

**CHINA-AFRICA INVESTMENT RELATIONS: A CASE  
STUDY OF NIGERIA**

# **Final Report**

**BY**

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# 1.0 Introduction

## **1:1 Problem Statement**

Nigeria's traditional development partners are mainly from Europe and the Americas (U.S. A. and Canada). These groups have dominated the flow of trade, investment (in terms of foreign direct investment-FDI) and grants and financial as well as technical aid to the country. These economic relationships are governed by various bilateral and regional agreements that exist between these countries and Nigeria. Although Nigeria and these countries have come a long way in their relationship, it is contestable if such has in any significant way assisted the country in its quest for development. The relationship appears to be exploitative at least from the trend in the structure and pattern of FDI inflow to the country. This is based on the fact that oil and gas sector dominates the country's exports to the tune of about 98% and FDI inflows to the oil and gas sector accounted for about 40% (Ogunkola, Bankole and Adewuyi, 2008).

Although China-Nigeria relationship dates back to 1971 (more than three decades), recent developments call for a careful and detailed analysis of this relationship and its potential impact on the economies. The growing relationship between China and Nigeria is induced by the fact that the two countries have economic complementarities. On one hand, a major development challenge in Nigeria is infrastructure deficiency, with huge investment need. Complementarily, China has developed one of the world's largest and most competitive construction industries with particular expertise in the civil works critical for infrastructure development coupled with its ability to provide the necessary financial assistance to the countries in need including Nigeria. On the other hand, China's industrialization drive and massive inflow of FDI into the country led to fast growing manufacturing economy which requires oil and mineral inputs that are outstripping the country's domestic resources, hence the need to source them from abroad including Nigeria which is well blessed with these resources.

Prior to the financial crisis, foreign direct investment (FDI) inflows to Africa had been rising strongly since 2002, reaching USD 53 billion over 2007, a 47.2 per cent increase on 2006 and their highest historical level. Although, Africa's share of global FDI flows registered a significant decline to 2.9 per cent of global FDI in 2007, down from 3.2 per cent

in 2006, recent estimates reveal that global FDI flows in 2008 to Africa have remained resilient, growing by 16.8 per cent to USD 61.9 billion over 2008, despite the slowdown. It is argued that the rate of return of FDI in Africa has been increasing since 2004 and, at 12.1 per cent, was the highest among developing host regions in 2007. Mergers and acquisitions (M&As) in Africa rose by an estimated 157 per cent to USD 26 billion in 2008.

Positive developments have been recorded recently in respect of the net FDI inflow from China to Nigeria, as it has doubled from US\$3 billion in 2003 to more than US\$6 billion in 2005. The share of the oil and gas sector was about 75 percent. This proportion of Chinese FDI to Nigeria implies the expressed and explicit desire of China in Nigerian oil and gas resources. It further reinforces the prevalence of a link between Chinese FDI and trade in the context of China-Nigeria investment relations. In Nigeria, like in some other African countries, three related factors explain the observed positive developments in Chinese FDI flows. These are change in FDI regime; privatization programme of the government; and the aggressive drive of government in attracting FDI into the country. The recent developments notwithstanding, there is a huge investment gap in the development of the Nigerian economy and the required investment can only be expected after the investment climate has improved. Beyond this, and since FDI constitutes a key channel through which impacts of China's economic growth<sup>1</sup> can be transmitted to the typical African economy, therefore for existing and future FDI inflow from China to be beneficial to Nigeria (and China) the following issues or questions become pertinent for research.

- To what extent is China different from other exploitative practices?
- In what sectors is incoming FDI from China directed?
- To what extent is Chinese FDI bundled with inflows of aid?
- Does this FDI augment productive capacity, or do the funds represent a change in ownership?
- Is incoming Chinese FDI resource- or market-seeking, and is the output targeted at the domestic or external market?
- What economic benefits arise from Chinese FDI in terms of exports, import-substitution, contribution of value added and employment?
- Does Chinese FDI exclude or strengthen the position of domestically-owned enterprise, and is there differential between the size of domestic firms? Is incoming FDI wholly-owned, or does it involve joint ventures, including with local partners?

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<sup>1</sup> However, the on-going global financial crisis has serious implications for inflow of FDI from China and indeed all Western investors. For instance, a decline in aggregate demand sequel to the financial crisis globally for Chinese goods and services will have negative impact on the Chinese economy with a possibility of imposing limitation on her FDI commitments. This study will attempt to capture the likely effect of the global financial crisis on China-Nigeria investment relations.

- Outside of the specific investments, what are the spread effects to the domestic economy in terms of skill development and capability building, the use of local inputs, supply chain management and technology transfer?
- How does Chinese FDI differ in character from FDI sourced from other sources?
- Are all Chinese investment flows inward, or does the country also invests in China?

Corresponding to these research issues is the following set of policy questions:

- What mechanisms are available for encouraging the inflow of beneficial Chinese FDI and discouraging the inflow of harmful ones?
- What policies might be introduced to maximize the positive impact of incoming Chinese FDI in terms of employment creation, foreign exchange generation, value deepening, employment, training, local sourcing and technology transfer?
- To what extent can inward Chinese FDI be directed to meeting the needs of the less advantaged population, for example through its product profile or the technology which is utilized?
- To what extent can effective policies towards incoming Chinese FDI be determined at the national level, or does it require coordination with other regional economies, the African Union (AU) and other regional bodies?
- How can Chinese FDI be leveraged to provide preferential access to Chinese markets?
- How can governments play off Chinese and other sources of FDI to maximize the development impacts of FDI?

## **1:2 Objectives of the Study**

The scope of the study covers 1997-2007 and the objective of this study is to analyze the economic relation between China and Nigeria in the area of foreign direct investment (FDI) with a view to determining its developmental impacts. Specifically, the objectives include:

- An inventory of FDI inflows from China including their sectoral breakdown and an analysis of trends;
- An estimation of the extent to which this FDI represent the creation of new or augmented production capacities or a change in ownership of existing production units;
- An analysis of the extent to which overall Chinese FDI inflows are bundled with aid;
- A description of the regulatory regime governing FDI inflows and the extent to which they embody China-specific provisions;

- An analysis of the characteristic of major Chinese FDI, i.e., whether they are resource- seeking or market-seeking, and whether the output is targeted at the domestic or external market;
- An assessment of the economic benefits that arise from major Chinese FDI in terms of exports expansion, reduction of import dependence, contribution of value added and employment, government revenue, etc;
- An assessment of the extent to which major Chinese FDI exclude or strengthen the position of locally-owned enterprises;
- Analysis of the ownership structure of incoming FDI, i.e., wholly-owned, joint ventures with local partners or joint ventures with other foreign partners or joint ventures with local and foreign partners ;
- Outside of the specific investments, an assessment of the spread effects of the FDI to the other sectors of the economy in terms of skill development and capability building, the use of local inputs, supply chain management and technology transfer;
- A comparative analysis of the characteristics and practices of Chinese FDI and those from other sources;
- A determination of features, size and sectoral distribution of the country's investment in China (if any) and the nature of support such outward investments the received from the home government as well as from Chinese Authorities;
- An articulation of options for supporting the development of locally owned firms that can partner effectively with Chinese FDI and also invest in China;
- An articulation of strategies for taking maximum advantage of low cost of delivery of development infrastructure by Chinese construction companies while maintaining quality;
- An articulation of strategies for ensuring high quality of Chinese construction services, discouraging unwholesome business practices and controversial labor practices;
- Articulation and analysis of the policy responses necessary to optimize investment relations with China if and when China acquires the attributes of an advanced industrialized economy and the associated changes in the features and pattern of its investment relations with the country.

### ***1:3 Organization of the Report***

The report is organized as follows. Section 2 is the background to the study. In section 3, the review of literature and theoretical framework is carried out. The theoretical framework adopted for the study as well as the methodology for the macro, micro and case studies carried out in the study are discussed in section 4. In section 5, the empirical analysis in the context of macro, micro and case studies dimensions of the study is presented. The final section, section 6 contains the conclusions as well as the policy recommendations arising from the findings of the study.

## **2.0 Background of the Study**

### ***2:1 Profile of the Nigerian Economy***

#### **2:1:1 Macroeconomic Performance and Business Environment in Nigeria**

Nigeria's economy has experienced strong growth in recent years, sequel to various economic reform measures put in place to aid the performance of the economy. Real GDP growth averaged 6.3 percent from 2004 to 2007, and growth of 6.4 percent in 2008. This level of real GDP growth was considered satisfactory compared to less than one percent in 1999. The growth was attributed mainly to sound monetary and fiscal policies complemented by the favourable weather which enhanced agricultural output. Between 2002 and 2008, main driver of the growth phenomenon was the non-oil sector as non-oil GDP growth averaged 8.9 percent. At sectoral level, average rate of growth in respect of 2004-2008 indicated that the agricultural sector grew by 7 percent, while wholesale and retail trade, services and the building and construction subsectors recorded growth rates of 13.6, 9.3, and 12.3 percent, respectively. Industrial output for the same period however indicated a negative growth rate of 0.5 percent due mainly to the poor performance of the oil sector (see Table 1). Foreign Direct Investment (FDI) has grown from an annual of below US\$ 1 billion in 1999 to about US\$ 13 billion in 2007. The country's external reserves have also grown phenomenally, from below US\$ 5 billion in 1999 to US\$ 53 billion in 2008 and indeed could support 16.6 months of imports (CBN, 2008).

**Table 1: Real Growth Rates, 1982-2008**

<i>ACTIVITY SECTOR</i>	<i>1981-90</i>	<i>1991-2000</i>	<i>2001-08</i>	<i>2000</i>	<i>2001</i>	<i>2002</i>	<i>2004</i>	<i>2005</i>	<i>2006</i>	<i>2007</i>	<i>2008</i>
<b>AGRICULTURE</b>	4.5	3.4	5.8	2.9	3.9	4.3	6.5	7.1	7.4	7.4	6.5
<b>INDUSTRY</b>	1.4	1.6	1.5	3.1	4.9	6.4	4.2	1.7	-2.5	-3.5	-2.2
<b>BUILDING &amp; CONSTRUCTION</b>	-5.9	4.0	10.2	4.0	12.0	4.3	10.0	12.1	13.0	13.1	13.1
<b>WHOLESALE AND RETAIL TRADE</b>	2.7	1.9	9.8	1.6	2.5	6.5	9.7	13.5	15.3	15.3	14.0
<b>SERVICES</b>	4.3	3.6	9.9	3.8	4.6	24.8	8.8	8.0	9.2	9.8	10.5
<b>TOTAL GDP</b>	3.2	2.1	5.7	<b>5.4</b>	<b>4.6</b>	<b>3.5</b>	<b>6.6</b>	<b>6.5</b>	<b>6.0</b>	<b>6.2</b>	<b>6.4</b>
<b>NON-OIL GDP</b>	2.8	2.9	7.5	<b>2.9</b>	<b>4.3</b>	<b>8.0</b>	<b>7.8</b>	<b>8.6</b>	<b>9.4</b>	<b>9.6</b>	<b>9.1</b>
<b>OIL</b>	4.2	0.8	<b>-0.1</b>	<b>11.1</b>	<b>5.2</b>	<b>-5.7</b>	<b>3.3</b>	<b>0.5</b>	<b>-4.5</b>	<b>-5.9</b>	<b>-8.8</b>

*Source:* Underlying Data obtained from CBN Statistical Bulletin, 2008.

USAID (2008) observed that the World Bank’s composite Doing Business indicators for 2007 ranked Nigeria at an unsatisfactory 108 of 175 world economies. While this compares favourably to the low-income (LI) median rank of 147 and Indonesia’s 123, it is far behind Kenya’s 72. Kenya was labeled a “top 10 reformer” in 2007. Major weaknesses in the business environment of Nigeria are in the areas of lack of reliable physical infrastructure<sup>2</sup>. While Nigeria’s infrastructure is comparable to or better than regional standards, the private sector still finds it unsatisfactory by international standards. For example, the 2007 World Economic Forum’s annual index of infrastructure quality scored Nigeria 2.3, on a 0 to 7 scale, worse than Kenya (2.7), Indonesia (2.6), and the LI-SSA median (2.4). Despite weaknesses in the Nigerian business environment, investors’ interest is increasing because of the country’s strong growth, moderate inflation, declining external debt, high international reserves, and expectations of continued strength in the naira.

Recently, a number of structures have been put in place through the regulatory framework meant to encourage the inflow of FDI to Nigeria. Particularly, Nigeria’s investment regime offers a plethora of incentives, including tax holidays, reduced taxes, capital allowances, capitalization of expenditure, accelerated depreciation, import duty rebates, investment tax credits, repatriation of profits, and transferability of funds. Some of these incentives can be negotiated on a case-by-case basis with both Federal and State authorities (see Table 2). In addition, further investment opportunities are being created

<sup>2</sup> Institutional barriers to doing business as well as perceived corruption in government are also critical determinants of private sector development and prospects for sustainable growth. Over the past four years, the Government of Nigeria has been engaged in comprehensive investment climate reform at the Federal and State levels.



through the current privatization programme. Government created more incentives for the gas sector under the pioneer industries incentives program. These incentives range from tax holidays for oilfield development to allowances for capital investments and tax deductible interest on loans.

**Table 2: Investment Incentives in Nigeria**

Sector	Description
All sectors	<p>Tax-related:            (i) 30% companies income tax in all sectors, except petroleum; (ii) five-year tax holiday on companies investing in pioneer industries; (iii) tax relief on up to 140% of expenses on research and development; (iv) 2% tax concessions for a period of five years for industrial establishments that set up in-plant training; (iv) 20% of the costs of providing infrastructure that should normally have been borne by government (e.g. electricity) are tax deductible; (iv) tax holidays of up to seven years on investments in economically disadvantaged areas; (v) tax concessions on companies with high labour capital ratio; (vi) 10% tax concession for five-years on local value-added; (vii) tax credit of 20% for five years to industries that attain a certain minimum level of local raw material sourcing and utilization; capital allowances range from 5% to 30% depending on expenditure.</p> <p>Others            (i) unconditional transferability of funds through an authorized dealer in freely convertible currency; (ii) no enterprise shall be nationalized or expropriated by any government of the federation, unless the acquisition is in the national interest or for public purpose, in which case there are legal procedures to follow; (iii) any company incorporated in Nigeria is allowed to have access to land rights for the purpose of its activity in any state in the country.</p>
Industrial sector	<p>(i) companies investing in economically disadvantaged areas, benefit from a 100% tax holiday for seven years and an additional 5% depreciation over and above the initial capital depreciation; (ii) for a five-year period companies also benefit from tax concessions of up to 30% if involved in local raw material development, 10% if involved in local value added, 15% if involved in labour-intensive processing, 10 % if involved in export-oriented activities, 2% if involved in-plant training; (iii) companies with turnover of less than N1 million are taxed at a low rate of 20% for the first five years of operation if they are into manufacturing; (iv) up to 120% of expenses on research and development are tax deductible; (v) up to 20% of the cost of providing infrastructure such as roads, water, electricity, where they do not exist is tax deductible; (vi) all excise duties have been abolished (since 1 January 1999); (vii) 25% import duty rebate; (viii) tax allowance in respect of qualifying capital expenditure incurred within five years from the date of the approval of the project; (ix) dividends of companies in the manufacturing sector with turnover of less than ₦ 100 million are tax-free for the first five years of their operation.</p>
Energy	<p>All investments in this area are considered to be pioneer, hence benefit from a five to seven year tax holiday.</p>
Oil and gas	<p>(i) tax rate under the Petroleum Profit Tax (PPT) Act to be at the same rate as company tax, currently at 30%; (ii) capital allowance at the rate of 20% per annum in the first four years, 19% in the fifth year and the remaining 1% in the books; (iii) investment tax credit at the current rate of 5%; (iv) tax holiday under pioneer status; (v) capital allowances; (vi) repatriation of profits; (vi) no foreign exchange regulation; (vii) dividend derived from manufacturing companies in petro-chemical and liquefied natural gas subsector are exempt from tax.</p>
Agriculture	<p>(i) companies in the agro-allied business do not have their capital allowance restricted to 60% but graduated in full – 100%; (ii) agro-allied plant and equipment enjoy enhanced capital allowances of up to 50%.</p>

<b>Sector</b>	<b>Description</b>
Solid minerals	(i) three to five-year tax holiday; (ii) possible capitalization of expenditure on exploration and surveys; (iii) provision of 100% foreign ownership of mining companies or concerns; (iv) capital allowance.
Tourism	(i) tax holidays; (ii) longer moratorium and import duty exemption on tourism-related equipment; (ii) tax exemption on 25% of incomes derived from tourists by hotels.
Telecommunications	Rebate and tax relief.
Exporting	(i) company profits in respect of goods exported are exempt from tax under certain conditions; (ii) profits of companies whose supplies are exclusively input to the manufacturing of products for export are excluded from tax; (iii) export processing zone companies are allowed full tax holidays for three consecutive years; (v) investment tax credits; (vi) retention of export proceeds in a foreign currency in a domiciliary account with a Nigerian bank; (vi) export development fund to cover expenses on export promotion activities; (vii) export adjustment fund to compensate exporters for high cost of local production, arising mainly from infrastructural deficiencies; (viii) unrestricted remittance of profits and dividends; and (ix) zero-rated VAT.

