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ESADE
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ESADEgeo-CENTER FOR GLOBAL ECONOMY AND GEOPOLITICS

Chinese Investment in Europe

2015-16

Promoters:

KPMG

Cuatrecasas, Gonçalves Pereira

Collaborators:

Ajuntament de Barcelona

Catalonia Trade & Investment

Generalitat de Catalunya
Government of Catalonia

WORD WORKS

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Foreword

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Growth in the Chinese economy may well be trailing off, but global investments made by Chinese companies and investment funds are soaring to record levels year after year. While already a world power in terms of manufacturing output, merchandise exports and as a holder of reserves, in recent years China has also become one of the world's leading exporters of capital. In 2013 China ranked as the third largest investor in the world, behind only the United States and Hong Kong (China). Its investments already encompass 184 countries.

In the global arena, investment from China is a dynamic phenomenon that goes hand in hand with, and mirrors, the shift of the Chinese economy itself and of its resident companies towards higher value-added activities, with the public sector allowing a greater margin for private initiatives. At present, Chinese investment is characterised by a scenario in which state-owned enterprises compete with private firms when moving into the external market. Investments are primarily made in the mining and quarrying industries and in natural resources, with emphasis also on significant technology projects. As the sectors that receive foreign investments are changing, more transactions are being undertaken in advanced economies, for example the European Union (EU) and the United States, rather than markets such as Latin America and Sub-Saharan Africa.

The number of transactions in the EU increased hugely in 2014 and thus far in 2015, reflecting China's growing interest in ploughing capital into this area of the globe. A combination of factors make the EU a prime target for China to expand its FDI. Not only is it a sizeable market that enjoys great stability both politically and economically speaking; it also has first-class infrastructure and a wealth of human and technological capital. Moreover, as the number of investments rises, so the strategy and interest of Chinese firms with regard to investing in the EU become more apparent, the British real estate sector and medium-sized German industrial firms in particular being targeted.

With a view to gaining further insight into China's investor relations with the EU, and the ensuing economic and business factors, ESADE Business School and ESADEgeo – together with our partners KPMG, Cuatrecasas, Gonçalves Pereira, ACCIO - Catalonia Trade and Investment, and the Ajuntament de Barcelona – have launched the second report on Chinese FDI in Europe. This is a pioneer undertaking in Spain and the only report on Chinese investments in the EU to be published annually in Europe. The report was drawn up as part of the most extensive initiative embarked upon by ESADE China Europe, a business platform set up to raise awareness and boost economic and institutional relations with Chinese enterprises in Europe.

This second edition of the report has the same structure as last year's report. The first chapter contains an in-depth analysis of the main characteristics of Chinese investment worldwide, with particular emphasis on the principal transactions and trends and the impact of Chinese capital on the EU. The second chapter looks at the main sectors selected for investment in Europe and reflects the growing number of industries targeted by Chinese FDI. In the third chapter, the focus is on the expansion of Chinese investment in Spain. This report also contains a number of external contributions concerning matters of interest relating to the increasing presence of Chinese enterprises around the world, including the Silk Road, the Asian Infrastructure Investment Bank and International Expansion of Chinese Firms from a Legal Perspective.

Javier Solana,
Chairman of ESADEgeo

Executive Summary

Executive Summary

• Doubts concerning the accuracy and sustainability of the macroeconomic outlook presented by the Chinese government, coupled with the depreciation of the Yuan in August, have caused a crisis of confidence among international investors. As a result, since the summer of 2015 **Chinese capital markets have been in considerable turmoil**, with a 40% drop in the country's stock market. The true extent of this financial crisis and its impact on the international expansion of Chinese firms **will not be clear until macroeconomic indicators are published at the end of 2015**. In the meantime, data show that China has become the world's third largest investor, and trends suggest that Chinese companies will continue to internationalise.

• In 2014, driven by extraordinarily large reserves (USD 3.7 trillion), a determined push to deregulate and a need to acquire foreign assets, **China became the world's third largest investor** in terms of investment flows, surpassed only by the United States and Hong Kong (China). Chinese FDI is set to continue growing in the medium term and President Xi has estimated that it will exceed **USD 1.25 trillion over the next ten years**.

• To date, around **15,300 Chinese firms** have invested abroad, amassing an **FDI stock of USD 776,500 million** at the end of 2014 according to MOFCOM. Outbound Chinese FDI has generated almost **two million jobs abroad and funnelled USD 37,000 million in taxes** into the investee countries.

• In terms of the **FDI format**, this is fairly equally distributed amongst shareholdings (31.2%), reinvestment of profits (39.9%) and other investments (28.9%). Notably, almost all of the Chinese companies that have invested abroad are based in the country's **coastal provinces** and there is a growing proportion of **privately-owned companies – now representing 48.8% of foreign investment** – compared to state-owned enterprises.

• Chinese foreign investment now extends to **184 countries**. According to the latest official data from the end of 2013, 67.7% of the country's FDI stock is in Asia, 13% in Latin America, **8% in the European Union**, 4.3% in North America, 4% in Africa and 2.8% in Oceania. In any case, these volumes of investment are a result of transactions being channelled through **offshore financial centres (OFCs)** or due to **round tripping**. There are indications that if corrected for these two effects, investment in Asia and Latin America would be lower than that shown in official data, while that in the European Union and North America would be significantly higher.

• Many major Chinese companies and sovereign wealth funds have undertaken **substantial investments globally for amounts exceeding USD 5,000 million**, reflecting China's considerable financial muscle: CNOOC (hydrocarbons), Minmetals and Chinalco (metals), Chemchina (chemicals), Sinopec (hydrocarbons), Shuanghui (agri-business), CCB and ICBC (finance) and CIC (sovereign wealth fund).

• Despite the slowdown in the Chinese economy, outbound FDI exceeded the USD 100,000 million threshold in 2013 for the first time ever, **and in 2014 China posted a new record high as an outbound investor, laying out USD 116,000 million, 15.5% more than in the previous year**. This volume is very close to the USD 119,000 million China has received in inbound foreign investment, bringing the country closer to being a net capital exporter.

• The EU is a key destination for investment by Chinese firms. According to official data from China's MOFCOM, **2,000 Chinese firms** currently have establishments in the EU; these **employ 47,000 people** and amass a cumulative investment of **USD 40,097 million**, i.e. 4 out of every 10 USD invested in developed countries.

• Over the past two years, there have been marked **trends in Chinese investment in Europe**. A larger number of transactions were carried out by **privately-owned companies**, with a greater proportion of **purchases of minority interests** rather than acquisitions, and increased **sector diversification**, with more real estate, hotel and agri-business firms in relative terms.

• Chinese investment in the EU reached an **all-time high in 2014, at USD 20,170 million, indicating growth of 117% compared to 2013** according to the Esade China Europe database. Notable transactions include the purchase of 35% of the Italian bank Cassa Depositi e Prestiti (CDP) Reti by State Grid in the electricity sector; the acquisition of 80% of the Portuguese financial institution Caixa Xeral by the Fosun Group; the purchase of the Dutch-based agricultural conglomerate Nidera by the food group COFCO; and the automotive firm Dongfeng buying into the French enterprise Peugeot.

• By countries, **Chinese investment in Europe is concentrated in the core economies of the region**. In 2010-2014, according to the ESADE China Europe database, the United Kingdom received 46.7% of total investment in the EU (USD 58,300 million), followed by Italy (21%), Portugal (10.6%) and France (9.5%). Investments in Greece and Eastern Europe are also of strategic importance to China.

• A number of factors will drive Chinese FDI in Europe over the coming years, including ongoing negotiations to sign a **new investment agreement**, Chinese citizens' **increased disposable income**, the **Juncker Plan**, new **joint investment vehicles** created by the Chinese government and a number of its European counterparts, megaprojects such as the **New Silk Road** and newly created institutions such as the **Asian Infrastructure Investment Bank (AIIB) and the New Development Bank (NDB)**.

• Globally, Chinese capital is now **invested in almost all economic sectors**, including business services and leasing, the financial sector, mining and extraction, manufacturing, retail and wholesale and transport. However, there is some degree of sector concentration according to geographical areas: greater investment in extraction and natural resources in Latin America and Africa and more substantial investment in the financial sector, manufacturing and technology in the United States and the European Union.

• Seven sectors accounted for 95% of Chinese investment in the EU from 2010 to 2014: **energy** (USD 18,170 million, 31.2% of the total), **real estate** (USD 13,350 million, 22.9%), **manufacturing** (USD 7,850 million, 13.5%), **agri-business** (USD 4,880 million, 8.4%), **the financial sector** (USD 4,250 million, 7.3%), **logistics, transportation and infrastructure** (USD 4,060 million, 7%) **and telecommunications and software** (USD 2,650 million, 4.5%).

• Chinese investment in Spain is a recent phenomenon, but is growing at a fast pace. According to official data from Spain, **93.8% of Chinese FDI in Spain since 2000 (€1,662 million) was carried out between 2012 and 2014**. Chinese FDI in Spain reached a record level of €610 million in 2014. In the first half of 2015 transactions continued in the real estate, hotel and agri-food sectors, following the trend at the European level.

• At present, around **75 Chinese companies are operating in Spain**. Over the past two years a number of groups and companies have invested in Spain for the first time, such as **the China Construction Bank, Dalian Wanda, the Fosun Group, the Bright Food Group and the HNA Group**. Other companies that are well established in Spain, such as Huawei, ZTE, Lenovo, Haier, Cosco, ICBC, Air China and KeewayMotors, have continued to expand their market shares and workforces.

• Investments in Spain, with a stock of almost **€2,000 million** just a few months before the end of 2015, are forecast to grow exponentially. According to the president of China's Chamber of Commerce, **over the next two to three years** China will invest up to **€3,000 million** in Spain, focused on the **real estate, tourism, renewable energy and agri-food sectors**.

• Analysis of investments from 2010 to 2015, interviews with management of Chinese companies in the ESADE China Europe Club and the results of a survey of 24 Chinese firms with investments in Spain show that the **inherent appeal of the Spanish market and its potential as a doorway to Europe and Latin America** are the two main reasons Chinese businesses invest in Spain.

• Over the past three years, Chinese firms were asked to rate the business climate in Spain on three occasions. In general, the rating was more than positive. The two most prominent positive factors are the **level of training of human resources and the quality of infrastructure**, above all ports and airports. Bureaucracy and the tax burden are the factors with the lowest scores.

• Lastly, the key challenges Chinese businesses face in terms of competition in Spain were identified and analysed. The two main hurdles were considered to be **brand recognition** and the **competitiveness of local firms**. Despite these obstacles, 90% of the companies surveyed considered that they had achieved their learning and financial objectives to a satisfactory or very satisfactory degree.

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CHAPTER I

Chinese investment in Europe

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Boxes

Charts and tables

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1.1 The path to a new Chinese economy

The Chinese economy expanded 7.4% in 2014, which is the lowest growth rate for the last 24 years and denotes a "soft landing" following a prolonged boom with spectacular average growth of 10.2% from 2000 to 2011. Forecasts from the International Monetary Fund (IMF) and the Chinese government for the coming years indicate a cruise speed of between 6% and 7% growth, implying a "shift in the norm" for China, a new economic scenario with more moderate growth moving forward. That said, if the current economic transition is successful, growth will be more sustainable and with higher added value. For 2015 the Chinese government set a growth target of 7%, which is precisely how much the economy grew in the first quarter of the year. In the year underway the IMF has slightly amended its forecasts for 2015, bringing its figures down three points to a predicted 6.8% growth in GDP. It has also reduced its growth forecast for 2016, from 6.8 to 6.3%. Without a doubt, the latest macroeconomic data coupled with stock market turbulence around the globe have dampened optimism, hinting at a cooling-off in the Chinese economy.

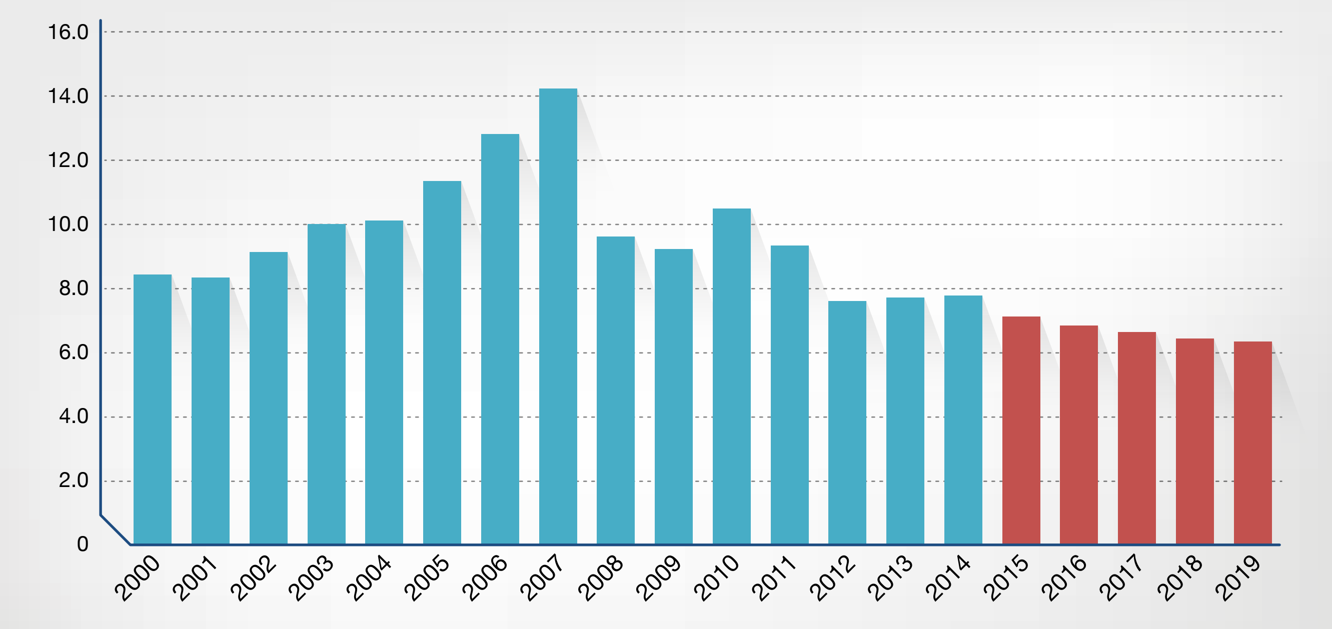
The foundations of the Chinese economic model, which opened the way for the country's rapid ascent up the development ladder to reach middle-income status[1], were primarily mass public investment and exports on the demand side, teamed with low value-added manufacturing on the supply side.

However, in recent years these growth sources have become visibly weary, forcing the government to strive for change in the model so as to prevent the country falling into the *middle-income trap*, characterised by deceleration in growth and stagnation in the standard of living.

This is because the factors that drove the rapid growth and gave rise to competitive advantages at the early stages of development can no longer serve to boost growth once the country attains middle-income status. China's progress was marked by an accumulation of production-related factors such as capital and employment. But the path to a higher level of development is through a continuous increase in productivity and, in particular, the total productivity of the factors involved. By way of example, the mass relocation of rural inhabitants to urban hubs generates a productivity shock, although the fall-out of that shock is limited. China faces a sizeable challenge in its quest to elude the middle-income trap: according to the World Bank, of 101 economies considered to have middle-income status in 1960, only 13 are currently high-income countries[2].

Over the last few decades, the Chinese economic model has generated substantial imbalances and bottlenecks in growth that have come to the surface in recent years. **Firstly**, in a setting of interest rate manipulation and substantial private savings, public investment was mainly funnelled into unproductive and inefficient projects.

Chart 1 Growth in Chinese GDP (2000-2019)



Source: IMF. World Economic Outlook Database. 2015.

[1] The World Bank classifies China as a middle- to high-income country.

[2] See: http://siteresources.worldbank.org/EXTPREMNET/Resources/EP98.pdf

These unsuccessful investments could amount to as much as USD 6.8 trillion (more than the GDP of Germany and France combined) according to calculations published recently by The Economist[3]. This affects financial institution balance sheets and local government accounts alike[4].

Secondly, the low value-added manufacturing model for exports has a substantial limitation: rising labour costs (which climbed 20% a year from 2008 to 2012[5]) due to economic development, resulting in an erosion of manufacturing competitiveness vis-à-vis foreign markets.

Thirdly, the hefty environmental degradation is giving rise to considerable social and economic problems. At present, less than 1% of Chinese cities meet the environmental standards set by the World Health Organisation (WHO), and environmental degradation cost 9% of domestic income according to the World Bank[6]. Fourthly, immigration has got out of control – more than 300 million people have migrated from rural to urban areas in the last 30 years, with 160 cities now having a population in excess of one million, while 14 have over five million inhabitants – and this represents a huge challenge for public services such as transport, healthcare, waste management and water treatment.

As such, to stay on the path towards becoming a high-income country, and to redress the imbalances described above, China must profoundly transform its economic model. On the aggregate demand side, private household and corporate consumption should gradually gain ground against public investment, while on the supply side the services sector and technology- and knowledge-based activities are expected to increase their contribution to GDP, to the detriment of low value-added manufacturing. In addition to these factors, China needs to undertake further substantial reforms, such as an overhaul of its financial system, interest rate liberalisation, infrastructure enhancements (including technology), as well as a tax reform to alleviate the pressure on local government public accounts. The Chinese government has been decisively addressing these challenges through a wide range of measures and projects already specified in the 12th Five-Year Plan (2011-2015), and which are set to be covered in more detail in the 13th Five-Year Plan, covering the 2016-2020 period.

The question is whether economic inertia in itself and the government measures in place are taking China towards a new economic model, whether the forecast new sources of growth have indeed been opening the way in recent years, and whether imbalances are being redressed. There is certain evidence of expansion in consumer spending as the driver of GDP, alongside lesser dependence on public investment and exports and an economic model in which services are gaining ground against manufacturing. Technology- and knowledge-based economic activities have also made headway in recent years. Consumer spending rose 3 points in 2014, up to 51.2%, while household disposable income also climbed 8%[7]. Nonetheless, instability in the real estate market, the slump in the labour market and declining economic and business expectations are set to hinder any increase in consumer spending in the short term. While private consumer spending gained ground, the contribution of investments to GDP growth slipped from 8.1% in 2009 to 4.2% in 2014, and negative expansion was posted for investments in fixed assets, sliding from 33% to 16% in the same period[8].

China is also seeing a change in its GDP mix on the supply side. From 2010 to 2013, the industrial sector's contribution to GDP growth contracted from 47% to 44%, with these three percentage points being picked up by the services sector, which contributed 46% instead of 43%[9]. This means that for the first time ever the services sector made a greater contribution to Chinese GDP than the industrial sector. Even so, the Chinese economy still has a lot of ground to cover before it can post similar ratios to those of advanced countries in terms of the GDP mix: the services sector represents 68% of the economy in Germany, 73% in Japan and 78% in the United States[10].

Moreover, China is making strides towards a production model that is more based on value-added activities and knowledge. The pace at which this process is moving forward may be questionable, but there is no doubt as to which direction the Chinese economy is taking: available data indicate that China aims to become a world power in innovation. Its share of global exports with a high technological content rose from 8% in 2003 to 24% in 2014, public expenditure on R&D is expanding by 18% a year, and it is currently the highest ranking country in the world in terms of the number of university graduates, which could amount to 29% of the worldwide total by 2020[11]. The government is leading the change in China's model – seeking a shift from assembling iPhones to creating the world's next benchmark smartphone – through a number of programmes and initiatives. By way of example, at the 2015 National People's Congress, the government announced its "Made in China 2025" strategy, which intends to transform the Chinese manufacturing model by introducing highly innovative and ground-breaking elements[12].

3 Calculations performed by Xu Ce, of the National Development and Reform Commission, and Wang Yuan, of the Academy of Macroeconomic Research.

4 Local government debt could total USD 3 trillion. "A Peek at China's Local Debt Mess". Bloomberg Business Week. 2014.

5 "The End of Cheap China". The Economist. 2012.

6 "China's Environmental Crisis". Council for Foreign Relations. 2014.

7 "China's growth outlook is still subject to mounting headwinds despite the achieved soft-landing in 2014". BBVA Research.

8 "La economía china que viene" ("The Chinese economy to come"), Zhang Monan. Project Syndicate. 2015.

9 Source: World Bank Indicators.

10 Source: World Bank Indicators.

11 See: http://monitor.icef.com/2012/07/china-and-india-to-produce-40-of-global-graduates-by-2020/

12 "It's official: China is becoming a new innovation powerhouse". Foreign Policy. 2014.

Box I.

The Chinese Economy: anecdotes and categories[13]

Author: Eugenio Bregolat, former Spanish Ambassador to China and collaborator of ESADEgeo – ESADE China Europe

"I don't even want to imagine where the world economy would be without the Chinese stimulus package," said Christine Lagarde back in 2012. In fact, China has contributed somewhere between a third and almost half of worldwide growth since the onset of the crisis. It therefore comes as no surprise that the transformation in its economy in recent weeks has caused stock exchanges the world over to tremble, while casting doubt on the incipient recovery of the global economy. What does this really mean?

After several years of slumber, the Chinese stock exchange grew 150% between the middle of last year and the beginning of last summer. Rectification was inevitable, to the tune of 40%. As always, the last ones to jump on the bandwagon – usually the most naïve – got caught out, while the early birds are reaping substantial rewards. Buyers of shares, or buildings, are seeking a higher return than the meagre interest rate on savings (which is often negative, in view of inflation) offered by the official banks. Moreover, the Chinese passion for gambling knows no limits: Macao outplayed Las Vegas by six times before Xi Jinping's decisive anti-corruption campaign put paid to the euphoria. The immaturity of the Chinese stock exchange is no secret – it was created as recently as 1990. And this is not its first bubble. In June 1999 the stock exchange climbed 70% in the period of a month, only to then lose 50% of its value between mid-2001 and 2005. Manipulation and insider information are frequent ingredients of corruption – arrests have been made and an investigation launched in connection with the latest commotions. For many years Wu Jinglian, one of the key and most influential Chinese economists and a professor at the CEIBS, has condemned irregular activity on the Chinese stock exchange, which he defines as a "lawless casino". The stock exchange is not a true reflection of the Chinese economy: just as it was stagnating at a time when China was growing vigorously, it then soared out of all proportion when growth decelerated. The government took landmark action back in July, stepping in to put a halt to this descent, when the official strategy is to leave the market to its own devices. By August, though, faced with new market slumps, the government was no longer trying to combat the law of gravity, in view of the futility of its efforts.

However, with respect to the depreciation of the Yuan, Chinese government policy has been brought into line with the strategy that gives the market a more prominent role in setting exchange rates. China intends for its currency to be integrated into the IMF Special Drawing Rights basket, which would equate to acknowledgement of reserve currency status. For this to happen, the IMF requires the People's Bank of China (PBC) – the central bank – to accept a floating exchange rate for its currency; i.e. the value of its currency would be set by the market. Last year, the PBC took steps to prevent devaluation of the Yuan (rather than provoking it, as had been the case for decades), when the Chinese economy tumbled and the US Dollar took an upturn. The PBC ceased its intervention on 11 August. This resulted in the Yuan depreciating by around 3% for a couple of days, until the PBC once again stepped in to prevent the currency sliding further. In other words, the PBC intervened to put a halt to the devaluation of its currency, rather than to cause it. Li Keqiang made it quite clear that the bank would not be stepping in for the opposite purpose. The 3% depreciation is not enough to enable a significant increase in Chinese exports, as the Yuan exchange rate is now around 10% stronger than one year ago. And the IMF has taken into consideration the last few months when break-even was achieved.

The wavering stance in the face of the crumbling stock market and the Yuan exchange rate episodes has fuelled suspicions that the stimulus package set in motion to contain the impact of the global crisis on the Chinese economy was founded on excessively lax credit and tax policies that have contributed to the stock market and real estate bubbles, and helped raise public debt to dangerous levels.

Are these events mere anecdotes soon to be forgotten? Or, on the contrary, are they signs of a systemic crisis? Are Chinese leaders losing their grip on the economy? Have they lost their bearings? To answer these questions we need to examine the macroeconomic setting for the development of the Chinese economy in relation to the strategic objectives. These objectives were defined at the 18th National Congress of the Communist Party of China (CPC) in 2012, and at the 3rd plenary session of its Central Committee in November 2013, the approach being to replace the economic model introduced by Deng Xiaoping in 1978, based on investment and exports, with a different model founded on domestic consumption, services and innovation. The aim is to reinforce the role of the market, cutting back on the privileges of major public companies in favour of the private sector, which is far more efficient. The resolution of the 3rd plenary session decided that: "The Gordian Knot of the reform is to achieve an apt relationship between the government and the market, wherein the latter plays the decisive role in assigning resources". This strategy has to enable China to escape the "middle-income trap". Having ruled out double-digit GDP growth, 7% has been set as the "new normal".

The IMF forecasts GDP growth of 6.8% for this year and 6.3% for the next, falling short of the 7% target, albeit only marginally, and nonetheless an enviable figure from the standpoint of almost any country in the world. When rightly pointing out that China is growing to a lesser extent than at the outset of the economic reform in 1978, usually no mention is made of

[13] Also published in the November-December 2015 issue of "Política Exterior" (in preparation).

the fact that the 12th Five-Year Plan, which draws to a close this year (2011-2015), projected 7% annual growth, resigned to the impossibility of maintaining double-digit expansion. The annual average for the five-year period exceeded 8%. In other words, it is not that the growth rate has fallen despite government efforts to sustain progress; rather, it is the government that failed to reduce the rate as much as it sought to. When a Five-Year Plan is approved, work begins straight away on the next plan. As such, for some ten years now the Chinese government has been envisaging the inevitable reduction in the growth rate, with a view to introducing a healthier, more sustainable rate.

Domestic consumption (private and public combined) climbed from 47% in 2010 to 51.2% in 2014, and is expected to increase a further three or four points by 2020. The services sector generated 48.2% of GDP in 2014, compared to 46.9% in the previous year. Employment has exceeded growth expectations as a result. This year R&D expenditure is set to reach 2.2%, while projections indicate that it will surpass that of the United States in 2019. Neither inflation nor deflation are cause for concern. The macroeconomic setting remains reasonably healthy and the economic model is gradually undergoing a transformation in terms of the key variables. The IMF has advised that it is "totally premature to speak of a crisis in China".

The negative consequences of the package of anti-crisis measures adopted by China include an increase in public debt and in credit granted by the financial system. In terms of volume, public debt is manageable: 20% in 2014, compared with more than 90% in the European Union, over 180% in the United States and almost 250% in Japan. Debt incurred by local authorities gives greater cause for concern, rising from 18% of GDP in 2008 to 36% in 2013. Credit granted by the financial system leapt from 153% of GDP in 2008 to a present-day ratio of 282%. Based on past experience, experts are warning of how similar bubbles have ultimately burst.

But the biggest challenge of all is that of boosting the market and the private sector, since large state-owned enterprises are reluctant to lose their privileges (monopolies, access to credit and land under highly advantageous terms and conditions, minimal tax pressure, etc.). Before the 18th National Congress of the Communist Party of China (CPC) in 2012, Xi Jinping stated that: "China must break the barriers from entrenched interest groups to further free up social productivity and invigorate creativity". Premier Li Keqiang seconded this motion in 2013, at the annual plenary session of the National People's Congress, the Chinese parliament: "Stirring up vested interests is more difficult than stirring up one's soul. But no matter how deep the water is, we must wade through because we don't have other options". On 19 August, China Central Television (CCTV), the mouthpiece of the CPC, warned that "the extent of opposition, the...ferocity...of those who haven't adapted to reform or even oppose it go far beyond what most people imagine". Xi Jinping will need all the power he can muster to win this battle. Moreover, with the country's future at stake, it is easier to understand why he is amassing such power. In Wu Jinglian's view, meanwhile, it is a question of determining whether China will create a healthy market economy based on the rule of law, or whether the situation will lead to what he calls "crony capitalism", where those in power intervene in the market and exploit the people.

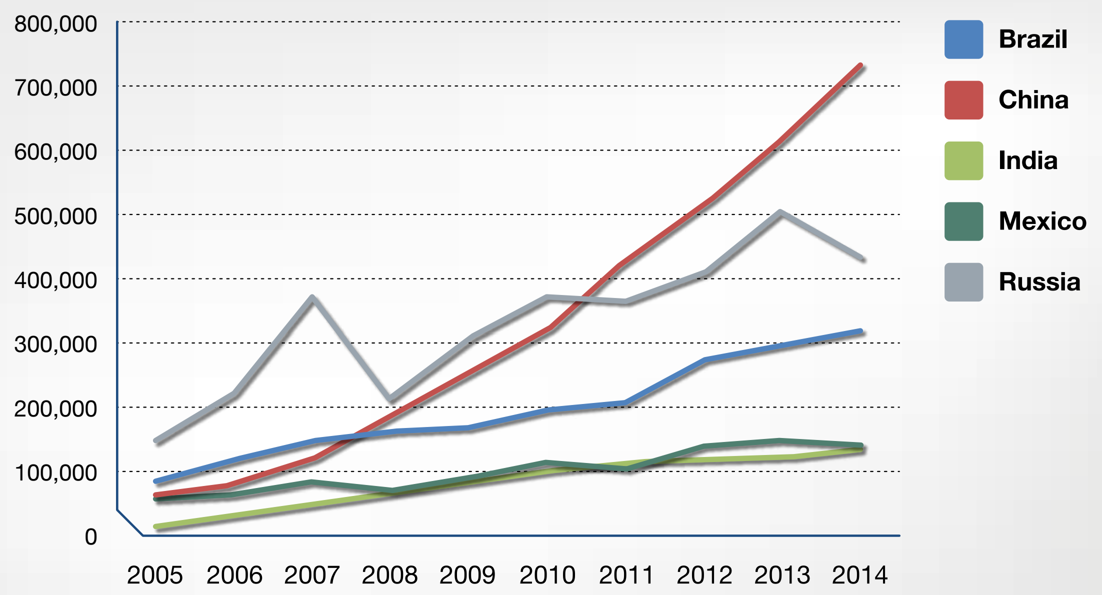
Those in charge of Chinese economic policy – heirs to the age-old meritocratic tradition of the mandarinate and armed with the powerful leverage of the authoritarian state – have earned themselves a great reputation, having played a leading role in the fastest economic development process in world history. Per capita GDP has rocketed from a little above USD 200 in 1978 to almost USD 8,000 at present. When Donald Trump said recently that Chinese leaders "are much smarter than our leaders", he was expressing an opinion that is widespread in political and economic circles the world over. I have been observing developments in China since 1987 and have heard a constant stream of prophecies hinting at an imminent crash – so far, it is we who have crashed, Europe and the United States. Since the outset of the economic reform, the response capacity of the Party-State has enabled it to overcome the challenges (a technically bankrupt banking system, crumbling state-owned enterprises, entry into the WTO, the global economic crisis, etc.). The current challenge – replacing the economic model introduced by Deng Xiaoping – is greater than any before, except for the implementation of the economic reform itself and preventing the Tiananmen Square protests of 1989 from quashing that reform. The crux of the matter, in my view, is whether the response capacity of the Party-State will continue to be equal to these challenges as management difficulty escalates, inasmuch as the economy is becoming increasingly complex while society becomes richer and more educated, informed and demanding; or whether, on the contrary, the challenges will become so huge as to overwhelm the mandarinate. This is precisely what happened in Russia with Gorbachev and Yeltsin; in the United States as a result of opaque financial instruments, excessive leverage, subprime mortgages, Greenspan's naïve view of human nature, etc.; and in the Eurozone with the ill-fated creation of the euro. Xi and Li will need a political will of iron and first-rate economic management capability, in equal measure. This, rather than the contingencies of the last few months, will be the test as to whether the reputation of Chinese leaders is too good to be true. Time will tell.

