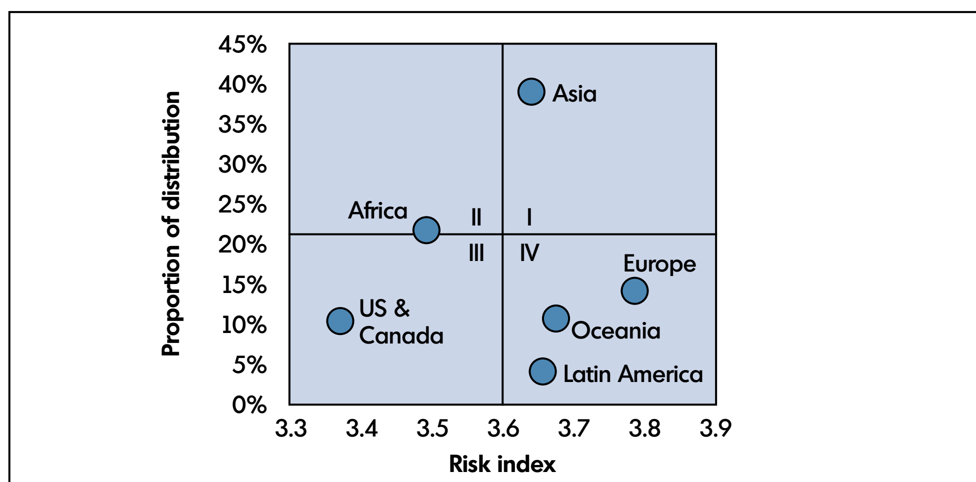


Figure 4: Geographic distribution and risk index of China's overseas FDI flows in 2008

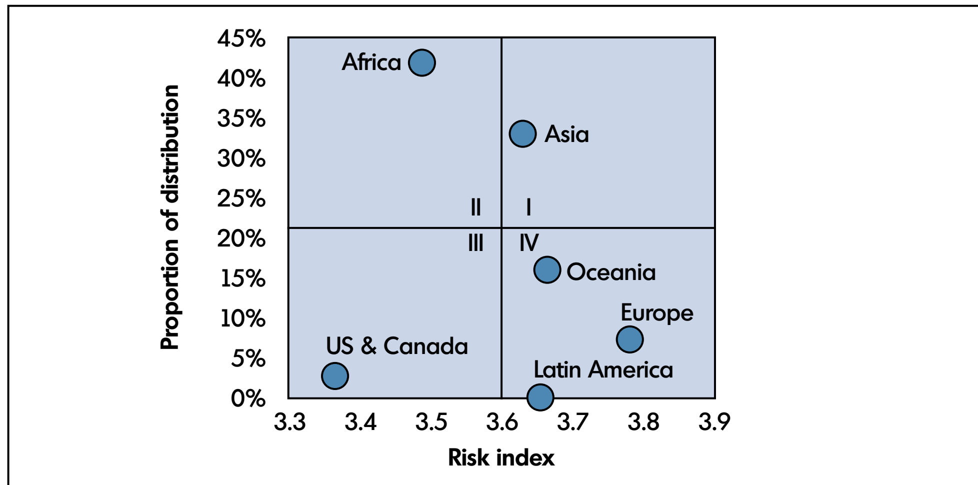
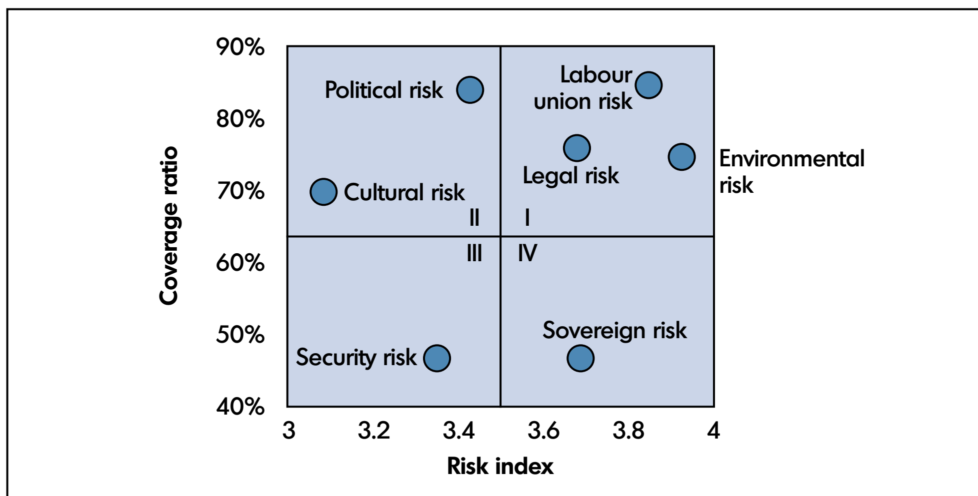