*Source: WTO Trade Policy Review of Nigeria, 2005.*

Although the corporate income tax rate in Nigeria is 35 percent, a 20 percent income tax rate applies to agricultural, mining, and manufacturing companies with a turnover less than N1 million for the first five years of operations. New manufacturing companies that derive most of their revenues from export and mining enterprises may be eligible for exemption from income tax for the first three years of operations if they operate. Petroleum companies are also eligible for a three-year tax holiday and significant incentives for the following years. A 10 percent tax is imposed on capital gains. Dividends and interest are both subject to a 10 percent withholding tax. As a concession to its partners, a lower tax rate of 7.5% is applied on dividends, interests, rents and royalties going to countries with which Nigeria has Double Taxation Agreements. Nigeria has also signed investment promotion and protection agreements (IPPAs) with some countries.

The establishment of a Nigerian Export Processing Zone Authority (NEPZA) in 1992 was an additional effort to attract foreign investment. Other measures to promote investment include deregulation of the foreign exchange market and financial sector reform. An Independent Corrupt Practices and Related Practices Commission, and an Economic and Financial Crimes Commission (EFCC) were established to curb the level of corruption, and protect national and foreign investments in Nigeria. Moreover, macroeconomic reforms are being pursued and steps are being taken to improve poor infrastructural facilities (e.g. power, telecommunications, water, roads).

## **2:1:2 Bilateral Investment Treaties (BITs) Between China and Nigeria**

Bilateral investment treaties (BITs) are important instruments for promoting free and massive flow of foreign investment between countries. BITs constitute a universe of regulatory structure designed to stipulate terms of relationship between host countries and the foreign investors in conformity with specific international standard norms. The minimum standard envisaged and expressed in International investment treaties stipulates that a host country should ensure ‘fair and equitable treatment, alongside with other relevant standards, as part of protection due to foreign investment by host countries.

In practice, BITs are meant to cover the specific areas of definition of investment, scope of application, investment promotion and protection, and dispute settlement procedures. In the context of the principles of most-favoured-nation (MFN) and national treatment, parties are to ensure that investment and returns of nationals or firms are not treated in ‘less favourable’ way than investment of a third country. In cases where special incentives to promote the creation of local industries are to be granted, these should not harm the investment of the other party to the agreement. Further, the provision on expropriation (though prohibited) and losses emanating from unforeseen events such as wars require parties to pay compensation, restitution, indemnification or other settlements based on national treatment and MFN principles.

### **Box 1: Bilateral agreements between Nigeria and China**

Since May 1999 after Nigeria returned to constitutional democracy, former President Olusegun Obasanjo visited China twice, in 2001 and 2005 with his Chinese counterpart reciprocating both visits. Many high level visits have taken place between ministers and top officials of both nations.

These visits have yielded lots of benefits to both nations, including the following:

- During President Obasanjo’s 2001 visit, both leaders signed Agreements on Trade, Investment Promotion and Protection. Supporting agreements on sincere friendship, mutual trust, mutual economic benefit and common development, and enhanced consultation and mutual support were also signed.
- In April 2002, the two governments signed the “Agreement between the Government of the People's Republic of China and the Government of the Federal Republic of Nigeria for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income”.
- In July of the same year, they signed the Agreement on Consular Affairs, the Agreement on Cooperation on Strengthening Management of Narcotic Drugs, Psychotropic Substances and Diversion of Precursor Chemical, and the Agreement on Tourism Cooperation.
- Both nations agreed to establish a strategic partnership featuring mutual political trust, mutual economic benefit and mutual support in international affairs in 2005.
- Nigeria and People’s Republic of China on 13 October 2005 signed a contract agreement for the construction of water schemes for 19 states and the Federal Capital Territory (FCT) at the cost of N695 million.
- During President Hu Jintao’s visit to Nigeria in April 2006, Nigeria and China signed four Agreements and three Memoranda of understanding (MOUs) on a range of programmes to enhance their economic ties, including:  
**I.** The financing agreement of N8.36 billion (\$500 million) concessionary export grants to support the development of infrastructure by China Export Import Bank.

- II. The provision of about N670 million (40 million Chinese Yuan) for the training of 50 Nigerian officials and medical personnel on comprehensive malaria prevention and control.
  - III. The supply of anti-malaria drugs worth N83.6 million (5 million Chinese Yuan) in support of the Roll-Back-Malaria programme.
  - IV. An agreement centred to set up a team of experts for the Nigeria-China friendship cultural project.
  - V. A memorandum of understanding on the provision of National Information Communication Technology Infrastructure Backbone between the Federal Ministry of Science and Technology and Huawei Technologies.
- Source: Nigeria-China relations in Perspective: 1999 – 2006. <http://www.nigeriafirst.org/cgi-bin/artman/exec/view.cgi?archive=1&num=5899&printer=1> (Accessed August 23<sup>rd</sup>, 2009).

China had signed 115 bilateral investment protection agreements and 86 agreements on avoidance of double taxation by the end July 2005. In addition, China's CEPAs signed with Hong Kong, China, and Macao, China provides certain privileges to investors from these special administrative regions. As at 2005, China had concluded BITs with 25 African countries including Nigeria, while it had also reached economic and technical cooperation agreements with 38 of them. Under the Chinese legal system such international treaties supersede domestic laws.

Nigeria is not that prompted to sign as many BITs as China. However, it had signed about 30 bilateral investment treaties for the protection of investments and for the avoidance of double taxation with a number of developed and developing countries including China. Some of the specific agreements between Nigeria and China are summarized in Table 3 below.

**Table 3: Selected Investment related Agreements between Nigeria and China, 1997 to 2006**

Agreements	Year
Agreement on Investment Promotion and Protection	1997
Agreement on Investment Promotion and Protection	2001
Agreement for the avoidance of double Taxation and Prevention of Fiscal Evasion with respect to Tax and Income	2002
Agreement on Tourist Cooperation	2002
Strategic Partnership Agreement	2005
A Memorandum of Understanding on Investment Cooperation between the Federal Ministry of Commerce of Nigeria and Ministry of Commerce of India	2006
Economic Cooperation Agreement between Nigeria and Xinguang International Group of China	2006

Source: Authors' compilation

The visit of a former premier of the China State Council Li Ping to Nigeria in 1997 engendered the signing of a number of protocols on investment promotion and protection and enhanced cooperation in the electric, steel and iron industries. The numerous visits of the former President Olusegun Obasanjo and the reciprocal visits of China's president and government officials and representatives led to signing of some protocols. The BITs concluded by Nigeria with China are characterized by the following:

- A broad asset-based definition of investment covering movable and immovable properties, real estate, corporate shares and stocks, copyright, intellectual property rights and royalties;
- Coverage of investment in accordance to domestic laws and regulations;
- Fair and equitable treatment and most-favoured nation (MFN) treatment for foreign investors;
- Protection of investors against expropriation and nationalization;
- Guarantee free transfer of funds related to investment; and
- Settlement mechanism for state-state dispute.

In particular, the Article 1 of the Memorandum of Understanding (MOU) on investment cooperation between the Ministry of Commerce of the Federal Republic of Nigeria and the Ministry of Commerce of the People's Republic of China states that it is an attempt to enhance and expand bilateral cooperation in the spirit of reciprocity, mutual benefit and common development. With this MOU, the two countries shall encourage enterprises to cooperate and invest in the areas of textiles, clothing, home appliances, telecommunication equipment, agricultural machinery, processing of agricultural products and development of natural resources. Indeed, these areas of cooperation are real investment in which if actualized can generate mutual benefits to the two countries in terms of employment, output, revenue and human capital development.

In order to actualize this kind of MOU, Nigeria's government has to provide enabling environment particularly infrastructure to induce Chinese firms and investors to come to Nigeria. The high levels of corruption and insecurity have to be checked. Employment effects of these efforts can be internalized when the attitudes of Nigerians to work changed because Chinese are known to have a good attitude to work. However, given that some Chinese firms have been noticed to treat workers badly, Nigerian government has to plead with them to treat its citizens in not less than ways they are been treated by employers in their country. Chinese firms should be able to train Nigerians employed by them to be able to cope with tasks assign to them.

## **2:2 Policy Environment**

### **2:2:1 Overview of Nigeria's Investment Policy**

Prior to 1995, Nigeria placed considerable restrictions on FDI. However, in 1995, Nigeria adopted one of the most liberal regimes in Africa for the entry of foreign investors, virtually opening all its economy to FDI and reversing the severe restrictions on FDI imposed by the “indigenization” policy of the 1970s and 1980s. Initial steps to open the economy were taken in the late 1980s. For example, in 1988, the Industrial Coordination Committee (IDCC), the forerunner of today's Nigerian Investment Promotion Commission (NIPC), was established to coordinate the grant of all approvals (business permits, expatriate quotas and incentives) in respect of establishing new businesses with foreign interests. The major amendment was introduced in 1989. Many sectors were partially re-opened to FDI and foreigners were allowed to invest in a list of activities provided they complied with a total project investment of N20 million (\$2.7 million in 1989) and a citizens' ownership of at least 40 per cent. Finally, in 1995, the Nigerian Enterprises (Repeal) Act abolished restrictions on limits to foreign shareholding while the Nigerian Investment Promotion Commission Act established the NIPC as a successor to the IDCC, to become the agency in charge of promoting and facilitating foreign investment in Nigeria.

The NIPC Act is Nigeria's investment law and governs the entry of FDI. It allows for 100 per cent foreign ownership of firms in all but the petroleum sector, where investment is limited to the existing joint ventures or new production-sharing agreements, and in a short negative list<sup>3</sup>. The Corporate Affairs Commission (CAC) is charged with the sole responsibility of incorporating companies (both local and foreign) before such companies get registered with the NIPC. It is on record that the CAC to date has been providing clients with an excellent way of incorporating companies. Beyond the level of companies' incorporation, all investments with foreign participation are required to be registered with the NIPC to be covered by the treatment and protection clauses of the act (sections 17 and 27).

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<sup>3</sup> The short negative list refers to investment in industries considered crucial to national security, which are precluded to both Nigerian and foreign investors. These include the production of: Arms and ammunition; Narcotic drugs and psychotropic substances; and Military, paramilitary disciplined services uniforms. The Federal Executive Council may, from time to time, determine what other items enter the negative list. No changes to the list have, however, been adopted since its introduction in 1995.

In practice, the NIPC has attempted limiting the registration to companies investing a minimum share capital of N10 million (about \$80,000). However, registration with NIPC is not necessary for companies establishing in the Export Processing Zones (EPZs), or obtaining the “Export Processing Factory” status. Investment approval and licensing of such companies are carried out by the Nigerian Export Processing Zones Authority. Sequel to the introduction of the National Economic Empowerment and Development Strategy (NEEDS), the NIPC has been transformed into a promoter, facilitator and advocate of FDI. To this effect, in March 2006, a One-Stop-Shop Investment Centre (OSIC) was established within the NIPC premises (See Box 2. The NIPC reports that, since the introduction of the OSIC, the steps necessary to obtain a Business Permit have been reduced from nine to three and that business permits are issued fairly automatically in 10 minutes (See Box 3). The legislation of the two major laws in 1995 (the Nigerian Investment Promotion Commission-NIPC Act 16 and the Foreign Exchange (Monitoring and Miscellaneous Provision) Act 17) altered significantly the status-quo in the Nigerian FDI environment (See Box 4).

#### **Box 2: Nigeria’s One-Stop-Shop Investment Centre is Created**

A One-Stop-Shop Investment Centre (OSIC) has been operational in Nigeria since March 2006. It is housed within the premises of NIPC in Abuja and a site for the forthcoming Lagos branch has been acquired. OSIC was opened with the stated objective of addressing “problems related to the multiplicity of agencies involved in various aspects of investment facilitation in Nigeria and the resultant inter-agency rivalry, complicated by conflicting statutory laws/legal frameworks; arbitrary use of discretion in granting approvals; limited transparency; bureaucratization in procedures; and poor service orientation” (NIPC, 2006). Since inception, OSIC has registered more than 2,500 companies.

While the ultimate goal is to get the agencies involved in the OSIC to work in harmony to reengineer and streamline their processes, procedures and requirements for granting business entry permits, licences and approvals, it was decided to adopt a “Coordinated One-Stop Approval Framework for the One-Stop-Shop (OSS) of Nigeria. This model implies that the various agencies/authorities maintain their existing mandates and responsibilities within the structure of the OSIC. In this regard, the following agencies have opened desks in the Centre:

- The Nigerian Investment Promotion Commission (NIPC);
- The Corporate Affairs Commission (CAC);
- The Central Bank of Nigeria (CBN);
- The Ministry of Federal Capital Territory;
- The Ministry of Solid Minerals Development;
- The Federal Ministry of Finance;
- The National Bureau of Statistics;
- The Nigeria Immigration Service (NIS);
- The Nigeria Customs Service (NCS);
- The Federal Inland Revenue Service (FIRS);
- The National Office for Technology Acquisition and Promotion (NOTAP);
- The Standards Organization of Nigeria (SON);
- The National Agency for Food and Drug Administration and Control (NAFDAC);
- The Nigeria Maritime Administration and Safety Agency;
- The Northern Nigeria Development Corporation; and
- The O’dua Investment Corporation Limited.

OSIC is currently envisaging an e-payment solution to facilitate payment of fees charged by the various agencies. To this end, all agencies involved need to conform to the agreed service standards as shall be enunciated in the forthcoming Client Charter. UNCTAD, invited to comment on the OSIC initiative on the occasion of the Presidential Retreat of 20 March 2006, recommended that the creation of the OSIC did not obviate the need to streamline business regulation, nor bring a better service culture within key regulatory agencies. UNCTAD's recommendations, geared towards achieving a "Team Nigeria" approach, include:

- (a) The NIPC should negotiate protocols of cooperation with the agencies participating in OSIC. These should spell out the extent of empowerment of OSIC-located officers, NIPC oversight arrangements, the quality and number of staff assigned and service delivery expectations;
- (b) OSIC should function in large part as a "virtual" OSIC, taking advantage of the opportunities opened by Internet technology. Online applications and inter-agency exchange would not only lead to faster information flow, better monitoring and accurate and timely reporting, but also extend the OSIC services to all areas of the country with Internet access. This has now been adopted as an official objective with proposed full implementation in three years.
- (c) Use of OSIC services should not be mandatory. Investors should be able to apply directly to the regulatory agency if they choose. It is up to OSIC to perform. This is now official policy and the authorities are now determined to make OSIC an irresistible choice for investors.

Wherever feasible, regulatory officers sitting in OSIC should be "empowered" to approvals as distinct from channelling applications back to their headquarters.

*Source:* UNCTAD, based on information from the NIPC.

### **Box 3: Procedure to Obtain Work and Residence Permits in Nigeria- The BP/EQ Scheme**

1. The foreign investor requests a Business Permit (BP) and applies for the right to hire expatriates for designated positions, the Expatriate Quota (EQ). This is done either through the NIPC, by means of Form 1 mentioned earlier or directly at the Ministry of Internal Affairs, through the corresponding Form T1.58 Most applications are made directly. Each expatriate position requires the employment of two Nigerian understudies who must be trained to take over within three years.
2. It appears that, where the investor was already granted an EQ, the consulates can grant the entry visa before the employment permit requests are completely processed, Thus character, credentials and health checks are administered by the missions abroad (mission interviews and Investor's Roadmap). Hiring against an EQ requires an application to the Comptroller General of Immigration for a Subject to Regularization Visa (STR). STRs are collected at the consulate nearest the entering expatriate's place of residence.<sup>59</sup> Among other forms, the application must be accompanied by the letter of invitation accepting "immigration responsibility".
3. Statutory responsibility for issuing EQs rests with the Ministry of Internal Affairs (the parent ministry of the Nigerian Immigration Service), which decides on a discretionary number of expatriates (EQ positions) per company that can enter Nigeria.
4. Once in Nigeria, expatriates apply for regularization of their STR visas to obtain a "Combined Expatriate Residence Permit and Alien Card" (CERPAC), i.e. a one-year residence and work permit (the validity is two years according to the guidelines issued by the Nigerian Immigration Service, but it appears that, in practice, most CERPAC are issued for a one-year period).
5. An alternative to CERPAC is the "Permanent Until Reviewed" (PUR) Status. PURs are available only for sole owners/CEOs of a foreign invested enterprise and are subject to the employment of Nigerian Deputy CEO and payment of a \$10,000 fee. The company needs also to show proof of an appreciable net profit of which not less than N2 million (\$15,500) has been paid as corporate tax. Other factors considered are the "political/policy direction of Government; the company's area of business; evidence that the PUR would guarantee technology transfer and that the company has a large quota portfolio and corresponding share holdings as an added qualification".



Exceptions to the above EQ approval procedure apply to ECOWAS nationals, who do not need an EQ or residence permit and are required only to register with the authorities for record-keeping purposes. Also, Free Zones are not subject to the EQ process because they are deemed to be extraterritorial. However, the STR, then residence permit is, strictly speaking, only for sojourn in a zone. Foreigners with this status need a pass to travel to the “hinterland”, but according to the Nigeria Immigration Service, these are readily issued by its officers stationed in the zones.

*Sources:* UNCTAD and Nigeria Immigration Service.