1.2 The gradual but inexorable international expansion of Chinese enterprises

Chinese outbound FDI has made firm headway since the regulatory changes brought in by the “Go Out Policy” in 1999, and a new record for overseas investment has been posted year after year, irrespective of the domestic or international economic climate. The international expansion of Chinese firms has now become another structural feature of the economy[14], besides generating almost two million jobs abroad and funnelling USD 37,000 million in taxes into the investee countries. There is also a substantial margin for growth, given the foundations on which it is based. As we mentioned in the previous edition of this report, these factors primarily include the substantial savings (the highest reserves of world currencies are amassed in China, with USD 3.6 trillion); deregulation and financial incentives for foreign investments, both for state-owned enterprises and private firms; the enormous need for commodities to sustain industrial capacity; and technological know-how to keep climbing up the development ladder[15].

In just a few years China has become one of the world’s main investors, undertaking transactions abroad that indicate growing influential capacity, not only in economic and business terms, but also on the social and political front. Based on data for the last available year, continental China ranked as the 3rd investor in the world in 2014 with investments totalling USD 116,000 million – according to both MOFCOM and UNCTAD – and falling short only of the United States and Hong Kong (China)[16]; and 9th in terms of cumulative investments (in 2000 it ranked 23rd). It is estimated at present that around 15,300 Chinese firms have invested abroad, amassing an FDI stock of USD 776,500 million at the end of 2014 according to MOFCOM and USD 729,585 million as per UNCTAD data; an all-time high from the standpoint of both of these organisations[17]. Far ahead of other economies, China has led the mass process of international expansion and foreign investment in which major firms from emerging countries have played a key role. This process evidences a shift of economic power towards the south and the emergence of an increasingly multipolar world. India and Russia are way behind China and their companies are much less global in nature than Chinese firms, with a lesser influential capacity abroad not only on a business level, but also in a political and strategic sense. The same can be said of the so-called *multilatinas* in Brazil and Mexico, which, all bar a few exceptions, are less global companies that could bear the brunt of the deteriorating economic climate in Latin America.

Chart 2 FDI accumulated abroad in emerging economies (2005-2014)



Source: UNCTAD. 2015. Millions of USD

[14] “The internationalization of Chinese Companies and their presence in Europe”, I. Casaburi & C. Brasò, ebook ESADEgeo. 2015.

[15] “Inversión China en Europa 2014” (“Chinese investment in Europe 2014”). I. Casaburi (publisher). Esade China Europe Club Report. 2014.

[16] “Global Investment Trends Monitor”. UNCTAD. 2015 http://unctad.org/en/PublicationsLibrary/webdiaeia2015d2_en.pdf

[17] China’s investment stock at the end of 2014 according to MOFCOM has been calculated as the sum of closing stock at the end of 2013 and investments announced by the Chinese government for 2014. Another statistical source would be the Chinese monetary authority and sovereign wealth fund State Administration of Foreign Exchange (SAFE), which records the inflows and outflows of capital into and out of China through the balance of payments, giving growth of 12.6% and a stock of USD 774,289 million. As can be seen, the two closing figures reflecting the cumulative amount for 2014 are very similar.

Which are the most global Chinese firms? How do they operate? Where do they invest?

In its statistical yearbook on foreign investment, MOFCOM offers aggregate data that enables a profile of Chinese firms abroad to be drawn up, focusing on different aspects and affording greater insight into their operations. The yearbook indicates that the preferred method of market entry for Chinese enterprises abroad is to establish a subsidiary – this is the chosen legal form in 86% of cases[18]. In terms of the investment format, this is fairly equally distributed amongst shareholdings (31.2%), reinvestment of profits (39.9%) and other investments (28.9%)[19].

Furthermore, the source of Chinese FDI is highly concentrated in the coastal provinces, where the main business hubs and the headquarters of the state-owned enterprises (SOEs) are located. Of the 10 provinces that had issued the highest volume of FDI at the end of 2013, eight are located on the coast (Guangdong, Shanghai, Shandong, Beijing, Jiangsu, Zhejiang, Liaoning and Fujian). Only two (Hunan and Yunnan) are situated inland, and the volume of FDI they issued is far below that of the coastal provinces. In terms of the number of companies abroad, and not considering SOE headquarters, the province with the highest number of firms overseas is Guandong (3,971), followed by Zhejiang (3,178), Jiangsu (2,277), Shandong (1,497) and Shanghai (1,383).

As regards the nature of ownership of Chinese firms with overseas investments, private companies have been gaining ground over SOEs in recent years. At the end of 2013 private firms accounted for 48.8% of the total, denoting 4.6% growth year on year. With respect to the volume of foreign investment, however, SOEs continue to hold their own, particularly those associated with sectors that are strategic for the Chinese government, such as oil and construction. Traditionally, these have been the largest firms in an economy where private activity was to a great extent restricted until a few years ago, and state-owned enterprises were therefore the only companies in a position to make inroads abroad and invest in large-scale projects. Moreover, these foreign investments benefitted from incentives offered by the government, which used them as a tool in its economic policy, primarily for the purpose of acquiring strategic assets that were lacking within the country's frontiers until then.

Chinese companies are present in practically all corners of the globe – in 184 countries, to be precise. In 2013 the Asian nation moved into a further five countries where previously it did not have a presence: the Maldives, Nicaragua, Kiribati, Belize and Burkina Faso. The main targets for Chinese enterprises have been developing countries, which received 8 out of every 10 USD invested in FDI, according to official figures released by MOFCOM, compared with 2 out of every 10 USD in advanced economies. In all regions worldwide except Europe and the United States, China's biggest overseas transactions have been undertaken by SOEs in the commodities and energy sectors, as we will see in more detail in chapter 2.

Table 1

Main non-financial Chinese transnational companies in terms of assets held abroad (2013)

1	CHINA PETROCHEMICAL CORP
2	CHINA NATIONAL PETROLEUM CORP
3	CHINA RESOURCES
4	CHINA NATIONAL OFFSHORE OIL COMP
5	CHINA UNICOM CORP
6	CHINA STATE CONST ENGINEERING CORP
7	CHINA MERCHANTS GROUP
8	SINOCHEM CORP
9	CHINA OCEAN SHIPPING
10	CHINA NATIONAL CEREALS, OILS & FOODSTUFF
11	ALUMINIUM CORP OF CHINA
12	CHINA MOBILE COMMUNICATIONS CORP
13	BEIJING ENTREPRISES GROUP COMP
14	CHINA MINMETALS CORP
15	GUANGZHOU YUEXIU HOLDINGS
16	CITIC GROUP
17	CHINA COMMUNICATION CONSTRUCTION COMP
18	CHINA POWER INVESTMENT CORP
19	BOE TECHNOLOGY GROUP
20	HUAWEI TECHNOLOGIES

Source: MOFCOM, 2014

Asia is by far the principal recipient of Chinese FDI, amassing 67.7% of the total stock, although this is largely due to investments made in Hong Kong (China), which could either revert to China itself through "round tripping" transactions, or may have an alternative final destination. China has set up 7,000 companies in Hong Kong (China), through which it has channelled numerous foreign investments, although no official data pay testament to the exact volume . Other Asian countries that have also received substantial investment from China are those in its area of influence, where Chinese firms have sought access to capital markets, natural resources, infrastructure construction, or market niches for their products. These countries include Singapore, Kazakhstan, Indonesia, Myanmar, Mongolia, Iran, Laos, Thailand, India, Pakistan and Vietnam. The largest transactions in this region have been undertaken in the commodities sector. By way of example: the acquisition of 67% of the oil company PetroKazakhstan for USD 4,200 million and 46% of Singapore Petroleum by China National Petroleum Corporation (CNPC); the Norinco operation in the copper sector in Myanmar amounting to USD 1,480 million; the sovereign wealth fund China Investment Corporation (CIC) buying into Indonesia's coal industry for USD 1,300 million; and the Chinalco transaction in the Malaysian aluminium industry for an amount of USD 800 million.

[18] A subsidiary is a company that is dependent on another (the parent). The parent, in turn, allocates funds enabling the subsidiary to operate on its own account, but retains control through ownership of a majority shareholding.

[19] Other investments include loans and debt transactions between the foreign investor company and the resident investee firm.

The region with the second highest presence of Chinese firms in the world is **Latin America**, which concentrates 13% of the total. The data may be misleading, however, in view of the huge volume received by two OFCs[21] – the Cayman Islands and the British Virgin Islands – which account for 88% of the total for Latin America. Without the flow of investments through these tax havens, Latin America loses considerable ground in China's investment map. In any case, Venezuela, Argentina, Ecuador, Peru and Mexico receive a substantial amount of investment from China. Major Chinese investments in the region have also been concentrated in commodities and energy. These include the acquisition by Minmetals and other Chinese investors of Glencore in Peru for USD 6,990 million in the copper sector, the oil company Sinopec acquiring 30% of Galp Energia in Brazil for USD 4,800 million, and the oil firm CNPC's purchase of the Brazilian enterprise Petrobras for USD 2,890 million.

The world region that receives the third largest volume of Chinese FDI stock is **Europe**, which concentrates 8% of the total (although Chinese statistics include not strictly European countries in this region). However, not taking into account investments made in certain OFCs (namely Hong Kong, the Cayman Islands and the British Virgin Islands), Europe would be the world's primary recipient of Chinese investment. Chinese companies have shown greater interest in channelling funds into major European economies, particularly the United Kingdom, followed by Germany, France, Portugal and Italy. Chinese FDI in Europe is distributed across a range of industries, although the bulk of investment lands in the electricity, real estate and industrial sectors, with a substantial technological or agro-industrial component[22]. Notable recent transactions include CIC's purchase of an interest in Chiswick Park in London for USD 1,200 million in 2014; the acquisition of a stake in Energias de Portugal by Three Gorges in 2011, valued at USD 3,500 million; and, more recently, ChemChina buying 26% of the Italian firm Pirelli for USD 7,200 million in 2015.

North America ranks fourth amongst the recipients of Chinese investments (4.3%), even though the attempts of certain Chinese firms to acquire strategic assets in the United States were obstructed in the past. Investments in the US financial sector are noteworthy, such as the acquisition of 10% of Morgan Stanley for USD 5,000 million and 3% of the investment fund Blackstone by the sovereign wealth fund CIC[23]. More recent significant transactions include Shuanghui's purchase of the food giant Smithfield Foods for USD 7,000 million in 2013. In Canada, large-scale transactions are concentrated in the commodities sector and include one of China's most significant overseas deals, namely the acquisition of Nexen by the oil company China National Offshore Oil Corporation (CNOOC) for USD 15,000 million.

Fifth in the ranking of recipients of Chinese investments is **Africa**, which amasses 4% of the total. Major transactions have been undertaken in South Africa, Zambia, Nigeria, Angola and Zimbabwe, almost exclusively in the commodities and energy sectors. Amongst the most significant of these are China Power Investment buying into the aluminium sector in Guinea for USD 5,950 million and CNPC's USD 5,000 million investment in the oil industry in Niger. Despite widespread media coverage and the interest aroused by Chinese investment in Africa, figures indicate that Chinese companies have a far greater presence in other economic regions. The investment relationship between China and Africa is markedly asymmetric, inasmuch as these transactions are far more relevant in terms of their economic and business impact on countries in Africa than they are for China.

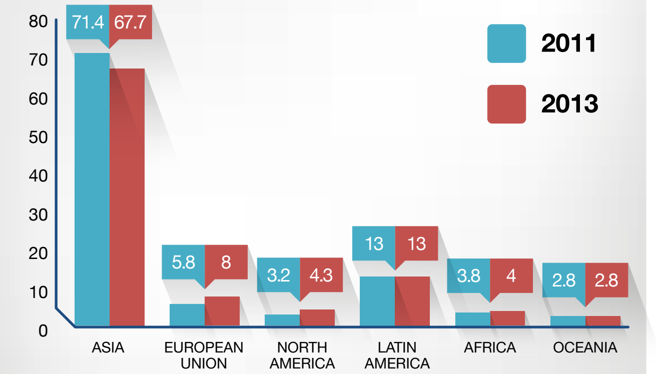
Lastly, **Oceania** concentrates only 2.9% of total Chinese stock abroad. Chinese companies have made numerous investments in various industries in Australia, the most significant, once again, targeting the commodities and energy sectors. These include Yanzhou Coal's acquisition of Felix Resources for USD 2,950 million, CITIC's purchase of a stake in Mineralogy for USD 2,920 million, and the electricity company State Grid buying into the subsidiary of Singapore Power in an amount of USD 2,350 million. It is worth highlighting that China has undertaken one of its most significant investments ever in Australia: the purchase of 11% of the world's largest aluminium company, Rio Tinto, by Chinalco for USD 12,800 million.

Regional adjustments in the pattern of Chinese foreign investment

An analysis of trends in the investment stock for 2013 compared to 2011 – reference data in the previous edition of this report – indicates regional adjustments in the pattern of Chinese foreign investment. Asia's share has declined by 3.7 percentage points, which have been redirected to investments in developed countries, particularly in Europe and North America. Meanwhile, Latin America, Africa and Oceania have retained their share with respect to the data published two years ago.

Chart 3

Chinese FDI stock by recipient geographical region (% of total)



Source: MOFCOM, 2014

[21] Offshore Financial Centres.

[22] Chinese FDI in Europe is discussed in detail in section 1.3.

[23] China Investment Corporation.

Table 2 Significant Chinese investments abroad by volume in excess of USD 5,000 million

YEAR	INVESTOR	VOLUME	% of TOTAL	COMPANY ACQUIRED	SECTOR	COUNTRY
2012	CNOOC	$15,100	n/av	Nexen	Energy	Canada
2008	Chinalco	$12,800	11%	Rio Tinto	Metal	Australia
2015	ChemChina	$7,860	26%	Pirelli	Transportation	Italy
2009	Sinopec	$7,200	100%	Addax Petroleum	Energy	Switzerland
2010	Sinopec	$7,100	40%	Repsol	Energy	Brazil
2013	Shuanghui	$7,100	100%	Smithfield Foods	Agriculture	United States
2014	Minmentals and others	$6,990	15%	Glencore	Metal	Peru
2013	China Power Investment	$5,950	n/av	Greenfield	Metal	Guinea
2007	ICBC	$5,600	20%	Standard Bank	Financial	South Africa
2009	CNPC	$5,590	37%	BP and Iraq South Oil	Energy	Iraq
2013	CNPC	$5,300	8%	KazMunaiGas National	Energy	Kazakhstan
2007	CIC	$5,000	10%	Morgan Stanley	Financial	United States

Key:
CNOOC: China National Offshore Oil Corporation; **Chinalco:** Aluminum Corporation of China Limited;
ChemChina: China National Chemical Corporation; **ICBC:** Industrial and Commercial Bank of China;
CNPC: China National Petroleum Company; **CIC:** China Investment Corporation.

n/av: not available.

Source: Heritage Foundation (2015)

In recent years we have seen China conduct a greater number of large-scale transactions throughout the world, some amounting to more than USD 5,000 million, usually entailing the acquisition of a majority or minority shareholding in a major local company. A few key examples of these transactions are described later in this chapter of the report.

Approximate volume of Chinese investment worldwide, excluding OFCs and round tripping

According to MOFCOM data, Chinese overseas investment totalled a cumulative amount of USD 660,000 million at the end of 2013. However, as mentioned in the previous edition of this report, recording the total volume of investment and analysing the recipient countries and sectors both fall prey to a two-sided issue. On the one hand, up to 70% of Chinese outbound FDI is carried out through OFCs, such as Hong Kong, the Cayman Islands and the British Virgin Islands. On the other hand, some investments just leave China temporarily only to return again (round tripping); such investments therefore cannot be considered as long-term and having the objective of establishing a lasting interest (in line with the definition of FDI).

Very few studies have recalculated Chinese investment flows to take these limitations into account, and any such studies are inconclusive. To help remedy this lack of information, BBVA Research recently published an analysis of China's worldwide investments, considering both OFCs and round tripping, and drawing some interesting conclusions.

The total volume of investments could actually fall considerably short of the figures published by MOFCOM. More specifically, BBVA estimates the Chinese FDI stock held abroad at the end of 2013 to be USD 498,460 million, as opposed to USD 660,620 million as per official MOFCOM data.

The results pertaining to the geographical distribution of Chinese FDI stock held abroad are even more eye-opening. In 2013, stock concentrated in Asia amounted to 49% of the total, rather than 68% as per official data. Similarly, the proportion corresponding to Latin America (where the Cayman Islands and British Virgin Islands tax havens are located) was estimated at 5%, compared with 13% as per official data. Conversely, Chinese FDI in North America was pushed up from 4% as per official data to 13%; the same is true of Africa, where the figure doubled from 4% to 8%. With respect to Europe, the focal point of this report, the BBVA study suggests that Chinese FDI is considerably higher than official statistics indicate. It would appear that Europe received 19% of FDI (rather than 8% as per MOFCOM data), i.e. almost 1 out of every 5 USD of Chinese outbound FDI, or a total of USD 95,190 million (investment stock).

2014: another record year for Chinese FDI in the world

So far, the slow-down in China's economy and the shift towards growth rates of around 6%-7% of GDP have not dampened Chinese firms' investments overseas. Conversely, outbound FDI exceeded the USD 100,000 million threshold in 2013 for the first time ever, and in 2014 China posted a new record high as an outbound investor, laying out USD 116,000 million, 15.5% more than in the previous year.

The international expansion of Chinese enterprises and the establishment of offices abroad continued at a giddy pace, with a total of 6,128 firms investing in 154 countries. For the first time, outbound FDI was almost on a par with inbound FDI, which amounted to USD 119,560 million in 2014. This highlights China's economic transition from an importer to an exporter of capital[24]. Based on these data, cumulative outbound investment totals USD 776,500 million as per MOFCOM and USD 729,585 according to UNCTAD.

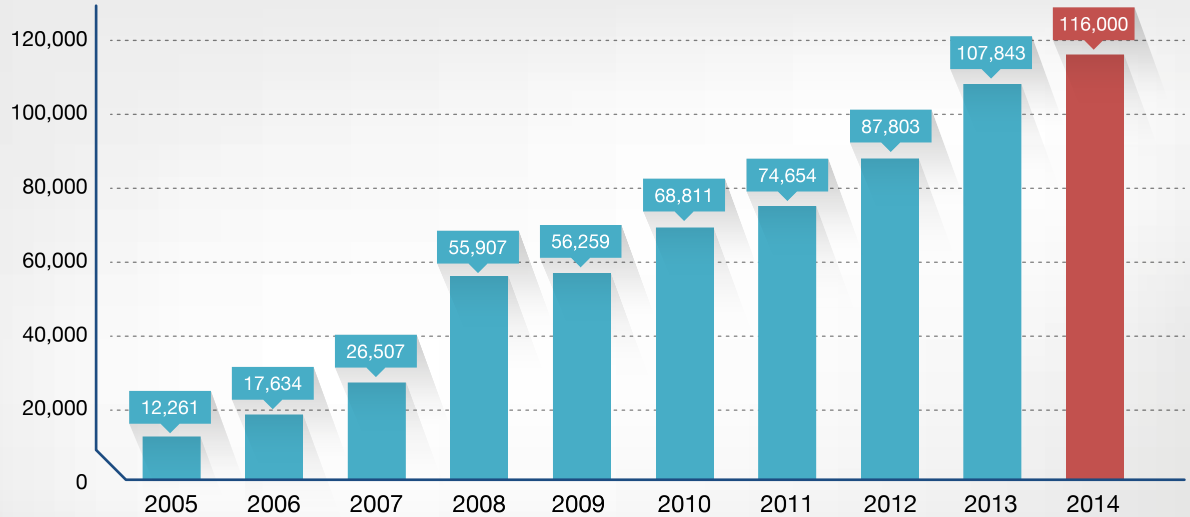
In 2014 Chinese firms undertook M&A transactions for an amount in excess of USD 50,000 million, equivalent to a little over 40% of total investments that year, according to various private sources[25]. Foremost amongst these transactions are the investment made by China Minmetals, alongside Guoxin Investment Corp International and CITIC, in the Las Bambas mine in Peru for USD 5,850 million, and Lenovo's investment in the mobile device multinational Motorola for USD 2,910 million, besides various other significant operations in Europe, details of which are provided later in this report. The tactic applied by these companies has become increasingly visible as the number of outbound investments undertaken by China worldwide has multiplied.

Generally speaking, and notwithstanding certain significant exceptions and nuances, a dual strategy has been implemented. One very clear strategy has been executed in developing economies, and even least developed countries (LDCs)[26], dominated almost exclusively by SOEs for geopolitical purposes, and based on access to commodities and natural resources. Meanwhile, another strategy has been applied in advanced countries – with private firms taking the leading role in this instance – based on access to new markets, know-how and technology. In any case, as already mentioned, there are notable exceptions, such as the advanced economies of Canada and Australia, where China has undertaken major transactions in the natural resources sector.

New drivers of Chinese outbound FDI

There is a general consensus as to the wide growth margin in Chinese outbound investment. As China progresses through its economic development, the number of companies that are competitive enough to venture abroad is rising, although the country still has a long way to go in comparison with the world's leading economies. China's cumulative outbound investments by size of economy (measured in terms of GDP) amount to only 7%, a long way off the 37% of the United States or the 42% of Germany. At the APEC summit held in Beijing in 2014, President Xi estimated that Chinese outbound FDI would exceed USD 1.25 trillion over the next ten years[27]. The analysis firm Rhodium Group projects even higher growth, which would situate Chinese FDI at approximately USD 1-2 trillion by 2020[28].

Chart 4 Chinese FDI in the world (2005-2014)



Source: MOFCOM, 2014. In millions of USD.

[24] Data taken from the Regular Press Conference of the Ministry of Commerce, held on 21 January 2015.
[25] "China's Global Outbound M&A in 2014". Rhodium Group, 2015.
[26] The United Nations list of LDCs is available at: http://www.un.org/en/development/desa/policy/cdp/ldc/ldc_list.pdf
[27] "Chinese outward investment – keeping up the pace". United Kingdom Trade and Investment (UKTI). 2014.
[28] "China's Reform Era and Outward Investment". Rhodium Group. 2013.

The optimism of private analysts and the Chinese government alike vis-à-vis the expansion of Chinese firms in the years to come is dependent on the drivers mentioned above and the high savings rate persisting over the next few years, the need to maximise the yield on reserves, the government stepping up its drive to promote overseas expansion, and the growing need to access different assets and capabilities in order to compete in the global market. Other additional factors arising from China's economic development in recent years are also in the mix.

Firstly, the slow-down in the Chinese economy, with annual GDP growth rates of 9%-10% slipping to 7% and even lower, makes for a less attractive domestic market in China. A combination of lower growth expectations, greater instability in the labour market and real estate market price stagnation could lead to a slump in consumer spending, casting doubt concerning domestic market performance. This situation should force major Chinese firms to expand their international diversification strategy in order to mitigate the potential risk of excessive concentration in the domestic market.

Secondly, in view of the rising labour costs in the Chinese economy in recent years, many foreign companies have relocated their factories and industrial plants to countries where salaries are more competitive, with some – for example, Dow Chemical, Caterpillar and Ford – even returning to home ground. Chinese enterprises are not immune to this trend: on the global stage, they will increasingly be forced to fragment their value chain and conduct their labour-intensive activities in lower-cost countries. The hourly minimum wage in China is USD 1.19, compared with USD 0.28 in India, USD 0.52 in Indonesia, USD 0.73 in the Philippines and USD 0.64 in Vietnam. Furthermore, company contributions to the social insurance cost amount to 35% of wages for the Asian giant, as opposed to 7.4% in India and 8.8% in the Philippines[29].

Thirdly, several technology firms are growing at whirlwind speed by exploiting the huge domestic market peopled by more than 500 million Chinese internet users. As a result, these enterprises become sizeable businesses in just a few years, accumulating a sufficient critical mass to undertake overseas investments. Such firms mushroomed in 2014. For example, the online sales portal Alibaba launched an IPO on the New York stock exchange with a price tag of USD 25,000 million; the smartphone manufacturer Xiaomi, with a track record of just four years, was crowned the world's most valuable technology start-up[30]; and Lenovo acquired Motorola Mobility from Google.

A fourth factor driving a new wave of Chinese overseas investment is the accumulation of wealth amongst Chinese citizens, who have amassed more than USD 15 trillion in bank deposits, and USD 2 trillion per year more according to McKinsey. Another report, produced by Bain & Company, indicates that Chinese citizens hold assets amounting to USD 13 trillion[31], including bonds, shares, funds, insurance, banking products, deposits and real estate property. According to the Bloomberg Billionaires Index, 11 of the world's top 100 billionaires are Chinese; China is second only to the United States in this sphere. One such billionaire is Wang Jianlin, who in 2014 acquired one of the largest empty buildings in the centre of Madrid for USD 360 million. Private investors are becoming increasingly ambitious and sophisticated, demanding greater diversification of their investment portfolio and a higher yield, and financing projects overseas when not investing directly.

29 http://www.china-briefing.com/news/2014/06/03/china-asean-wage-comparisons-70-production-capacity-benchmark.html

30 See http://www.wsj.com/articles/xiaomi-becomes-worlds-most-valuable-tech-startup-1419843430?KEYWORDS=china+tech

31 See: http://www.bain.com/Images/2013_China_Wealth_Report.pdf

Box II.

Chinese foreign investment from a legal perspective

Authors: Brígida Galbete, Senior Associate, and Qinyi Tang, Associate. Cuatrecasas, Gonçalves Pereira

Outbound direct investment (ODI) by the People's Republic of China has grown rapidly and continuously over the past decade. According to data published by China's Ministry of Commerce, the country's ODI amounted to USD 102,900 million in 2014, an increase of 14.1% on 2013[32]. A significant portion of this investment comes from privately owned enterprises (POE).

It is clear that China has become one of the key global investors. This marked change is due to a number of factors, but primarily to policies introduced by the Chinese government in recent years to promote investment. Since assuming power in 2012, the country's new leadership has undertaken a set of reforms aimed at expanding China's outbound direct investment.

The government's contribution to the trend in China's outbound direct investment

Since launching the national policy known as the "Going Global Strategy" at the beginning of the century, the Chinese government has increasingly encouraged Chinese companies, particularly state-owned enterprises (SOEs), to invest abroad. The factors favouring ODI by SOEs include the following:

• SOEs are managed by the State-owned Assets Supervision and Administration Commission of the State Council (SASAC), meaning that they may invest abroad without supervision, provided that the purpose of the investment forms part of their principal activity.

• SOEs benefit from easy access to inexpensive financing and subsidies for foreign investment.

• The financial support of the central government mitigates investment risk, offering greater freedom and flexibility when undertaking projects outside China.

These factors help to explain why China's foreign investment during the 21st century to date has mostly been dominated by large SOEs. The Chinese government is clearly highly supportive of SOEs' expansion abroad. The reasons for this interest include:

• Ensuring access to foreign natural resources for domestic use.

• Acquisition of foreign brands as a strategy to access high profile technology, overseas market share, improved management capacities and talent abroad.

• The gradual loss of dominant positions in the domestic market, which has driven SOEs to diversify internationally.

• A search for less expensive labour in neighbouring countries in South-east Asia and Africa.

However, the role of private capital in foreign investment is changing. POEs are becoming the new protagonists of China's economic internationalisation, taking over from SOEs. This may be partially due to the Chinese government reinforcing its oversight of ODI projects as part of anti-corruption controls, restricting SOEs' foreign expansion.

A look at legal procedures

Chinese foreign investment has generally involved numerous government agencies, primarily:

• The National Development and Reform Commission (NDRC), which must be sent prior notice of the foreign investment project.

The NDRC is assigned the task of reviewing whether the investment project complies with state industrial policies and whether the applicant has the investment capacity required to undertake the project.

• The Ministry of Commerce (MOFCOM) registers projects in conjunction with the NDRC and, where applicable, issues an authorisation.

The MOFCOM has the power to review any matters relating to cross-border investments, whether they are ex novo investments, restructuring processes or other forms of investment.

• The SASAC, with which state-owned enterprises are obliged to register. In some cases, this registration is the only formality for SOEs.

• The State Administration of Foreign Exchange (SAFE). Until the latest reforms were implemented in 2015, all projects had to be registered with SAFE.

Incipient deregulation of Chinese foreign investment

In its 12th Five-Year Plan on Foreign Investment and Outbound Investment Utilisation, published on 17 July 2012, the Chinese government maintained its objective of expanding the country's foreign investment. In the plan, it identified a set of key sectors, such as energy, telecommunications, manufacturing of high value-added equipment and industrial processes relating to certain commodities in countries with abundant mining and energy resources.