Figure 5: The coverage rate-risk index matrix



CONCLUSION

After analysing the current situation and main features of China's outward FDI in 2008–2009, the losses suffered and the major risks faced, the preliminary conclusions are: (1) China's overseas FDI has experienced a rapid development but is still low in absolute terms, while the concentration trend of geographical and industrial distribution is obvious. This indicates that the 'going-out' strategy has been faithfully implemented, but also contains high risks. (2) The risks of China's overseas FDI emanate from four main aspects: breach of contract and unexpected transactional costs; exchange loss; premium transactions; and failure of integration. (3) Overseas FDI faces systemic risks. The internal causes from the Chinese side include a high concentration of investment; excessive government intervention; low international business management ability; and a lack of

overseas investment strategies. (4) Based on a country risk analysis of China's overseas FDI, the most important issues are the legal, political, social and other institutional differences and conflicts. This indicates that China, host countries and the international community need to continue to strengthen co-operation and mutual institutional transformation. And, as importantly, as an emerging world power, China should take on more international responsibility.

ENDNOTES

1 Jiang Zeming's address at the meeting of the Political Bureau of the Central Committee on 20 January 2000. 'Jiang Zeming Analects', 2, Beijing: People Publishing House, 2006, pp. 569.

2 According to *China Statistical Yearbook 2008*, outward FDI is defined as an economic activity whereby China's domestic investors establish or purchase enterprises abroad or outside of customs territory by cash, intangible or tangible assets etc. with a view to getting the right of control to operate or manage the enterprise.

3 Chen Weishu argued that China's overseas interests exist outside the effective jurisdiction of Chinese sovereignty. The narrow concept is the security of life, property and activities for overseas Chinese organisations and citizens. The broad concept includes all kinds of effective agreements and contracts related to the interests of Chinese government, corporations and citizens, and the dignity, reputation and image fairly accessed by official and civil society. See Weishu C, 'General vision of China's overseas interests', *International Review*, 2, 2009. Su Changhe argued that China's overseas interests are defined as a type of national interests which entitled in international institutions and distributed in extra-territorial areas within the established global linkages of domestic multi-actors. See Changhe S, 'On China's overseas interests', *World Economics and Politics*, 8, 2009.

4 Nominal GDP of Cayman Islands is KYD 2.03 billion (about $2.5 billion). Cayman Islands Government website, http://www.gov.ky/portal/page?_pageid=1142,1481068&_dad=portal&_schema=PORTAL). The 2006 Statistical Bulletin of China's Outward Foreign Direct Investment demonstrates that China's direct investment flow to Cayman Islands is $7.83 billion. The GDP of British Virgin Islands was about $1.1 billion in 2007. Data calculated according to the British Ministry of Foreign Affairs, http://www.fco.gov.uk/en/travel-and-living-abroad/travel-advice-by-country/country-profile/north-central-america/british-virgin-islands?profile=economy. The 2007 Statistical Bulletin of China's Outward Foreign Direct Investment demonstrates that China's direct investment flow to British Virgin Islands is $1.88 billion. By contrasting these figures, it is obviously very difficult to believe that these investments are truly settled locally.