#### **Box 4: FDI Policies in Nigeria before and after 1995**

The indigenization policy started in 1972 with “the Nigerian Enterprises Promotion Decree” (NEPD). The decree imposed several restrictions on FDI entry. As a result, some 22 business activities were exclusively reserved for Nigerians, including advertising, gaming, electronics manufacturing, basic manufacturing, road transport, bus and taxi services, the media and retailing and personal services. Foreign investment was permitted up to 60 per cent ownership and provided that the proposed enterprise had, based on 1972 data, share capital of N200,000 (\$300,000) or turnover of N500,000 (\$760,000). The second indigenization decree, the Nigerian Enterprises Promotion Decree of 1977, tightened restrictions on FDI entry in three ways: (a) by expanding the list of activities exclusively reserved to Nigerian investors (e.g. bus services, travel agencies, the wholesaling of home products, film distribution, newspapers, radio and television and hairdressing); (b) by lowering permitted foreign participation in the FDI-restricted activities from 60 to 40 per cent and adding new activities restricted to 40 per cent foreign ownership such as fish-trawling and processing, plastic and chemicals manufacturing, banking and insurance; and (c) by creating a second list of activities whereby permitted foreign investment was reduced from 100 to 60 per cent ownership, including manufacturing of drugs, some metals, glass, hotels and oil services companies. Relaxation of these restrictions began in 1989. The NEPD was amended so as to leave a single group of 40 business activities in which foreign participation was completely prohibited unless the value of the enterprise exceeded N20 million (\$2.7 million in 1989). In addition, foreign investors could hold only a share of up to 40 per cent in insurance, banking, oil production and mining. Finally, in 1995, the Nigerian Investment Promotion Commission Act opened all sectors to foreign participation except for a short negative list (including drugs and arms) and allowed for 100 per cent foreign ownership in all sectors, with the exception of the petroleum sector (where FDI is limited to joint ventures or production sharing).

*Sources:* NIPC and UNCTAD.

### **2:2:2 Nigerian FDI Institutional Arrangement**

In Nigeria, foreign direct investment (FDI) is conceived as investment undertaken by an enterprise that is either wholly or partly foreign-owned. The Investment Code that created the Nigerian Investment Promotion Commission (Decree No. 16 of 16 January 1995) and the Foreign Exchange (Monitoring and Miscellaneous Provision) also enacted in 1995 gives full legal backing for FDI in the country. Nigerian government promotes FDI into the country. With the implementation of the IMF monitored-liberalization of the economy, foreign investors in the manufacturing sector are welcomed. Also, incentives for ownership of equity in all industries, except for petroleum and key industries such as military equipment, creation

of some Export Processing Zones and participation in regional integration schemes are equally embarked upon.

As the overall focus of its development strategy, Nigeria pursues a private sector-driven economic growth and development. Thus, government provides the enabling environment for private investors (both domestic and foreign) to operate. A number of measures have been introduced to promote private investment in the country. In 1999, government repealed and amended 11 Decrees that inhibited competition or conferred monopoly power in public enterprises in the petroleum, telecommunications, power and mineral sectors. Thus, the main law governing investment in Nigerian Investment Promotion Commission (NIPC) Decree No.16 of 1995 liberalises the foreign investment regime. The NIPC was established under this law as a federal agency which succeeded the Industrial Development Co-ordination Committee (IDCC). The NIPC seeks to, among others:

- coordinate, monitor, encourage, and provide necessary assistance and guidance for the establishment and operation of enterprises in Nigeria;
- initiate and support measures that enhance the investment climate in Nigeria;
- promote investment in and outside Nigeria; and
- assist incoming and existing investors by providing support services.

The major responsibility of NIPC is to serve as a one-stop facilitating centre for the registration of companies, the acquisition of business permits, and expatriate quotas, and a host of incentives. Under the NIPC Decree, investors (both domestic and foreign) can participate in all sectors of the economy with the exception of the production of arms and ammunition, narcotic drugs, and psychotropic substances. Foreign companies are allowed to operate in Nigeria through a subsidiary that must be incorporated in Nigeria.<sup>4</sup> Under the Companies and Allied Matters Act of 1990 (as amended), the Corporate Affairs Commission is charged to regulate and supervise the formation, incorporation, and registration of companies in Nigeria. The legal authority in Nigeria for the management of technology is the National Office for Technology Acquisition and Promotion (NOTAP). It is charged with monitoring on a continual basis, transfer of foreign technology. NOTAP implements this

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<sup>4</sup> Exemptions to this requirement exist for: foreign companies invited to Nigeria by or with the approval of the Federal Executive Council to execute a specified individual project; foreign companies in Nigeria for the execution of a specific individual loan project on behalf of a donor country or international organization; foreign state-owned companies engaged solely in export promotion; and engineering consultants and technical experts engaged in any individual government-contracted (including from government agencies) project.

measure through registering contracts and agreements dealing with transfer of foreign technology. NOTAP ensures that a foreign investor issues:

- a license to use trademarks and patented inventions;
- supply of technical expertise in the form of preparation of plans, diagrams, operating manuals or any other form of technical assistance of any description whatsoever;
- supply of detailed engineering drawings;
- supply of machinery and plant and;
- provision of operating staff or managerial assistance and the training of Nigerian personnel.

Compliance with these measures ensures that foreign investors in technical, management and consultancy services can remit fees outside Nigeria.

Foreign direct investment (FDI) inflows increased from US\$1.0 billion in 1999 to US\$2.0 billion in 2003, making Nigeria the fourth largest recipient of FDI inflows amongst African countries. Most FDI inflows are to the oil and natural gas subsector. However, telecommunications services have also benefited due to the ongoing privatization and deregulation reforms.

### **2:2:3 *China's FDI Policy***

China's African policy document was launched in January 2006. This policy articulates the objectives of Chinese policy toward Africa and how they are to be realized. The broad objectives stated in the policy include, mutual benefits, common development, and win-win results in economic relations. The policy document highlights government actions to foster trade, investment, financial services, agriculture, infrastructure, resources development and tourism. The implementation of the policy is supported by financial and technical assistance in non-commercial areas such as health and education (Wang, 2007). During the Beijing Summit of the Forum on China-African cooperation in November 2006, China's President announced new commitment to Africa for 2007-2009. Among the items in the new commitment related to investment are:

- US \$5billion China-Africa Development Fund to support Chinese FDI in Africa including Nigeria;
- Preferential credits totalled US\$5 billion, consisting of US\$3 billion concessional loans and US\$2 billion export credits;
- Grants element in investment
- Technical assistance to upgrade the required skill for managing investment.

According to WTO trade policy review report, China was the largest developing country recipient of FDI and the third largest recipient of FDI in the world in 2004, after the United States and the United Kingdom. This shows China's commitment to providing a business environment conducive to FDI since 1978. Foreign investment has been encouraged mainly in manufacturing with a particular emphasis on high value-added production. One of the key features of the FDI regime is that China provides better than national treatment in its taxation policies for foreign-invested enterprises. For instance, while the enterprise income tax rate is 33 per cent foreign-invested enterprises may enjoy rates of 15 per cent or 24 per cent depending on where they invest coupled with tax holidays for varying lengths of time depending on their activities.

Another landmark in China's investment regime is the recent favourable policy toward encouraging outward FDI, basically to upgrade technical skills and to secure supplies of key raw materials, such as petroleum and iron ore. The Central Government and some provincial governments have been encouraging firms to invest abroad by relaxing approval procedures and providing financial support. For instance, on 27 October 2004, the Export-Import Bank of China (EIBC) issued a "Notice on Loan Support Policy for Key State-Encouraged Overseas Investment Projects" which specifies that preferential interest rates may be accorded overseas investment loans. A particular sector of interest to China is the petroleum sector in which it invests in countries such as Indonesia, Kazakhstan, Myanmar, Sudan, Yemen and Nigeria, as well as in aluminium, iron ore, and coke industries in Brazil. Acquisition of shares in foreign enterprises is becoming attractive to some Chinese enterprises.

In China, specific FDI related laws and regulations are the "Law on Chinese-Foreign Equity Joint-Ventures"; "Law on Chinese-Foreign Contractual Joint Ventures"; "Law on Foreign-Capital Enterprises"; and their implementing regulations. Under these laws, foreign-invested enterprises include equity joint ventures (with the proportion of foreign investment

no less than 25 per cent of registered capital), contractual joint ventures, and wholly foreign-owned enterprises (WFOEs). Since China's accession to the WTO, restrictions on foreign-invested enterprises have been relaxed. The revisions of the three laws in 2000 and 2001 reduced market access limitations and export balancing requirements, while technology transfer requirements were also relaxed.

In 2005, guidelines for encouraging and supporting the development of the non-public sector including individual and private enterprises were issued by the State Council. Thus, they were meant to improve market access by private companies to many industries that were previously restricted, including those dominated by state monopolies and heavily regulated sectors such as public utilities, financial services, social services, and supplies of national defence equipment. The guidelines also stipulate that foreign investors will have the same access as domestic investors in any sector where it is not explicitly forbidden by law. Revised provisions for guiding foreign investment direction were promulgated in 2002 and became effective. They classify foreign investment projects into four categories: encouraged; permitted; restricted; and prohibited. The most recently amended Catalogue for guiding foreign investment industries groups industries as been 'encouraged', "restricted" and "prohibited" while projects that do not fall into these three groups are termed as "permitted". The amendment includes: extending the list of industries in the encouraged category in accordance with the State's industrial policies; relaxing restrictions on market access in service industries; removing so-called "over-invested industries" from the encouraged category (certain steel processing, for example, was moved from the encouraged to permitted category). The authorities noted that a distinctive feature of the Catalogue was that "it expanded the degree of opening up and took encouraging foreign investment as a general policy". Projects in the "encouraged" category are those that utilise improved technology and are less polluting, while "restricted", and "prohibited" projects are those that use obsolete technologies, over-exploit scarce natural resources, and tend to endanger the environment. Foreign equity limits tend to depend on industry type and are not necessarily based on the category. Thus, "encouraged" industries may have foreign equity restrictions, while "restricted" industries may be wholly foreign owned.

Foreign investors in the "encouraged" category are permitted to import capital equipment duty free. In addition, they may enlarge their scope of business, with approval, if they are engaged in the construction and operation of infrastructure facilities related to energy, transportation, and urban utility sectors (coal, oil, natural gas, power, railways, ports,

airports, highways and urban roads, sewage treatment, and garbage disposal, etc.), which need a large amount of investment and a long payoff period. Furthermore, the threshold of projects in the "encouraged" category that may be approved by local governments has been raised. In addition, investors in the "permitted" categories that export all their products directly enjoy the same preferential treatment accorded to "encouraged" projects, as do projects listed in the Catalogue of Advantaged Industries for Foreign Investment in Central-Western China. Foreign investment in the "restricted" category may be regarded as "permitted", if export sales amount to over 70 per cent of the total sales of the product. Foreign enterprises in China enjoy a low-tax policy.

China grants preferential tax treatment for investment in industries and regions where investment is encouraged. As stated earlier, one of the most distinctive features of the tax system is the differential treatment of domestic and foreign enterprises with respect to the enterprise income tax. The standard enterprise income tax rate is 33 per cent. However, an enterprise income tax rate of 15 per cent applies to foreign enterprises located in the special economic zones (SEZs), or to foreign enterprises involved in manufacturing in the economic and technological development zones (ETDZs), while a rate of 24 per cent applies to those involved in manufacturing and located in the coastal economic open zones (CEOZs), or the old urban districts of cities where the SEZs or ETDZs are located. In cases where a foreign enterprise has subsidiaries in different locations, they may be taxed differently. In essence, it seems that such preferential tax treatment is not available to domestic enterprises except those established in the State high-tech development zones and in the western areas. Further, foreign enterprises engaged in manufacturing with an operating period exceeding ten years may enjoy an income tax exemption during the first two years after becoming profitable, followed by a 50 per cent reduction for the next three years.

Hi-tech foreign enterprises located in hi-tech industrial zones also enjoy the two-year income tax exemption, while those involved in manufacturing also enjoy the 50 per cent income tax reduction in the next three years. Export-oriented foreign enterprises benefit from the same two-year exemption and the 50 per cent reduction as long as export quantity per annum accounts for more than 70 per cent of the general sales of the enterprise. If a foreign-owned enterprise purchases domestically made equipment, which, if imported, would be entitled to tariff exemption, it is granted a VAT refund on such equipment. In addition, it would appear that FIEs together with domestic enterprises operating in designated manufacturing industries in the western and central regions of China enjoy a complete tax

holiday during the first two years after making profits and a 50% income tax reduction during the following six years. A foreign enterprise which directly reinvests after-tax profits; increases the registered capital or uses profits to establish another enterprise with an operational duration of not less than five years will enjoy a refund amounting to 40 per cent of the enterprise income tax paid on the sum reinvested. Further, dividends of foreign investors are exempted from income tax. The losses recorded by a foreign enterprise may be offset by the income earned in the next payment year and if such losses cannot be fully offset in the next year, they may be carried forward for a maximum of five years.

Relative to major origin countries of Foreign Direct investment (FDI), Chinese outward investment is highly regulated. Before a new strategy was articulated, China's ODI policy was driven chiefly by central government priorities. Thus, prior to 2002 when the leadership announced the new strategy to encourage enterprises to look outward by investing in overseas markets, Chinese ODI was generally discouraged by the central authorities. The ODI policy witnessed series of reforms through the 1980s and 1990s, although many of these changes were of a political or administrative nature. The impetus for deeper reform in ODI policy has only come about in the last few years, coinciding with China's increased presence on the global economic scene, and with the ability and desire of Chinese firms to spread their wings internationally. In general form, Chinese ODI policy can be categorised into five phases which are discussed below.

#### ***PHASE ONE (1979 – 1983): Case-by-Case Approval***

During this period only state-owned trading corporations and provincial or municipal-based international economic and technology cooperation enterprises were the entities allowed to invest overseas on a case-by-case basis. The sole authority responsible for examining and approving overseas investment was the State Council. Outward investment was in effect prohibited unless specifically approved by the State Council, and hence there were serious regulations on ODI.

#### ***PHASE TWO (1984 – 1992): Standardization of Approval Procedures***

During this period, prohibitions against ODI were liberalized as the government permitted a wider range of enterprises to invest overseas. For instance, non-state firms were permitted to set up subsidiaries in other countries. However, prior approval was still required

from the central authorities, but the approvals process moved gradually from a case-by case approach to more standardized procedures.

***PHASE THREE (1993 – 1998): Greater Scrutiny of Overseas Investment Projects***

A surge in outward investment in the previous period promoted by the relaxation of ODI rules and an overvalued exchange rate resulted into a number of debacles by Chinese firms speculating on the Hong Kong real estate and stock markets. Consequently, Beijing introduced a more rigorous process for screening and monitoring ODI projects to ensure that these investments were for “genuinely productive purposes”.

***PHASE FOUR (1999 – 2002): Overseas Investment in Processing Trade Activities***

China’s policy towards ODI witnessed a significant turnaround during the period spanning its entry into the World Trade Organization. In recognition of the increasingly crucial role of Chinese enterprises in global trade and production networks, Beijing introduced new policies to encourage firms to engage in overseas activities that augmented China’s export drive, otherwise known as “processing trade” projects. The light industrial goods sector including textiles, machinery and electrical equipment, was encouraged to establish manufacturing facilities overseas that would use Chinese raw materials or intermediate goods. The Chinese government offered a variety of incentives including export tax rebates, foreign exchange assistance, and direct financial support.

***PHASE FIVE (2002 – Present): The “Stepping Out” (Go Global) Strategy***

At the Chinese Communist Party’s Sixteenth Congress in 2002, the leadership announced a new strategy of encouraging Chinese companies to “Step Out” into the global economy not only through exports, but also by investing overseas. This policy reform was perceived to be a necessary complement to the successful implementation of the inward investment and export policies of the 1980s and 1990s, and as part of the ongoing reform and liberalization of the Chinese economy. It also reflects a commitment on the part of the Chinese government to create world class companies and brands, whereby Chinese firms are recognised as more than secondary nodes in production networks that are ultimately controlled by multinationals based in industrialized countries. Recent reforms in ODI policy have focused on the following five areas:



- creating incentives for outward investment;
- streamlining administrative procedures, including greater transparency of rules and decentralization of authority to local levels of government;
- easing capital controls;
- providing information and guidance on investment opportunities; and
- reducing investment risks.

The last 20 years testify to the dramatic change that has occurred in China's government's attitude towards outward investment. Since 1980, the emphasis on political objectives in determining Chinese ODI policy has gradually been replaced by the primacy of commercial interests. Further, the ODI approval process has been significantly simplified, with decision making authority delegated first from the central government to local governments, and more recently to the enterprise itself. The motivation for outward investment, in turn, has generally evolved from one that was based largely on accessing natural resources to a more complex set of objectives related to securing access to markets, technology, and brands, as well as the traditional interest in natural resources.

#### ***2:2:4 China's FDI Institutional Arrangements***

The institution that promotes foreign investment in China is the Ministry of Commerce (MOFCOM) through its Investment Promotion Agency (CIPA) and the International Investment Promotion Centre of China (IIPCC). Majority of the provinces render one-stop services to foreign investors, and each province sets up an investment promotion centre. China also promotes investment through the International Fair for Investment and Trade, Hi-Tech Fair, and Export Commodities Fair.

Institutions connote the regulatory structures, governmental agencies, laws, courts, and professions (Scott 1987). Hence, the institutional environment comprises the rules and requirements with which organizations must comply to gain the desired rewards of support and legitimacy (DiMaggio and Powell 1983). In China, Chen (2004) identified five types of FDI approved by the foreign direct investment policy in China as follows:

- Equity joint ventures
- Contractual joint ventures,
- Foreign-funded enterprises,
- Share-holding enterprises, and

- Cooperating development.