Since the plan was published, the administrative framework for foreign investment has undergone a number of changes to simplify the procedure and decentralise control and registration duties. As a result, we are seeing a new wave of foreign investment, particularly by POEs, aiming to diversify geographically and in terms of assets.

[32] http://data.mofcom.gov.cn/channel/includes/list.shtml?channel=dwjjhz&visit=A

As part of this drive to promote foreign investment, both the NDRC and MOFCOM, the main authorities responsible for processing projects, are notably speeding up the procedure for approving and registering investments. The most significant measures are:

Limits on the NDRC's verification powers

a. Administrative Measures for the Verification, Approval and Record-Filing of Outbound Investment Projects, modified by the NDRC and in force since 8 May 2014

The most significant change introduced by the NDRC as part of these measures is the substitution of the former pre-approval framework with a system for registering foreign investment projects, with one exception: investments in sensitive countries, regions or industries still require approval, although the power to grant authorisation has been decentralised and delegated to local authorities.

A "sensitive" country or region is understood to be any area which does not have diplomatic relations with China, is subject to UN sanctions or which is classified as sensitive by the MOFCOM. "Sensitive" industries are primarily those which work with products or technologies that are subject to export restrictions in China.

These administrative measures also simplify the formalities and significantly reduce the time required for applications to register foreign investment projects. Specifically, a period of 30 days has been established for reviewing projects (20 working days, extendible by a further 10) and a deadline of five working days from the application date has been set, for the first time, for the NDRC to request rectification of omissions from the application. Prior to this regulation, the entity had the power to use a significant degree of discretion in its assessment of whether the documentation provided at any point in the procedure was sufficient.

b. Catalogue of Investment Projects Subject to Governmental Approval, revised by the State Council on 19 November 2014 (the "2014 List")

The 2014 list indicates that, in line with the aforementioned administrative measures adopted by the NDRC, only investment projects in sensitive geographical areas or business sectors require authorisation, either from the NDRC or the MOFCOM. In all other cases, only registration requirements must be met.

These measures therefore eliminate the threshold of USD 1 billion, above which authorisation was previously required from the NDRC.

Simplified MOFCOM registration procedure

a. Administrative Measures for Outbound Investment, published by the MOFCOM, in force since 6 October 2014. In line with the 2014 List and the new regulations introduced by the NDRC, the MOFCOM also sees a registration system, rather than an authorisation procedure, as a priority formality.

It is notable that the MOFCOM has adopted a negative list approach to administrative regulation of outbound direct investments. Under this system, only certain types of investments that appear in the negative list are subject to review by MOFCOM and its corresponding bodies in the provinces. All other projects are exempt from review, irrespective of their size or nature.

The MOFCOM's negative list includes four types of investments:

- Investments that are a threat to the country's sovereignty, national security or public order or which are not permitted by the legal system.

- Investments that may damage Chinese relations with the country or region in question.

- Investments that breach any international treaty or convention to which China adheres or is party.

- Investments that entail foreign trade of products or technology which may not be exported.

Easing of foreign exchange controls to facilitate outbound direct investment

a. Circular of the State Administration of Foreign Exchange on Foreign Exchange Administration Issues concerning Encouraging and Guiding the Healthy Development of Private Investments, in force since 7 July 2012 ("Circular 33")

Circular 33 allows Chinese companies to borrow in foreign currency from domestic banks to finance foreign direct investment projects.

It also allows Chinese nationals to provide guarantees for foreign direct investment projects, provided that another Chinese entity has also extended guarantees.

b. Circular of the State Administration of Foreign Exchange on Further Improving and Adjusting the Policies on Foreign Exchange Administration of Direct Investments, in force since 1 June 2015 ("Circular 13").

Circular 13 represents a significant step forward in terms of relaxing the administrative procedures relating to foreign investments, as it eliminates the obligation for investors to apply to SAFE to register the project. This formality, which could take several weeks, was necessary to transfer the required currency abroad to finance projects. As a result of Circular 13, Chinese banks which share their data platforms with SAFE are authorised to directly register the amounts exchanged in relation to the foreign project.

Circular 13 also eliminates the registration process for reinvestment abroad by foreign companies with Chinese shareholders.

Remaining hurdles: the way forward

Although the regulatory framework for Chinese foreign investment is being made increasingly flexible, it is important to keep in mind that the new measures are based on certain long-standing principles which must be met by all outbound investments from China. This could have a significant impact on the progress of such projects. Examples of this can be found among recent administrative measures adopted by the NDRC, including:

1. The Regulations maintain the stipulation that other Chinese government agencies involved in internationalisation processes – such as customs, immigration and the tax authorities – may not intervene until the project has been registered with the NDRC or has been duly approved by it, as applicable.

2. The Regulations also reiterate the ban on Chinese financial institutions financing outbound investment – often the main source of funding for such projects – until they have been registered with the NDRC or have been duly approved by it, as applicable.

3. Thirdly, the Regulations maintain the requirement for Chinese investors to submit a report on the investment project and obtain a letter of approval issued by the NDRC before adopting any substantial measures in relation to the project (e.g. a binding offer) if the amount of the investment exceeds USD 300 million. In such cases, the disadvantages of the former pre-approval framework may therefore persist in the new structure, for projects of considerable economic importance.

4. If investments require a long period of preparation or a substantial initial outlay, the Regulations still require Chinese investors to perform the necessary formalities with the NDRC.

Moreover, the MOFCOM's new regulations for foreign investment bar Chinese investors in breach of these provisions from obtaining government assistance for internationalisation for a period of three years.

Finally, although the requirement for investors to register projects with SAFE has been eliminated, this does not represent deregulation of foreign exchange transactions; as stipulated in Circular 33, the banks responsible for the investment are obliged to examine the project documentation and report thereon to SAFE through the data platform created for this purpose.

Conclusions

The incipient but ongoing deregulation of Chinese foreign investment is clearly encouraging the country's investors to look beyond its borders for business opportunities. These actions, together with other measures of a more economic nature, are a reflection and result of the Chinese government's firm commitment to internationalisation. The "Going Global Strategy" requires a more flexible legal framework in the country, but within the limits of the system itself.

This is a win-win process, but it is particularly beneficial for private sector companies, which will increase their international presence and begin to operate in the spheres that, for a number of reasons, state-owned enterprises are vacating.

1.3. The EU as a target for investment: acquiring capacities in Europe

Relations between the EU and China are fluid at present, with no relevant conflicts and founded on close bilateral economic and business links. On a commercial level, the EU is China's main partner, while China is the EU's second-ranking partner. Both regions market goods and services amounting to €1,000 million a day[33]. In terms of overseas investment, the EU is the leading investor in China and, in turn, one of the principal recipients of Chinese investment. There is also a clear intention to expand and enhance this economic relationship through various undertakings: negotiation of a new investment agreement (see 1.4.); the EU's granting of market economy status; improvements to the intellectual property system for European companies in China; and updates to export credit policies[34]. At present, the roadmap that defines the strategy between China and the EU is the "EU-China 2020 Strategic Agenda for Cooperation", adopted during the 16th EU-China Summit held in November 2013.

In 2014 President Xi Jinping made his first visit to Europe since taking office in March 2013, accompanied by 200 entrepreneurs. President Xi travelled to Germany, France and the Netherlands, as well as visiting the European institutions headquartered in Brussels. In the economic and business sphere, talks between the leaders of both economies entailed negotiations and trade agreements, with particular emphasis on the aeronautics and automotive industries. Overseas investment relations are also playing a growing role in these bilateral encounters. European heads of state are calling for doors to be opened wider to foreign investments – in sectors such as transport and healthcare – and for the operations of European companies in China to be eased. To this end, a request was lodged to eliminate or reduce the requirement to set up a joint venture with a local partner entailing technology transfer, while the difficulties involved in accessing government contracts, and the lack of transparency in doing so, were highlighted.

More recently, in June 2015, the 17th EU-China Bilateral Summit was held in Brussels (coinciding with the 40th anniversary of diplomatic relations between the two regions). The Summit was chaired by the President of the European Commission, Jean-Claude Juncker, and the Chinese Premier, Li Keqiang. During the Summit, the leaders of both economies undertook to continue working in unison to comply with intellectual property rights, facilitate trade and reduce the carbon footprint. China also expressed an interest in taking part in the Juncker Plan[35].

Within this setting of cooperation and enhancement of bilateral relations, many European countries requested entry, as founding members, to the Asian Infrastructure Investment Bank (AIIB), a new large-scale initiative presented by China 2015. Austria, Denmark, Finland, France, Germany, Italy, Luxembourg, Malta, the Netherlands, Poland, Portugal, Spain, Sweden and the United Kingdom chose to back the financial institution, which aims to finance major infrastructure projects in Asia. The bank's initial subscribed capital is USD 50,000 million, and this could rise to USD 100,000 million. Beijing is therefore promoting a new multilateral bank to operate in areas that have already been served by the World Bank and the Asian Development Bank for decades, in what, from a broader perspective, could be seen as an ambitious venture to develop an alternative form of multilateralism to that proposed by Washington (and Japan), and which is supported by the majority of European nations.

Characteristics of Chinese investment in the EU

The EU is a priority recipient of Chinese investment, especially for companies seeking to access a major market with high purchasing power, increase their technological capacity, and develop or have access to a global brand. According to official data published by China at the end of 2013, 2,000 Chinese firms currently have establishments in the EU; these employ 47,000 people and amass a cumulative investment of USD 40,097 million, i.e. 4 out of every 10 USD invested in developed countries[36]. Official European data published by Eurostat indicate that cumulative Chinese FDI at the end of 2013 amounted to €25,500 million (USD 35,167 million)[37]. Although the EU is a key recipient from China's perspective, in terms of both volume and strategy, from a European standpoint investment from China continues to represent a very minor percentage of total investments received (1% of total FDI), although this is rising at a fast pace.

Luxembourg receives a considerable volume of investment from China (USD 10,424 million), as a large number of Chinese firms set up their holdings and/or European headquarters in this country, before subsequently reinvesting these funds in other EU countries. This is particularly true in the financial sector, where Luxembourg is set to become the first European country to host the six largest Chinese banks (Bank of China, ICBC, China Construction Bank (CCB), Agricultural Bank of China, China Merchants Bank and Bank of Communications)[38].

33 See: http://ec.europa.eu/trade/policy/countries-and-regions/countries/china/
34 http://representacionpermanente.eu/wp-content/uploads/2014/09/C17-COMERCIO-CHINA-ita.pdf
35 See: http://europa.eu/rapid/press-release_IP-15-5279_en.htm
36 Source: MOFCOM.
37 Euro-US Dollar exchange rate at 31 December 2013.
38 See: http://www.scmp.com/business/banking-finance/article/1610250/mainland-chinese-banks-eye-luxembourg-euro-zone-hub

Official Chinese data (cumulative at 2013)

Leaving aside the exceptional case of Luxembourg, official Chinese data indicate that cumulative Chinese investment in Europe up to 2013 has been funnelled into the major European economies.

The **United Kingdom** is the preferred destination of Chinese investors in Europe. This nation concentrates USD 11,798 million of cumulative investment across practically all sectors of its economy, including billion dollar transactions such as China Development Bank buying into Barclays for USD 3,040 million and Bright Food's acquisition of Weetabix for USD 1,940 million.

In **France** (USD 4,498 million), the sovereign wealth funds CIC and SAFE stand out, having acquired minority stakes in major firms, particularly in the energy sector, seeking a stable return that is long-term and low-risk, with no management involvement. CIC's purchase of 30% of Gaz de France (GDF) Suez for USD 3,240 million is noteworthy in this area.

In **Germany** (USD 3,979 million), Chinese investors have focused their investments on medium-sized industrial companies with high technological capability, such as the holding of the transportation equipment firm China International Marine Containers in Burg Industries, Jinsheng Industries' stake in the machine manufacturer EMAG, CITIC's interest in the automotive components manufacturer KSM Casting, and Wuhan Iron & Steel's share of the lift manufacturer ThyssenKrupp.

Cumulative investment in the **Netherlands** (USD 3,193 million) is also significant. This country offers Chinese investors distinct advantages; for example, tax breaks and a business-friendly commercial environment. As a result, numerous operations are orchestrated through this country, such as China National Petroleum's acquisition of a stockholding in North Caspian Operating Company, while other firms set up their European or international headquarters here. USD 2,737 million of Chinese investments have been funnelled into Sweden, albeit highly concentrated in two transactions undertaken by the automotive industry MNC Geely in 2010, when it purchased stakes in the Ford subsidiary and Volvo for USD 1,800 million and USD 900 million, respectively.

Italy has received USD 608 million, and also has stakes in approximately 195 Chinese firms[39] that have invested in the country in recent years. Over the last few years, the Chinese government has acquired minority interests in landmark Italian firms through the sovereign wealth fund SAFE, enabling the Italian government to dispose of assets at an attractive price. On the business front, the multinational Huawei has been particularly active, investing an amount potentially in excess of USD 2,000 million to increase its presence in the technology services segment, the second largest market for this company in Europe after the United Kingdom. Chinese enterprises have also bought into companies with a prominent brand image whose target audience is made up of consumers with high purchasing power. By way of example, Shandong Heavy's acquisition of 25% of the pleasure boating firm Ferretti.

Spain, the fifth largest European economy, received USD 315.7 million in Chinese investments, a volume that falls substantially short of the amount ploughed into countries such as the United Kingdom and Germany. Spain offers a unique advantage in the European environment, acting as a springboard for Chinese investment in Latin America in view of its deep-rooted historical, cultural, economic and business links with that region, which have led to the entry of Chinese capital into multinationals such as Telefónica. The presence of Chinese companies in Spain has grown rapidly in recent years, with investments becoming more comprehensive and encompassing a wider range of economic sectors. In the financial sector, the Chinese banks ICBC and CCB are physically present in several Spanish cities. In renewable energies, Trina Solar and Suntech Power have undertaken projects in Spain, as have Cosco and Hutchinson in the logistics and transportation industry and NHA in the hotel and tourism trade[40].

[39] Fondazione Italia Cina data.

[40] Spain is discussed in detail in chapter 3.

Box III.

The Asian Infrastructure Investment Bank: a step forward in China's international expansion

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On 29 June, China's international prominence reached a new level through the signing of the articles of agreement of the Asian Infrastructure Investment Bank (AIIB), which is expected to start operating at the end of the year.

This new multilateral financial institution, the first to be founded in the 21st century, was envisioned, created and spearheaded by China, with the aim of becoming a powerful catalyst for development in Asia. The bank is also the first real evidence in recent history of Beijing's interest in expanding its presence within the global system for management of economic affairs.

The institution, headquartered in Beijing, will initially focus on developing infrastructure and other sectors in Asia, such as energy, transportation, telecommunications, rural and agricultural infrastructure, water supply, environmental protection and urban development. The AIIB will also complement and collaborate with existing multilateral development banks, such as the World Bank, the Asian Development Bank and the International Monetary Fund, in providing financial support for infrastructure and regional interconnectivity in Asia.

In fact, Jim Yong Kim, President of the World Bank, recently acknowledged that the combined efforts of all of the multilateral development banks would not be sufficient to meet Asia's considerable infrastructure financing requirements. According to the Asian Development Bank, investment of USD 8.22 trillion is needed in Asian infrastructure in the twenty-tens, although this figure may rise due to the rapid rate of urban development.

The most active banks in the region – the World Bank and the Asian Development Bank – cover just a quarter of this amount, and public and private financing seems insufficient to absorb the remainder.

The cross-border character of the new institution and its international popularity are clearly reflected by the 56 signatory countries from different regions of the globe, including developed economic powers such as France, the United Kingdom, Germany, Spain, Australia and Norway, as well as emerging economies such as Brazil, Russia, the United Arab Emirates, South Korea, Qatar, Turkey and Vietnam. What is more, according to the AIIB's Secretary General, the number of members is expected to reach 70 in the near future.

The AIIB's initial capital is USD 100,000 million (almost half that of the World Bank and more than half that of the Asian Development Bank), 75% of which is held by Asian countries, in accordance with the institution's regional commitment and focus. In addition to China, the main shareholder with 26% of the institution's capital, other significant investors include India, Russia, Germany and South Korea. Spain has subscribed almost USD 1,800 million, equivalent to an interest of 1.76%. The United States, Japan and Canada are all notable absentees, citing concerns over the transparency and governance of the institution.

The AIIB's considerable popularity among the core Western economies reflects their governments' keen interest in home-grown companies participating in development of infrastructure in Asia, one of the region's key challenges. As previously mentioned, Spain – which China usually calls its closest ally in Europe – is one of the AIIB's twenty non-Asian founding member states. Representation on the bank's management bodies will improve access to supplementary financing for Spanish companies operating in the region.

The creation of the bank forms part of China's plan to boost trade and economic collaboration with other ASEAN countries by improving interconnectivity in the region, an initiative known as the "New Silk Road". The AIIB will act as a platform for China to export capital, labour and experience to assist in the infrastructure construction drive in emerging Asian markets.

The infrastructure deficit – in transportation, telecommunications and energy among other areas – in Asia and particularly in China (despite spending 8.5% of its GDP on domestic infrastructure from 1992 to 2011) is holding back development in the region, especially now that the Chinese economy is slowing down – a situation known as the "new normal".

Another of the plan's objectives is to diversify land and sea trade routes with the country's main economic partner, the European Union, to reduce geopolitical risk.

The bank is also a new instrument of economic influence in Asia, alongside the recently created New Development Bank (NDB), whose purview is global and whose shareholders are the BRICS nations. According to MOFCOM data, 68% of China's foreign direct investment in 2013 was in Asia, resulting in a stock of USD 76,000 billion. All of the above clearly demonstrates China's role as a driving force and influencer throughout Asia.

The creation of a new institution also reflects the nation's efforts to attract business, investments and other financial activities in Yuans, in response to the prospect of increased use of China's currency in international transactions, whilst channelling the country's enormous foreign exchange reserves (approximately USD 4 trillion, similar to Germany's GDP) into capital-intensive projects.

Despite this, in some circles the creation of the AIIB has been interpreted as China challenging the United States and its influence on the financial and monetary system originating from the UN's Bretton Woods Conference in 1944. But the new economic status quo necessitates a change in the system of multilateral financial institutions to adapt to the new circumstances and challenges, especially in relation to emerging markets and their growing contribution to the global economy.

In fact, China's relative representation on the decision-making bodies of multilateral institutions reflects the geopolitical situation following the Second World War rather than its current economic standing. It seems that, in the interests of a healthy global economy, China's considerable contribution to the global market – it is the largest economy in the world in terms of purchasing power parity and the second largest in absolute terms – should be reflected by greater influence on the international financial framework.

Creating an institution of this kind is a long and complex process, entailing a number of economic, political and financial variables. In any case, this project is of strategic importance to China and the country can therefore be expected to pour resources into the institution to make it a symbol of the leading role the nation wishes to play on the international stage.

In short, other than China joining the World Trade Organisation, this ambitious project is the most convincing evidence that the country is working towards much more active multilateralism, leaving behind the bilateralism characteristic of its 20th century undertakings. The fact that the AIIB has numerous founding member states promotes this new direction, ensuring that the institution works effectively and is well designed. European countries, which have substantial experience in multilateral projects and infrastructure development, have joined this initiative, demonstrating once again that the way forward is to build bridges and strategic alliances between China and Europe.

1.4. Latest transactions and trends (2014-2015)

Chinese investment in the EU reached an all-time high in 2014, at USD 20,170 million, indicating growth of 117% compared to 2013 according to the Esade China Europe database. Numerous large-scale operations with a price tag in excess of USD 1,000 million were undertaken in the course of last year, enabling Chinese FDI to cross the USD 20,000 million cumulative investment threshold for the first time. These notably include the purchase of 35% of the Italian bank Cassa Depositi e Prestiti (CDP) Reti by State Grid in the electricity sector; the acquisition of 80% of the Portuguese financial institution Caixa Xeral by the Fosun Group; the purchase of the Dutch-based agricultural conglomerate Nidera by the food group COFCO[41]; and the automotive firm Dongfeng buying into the French enterprise Peugeot. As can be seen in chart 5, cumulative Chinese investment in Europe dropped in 2013 after consecutive years of growth[42]. This decline was largely due to the absence of large-scale transactions in strategic industries – such as the energy or financial sectors – on a par with those conducted in 2014, which are described earlier in this report.

Chart 5

Chinese FDI in Europe (2010-2014) in millions of USD

Source: ESADE China Europe based on Bloomberg, FDI Markets, Heritage Foundation and own research.

In 2014 and early 2015 three important trends in Chinese investments in the EU as a whole were confirmed. **Firstly**, and in keeping with an economy in which the private sector takes up a growing amount of space, Chinese investment increasingly stems from private enterprises. A substantial number of expansion operations have been undertaken recently by non-state-owned companies, such as Fosun (China's largest private industrial conglomerate), Hony (private equity firm), Ping An (insurance and financial services) and Anbang (insurance company). Private Chinese firms conduct a greater number of transactions than state-owned Chinese companies in Europe, although the latter channel in a higher volume of investments as they have greater financial capacity and undertake operations that are strategic for the Chinese government.

[41] China National Cereals, Oils and Foodstuffs Corporation.

[42] On completion of this report, neither Eurostat nor MOFCOM had published official statistics for 2014 on Chinese investment in Europe.

Secondly, in recent years preferences have leaned towards acquiring minority stakes in European companies, as opposed to purchases of majority interests (more than 51%) to take control of a company or 100% shareholdings, as seen in past years.

Thirdly, as will be seen in chapter 2 of this report, over the last few years transactions have been undertaken in a greater diversity of industries, with sectors such as real estate and agri-food becoming increasingly important in Europe for Chinese firms.

Recipients of Chinese investment in Europe

In 2014 a high concentration of transactions were carried out in the **United Kingdom**, where USD 8,370 million, or 46.7% of Chinese investments for that year, were received. Investments encompassed a wide range of sectors, particularly real estate, which is increasingly important for Chinese investors – especially premium assets, usually located in the most exclusive districts of London. Two examples are the acquisition of an office building in the City by China Construction Bank (one of the big five, which recently entered the Spanish market opening its first branch office in Barcelona) for USD 190 million, and the announcement made by the Chinese holding Greenland, which constructed some of China's principal skyscrapers, of a real estate development to build an apartment and office block in Canary Wharf.

The largest Chinese producer of nuclear energy, the SOE China General Nuclear Corporation (CGNC), entered the European renewable energy market by purchasing three wind farms in the United Kingdom from French firm GDF. This transaction reflects China's interest in this sector with a view to diversifying its energy map, continuing along the lines of earlier investments made by Three Gorges in Portugal and Ginko Tree in Norway[43]. The interest of Chinese investors – possibly CGNC itself – in acquiring a stake in the development of nuclear energy in the United Kingdom, more specifically in the Hinkley Project in Somerset, which should provide five million homes with electricity[44], has stirred great controversy, inasmuch as nuclear energy is a particularly sensitive sector in terms of national security.

The European country that received the second highest volume of Chinese investment in 2014 was **Italy**, with a total of USD 3,750 million, or 21% of investments for that year. In Italy, the sovereign wealth fund SAFE, whose investment strategy is to act as a purely financial long-term partner with no management involvement, bought minority interests of 2% in Ente Nazionale Idrocarburi (ENI) and 3% in ENEL (Ente Nazionale per L'Energia Elettrica), for a combined amount of USD 2,670 million[45]. In the latter case, the strategic nature of the transaction is prominent, giving access to third markets, as ENEL owns the Spanish firm Endesa and its Latin American assets. Meanwhile, the electricity enterprise State Grid acquired 35% of the holding CDP (Cassa Depositi e Prestiti) Reti for USD 2,800 million, and Power Construction Group purchased 40% of the energy company Ansaldo Energia for USD 560 million. SAFE's purchase of a minority interest in landmark Italian firms such as Fiat Chrysler and Telecom Italia is also noteworthy. A greater number of transactions is expected to be seen in the coming years, in view of the investment vehicle set up by Fondo Strategico Italia and the sovereign wealth fund CIC for €1,000 million. More recently, in early 2015, the tyre manufacturer Pirelli announced its sale to the state-owned chemicals firm China National Chemical Corporation (ChemChina) for USD 7,860 million, in one of the biggest overseas investment transactions undertaken by China in Europe – this amount exceeds investments received by Italy for the whole of 2014.

Portugal ranked third amongst the recipients of Chinese FDI in 2014, with 10.6% of the total for Europe. Chinese investors have purchased 45% of the assets encompassed by the Economic Adjustment Programme in the last three years. Chinese investment has made vigorous inroads into the Portuguese electricity sector. In 2011, Three Gorges Corporation acquired 21% of the state-owned company Energias de Portugal and China State Grid purchased 25% of Redes Energéticas Nacionais (REN). In 2014 the most relevant transaction was the acquisition of 80% of the insurance firm Caixa Seguros by the Fosun conglomerate for USD 1,360 million. In some cases Chinese investors may follow a triangulation strategy, investing in Portugal to access distribution networks and gain knowledge of certain markets that were former Portuguese colonies, such as Angola, Mozambique or Brazil, where China has substantial interests.

The country that received the fourth largest volume of Chinese investments last year was **France**, with USD 1,700 million, or 9.5% of the total. In France Chinese investors have continued to focus on vineyards and wineries, particularly in the Bordeaux area, with a view to serving certain market segments previously covered by foreign companies or through imports. In the automotive industry, Dongfeng Motor's purchase of an interest in PSA Peugeot Citröen for USD 1,100 million stands out, being the largest transaction undertaken by China in the European automotive sector since the acquisition of the Swedish firm Volvo by Geely Auto in 2010. This stake in PSA's capital will give the Asian firm access not only to technological know-how, but also to the markets in which the French firm already operated. Other key transactions in 2014 include the sale of Alcatel-Lucent's Enterprise division to China Huaxin Post & Telecommunication Economy Development Center

43 http://www.ft.com/intl/cms/s/0/db8c9540-838f-11e4-9a9a-00144feabdc0.html#axzz3PvBGkSgD
44 http://www.nytimes.com/2013/10/18/business/international/britain-to-let-chinese-buy-into-nuclear-power-plants.html?pagewanted=all&_r=0
45 These transactions were not reflected in the ESADE China Europe Club database as the purchase amounted to less than 10% of the resident firm's capital and therefore did not meet the generally accepted definition of FDI, as set out by the IMF and the OECD.

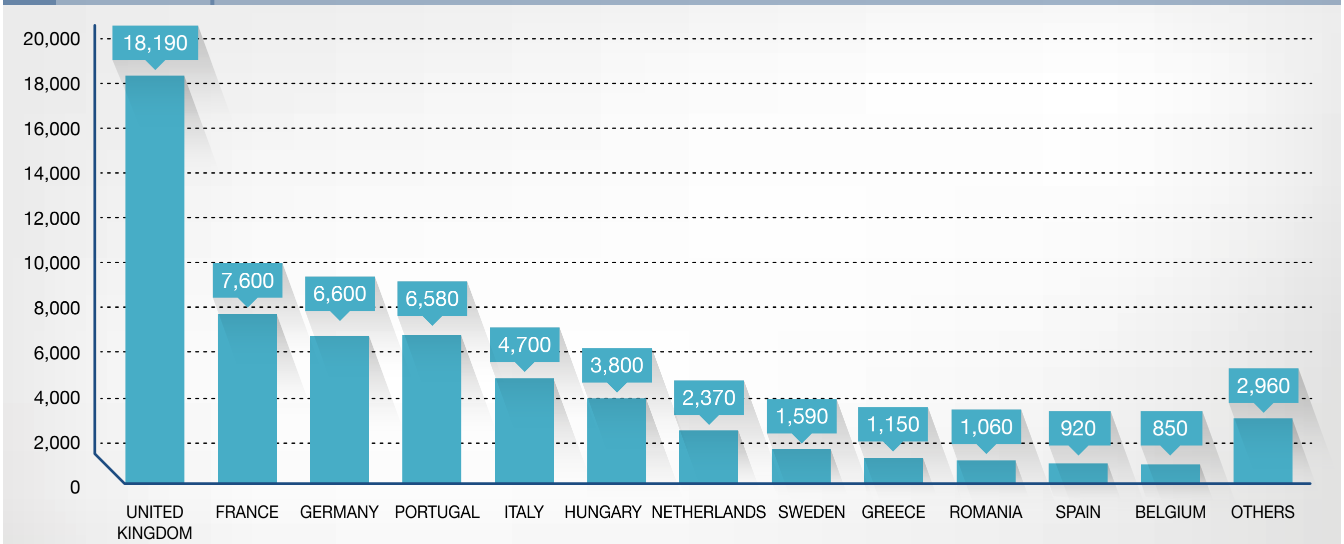
for USD 310 million, and the acquisition of the train wheelset manufacturer Valdunes by the Chinese firm Maanshan Iron & Steel for USD 17 million. The French government also authorised a consortium of Chinese investors to buy into the capital of Toulouse airport. This has raised certain suspicions in view of Toulouse being the host city of Airbus, Europe's largest aircraft manufacturer, which uses the airport for flight testing its different models.

The **Netherlands** ranked fifth amongst recipients of Chinese investments, with 8%. Practically all of the investment in the Netherlands was channelled in by the food conglomerate COFCO – one of the main Chinese SOEs in the sector – to acquire the agro-food company Nidera for USD 1,200 million. The Eurozone's leading economy, Germany, received 4.4% of the total investment. As in previous years, Chinese investments in Germany were primarily concentrated in the manufacturing sector, particularly niche firms with a distinct speciality or technological know-how. In 2014 China undertook investments in the cement company KHD, in which it already had a stake, and which works on energy efficiency in concrete manufacturing processes; the electricity firm Schweizer Electronic; Heidelberger, a company specialised in printers; the crane manufacturer Wilbert Kranservices; and ZF Friedrichshafen AG, an automobile parts firm. Outside the industrial sector, the private group Fosun announced its possible purchase of a stake in the private institution BHF Bank, owned by Deutsche Bank.