5 Note that excluding the Cayman Islands and British Virgin Islands investment.

6 Note that excluding Hong Kong, Macao and Taiwan investment.

7 This paper consolidated the completion of non-financial sector M&A cases that Chinese enterprises announced between 1 January 2008 and 31 December 2009. The top 20 transactions are listed at the end of the paper. Unless the source is indicated, the author calculated the cross-border M&A transactions from publicly available reports in China and overseas, corporate annual reports and other notices or orders. Due to the wide variety, the sources cannot all be listed.

8 Some independent research institutes have indicated that for many years, cross-border M&A of Chinese enterprises focused on energy, mining and utilities. Deloitte's study showed

that from 2003 to the third quarter of 2009, acquisitions by Chinese enterprises in these sectors accounted for 29% of their cross-border M&A activities, and 66% of the total value of transactions. In the first three quarters of 2009, deals acquisitions completed by Chinese enterprises in these industries accounted for about 41% of their cross-border M&A deals, and up to 93% of the deals value. See Deloitte China, *China's rise: New areas of cross-border mergers and acquisitions*, November 2009, http://www.deloitte.com/assets/Dcom-China/Local%20Assets/ Documents/Services/Global%20Chinese%20Services%20Group/cn(zh-cn)_gcsg_EmCnNewFront_011209.pdf. Thomson Reuters' study confirmed that in 2009 China's cross-border M&A focused on the energy and raw materials sectors, 'Fourth quarter 2009 financial advisors: Mergers & acquisitions review', http://online.thomsonreuters.com/DealsIntelligence/Content/Files/4Q09%20MA%20Financial%20Advisory%20Review.pdf.

9 Hongmei H, 'M&A: Systemic strategy is more important', from the website of the Chinese Academy of International Trade and Economic Co-operation.

10 Development Research Center of the State Council, 'An analysis to the strategy on M&A of Chinese large oil enterprises', DRC net Monthly Analysis of Petroleum and Chemical Industry Report, 14 August 2009.

11 You Z, 'The reasons of "going out" failure, three strategies experts given', *21st Century Business Herald*, 9 August 2007.

12 RMB: renminbi (Chinese currency).

13 Chuan J, 'Hurried withdraw overseas acquisitions: China's 200 billion RMB tuition test waves', *China Securities Journal*, 18 December 2008.

14 CAD: Canadian dollar.

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16 'Verenex shareholders approve sale to Libyan government arm', *Wall Street Journal,* 14 December 2009, http://online.wsj.com/article/SB10001424052748704201404574590080869123634.html.

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18 'Congo (DRC) announced details of the $9.25 billion transaction with China', *FT Chinese*, 12 May 2008, http://www.ftchinese.com/story/001019267.

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20 'China's largest investment in Africa delay', *FT Chinese*, 10 February 2009, http://www.ftchinese.com/story/001024589.

21 IMF, statement by IMF staff mission to the Democratic Republic of the Congo. Press Release, 08/346, 23 December 2008. See http://www.imf.org/external/np/sec/pr/2008/pr08346.htm.

22 Wallis W, 'Chinese deal threatens IMF aid for Congolese', *Financial Times*, 15 May 2009. See http://www.ftchinese.com/story/001026447/en.

23 IMF, 'Democratic Republic of the Congo: Request for the rapid-access component of the exogenous shocks facility and report on the 2008 staff monitored program', *IMF Country Report,* 09/317, 17 November 2009. See http://www.imf.org/external/pubs/ft/scr/2009/cr09317.pdf.

24 'IMF put pressure on China and the DRC shrinks agreement', *STNN,* 20 August 2009. See http://www.stnn.cc/chinafin/200908/t20090820_1088718.html.