The typical institutions that foreign investors in China have to cope with are Chinese culture, governmental system and NGOs<sup>5</sup>. Initially, Chinese governments show the following characteristics as far as business is concerned:

- i) Extensive government intervention in economic affairs. Indeed, in the 1990s, to get government approval, a typical major construction project experienced checks by 7 ministries, 8 examining and approval bureaux, and had 58 red stamps and 169 officials' signatures, and this process lasted two years.
- ii) China is a country with a decentralized government structure. National laws are often only broadly drafted at the central level and their implementation is left to the discretion of regional and local administrations (Holtbrugge and Berg 2004). The decentralized government structure gives provincial and local governments the freedom to intervene in economic activities. 'In this context any prominent administrator is in a position to give a go-ahead to an exception and can find out a suitable reason for it, such as to relieve rural poverty, to reduce losses incurred by a state-owned firm, or to defuse disturbances among a group of employees' (Blackman 2000).
- iii) Phenomenon of conflicts among different administrators. Conflict among different levels of authority arises for the following reasons: (a) inconsistent interpretations of laws and regulations, (b) different political priorities of economic issues, and (c) various stakes acquired from MNEs (Chen 2004). In addition, the division of jurisdiction among different ministries is not very clear in China.

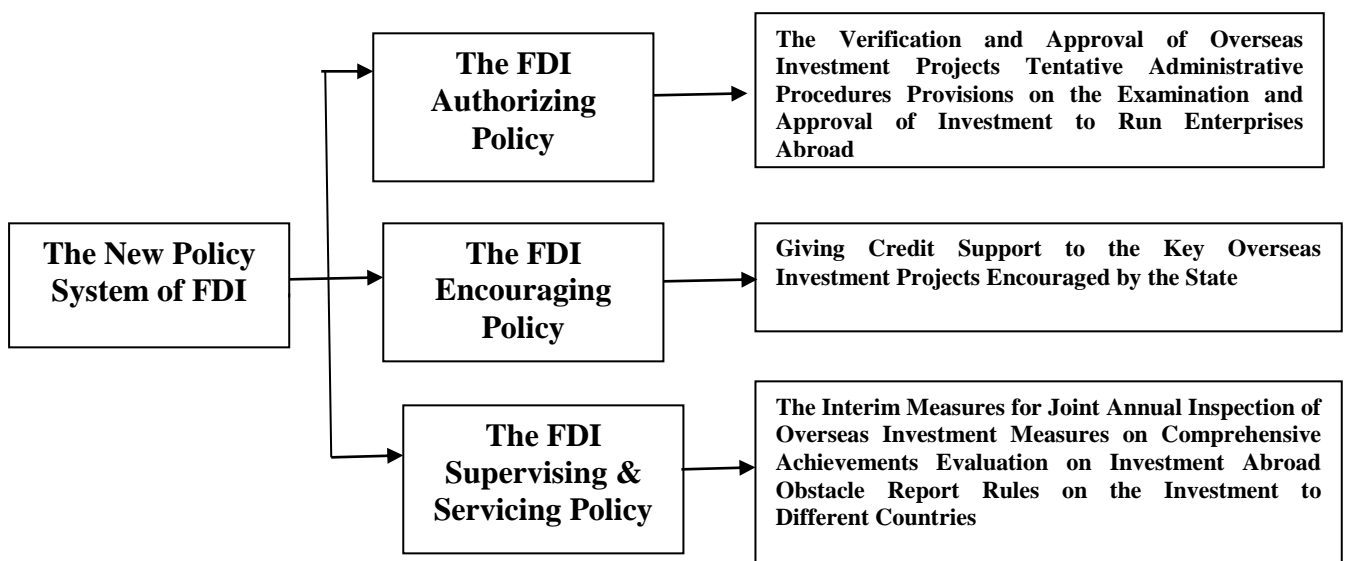
The situation captured by the aforementioned characterization prevailed prior to October 2000 when the Chinese government put forward the "Go Global" strategy. By October 2004, the new framework of Chinese new policy system of FDI has emerged. The Verification and Approval of Overseas Investment Projects Tentative Administrative Procedures was enacted by the National Development and Reform Commission. It is the replacement of The Regulations on Examination and Approval of Project Proposal and

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<sup>5</sup> For detailed discussions of the characteristics of these three institutions, See Yongqiang Gao

Feasibility Report on FDI Projects issued in 1991. The document makes it clear that the government plays mainly as guider, service provider and supporter of FDI. Hence, the Chinese enterprises are to make their own decisions of FDI, while the Ministry of Commerce (the former Ministry of Foreign Trade and Economic Cooperation) now issues Provisions on the Examination and Approval of Investment to Run Enterprises Abroad and replaced the former regulations. In clear terms, measures to promote Chinese FDI are indicated in the *Giving Credit Support to the Key Overseas Investment Projects Encouraged by the State* issued by the National Development and Reform Commission and the Export-import Bank of China in October of 2004. These two institutions jointly established the supporting mechanism of foreign investment credit. In the plan, certain volume of credit capital will be earmarked for key foreign investment projects to be encouraged by the government, thereby qualifying to enjoy lower interest rate of export credit. Apart from the *Interim Measures for Joint Annual Inspection of Overseas Investment and Measures on Comprehensive Achievements Evaluation on Investment Abroad* issued by the Ministry of Foreign Trade and Economic Cooperation in October of 2002, the Ministry of Commerce issued the *Obstacle Report Rules on the Investment to Different Countries* in October of 2004. These three documents jointly normalized the Chinese government’s supervision and service for overseas investment (See Figure 1)

**Figure 1: Current policy system of Chinese FDI**



**Source:** Cheng Li-ru & Zhou Xuan (2007).

The overriding features of the Chinese new FDI policy system are summarized by Chengu and Zhou (2007) as follows:

***From examining and approving to verifying and approving***

In the area of examination of foreign investment projects, as against the situation with *The Regulations on examination and Approval of Project Proposal and Feasibility Report on FDI Projects*, *The Verification and Approval of Overseas Investment Projects Tentative Administrative Procedures* has a number of strengths. Firstly, the process of examining and approving becomes much more succinct. According to the new regulations, the long used double-deck approving procedure has been abandoned, and the enterprises' reports of feasibility are not required any more, the government will no longer pay too much attention to the economic and technical feasibility, and shift its focus to the inspection of the projects' compliance with the regulations. Secondly, the authorization of examination and approval has been empowered to lower levels. According to the new policies, the national authorities will be only responsible for the resource exploiting projects exceeding 30 million US dollars and the projects exceeding 10 million US dollars, respectively increasing 30 times and 10 times compared with the old limitations. Besides, the state-owned enterprises get more freedom to invest overseas. In addition, the reply time limits have been curtailed to 20 work days from 60 work days. In order to avoid the delaying on some step of official replies, *Provisions on the Examination and Approval of Investment to Run Enterprises Abroad* has even strictly stipulated the time limits for each step in Statute No.9, No.10, No.11 and No.13. Objectively, it can be said that the new administrative measures issued in 2004 are much more rigorous.

***From negative to positive: the shift of government's attitude***

The new policy system introduced an important change is the government's basic attitude to Chinese FDI. The Chinese government gradually encourages overseas investment rather than restricting FDI. It was pointed out in the *Opinions of Enhancing the Administration of Overseas Investment in 1991* that overseas investment should be undertaken under the national macroscopic management. But in the new regulations, establishing overseas branches or subsidiaries by Chinese enterprises with comparative advantages in any form of ownerships is encouraged and supported by the government. Indeed, other related departments have promulgated policies to cooperate. *The Notice of*

*Giving Credit Support to the Key Overseas Investment Projects Encouraged by the State* promulgated by the National Development and Reform Commission and the Export-Import Bank of China became an instrument of providing considerable financial support for four kinds of FDI encouraged by state. The State Administration of Foreign Exchange has simplified the procedures of foreign exchange management investment and abolished the restriction of the amount of foreign exchange in respect with overseas investment in order to satisfy the Chinese enterprises' foreign exchange needs. Government has began to realize the importance of its service role in FDI and enacted the *Industrial Oriented Index of Overseas Investment in Different Countries*, the *Statistic Gazette of Chinese Foreign Direct Investment in 2003 and Reporting System of the Obstacle Report Rules on the Investment to Different Countries* successively in 2004, which gives directive guidance to enterprises' overseas investment.

#### ***More strict supervision for the enterprises' overseas investment***

In the context of the former policy system, the initial examining and approving process of enterprises' overseas investment was very strict, but when the process finished, government's supervision on overseas enterprises' subsequent operating was not effective enough. The new policy system tries to solve this problem. Together with the examining and approving procedures, a series of laws and regulations were enacted to strengthen the following supervision over the daily operation of overseas enterprises. *The Interim Measures for Joint Annual Inspection of Overseas Investment and Measures on Comprehensive Achievements Evaluation on Investment Abroad* was enacted successively to constitute the detailed rules on the operations of overseas enterprises. Undoubtedly, these measures in the new policy system have greatly and positively influenced the macro supervision and accelerated the healthy development of Chinese overseas investment.

In sum, China appears to have provided sufficient incentives to attract foreign investment and this is the rationale behind the massive inflows of such investment into the country. The combined effect of both the policy and institutional environment can be appreciated by the volume of outflow and inflow of FDI in China as presented in Table 4 below since 1980.

**Table 4: China FDI Inflows**

Year	Inflow		Outflow	
	Flow	Stock	Flow	Stock
1980-1989	1,618.7	6,696.6	453.125 <sup>6</sup>	1395.875
1990-99	29,042.7	96,404.9	2322.761	16075.24
2000	40,714.8	193,348.0	915.8	27,768.4
2001	46,877.6	203,142.0	6,885.4	34,653.8
2002	52,742.9	216,503.0	2,518.4	37,172.2
2003	53,504.7	228,371.0	2,854.7	33,222.2
2004	60,630.0	245,467.0	5,498.0	44,777.3
2005	72,406.0	272,094.0	12,261.2	57,205.6
2006	72,715.0	292,559.0	21,160.0	73,330.0
2007	83,521.0	327,087.0	22,468.9	95,798.9

Source: UNCTAD World Investment Directory, 2008.

## 3.0 Literature Review

### 3:1 Theoretical Review

The theory of factor mobility has been analysed in an analogous way as the theory of trade using the concept of inter-temporal comparative advantage in production and trade. Standard trade literature proves that the basis of cross border factor mobility is the differences in factor endowment, propensity to consume and preference between present and future consumption between or among nations. It is argued that a labour abundant economy may witness unemployment of labour and low real wage which may lead to labour mobility since real wage may be low compared to what obtains elsewhere. It is also argued that a country that possesses a comparative advantage in future production of consumption goods is one that without international lending and borrowing would have a relatively low price of future consumption (a high real interest rate). This high real interest rate corresponds to a high return on investment. This means that a high real interest rate in the borrowing nation influences the lending nation to divert resources from current production or consumption to lending in order to enhance their economies future ability to produce or consume. Therefore, resources endowment, market size, real interest rate and wage rate are major factors determining international capital and labour mobility respectively.

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<sup>6</sup> The average figure covers the period 1982-1989.

An important part of capital mobility that has received more attention in research takes the form of foreign direct investment (FDI). It is seen as foreign capital flows in which a firm in one country establishes a subsidiary in another. FDI is characterized by transfer of resources and acquisition of control. Multinational enterprises have been seen as a vehicle for international capital mobility. The modern theory of multinational enterprise focuses on the analysis of two important issues. The first is the reason why a commodity is produced in two (or more) different countries rather than one. This is the issue of *location*. The second is the reason why production in different locations is carried out by the same firm rather than by separate firms. This is the issue of *internalization* (Dunning, 1999; Krugman and Obstfeld, 2000 and Appleyard and Field, 2004).

The location (of production and trade) is determined by resources, transport cost and other barriers to trade. There are two views about the benefits of internalization. The first view of the benefit of internalization is that it leads to transfer of technology from one country to another. The second view is that it enhances vertical integration. The theories of location, agglomeration and internalization have been well treated in economic geography and physics (Newtonian physics notion) in the context of gravity model. This gravity model was first applied in the early 1960s (by Tinbergen and Polyhonen in their respective studies) to analyse trade relations in form of examining the trade creation and diversion effects of bilateral and regional co-operations. Since then the model has found applications in some areas of empirical economic analysis including analysis of impact of FDI. The basic gravity model demonstrates that trade between two countries depends upon the distance between them, population size and their level of income or output. There have been various extensions of the model to capture other factors such as common border between the two countries and cultural similarities. In short, the model predicts that trade flows between two countries depends on each country's attraction forces between them.

The theoretical and empirical analysis of determinants of FDI flows have been based on two main groups of factors or a combination of the two. These are the pull-factors (demand side factors) or the push-factors (supply side factors). The pull-factors are those factors that could induce multinational corporations (MNCs) to desire to create or expand their operations overseas. These factors explain why national firms evolve into (MNCs), and why they decide to locate their production in another country rather than licensing or exporting (Singh and Jun, 1995). On the other hand, the push-factors are the host-country specific conditions that influence the flow of FDI. These are factors that attract FDI when the

decision to invest out of home country is conceived by the MNCs. Many socio-economic and political factors exist in the host country that determine available business opportunities and potential political risk, and all these influence the decision of MNCs to locate their activities in a particular country. It can be deduced that pull factors determine which country receives what share of FDI, while push-factors influences the overall size of FDI (Asiedu, 2002; Akinkugbe, 2003). Among these factors that are commonly cited in the standard economic literature in this area are distance from major markets, market size, infrastructure, labour cost, political stability, effectiveness of the legal system, fiscal and other non-tax incentives, level of human capital development exchange rate, interest rate and monetary policies, openness of the economy to foreign trade and natural resources endowment such as petroleum, diamond forest reserves, etc (Billington, 1999; Asiedu, 2002; Akinkugbe, 2003 and Campos and Kinoshita (2003). Other factors discussed in the literature to have influenced trade and factor mobility in developing countries are trade and investment agreements and colonial heritage.

In the economic literature, several factors have influence the developmental impacts of FDI. These include the development strategy and regulatory policy/ environment in the host country (level of participatory and involvement of foreign partners in the economy) and the degree of partnership arrangement between the local and the foreign firms, which determines the flow and adoption of modern technology embodied in the FDI. Within these factors are the regulations on employment, local content, taxation, repatriation of income, and so on.

A number of benefits and costs have been identified in the literature to accrue to the host country from inflow of foreign investment particularly the FDI. The plausible benefits of FDI have been summarized by the South Centre (1992) to include;

- The transfer of technology to individual firms and technological spill-over to the entire economy;
- Improved productive efficiency due to competition from multinational subsidiaries;
- Improvement in the quality of the factors of production including management in other firms apart from the host firm, leading to increased output/income, savings and investment;
- A healthy balance of payments through the inflow of investment funds;
- Increased exports;
- Increased government revenue from taxation
- Faster growth of output and employment; and



- Improvement in welfare as a result of lower prices of goods and introduction of new or better quality goods.

One of the major acclaimed benefits of FDI is technology transfer. However, the usual underlying assumptions have been that the transferred technology is completely adaptable and factor markets are efficient. There is the issue of how well the transferred technology is absorbed, utilized and diffused in the host country and the contribution that it makes to the technological capability development of the host economy. In order to benefit adequately, the host countries need to develop new skills, knowledge, institutions and organizational structures to master the technology they import.

It should be mentioned that direct employment generated by FDI and multinationals depends on some factors. These include the nature of investment (whether green-field-sites or joint ventures or mergers and acquisitions), trade and industrial policies, and the labour market institutions of the host country. Employment generation opportunities are higher in green field FDI and within export-oriented regimes with abundant cheap labour, while mergers and acquisitions often engender labour displacement. The greatest benefit of FDI can be derived where labour can move easily to new jobs or enter new types of employment, and where information on job opportunities is transparent and accessible. It is pointed out in the literature that indirect employment opportunities generated by multinationals could be great, ranging from 1 to 2 times the number of jobs created directly in affiliates. This is common among activities that involve backward linkages with a large number of input suppliers, output marketing outlets or subcontractors and service firms.

In the same vein, the benefits of FDI can be categorized into four contributions (Todaro, 1994). First, the resource gap between targeted or desired investment and domestically mobilized savings can be filled by FDI. Second (which is closely related to the first) is that the gap between targeted foreign exchange requirements and those derived from net export earnings including net public foreign debt can be filled through attraction of FDI. Third, FDI fills the gap between targeted government tax revenue and locally generated taxes revenue. Lastly, FDI assists in filling-up perceived management, entrepreneurship, technology and skill gaps by the local operations of private foreign firms.

In spite of the several benefits of FDI highlighted above, a set of arguments have been advanced against private foreign investment in general the activities of the multinational in particular. The first argument is that while some capital for development is provided through foreign investment particularly the multinationals, domestic savings and investment rates

may be reduced by stiff competition propelled by the former against the domestic firms. This problem can result from exclusive production agreements with the host governments or failure to reinvest much of their profits or when foreign investment generate income for groups with lower savings propensity. The second argument is that the balance of payments problem in the host countries can be compounded by the multinationals either as a result of their heavily dependence on importation of intermediate products (inputs) and capital goods or their overseas repatriation of profits, interest, royalties, management fees and other funds. The third argument is that there is a high tendency that the contribution of foreign investment to revenue of the government in the host countries in form of corporate taxes will be less than envisaged because of fiscal incentives such as liberal tax concessions, the practice of transfer pricing, excessive investment allowances, implicit public subsidies and tariff protection provided by the host governments. It is also been argued that FDI or multinationals sometimes engender or contribute to unbalanced development by constituting or reinforcing dualistic economic structure and exacerbates income inequality. In addition, they sometimes employ their economic power to influence polity and government policies in directions that are unfavourable to their host countries.