In **Spain**, where cumulative investment at 2014 amounts to almost USD 1,000 million, Chinese investments have been diversified to a greater extent in the last year. In the agro-food sector, Fosun acquired an interest in Osborne, while very recently the Chinese giant Bright Food purchased 100% of the Catalan firm Miquel Alimentació. Several transactions also took place in the real estate sector throughout Spain, often with a tourism industry slant. These notably include the purchase of the Edificio España building in Madrid by the Dalian Wanda Group and, in the sports world, the acquisition of a stake in the Atlético de Madrid football team. Chapter 3 of this report deals exclusively with Chinese investment in Spain, taking an in-depth look at the opportunities and challenges this market offers Chinese investors, including an analysis of the main transactions.

Lastly, in 2014 Chinese investors continued to cash in on the economic decline of **Greece** to continue making inroads into strategic sectors. Cumulative Chinese investment in Greece amounts to USD 1,150 million for the last five years, with funds from China being concentrated in the shipbuilding and tourism industries. COSCO's involvement in the Port of Piraeus – where it holds a 35-year concession – goes beyond operating a container loading bay, and a railway line has been opened to transport merchandise to the lines connecting Greece with Central Europe. Chinese investors are also interested in submitting a tender for the privatisation of the Piraeus Port Authority (OLP). China continued to invest in Greece in 2014, signing a shipbuilding agreement with Costa Mare for USD 2,300 million, financed by the China Development Bank (CDB). China's commitment to and interest in Greece were demonstrated when Chinese Premier Li visited the island of Crete, where a Chinese consortium is tendering for the construction and management of an international airport.

Chart 6 Recipient countries of Chinese FDI in the EU (2010-2014), in millions of USD



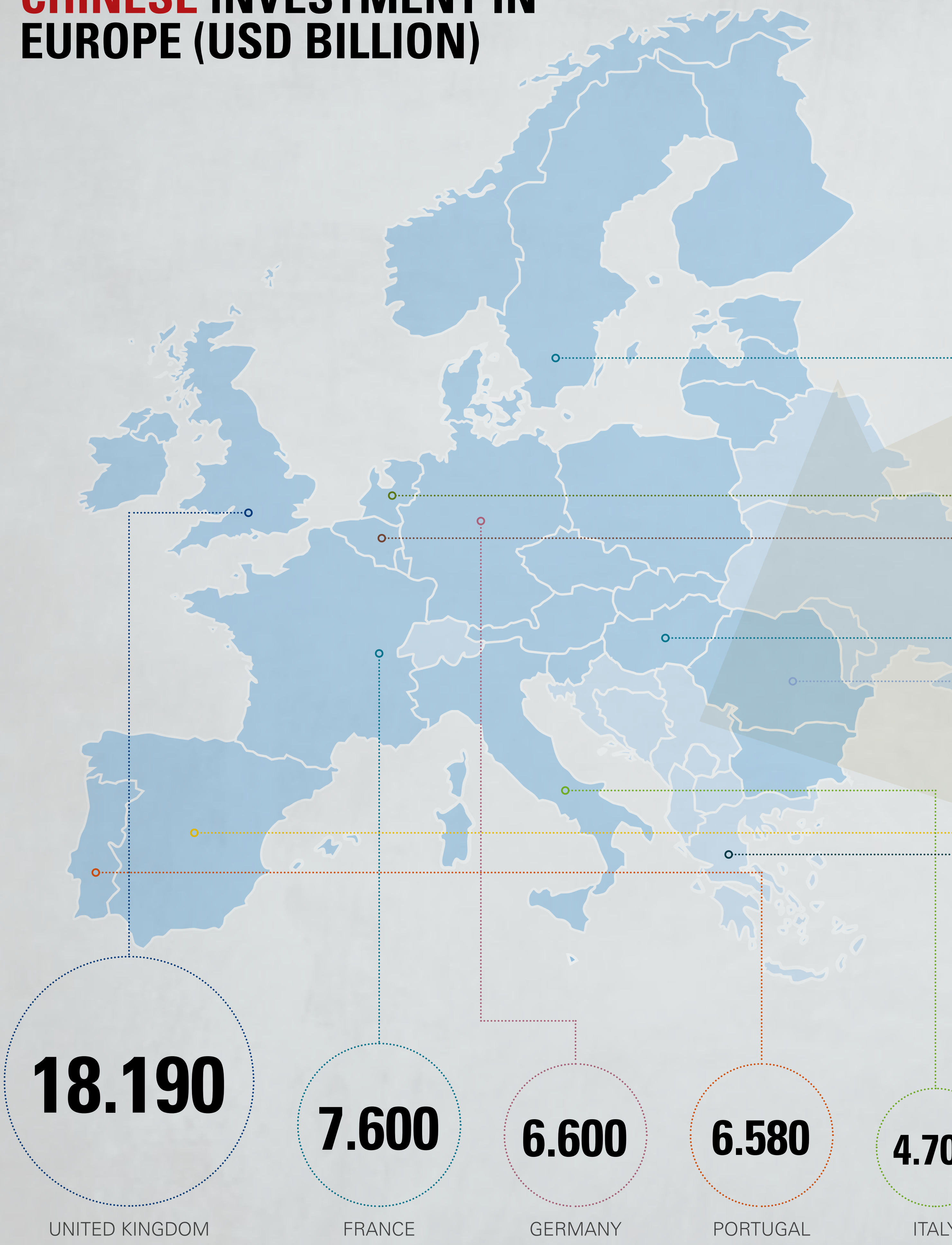
Source: ESADE China Europe based on Bloomberg, FDI Markets, Heritage Foundation and own research.

An economic region on which many Chinese investors – particularly state-owned ones – have set their sights is **Central and Eastern Europe**. These countries represent an attractive investment opportunity, offering a combination of moderate salaries, qualified human resources and low-priced assets, and being in an earlier stage of development than the major European economies. In the last five years, China has invested USD 3,800 million in **Hungary**, a higher amount than that invested in many large European economies, while **Romania** received USD 1,060 million and **Bulgaria** USD 830 million. Towards the end of last year, the Chinese government announced that it would be setting up a USD 3,000 million investment fund for Central and Eastern Europe, in order to reinforce these countries' capabilities as the European entryway for products and services arriving from China. Premier Li also announced an agreement with the governments of Hungary and Serbia to finance and construct a high-speed train to operate between Budapest and Belgrade. Transactions undertaken in this region have a different profile, being more focused on the transport, logistics and distribution sectors.

Official statistics for China published by MOFCOM rank **Luxembourg** as the second recipient of Chinese investments in the EU, with a cumulative amount of USD 10,424 million, in the wake only of the United Kingdom. This is because Luxembourg is the European headquarters of many Chinese firms, which set up a European subsidiary in this country for tax reasons and consolidate their accounts there, although a part, even the majority, of their activity is conducted in other countries. However, ESADE China Europe statistics – which are more accurate as an analysis of operations, rather than investments, is undertaken – estimate that "actual" investment in Luxembourg falls far short of the amount invested in the main recipient countries of Chinese FDI in the EU[46]. Various sources agree on a cumulative amount of between USD 500 million and USD 1,000 million.

[54] Along the same lines, the Heritage Foundation database only reflects one Chinese transaction in Luxembourg in the 2005-2014 period, and FDI Markets only seven (minimal investments, primarily in financial institutions) in the 2003-2014 period. Likewise, in line with the ESADE China Europe results, the report entitled "Reaching New Heights" drawn up by Baker & McKenzie and Rhodium Group, which also have their own database of Chinese investments in Europe, estimates total Chinese FDI in Luxembourg at between USD 500 million and USD 1,000 million, which is a very different figure from the volume invested in the main recipient countries of Chinese FDI in the EU.

CHINESE INVESTMENT IN EUROPE (USD BILLION)



SOURCE: OWN RESEARCH ESADE CHINA EUROPE CLUB

1.5. Tailwind for the coming years

The outlook for foreign investment by Chinese firms over the coming years is decidedly positive, according to analysis by private firms such as the Rhodium Group and Citibank and the Chinese government itself, which forecasts rises in the number and volume of foreign investments. The EU can reasonably be expected to be a key destination in Chinese companies' expansion, either through reinvestment of profits, investment extensions or new investments. In a World Economic Forum (WEF) survey of the 100 largest Chinese firms, 43% responded that they plan to expand in Western Europe and 44% in Eastern Europe over the next five years.

The EU offers clear advantages to foreign investors and particularly for Chinese capital.

- The EU is the world's largest economy and its biggest market, with approximately 500 million inhabitants whose average purchasing power exceeds USD 25,000.
- The EU offers first-rate human, physical and technological capital, a stable investment climate, transparency and less bureaucracy than other regions of the globe.
- European companies are leaders in numerous sectors and highly sophisticated businesses which invest in R&D and have the capacity to internationalise. Moreover, in the coming years a number of meaningful factors which are currently incipient will consolidate, acting as a tailwind for China-EU investment.

  Ongoing negotiations to sign a new investment agreement will promote and simplify the investment framework, facilitating bilateral investments.
- Chinese citizens' higher level of disposable income will lead to increased investment in the EU by Chinese companies to increase their manufacturing capacity or access know-how to allow them to manufacture in China.
- The need for demand-side policies to reinvigorate economic activity in the EU, as evidenced in the Juncker Plan, is taking form in a public-private partnership which is expected to attract active participation from foreign investors, potentially including Chinese capital.
- New joint investment vehicles created by the Chinese government and different European governments, some of which are already operating, should also stimulate bilateral investment.
- Lastly, megaprojects such as the New Silk Road will fuel Chinese investment in the infrastructure of countries which are directly affected, with financial support from newly created institutions such as the Asian Infrastructure Investment Bank (AIIB) and the New Development Bank (NDB).

A bilateral investment agreement

In 2014, China and the EU entered into talks with a view to signing a new investment agreement to substitute the existing 26 BIAs[47] between the Asian country and the member states. These agreements established conditions for foreign companies to be treated fairly and equally to domestic firms, a right to compensation in the event of expropriation and free movement of funds, among other matters. Through the new agreement, in addition to these issues, the EU is also aiming to develop a new mechanism for resolving disputes between investors and governments, include clauses concerning environmental protection and workers' rights and establish certain principles concerning the conduct of SOEs.

Through the negotiating process, the EU also intends to improve access to China for European companies, with further liberalisation of sectors in which foreign investment is still subject to restrictions or compliance with abusive requirements (equity caps, mandatory joint ventures, technology transfers, etc.). Meanwhile, the Chinese government is asking for a clearer and more transparent legal framework to enable the country's firms to invest in Europe, where businesses currently have to deal with a regulatory tangle of 28 different legal systems.

The results of the China-EU investment agreement will be determined by a complex mesh of sector interests at a time when various cross-border agreements are being negotiated. For example, at the APEC summit in Beijing, China recently presented a free trade area for Asia (Free Trade Area of the Asia Pacific - FTAAP) as an alternative to the Trans-Pacific Partnership (TPP) spearheaded by the United States. The results of the negotiations are also key to the EU maintaining the status quo of having more favourable regulations for Chinese companies and being more open to investment from the country's firms than its main competitor for this capital, the United States. It is notable that China is also negotiating an investment agreement with the United States, while the US is, in turn, in negotiations with the EU (Transatlantic Trade and Investment Partnership – TTIP). Moreover, China and Canada recently signed an investment agreement which could facilitate Chinese firms' access to the US market through NAFTA.

The largest consumer market

Improved quality of life and standards of living in China, as reflected by a marked increase in salaries, are causing a far-reaching change in consumer behaviour in the country. A new vibrant urban class has emerged with high purchasing power and consumer preferences which are increasingly similar to those of the West. For example, China consumed more than 13 million tonnes of chicken in 2012, more than the United States, following growth of 54% from 2005 to 2010[48].

[47] Bilateral Investment Agreements.

[48] McKinsey Report.

This new demand from Chinese consumers may drive foreign investments, such as that of Chinese Shuanghui International, which invested USD 7,100 million in acquiring the American meat company Smithfield, to extend its production capacity and acquire new meat processing skills and know-how.

In the agri-food sector, China has been actively investing in French vineyards in the Bordeaux region and Chinese companies have been making frequent visits to olive oil mills in Southern Europe. In addition, the major Chinese firm Bright Food recently acquired 100% of the distribution company Miquel Alimentació for USD 110 million. Foreign transactions by Chinese companies to meet domestic demand for certain products are not limited to the agri-food sector. As previously mentioned, Chinese investors have acquired firms with strong brand positioning, especially in the luxury goods sector, to meet the demand of Chinese consumers who are increasingly wealthy and Western in their tastes. One example of such a transaction is China buying into the luxury yachts market to meet domestic demand and access know-how to enable subsequent manufacturing in China.

Involvement in the Juncker Plan

Over the course of 2014 there was a shift in EU policy, implementing measures to reinvigorate growth in the region. Specifically, at the end of 2014, the new President of the European Commission, Jean-Claude Juncker, announced an ambitious plan to invest €315,000 million to bolster demand and economic activity in the EU. Of the announced total, just €21,000 million will be publicly-funded, with €16,000 coming from the EU budget and €5,000 million from the European Investment Bank (EIB). The remainder of the total will come in the form of private or foreign capital, through investments in the different projects submitted to the Commission by member states.

By July 2015, the European Commission and the EIB had approved a total of eight projects: Copenhagen Infrastructure II / Abengoa research, development and innovation II / Energy efficiency in residential buildings / Grifols Bioscience R&D / Äänekoski bio-product mill / Redexis Gas Transmission and Distribution / Arvedi Modernisation Programme / Primary healthcare centres PPP. In addition, the central banks of the core European countries, such as the United Kingdom, Germany, France, Italy and Spain, have announced contributions to the investment plan[49]. The Chinese government has already expressed great interest in investing in some projects[50].

Public joint investment funds

In recent years joint investment vehicles have been created by Chinese sovereign wealth funds and financial institutions in conjunction with public institutions and holding companies from a number of European countries. In 2012, the A Capital investment fund was created in Belgium, in which the state-owned Belgian holding company and China's CIC sovereign wealth fund both have interests. The A Capital fund, amounting to between €250 million and €300 million, invests in midcaps and has offices in Brussels and Beijing. The fund's investments to date include acquiring a 7.7% interest in the Danish company Bang & Olufsen for USD 30 million in a transaction also involving the Chinese investor Sparkle Roll Holding[51]. A Capital also recently invested €5 million in the digital sector through the French company Viadeo, thus obtaining representation on its board of directors. The transaction should allow the French company to increase its market share in China, where it is already allied with Tianji, a leader in the country's digital market[52].

In France, Caisse des Dépôts and China Development Bank (CDB) created a venture capital fund to promote growth in high-potential Chinese and French SMEs. Each party contributed €75 million to the fund, which was managed by Cathay Capital Private Equity. In France, the fund invested in Flexitalic, an industrial technology firm, and Hologram Industries, in the digital sub-sector. In China, the fund acquired interests in the healthcare company Meinian One Health and the logistics business ZM Logistics. As a result of this successful venture, in 2014 the public investment bank BPI France and the CDB created a new larger USD 500 million private equity fund to invest in mid-sized companies in the two countries, through more substantial transactions. Each of the entities contributed USD 100 million and they expect to raise the remaining USD 300 million from other investors[53].

In Italy, the Italian Strategic Fund (FSI) had already created vehicles for joint investment with the Kuwaiti sovereign wealth fund Kuwait Investment Authority (KIA) and the Russian sovereign wealth fund Russian Direct Investment Fund. In the autumn of 2014 a MoU[54] was signed to enter into a joint investment agreement for a total of €1,000 million with China's CIC sovereign wealth fund, to promote bilateral cooperation between the two countries.

In short, although Chinese investment in Europe retreated slightly in 2013 due to a lack of major transactions in strategic sectors, from 2014 Europe is once again set to be a strategic destination for investment from China's public sector, primarily in Central and Eastern Europe, and its private sector, which is more interested in Western Europe. Both China and Europe are working in this direction, launching new projects, initiatives and platforms to jointly contribute to development of the global economy.

49 For more information see: http://europa.eu/rapid/press-release_IP-15-5420_en.htm
50 See: http://www.wsj.com/articles/china-expresses-genuine-interest-in-eus-new-investment-plan-1417610133
51 See: http://www.acapital.hk/A_CAPITAL_BANG_OLUFSEN_19_July_2012_Press_Release_English.pdf
52 See: http://www.acapital.hk/ACAPITAL%20Viadeo%20PressRelease%2027%2006%202014%20ENG.pdf
53 See: http://www.ft.com/intl/cms/s/0/66d449d8-0062-11e4-8aaf-00144feab7de.html?siteedition=intl#axzz3PXd8wYcq
54 Memorandum of Understanding.

Box IV.

The New Silk Road, a major challenge

Author: Javier Solana, Chairman of ESADEgeo

The rise of China is probably the most significant geostrategic event of the past twenty years. However, the West has not accommodated China or other emerging markets in global governance frameworks to the extent of their geopolitical and economic influence.

The expansion of China's presence in Asia, Africa and Latin America has been marked by strictly bilateral relations and investment in infrastructure, primarily to obtain commodities. This strategy has been implemented by state-owned enterprises, often failing to comply with certain international standards. As a result, by leveraging its USD 3.8 trillion foreign exchange reserve, China has become the top provider of financing to developing countries. In fact, the China Development Bank already extends more loans than the World Bank itself.

For some time, the West has been urging Beijing to switch from bilateral financial diplomacy to a multilateral approach more in tune with Western standards. It is often said that China should be more involved in providing global public goods. President Obama even went so far as to accuse China of being a free rider.

The long-awaited time for change came with Xi's ascent to power, either due to growing Chinese interest in global affairs or to economic necessity. The Asian giant is experiencing slowing growth at the same time as key trading partners are introducing protectionist policies. Exports alone are no longer enough, internal markets must also be cultivated abroad. This will drive demand for Chinese products and provide an outlet for the surplus capacity in some of the country's sectors. With this purpose in mind, a more multilateral approach is needed, along with minimisation of investment risk. This has been reflected in China's recent foreign policy initiatives and its greater commitment to the globalisation process, which is highly beneficial for the nation.

The creation in July last year of the New Development Bank (NDB) was a step in this direction. The NDB brings together the five BRICS economies – Brazil, Russia, India, China and South Africa – and has capital of USD 100,000 million. Following the same lines, during the Asia-Pacific Economic Cooperation Forum (APEC) in Beijing, Xi announced the creation of the Asian Infrastructure Investment Bank (AIIB), headquartered in Shanghai.

Lastly, there is the creation of a USD 40,000 million fund to finance the New Silk Road, complementing prior commitments to invest in Central Asia totalling more than USD 50,000 million. The fund forms part of the New Silk Roads initiative through which China intends to invest in Eurasian infrastructure projects. The plan encompasses sixty countries, home to almost two thirds of the world population, representing a third of global GDP. It will include an overland "economic belt" passing through Central Asia and a "21st century maritime route" through the Indian Ocean, the South China Sea and the Mediterranean. Combined, the two routes will form a network, rather than a single path, facilitating connections between Asia and Europe.

The European segment of the network will include the Greek port of Piraeus in its maritime branch, which is partially operated by the Chinese state-owned shipping company COSCO. Approximately 80% of China-EU trade is maritime. Piraeus will be connected to the rest of Europe through infrastructure in the Balkans and Hungary, financed by China. This improved connectivity will consolidate China's position as the EU's main trading partner, a position it has held for the past ten years. This initiative is another demonstration of China's commitment to consolidating its status as a Eurasian power connected to the two most dynamic points of the continent: East Asia and Western Europe. China also occupies the positions lost by Russia in Central Asia and is attempting to put an end to territorial disputes with its neighbours.

In this context, the United Kingdom's founding membership of the AIIB seems particularly significant. The UK's new position has encouraged other European countries (France, Germany, Italy, Austria, Switzerland and Luxembourg) and nations from Asia-Pacific (Korea and Australia) to invest in the AIIB. This shift is seen by Washington as a geopolitical setback for the United States.

In my view, this interpretation is incorrect. We have not successfully reformed the international institutions created following the Second World War, to make them inclusive and effective. The Asian Development Bank (ADB) is a good example of this. It is led by Japan and the US, each of whom hold 13% of the voting rights, and has always had a Japanese president. China's share of votes is less than 6%. The same is true of the World Bank and the IMF, which remain controlled by Europe and North America. The reform agreed in 2010 at the G20 summit in Seoul increased China's quota from 3.65% to 6.19%. But even though this reform was a small step in the right direction, it has not yet been implemented, as the executive branch of the US government is unable to convince Congress to approve the agreement. Worse still, five years later, the reform is now outdated.

In view of all of this, it should be no surprise that China has created a new regional development bank, in this case specifically for infrastructure. This demonstrates that China's new initiatives are not revisionist but instead reactive. If existing institutions do not incorporate China and other emerging markets, these nations will be forced to create new structures. As a result, global governance could fragment into a system of ideological and economic blocs – a form of subdivided globalisation. The inclusion of the United Kingdom and other European countries in the AIIB is therefore welcome, as it may promote complementary action by these new institutions rather than rivalry. If this were to happen, we would no longer be facing a zero-sum game. Ideally, the two Asian development banks should be able to complement each other, as is the case in Latin America of the Inter-American Development Bank (IDB) and the Development Bank of Latin America (CAF). This would also have been a great opportunity for the European Union to be represented directly in united form at the AIIB, as is the case at the G20 and the World Trade Organisation.

The West must remain open to new Chinese proposals, whilst working determinedly to ensure multilateralism, transparency and accountability in new institutions. Investments would thus have to meet market criteria, environmental protection requirements and baseline employment standards. More measures must be implemented, such as including the Renminbi in the basket of currencies used to calculate the IMF's Special Drawing Rights. Complementary characteristics must also be found in the two major trade negotiations in Asia: the Trans-Pacific Partnership (TPP), spearheaded by the US, and the Free Trade Area of the Asia-Pacific (FTAAP), favoured by China. In general, a Western approach of this kind would impel China to assume proportional responsibility for providing global public goods.

China's more multilateral approach and greater commitment to globalisation are good news. Over the coming months it would be beneficial if the EU, US and China were able to align their interests, with a view to Beijing's presidency of the G20 in 2016. Now seems the right time for the US and China to promote mutual trust in strategic matters to move forward with assuming global responsibilities. In today's extensively interdependent world, this is an unmissable opportunity.

Methodology

This report uses three official sources of statistics to calculate Chinese FDI: MOFCOM (official Chinese source), UNCTAD (source for international comparison) and Eurostat (official European source). These sources allow for analysis of an extended period of time, comparisons of countries and a breakdown of Chinese investment by business sectors. However, as mentioned in the prior edition of this report, these official sources offer a limited view of China's foreign investment, for a number of reasons[55]. In particular, most Chinese investment is through OFCs, which are not generally the final investment destinations, and prevent transactions from being traced through official records such as those of the MOFCOM. For example, in Latin America up to 88% of Chinese FDI is carried out through tax havens such as the Cayman Islands and the British Virgin Islands, meaning that the ultimate destination of the investment cannot be identified. Another significant problem is that up to 88.2% of FDI in Asia is in Hong Kong (China), a region used to obtain improved access to financial markets for companies which eventually invest in China once again (round tripping). The presence of OFCs and round tripping in official statistics makes it very difficult to interpret China's global investment.

To resolve this problem, ESADE China Europe has created its own database, which records business transactions using its own and secondary sources, a methodology that has already been employed by other advisory firms and think tanks specialised in monitoring China's global investments. Although the database offers a more faithful picture of the actual amount and characteristics of Chinese investment in Europe than that given by official sources, it is not without limitations, as many transactions are not public or have not been recorded by official bodies. Estimates and application of a number of criteria are therefore necessary. The FDI which forms the basis of the database is understood to comprise transactions that entail acquisition of at least a 10% interest in a resident company by a non-resident firm for an amount exceeding USD 30 million.

The transactions used to create the ESADE China Europe database are those recorded by the Heritage Foundation, Bloomberg, FDI Markets and ACCIÒ-Catalonia Trade and Investment, complemented through the monitoring of transactions by the ESADE China Europe research team which prepared this report: Ivana Casaburi, Qiaoshan Xue and Adrián Blanco.

We would like to thank the ACCIÒ-Catalonia Trade and Investment team for contributing their experience and know-how to the creation of the ESADE China Europe database, and especially for assisting with analysis of the FDI Markets data.

55 See page 57: http://itemsweb.esade.edu/research/esadegeo/ESADE_ES_PDF.pdf

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CHAPTER II

The main target sectors for Chinese investment in Europe

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The main target sectors for Chinese investment in Europe

Boxes

Charts and tables

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2.1. Which sectors are targets for Chinese investment, globally?

Fifteen years after China first allowed companies to make foreign investments (Go Out Policy), Chinese capital is now present globally in almost all economic sectors, including extraction of commodities, research centres, smartphone development, airports, construction of port docks, premium real estate in major cities, hotels, vineyards, wineries, heavy machinery and the chemicals industry. In recent years, the country's investment has expanded to such a great extent internationally that no sector has been left untouched by Chinese private investors, businesses or sovereign wealth funds.

Although globally Chinese firms operate in almost all economic sectors, they are largely concentrated in six industries, in terms of dollars invested: business services and leasing, the financial sector, mining and extraction, manufacturing, retail and wholesale and transport. Investment in these industries, and above all in the financial and mining sectors, requires a substantial volume of resources, hence their significant statistical importance. Examples of these transactions in the financial sector include ICBC's USD 5,600 million investment in South Africa's Standard Bank, and in the mining sector Minmetals' USD 5,850 million investment in Glencore in the Peruvian copper sub-sector. In terms of the number of Chinese businesses operating outside the country, the most significant sectors are retail-wholesale (including distribution) and manufacturing, with 7,400 and 5,600 companies, respectively.

The top sector for investment, receiving a cumulative total of USD 195,500 million and accounting for 29.6% of the total, is the **business services and leasing** sector. This industry reflects a considerable volume of investment, as it includes incorporations of holding companies, even if investments are subsequently focused on other economic sectors. Many of these transactions are performed in locations with special benefits for companies of this kind, such as Hong Kong and Singapore in Asia or Luxembourg and the Netherlands in Europe.

The sector with the second highest volume of Chinese investment globally is the **financial sector** (USD 117,000 million, 17.7% of the total). The largest transactions were concentrated at the beginning of the subprime crisis, which drove down the value of financial institutions in the US and Europe due to their exposure to toxic assets, thus fuelling acquisitions by Asian investors. In fact, on many occasions the international investments in this sector have been by China's two main sovereign wealth funds, CIC and SAFE, which have acquired interests in some of the major global investment funds, such as JC Flowers, Blackstone and Blackrock.

Chinese investment in the financial sector takes two very different forms: acquisitions of large blocks of shares whereby the investor becomes a sleeping partner with no management involvement, or opening of offices overseas, in order to provide financial coverage to Chinese companies' internationalisation processes and to access new retail banking markets. Examples of purchases of blocks of shares include CIC's acquisition of 9% of the Blackstone investment fund (USD 3,000 million), China Development Bank's (CDB) acquisition of 3% of Barclays (USD 3,000 million), Ping An's acquisition of 4% of Fortis (USD 2,700 million) and CIC's acquisition of 10% of Morgan Stanley (USD 5,000 million). Entities that have established foreign offices and branches around the world include ICBC, Bank of China and China Construction Bank.

However, Chinese financial institutions' global presence is not limited to direct investment via acquisitions of local firms and opening offices to expand their foreign network. In addition to such investments, Chinese banks, and particularly CDB and EXIM Bank, have extended sizeable loans in view of the limited access to international financing and the close relationship between these institutions and the government in Beijing. Financing for such projects has primarily been extended in Latin America, totalling USD 116,000 in the region, and has even on occasion exceeded the combined annual total of financing provided by the World Bank and the Inter-American Development Bank[1].

A third very important sector in terms of China's global investments is **mining and extraction**, including oil and gas (a cumulative amount of USD 106,000 million, 16% of the total). The country's substantial investment in these sectors is driven by its appetite for commodities as a result of its extensive industrial and urban development. The *modus operandi* of Chinese firms, and especially state-owned enterprises, is to invest through majority or minority interests in local companies. In terms of developed countries, Chinese businesses have made numerous investments in Australia and Canada, both economies which are characterised by their abundant natural resources. They are also locations in which Chinese firms have not encountered barriers to investment. Examples of these transactions include the mining firm Yanzhou Coal's acquisition of the Australian company Felix Resources for USD 2,950 million or the CIC sovereign wealth fund's USD 1,500 million purchase of an interest in the Canadian copper company Tech Resources.

Chinese energy companies have been particularly active in developing countries, with state-owned hydrocarbon management companies undertaking many major acquisitions. For example, CNOOC acquired 45% of South African Petroleum in Nigeria, while Sinopec purchased 97% of Rosneft in Russia and 51% of National Iranian Oil in Iran. In addition to hydrocarbons, Chinese firms have also made substantial investments in mining and extraction, either by acquiring local companies or by winning tenders to exploit mining assets. The most significant minerals in terms of Chinese investment are iron, coal, copper and aluminium and most of the related transactions took place in sub-Saharan African countries such as Uganda, Ghana, Zambia, Cameroon and Sierra Leone, as well as in Latin America – above all Peru.

Chinese investment in the primary sectors of developing nations is very important for these countries, beyond the benefits traditionally associated with foreign direct investment (job

[1] Source: "China-Latin America Finance Database". Inter-American Dialogue. 2015.

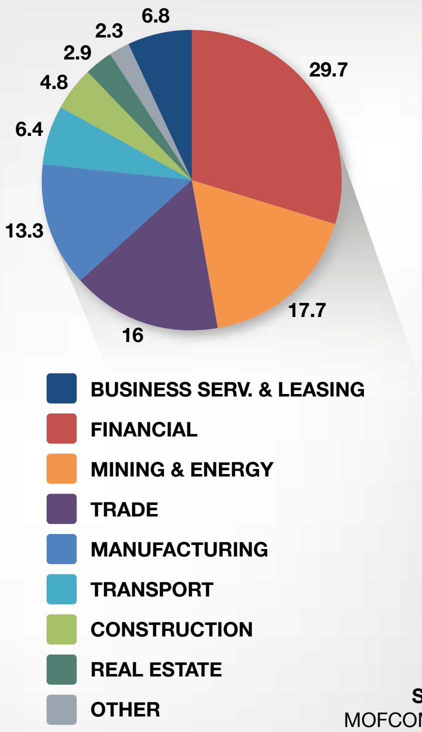
creation, government revenue and externalities). Firstly, such investment helps to increase countries' capacity for generating energy and producing minerals, which is crucial in nations with strong growth in demand for energy from both industry and households. Secondly, following extraction, most products are exported to China, generating a considerable transfer of wealth from China to the producing countries. In contrast, the downside of a commercial relationship based on exports of commodities is that it has resulted in numerous countries being over dependent on Chinese demand for products and, in turn, on China's economic cycle.

