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What is China seeking from Africa? An analysis of the economic and political determinants of Chinese Outward Foreign Direct Investment based on Stochastic Frontier Models☆,☆☆

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ABSTRACT

Chinese investment in the African continent is rapidly spreading. Unlike the Maoist proselytism that defined past diplomatic relations between China and a few African countries, the current distribution of current Chinese Foreign Direct Investment has economic motivations. However, our study also found that Chinese investors are attracted to the political and institutional particularities of each African country. Using Stochastic Frontier Models, it has been concluded that dynamic national markets with a large population and significant forest area are the most preferred for the allocation of Chinese Foreign Direct Investment in 48 African countries between 2003 and 2010. According to our results, the efficiency of this allocation can be maximized by increased political stability and regulatory quality, with government effectiveness being an additional factor required for this efficiency.

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1. Introduction

Foreign Direct Investment continues to be a pressing issue. Most scholars recognize that Foreign Direct Investment (FDI) serves not only as a source of economic growth for recipient countries but also signals the maturity of the recipient economies. More recently, FDI has become a crucial issue for emerging markets. Over the last decade, emerging countries have not only become the primary targets of FDI but have also assumed an active role as investors, as is the case in China, India and Brazil (Carvalho, Duysters, & Costa, 2010; Hill & Jongwanich, 2011).

The case of China exhibits particularities that will be discussed in the following sections. However, this study will focus on Chinese FDI in African countries. The relationship between China and Africa is intriguing for several reasons. Firstly, a relationship that was modest in the past and restricted to a few African partners has now spread over the continent. Secondly, although Maoist

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China sustained a certain political proselytism in their diplomatic relations in the past, Chinese investors are now motivated to invest in Africa for other reasons. Finally, we will also analyze the social and political variables of African countries that determine how Chinese FDI is distributed in each African country (He, 2010; Yao, 2009; Bhaumik & Co, 2011).

This study discusses Chinese FDI in Africa. The traditional economic dimensions that affect the distribution of FDI will be analyzed. We will also test the ways in which political dimensions (such as Political Stability, the Control of Corruption or Government Effectiveness) can enrich conventional explanations. To do so, Stochastic Frontier Models and methods for estimating efficiency scores will be utilized (Battese & Corra, 1977).

There are three main contributions from this paper. First, it will list a statistically significant set of determinants for the Chinese Outward Foreign Direct Investment in Africa. Therefore, if African policy-makers are interested in attracting Foreign Direct Investment, they will find a list of dimensions to manage in this paper. Second, this paper will provide estimates for the efficiency scores of African countries. Identifying the most efficient African cases is important for understanding their relative success and the relative failure of other cases. Finally, given the complexity of the Sino-African relationships and the originality of this methodology, this paper will contribute to the emerging literature on Chinese Outward Foreign Direct Investment and African Inward Foreign Direct Investment. The structure of this article is as follows. Section 2 briefly reviews the literature on FDI, the role of emerging economies and the Chinese and African relationship. Section 3 describes the empirical design, data and methods and discusses the results. Section 4 concludes the article.

2. Foreign Direct Investment — a review of the literature regarding new actors on an old stage

2.1. The rising role of emerging economies

Although Foreign Direct Investment (FDI) is a historical issue, it continues to be a pertinent issue today because of the “entrance of capitals,” the “generation of local income,” and the “local prestige” that FDI promotes in the economies that receive the investment.

Before discussing these forces, “Foreign Direct Investment” must be defined. Following Petranov (2003), we identify “Foreign Direct Investment” as “an international investment, in which the direct investor, the resident of a foreign economy, acquires a lasting interest.” Similar definitions are put forth in Barrios, Dimelis, Louri, and Strobl (2004), Kolstad and Villanger (2008), Sanda and Dana (2007), and Ciobanu (2007). Accolley (2003) provides an extended discussion of various notions of “Foreign Direct Investment.”

In addition to defining Foreign Direct Investment as a “lasting interest” (Petranov, 2003), it is important to identify the forms of Foreign Direct Investment. Following Accolley (2003), Foreign Direct Investment assumes three main forms: the acquisition of lands, civil structures, or buildings; the acquisition of firms, holdings and companies; and the use of lands, civil structures, buildings, and firms or other productive structures.

The predominance of these forms has changed over the last few decades. As Strandskov and Pedersen (2008) argue, the first forms were concentrated in the simple acquisition of lands or buildings by single entities; today, however, complex systems of contracts allow joint-ventures, for example, the acquisition of shares of firm assets or parts of durable goods (Salavrakos, 2006). Other more detailed examples are provided by Merlevede and Schoors (2005) and Baltagi, Egger, and Pfaffermayr (2007).

The postwar period witnessed a continued increase in Foreign Direct Investment worldwide, which spurred several studies on the phenomenon (Suntum, 2005). The study of Foreign Direct Investment continues to be prompted by several factors. The main factor positively relates Foreign Direct Investment to economic growth (Choe, 2003; Ok, 2004; Osinubi & Amaghionyeodiwe, 2010; Popa, 2010). The second factor is related to national studies. Recently, it has been found that the dimensions attracting Foreign Direct Investment to country A are not the same dimensions attracting Foreign Direct Investment to country B. Consequently, this evidence led to an increase in the number of studies on each country's factors of attractiveness. Finally, most studies highlight the net advantages of Foreign Direct Investment for a given country; if there is this type of consensus among scholars,[1] studying Foreign Direct Investment is crucial for developing economies and societies (Lim, 2001; Hansen & Rand, 2006). Recently, the study of Foreign Direct Investment has acquired a new focus. Several studies (Hansen & Rand, 2006; Bouoiyour, 2007; Carvalho et al., 2010; Kim & Yang, 2011) have focused on the particularities of emerging economies' FDI (mixture of causes, no longer net recipients of Foreign Direct Investment, and political and social concerns).

2.2. The inward Foreign Direct Investment in Africa

As discussed by Henley, Kratzsch, Kulur, and Tandogan (2008), Africa has been receiving FDI from various investor countries. From 1990 to 1997, Africa's most important investor countries were France, Germany, United Kingdom and the United States of America (UNCTAD, 1999). However, according to the UNCTAD (2007), in 2002, such emerging countries as China, India, and Malaysia became sources of more significant values of Outward FDI (OFDI) to Africa than France, Germany and the United States of America. Studies such as these and those of Scherr (2004) and Abid and Bahloul (2011) have shown that African countries exhibit a number of important areas of attractiveness for investors, namely unexplored natural resources.

[1] A few studies that highlight the “costs” of Foreign Direct Investment to the recipient countries have been conducted by Jenkins and Evans (1980) or Ivan and Iacovoiu (2008). Among other costs, we can also identify the excessive exploitation of natural resources, the unexpected pressures on national demand and the local supply of goods and services, or the “social dumping” that some cases have recorded.