International competitiveness of the host economy can be improved by multinationals through provision of privileged access to the flows of goods, services and information within the corporate system. Preferences in terms of market access can be granted to products from the host countries. Some components of investment can be in form of aid to promote trade and development.

It has been argued that even though technology spill over effects may exist, foreign producers can draw demand from less efficient domestic producers, thereby forcing them to cut production (Aitken and Harrison, 1999). This competitive effect is been referred to as market stealing. Market stealing can be a one-time phenomenon, realized at the time of foreign entry into the domestic industry, or it can arise gradually over time as foreign firms increase their production in the domestic markets. The latter phenomenon can be denoted as “dynamic crowding out” (Kosova, 2004), while the former represents a static crowding out effect. If crowding out is a dynamic phenomenon, then holding domestic market constant, foreign sales expansion/growth should reduce the sales of domestic firms over time and thus lower domestic growth rates and hence hinder domestic investment. In that case foreign growth should have a negative impact on growth rates and mean survival time of domestic firms, and hence a positive effect on a probability of exit at a point of time.

Theoretically, either complementarity or substitutability relationship could hold between FDI and exports. Usually, the motivation is to produce locally in the FDI host nation, products that had previously been exported from the FDI origin nation, and when this happens, FDI and origin nation's exports are substitutes. In the same vein, the FDI origin nation operations of a multinational firm can be vertically linked with host nation operations, such that an increase in the activity in the latter generates increased demand for intermediate products (including capital goods) from the former. Also, marketing and distribution capabilities created by FDI might enable the origin nation's operations to export final goods and services to customers that would otherwise not be reached in the absence of FDI. When either of these happens, home country FDI and exports will be complements. Overtime, the relationship between FDI and exports could change. For instance, the host nation over time can become relatively more efficient in the production of a particular class of final goods and the origin nation can become relatively more efficient in the production of intermediate goods used to produce these final goods. If this happen and if multinational firms were to hold specialized skills enabling the realization of internal economies associated with vertically linking the production of the two sets of goods, the relationship between additional FDI and exports by these firms could become increasingly complementary even if at some earlier point in history an initial FDI served to displace home country exports.

### ***3.2 Major Findings in China-Africa Economic Relations Scoping Studies***

The incursion of China into Africa in the area of investment has produced a number of opportunities and challenges with respect to the recipients' economies in Sub-Saharan Africa (SSA). Studies have shown that Chinese investment is primarily located in the telecommunications infrastructure and extractive industry sectors, particularly oil (Corkin, 2008). However, the benefits to the general populace from Chinese investment in the oil sector are limited with respect to employment. For example, Sonangol, employs approximately 7,000 Angolans out of a total labour force of 5.1 million people. Nevertheless, the activities of Chinese construction companies have offered ample opportunity to rehabilitate and improve on much-needed telecommunications and other infrastructure to the benefit of the general populace in terms of service provision.

Available statistical evidence has equally revealed a phenomenon of a general upward trend in the inflow of FDI from China to Africa as the situation in Nigeria has shown. However, Chinese FDI has been found to be highly fragmented. For example, information obtained from the Nigerian Investment Promotion Commission (NIPC) revealed that Chinese private FDI is composed of agro-allied industry, manufacturing and communications sectors. Chinese FDI is also found to be incentives-sensitive. Again, the quest for oil and gas by the Chinese seems to be of importance in the resurgence of the current wave of relations in Africa, Nigeria as a reference point.

The interest of Chinese FDI in the area of manufacturing and service sector is also evident. Chinese FDI has flowed into the textile industry especially into spinning operations in a country like Mauritius. In most cases, Chinese companies operating in the mining and service sector in African countries are often not based on joint venture. The firms established so far are most fully owned by the Chinese companies. In effect, there is very limited joint ownership or local capital. In terms of employment, it is observed that the structure of employment in Chinese investment ventures has continually shown an increasing proportion of Chinese employees.

Emerging from these scoping studies is the obvious fact that Chinese investment in Africa is concentrated in a few sectors that are of strategic interest to China, especially in the extractive that focus on the exploration and/or exploitation of oil and other mineral products all over Africa. The case of Angola and Nigeria is a good example of this scenario. The largest proportion of China's foreign direct investment in Africa is in the oil sector followed by other solid minerals. A negligible proportion of Chinese investment could be found to be in the manufacturing sector, especially, agro-processing, pharmaceutical and telecommunications sectors. Another common characteristic from the studies reviewed above on China's investment in Africa is that they are usually carried out largely by state-owned enterprises or joint ventures. In addition, trade between China and its African counterparts are generally uni-directional, with South Africa as the only exception that has significant investment in China.

In summary, Chinese FDI into Africa can be regarded to be both resource seeking and market seeking motive-wise. In contrast, Chinese investments in OECD countries are primarily market seeking, in which case, they go into strategic partnership with enterprises in the host countries. Chinese FDI in Africa is also typically accompanied by Chinese workers and most of the supplies are sourced directly from China. This is not universally the case. For

example, in response to complaints by Nigeria and South Africa, the Chinese Ministry of Commerce has encouraged its companies to increase investment spending in developing countries, aiding technology development and personnel training (Ajaikaye, 2008).

The scoping studies are meant to provide some information about the emerging China-Africa relations, which they did as can be seen from the above review. The scoping studies have been limited by some factors including finance, data availability and the fact that literature is just building up on the issues particularly with reference to China and Africa. However, a deeper understanding of the relations between China and each of the selected African countries with more interesting findings on country case study (which will inform useful and more concrete policy recommendations) can be obtained if comprehensive study is embarked upon. This is the justification for this present study.

### ***3:3 Review of Methodological Framework***

Economic theory remains the basis for methodological framework in terms of what to expect where cross-border investment and spillovers are undertaken. It is argued that multinational enterprises (MNEs) often possess firm specific advantages in the area of the production methods they use, the way they organise their activities, the way they market their products/services and so on. By intuition, it is believed that once they have set up a subsidiary, some of the benefits of their advantages will spill over to indigenous firms via imitation, labour mobility, competition or local firms learning to export. In effect, these spillovers will help to raise productivity and their exploitation might be related to the structural characteristics of the host economy, in particular absorptive capacity.

Models of FDI have led to the emergence of several theories put forward to explain what determines the flow of FDI. Three of the most influential models are the theoretical model, the eclectic theory, and the gravity models.

#### ***The Theoretical Model***

The centre-point of the theoretical model of FDI is that FDI is a function of interest rates. This is so because interest rates constitute the return on capital, and that interest rates are low in capital abundant countries and high in capital scarce economies. Advocates of this model argue that capital controls are responsible for interest rate differentials and that when

these controls are relaxed, capital constraints will disappear and thus reduce interest rates even in capital scarce economies. In this wise, this methodological premise will always consider both the level and volatility of exchange rates as a major determinant of investment decisions. Exchange rate volatility hampers investments by increasing the level of uncertainty. For export-seeking and market-seeking FDI, it is theoretically consistent to expect that an appreciated real exchange rate will reduce FDI since it not only reduces competitiveness abroad but also reduces the price of imported substitutes in the domestic market. Conversely, it can be argued that an appreciation of the local currency increases FDI (especially in the form of imports). A phenomenon of real depreciation in the host country's currency reduces the domestic costs of production if valued in foreign currency, which induces FDI. Again, a depreciation in the host country's currency increases the relative wealth of foreign firms and hence their capacity to invest in the context of imperfections in the capital market (Domar, 1997).

### ***The Eclectic Model***

The theories of imperfect competition and market failure form the theoretical premises of this model. The general thrust of the model is that there are at least three sets of advantages that influence the decision of multinationals to invest abroad. These advantages are ownership ("O"), locational ("L) and internalization ("I") advantages. These advantages have been labelled the OLI paradigm. The "O" advantages provide justification for why some firms go abroad to invest. The advantages guarantee that such firms will succeed investing abroad because they enjoy some firm-specific advantages that will allow them to overcome the costs of operating in a foreign country. Such ownership-specific (or firm-specific) advantages are normally intangible and can be transferred within the multinational enterprise at low cost. The "O" advantages guarantee higher revenue and/or lower costs that can offset the costs of operating at a distance in a foreign location. Hence, undertaking FDI is premised on the fact that a firm has developed strong and specific characteristics that enable it to be competitive in the home market. It is presumed that such characteristics must be transferable abroad and strong enough to compensate for the extra costs and barriers characteristic of doing business abroad (Dunning 1988).

Given that the "O" advantages by themselves are not guarantee to justify foreign production, FDI is also explained by the countries (where a firm (MNE) intend to invest) locational ("L") advantages. These advantages (locational) are relevant for consideration

because they compensate for the usual handicaps of foreign production. Locational advantages relate to a number of fundamental factors that are often shaped by the host country's comparative advantage. This advantage is otherwise referred to as transactional cost advantage (Gastanaga, Nugent and Pashamova 1998). For example, if there a pool of cheap labour in the case of labour-intensive production, it constitutes a locational factor that will attract FDI into a country. The presence of series of incentives such as tax holidays and duty concessions constitutes "L" advantages.

The last set of advantages is referred to as the internalization ("I") advantages in this model. Internalization advantages explain why a firm would, for instance, choose to serve a foreign market through FDI rather than pursue alternative modes of operation, without ownership control of a foreign activity. When these advantages exist, FDI is usually a superior mode of entry than technology licensing or exporting as it allows investors to expand and exploit opportunities more efficiently abroad without concerns that their trade secrets would be exploited. Markusen (1995) argues that, because internalization focuses on characteristics of knowledge capital as opposed to physical capital, by investing directly rather than through licensing, the firm is able to eliminate or minimize risk of disclosing its trade secrets.

### ***The Gravity Model***

In the context of FDI, the gravity model<sup>7</sup> identifies market-related variables, distance-related variables and endowment-related variables as important determinants of FDI. Market-related variables in this model include GDP of the host country (indicator of market volume), the level of development (indicator of the degree of product differentiation) and population size (indicator of the size of the host country). Distance-related variables include geographical distance between capitals of economic centres and factors affecting economic distance between the countries. The endowment-related variables include wages in the host country (indicator of labour cost), skills of employees in the host country and GDP per capita as an indicator of technology and general development levels.

Beyond the theoretically-oriented methodological frameworks of FDI examined above, Kaplinsky (2007) has offered a pragmatic and operational methodological framework

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<sup>7</sup> Gravity models were originally used to explain bilateral trade flows between countries in an analogy to Newton's laws of motion (see Breuss and Egger, 1997). The basic gravity model postulates that trade between two countries is a function of the size of their economies as measured by the gross domestic product and population, the geographical distance between the two countries, and some preferential trade considerations.

for the impact analysis of China and India on economies of sub-Saharan Africa (SSA). This framework is particularly useful and relevant for gauging and tracking the competitive and complementary impacts of FDI from China as well as the direct and indirect impacts of Chinese FDI in SSA. This framework is designed with a view to gaining full insight into the various channels through which the Asian Driver economies interact with the global economy in general and the low economies of SSA in particular.

Having identified FDI as one of the six channels<sup>8</sup> of interaction between Asian Drivers (China is one of the Asian Drivers), the Kaplinsky's framework recognises the four primary types of FDI – technology-leveraging, resource seeking, market seeking and cost reducing and permits the examination of the impacts of any form of FDI to SSA. Given the fact that Chinese outward investment clearly fits-into the resource-seeking and market-seeking investments in the context of Chinese FDI in SSA and other developing economies, this framework is placed at the centre of the impact analysis of Chinese FDI in Africa while other methodological frameworks compliment where and when necessary.

### ***3:4 Review of Empirical Literature***

Empirical studies aimed at explaining the impact of FDI on host economies are replete in the literature. For ease of identification of these studies, Krogstrup and Matar (2005) revealed that the studies are often divided into two overall categories: those searching for an overall, or unconditional, linear effect of FDI on growth by including FDI flows in growth, technology or productivity regressions; and the studies which assume that the impact of FDI on growth is non-linear and that FDI depends on absorptive capacity of host economies.

#### *a) Studies of the unconditional impact of FDI on growth*

Studies which have sought to estimate the unconditional effect of FDI on growth (or some component or indicator of growth) find ambiguous and not very stable results. This is because some of the studies find zero or even negative correlations between FDI and growth,

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<sup>8</sup> Other channels are trade, finance, global governance, migration, and environmental spillovers. See Kaplinsky (2007) for detailed discussion on each of these channels.



while other studies find a significantly positive relationship. Examples of the the former type of study include van Pottelsberghe de la Potterie and Lichtenberg (2001) and Sadik and Bolbol (2001). The studies revealed that FDI has not had any manifest positive spillovers on technology and productivity over and above those of other types of capital formation. However, there are some indications that the effect of FDI on total factor productivity has been lower than domestic investments in some of the countries covered by the studies, indicating a possibly dominating negative crowding out effect.

Studies that find a positive unconditional effect of FDI on growth include Haddad and Harrison (1993), Blomström and others (1994), and Li and Lui (2005). Haddad and Harrison (1993) uses industry level survey data on Moroccan firms to link the productivity of Moroccan firms with the firm specific degree of foreign ownership as well as the degree of foreign ownership of the sector to which the firm belongs. Their findings reveal a higher overall level of productivity of firms with higher degree of foreign ownership, and that firms in sectors with a higher ratio of foreign ownership have higher levels of productivity, independently of the firm specific degree of foreign ownership. The caution about this result is the fact that foreign direct investment might have flown to sectors and firms with higher overall productivity. They observe that it is not possible to show that the presence of foreign direct investment should have accelerated the growth rate, and not just the level, of productivity in domestically owned firms in sectors with higher degree of foreign ownership.

The emerging import of the set of studies trying to establish unconditional impart of FDI on growth is that while there might be a level effect of FDI on GDP, evidence is scanty to establish that host countries to FDI have been benefiting from FDI inflows in terms of growth. Presently, the results in the literature regarding FDI-growth nexus are ambiguous and this ambiguity is often ascribed to misspecification of the estimating equation. In clear terms, it is often argued that the relationship between FDI and growth is likely to be non-linear owing to the role played by absorptive capacity in determining the sign and size of the impact. It is feared that many developing countries may in fact not have reached the necessary levels of absorptive capacity that would have guaranteed a positive impact of FDI on their economies. This opens up the search of the impact of FDI on growth to the set of studies that care to examine the level of absorptive capacity of the host economies.

*b) Studies conditioning on absorptive capacity: the technology gap*

Beyond estimating the unconditional impact of FDI on growth, Blomström and others (1994) also attempt to investigate the FDI effect conditional on the technology gap of the host country. This they do by splitting their sample of developing countries into two halves, one sub sample of low income countries and one sub sample of not-so-low income countries. They find FDI to be growth enhancing only in the latter group. Li and Liu (2005) look at the influence of the technology gap on the growth effects of FDI in developing countries, using the ratio of the gap between United States GDP and host country GDP relative to host country GDP as proxy for the technology gap. Accounting for technology gap in their estimation produce results that show that the lower the level of technological development of the host country, the smaller (or more negative) is the impact of FDI on growth. Their results imply a threshold value for the technology gap of 12.6<sup>9</sup>, above which FDI is no longer beneficial for the recipient country.

*c) Studies conditioning on absorptive capacity: Education of the workforce*

UNCTAD (1999) conducts an analysis of the impact of FDI on growth in developing countries, and finds that FDI is only significantly positive when entered in interaction with the number of years of schooling. Lu and Liu (2005) also find a positive interaction between years of schooling and FDI on the effect on growth, adding to an overall positive direct effect. Borensztein and others (1998) find more detailed results along the same lines. They study the growth effects of FDI inflows in a panel of developing countries and show that FDI does indeed contribute to economic growth over and above other forms of capital formation, but only when the effect is made conditional on the level of human capital development of the host country in question. More specifically, Borensztein and others find that FDI has a positive impact on growth when the average years of secondary schooling of the male population above 25 years of age exceeds the threshold of 0.52.

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<sup>9</sup> A critique of how Li and Liu (2005) measured technological gap revolves around the argument that GDP per capita might not be a good proxy for technological absorptive capacity. This is particularly true of economies that rely on natural endowment such as oil where oil revenues in such countries account for a very large part of total GDP, but do not imply any particular level of technology. More research on how to account more appropriately for the technology gap in so-called rent economies is therefore warranted.

*d) Studies conditioning on absorptive capacity: Financial development*

A number of studies have found indications that FDI may have a positive effect on growth when the host country's financial market development has reached a certain degree of development. Durham (2004) studies the impact of FDI on growth in a broad panel of countries, investigating the interaction between FDI and a list of factors suspected of determining the level of absorptive capacity. The two factors which come out significant are financial sector development and institutional development. Regarding financial development, Durham measures financial market development by total stock market capitalization relative to GDP. Four Arab countries are included in the study, namely Algeria, Egypt, Jordan and Tunisia. According to his results, only Jordan scores high enough on stock market capitalization to potentially benefit from FDI owing to sufficiently developed financial markets. Hermes and Lensink (2003), also conducting a broad country panel study, find that a certain degree of host country development of the financial system, measured as domestic credit to the private sector provided by the banking sector, is an important prerequisite for FDI to have a positive effect on the host economy. Their results imply that domestic credit provided by the banking system should exceed 12 percent of GDP for the host country to be able to absorb the potential technology diffusion of FDI.