The fourth most important sector in terms of Chinese foreign direct investment is **retail-wholesale**, with cumulative investment of USD 87,000 million (13.3% of the total). This market segment amasses the highest number of Chinese companies with foreign operations, with more than 7,400 firms. Most operations in the retail-wholesale sector are focused on expanding and facilitating the commercial activity of Chinese companies abroad. In recent years, such businesses have grown exponentially, accompanying China's export and import activity and positioning the country as the world's leading goods trader in 2013.

The sector with the fifth largest volume of Chinese foreign direct investment is **industry and manufacturing** (a cumulative amount of USD 42,000 million, 6.4% of the total).

Chart 1

Main recipient sectors of cumulative Chinese foreign investment (2013 data) as a percentage of total investment



Source: MOFCOM, 2014

These operations can be divided into three types. Firstly, Chinese companies have invested in factories abroad – often with Chinese materials and personnel – to produce and sell goods in local markets. Such activities have been undertaken by major industrial groups in countries which are geographically remote and have sufficiently attractive labour costs. An illustrative example is the automotive industry, with Chery opening factories in Venezuela to manufacture cars and BYD investing in Indonesia to produce batteries.

Secondly, major Chinese companies have taken over or invested in manufacturing companies in developed countries, to access their know-how, technology, management techniques or brand image. Noteworthy transactions have been undertaken, again in the automotive industry, such as Geely's acquisition of Volvo (USD 1,500 million) and Dongfeng's investment in Peugeot (USD 1,100 million). Significant investments have also been made by China in the manufacturing subsectors of shipbuilding, textiles, chemicals, pharmaceuticals, computing and electronics.

Thirdly, in response to sharp rises in domestic labour costs, Chinese firms have started to invest in offshoring a number of labour-intensive activities to neighbouring Asian countries where salaries are lower. The minimum hourly wage in China is USD 1.19, compared to USD 0.28 in India, USD 0.52 in Indonesia, USD 0.73 in the Philippines and USD 0.64 in Vietnam[2]. This situation has driven Chinese companies to invest in new factories in these countries, above all in the textile sector.

A sixth key sector is **infrastructure, transport and logistics** (a cumulative amount of USD 32,000 million, 4.8% of the total). Chinese investments in these sectors have been made in conjunction with the country's growing commercial ties around the world. Chinese companies have invested to modernise and expand the capacity of infrastructure, on occasion managing the infrastructure itself, such as container ports. Some examples of these transactions, of a highly strategic nature, include China Ocean Shipping (COSCO) at the Port of Piraeus (Greece), China Merchants in the Port of Togo (West Africa), China Communications Construction in the Port of Colombo (Sri Lanka) and Hutchinson in the Port of Barcelona (Spain).

Occasionally, investments have been the result of Chinese construction companies winning contracts to develop infrastructure. In such tenders, Chinese firms have a threefold advantage against the competition: highly competitive pricing, strong financial backing for the construction company and the resulting reduction in countries' dependence on Western construction firms. Examples of such transactions include those undertaken by the SOE China Railway Construction Corporation, which recently built a key railway line in Libya, a motorway in Algeria and part of the Mecca Metro (Saudi Arabia). Lastly, a growing number of the country's logistics companies, such as SITC Logistics, Shanghai Yunda Express, Kerry Logistics and SF Express, have opened distribution centres in other nations, with the aim of increasing the commercial capacities of Chinese firms.

[2] See: http://www.china-briefing.com/news/2014/06/03/china-asean-wage-comparisons-70-production-capacity-benchmark.html

2.2. The main target sectors for Chinese investment in the EU[3]

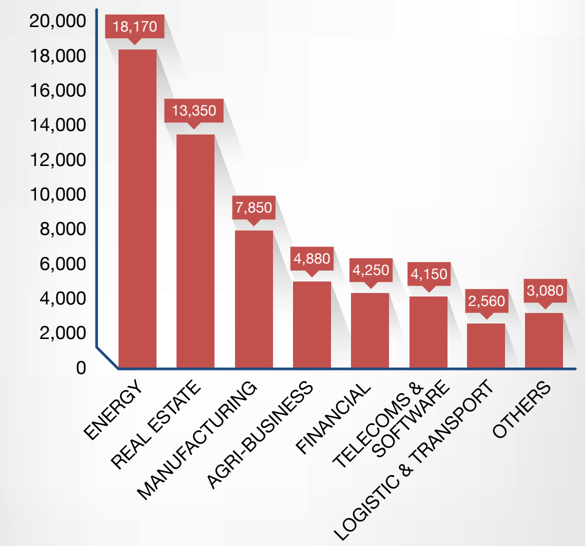
The pattern of Chinese FDI in the EU by sector differs from that in other regions of the world in three respects. **Firstly**, there is very limited activity in the mining sector and extraction industries, with almost no transactions. The EU has not been a target for investments in this sector due to both the smaller deposits of mineral resources and the stringent environmental controls imposed on extraction projects. Although there have been several significant transactions in the sector, they have been due to certain multinationals having their registered office and consolidating their accounts in London. For example, Sinochem invested in the commodities company Emerald, which specialises in oil and gas operations in the Middle East and Latin America, but has its registered office in London, where the transaction was recognised.

Secondly, there are more acquisitions of manufacturing companies by Chinese firms in the EU than in other regions of the globe. These investments are primarily in countries with sound industrial bases, comprising mid-sized highly specialised businesses, such as Germany or the United Kingdom. The main objective of Chinese companies in this flurry of transactions is to acquire technological capabilities and know-how. This thirst for knowledge is related to the change in China's growth model, wherein the private sector is set to expand, along with the top end of the value chain.

Thirdly, there are more investment projects related to scientific and technical research than in other regions of the world. Major Chinese firms have invested USD 765 million in such activities, by far surpassing the USD 460 million invested in the United States[4], a country where companies such as Huawei and ZTE have encountered difficulties and have been accused of ties to the Chinese government that could compromise national security. Chinese businesses see the EU as a very attractive destination for this kind of investment, due to the workforce's high level of scientific and technical training, the concentration and coverage of technological centres and world-class universities, the region's physical and technological infrastructure and the development and presence of numerous industrial clusters that collaborate closely with R&D centres.

Chart 2

Chinese investment in the EU by sectors, in millions of USD (2010-2014)



Source: ESADE China-Europe.

According to the database prepared by ESADE China Europe, 95% of Chinese investment in the EU in the period from 2010 to 2014 was concentrated in seven business sectors. The top sector for investment is energy, with USD 18,170 million (31.2% of the total). Second is the real estate sector, with USD 13,350 million (22.9% of the total). The sector that received the third largest volume of Chinese FDI in the period was manufacturing, with USD 7,850 million (13.5% of the total). The fourth sector was agriculture, with USD 4,880 million (8.4% of the total), followed by the financial sector with USD 4,250 million (7.3%), telecommunications and software with USD 4,150 million (7.1%) and the logistics, transport and infrastructure sector with USD 2,560 million (4.4%).

3 The geographical scope of Europe used for this analysis is limited to the EU-28, comprising Austria, Belgium, Bulgaria, Cyprus, Croatia, the Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden and the United Kingdom.

4 Source: MOFCOM

Interests acquired in the energy and electricity sector[5]

The European energy and electricity sector received the most Chinese investment in 2010-2014, with a total of USD 18,170 million, almost one third of the dollars invested by the country in Europe. Chinese investors have made a multitude of investments in the European energy and electricity sector, usually acquiring interests in state-owned enterprises through transactions of an exclusively financial nature. For European governments, Chinese investment represents a beneficial injection of liquidity without interference in how companies are run. For Chinese investors, such transactions are a means of diversifying their investment portfolio through a low-risk asset. Examples include the Three Gorges acquisition of 21% of Energias de Portugal, oil company Sinopec's purchase of 49% of Talisman Energy or the CIC sovereign wealth fund's acquisition of 30% of France's GDF Suez.

Chinese investments in this sector grew in 2014, including three major transactions in Italy. The first two were acquisitions of minority interests in state-owned enterprises: People's Bank of China bought 2% of the electricity company ENEL – which owns Spain's Endesa – and 3% of the oil company ENI, for a total of €2,700 million. The third transaction entailed joint investments. The Italian Strategic Fund and Shanghai Electric acquired 40% of the Italian energy company Ansaldo Energia, in a transaction that will result in two joint ventures – one to manufacture gas turbines for the Asian market and another to create a research and development centre in Shanghai. In mid-2014, the Italian government announced an investment of USD 2,800 million by Chinese investors in the electricity sector. Specifically, State Grid Corporation bought 35% of the shares in a subsidiary of the Italian bank CDP Reti, which in turn owns 30% of the gas transmission group Snam and which will also acquire 30% of the electricity company Terna.

Aside from these major financial transactions involving Chinese and European state-owned enterprises, a number of smaller Asian firms, specialised in renewable energy, have been increasing their presence in Europe. These businesses are looking to acquire new technological capacities in renewable energy to develop in China's domestic market, which suffers from serious environmental problems and overdependence on fossil fuels. These investments form part of a decisive strategy by the Chinese government to make the country the largest producer of renewable energy in the world, primarily from solar farms, wind farms and hydroelectric plants. Chinese firms that have invested in the EU's renewable energy sector include Giangsu, Comtec Solar and Trina Solar.

Table 1 Key Chinese investments in the **European energy and electricity sector 2010-2014** (in millions of USD)

YEAR	CHINESE CO.	AMOUNT	INVOLVED PARTY	COUNTRY
2011	Three Gorges	3,510	Energias de Portugal	Portugal
2011	CIC	3,240	GDF Suez	France
2014	State Grid Corp of China	2,811	Cassa Depositi e Prestiti SpA	Italy
2012	Sinopec	1,500	Talisman Energy	United Kingdom
2014	Znshine Solar	685	Alternative/Renewable energy	United Kingdom
2014	Power Construction Corp	560	Ansaldo Energia	Italy
2011	CNPC	510	INEOS Britain	United Kingdom
2011	CNPC	510	INEOS France	France
2012	State Grid	510	REN	Portugal
2012	Hanergy	510	Q-Cells	Germany
2012	China Three Gorges Corp	475	EDP Renovaveis SA	Portugal
2013	China Huadian Engineering	452	Greenfield	Romania
2012	Sinopec Kantons Holdings Ltd	273	Mercuria Energy Asset Management BV	Netherlands
2014	Unisun	268	Alternative/Renewable energy	Romania
2013	China Power Investment	260	Enemalta	Malta

Source: ESADE China-Europe.

[5] The financial sector is the only one of the main seven sectors not dealt with in section 2.2 as a full chapter of the last edition of the report analysed the industry in detail (see: http://itemsweb.esade.edu/research/esadegeo/ESADE_ES_PDF.pdf)

Real estate, Chinese investors' favourite sector

In recent years, it has become clear that real estate is of great interest to Chinese investors, whether they be individuals, private funds or sovereign wealth funds. Chinese investors' transactions in the sector from 2010 to 2014 totalled USD 13,350 million. European real estate assets fit well with many individual investors' and investment funds' strategy of diversifying their portfolios geographically, while retaining a low level of risk and stable long-term returns. Transactions in the real estate sector have involved all kinds of assets, including not only residential property but also logistics centres, hotels, offices, healthcare centres, shared service centres and student halls of residence. The city most favoured by investors is London, well ahead of other preferred locations such as Paris, Berlin, Frankfurt, Stockholm, Amsterdam and Madrid. In particular, premium assets are acquired in the most exclusive neighbourhoods of these European capitals, although there is some evidence of transactions in outlying areas.

Transactions in this sector mainly took place in 2013 and 2014, with more than USD 3,000 million of investments made in each year[6]. Major transactions include the purchase of the Chiswick Park building in London by the CIC sovereign wealth fund from the US Blackstone fund and Dalian Wanda's acquisition of Edificio España in Madrid. Other regular investors in this sector in Europe include Greenland Group, Chinese Overseas Land & Investment and R&F Properties. In the coming years, a rise in such transactions can be expected as scheduled projects take form. One example is the China Minsheng Investment, announced in 2015, which will inject USD 1,500 million into building a new financial district in London[7].

In the tourism segment of the real estate sector a number of key transactions have taken place within the hotel business. The HNA hotel chain acquired 20% of the Spanish group NH for USD 230 million, Dalian Wanda bought Edificio España in Madrid for USD 360 million to turn it into accommodation for executives, and the multimillionaire Guo Guangchang may purchase the French residential group Club Med for more than USD 1,000 million.

Table 2 Key Chinese investments in the **European real estate sector 2010-2014** (in millions of USD)

YEAR	CHINESE CO.	AMOUNT	INVOLVED PARTY	COUNTRY
2013	ABP China Holding Group	1,600	Greenfield	United Kingdom
2014	China Investment Corporation	1,285	Chiswick Park	United Kingdom
2013	Wanda	1,090	Greenfield	United Kingdom
2014	Shanghai Greenland	990	Commercial Estates Group	United Kingdom
2014	Shanghai Greenland	980	Minerva	United Kingdom
2014	China Life	950	Songbird	United Kingdom
2012	Shandong Heavy	930	Kion	Germany
2013	SAFE	840	UPP Group	United Kingdom
2014	Sanpower	790	House of Fraser	United Kingdom
2012	Sany Heavy	480	Putzmeister	Germany
2012	SAFE	440	Greenfield	United Kingdom
2012	CIC	400	Deutsche Bank	United Kingdom
2013	Ping An	390	Commerz Real	United Kingdom
2013	Fosun	360	Club Med	France
2014	Dalian Wanda	360	Santander	Spain

Source: ESADE China-Europe.

6 Source: Real Capital Analytics and ESADE China Europe Club

7 See: http://uk.reuters.com/article/2015/02/15/uk-china-britain-property-idUKKBN0LI04X20150215

Technology-based manufactured goods

The importance of Chinese investment in the European manufacturing sector stems from clearly complementary qualities. European firms have substantial technological capabilities and know-how in a number of industrial subsectors in which Chinese firms have a notable deficit. In contrast, Chinese companies are highly liquid and have financial muscle as a result of robust growth tied to the expansion of the country's economy in recent years – these qualities are welcomed by Europe's manufacturing sector. It is therefore no surprise that a growing number of Chinese companies have acquired interests in European businesses, or taken them over, in sectors such as heavy industry and the automotive field, for a total amount of USD 7,850 million in 2010-2014.
Transactions in the manufacturing sector can be divided into two types according to the size of the target company. On the one hand, Chinese firms have purchased substantial majority or minority interests in European multinationals. The Geely Group has been particularly active in this regard, acquiring Volvo and thus investing USD 1,500 million in Europe, as has Dongfeng, which acquired 19% of Peugeot for USD 1,100 million, and ChemChina, which acquired the Italian tyre company Pirelli for USD 7,100 million at the start of 2015[8].

On the other hand, Chinese companies have invested in the capital of mid-sized specialised technological-industrial companies or have taken over such firms, primarily in Germany ("Mittelstand") and the United Kingdom. Examples include Weichai's acquisition of Kion, a German firm specialising in hydraulic machinery, and Sany Heavy Industries' acquisition of the German company Putzmeister, specialised in construction machinery and trucks. Lastly, some industrial companies have opened sales offices and after-sales offices to meet European customers' requirements from a nearby location, such as the technological goods manufacturer Huawei and the electrical appliances manufacturer Haier.

Table 3 Chinese investments in the **European manufacturing sector 2010-2014** (in millions of USD)

YEAR	CHINESE CO.	AMOUNT	INVOLVED PARTY	COUNTRY
2010	Geely Auto	1,500	Ford	Sweden
2014	Dongfeng	1,100	Pugeot	France
2013	Wanda	500	Sunseeker	United Kingdom
2012	Shandong Heavy	460	Ferretti	Italy
2012	Wuhan Iron and Steel	450	ThyssenKrupp	Germany
2011	CITIC	420	KSM Castings	Germany
2013	CSR	400	ZF Friedrichshafen	Germany
2014	Geely Auto	200	Emerald Automotive	United Kingdom
2010	Great Wall Motors (GWM)	200	Automotive OEM	Bulgaria
2012	BYD Electronics	200	Greenfield	Bulgaria
2011	Saint-Gobain Performance Plastics Shanghai	167	NV Bekaert SA	Netherlands
2011	Wolong Holding Group Co Ltd	145	A-TEC Industries AG	Austria
2011	Wolong Holding	140	ATB Group	Austria
2011	Jinsheng Industry	130	EMAG	Germany
2014	Rizhao Jin He Biochemical Group	128	Chemicals	Hungary

Source: ESADE China-Europe.

8 This transaction, which is the largest performed by a Chinese group in Europe to date, has not been included as it took place in 2015, and the ESADE China Europe database covers 2010-2014

Growing interest in the agri-food sector

As a result of the country's economic development in recent years, Chinese citizens' personal income has increased and millions have entered the urban middle class. Higher income and assumption of Western lifestyles have driven demand for certain foods, creating a huge business opportunity for Chinese companies. This opportunity has fuelled Chinese firms' investment in the foreign agri-business sector, in particular in the EU, which amounted to USD 4,880 million in the period from 2010 to 2014. Chinese companies acquire mid-sized European businesses with a view to obtaining the technical and manufacturing know-how required to replicate their business models locally, to secure the supply of products in China and to control the whole production chain. Examples of this strategy include the acquisitions of French vineyards, especially in the Bordeaux region, Longhai International's takeover of Château Latour-Laguens, Fosun buying 20% of Spain's Osborne Group and the Bright Food Group's recent acquisition of the Catalan company Miquel Alimentació.

In addition to covering emerging demand for more sophisticated consumer products, other Chinese firms are looking to increase their production capacity to meet demand from the segment with the lowest purchasing power, which has increased exponentially in recent years. One example is the acquisition by WH International (formerly Shuanghui International Holdings) of the US company Smithfield – the largest producer of pork in the world. The transaction also affected the US multinational's European assets, which are now Chinese-owned, and the Spanish company Campofrío. This investment also forms part of Chinese businesses' strategy in response to the shift in China's base diet from rice to meat, whereby meat consumption has tripled since 1986. It is estimated that by 2050 China will import USD 150,000 million of chicken, pork and beef annually[9].

In addition to investing in the capital of existing European companies, Chinese investors have also been involved in financing ambitious agri-food development projects. For example, Tianjin State Farms announced in late 2014 that a consortium of Chinese investors would be backing agricultural operations in Bulgaria[10]. Moreover, in a strictly financial transaction, the Beijing private equity fund Hony Capital acquired the British company Pizza Express for €1,540 million in one of the largest investment transactions in the European agri-business sector involving Chinese investors. More recently, in 2015 the Chinese firm Bright Foods acquired the Catalan food retail group Miquel Alimentació for an estimated €110 million.

Table 4 Key Chinese investments in the **European agricultural sector 2010-2014** (in millions of USD)

YEAR	CHINESE CO.	AMOUNT	INVOLVED PARTY	COUNTRY
2012	Bright Foods	1,940	Weetabix	United Kingdom
2014	Hony Capital Ltd	1,540	Gondola Group Ltd	United Kingdom
2014	COFCO	1,210	Nidera	Netherlands
2012	Synutra	120	Sodiaal	France
2013	Tianjin State Farms Agribusiness Group	71	Greenfield	Bulgaria
2014	Fosun	n.av.	Osborne	Spain

Source: ESADE China Europe (n.av: not available)

2.3. Key sectors:

2.3.1. Investment in the telecoms, IT and start-up sectors

The telecoms and information technology (IT) sector has also seen a notable number of Chinese investments, amounting to USD 4,150 million in the 2010 to 2014 period. The most significant recent investments in telecommunications reflect growing Chinese interest in the sector. At the end of 2014, the French company Alcatel-Lucent, one of the largest European operators, sold its business division to the Chinese firm Huaxin for USD 310 million. This transaction will afford the French company a significant liquidity boost, allowing it to focus on its core activities, while the Chinese firm has gained access to the former's technology and sales networks. Also in 2014, the telecoms giant China Telecom – one of the country's top three operators, alongside China Unicom and China Mobile – extended its presence and network coverage in Europe by establishing a new Point of Presence (PoP) in Amsterdam, adding to its existing PoPs in London, Stockholm and Milan. In early 2015, meanwhile, the China Central and Eastern Europe Investment Cooperation Fund announced its plans to acquire a controlling interest in the Polish telecoms engineering firm Electronic Control System, which specialises in rendering services to telecoms operators and building and maintaining networks.

9 http://www.forbes.com/sites/jackperkowski/2014/09/25/chinas-growing-food-problemopportunity/

10 See: http://www.globalaginvesting.com/news/NewsListDetail?contentid=4862

In the IT sector, two technology companies have been particularly active, with years of investment and project development in Europe: Huawei and ZTE. Huawei is well established in the core European markets, offering a variety of technological services and solutions and employing 7,000 workers, and generating annual turnover of more than USD 4,000 million. From 2013 to 2014 alone, the company undertook more than 20 investment projects in Europe, such as acquiring the British internet-of-things firm Neul, and opening a new R&D centre in Sophia Antipolis (France) and an innovation centre in Walldorf (Germany). The technology company ZTE[11], which supplies telecommunications equipment and provides network solutions, is also present in 20 European countries and has invested in more than ten projects in Europe in the last two years. Smaller Chinese IT firms are also present in Europe, such as TP-Link Technologies, which specialises in routers, IP services and network maintenance. Haier, which produces electrical appliances, telecommunications handsets and also serves the energy sector, is another example of a Chinese business growing in Europe. Haier Europe, headquartered in France, has subsidiaries in Belgium, the United Kingdom, Italy, Poland, Russia and Spain. Its European sales in the 2014-2015 financial year amounted to USD 550 million, up 10% on the prior year. The company also employs around 400 workers in Europe. Having achieved six consecutive years of double-digit growth globally, the firm is aiming to lead the internet era by focusing on smart factories and smart devices. The company currently has a factory in the north of Italy and will open another in Russia next year

A number of technological start-ups have emerged from China in recent years, including Alibaba, whose market capitalisation of USD 230,000 million exceeds those of Facebook, Amazon and eBay[12]. Over the last few years, the Chinese economy has produced 27 "unicorns" (technology companies with a valuation of more than USD 1,000 million, generated through IPOs and rounds of financing), such as the smartphone manufacturer Xiaomi, the Baidu social network and the e-commerce baby goods seller Beibei. These companies, which are increasingly financed through IPOs, rounds of financing or by private equity, can be expected to step up their foreign operations, in a quest to increase their capital and enter new growth markets. This expansion is an interesting opportunity for European technology firms, in terms of both the capital injected and the access it would provide to the tightly guarded Chinese internet market. To date, Chinese internet firms have undertaken very few transactions in Europe, although there have been some notable examples, such as Tencent's acquisition of the mobile gaming firm Miniclip[13].

Table 5 Key Chinese investments in the **European telecoms and IT sector 2010-2014** (in millions of USD)

YEAR	CHINESE CO.	AMOUNT	INVOLVED PARTY	COUNTRY
2012	Huawei	1,500	Greenfield	Hungary
2011	Lenovo	670	Medion	Germany
2014	Huaxin	310	Alcatel-Lucent	France
2013	Huawei	200	Greenfield	United Kingdom
2010	Huawei Technologies	135	Communications	Italy
2011	ZTE	123.8	Greenfield	Austria
2013	Huawei Technologies	124	Greenfield	Denmark
2012	Huawei Technologies	91	Greenfield	Finland
2011	Huawei Technologies	80.9	Greenfield	United Kingdom
2011	China Unicom Americas	74.6	Greenfield	France
2010	Huawei Technologies	67.3	Greenfield	United Kingdom
2011	Huawei Technologies	67.3	Greenfield	United Kingdom
2011	ZTE	67.3	Greenfield	United Kingdom
2013	Huawei Technologies	62	Greenfield	Romania
2011	Huawei Technologies	55.4	Greenfield	Hungary

Source: ESADE China-Europe.

11 Zhong Xing Telecommunication Equipment Company Limited
12 "China's Dangerous Digital Agenda". Robert D. Atkinson and Paul Hofheinz. Project Syndicate, 2014.
13 See: http://blogs.wsj.com/moneybeat/2014/09/17/alibaba-highlights-european-growth-plans-as-roadshow-comes-to-london/

Box I.

The phenomenon of Smart Cities

Author: Dr. Mila Gascó, Institute for Public Governance and Management, ESADE Business & Law School

Cities are growing at a vertiginous pace, through an unprecedented process of urban development. Between 1950 and 2014 alone the urban population grew fivefold, and by 2050, according to UN forecasts, 70-75% of the global population is expected to live in cities.

China is no exception. A quarter of the world's 500 largest urban areas is located in China. In 2002 the country's proportion of city dwellers was 36%, but by 2050 this ratio is expected to rise to 70%, meaning that more than two thirds of the Chinese population will live in cities. This process of urban development is actually relatively new to the Asian giant. In fact, 2012 was a historical milestone for the country: for the first time, the People's Republic of China became a predominantly urban country, with 712 million people (52.6% of the population) living in cities.

This concentration in urban hubs has a positive impact, as it increases cities' political and economic influence globally. However, the process also entails considerable challenges, such as land administration, urban maintenance and creation and management of public services. With regard to the latter, a larger urban population also generates new demands in terms of water supply, sustainability of natural resources, education, security and transport, all of which must be met by local government. Competition between cities – to attract companies, tourists and, above all, talent – adds to this situation.

China also needs to adapt its cities and build new urban hubs that are able to manage resources and efficiently meet the needs of their inhabitants, absorbing the influx of citizens and successfully handling the challenges of urban growth (e.g. pollution – according to the World Health Organization's Air Quality Control, pollution in China is structurally higher than tolerable levels).

Innovation, especially technological innovation, can help local governments to meet the challenges of urban governance, improve urban environments, increase cities' competitiveness and respond to environmental concerns. To prepare for and manage these challenges, cities must innovate. In this context, the concept of smart cities is gaining more and more ground.

But, what is a smart city? Although numerous attempts have been made to define and describe the concept of a smart city, to date there is no consensus, and the term has not been used consistently. A number of studies have identified certain characteristics that may be found in a smart city. These include a smart economy (competitiveness), smart people (human and social capital), smart governance (participation), smart mobility (transport and technology) and smart environment (quality of life).

Despite their differences, the various definitions, indices and classifications share certain features that allow some meaning to be given to the concept of a smart city. On this basis, a smart city is characterised by:

1) An integrated overview of the city, resulting in initiatives relating to matters such as waste management, traffic control and water management.

2) A twofold technological and human approach. Technology is key to development of smart cities and is therefore the core tool. However, smart cities must be built for, by and with citizens, and the importance of urban governance, participation and investment in human and social capital should not be forgotten.

3) A threefold objective: to increase the efficiency of urban operations, improve citizens' quality of life and drive the local economy, whilst keeping in mind the issue of sustainability.

Cities around the world are making great efforts to become smart cities. In China, the 12th Five-Year Plan for National Economic and Social Development (2011-2015) specifically covers the need to strengthen and promote the urban smart technology sector. In fact, since 2011, the Ministry of Industry and Information Technology (MIIT), the National Development and Reform Commission (NDRC) and the Ministry of Housing and Urban-Rural Development (MOHURD) have all approved regulations to standardise development of smart cities in the country. In 2011, the MIIT drew up the 12th Five-Year Plan for Development of the Information Security Industry, the 12th Five-Year Plan for Development of the Internet of Things and the 12th Five-Year Plan for Development of E-commerce. In 2012, the MOHURD published the Notice on Carrying Out National Pilot Smart Cities and the Interim Measures for the Administration of National Smart Cities.

In August 2013, the MOHURD announced the launch of 193 pilot schemes for smart cities, including major cities, minor cities, districts and counties. To undertake the pilot programmes, the Ministry approved the creation of an investment fund, sponsored by the China Development Bank, for a total of USD 16 trillion. In November the same year, the EU-China Smartcities Cooperation Agreement was launched, adding a further 15 pilot cities. At September 2014, China was therefore working on more than 200 smart city pilot schemes. To support these actions, economic investment is expected to have exceeded CNY 2 trillion by the end of 2015 (approximately USD 320 billion).

However, building a smart city is no easy task. Although there is no single model and each city must adopt its own approach according to its specific circumstances and competitive advantages, certain aspects must always be taken into account:

1) Preparing a strategy for the city, which requires both political and organisational leadership.

2) Dealing with technological challenges. Interoperability, security and privacy are some of the matters that must be managed in relation to the use of technology, but more importantly smart cities must be cities for everyone. Therefore, technology must not be a factor for social exclusion.

3) Promoting public-private collaboration, collective intelligence and co-creation. Smart cities are an opportunity for economic development based on the new products and services that will emerge. For example, CISCO estimates that the smart cities business will be worth USD 1.2 trillion over the next ten years. However, beyond the development of local economies, smart cities cannot be built by public entities alone. The various stakeholders in cities (local government, companies, universities, entrepreneurs, citizens) must collaborate openly and creatively to accelerate development and implementation of smart services.

In this sphere, public-private collaboration is of particular interest. While continuing to allow companies to lead development of smart cities, as they have already on occasions, it is important to bolster public-private collaboration, engaging key stakeholders who form part of the innovation ecosystem. This type of cooperation is particularly relevant with respect to the budgetary restrictions of many local public entities. Traditional formats of public-private partnerships may help to finance construction of smart cities, which is one of the key challenges such projects face.