25 In January 2008, the exchange rate of RMB against the dollar increased by 7.5% over the same period of previous year. In January 2009, the exchange rate had increased by 6.0% year-on-year. (Data calculated according to the People's Bank of China's website statistics.)

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53 Organisation for Economic Co-operation and Development.

APPENDIX

20 largest cross-border M&A by Chinese enterprises (non-financial sectors), 2008–2009

Rank	Date of publication	Target company	Transaction content	Target industry	Target location	Buyer company	Location of the seller company	Value of the transaction ($ billion)
1	February 2008	Rio Tinto Plc	12% equity	mining industry	Britain	Alcoa Inc and Chinalco	Britain	14.000
2	August 2009	Addax Petroleum Corporation	100% equity	energy	Nigeria, Gabon and Iraq's Kurdish region	Sinopec International Exploration and Production Corporation (Sinopec Group)	Switzerland	7.560
3	July 2008	Awilco Offshore ASA	Full acquisition	energy	Norway	China Oilfield Services Limited (CNOOC subsidiary)	Norway	3.777
4	April 2009	JSC Mangistaum unaigas	100% ordinary shares	energy	Kazakhstan	CNODC (CNPC subsidiary), KazMunaiGas	Kazakhstan	3.300
5	October 2009	Felix Resources Limited	Conditionally approved the acquisition of 100% equity	mining industry	Australia	Yanzhou Coal Mining Company Limited	Australia	3.200
6	March 2008	Tuas Power Limited	100% equity	energy	Singapore	SinoSing Power Pte Ltd (China Huaneng Group)	Singapore	3.103
7	September 2008	Awilco Offshore ASA	Overall M&A	energy	Norway	China Oilfield Services Limited (CNOOC subsidiary)	Norway	2.500
8	December 2008	Tanganyika Oil Company Ltd	All shares	energy	Syria	Sinopec	Canada/ Sweden	2.000
9	November 2009	PT. Bumi Resources Tbk	Advanced mortgage debt	mining industry	Indonesia	China Investment Corporation	Indonesia	1.900

Rank	Date of publication	Target company	Transaction content	Target industry	Target location	Buyer company	Location of the seller company	Value of the transaction ($ billion)
10	August 2009	ASOC Mackay River and Dover oil sands projects	60% equity	energy	Canada	PetroChina Company Limited (CNPC subsidiary)	Canada	1.740
11	November 2009	AES Corporation	15% equity	Public utilities	US	China Investment Corporation	US	1.580
12	July 2009	Teck Resources Limited	17.2% equity	mining industry	Canada	China Investment Corporation	Canada	1.500
13	June 2009	OZ Minerals	Conditional offer to acquire the main assets	mining industry	Australia	China Minmetals Non-ferrous Metal Company Limited (China Minmetals Corporation)	Australia	1.386
14	May 2009	Singapore Petroleum Co.	45.51% equity	energy	Singapore	PetroChina	Singapore	1.020
15	August 2009	Fortescue Metals Group	17.34% equity	mining industry	Australia	Hunan Valin Iron & Steel Group	Australia	0.985
16	September 2009	JSC KazMunaiGas Exploration Production	11% of global depositary receipts, equity is not clear	energy	Kazakhstan	Fullbloom Investment Corporation (China Investment Corporation)	Kazakhstan	0.939
17	September 2008	Midwest Corporation Ltd.	98.52% equity	mining industry	Australia	China Steel Corporation	Australia	0.902
18	November 2009	Noble Group Limited	14.91% equity	commercial service	Singapore	China Investment Corporation	Hong Kong	0.858
19	March 2008	AED Oil in Puffin and Talbot	60% assets	energy	Australia	Sinopec	Australia	0.559
20	November 2009	Indophil Resources NL	100% equity	mining industry	South-East Asia	ZIJIN Mining Group Co., Ltd	Australia	0.504

Source: Based on domestic and international public reporting, corporate self-disclosure of information

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