*e) Studies conditioning on absorptive capacity: Institutional Development*

Again the study of Durham (2004) interacts the FDI term with institutional proxies, coming out with very interesting results. He uses an index for the regulation of business, an index for the protection of property rights and an index of corruption as institutional indices. The two proxies are found to significantly influence the impact of FDI on growth. More specifically, the business regulation index, which is discrete in nature and ranges from 1 to 4, is found to have a threshold value of just over 3, which implies that only four out of 32 countries in the sample pass the threshold. The property rights index is also discrete and takes on values from 1 to 5. This index is found to have a threshold value of just over 3, implying that 11 out of the 32 countries pass the threshold.

On the whole, the empirical literature on FDI in terms of its impact on the host countries suggests three policy-oriented implications. First, the literature reveals that FDI in and of itself is no guarantee for stronger economic growth. In fact, FDI can have, and has

occasionally been found to have, negative effects on growth in a host country due to negative crowding effects outweighing potentially positive externalities. Second, FDI stands to benefit host countries where sufficient and necessary absorptive capacity conditions are in existence. The third implication is that given the substantial intra-regional differences between SSA countries, the general lack of positive externalities from FDI does not preclude that some SSA countries may currently be benefiting from FDI, and that other SSA countries that are not currently benefitting from FDI would be in a position to benefit with small investments in absorptive capacity.

## 4.0 Theoretical Framework and Methodology

The investment development path (IDP) framework emanating from the work of Dunning (1981, 1986) and Dunning and Narula (1996) is adopted for this study. The central thesis of the IDP framework is that a country or region's international investment position is systematically related to its level of economic development. This framework, formalised in the concept of the investment development path (IDP), proposes that there is a U-shaped relationship between economic development and a country's international investment position. This implies that as economic development proceeds net inward direct investment will first grow and then decline. In the earliest phase, the country's infrastructure will be inadequate to support even vertical ("low labour cost seeking") inward investment. Such investment will grow however as the economy develops. It will take longer for firms from backward regions to accumulate the firm-specific assets that would allow them to engage in outward direct investment; Caves (1996); Dunning (1988). Over time, learning-by-doing will allow this process to evolve and outward FDI will emerge. At the same time, the country's absolute cost competitiveness will be eroded, reducing the incentive for vertical inward investment. The incentive for horizontal ("market seeking") and technology-sourcing investments may expand however as the economy becomes wealthier, and domestic firms will seek to maintain their competitiveness by engaging in outward vertical investments.

The choice of this theoretical framework is borne out of the fact that, the IDP is a dynamic concept and it draws on Dunning's eclectic paradigm of international production and is shaped by the OLI variables (ownership, locational and internalization advantages). The framework assumes, first, that development induces significant structural change to the

economy and, second, that such change has a systematic relationship with the pattern of FDI (Lall, 1996). It goes further to contend that the change in the locational advantage of a country as well as in its firm's ownership and internalization advantages *vis-à-vis* other economies explains how its international investment position evolves from only receiving inward FDI to exporting FDI. The transition from FDI recipient to FDI exporting status passes through a number of stages. Boudier-Bensebaa (2008) identified five distinct stages as summarized in Table 5.

**Table 5: Characteristics of the IDP**

Stage	Inward FDI	Outward FDI	NOIP <sup>10</sup>
1	Insufficient location advantages □ No inward FDI except natural resource-seeking FDI	Absence of domestic firms' ownership advantages □ No outward FDI	Around zero
2	Development of 'generic' location advantages □ Faster growth of inward FDI than of GDP	Emergence of domestic firms' country-specific ownership advantages (O) □ Little outward FDI	Increasingly negative
3	Erosion of location advantages in labour-intensive activities Development of created-asset location-advantages □ Decrease in the rate of growth of inward FDI	Growth of O advantages □ Increase in the rate of growth of outward FDI	Negative but increasing
4	Location advantages entirely based on created assets  □ Superiority of outward FDI over inward FDI	Firm-specific ownership advantages (O) more important than O advantages	Positive
5	Theoretically, fall and then fluctuation around zero of the NOIP, but in fact no longer a reliable relationship between a country's international investment position and its relative stage of development		

Source: Boudier-Bensebaa (2008).

This study covers between 1997 and 2007 subject to data availability. It employed the use of quantitative (descriptive analysis such as ratios, percentages and correlation as well as cross tabulations), qualitative (key informant interviews and surveys) and case studies-for example the Railway Transport project handled by the Chinese. The use of surveys assisted

<sup>10</sup> NOIP means Net Outward Investment Position.

to generate firm-level data that allowed the analysis of China-Nigeria investment relations with respect to concerns such as the employment effects as well as the competitive and/or complementary effects of Chinese firms to local firms. The use of content analysis of relevant documents and reports obtained from various sources was equally involved to corroborate the result obtained from primary data obtained. Documents containing investment policy regime in both Nigeria and China were reviewed so as to see the policy adequacy and the need to fine-tune policy to make FDI flows from China to Nigeria beneficial.

In addition, in-depth interviews of key informants/stakeholders (both Nigerians and Chinese; representatives of government, embassies; National Planning Commission, Central Bank of Nigeria, Ministry of Finance, Nigeria Investment Promotion Council, Chamber of Commerce, National Association of Small and Medium Enterprises, etc) and case studies of some selected Chinese firms in Nigeria provided the database required for the qualitative impact analysis of China-Nigeria investment relations.

## 5.0 Empirical Analysis

### ***5.1 Magnitude, Pattern and Structure of Investment between China and Nigeria***

#### *Volume of Chinese FDI in Africa and Nigeria*

In 2003, China was the fifth largest investor in the world, after the United States, Germany, the United Kingdom and France. Its foreign investments amounted to US\$2.087 billion, which represented an increase of 112.0 per cent over the amount for 2002, and made it actively present in 160 countries. China is investing massively in raw material deposits overseas, and is multiplying its trading partnerships in order to secure regular supplies (Lafargue, 2005). In 2005, it was estimated that the cumulative value of Chinese investment in Africa was US\$4.5 billion, which was over 12.0 per cent of total FDI stock of US\$37 billion in Africa (China Monitor, May 2006). Nigeria was listed among the largest fifteen host countries of Chinese outward FDI between 2003 and 2006. Indeed, Nigeria occupied the twelfth position with the sum of US\$191.01million and placing third after Sudan and Algeria among African countries that received FDI inflows from China during the same period<sup>11</sup>

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<sup>11</sup> See Appendix Tables 1 and 2.

(Kolstad and Wiig, 2009). In terms of the pattern of investment relations, up till the 1990s, FDI flows bilaterally between China and Nigeria, however, the situation changed towards the late 1990s and 2000s and it has become a unilateral flow from China to Nigeria as will be observed in the subsequent sub-sections.

### *Chinese FDI inflow to Nigeria*

Table 6 presents a global picture of FDI inflow to Nigeria from different regions/countries including Asia-Pacific and China, from 1999 to 2006. All the regions recorded significant increase in FDI inflow from the 1999 level. Thus, the upward increase in the aggregate FDI flows to Nigeria from about \$190.61 million in 1999 to about \$4169.14 million in 2006 is a joint increase in the levels of FDI by all the regions. Available information points to a general upward trend in the inflow of FDI from China to Nigeria. Although FDI inflow from other sources have been increasing, Chinese FDI to Nigeria has been increasing at a very rapid rate beginning from 2000 (Table 7)

**Table 6: Foreign Direct Investment in Nigeria, 1999-2006, \$ Million**

Region/Country	1999	2000	2001	2002	2003	2004	2005	2006
North America	7.35	9.84	12.10	36.16	40.34	4354.14	5166.32	1601.28
South America	1.15	2.96	0.39	0.05	7.14	60.04	24.56	11.76
Asia/Pacific	2.94	5.93	4.45	5.17	1.54	32.12	47.29	39.63
China	0.02	1.08	2.39	0.0	0.05	0.51	1.88	5.50
Middle/Far East	7.41	2.75	10.92	5.30	6.74	23.27	21.22	13.39
Europe	164.95	136.46	98.86	200.24	293.66	2624.30	3084.68	2441.52
Africa	6.79	9.45	8.24	24.30	91.41	173.62	169.04	56.06
Total	190.61	168.47	137.35	271.22	440.88	7268.00	8514.99	4169.14

Source: Based on data from Nigerian Investment Promotion Commission (NIPC)

Compared to other regions, South American region contributed the least to the level of FDI inflow to Nigeria. This was followed by the Asia-Pacific region. By 2006, though the relative positions remained unchanged as the South America maintained its position, FDI inflows from Asia Pacific region have surpassed the inflows from the Middle and Far East region. Thus, between 1999 and 2006, FDI inflows from Asia- Pacific region to Nigeria increased at a higher rate than their similar inflows from the Middle and Far East region. This suggests increasing importance of China in the observed trend. A further analysis of inflow of FDI from this region revealed that although China ranked 5<sup>th</sup> in the magnitude of FDI in

flows from the region to Nigeria behind India, Singapore, Hong Kong, and Japan in that order, the country seems set to overtake these leading countries. This is not far-fetched given that Chinese FDI inflows to Nigeria increased from an average of \$0.55 million in 1999-2000 to about \$5.5 million in 2006. This is a tenfold increase compared to 9-fold increase by the region as a whole.

**Table 7: Nominal Growth Rate of Inflows of FDI into Nigeria**

Region/country	2000	2001	2002	2003	2004	2005	2006
North America	33.9	23.0	198.8	11.6	10693.6	18.7	-69.00
South America	157.4	-86.8	-87.2	14180	740.9	-59.1	-52.1
Asia/Pacific	101.7	-25.0	16.2	-70.2	1985.7	47.2	-16.2
<b>China</b>	<b>5300</b>	<b>121.3</b>	<b>-100</b>	<b>-</b>	<b>920</b>	<b>268.6</b>	<b>192.6</b>
Middle/far East	-62.9	297.1	-51.5	27.2	245.3	-8.8	-36.9
Europe	-17.3	-27.6	102.6	46.7	793.7	17.5	-20.8
Africa	39.2	-12.8	194.9	276.2	89.9	-2.6	-66.8
Total	-11.6	-18.5	97.5	62.6	1548.5	17.2	-51.0

Source: Computed from the above Table 6.

### *Nigerian FDI Outflow to China*

By the 1990s, the destinations of Nigerian FDI are Belgium/Luxembourg, France, and China (Table 8). However, by the 2000s, China and some other countries ceased to be destinations of the outflow of the Nigerian FDI. Recently, France, United States and Germany are the major destinations of the outflow of the Nigerian FDI. Given this trend, the factors responsible for the redirection of FDI against China should be investigated particularly now that that we have accumulated huge reserves and therefore should be investing within and outside the country. Besides, it seems as China's business environment is attractive as FDI flows massively to the country in recent times.

**Table 8: Nigeria FDI flows Abroad by Geographical Destinations, 1992 to 2004 (\$ millions)**

Region/country	1992	1993	1994	1995	1999/2000	2001	2002	2003	2004
Belgium/Luxembourg	0.7	0.1	-	-	-2.1				
China	0.1	1.4	0.6	0.4	-	-	-	-	-
Czech Republic					3.0				
France	0.4	1.4	0.4	0.2	104.1	247.9	19.8	-22.6	-
Germany	-	-	-	-	-	0.9	0.9	-5.6	-
Malaysia		1.2	-	-	-	-	-	-	-
Portugal	-	-	-	-	-	-	0.2	-	-
United States	-	-	-	-	5.0	-	3.0	21.0	-7.0

Source: UNCTAD World Investment Directory (WID) Country Profile, 2006.



## Structure of Investment

Chinese investment in Africa covers mainly manufacturing and construction activities (particularly in the area of infrastructure) as well as services. It also covers trading, resource extraction and agriculture (See Tables 9 and 10). Table 11 shows that FDI inflows into Nigeria between 2007 and 2008 generated some employment. However, further investigation is needed to verify whether significant part of employment generated is for Nigerians or China.

**Table 9: Sectoral Distribution of Chinese FDI in Africa, 1979 to 2000**

Sector/Industry	Number of Projects	Investment value (\$ millions)
Agriculture	22	48
Resource extraction	44	188
Manufacturing	230	315
-machinery	20	16
-Home appliances	36	25
-Light industry	82	87
-Textiles	58	102
-Other manufacturing	34	86
Services	200	125
Others	3	6
Total	499	681

Source: UNCTAD and MOFCOM

**Table 10: Top Ten Sectors Receiving China's OFDI in Africa: 2006 Flows and Stocks**

2006 Flows				2006 Stocks			
Sector		US (Million)	%	Sector		US (Million)	%
1	Mining	8539.51	40.74	1	Leasing & Business Services	19463.60	22.52
2	Leasing & Business Services	4521.66	21.58	2	Mining	17091.61	19.78
3	Finance	3529.99	16.84	3	Finance	15605.37	18.06
4	Transport, Warehousing & Postal	1376.39	6.57	4	Wholesale & Retailing	12955.20	14.99
5	Wholesale & Retailing	1113.91	5.32	5	Transport, Warehousing & Postal	7568.19	8.76
6	Manufacturing	906.61	4.33	6	Manufacturing	7529.62	8.71
7	Real Estates	383.76	1.83	7	Real Estates	2018.58	2.33
8	Science & R&D	281.61	1.34	8	Construction	1570.32	1.82
9	Agriculture, Forestry & Fisheries	185.04	0.88	9	IT	1449.88	1.67
10	Power & Utilities	118.74	0.57	10	Residential & Other Services	1174.20	1.36
<b>Total</b>		<b>20957.22</b>	<b>100.00</b>			<b>86426.57</b>	<b>100.00</b>

Source: Computed from the *2006 Statistical Bulletin of China's Outward Foreign Direct Investment*, Joint publication of MOFCOM, NBS, and SAFE, Government of China, Beijing.

**Table 11: Sectoral Distribution of Some Chinese Private FDI in Nigeria, 2006-2008**

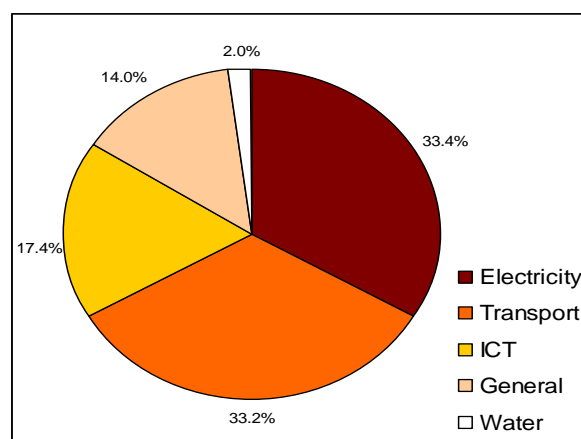
Sector/year	2006-08	2007	2007	2008	2008
Sector	No of firms	Capita N' million	Employment	Capita N' million	Employment
Oil exploration, Quarrying & Mining	5	82	95	30	80
Manufacturing	15	160	6455	30	365
Agriculture	2	-	-	12650	100
Building & Construction	5	115	853	20	40
Trading	14	78	433	62	140
Services	7	17	670	30	210
Lumbering, Timber & saw mills	1	10	80	-	-
General	11	128	1310	44	800
Total	60	590	9896	12866	1735

Source: UNCTAD and MOFCOM

According to a new World Bank –PPIAF data base, the estimated Chinese financial commitments to African infrastructural projects (most of which are financed by either government or Export-Import Bank) on an annual basis increased from less than \$1.0 billion over 2001 to 2003 to almost \$2.0 billion during 2004 to 2005 and reached about \$7.0 billion in 2006 before it fell to \$4.5 billion in 2007.

On sectoral basis, a significant proportion of Chinese finance is allocated to general, multi-sector infrastructure projects, within the framework of broad bilateral cooperation agreements that permit resources to be distributed according to government priorities. It can be observed from the Figure 1 below that the two largest beneficiary sectors are power (mainly hydropower) and transport (mainly railroads).

**Figure 1: Confirmed Chinese Infrastructure Finance Commitments in Sub-Saharan Africa by Sector, 2001-2007**



Source: World Bank–PPIAF Chinese Projects Database, 2007

In the power sector, China's investment activities have revolved around the construction of large hydropower schemes across Africa. By the end of 2006, China was providing US\$3.5 billion toward the construction of six major hydropower projects amounting to some 6,000 megawatts (MW) of installed capacity. China has recorded a major investment in the rail sector, with financing commitments in the order of US\$4 billion across Africa. The investment includes rehabilitation of more than 1,350 kilometres of existing railway lines and the construction of more than 1,600 kilometres of new railroad. The entire African railroad network amounts to around 50,000 kilometres. The largest deals have been in Nigeria, Gabon and Mauritania. China's involvement in the information and communication technology (ICT) sector, basically takes the form of equipment sales to national incumbents, either through normal commercial contracts or through intergovernmental financing tied to purchases of Chinese equipment by state-owned telecom incumbents. A major focus has been on the development of national backbone infrastructure. Over 2001–07, Chinese telecom firms supplied almost US\$3 billion worth of ICT equipment, mainly in Ethiopia, Sudan, and Ghana. With respect to the road and water sectors, although the sums involved are much smaller than in the other three sectors, China has been involved in financing a significant number of projects in these sectors, with about US\$700 million gone to the two sectors combined.