Joint investment is required to amass the substantial amounts needed to develop smart cities, but this alone is not enough. Public-private collaboration undertaken in building smart cities entails a new approach to the traditional relationship between the public and private sectors. For example, it is becoming increasingly apparent in smart city projects that services must be integrated, concentrated and grouped to achieve critical mass, obtain a reasonable return on investments, exploit synergies between different urban services and achieve efficiency through economies of scale. This working method – based on a governance model that encompasses all services – can truly be called smart, as it allows for more global and qualitative city services.

It seems that China has understood this. In 2012, the Ministry of Science and Technology (MOST) organised the Strategic Alliance of Smart City Industrial Technology Innovation, and in 2013 the MIIT set up the China Smart Cities Industry Alliance. Furthermore, in spring 2014, the NDRC launched the Smart City Development Alliance. The main purpose of these alliances is to coordinate efforts and investment by companies and the government to develop smart cities in China. Companies do not necessarily belong to all of these alliances. While some firms do participate in all three, others are only involved in one or two.

It is too soon to say how China's smart city venture will play out. In fact, there is almost no information on the development plans for the pilot schemes, which were to be drawn up by the MOHURD. Nor is there any indication as to the national evaluation model for smart cities, which was also the responsibility of this ministry. However, cities cannot be transformed overnight and in view of the developments already undertaken, and its increasingly important international position (in November 2015, following in Barcelona's footsteps, China held its first Smart City China Expo & Congress in Shanghai), the People's Republic of China can be said to be committed to its cities and convinced that technology can make them more manageable and better places to live. It therefore seems that China is aware that successful development of smart cities is key to its long-term prosperity.

2.3.1. Investment in the logistics / infrastructure sector, accompanying foreign trade

Chinese investors have invested heavily in the European infrastructure and logistics sector, for a total of USD 2,560 million in the period from 2000 to 2014. In addition, Hong Kong's Hutchison Group invested €500 million in the Port of Barcelona, and has already completed the second stage of its investment project.

Investments in this sector can be divided into two types. Firstly, financial investments, whereby Chinese funds have acquired interests in assets or existing companies but are not involved in management. This strategy was followed in CIC's acquisitions of interests in Spain's Ferrovial at Heathrow Airport and the UK water provider Thames Water. Physical and service infrastructure in the United Kingdom is highly attractive to Chinese investors, and the capital injected into the sector could amount to GBP 105,000 million by 2025[14].

Secondly, Chinese companies have invested in infrastructure with a view to extending its commercial capacity, the main objective being to open the way for Chinese products to enter the European market. Examples include China Ocean Shipping's (COSCO) investments in the Port of Piraeus in Athens and the Hutchison Group's investment in the Port of Barcelona (COSCO also operates in the Italian port of Naples and the Belgian port of Antwerp). Alongside shipping ports, Chinese investors are also increasingly present in European airports. In 2014, a consortium of investors acquired 49.9% of Toulouse Airport (France), in a transaction that proved controversial as the airspace is used to test the new Airbus models, and the e-commerce firm IZP acquired 67% of Parma Airport (Italy) in order to establish a logistics centre for its operations between China and Europe. Moreover, a number of logistics platforms have been set up in other airports, including LinkGlobal Logistics in Germany's Parchim Airport.

This interest in developing European infrastructure projects also extends to financing innovative projects. In 2014, the Sino-German Quality Infrastructure Project was launched. Under the leadership of Germany's Ministry for Economic Affairs and Energy, the project's aim is to "harmonise the infrastructures in the two countries" with a view to bolstering bilateral trade. Specifically, the purpose of this scheme, which takes the form of a fund, is to support innovative projects in sectors such as infrastructure, up to a maximum of €200,000 per project. Another undertaking, Barcelona China's European Logistics Center (Barceloc), overseen by Catalonia Trade and Investment and the Port of Barcelona, aims to attract Chinese companies in order for them to establish their logistics platforms for the Mediterranean in Barcelona. The BEST terminal at the Port of Barcelona, managed by the Chinese logistics giant Hutchison Port Holdings, is already working with Barceloc.

Lastly, the announcement of the New Silk Road and the Juncker Plan could fuel further Chinese investment in EU infrastructure in the coming years[15].

Table 6 Key Chinese investments in the **European infrastructure and logistics sector 2010-2014** (in millions of USD)

YEAR	CHINESE CO.	AMOUNT	INVOLVED PARTY	COUNTRY
2014	Aviation Industry Corp of China	629	Endurance Capital AG	Hungary
2013	China Merchants	530	CMA CGM	France
2013	China Ocean Shipping	300	Greenfield	Greece
2013	AVIC International Holding	242	Greenfield	United Kingdom
2013	Henan Civil Aviation	220	Cargolux Airlines	Luxembourg
2012	SAFE	200	Veolia Water	United Kingdom
2014	Fosun	200	Latsis	Greece
2012	China Ocean Shipping	150	Greenfield	Greece
2011	Burg Silvergreen	134.1	Greenfield	Germany
2013	TP-Link Technologies	55	Greenfield	Poland
2013	TP-Link Technologies	55	Greenfield	Romania
2014	Shanghai Yunda Express	54.5	Transportation	Germany
2014	SF Express	43.6	Transportation	Lithuania

Source: ESADE China Europe (n/av: not available). Investments by Hong Kong companies are not included.

14 See: http://www.ft.com/intl/cms/s/0/501808f6-5b89-11e4-b68a-00144feab7de.html#axzz3RSD2AlkH

15 See: http://www.wsj.com/articles/china-expresses-genuine-interest-in-eus-new-investment-plan-1417610133

Box II.

Key logistics trends around the world and in Europe

Author: Jordi Torrent,
Head of Strategy, Port of Barcelona

Highly demanding markets and pressure on costs require increasingly complex and efficient supply chains. Stevedore firms are looking to make their logistics more competitive, and to do so they need more control over chains and more integration between the parties involved. Chains, rather than products, compete with each other. This has led to a transformation of the logistics sector, characterised by:

- A larger proportion of logistics expenses in the market price of products and growing pressure to reduce such expenses. In many industrial sectors, logistics expenses are now significantly higher than the cost of the labour required to manufacture products (agri-food, automotive, fashion and footwear, etc.). Companies are therefore under increasing pressure to reduce these expenses and the need to optimise logistics chains is driving changes in all providers of logistics services.

- A focus on supply chain excellence. The concept of a comprehensive and integrated logistics chain, combined with the new service requirements, is spurring more complex, sector-specific logistics. Expectations in terms of reliability and speed, which were already high, are also increasing, in particular in sectors where stock tends to diminish and/or disappear.

-Increased relevance of stevedore firms, logistics operators and integrators (3PL-Third Party Logistics, and 4PL-Fourth Party Logistics) in comparison to industrial manufacturers and traditional transport companies, when making strategic decisions relating to the supply chain.

-The importance of resilient logistics chains. Recent events (market volatility, natural disasters, government decisions, etc.) have exposed the fragility of logistics chains, which are highly dependent on occurrences around the world. It is increasingly common for major players to look for robustness in their logistics approach (secure supply) over other characteristics.

The maritime sector is also undergoing a process of change, mainly characterised by the following:

-Concentration of shipping companies and business integration strategies. In terms of horizontal integration (mergers and alliances), the crisis and the search for economies of scale have accelerated concentration among shipping companies – either of businesses or of resources. This concentration of flows is resulting in movements of shipping companies between terminals and ports. In the case of vertical integration, the crisis appears to have stopped the trend of shipping companies becoming involved in the terminal sector. Shipping companies' penetration in logistics operations (inland terminals, rail services, etc.) also seems to be abating globally.

-Volatility in maritime markets, fuel prices, freight costs, rotation and ports of call. There is a trend of decreasing speeds and increasing journey times (slow steaming and super slow steaming), frequent changes in rotation and ports of call and significant fluctuations in freight prices. All of this is linked to the manufacturing and consumer cycles, the surplus capacity generated by new megaships and slowing growth in international trade.

-Concentration of terminals run by large operators, especially in the case of container shippers which tend to develop solid network strategies.

-Larger ships, which are faster than expected – especially container ships – and have not yet hit a ceiling. Suitable infrastructure, operations and services are required to dock such ships.

-Increasing competition between ports. The crisis and the surplus supply of ports have fuelled competition, which is set to be further driven by the increasing power of shipping companies and global logistics providers, resulting in heightened pressure on prices.

-Greater competition between regional port clusters, even more than between ports themselves. There are numerous examples of collaboration, integration and even merger strategies between ports. In this new environment, ports act as value-added hubs of logistics networks and competition is between such networks and logistics chains. Means of integration between ports are therefore required to offer services in the hinterland that can compete with those offered by other port clusters.

Logistics in Europe

In Europe, these circumstances are accompanied by other factors driving substantial regional change, such as:

-Changes in distribution structures in Europe, with a trend towards decentralisation to reduce the impact of transport. The increase in costs and the optimisation of logistics chains entails a reduction in the concentration of distribution centres in the north of Europe, a shift towards Southern and Eastern Europe, and development of regional logistics hubs located in the European periphery.

-Rebalancing of traffic to and from Asia between Europe's northern and southern port regions to improve transport efficiency, reduce the environmental impact of logistics chains and prevent transport infrastructure becoming more congested.

-More stringent environmental requirements. Consumers, institutions and companies are demanding a reduction in the environmental cost of logistics chains and particularly of transport, spurring sustainable logistics and intermodal transport (increasing opportunities for sustainable rail and short sea shipping services) and the use of more sustainable energy, etc.

In this context, Southern Europe's importance as a distribution platform for Europe and the Mediterranean has grown year after year, and Barcelona is in a privileged position. Its unique characteristics as a logistics hub have allowed the city to attract industrial and logistics investments in recent years by foreign and Spanish companies that use Barcelona as a distribution platform for Mediterranean Europe. Investments of this kind have been made by groups such as Hutchison, Lukoil, Grimaldi, TCB, Honda Logistics and Nissan.

Barcelona: a distribution centre for Mediterranean Europe

In recent years, Barcelona has established itself as a European logistics capital and the main logistics hub in the Mediterranean. This is a result of four unique pillars in its territory of Southern Europe and the Mediterranean:

-Industrial specialisation. Barcelona and its province represent one of the main industrial driving forces in Southern Europe. Important industrial clusters are concentrated in Barcelona, such as the automotive, chemicals, agri-food, pharmaceutical, fashion and footwear sectors, as well as a growing e-commerce business. Barcelona has innovative industries in these sectors and many others, successfully competing at both European and global level. Brands such as SEAT, Nissan, Mango, Desigual, Grifols, Tous, etc. have their headquarters in Barcelona for the purpose of manufacturing and/or distribution to the rest of Europe and the world.

-Logistical specialisation. Industrial development in Barcelona has resulted in the generation of a significant logistics sector, which renders a wide range of specialised added-value logistics services to these industries. Barcelona offers the largest selection of logistics services in the Iberian Peninsula and in Southern Europe, either through local companies or through Spanish subsidiaries of major global operators. Any company that wishes to establish either manufacturing or distribution facilities in Barcelona will therefore find a wide range of logistics services to meet the needs of their specific sector.

-Distribution and sales networks able to reach the main markets and cities in Europe and North Africa in 24/48 hours. Goods can be distributed from Barcelona at very competitive prices to any location in Western Europe or North Africa in less than 24/48 hours by plane, ship, lorry or train. The city is also an excellent hub from which to reach the West African markets and connect with Latin America, a region with historical and cultural links to Spain.

-A unique concentration of logistics infrastructure. Within a few square kilometres, the city of Barcelona contains a port (Port of Barcelona), an international airport (El Prat-Barcelona Airport) and more than 500 hectares of multi-purpose logistics warehouses in logistical areas *(Zona de Actividades Logísticas)* and Free Zones *(El Consorci de la Zona Franca de Barcelona).*

-Barcelona China's European Logistics Center (BARCELOC) is a joint initiative between Catalonia Trade & Investment, the Port of Barcelona and Spanish and global logistics players operating from Barcelona, which aims to attract Chinese and other Asian industrial companies in order for them to establish manufacturing and distribution facilities. The initiative aims to leverage the value of Barcelona's infrastructure and logistics services, which are the best in Southern Europe. As a result of the services it offers, Barcelona is the ideal location to distribute Chinese and other Asian industrial products to the Iberian Peninsula, Southern Europe, North Africa, West Africa and Latin America. BARCELOC offers free advisory services – in Barcelona and through three offices in Shanghai, Beijing and Hong Kong – to Chinese and Asian companies seeking to optimise their logistics in Europe by setting up logistics operations in Europe or finding industrial/commercial partners to distribute in the region.

Some conclusions on the sector profile of Chinese investment in the EU

In recent years, Chinese investment in Europe has rocketed and has also become more complex. New public and private investors have joined the wave of investment from China and those already present in Europe have stepped up their activity and diversified. As a result, Chinese investments have been made in numerous sectors in Europe. But while their impact is growing, it still remains limited.

The target sectors for Chinese transactions in Europe reflect a threefold objective for investors. Firstly, as previously mentioned, many Chinese companies are active in Europe and are looking for assets that will allow them to develop more technologically advanced and specialised products, improving their competitiveness in the local and international markets. Chinese firms are therefore investing in companies from Europe's technology and agri-business sectors and undertake R&D directly, taking advantage of existing human capital and technological infrastructure in the region.

Secondly, in recent years a growing number of Chinese firms have invested in sectors related to logistics and infrastructure, and may therefore help to facilitate trade between China and Europe. These investments, which have taken the form of increased interest in developing projects to extend the capacity of ports, airports and logistics centres, are aligned with the foreseeable growth in trade between the two regions, which should drive large-scale projects such as the New Silk Road.

Thirdly, some of China's large state-owned enterprises – particularly its sovereign wealth funds – have continued to invest in numerous companies in sectors related to infrastructure and energy and also in real estate. These investments, which are strictly financial and entail no managerial involvement, allow these investors to diversify their portfolios through low-risk assets with reasonable returns – two invaluable characteristics given the volatility of Chinese stock markets in recent months.

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CHAPTER III

Chinese investment in Spain

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Chinese investment in Spain

Boxes

Charts and tables

3.1. China-Spain relations, gathering momentum

Institutional relations between Spain and China are both fluid and free from significant differences of opinion, focusing on shared economic and business interests. The last major bilateral institutional meeting of the two countries was in May 2015, when the Premier of the People's Republic of China, Li Keqiang, visited Palma de Mallorca for two days[1]. Another important high-level meeting took place in September 2014, when the Prime Minister of Spain paid an official visit to China. The trip was dominated by the meetings with President Xi Jinping and Premier Li Keqiang, as well as with key business figures from the country, such as Wang Jianlin (who owns Dalian Wanda). Fourteen bilateral agreements were signed during the visit, which will help to strengthen the economic and business relationship between the two nations. These accords include a collaboration agreement between Telefónica and Huawei, in addition to their existing shared laboratory in Spain; the agreements in place between Santander and Bank of Beijing since 2014; electricity generation projects in China undertaken by the Andalusian company Abengoa; the sale of wind turbines by Gamesa's Chinese subsidiary to the local company Hebei; the supply of radiation containment equipment by the Spanish company Enusa to the Suzhou Nuclear Power Research Institute; and the sale of Airbus 320 simulators to China.

The already extensive commercial relationship between the two countries should be further bolstered by these agreements. In 2014, Spanish exports to China grew for the sixth consecutive year and China was the 14th largest buyer of Spanish products, at 1.1% of the total. In terms of imports, China was Spain's 5th largest supplier, providing 5.4% of total imports, only surpassed by the European country's traditional trading partners: Germany, France, Italy and the United Kingdom. Trade between the two countries amounted to €35,700 million last year, almost €100 million a day. However, this trade relationship is clearly biased in China's favour, as it sells many more products to Spain than vice versa. The same is true of the Asian country's relationships with other developed economies.

Nonetheless, the infrastructure megaprojects currently being undertaken by China, such as the Silk Road, should help to facilitate trade between the two countries, reducing its cost, improving security and increasing the volume of transactions. One example of the improvements to the infrastructure network and the opening of trade routes that could benefit trade with Spain is the freight train which, in late 2014, covered the 21,000 kilometres between the Yiwu manufacturing centre on China's coast and Madrid, passing through Kazakhstan, Russia, Belarus, Poland, Germany and France. The journey took 21 days, moving 1,400 tonnes in 70 containers.

These initiatives complement the existing maritime trade route, which is the main means of entry into Spain and Southern Europe for Chinese products. In fact, Spain's port infrastructure, centring on the Port of Barcelona, once again appears in the study prepared by ESADE as one of the most highly rated factors in the business climate survey conducted amongst Chinese investors located in Spain.

According to official Spanish data[2], in terms of bilateral investment, Spain's FDI in China (€1,258 million in 2010-2014) is greater than China's FDI in Spain. This situation is consistent with Spanish multinationals' more extensive experience and history of foreign investment. In contrast, Chinese firms started to invest abroad regularly only a few years ago. In coming years, Chinese investment in Spain can be expected to exceed Spain's investment in China, as the Asian country has a greater capacity for capital export.

In 2014, China ranked as the 16th destination for investment by Spanish companies, representing 1.9% of the total, up 143% on 2013. Although this proportion of total Spanish foreign investment may appear limited for a market as relevant as China, it is important to note that Spanish investment in the Asian nation is a recent phenomenon, and one that is clearly on the rise. In 2000, China ranked as just the 35th destination for Spanish FDI, with less than 0.1% of total investment. China's lower significance as a destination for Spanish investment can be explained by factors such as geographical remoteness, cultural differences and tight controls on foreign investment in China. In this regard, Spanish companies have traditionally focused on two key targets for investment: European countries and Latin America.

Official data for Spanish foreign investment in China may be understating current business activity, as most multinationals operate in the country via Hong Kong. In any case, some Spanish multinationals have disposed of or reduced their investments in China over the past year through transactions of a primarily financial nature.

For example, the telecoms firm Telefónica sold shares in China Unicom for €687 million, half of its interest in the latter, equivalent to 2.5% of the share capital of the Hong Kong company. Telefónica will retain its minority interest of 2.5% in the Chinese business, as well as its strategic alliances and ongoing projects. In October 2015, the two companies announced an agreement to share capacity at their data centres in order to offer a better service to multinational clients. The project will undoubtedly strengthen the relationship between the two firms.

[1] See: http://www.elmundo.es/baleares/2015/05/27/5565bf53e2704ea1738b457a.html
[2] Ministry of Economy and Competitiveness Investments Register

Meanwhile, the Spanish bank BBVA sold 4.9% of China CITIC Bank to UBS for €1,460 million, resulting in a gain of €400 million. In contrast, other multinationals have reinforced their commitment to the Asian country. These notably include Inditex, which in 2015 will reach a total of 500 points of sale in China in 60 cities. Moreover, at the end of 2014, the clothing company started to sell its products online through Tmall, owned by Alibaba, as a means of entering China's enormous e-commerce sector.

China is also showing signs of confidence in Spain's economic recovery by strengthening trade and investment relations, and also by investing in Spanish sovereign debt, as reflected in subscriptions to Treasury bond auctions in recent quarters.

Financial sources have indicated that purchases by Chinese investors in October 2014 could total €500 million. This may be one of the largest subscriptions to Spanish debt securities since the €1,000 million acquired by the SAFE sovereign wealth fund through a syndicated issue in 2012[3].

As the table shows, in terms of international trade, China is the 14th most important destination for Spanish exports and the 5th largest importer into Spain. In investment, China is ranked 16th in terms of outbound Spanish investment and is the 7th largest investor in Spain.

Table 1 China's position in trade and investment relations with Spain (2014)

	EXPORTER	% of TOTAL	IMPORTER	% of TOTAL	OUTBOUND FDI	% of TOTAL	INBOUND FDI	% of TOTAL
1	FRANCE	18.2	GERMANY	13.9	IRELAND	17.6	UNITED STATES	19.4
2	GERMANY	11.3	FRANCE	13.5	BRAZIL	15.8	LUXEMBOURG	13.4
3	PORTUGAL	8.7	ITALY	7.9	UNITED STATES	10.6	UNITED KINGDOM	8.7
4	ITALY	8.4	UNITED KINGDOM	5.5	CAYMAN ISLANDS	7.3	FRANCE	8.4
5	UNITED KINGDOM	7.6	CHINA	5.4	CHILE	6.3	NETHERLANDS	6.2
6	UNITED STATES	4.1	UNITED STATES	4.2	UNITED KINGDOM	6.0	MEXICO	6.0
7	NETHERLANDS	3.2	NETHERLANDS	4.1	CURAÇAO	4.1	CHINA	3.1
8	BELGIUM	2.5	PORTUGAL	3.3	PERU	2.9	JAPAN	2.4
9	MOROCCO	1.7	BELGIUM	2.5	PORTUGAL	2.7	URUGUAY	2.3
10	TURKEY	1.7	RUSSIA	2.2	SWEDEN	2.7	GERMANY	2.1
11	SWITZERLAND	1.5	JAPAN	2.0	NETHERLANDS	2.7	SWITZERLAND	2.1
12	MEXICO	1.4	ALGERIA	2.0	COLOMBIA	2.4	IRELAND	2.0
13	POLAND	1.3	NIGERIA	1.6	MEXICO	2.4	SINGAPORE	2.0
14	CHINA	1.1	SAUDI ARABIA	1.4	ITALY	2.1	VENEZUELA	1.9
15	BRAZIL	1.0	IRELAND	1.3	POLAND	2.0	GUERNSEY	1.6
16	GREECE	1.0	MEXICO	1.2	CHINA	1.9	CANADA	1.6
17	ALGERIA	1.0	SWITZERLAND	1.2	LUXEMBOURG	0.9	HONG_KONG	1.3
18	SWEDEN	0.9	SWEDEN	1.2	BELGIUM	0.8	ISRAEL	1.1
19	RUSSIA	0.9	TURKEY	1.1	CANADA	0.8	CURAÇAO	1.0
20	JAPAN	0.9	BRAZIL	1.0	ROMANIA	0.7	BRAZIL	1.0

Source: own research based on Investments Register data

3 http://www.expansion.com/2014/10/09/mercados/1412880721.html

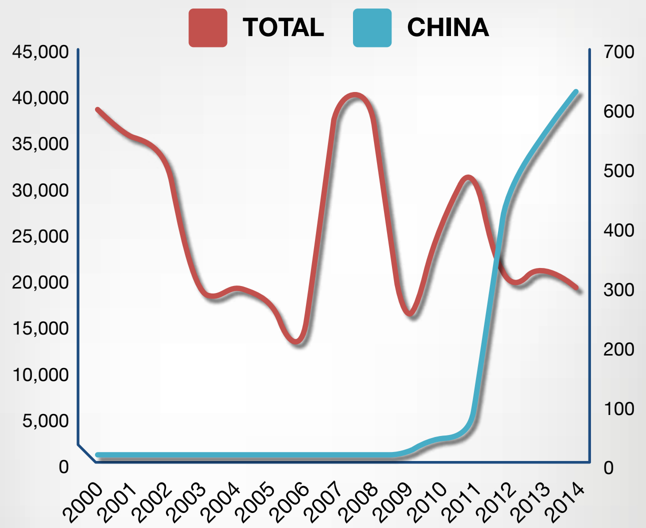
3.2. Chinese companies in Spain

Chinese investment is becoming increasingly important to Spain and is clearly on the rise. According to official Spanish data, there has been a gradual increase in FDI from €1 million in 2008 to €610.3 million in 2014. Historical data show that Chinese investment in Spain has been concentrated in the last three years (2012-2014), with transactions averaging €520 million a year. In 2014, China became Spain's 7th largest investor, overtaking economies with a long history of investing in the country, such as Germany and Japan. In addition, while Spain's inbound FDI has fluctuated in recent years, China's FDI has stayed on course, becoming one of the most significant sources of direct investment for Spain.

In cumulative terms, since 1993, when the Investments Register was started, **China has accumulated FDI in Spain amounting to €1,670 million.** The Asian country is Spain's 23rd largest investor, with 0.4% of total cumulative investment. However, in relative terms China has become a more important investor for Spain, and its pattern of investment in recent years has been more consistent than that of Spain's traditional key investors, such as Germany and France, for whom Spain is already a mature market. Nonetheless, Chinese investment is taking its first steps abroad, and in Spain; hence its considerable upside potential and room for growth. Chinese companies have started to show an interest in the opportunities offered by different Spanish sectors, as reflected by the numerous business visits to Spain in recent years, some of which have led to significant investment.

Chart 1

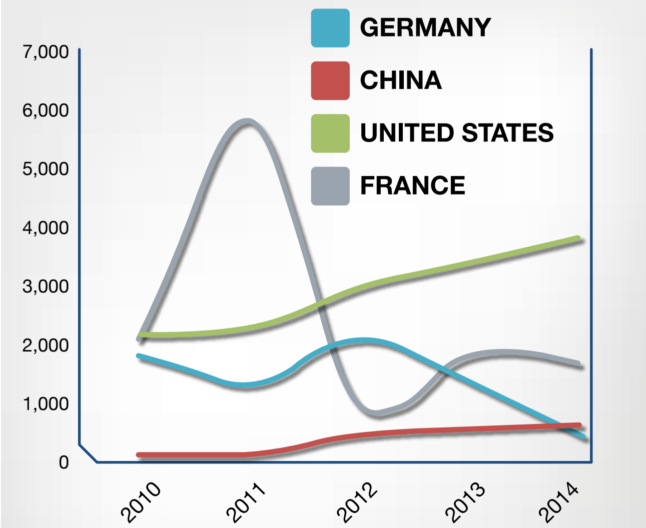
Inbound FDI in Spain from China and the rest of the world (2000-2014) (€ Million)



Fuente: Investments Register

Chart 2

Investment in Spain from a selection of countries (2010-2014) (€ Million)



Source: Investments Register

According to data gathered by the ESADE China-Europe Observatory, a total of 75 Chinese companies are currently undertaking business operations in Spain (companies with headquarters in mainland China or Hong Kong). These companies operate in many different economic sectors and their investment profiles vary considerably. In Spain, Chinese firms have opened retail bank branches, extended ports, acquired properties, sponsored football teams, acquired manufacturing companies to expand production capacity, invested in agri-food firms and created joint ventures for the purpose of strategic collaboration between technological firms, among other initiatives. The major Chinese companies – apart from the main SOEs specialised in extracting natural resources and construction – are present in Spain, including CCB, ICBC, Huawei, Lenovo, ZTE, Haier, Air China, COSCO, China Shipping, KeewayMotors and Minmetals.

The number of Chinese companies with operations in Spain is increasing steadily. Over the past two years, the ESADE observatory has seen new companies arriving, such as China Construction Bank, the Wanda Group, the Fosun Group and Bright Food, while also witnessing growth in established companies such as Air China, Haier, Lenovo, ICBC, Huawei and ZTE.

In addition to large groups, estimates of Chinese investment in Spain should take into account smaller, less mature businesses, which nonetheless contribute to economic activity and create jobs. There is no statistical information concerning cumulative investment or the number of establishments of this type, although, based on the figure of almost 45,000 Chinese nationals registered with Spain's social security system as self-employed workers, it is clear that this business activity is widespread in the country. This type of business has doubled since 2008, reflecting growing interest in Spain among Chinese owners of small businesses[4].

Nonetheless, although Chinese investment is increasingly important for Spain and its industry, neither Europe nor Spain are priority destinations for China. This is due largely to the tendency among Chinese companies to first internationalise into natural markets, i.e. other Asian countries such as Indonesia or countries with substantial natural resources, such as Kazakhstan. These two countries, which are geographically close to China, have received more FDI from China than Germany, a global economic power. Even in comparison to the EU, according to official data, Spain is merely the 10th destination for Chinese FDI, with 0.8% of total FDI for the region. The core European economies, such as the United Kingdom, Germany and France, financial hubs such as Luxembourg and the Netherlands, and Eastern European countries that have more competitive labour costs, such as Hungary, have all received more Chinese FDI than Spain. Even so, the number of investment projects is growing at a rate of 20% a year, making Spain a market with considerable potential, above all in value-added sectors that require highly trained personnel and management.

[4] "Chinese-owned businesses in Spain have doubled in six years".

Table 2 Chinese companies in Spain – ESADE Observatory (2015)

COMPANY	SECTOR
Xinhua News Agency	COMMUNICATIONS
Air China Limited Sucursal en España	AIR TRANSPORT
Air Sea Worldwide Spain S.L.	TRANSPORT AND LOGISTICS
ANSTEEL SPAIN S.L.	STEEL AND OTHER MATERIALS
ANTAI TRADING S.L.	TOURISM - HOTELS
Aranda Coated Solutions	METALS AND METALLURGY
Au'some CANDIES EUROPE S.L. (HK)	FOOD AND BEVERAGES
BAOSTEEL ESPAÑA S.L.	STEEL AND OTHER MATERIALS
Bluestar Siliconas España	CHEMICALS
Bright Food (Group) CO. (Miquel Alimentació 100%)	FOOD AND BEVERAGES
BYD ESPAÑA	ELECTRIC VEHICLES
CATHAY PACIFIC AIRWAYS (HK)	AIR TRANSPORT
CCS China Classification Society	SERVICES
Changyu Pioneer (interest in Bodegas Marqués del Atrio)	FOOD AND BEVERAGES
China Certification Inspection Group Co Ltd Sucursal en España	SERVICES
China Construction Bank (Europe) S.A. Spanish Branch	BANKING
CHINA NATIONAL FISHIERIES COMPANY	FOOD AND BEVERAGES
China Shipping Spain Agency S.L.	TRANSPORT AND LOGISTICS
CHINT ENERGY S.L.U.	ELECTRICAL MATERIALS
Chongqing Kangde Industrial (Group) Co., Ltd. (Hotel Barceló Santiago - Canarias)	TOURISM - HOTELS
Citic HIC Gandara Censa S.A.U.	SUNDRY MATERIALS
CK Hutchison Holdings Limited	PORTS AND LOGISTICS
CNCC CHINA NATIONAL CHEMICAL CORPORATION	CHEMICALS
COSCO IBERIA S.A.	TRANSPORT AND LOGISTICS
CROWN RELOCATIONS (HK)	TRANSPORT AND LOGISTICS
CZICC China Zhenjiang International Economic	CONSTRUCTION
DALIAN WANDA GROUP (Wanda Madrid Development S.L.U.)	REAL ESTATE AND TOURISM
Daxiong Spain S.L.U.	METAL PRODUCTS
Hebei Iron and Steel Group (DUFERCO ESPANA S.L.)	METALLURGY
ELAI CULTURAL S.L.	TOURISM
ELKEM IBERIA SL (China National Bluestar Group)	RENEWABLE ENERGIES
ESPRIT HOLDINGS LTD	FASHION
Fosun Group (Osborne)	FOOD AND BEVERAGES
GIGABYTE TECHNOLOGY ESPANA S.L.	TELECOMMUNICATIONS
GOLDBRIDGE BRUDER S.A.	AUTOMOBILE ACCESSORIES
GRAN VIEW CONTAINER TRADING	TRANSPORT AND LOGISTICS
GREE SPAIN CORPORATION S.L.	AIR CONDITIONING

COMPANY	SECTOR
HISENSE Electronic Iberia S.L.	ELECTRICAL APPLIANCES
HISOFT	TELECOMMUNICATIONS
HNA Group (29.5% of NH Hotels)	TOURISM - HOTELS
Huawei Technologies España, S.L.	TELECOMMUNICATIONS
Huayi Compressor Barcelona S.L.	COMPONENTS
Industrial and Commercial Bank of China (Europe) S.A. Sucursal en España	BANKING
Jiangsu GPRO Group Co., Ltd. (Hotel Valparaíso Palace & Spa)	TOURISM - HOTELS
Jiangsu Sunrain Solar Energy Co., Ltd.	RENEWABLE ENERGIES
JINKO SOLAR	RENEWABLE ENERGIES
KEEWAYMOTOR España, S.L.	VEHICLES
KERRY LOGISTICS	TRANSPORT AND LOGISTICS
KING & WOOD Mallesons SJ Berwin (HK)	LEGAL SERVICES
LEE'S FOOD IBERICA S.L.	FOOD AND BEVERAGES
LENOVO	TELECOMMUNICATIONS
LOUVRE HOTELS ESPANA S.L. (Jin Jiang Group)	TOURISM - HOTELS
Midea Europa	ELECTRICAL APPLIANCES
MINDRAY Medical España S.L.	MEDICAL DEVICES
Minmetals España S.L.U.	IRON AND OTHER MATERIALS
MOTIC SPAIN S.L.U.	MEDICAL DEVICES
OP-POWER	RENEWABLE ENERGIES
SANHUA EUROPE	ELECTRONIC COMPONENTS
SANY European Machinery S.L.	CONSTRUCTION MACHINERY
Shuanghui Group (CAMPOFRÍO)	FOOD AND BEVERAGES
SINOCHEM ESPAÑA	PETROCHEMICALS
SINOVEL WIND SPAIN S.L.	RENEWABLE ENERGIES
SIU FASHION S.L. (Neo Concept Group)	FASHION
SOLARFUN POWER HOLDINGS LTD	RENEWABLE ENERGIES
SUNFOR LIGHT S.L.	LED PRODUCTS
TRINA SOLAR	RENEWABLE ENERGIES
Tzaneen Internacional (Ciudad Real Airport)	INFRASTRUCTURE – AIRPORT
VERDINIA GARDEN S.L. (Hispano-Chinese JV)	ARCHITECTURE AND ENGINEERING
Vita Green Europa S.A.	PHARMACEUTICALS
Wuxi Suntech Power Co., Ltd.	RENEWABLE ENERGIES
Xtep España	SPORTSWEAR
YINGKE ADARVE LAW FIRM	SERVICES
YINGLI GREEN ENERGY SPAIN S.L.U.	RENEWABLE ENERGIES
ZTE España S.L.U.	TELECOMMUNICATIONS

3.3 Recent key transactions (2014-2Q2015) and new sectors of interest

In 2014 and the first two quarters of 2015, a number of Chinese investments were made in Spain, clearly indicating a consolidation of the trend described in the previous edition of this report, towards a larger presence of Chinese businesses in the country. Chinese capital is entering an increasing number of sectors and businesses in Spain, and is strengthening its position in sectors where it was already present. In the period in question, from 2014 to the second quarter of 2015, a number of Chinese investments were made in Spain in the real estate, hotel, tourism, agri-food, shipbuilding, financial, service infrastructure, leisure and sports sectors.

Real estate and tourism

In the real estate sector, one of the largest Chinese investments in Spain in the past year involved the **Dalian Wanda Group**. The group's chairman, Wang Jianlin, is China's richest man and the 31st richest person in the world, according to the Forbes list, and the firm has four lines of business: commercial property, hotel development, culture and leisure. The group's acquisition of the world's largest cinema operator, the US company AMC, for USD 2,600 million in 2012 gives an idea of its investment capacity and its determination to expand its reach globally.

In mid-2014, the banking group Santander sold the landmark Edificio España building in the centre of Madrid to Renville Invest S. L., a subsidiary of the Chinese group Dalian Wanda, for €265 million. Edificio España has 25 floors and stands 117 metres high. The building has been empty since 2006 and it is considered to be Spain's first skyscraper. The renovation work will cost Dalian Wanda approximately €150 million, transforming the property into luxury housing and a leisure complex. Wang Jianlin met the Spanish prime minister during the latter's visit to China, and assured him that he intends to invest around €3,000 million in Spain through various projects in the real estate and leisure sectors.

Meanwhile, the **Fosun Group**, which has already undertaken a major transaction in Portugal whereby it purchased the insurer Fidelidade and thus acquired a €700 million portfolio of real estate assets, has entered the Spanish market through Fosun Property, its real estate branch, with a view to exploring investment opportunities and studying potential transactions[5].

In the tourism and hotel sector, the Chinese investment group **Jiangsu GPRO** acquired Hotel Valparaíso in Palma de Mallorca for €48 million in 2014. The ultimate objective is to develop a chain of hotels in Spain in anticipation of the foreseeable growth in the number of Chinese tourists in the coming years, who will be sent to these hotel complexes by local tour operators.

Another recent transaction was the acquisition of the Barceló Group's Hotel Santiago Barceló in Tenerife by China's **Chongqing Kangde Group**, for €50 million.

In mid-2015, the large Asian hotel group **Mandarin Oriental International**, which specialises in luxury hotels, joined forces with the Arab group Olayan to acquire the Ritz Hotel in Madrid for €130 million. This brings and influx of Chinese (and Arab) funds into one of the capital's most emblematic buildings, construction of which was promoted by King Alfonso XIII in the style of the most luxurious hotels of the period. A further €90 million is expected to be invested in fully renovating the property.

In the same sector, **China's HNA Group** increased its shareholding in the NH hotel chain, adding to the 20% acquired in 2013. In 2014, HNA acquired shares in NH from Italy's Intesa Sanpaolo, which were valued at €29 million (on top of the existing €234 million), giving it control over 29.5% of the Spanish company. The transaction was not only a significant injection of capital for the Spanish company, it also allowed it to expand into China through its new shareholder. NH began its process of expansion through HNA in 2014 by managing six hotels owned by the latter, with a total of 1,312 rooms, as well as managing hotels for third parties.

At the end of last year, the two companies created a joint venture, headquartered in Beijing, called HNA-NH Hotel Management Joint Venture Company. Initial share capital is USD 20 million, with 49% owned by NH and 51% by HNA. The HNA Group is also negotiating the acquisition of the Spanish airline Air Europa for approximately € 1,000 million, potentially making it the largest Chinese investment in Spain to date. It has emerged that the transaction is very close to being finalised, the main hurdle being the difference over the valuation of the company, which forms part of the Globalia Group chaired by Juan José Hidalgo. Globalia currently owns 53.59% of the airline, and its other shareholders include Banco Popular and Unicaja.

Injections of Chinese capital into foreign companies operating in Spain may be indirectly beneficial for the Spanish economy. For example, in the tourism sector, the Fosun Group, which owns the largest travel agency in China, acquired 5% of the British tour operator Thomas Cook for €126 million. The Managing Director of Thomas Cook acknowledged that Spain was pivotal to the transaction, in particular due to the British company's network of hotels in the Canary Islands, which would be used by Fosun to channel Chinese tourists towards Spain. The British company could therefore be key to increasing Chinese tourism in Spain, which may in turn generate further investments by the Chinese group to construct new hotels or expand existing ones.

5 See: http://www.elconfidencial.com/empresas/2015-07-05/fosun-property-se-une-al-desembarco-chino-en-espana-atraido-por-el-despertar-del-ladrillo_914724/

Another example is the €1,500 million acquisition of the French group Louvre Hotels by a Chinese group with Jin Jiang at the helm. Negotiations for this deal began in late 2014 and included 10 budget hotels located in Spain. This is not the first time the Chinese group has approached the Spanish market. In 2011, it signed an agreement with the Meliá International group, providing Meliá with access to the Chinese market and the Chinese group with a means to enter Europe.

The agri-food sector

Three noteworthy transactions took place in the agri-food sector, including the acquisition of a majority interest and a minority interest in a Spanish company. In June 2014, the Chinese group **WH Group Limited** (formerly Shuanghui) and the Mexican firm Sigma took over the Spanish meat company Campofrío, controlling a total of 80.9%. The transaction allows the Spanish company to boost its size and financial capacity, but most importantly it also provides access to the Chinese and Latin American markets for its products, through the new shareholders.

The Fosun Group acquired 20% of the Osborne Group in the food and beverages sector, with the remaining 80% retained by the Andalusian family that controls the group. As a result, the Chinese investor now has a seat on the board of the Spanish group, and the latter will benefit from a substantial injection of capital enabling it to finance foreign expansion, particularly through acquisitions of other mid-sized companies. The Osborne Group will also sell its premium products on the Chinese market through its Chinese shareholder, greatly reinforcing its expected international growth.

In summer 2015, **China's Bright Food Group**, the second largest Chinese food distribution company with a turnover of €18,000 million, announced a preliminary agreement with the Catalan distribution firm Miquel Alimentació, one of the largest wholesale food groups in Spain, with a turnover of approximately €900 million. The final agreement was signed in October 2015, resulting in the acquisition of 100% of the distribution firm for €110 million. The Chinese enterprise had already been active in Europe, acquiring 60% of the British firm Weetabix and 70% of the French wine distributor Diva.

Leisure and sports

Within the leisure and sports sector, in early 2015 it was announced that the magnate Wang Jianlin, owner of the **Wanda Group**, had acquired an interest in the Atlético de Madrid football club, investing €45 million by subscribing a capital increase undertaken for this purpose. Wang Jianlin controls 20% of the club as a result of this transaction, making him the first Chinese investor in a major European football club. Atlético de Madrid currently has the third largest budget of Spanish football clubs, and the transaction will inject substantial liquidity into the business, also reducing its level of debt and providing a means of entry into the Chinese market. The club hopes to establish its brand image and attract new fans in China, a process which has been successful for various clubs from England's Premier League. For this Chinese investor, the European football industry is an opportunity to further diversify his portfolio in a consolidated low-risk sector, and to support the establishment of a brand in Europe. It is also a dream for the magnate, who previously owned one of the most successful football clubs in China – Dalian Wanda FC[6] – from 1994 to 2000. The collaboration agreements arising from the transaction include the creation of a football academy in China.

Chinese firms' increased interest in establishing a brand image in the Spanish market is also reflected in the technology company **qbao.com's** sponsorship of Real Sociedad football club in the 2014-2015 season. Qbao.com is a subsidiary of Qianwang Intelligent System, with activities focusing on developing smartphone technology and supplying smart applications and tools through such devices. The firm has five million customers, a modest market share in the gigantic Chinese market, but is currently expanding and has good growth prospects. The agreement includes making the qbao.com brand visible on advertising materials – and the team shirt – and at marketing events, as well as the possibility of Real Sociedad being involved in training players from the Chinese club owned by the same company, Nan Jing Qianbao.

Also in the sports industry, the sportswear company **Xtep**, which specialises in designing, developing, manufacturing and distributing sportswear and provides kits for teams such as Villarreal CF, continued to expand in Spain by opening a network of points of sale in 2014 and 2015. The company started in the Valencia region and is planning to open stores in Madrid and Barcelona.

Other key sectors

In the **shipbuilding sector**, in 2015 the Galician shipyard Rodman – which specialises in pleasure boats – was acquired by **China Sonangol** International Holding, a firm with 70% Chinese and 30% Angolan capital that specialises in oil and natural gas, and which has numerous foreign subsidiaries. The transaction, valued at €100 million, was signed a few months after the shipyard received an order for 40 patrol boats and 30 catamarans from Angola. Sonangol, which operates primarily in the oil industry, became interested in Rodman through the latter's investee Metalships & Docks, a shipyard specialised in steel vessels which in recent years has focused on support vessels for the oil industry.

In the **financial sector,** over the course of 2015 **China Construction Bank** (CCB) became the Chinese bank with the second largest physical presence in Spain, surpassed only by ICBC. The Chinese behemoth CCB has a capitalisation of almost €200,000 million, double that of Santander, and has entered the Spanish market by opening a branch in Barcelona. The branch in fact belongs to its Luxembourgian subsidiary, and is therefore an EU bank in the eyes of Banco de España and covered by Luxembourg's Deposit Guarantee Fund (DGF). CCB is one of the "big four" Chinese banks, the second largest bank in

6 "Dalian Wanda scores 20% stake in Atletico Madrid". Financial Times. 2015.

the world in terms of market cap and has extensive operations around the world, including Europe. It has a 10% interest in Bank of America and has a relationship with Spain's Santander, with which it created a joint venture (19.9% owned by Santander) to render banking services to rural areas of inland China. CCB opened a Spanish branch in Barcelona in the summer of 2015, with registered capital of €20 million.

In the **service infrastructure sector**, Madrileña Red de Gas, which is responsible for distributing gas to the city of Madrid, announced that it had been sold to **China's Gingko** Tree sovereign wealth fund and the Dutch pension fund PGGM for €1,300 million. The company's former majority shareholder, Morgan Stanley, considered listing the firm's shares, but eventually decided to sell instead. The winning consortium, which competed with another two bidders – one comprising the Canadian company CPP and the German insurer Allianz, and the other formed by the Canadian company PSP and the fund manager Arcus – will also assume Madrileña Red de Gas's debt of €775 million.

Chinese companies present in Spain are continuing to grow in sectors which offer greater added value.

In addition to these new investments, certain major Chinese companies already established in Spain have continued to consolidate and expand their activities. In 2014, the technology company **Huawei**, whose business activities in Spain began in 2011, sold more than one million handsets, consolidated the services it renders to customers such as ADIF[7], Indra and the Andalusian Regional Government and opened a Demo Room in its Madrid offices to demonstrate its most innovative products to shareholders and customers. Huawei has also stepped up its CSR activity in Spain, including a number of educational projects, such as a grant for Spanish engineers to study and train in China.

In 2014, a second technology company, **ZTE**, signed an agreement with the Basque telecommunications operator Euskaltel to manage its network. The agreement also subsequently led to ZTE establishing its headquarters for Southern Europe in the Basque Country. The Chinese company has a similar centre in Germany, with 1,000 engineers; representatives of the company have stated that the same level could be reached in Spain. The agreement offers a number of synergies and could be scaled up to include new telecommunications projects over the coming years. In addition, at the end of 2014 ZTE opened an online store for the Spanish market.

Lenovo has also continued to grow through acquisitions, most recently in October 2014, when it acquired Motorola from Google for USD 2,910 million, making it the third largest smartphone manufacturer, behind Apple and Samsung. Although the transaction was accounted for in the US, in terms of growth of the company it has repercussions for all of Lenovo's markets, including Spain. Last year, Lenovo grew by 40% in the Spanish market and in PC sales its market share was 11.7%. The company also grew structurally, significantly expanding its workforce at both its Madrid office, where it opened new facilities, and at its Barcelona office.

Meanwhile, Telefónica has announced that it intends to carry out further joint acquisitions with **China Unicom**, with which it has crossholdings and an agreement to undertake joint projects, such as purchases of handsets. Their negotiating power is difficult to beat in the telecommunications sector, as Telefónica has 319 million customers and Unicom 439 million. In October 2015, the two companies formed a new alliance to share databases, in order to offer a better level of service to international customers.

Haier specialises in air conditioning equipment and electrical appliances, but offers a much wider range of consumer electronics in China. In 2014, it launched its first smartphones onto the Spanish market, reaffirming its commitment to Spain and its expectations for the country, having terminated its agreement with Fagor Electrodomésticos in 2013, when this firm was experiencing considerable financial difficulties. Haier has confirmed its position in Spain as one of the first Chinese companies dedicated to creating a global brand of Chinese origin and being a pioneer in European e-commerce.

The Chinese bank **ICBC**, which has been operating in Spain for four years, continued to focus on retail banking but has also expanded its product portfolio by creating an OEIC in Luxembourg, whose funds will be distributed through its Spanish subsidiary. ICBC recently opened a new space at its office in Madrid to host and house Chinese companies interested in exploring opportunities to enter the Spanish market.

In the sea transport sector, **Cosco Iberia**, the Spanish subsidiary of the Chinese shipping company Cosco, has continued to extend the services it offers its customers by increasing its activity at Spanish ports. By way of example, the Port of Castellón was added as a port of call on routes between Africa and Europe in 2014. The Hong Kong company **Hutchison Port Holding**, meanwhile, upped its investment in the Port of Barcelona terminal expansion by €150 million.

Moreover, **Air China**, which has offices in Madrid and Barcelona, has continued to expand in Spain by exploring new routes, such as a possible direct flight from Barcelona to Shanghai, in competition with Germany, which would complement the existing direct route from Barcelona to Beijing.

[7] Administrador de Infraestructuras Ferroviarias, Spain's state-owned rail infrastructure administrator

What can a country like Spain and its economy offer Chinese FDI?

Spain shares a number of attractive features with other European countries, but also has singular characteristics. The attributes it shares with other European nations include institutional and economic stability, a market with high purchasing power, a qualified workforce and top level infrastructure. Its singular features include the privileged and entirely unique relationship with Latin America, offering an unrivalled opportunity for Chinese companies to operate in the region through Spanish firms, a geostrategic position adjacent to North Africa and its high quality of life. These factors now go hand-in-hand with the depreciation of assets, including real estate and industrial land, and the decline in labour costs caused by the economic crisis. This makes the country a particularly appealing means of investing in Europe due to its attractive return on investments.

According to sources cited by the official news agency Xinhua, in early 2015 the Chairman of China's Chamber of Commerce estimated that the country's investment in Spain would amount to €3,000 million over the next two to three years. He also stated that investments would focus on four sectors: **real estate, tourism, renewable energies and agri-food**[8]. Further and more significant Chinese investment in Spain can be expected in these four sectors for two reasons. On the one hand, the change in China's economic model and the rising disposable income of the country's inhabitants will drive investment in these industries. On the other, these are economic sectors in which Spain has clear competitive advantages in terms of attracting investors, even at European level.

Firstly, the **Spanish real estate market** has a number of attractive characteristics to appeal to Chinese capital. The surplus of housing built during the boom has resulted in an enormous stock of real estate assets which is not covered by current demand and is therefore pushing prices down. In fact, house prices have fallen by 30% to 50%, according to different sources. The decline in value has also extended beyond housing, affecting industrial land, land for development, emblematic public buildings, offices and shopping centres. Problematic assets on the balance sheets of financial institutions were transferred to SAREB (Spain's "bad bank"), which has played an important role in channelling real estate assets towards foreign investors. The favourable situation for investment in the sector in Spain has been bolstered by a large number of transactions involving foreign funds and SOCIMIs[9] in 2014, with a total of €9,000 million invested in the real estate sector[10]. To date, the largest investment of Chinese capital in Spain's real estate market is that carried out by the Dalian Wanda Group. The new "Golden Visa" launched by Spain may also attract Chinese investors, increasing investment in the sector.

Secondly, in the **tourism sector**, Spain is a world power, figuring year after year amongst the top three destinations for tourists in terms of revenues and the number of visitors, usually ranking below France and the United States but above China and Brazil. In 2014, 65 million[11] foreign tourists visited Spain, the largest increase in the past 14 years. However, Chinese tourists represent a very small portion of this total, at around 200,000 to 300,000 a year, although this figure has grown in recent years. Spain only attracts 5% of Chinese visitors to Europe. On average, Chinese tourists have substantial purchasing power, spending €2,000 during their stay, double that of German tourists. The imbalance between a country that is set to become one of the top nations in terms of outbound tourists and Spain, which is ranked third in terms of inbound tourists, should be evened out over the coming years. This room for growth is expected to give rise to significant new investment in Spain from China. Transactions to date have targeted the hotel sector, including the investments and stakes purchased in the NH chain, in which the HNA Group has continued to expand its shareholding; the acquisition of Hotel Valparaíso in the Balearic Islands by GPRO; and, more recently, the Chongqing Kangde Group's acquisition of Hotel Santiago Barceló in the Canary Islands. However, other business initiatives, such as HNA's interest in Air Europa and the Globalia Group, and institutional projects, such as the increase in the number of air routes between the two countries, reflect Chinese investors' growing interest in the Spanish tourism sector. Last year, Air China began operating a direct flight from Beijing to Barcelona, and is currently studying the case for direct flights between the Chinese capital and Malaga or between Shanghai and Barcelona. A number of other companies have also added routes to meet the requirements of Chinese tourists during visits to Spain. Moreover, in recent years a number of agreements have been signed to promote tourism, such as the 2014 accord between the councils of Madrid and Zhengzhou, capital of the Henan province, and Costa Adeje's (Tenerife) agreement with China's Council for the Promotion of International Trade.

8 http://www.radiocable.com/xinhua-china-invertira-esp-3000. html

9 SOCIMIs (Spanish real estate investment trusts) are entities whose shares are traded on the secondary market, acting as an instrument for investment in the property rental market

10 http://www.expansion.com/2014/12/30/empresas/inmobiliario/1419955783.html

11 http://www.elmundo.es/economia/2015/01/22/54c0e4ad268e3e1c6b8b4584.html

Thirdly, in the **energy sector** China will continue to make substantial efforts to transition to a more sustainable energy system with a larger proportion of renewable power. The country's overdependence on fossil fuels has led to a rapid deterioration of its environment, threatening the health and life expectancy of the millions of inhabitants of urban areas. This factor is one of the primary potential sources of social and political instability. Faced with this situation, China is looking to obtain the know-how and technology to boost renewable energy, while Spain has cutting edge technology in the solar photovoltaic and wind power segments. Last year, some minor transactions took place in the sector, such as the acquisition by China's Huadian Corporation– a state-owned enterprise specialised in electricity generation – of a wind farm from Spain's Gamesa. In the coming years, we may see more transactions of this kind, including investments of Chinese capital in Spanish energy groups.

Lastly, in the **agri-food sector,** exports of food and beverages from Spain to China rose by 18% last year, reflecting considerable interest among Chinese citizens in Spanish products. One particularly appealing subsector is wine, which has grown rapidly in China in recent years. Wine is seen as a status symbol and a sign of sophistication by citizens with substantial purchasing power. In response to the low quality and production capacities of local vineyards, a number of Chinese investors have looked to acquire foreign wineries.

In Europe a number of transactions have taken place involving wineries from the Bordeaux region of France, and there is growing interest in exploring the Spanish market. In fact, the Fosun Group has acquired 20% of the Osborne Group and Changyu Pioneer Wine recently acquired a shareholding in the Marqués de Atrio winery, which in turn has announced plans to expand into China. This transaction enabled the Changyu Group to strengthen its plans for international expansion and its presence in Europe, adding to its existing interests in Italy and France. At the end of last year, it was announced that the first Spanish wine academy would be opened in China, training students in viniculture and bolstering bilateral relations in the sector. In addition to wine, there have also been signs of interest in identifying oil mills which could provide access to the know-how and production techniques used in the olive oil subsector. However, to date no acquisitions have been made. In any case, the financial circumstances and lack of liquidity at Spanish wineries and oil mills may contribute to Chinese investment in various companies over the coming years.

In other sectors, Hebei Iron and Steel Group acquired 51% of Duferco International, headquartered in Switzerland, also consequently investing indirectly in the Spanish metallurgy company Duferco España, located in Catalonia.

Box I.

Catalonia – a doorway to Europe, Africa and Latin America

Author: Roger Costa, Investment Promotion Manager, Catalonia Trade & Investment

Catalonia is a natural doorway to Europe and Africa and an excellent stepping stone between Asia and Latin America. It is also one of Europe's most important manufacturing hubs and most attractive business centres. Its industrial heritage and openness to foreign markets (its exports represent 25% of the Spanish economy) have led to the development of a robust logistics sector which can compete on the global stage.

Barcelona is the only city in Southern Europe that simultaneously boasts one of the most important ports in the Mediterranean, a high-speed train service, an international airport and connections to the European road network, as well as being the largest logistics area in the region. What is more, all of this infrastructure is located within a radius of 10 kilometres.

Catalonia's production and demography are highly concentrated: with double the average population density of Europe and a per capita GDP 12% above the European mean, the region has enormous potential in terms of manufacturing and consumer spending. It also attracts companies from the logistics sector and is a means of generating added value.

With its extensive interconnected network and efficient logistics infrastructure, Catalonia has an area of influence encompassing 400 million consumers, equivalent to 60% of the European Union's GDP, who can be reached within just 48 hours.

Catalonia's industrial and logistics sectors are highly attractive to foreign capital – the region has approximately 40,000 transport and logistics companies that render high value-added services.

Logistics firms such as Cosco or China Shipping were the first Chinese investors to set up operations in Catalonia, and they have been followed by other key companies from the sector, such as Kerry Logistics. Notably, the Hong Kong company Hutchison Port Holdings, one of the world's largest port operators, has invested in Barcelona by establishing its base of operations in the city. This first semi-automated terminal ("BEST terminal") is the largest in Southern Europe. BEST is the only terminal in the Mediterranean with 11 gantry cranes that can operate simultaneously. In 2014, Hutchison expanded on its initial investment in the Port of Barcelona by €150 million to extend the freight terminal. In 2015, the company has undertaken further acquisitions to allow it to offer comprehensive logistics solutions through development of the hinterland in Spain and southern France.

Chinese- and Hong Kong-owned logistics operators and shipping companies with bases of operations in Catalonia:

CHINA	GRAND VIEW CONTAINER TRADING SOUTH EUROPE SL.
CHINA	COSCO IBERIA SA
CHINA	CHINA SHIPPING SPAIN AGENCY SL
CHINA	UBC ESPANA SL.
CHINA	CONTAINER MULTIMODAL SERVICES LOGISTICS SPAIN SL.
HONG KONG	AIR SEA WORLDWIDE SPAIN S.L.
HONG KONG	VANGUARD LOGISTICS SERVICES SA
HONG KONG	CROWN WORLDWIDE MOVERS S.L.
HONG KONG	HUTCHISON PORT HOLDINGS
HONG KONG	KERRY LOGISTICS.

Catalonia is extremely well suited for logistics: its geostrategic location, transport infrastructure network, capacity for consumer spending and its business network make the region, and specifically the city of Barcelona, one of Europe's connectivity nerve centres. Multinationals such as Honda, Schneider Electric, Mango and the Inditex Group have benefited from these advantages by establishing their distribution centres in Catalonia.

These factors, together with the availability of industrial and logistical land at attractive prices, increase the competitiveness of Chinese companies wishing to establish operations in Europe. One recent example is Nanfang Pump Industries, which chose Catalonia as its logistical operations base for Europe, North Africa and Latin America.

3.4. Study on Chinese investment in Spain: reasons for investment, challenges and outlook

The conclusions drawn in this chapter are taken from a study conducted by ESADE on Chinese companies with investments in Spain. The ESADE China-Europe Observatory identified a total of 75 Chinese companies[12] registered in Spain. The list does not include companies incorporated by Chinese entrepreneurs who reside in Spain or collaboration agreements between Chinese and Spanish firms. One example of the latter is the sponsorship and marketing agreement between the Chinese telecoms company qbao.com and the Real Sociedad football club, which was first signed in 2014 and then renewed for the 2015-2016 season.

To study Chinese investment in Spain, in addition to monitoring and analysing investments in the country, a survey was performed using a questionnaire with 25 categories of questions, which was very similar to the one used in 2013 for Chinese companies in Spain (results published in the ESADE report for 2014). This is therefore ESADE's second survey on companies from the world's second largest economy that have invested in Spain. Many of the top Chinese firms in terms of foreign assets participated in the survey. The sample encompasses a total of 24 companies and their answers were compiled in the period from 3 March to 3 July 2015. In most cases, the respondent was the general manager or another member of the management team. Table 3 lists the companies that took part in the study and the sector in which they operate. As shown in the table, despite the wide range of sectors – 15 industries are represented – there is some degree of concentration in the telecommunications, consumer electronics, transport and logistics sectors.

Table 3 Chinese companies taking part in the ESADE study (March-July 2015)

COMPANY	SECTOR
AIR CHINA	Transport and/or logistics
Air Sea Worldwide Spain, S.L.	Transport and/or logistics
Ausome Europe S.L.	Food and beverages
BAOSTEEL ESPAÑA S.L.	Metallurgy
Bluestar Siliconas España S.A.	Chemicals
China Construction Bank (Europe) S.A. Spanish Branch	Financial activities
Chint Energy S.L.U.	Energy
COSCO IBERIA S.A.	Transport and/or logistics
DAXIONG SPAIN S.L.	Metallurgy
ELAI CULTURAL S.L.	Tourism and entertainment
Gree Spain Corporation, S.L.	Electronic components and electrical appliances
Haier Iberia	Electronic components and electrical appliances
Hisense Iberia S.L.U.	Electronic components and electrical appliances
HUAWEI TECHNOLOGIES	Telecommunications
ICBC	Financial activities
Keewaymotor Spain, S.L.	Vehicles
KERRY LOGISTICS (SPAIN) SAU	Transport and/or logistics
Lenovo Spain	Telecommunications
Mindray Medical España S.L.	Healthcare
MINMETALS ESPANA, S.L.	Metal materials
Wanda Group	Real estate
YINGKE ADARVE LAW FIRM	Legal
Zhongli Science and Technology Group	Energy
ZTE ESPAÑA S.L.U.	Telecommunications

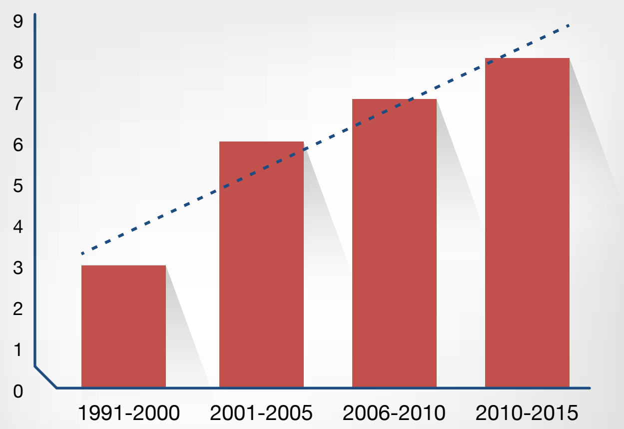
[12] The term "Chinese company" refers to businesses whose registered office is in Mainland China or Hong Kong.