### ***Composition of Chinese FDI in Nigeria***

Although, information about Chinese activities in the country points to increasing economic (trade, commerce and investment), social (health and education) and technical relation, the composition of Chinese FDI into Nigeria is fragmented. According to a source: China has set up over 30 solely owned companies or joint venture in Nigeria actively involved in the construction, oil and gas, technology, services and education sectors of the Nigerian economy (Ogunkola, Bankole and Adewuyi, 2006). Big Chinese financial institutions have been involved in the acquisition of holdings in some financial institutions such as the Standard Chartered Bank and the IBTC-Chartered Bank in Nigeria.

The increased Chinese economic interests in Nigeria can be broadly classified into two: private and public. According to information obtained from the Nigerian Investment Promotion Commission (NIPC), Chinese private FDI is composed of agro-allied industry, manufacturing and communications sectors. On one hand, some of these investments are joint

venture mainly between Chinese and Nigerian investors<sup>12</sup>. On the other hand, some are wholly foreign owned either wholly by the Chinese<sup>13</sup> or in partnership with other foreign investors.<sup>14</sup> Some of the Chinese investments have also benefited from investment incentives in the country such as pioneer status and expatriate quotas have been granted to some of these companies (see Table 12).

**Table 12: Sectoral Distribution of Some Chinese Private FDI in Nigeria, 2006-2008**

Sector/year		2006-08	2007	2007	2008	2008
Sector	Nature of investment	No of firms	Capita N'million	Employment	Capita N'million	Employment
Oil exploration, Quarrying & Mining	Both joint venture & wholly owned	5	82	95	30	80
Manufacturing	Both joint venture & wholly owned	15	160	6455	30	365
Agriculture	Both joint venture & wholly owned	2	-	-	12650	100
Building & Construction	wholly owned	5	115	853	20	40
Trading	Both joint venture & wholly owned	14	78	433	62	140
Services	wholly owned	7	17	670	30	210
Lumbering, Timber & saw mills	wholly owned	1	10	80	-	-
General		11	128	1310	44	800
Total		60	590	9896	12866	1735

**Source:** Compiled from the Data supplied by NIPC

Thus in 2005, the official record by Nigeria was \$130 million FDI inflow from China. This seems to be at variance with the impression created in the media. Various explanations can be adduced for the seemingly paucity of observed figure: First, the upsurge in Chinese FDI inflow to Nigeria occurred only in the recent time i.e. between 2006 and 2008, a period that is not covered by the available data. Second, there is also the possibility that the promises and declarations captured by the media did not eventually materialised. A case in point is the sales of Kaduna Refinery that was announced in January 2006. It was meant to be a \$2.3 billion worth of investment by the Chinese state controlled energy company, CNOOC. By March 2007, the government was considering a review of the deal.

According to World Bank PPIAF Chinese project data base, in 2006, both China National Offshore Oil Corporation (CNOOC) and Chinese National Petroleum Corporation (CNPC) won substantial interests in Nigerian oil exploration. The CNOOC purchased 45

<sup>12</sup> See table 11, Firm number 1 (oil exploration and Quarrying and mining)

<sup>13</sup> See table 11, Firms number 4 to 6

<sup>14</sup> See table 11, Firm number 5

percent of Block ML130 in the Niger Delta, with reserve estimates of 600 million barrels covering about 500 square miles of Akpo Oilfield and other discoveries. The total deal offered by CNOCC was worth US\$2.7 billion. Subsequently, CNPC completed the acquisition of a 51 percent stake in the Kaduna refinery for a total consideration of US\$2 billion. The refinery was designed to refine 110,000 barrels of oil per day; however, due to lack of maintenance, its actual refinery capacity was only 70 percent of that capacity. Sum together, CNPC received the license for four oil blocks—OPL 471, 721, 732 and 298. Following these deals, Chinese state-owned oil companies committed to invest at least US\$5 billion in the country’s petroleum industry (Table 13).

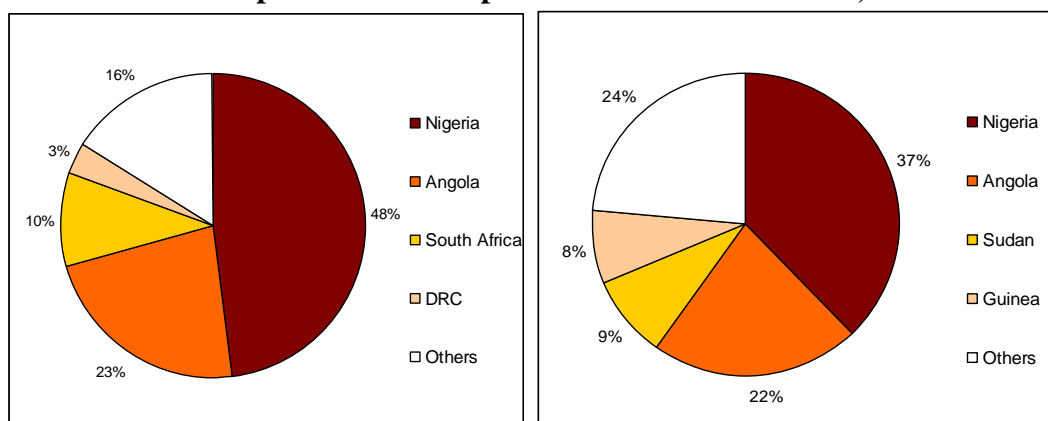
**Table 13: Chinese Investment Commitments in Natural Resource Sector in Sub-Saharan Africa, 2001-2007 (US\$ millions)**

	Oil	Minerals	Total
Angola	2,400	0	2,400
Congo, DRC	—	>370	>370
Nigeria	>4,762	319 <sup>1</sup>	>5,081
South Africa	0	>1,047	>1,047
Others	>314	>287	>1,693
<b>Total</b>	<b>&gt;7,476</b>	<b>&gt;2,023</b>	<b>&gt;10,591</b>

Notes: Oil and solid minerals; “—” = project was reported but that the value of the commitment was not given.

Source: World Bank–PPIAF Chinese Projects Database, 2007

**Figure 2: Country shares of Chinese natural resource investment and finance commitments into power and transport in Sub-Saharan Africa, 2001-2007**



(a) Natural resource commitments

(b) Power and transport commitments

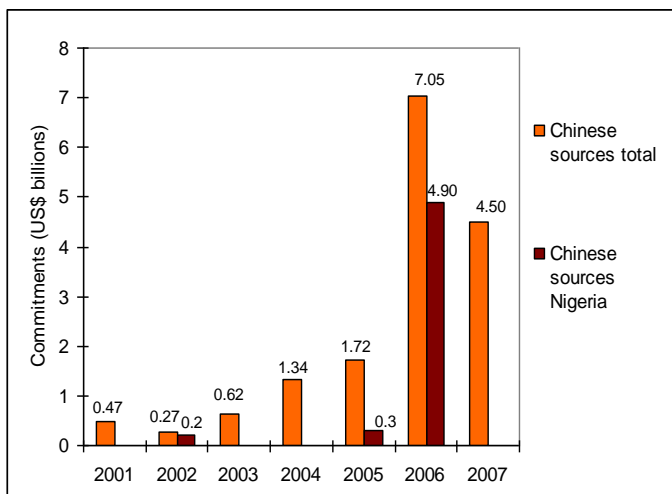
Source: World Bank–PPIAF Chinese Projects Database, 2007

Generally, there exist some correspondence between countries with large Chinese natural resource investments and those with large Chinese infrastructure financing for power

and transport (Figure 2). In some cases, the infrastructure financed by Chinese official loans forms part of an integrated package of natural resource development. This is because, for example, there is a need to link mining deposits with power required for processing and rail and port infrastructure required for export.

According to information from a new World Bank –PPIAF data base, for African, Nigeria has been a major recipient of Chinese infrastructure finance. It received relatively small volumes of Chinese infrastructure finance during 2002 and 2005. However, in 2006 a major surge occurred, when China made almost US\$5 billion of infrastructure finance commitments to Nigeria, which accounts for 70 percent of China’s total commitments to Sub-Saharan Africa that year (Figure 3).

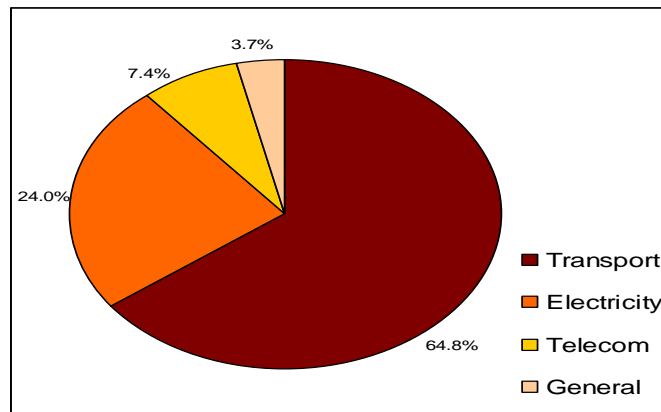
**Figure 3: Estimated value of Chinese infrastructure finance commitments in Sub-Saharan Africa and Nigeria, 2001–07**



Source: World Bank–PPIAF Chinese Projects Database, 2007

Some 40 confirmed projects involved Chinese commitments of about US\$50 million. However, Chinese finance has been found in about half a dozen cases to be relatively very large amounting to over US\$1 billion in value for single projects. There exist three such mega-projects committed in Nigeria, with the rest of Nigeria’s projects falling into the mid-sized category with commitments of the order of US\$200-300 millions. The sectoral spread of Chinese infrastructure finance in Nigeria is a little different from the entire Africa, with transport projects amounting to 65.0 percent of all commitments followed by power with 24.0 percent (Figure 4).

**Figure 4: Confirmed Chinese infrastructure finance commitments in Nigeria by sector, 2001–07**



Source: World Bank–PPIAF Chinese Projects Database, 2007

In the transport sector, China has registered a major financial commitment in the Nigerian rail sector; with the major rail projects include the Lagos-Kano rehabilitation project and the Abuja Rail Mass Transit System. In the power sector, by the end of 2006, China provided US\$3.5 billion toward the construction of six major hydropower projects amounting to some 6,000 megawatts (MW) of installed capacity across Africa. The largest hydro-power project on this list is the 2,600-MW Mambilla scheme in Nigeria. These schemes would increase the total available hydropower generation capacity in Sub-Saharan Africa by around 30 percent when completed. There have also been some activities in thermal generation and transmission, most of them in Sudan and Nigeria. In Nigeria, the Federal Government is constructing three gas-fired power stations with the assistance of a credit line from China Exim Bank. In the information and communication technology (ICT) sector, an important focus has been the development of national backbone infrastructure. Nigeria’s National Rural Telephony project and first communication satellite NigComSat-1 received financing from China Ex-Im Bank.

## **5.2 Characteristics of Chinese FDI and Loans in Africa and Nigeria**

A major characteristic of Chinese investment in African countries including Nigeria is its concentration in a few sectors that are of strategic interest to China, especially in the extractive industries. Chinese firms have invested billions of dollars and used Chinese engineering and construction resources on infrastructure for developing oil, gas, minerals and other natural resources in a number of African countries including Nigeria. For example, in

2002 Sinopec, a Chinese oil company signed a 420 million euro contract to develop the Zarzaitine oilfield in the Sahara (Ajakaiye, 2006). Simultaneously, China is increasing its presence in exploration and/or exploitation of oil and other mineral products all over Africa. The largest share of China's foreign direct investment in Africa is in the oil sector followed by other solid minerals. It is noted that a relatively small proportions are in manufacturing sector, especially, agro processing, pharmaceutical and telecommunications sectors. Currently, Chinese pharmaceutical company is producing a new anti-malaria medicine in Uganda and another Chinese firm was recently awarded contracts worth US\$400 million for servicing mobile phone networks in Kenya, Nigeria and Zimbabwe (Ajakaiye, 2006).

Another characteristic of China's investment in Africa, and globally is that they are carried out largely by state-owned enterprises or joint ventures. They typically exhibit partnership with state-owned enterprises or enterprises with significant government equity holding in the host countries. According to the available information, currently there are more than 800 Chinese enterprises operating in Africa as at August, 2006. Not less than 674 representing 84.25% of them are state owned enterprises (SOEs). A Chinese pharmaceutical company is currently producing a new anti-malaria medicine in Uganda and another Chinese firm was recently awarded contracts worth US\$400 million for servicing mobile phone networks in Kenya, Nigeria and Zimbabwe (Ajakaiye, 2006).

Recently, uni-directional Sino-Africa investment relations can be observed, with exception of South Africa where a few of the companies are also wining contracts in China. A recent example is the South African Baterman Engineering that won a \$4million contract to supply in Yunnan province. Another is South Africa's SASOL that is involved in a \$10billion deal designed to diversify China's petroleum resources coupled with a joint venture between China and South Africa on nuclear technology (Ajakaiye, 2006).

Chinese FDI in Africa is also typically accompanied by Chinese workers and most of the supplies are sourced directly from China. This is not universally the case. For instance, in response to complaints by Nigeria and South Africa, the Chinese Ministry of Commerce has encouraged its companies to raise investment spending in developing countries, aiding technology development and personnel training. Similarly and specifically, in response to complaints by Nigeria's Minister of Science and Technology, Huwaei Technologies Nigeria Limited, a Chinese FDI has established a training centre in Nigeria to train 2000 telecoms engineers per annum. Therefore, these attempts to compromise the benefits of FDI should be persistently resisted by the Nigerian Government.



Chinese investment financing in African countries including Nigeria is offered with a relatively large aid component in form of concessionary interest rates and grant element. Besides, the investment loans are been offered without conditionalities attached to them as compared with loans from the multilateral finance organisations such as the World Bank and the International Monetary Fund (IMF). This allows for domestic policy flexibility, although this has been criticised because of poor governance and macroeconomic environment in African countries including Nigeria, which may hinder productivity and sustainability of investment.

Finally, aside from "push" factors, Chinese outward FDI is often associated to "pull" factors such as a host country's favourable investment policies, including incentives and other location-specific advantages. For example, a number of Chinese companies are reported to have chosen the United Kingdom to take advantage of investment grants. Thus, China is fond of extracting extremely generous terms for its investment outside the resource seeking activities. Table 14 presents the results of survey of Chinese firms with a view to discovering the drivers of Chinese FDI outflows.

**Table 14: Summary of survey results for 100 Chinese TNCs, 2000<sup>15</sup>**

<i>Why Invest Overseas?</i>		<i>What is most Attractive Factor in Host Countries?</i>		<i>Where is Your Priority Region?</i>	
47.1%	Expanding overseas markets	32.0%	Host country privileged policies	32.0%	Africa
16.9%	Better profit	28.7%	Requiring relatively small amount of investment	20.0%	Southeast Asia
14.5%	Sluggish demand in China	22.5%	Cheap labour	18.0%	Latin America
12.1%	Export to third country	8.4%	Cheap labour and proximity to raw materials	9.3%	Middle East
9.3%	Competition with export from China			8.7%	Eastern Europe
				8.0%	Central Asia
				4.0%	Others

Source: Wang (2002)

Perhaps, the conclusion is that Chinese direct investment in Nigeria and other African countries is driven mainly by the need to secure access and acquire key commodity and energy assets and capture under-exploited markets. In essence, Chinese FDI in Africa are primarily resource seeking and secondarily market seeking, in contrast to that in OECD

<sup>15</sup> 100 out of the 170 enterprises surveyed replied.

countries which are primarily market seeking. In the latter case, they go into strategic partnership with enterprises in the host countries.

### **5:3 Chinese Investments in Nigeria: Case Studies**

#### **OGUN STATE**

**Kajola Specialised Railway Industrial Free Trade Zone** is a strategic move by the Ogun State government to take maximum advantage of the Railway Modernisation Programme and the proposed Inland Container Terminal Project of the Federal Government. The aim is to attract specialised industries and businesses offering complementary services to these two projects of the Federal Government. Some of the investors expected in the zone include: Railway industrial park, Locomotive workshop, Railway related Service, Foundries, Metal fabrications, Haulage/Logistics, New Towns development, Mega Mart and shopping Centres, Commerce & Industries (Fruit Juice Processing, Ceramic Making, Dairy Production, Furniture Making, Adire and Garment production and Kola Processing. Various activities ranging from acquisition of 2000 hectares of land to sourcing of environmental baseline data to identification of resettlement sites for affected people to design of infrastructural development plan have culminated in the launch of the Zone.

The zone is a joint venture of the Ogun State Government and the Chinese Civil Engineering Construction Company (CCECC). The company's investment was estimated at about N115.8 billion. The government envisaged that the project will facilitate rapid industrialisation of the State and deepen foreign direct investment inflow to the state. It is also important to note that since this is one of the three free trade zones established in the State, it is meant to serve as a growth pole. This is within the larger concept of simultaneous development of all parts of the state.

**Ofada Vee Tee Rice Limited** is another project involving Ogun State and a Chinese firm. Indeed, the company's equity shares are to be owned by the Ogun State government, the Federal Government and Vee Tee Group with the latter holding the majority of the shares. The company has a designed capacity of 225, 000 (9000 bags) tons of rice per day and the capital out lay is estimated at about \$2 billion.

The company is to produce quality rice that will compare favourably with those from anywhere in the world. The local farmers are to supply paddy rice to the company that will be processed (de-husking, de-stoning, parboiling, sorting, polish, packaging and marketing) by the company. The large volume of rice imported into the country, is an indication of the huge potential demand for the commodity and thus market should not be a constraints to the effective performance of the company. The contribution of the company to self sufficiency in food production and foreign exchange savings is commendable. Optimal benefits from the establishment of Ofada Vee Tee Rice require proper integration of rice farmers into the plan of the company. The company's promise of provision of seeds and extension services may not be sufficient. The market for the paddy rice must be guaranteed. Hence a contingent plan for over- as well as under-supply of paddy rice to the company is required for effective response by the farmers.