Profile of Chinese companies in Spain

The presence of Chinese firms in Spain is a recent phenomenon. Chinese companies first arrived in Spain in the late nineties, and since then their presence in the country has steadily grown at an average rate of 20% annually over the past fifteen years.

Chart 3

Investments in Spain by Chinese companies (1990-2015) – (Sample of 24 companies)



Source: Own research.

Greenfield projects provided the means of entry into the country for 60% of companies, while 30% came in through representative offices and the remaining 10% through acquisitions or joint ventures. That said, there has not yet been a major acquisition of a local company in Spain, in contrast with other European countries that have attracted the most investment from China. The largest investment to date remains that of the Hong Kong company Hutchison in the Port of Barcelona, for a total of €400 million.

Of the companies surveyed, 70% financed their investment with own funds, 10% with assistance from the Chinese government and the remaining 20% with loans from Chinese and Spanish banks, in equal proportion. Although the sample of companies that participated in the study comprises companies and groups that have made substantial foreign investments, most of the Chinese businesses in Spain can be categorised as SMEs. Of the sample surveyed, Huawei has the most personnel, with 900 direct employees. Just 8% of companies have a permanent workforce of more than 200 employees; 21% have workforces totalling 51 to 100 employees and the vast majority have 20 to 50 employees. These are nonetheless subsidiaries of large multinationals, most of which are listed on the stock exchanges of Shanghai, Shenzhen, Hong Kong, London or New York.

The survey confirms the rise in the number of Chinese companies with private or primarily private capital, which represented 62% of the total, compared to companies with public capital, which amounted to 38%. However, if we analyse the management structure, the CEOs of two thirds of the Chinese companies surveyed are Chinese nationals. Non-Chinese CEOs can be found in Chinese trading companies, in which knowledge of local markets and distribution networks is critical. Such is the case of Haier. The same situation can be found in multinationals of Chinese origin (for example, Lenovo), which place considerable value on their global management structure and have incorporated different organisational cultures during the course of their international expansion. Finally, a large majority of Chinese companies in Spain and Europe still have Chinese leadership, accompanied by a general manager or deputy general manager from the local market.

Subsidiaries of Chinese firms in Spain predominantly report to a head office in Europe that is not usually located in Spain. This is the case for Haier Iberia, which reports to Haier Europe in France, and for most Chinese banks, which generally have their European headquarters in Luxembourg. Some Chinese firms – mostly SOEs, but also some private companies – report directly to their head office in China. One example of this profile in the electronics sector is Gree, a firm that manufactures and markets air conditioners, which reports directly to its parent in China.

Reasons for investment in Spain

One of the questions we asked in the study was: **What are Chinese companies' main reasons for investing in Spain?**

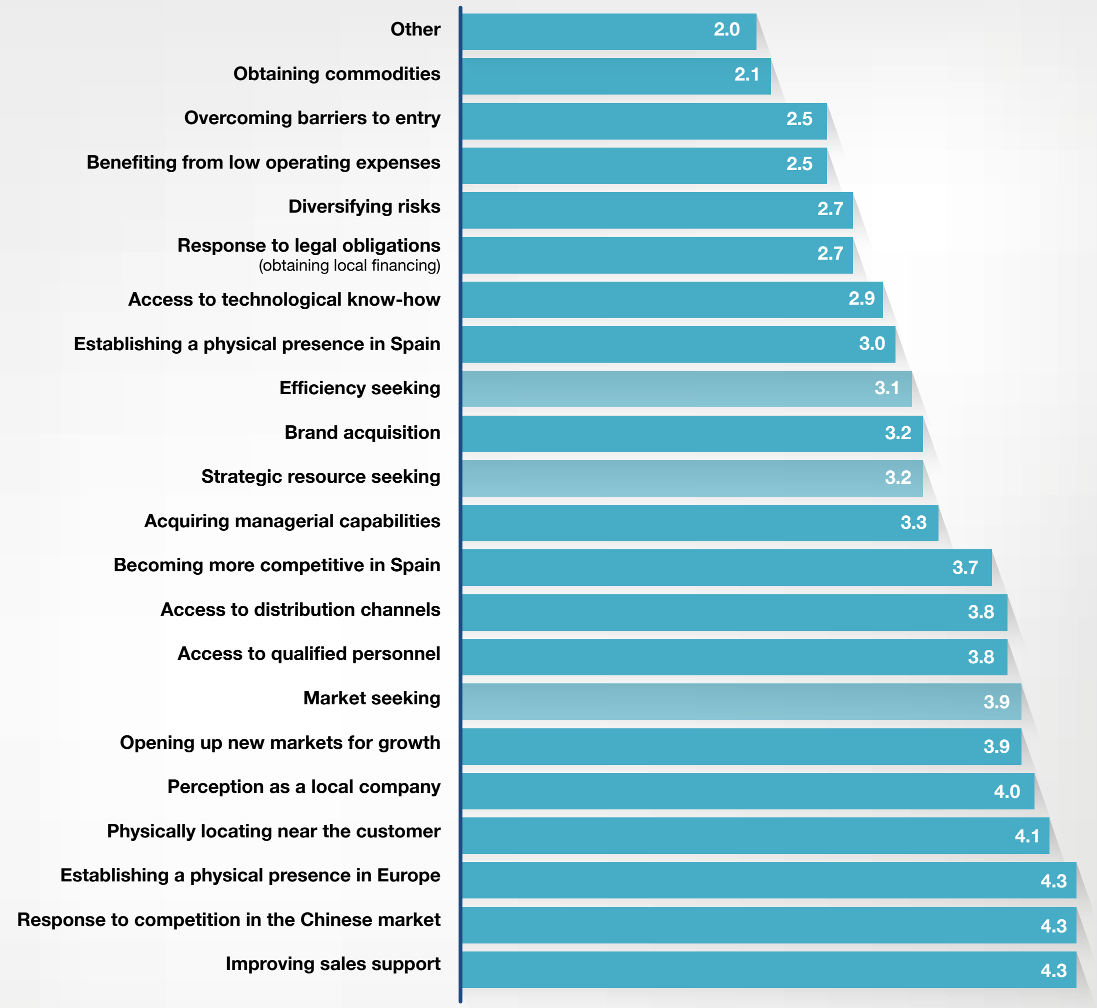
The three categories of reasons used in the 2013 study were again employed in the new survey. In this edition, the Chinese companies surveyed confirmed that their main reason for investing in Spain was market seeking, following by strategic resource seeking and lastly efficiency seeking.

Three factors received almost full points in the **market seeking** category: two factors related to the Spanish market and another related to the company's market of origin, China, all scored 4.3 points out of a maximum of 5. The surveyed companies indicated that the main purpose of their investment in Spain was to understand the Spanish market and adapt their products or services to the requirements of local customers and thus gain market share. A physical presence in Spain allows them to better understand the market and complement their portfolio of products or services with pre-sales and after-sales services. Entering the Spanish market also allows them to access the European market. In addition, for Chinese companies international markets are a means of reacting to increased competition in their home market, by diversifying risk across other markets or strengthening their competitive position in China.

The next category was **strategic resource seeking**, based above all on four factors: being perceived as a local company rather than a foreign undertaking; recruitment of highly trained personnel, which, as we will see in the analysis of the business climate, was ranked as Spain's main strong point this year; access to a local distribution network, and acquisition of advanced management techniques. Although Chinese companies consider that they learn a lot from their Chinese parent, they are also aware of the need to adapt to local markets and learn management techniques to minimise the cultural and management gaps.

The third ranked category was **efficiency seeking**. This category encompasses the acquisition of local brands and the value of having a physical presence in Spain. Evidence of this was found above all in the services sector, which includes hotels and large distribution establishments, such as the physical and online stores of the Chinese sportswear brand Xtep. In contrast, access to technological know-how does not yet appear to be one of the main reasons for entering the Spanish market. Technological know-how is generally handed down by the Chinese parent or comes from R&D centres in other European countries. Even so, there are some cases where Spanish subsidiaries of these Chinese companies are leading European or global projects from Spain and assuming responsibility for European operations from Spain. Examples include Lenovo, whose organisational structure interconnects European subsidiaries with cross-border responsibilities within Europe, and Haier, which recently assigned responsibility for European operations to its Spanish subsidiary.

Tabla 4 Chinese firms' reasons for investing in Spain



Source: Own research. Minimum score = 0; maximum score = 5

Business climate

As part of the survey, the Chinese companies were asked to rank 17 variables relating to the business climate in Spain, grouped into six areas: human resources, market, infrastructure, tax system, costs and regulations. The variables were the same as those used in the 2013 ESADE study, with the sole addition of an evaluation of Spain as a doorway to the European, Latin American and North African markets.

Generally speaking, Chinese companies' evaluation of the Spanish business climate is moderately positive, with a slight improvement on 2013. The average score for the six categories that measure the business climate rose from 3 to 3.3 out of 5. The highest scoring category received 3.9 points and the lowest ranked category 2.9, very close to a positive valuation (3 out of 5).

Of the six categories, the two with the highest scores were, once again, **"human resources"** and "infrastructure quality", both with higher ratings than two years ago (up from 3.3 in 2013 to 3.9 and from 3 to 3.7, respectively).

In the "human resources" category, Chinese firms rated all three component variables positively, in order of priority: the attitude of local human resources to China (up from 3.2 to 3.9 over two years) ; availability of labour (up from 3.3 to 4) ; and quality of qualified workers and management (up from 3.4 to 3.9). All of these aspects, but particularly the positive attitude of local human resources to China, are especially important for Chinese companies operating in international markets and working against a perception of their brands and companies which is not always positive.

The second highest rated category was **"infrastructure quality"**, whose score also increased on 2013, up from 3 to 3.7 out of 5, the largest rise in the study. The highest score was given to ports (3.9), closely followed by airports (3.8), roads (3.7) and the rail network (3.5). The quality of Spain's port infrastructure is also confirmed by the presence in the country of the major Chinese shipping companies, such as Cosco and China Shipping, and Hutchison's commitment to the Port of Barcelona. In Spain, both private and state-owned operators of all forms of transport are aware of the strategic importance of the sector for foreign investors. Support is therefore being given to new projects, above all to bolster integrated transport and logistics services. Examples include the European project for the Mediterranean Corridor, the Chinese project for the Silk Road and the local initiative Barceloc.

Chinese firms also take a positive view of Spain as a consumer market (3.2). The size of the country's market was given a score equal to the average for the category as a whole, reflecting the strategic position of Spain as a doorway to the European and Latin American markets, rather than to North Africa. However the highest score in this category (3.3) was that for Spanish consumers' and intermediaries' attitude to the products sold by Chinese companies in Spain.

Also rated positively were Spain's openness to foreign investment (3.4), and operating expenses such as labour costs (3.4), which continued to score above 3. Chinese firms are somewhat less appreciative of the cost of land and offices, which they consider to be high. Costs relating to the average level of bureaucracy (2.8) and taxation (2.9) were rated close to the average, reflecting areas for improvement.

Table 5

Evaluation of the business climate in Spain

TAXATION SYSTEM	**2,9**	
Tax burden		2,9
Corporate income tax		2,9
INFRASTRUCTURE QUALITY	**3,7**	
Ports		3,9
Airports		3,8
Railways		3,5
Roads		3,7
HUMAN RESOURCES	**3,9**	
Quality		3,9
Availability		4
Attitude to China		3,9
COST	**3,1**	
Labour		3,4
Land		3
Offices		2,8
Other operating expenses		3,2
REGULATION	**3,1**	
Low level of bureaucracy		2,8
Openness to foreign investment		3,4
MARKET	**3,2**	
Size of the local market		3,2
Access to other markets: North Africa		2,5
Access to other markets: Latin America		3,1
Access to other markets: Rest of Europe		3
Acceptance of Chinese goods		3,3
AVERAGE SCORE	**3,3**	

Source: Own research

Box II.

Barcelona, China-Friendly

Author: Barcelona Activa.
Barcelona City Council

Nowadays, no one doubts that the 21st century will be Asia's era and that China will unquestionably become the continent's and the world's leading economy. The country's progressive economic dynamism, through the upsurge in Chinese firms establishing corporate offices abroad as part of a process of internationalisation, is increasingly setting it apart as a potential source of investment.

Government policies on foreign investment, diversification, market prospecting and promotion of internationalisation (the "Go-Out Policy") have driven a change in the direction of capital outflows from the Chinese economy. The country has rapidly transformed from being the world's factory and a net receiver of foreign investment to being a net issuer of FDI.

Barcelona must take advantage of this trend, firmly positioning itself in this emerging market to attract high-quality Chinese firms that will increase the city's activity and economic standing.

A number of characteristics and conditions place Barcelona in a privileged position in terms of achieving this objective:

• Catalonia and Barcelona are China's main Spanish trading partners. Catalonia accounted for 26.60% of Spain's total exports to China in 2014, and 30.15% of its imports.

• The Chinese population in Catalonia has multiplied by 11 in recent years, up from 4,396 inhabitants in 2000 to 49,773 in 2014. Barcelona is the municipality with the highest concentration of Chinese residents: 16,435 Chinese citizens were registered as residents of the city, the third largest group of foreign residents in Barcelona, behind Italians and Pakistanis.

• In terms of composition, the Chinese community in Catalonia is decidedly young: 70% of Chinese residents are aged 16 to 44. The presence of a young, dynamic and entrepreneurial community is a positive and enriching factor for the society and economy of Catalonia and for relations between Barcelona and China.

• Barcelona has a logistics infrastructure which is tailored to the Asian market, including the new port terminal operated by the Chinese firm Hutchison and future projects such as the Mediterranean Rail Corridor, which will bolster imports and distribution of goods from Asia by increasing the competitiveness of the city's port in relation to Atlantic ports in Northern Europe.

Barcelona must seize these competitive advantages to attract Chinese investment. Barcelona City Council is fully aware of these opportunities, and has undertaken numerous actions and projects specifically targeting this market, with very positive results.

In 2000, Barcelona and Shanghai were declared twin cities. Since then, as part of this privileged relationship, a wide range of activities have been carried out each year to promote culture and the economy.

Ten years ago, the City Council created the "China Desk" to handle relations with Chinese investors, offering a service from specialised Chinese-speaking personnel with in-depth knowledge of the Oriental economy as well as the country's customs, protocols, traditions and culture.

The service has since attracted significant investments, most recently including a laboratory for industrial certification and inspection in Europe – CCIC Europe Testing – and the Spanish branch of China Construction Bank.

The Council has also organised a busy schedule of marketing events to position the city as an ideal business location for Chinese firms and to attract investment.

Examples include Barcelona's invitation to the 2014 edition of the Beijing Design Week trade fair, to publicise Catalan culture and design in the Chinese market; the 2015 edition of the Barcelona-Catalan Week in Shanghai to celebrate the 15th anniversary of the twinning of the two cities; the 10th anniversary of the Casal Català in Shanghai (Catalan Cultural Association) ; participation in eight editions of the China Hi-Tech Fair (CHTF) in Shenzhen and the latest edition of the Mobile World Congress in Shanghai.

In terms of its impact, Barcelona's attendance at the Hong Kong Business of Design Week 2015 (the first time a city and not a country has been invited) was also significant, with substantial representation of institutions, entities and companies from the city: Barcelona City Council, Regional Government of Catalonia, Port of Barcelona, Casa Asia, Institut Ramón Llull, Barcelona Centre Design, ESADE China Europe Club, as well as Catalan companies such as Roca, Mango, etc.

These actions are complemented by ongoing work to reinforce air routes with China. In 2014, the Barcelona-Beijing flight route was launched and negotiations are underway with institutions in the Catalan capital to establish connections with strategic cities such as Shanghai and Hong Kong.

Challenges and outlook

Chinese companies consider that they face two challenges when conducting business in Spain: brand recognition (3.83) and local competition (3.75). In fact, companies rated these two factors highest, citing both local consumers' lack of awareness of Chinese brands and high levels of competition from local firms as significant barriers to entry that raise concerns for management of Chinese businesses.

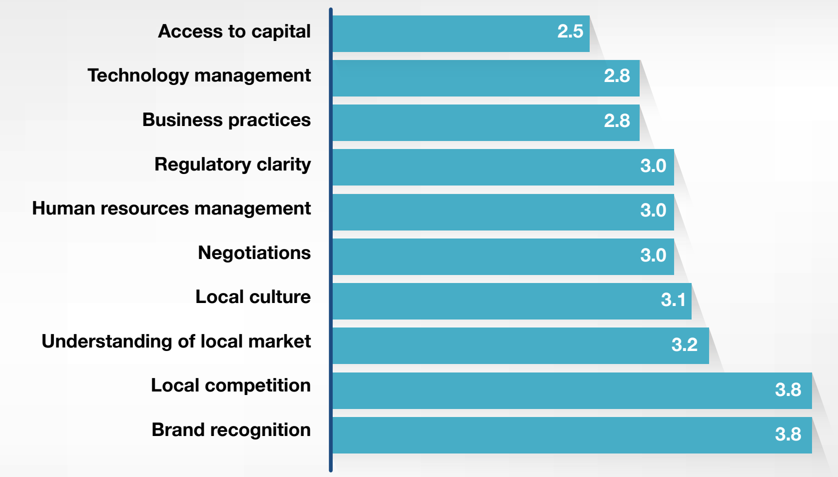
Secondly, the companies consider that understanding the characteristics of the market and local consumers, and adapting products and services to their needs, is also a key challenge. The clarity of regulations, management of human resources and knowledge of business practices are also seen as significant barriers. Conversely, Chinese firms are much more at ease with technology management in Spain; and access to capital is barely a concern, as their undertakings are generally funded from China, either using own funds or through financing from Chinese banks that are also undergoing internationalisation. As previously mentioned, two of the five major Chinese banks are currently operating in Spain: China Construction Bank (CCB), which recently entered the Spanish market, and ICBC, which has a four-year track record in Spain.

It is interesting to analyse the degree of satisfaction of Chinese companies in Spain. Regarding the expertise that Spanish subsidiaries can contribute to their Chinese parent companies, the surveyed firms took a very positive view of knowledge of foreign cultures and the know-how acquired through selling on new markets. They also have a positive perception of new product development and the knowledge acquired through international management. However, no value was seen to be contributed to the parent in terms of technological know-how or manufacturing processes, two factors that still largely depend on the parent or on subsidiaries in other countries.

With respect to financial performance over the past three years (2013-2015), 70% of the surveyed firms professed to be more than satisfied with their sales in Spain. In contrast with 2013, they also rated post-tax profits positively, with a score of 3 out of 5. Growth rates for companies in Spain likewise scored well, measured through workforce expansion (3.4) and market share (3.3).

In short, although Chinese investment in Spain is still a recent phenomenon, it is undergoing steady and sustained growth of 20% annually across a range of sectors, but with Chinese companies mainly concentrated in telecommunications, consumer electronics, and the transport and logistics sector. Three industries have significant investment potential: the tourism segment of the real estate sector, especially in relation to hotel investments; the agri-food sector, above all wine and access to local distribution networks; and the renewable energies sector, in which Spain is at the cutting edge globally. The forecasts provided by China's Chamber of Commerce are expected to be met over the coming years, whereby more than USD 3,000 million will be channelled into Spain, marking an end of the current incipient stage of investment.

Table 6 The main challenges facing Chinese firms in Spain



Source: Own research. Minimum score = 0; maximum score = 5

Box III.

Catalonia, a European partner for Chinese investment

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China's economic relationship with the rest of the world is being redefined at such a speed that we need to look back in time to understand the magnitude of the changes that have occurred. According to the United Nations Conference on Trade and Development (UNCTAD), China has moved up from being the thirtieth largest investor in the world in 2000, to the third largest in 2014. Combining China's and Hong Kong's investments, the country is the second source of outbound investment worldwide, behind the United States, with a total of USD 259,000 million, and ahead of third-placed Japan, with USD 114,000 million.

China has a large number of multinational companies in various sectors, such as logistics, IT and distribution. These companies are innovating, and have expansion strategies and the financial muscle to drive growth.

In recent years, many of these firms have found key investment opportunities abroad, especially in Europe. In this respect, Catalonia is well positioned to receive Chinese investment, either as a means of entering Europe or as the ideal stepping stone to North Africa or Latin America.

Catalonia, an industrial powerhouse

Catalonia's traditionally entrepreneurial nature has resulted in a dynamic economy that is home to approximately 600,000 firms. The region's business landscape is highly internationalised, beating its own export records over the past four consecutive years. With a rise of 3.1%, Catalonia had the fourth highest growth rate in export sales in the Eurozone in 2014[13].

Furthermore, Catalonia accounts for more than 25% of Spain's exports and houses almost 35% of Spanish companies that regularly export, percentages which more than exceed its 16% proportion of the nation's population[14].

The sound industrial base of the Catalan economy partly explains this export success. Industrial sectors represent 20% of Catalonia's GDP, which is above the average for the European Union and exceeds the European Commission's target for 2020.

Industry is a priority for the Catalan government. It has therefore approved an Industrial Strategy which – in line with European guidelines concerning smart specialisation, and taking into account the highly diverse nature of the Catalan economy – identifies the seven key fields in terms of critical mass, competitive advantages and leadership capacity.

These sectors, which offer interesting opportunities for capex investment, are: food and beverages, energy, chemicals and commodities, industrial systems, design, healthcare, sustainable mobility (going beyond automotive technology, and into IT and energy) and experience-based industries (creative, cultural, tourism and sports sectors). Each area has its own stimulus programme, comprising specific initiatives with a real impact on the sector as a whole.

Building strong relations between China and Catalonia

All of these factors represent values that are shared by China and Catalonia, including an entrepreneurial spirit, growing openness to international markets and a commitment to the industrial sector as the basis of a robust economy.

These common values have allowed the two regions to build a long and fruitful institutional relationship, promoting understanding between governments themselves, and between these public authorities and companies. Since the nineties, Catalonia has been working with key provinces such as Fujian, Jiangsu and Guangdong, and has signed memoranda of understanding with all of these provinces to strengthen economic and business ties. Barcelona is also twinned with Shanghai and works closely with Shenzhen, a city that shares the Catalan capital's pioneering role in establishing smart cities.

This highlights Catalonia's solid position in China, as reflected by Barcelona's invitation to the Beijing Design Week and the Hong Kong Business Week and its well-established participation in the China Hi-Tech Fair. At this latter trade fair, in 2013 the Catalonia-Barcelona stand was awarded the prize for the best design and activities.

The deepening of the relationship between the two territories is also demonstrated by the increased flow of tourists from China, as a result of improved air connections (Air China started operating a new direct flight in 2014). A total of 175,000 Chinese tourists visited Catalonia in 2014, and this figure is expected to exceed 200,000 in 2015, a rise of between 15% and 20%[15].

A doorway to EMEA and a bridge to Latin America

These relationships are very important in terms of favouring investment flows. However, one value proposal stands out above all the rest: Catalonia offers Chinese investors a doorway to Europe, the Middle East and Africa (EMEA) and an unbeatable bridge to Latin America. The region has a powerful logistics sector, with top quality infrastructure, scientific excellence, technological capabilities, talent and internationally renowned trade fairs and congresses.

13 Source: ACCIÓ based on provisional data released by ICEX and Eurostat.
14 Source: ICEX for exports and companies exporting regularly, and INE for population.
15 Source: Catalan Tourist Board.

The logistics and transport sector is an important part of the Catalan economy, representing 4% of its GDP and with 40,000 companies in the industry employing 155,000 workers[16]. Logistics, together with the industrial sector and tourism, is one of Catalonia's key strengths.

The Port of Barcelona has consolidated its position as the largest distribution centre between the Mediterranean and North Africa, with various scheduled routes to Asia. The Port of Tarragona, where a new chemicals dock was built in 2014, is also earning a positioning as the most important petrochemical platform in Southern Europe.

The high-speed connection with the rest of the continent through France, the first-class motorway network and an airport with ever-increasing passenger numbers all strengthen Catalonia's position as the key logistics hub for Southern Europe and the Mediterranean.

Catalonia's appeal goes beyond logistics; it also offers scientific excellence and a robust positioning in technology. Although it accounts for just 0.1% of the world population, Catalonia is responsible for 1% of global scientific output[17]. This excellence in science is supported by first-rate scientific infrastructure, such as the ALBA synchrotron and the Barcelona Supercomputing Center.

Catalonia's industry also stands out for its innovation. According to Barometer of Innovation in Catalonia data, 56.8% of Catalan companies with more than nine employees developed some kind of innovation in 2014. Many of these companies are highly technological and are therefore able to offer international investors added value.

Despite this beneficial positioning, the Government of Catalonia wants to extend access to technology to SMEs. With this goal in mind, EURECAT was created – an ambitious project to establish a major cutting-edge industrial technology provider in Southern Europe, which is now a reality.

Access to talent is another factor which attracts foreign companies choosing to establish a presence in the region. With its 13 universities and its internationally renowned business schools, such as ESADE, Catalonia is a major hub for national talent and also attracts foreign talent. In this respect, the government is committed to vocational training with a period of work experience, adapted to companies' requirements.

Finally, Catalonia in general and Barcelona in particular are venues for leading congresses and trade fairs, such as the Mobile World Congress (as part of Barcelona's position as Mobile World Capital until 2023), the Smart City Expo World Congress and Alimentaria. These trade fairs drive sectors such as IT and food and beverages, in which there is an ever larger proportion of Chinese companies, and create opportunities for local businesses and foreign visitors.

Growing Chinese interest in Catalonia

In view of these strong points, many foreign companies have chosen Catalonia as a base from which to expand (there are currently more than 6,400 multinationals established in the region). In recent years, numerous Chinese companies have selected Catalonia as the location for decision-making units, distribution centres or offices. As is to be expected in a diverse economy such as Catalonia, these actions have involved different sectors.

For example, in the agri-food sector, **Bright Food** is finalising its acquisition of Miquel Alimentació, the largest Catalan distribution group. Bright Food is China's second largest food and distribution company. It has a network of 4,000 establishments in the country and billings of around €18,000 million. The state-owned investment fund China Investment Corp, one of the largest sovereign wealth funds in the world, will be involved in this acquisition. This takeover will be Bright Food's first major transaction in Spain, and will afford the Catalan agri-food industry its footing in China.

In industrial systems, the Chinese firm **Nanfang Pump Industries** has reached an agreement with the Catalan company Inbrooll to create a new company, Hydroo Pump Industries, which will manufacture and sell industrial centrifugal pumps to European markets. In a second phase, the firm plans to expand into Africa and Latin America. Catalonia is at the heart of Nanfang's strategy; the company has established its head office for Europe in the region, from which it will drive its growth in the continent. Nanfang is one of the largest manufacturers of centrifugal pumps in China and is listed on the Shenzhen stock exchange. To date, the firm has invested in construction of a manufacturing plant, a testbed, a warehouse for finished products, an R&D centre and a customer training facility. The Catalan plant is the company's only combined manufacturing and sales facility outside China.

In the financial sector, **China Construction Bank** (CCB) has opened its first office in Spain in Barcelona. CCB is one of the leading Chinese retail banks, with assets totalling almost USD 208,000 million, a market capitalisation of approximately €200,000 million and nearly 15,000 offices around the world. The Barcelona office renders corporate banking services, working with Chinese companies operating in Spain and local firms with businesses in China or wishing to move into the Asian country.

In the IT sector, the Hong Kong communications provider **Cronos Group** selected Barcelona to expand its European operations and render services to its international customers. The company provides voice telecommunications and advanced data services in more than 80 countries and chose to invest in Catalonia based on factors such as its high quality human capital and its ideal operating conditions for IT companies.

[16] Source: Cimalsa Observatory and Cerdà Institute.
[17] Source: Recerca Foundation based on Thomson Reuters.

However, direct investments in Catalonia are not the only operations having an impact on the region. One clear example is the recent acquisition of Pirelli, a symbol of Italian industry, by the state-owned enterprise China National Chemical Corporation (ChemChina). The agreement, valued at approximately €7,100 million, is one of the largest expansions of a state-owned Chinese company abroad and its effects extend beyond Italy to the group's different subsidiaries, one of which is located in Catalonia.

ACCIÓ, an ally for Chinese investors

Most of these investments were supported by the Catalonian government through Catalonia Trade & Investment, an investor relations unit at ACCIÓ, a state agency promoting the competitiveness of Catalan companies. With 30 years' experience in supporting foreign investors and a range of services tailored to each particular case, the Catalan government aims to guide investors in bringing their projects to life.

This proximity is strengthened by Catalonia's network of 36 foreign Trade and Investment offices, including three in China (Beijing, Shanghai and Hong Kong).

Chinese investors are a priority for the Catalonian government. Specific communication and publicity campaigns have therefore been targeted at China, along with a range of tailored tax and legal advisory services for Chinese companies. Alliances have also been forged with other Catalan bodies present in China or which have operations in the country, such as the Port of Barcelona, Barcelona City Council and ESADE.

As a result of this collaborative framework, the Barceloc initiative recently got underway; the aim of the project is to attract investment from Asia – and from China in particular – in the industrial and logistics sectors, through an alliance of Catalonia Trade & Investment, the Port of Barcelona and a number of logistics operators.

All of these initiatives reflect the importance the Catalan government places on Chinese investors, as well as its intention and ability to guide their existing and future business projects, so as to maximise their probability of success. Catalonia is set to be the doorway to Europe for Chinese firms, with the Catalonian government as their key ally. This is our aim, and we will continue to work towards this goal.

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