However, the backward linkage of the company is important for the economy in terms of employment and rural livelihood. The current projection is that about 30,000 farmers are to supply paddy rice to the company. Other beneficiaries which include transporters and traders of the raw materials and the finished products, technological capabilities of Nigerians through learning by doing is necessary and this can be achieved by ensuring that qualified Nigerians man the company. Currently, only three Chinese are on ground out of about 100 people employed and the company plans to hire about 5000 hands when fully operational.

**Ogun Guangdong Free Trade Zone (OGFTZ)** is a tripartite project of two Chinese companies: Guangdong Xinguang International of Guangdong Province in china and china-Africa Investment Limited; and the Ogun State Government. The FTZ, located in Igbesa in Ogun State is one of the three free trade zones being established in the state. The zone which is being established at the instance of the Chinese consortium with the support of the state in the area of land acquisition, processing and securing various approvals especially from the Nigeria Export Processing Zone Authority (NEPZA) has about 30 Chinese currently working on the site. The cost of the project estimated at about \$500 million is to be financed by the Chinese consortium. The First Bank of Nigeria plc is collaborating with the consortium in the areas of investment banking, project financing, business advisory services and correspondent banking relationship.

When completed, the FTZ will consist of about 100 firms mainly engaged in the light to medium manufacturing activities including footwear and rubber production, ceramic

processing, furniture production, hardware and household appliances, real estate development, and light and heavy manufacturing plants. These activities promised to generate direct and indirect employment to different categories of Nigerians.

In addition, the development of the host community is expected to be positively enhanced. At least two related projects are in this direction:

- a \$700,000 primary school project; and
- dualisation of the road linking Igbesa (the FTZ site) to Badagry express way.
- Dredging to the zone to allow for free movement of new materials and finished products to and from the zone is under consideration.

The benefits from these projects involving Chinese firms have not been consistently and systematically evaluated neither is there any attempt at matching the cost of citing the projects in a particular community with the benefits. The cost-benefit analysis on the part of the Chinese consortium is not equally available. It will be interesting to compare the streams of costs and returns on investment over the life span of the project.

An analysis of the employment structure is required in order to strategically position Nigerians for the projects. It is not sufficient to state that the project will generate employment without rigorous analysis of the nature of employment. The categories of skills to be employed, the qualification and experience of the Chinese counterpart must be within the Nigerian laws on the expert quotas.

The establishment of the project also presents various government agencies with challenges of monitoring and evaluation with a view to ensuring that the zone and the firms operating within its jurisdiction conform strictly to Nigerian laws. Agencies such as Nigerian Customs, Immigrations, Ministry of Labour, and NEPZA have significant roles to play in this regard. For example, it was alleged that some Chinese who are engaged in one of the projects entered the country with a wrong type of visa. There may be need to empower these and other related organisations in discharging their duties given the specialised nature of free trade zone. There Committees of various stakeholders (especially of the host communities) in place and this phenomenon is commendable. However, there is the need to empower the technical capabilities of the committees in order to ensure its effectiveness. Rigorous analysis and follow-up activities are required. For example, the local farmers' capacity for the supply of

paddy rice as input for Vee Tee Rice should be carefully analysed and appropriate measures should be taking that over-supply and under-supply are minimised.

## **LAGOS STATE**

### **I CHINA TOWN IN LAGOS**

Findings obtained from some staff of Chinese enterprises in the market revealed that the market is managed by International Cooperation Industry Nigeria Limited with its office located at Surulere area of the state. Going through the market, it was observed that the market consists of 120 shops shared between Nigerians and Chinese. Further investigation shows that three-quarters of the shops are acquired by the Chinese who were physically present at their various shops and employ an average of 2 Nigerians as shop attendants. Traders in the market deal in products such as textiles and apparels, lace materials, baby wears and toys, foot-wears, handbags, household utensils, personal effects, items for decorations, electrical appliances, art works, among others. These are light manufactures. Investigation revealed that some of the products are produced by Chinese firms in Nigeria, while majority of them are imported from China. The market receives daily, relatively high potential participants with various missions. Apart from the fact that the products and sellers are readily available at the market, relatively high potential buyers patronise the market. Other participants in the market are the transporters, food sellers and the market management. There is a branch of the Intercontinental Bank (PLC.) at the market and this is expected to facilitate financial transactions of the market participants.

### **II LEKKI FREE TRADE ZONE (LFTZ)**

The signing of a Memorandum of Understanding (MOU) between the Lagos state Government (represented by Lekki Worldwide Investement Limited-LWIL) and the Chinese Government (represented by Nanjing Jiangning Development Zone in the Jiangsu Province and the China Railway Construction Corporation) in 2007 marked the beginning of the Lekki free trade zone. Prior to the signing of the MOU, the Lekki Free Trade Development Company was incorporated in Lagos in April 2006 as a joint venture among CCECC-BEYOND, the Lagos State Government and the LWIL. It was registered by the Nigerian

Export Processing Zones Authority (NEPZA) as the developer, operator and manager of the LFTZ

The main missions of the LFTZ include the following.

- to develop an offshore economic growth zone,
- attract foreign investment,
- promote export,
- create job opportunities,
- minimise capital flight, and
- establish a one-stop global business haven.

In an attempt to provide infrastructure in the zone, construction of roads into the zone began in October, 2007. Other infrastructure put in place is dedicated power plant which is independent of the national grid to ensure regular supply of energy, and also water and sewage treatment plants. The LFTZ featured at international trade fairs including the one held in South Africa in September 2007 and World Conference of Free Zones held at Kuala Lumpur, Malaysia in November 2007.

Abundant land is available for industrial projects and the first phase consists of the development of 3,000 hectares. There are opportunities and access of investors to supply raw materials particularly for activities such as agro-processing, clothing and textiles, food and beverages, forestry, mining and pharmaceuticals. The incentives available to investors in the LFTZ include:

- 100% foreign ownership of investment;
- One-stop approvals;
- Zero import and export licenses;
- Tax holidays; and
- Unrestricted remittances of capital and duty-free importation of raw materials.

#### ***5.4 Impact of China-Nigeria Investment Relations***

A number of benefits accrue from FDI, which include augmentation of domestic capital; transfer of technology, knowledge and skills; promotion of competition and

innovation; employment and enhanced output, export and revenue performance. These must be weighed against their costs such as anti-competitive and restrictive business practices; tax avoidance and abusive transfer pricing; volatile flows of investment and related payments deleterious for balance of payments; transfer of polluting activities and technologies; and excessive influence on economic affairs with possible negative effects on industrial development and national security.

A country desirous of hosting FDI must of necessity institute policies aimed at maximizing the direct and indirect benefits as well as in minimizing the possible negative impacts. A litmus test for gauging the motive of FDI is to classify such investments into resource-seeking, market-seeking or efficiency-seeking. Efficiency-seeking FDI is preferred to other forms at least from the perspective of the host country. However, for a country to attract efficiency-seeking type of FDI macroeconomic stability must be ensured and distinct, predictable and easy-to-access policy environment including incentives must be instituted.

Giving the list of private FDI and the sectoral concentration, efficiency motive may not be the driving force of inflow of Chinese FDI in the Nigerian economy. The list of public FDI in Nigeria suggests resource-seeking motive. However, there are other categories of FDI that cannot neatly fit into resource-seeking class. These include those in the area of building infrastructure and manufacturing which can be classified as market-seeking.

A veritable channel for optimal benefit is in the involvement of indigenous entrepreneurs in the affairs of the particular firm. A joint venture has higher potential of positive impact in the host economy. Beyond, the involvement of indigenous entrepreneurs at the management level, local expertise and other work force are the channels through which technology is transferred and technological capacity is developed. However, Chinese firms in Nigeria have been criticized for being “closed” as they hardly employ local experts. There are even submission that they mal-treat their workers. According to a report, the conditions of employment of Nigerians in Chinese firms neither conform with the Nigeria Labour Laws nor to that of the International Labour Organisation (ILO). It was reported that Chinese companies such as Wahum Nigeria Limited and Galvanising Company Limited are firms with the most inhuman condition of service (12 hours a shift) and many casual workers. Also there is the familiar report on the September 2002 fire incidence at a Chinese-owned factory in Lagos in which about 40 Nigerians were trapped as a result of the locked up of building factory by a foreman. Besides, how reasonable was the compensation given to the victims of the incidence (if any)? The Report also alleged that technology transfer from Chinese FDI is

insignificant because most of the Chinese firms bring into the country finished products and complete equipment with Chinese technicians. In a nutshell the expected benefits may not be realized. The lesson is for the country not only to design appropriate policies and regulations but also to ensure that these are implemented.

Although some of the Chinese investments are in critical areas of the Nigerian economy especially in infrastructure (telecommunications, water, electricity, housing, etc.) hence they have high social contents. However, there are reservations about the activities of Chinese investors especially those who are engaged in manufacturing. Such complaints include sharp practices such as importation and production of sub standard products, and lack of respect for their workers.

However, the quest for oil and gas by the Chinese seems to be of importance in the resurgence of the current wave of relations. Consequently, Chinese nationals are not immune from the spate of social unrest in the Niger Delta (the area where oil and gas are located in Nigeria). Some of the Chinese oil workers were recently abducted by militants who are agitating for a more equitable distribution of resources in the country.

In summary therefore, perhaps the most important opportunity offered by Chinese FDI in Africa and Nigeria in particular is the increase in investment in transformation activities. It should be noticed that China can be very responsive to the complaints across Africa countries including Nigeria. For instance, Nigeria's complaint over the lack of technological and human resources development impact of Chinese telecoms investment in the country has been favourably responded to. However, there have been few and limited complainants which might be a reflection of limited capacity of the country to develop partnerships with Chinese FDI.

The challenge, therefore, is for Nigeria to invest the inflow of resources from the commodity booms in improving investment climate, developing human resources necessary to support investment in new industries and establish development banks necessary to provide financial support to nascent private investors. Towards this end, there must be good and transparent governance while implementing these initiatives in order to ensure that the desired outcomes are realized. Successful implementation of these initiatives under good governance will create necessary conditions for Chinese FDI to have significant backward and forward linkages in the Nigerian economy. It is important to state that, careful monitoring and evaluation processes, including requisite research must be carried out regularly to ensure



that Chinese and, indeed, FDI from other sources and in any sector are beneficial to the host countries.

### *Potential Gainers and Losers*

All economic agents (producers, consumers and government) in the country will benefit from the China's transformational investment finance in Nigeria particularly in the area of infrastructure and social amenities. Provision of adequate infrastructure in Nigeria through China's financial resources will improve investment climate and welfare in the country. This is expected to promote output, export, employment and government revenue. This idea presupposes that all projects are completed; there is absence of white elephant projects and corruption in the process. This is because some people may hide under the financing arrangement or connive with some Chinese firms to stash away the country's funds. The issue of debt accumulation and servicing is important because Chinese financing or loans may not be as generous as we might thought and induce to contract.

The positive revenue effect of Chinese FDI may not be realized by the Nigerian Government because of too many tax and other fiscal incentives as well as the possibility for tax evasion/avoidance by Chinese firms (as evident by their recent collaboration with some Customs Officials in the importation and open sale of contraband goods at the China-town at Lagos-which led to a temporary closure of the market) coupled with the permission to repatriate profits and incomes.

Massive influx of Chinese FDI into the country to produce goods and services at cheaper prices coupled with import of cheap commodities from China will enhance the welfare of Nigerians. Besides, the establishment of China's export processing zone should promote export and increased foreign exchange earnings. However, given that Nigerian firms are not competitive, massive influx of Chinese FDI into the country to produce goods and services may lead to closure of domestic competing firms, with adverse employment effect particularly where Chinese firms are fond of bringing in workers from their country. Also, the fact that Chinese firms in Nigeria bring in inputs from their own country and set up their own market outlets implies that there may not be any (or major) backward and forward linkages between Nigerian and Chinese firms. Besides, widespread contract awards to Chinese firms will cripple activities of domestic contractors. All these have to be considered by the Nigerian Government in a country characterized by high level of unemployment.

The issues of negative externalities associated with Chinese investment in Nigeria is worthy of mention. Oil exploration and production as well as manufacturing activities have been known to be associated with series of environmental problems. This is a major cost of Chinese investment to be borne by the host communities and producers in which such activities are located. There is therefore the need to ensure compliance of Chinese firms with social responsibility laws in Nigeria. Needless to say that domestic firms operating in sectors of interest to China (such as oil and gas, power, construction, manufacturing and services) may lose as a result of lack of competitiveness.

***Sector specific opportunities and Challenges faced by Nigeria due to the effects of growth of investment relationship with China***

There are a number of sector specific opportunities and challenges faced by Nigeria as a result of the increased investment relationship with China. Some of these specific opportunities and challenges are presented in Table 15.

**Table 15: Sector specific opportunities and Challenges facing Nigeria due to its investment relation with China**

A	OIL AND GAS SECTOR	
	OPPORTUNITIES	CHALLENGES
	Availability of funds and expertise for exploration and production	The likely increased environmental problem and the crises in the oil producing areas
	Increased production to meet the rapidly growing world demand for energy products -	Limited absorptive capacity and lack of linkages of this sector with the rest of the economy since the activities in this sector is highly capital intensive. Non-encouraging local labour absorbing tendencies and incentive system and the need for regulation to promote local employment, skill acquisition and technology transfer.
		Dominance of foreign investment and influence of the foreign investors on the economy
B	SERVICES SECTOR	
	OPPORTUNITIES	CHALLENGES
	Availability of funds, expertise and technology for services infrastructure development	Intense competition with local firms producing similar services and the associated job losses.
	Availability of funds, expertise and technology for improved service delivery.	Exploitative tendencies of foreign services providing firms.
	Competition promotes efficiency in service delivery and affordability	Inadequate infrastructure to cope with the rapidly growing demand for services
	Promotion of employment, skill acquisition and technology transfer	Non-encouraging local labour absorbing tendencies or practices and incentive system and the need for regulation to promote local employment, skill acquisition and technology transfer.

		Avoidance and evasion of taxes
C	MANUFACTURING AND CONSTRUCTION	
	OPPORTUNITIES	CHALLENGES
	Availability of funds, expertise and technology for industrial development	Intense competition with local firms producing similar products and with local contractors
	Production of cheap goods for domestic consumption and export	Assurance of the quality of investment
	Promotion of employment, skill acquisition and technology transfer	Non-encouraging local labour absorbing tendencies or practices and incentive system and the need for regulation to promote local employment, skill acquisition and technology transfer.
		Environmental pollution and other associated problems
		Avoidance and evasion of taxes
D	INFRASTRUCTURE AND SOCIAL AMENITIES	
	OPPORTUNITIES	CHALLENGES
	Availability of funds, expertise and technology for economic and social development	Avoidance of white elephant and abandoned projects
	Aid element of the investment promote social development	Corruption in the infrastructure contract awards
		Assurance of provision of quality infrastructure through effective monitoring and evaluation

## 6.0 Conclusion

The study has focussed on the China-Africa investment relation with a view to investigating the impact of such relation on Africa using Nigeria as the case study. Having examined the theoretical premise for such relation as well as the literature evidence regarding the impact analysis of FDI on host country, the study relied on the strengths of a methodological framework that permits the appreciation of all likely impacts: competitive/complementary, direct/indirect impacts to execute the study of the current China-Nigeria investment relation. Both the push and pull factors behind the subsisting relation between the two countries as far as FDI is concerned seem to suggest that Chinese investment in Nigeria is both market-seeking and resource-seeking in outlook. Based on the findings of this study as discussed extensively in the preceding section, a number of policy implications, lessons and agenda for the future China-Nigeria economic relations are worth noting.

Attempts to compromise the benefits of FDI should be persistently resisted by the Nigerian Government through active government engagement and negotiation with the Chinese government and investors. Good governance and macroeconomic environment in the country should be ensured so as to promote productivity and sustainability of investment. A country desirous of hosting FDI must of necessity institute policies aimed at maximizing the

direct and indirect benefits as well as in minimizing the possible negative impacts. A litmus test for gauging the motive of FDI is to classify such investments into resource-seeking, market-seeking or efficiency-seeking. Efficiency-seeking FDI is preferred to other forms at least from the perspective of the host country. However, for a country to attract efficiency-seeking type of FDI macroeconomic stability must be ensured and distinct, predictable and easy-to-access policy environment including incentives must be instituted.

There is need to ensure implementation of laws and regulations in Nigeria and to ensure compliance by the Chinese investors. Such laws include labour law, social responsibility law and local content requirement. The Nigeria Labour Congress and its counterpart in the private sector should ensure the observation of the Nigerian labour law by all firms including the Chinese-owned firms. Similarly, the Raw Material Development Council (RMDC) should see to compliance of the local content requirements (in terms of human and physical materials) by all firms especially the foreign ones. The Nigerian Investment Promotion Council (NIPC) and other relevant organisations such as the Nigerian Extractive Industry Transparency Initiative (NEITI) should ensure compliance with the social responsibility law in Nigeria.

Nigeria needs to invest the inflow of resources from the commodity booms in improving investment climate, developing human resources necessary to support investment in new industries and establish development banks necessary to provide financial support to nascent private investors. Towards this end, there must be good and transparent governance while implementing these initiatives in order to ensure that the desired outcomes are realized. Successful implementation of these initiatives under good governance will create necessary conditions for Chinese FDI to have significant backward and forward linkages in the Nigerian economy. It is important to state that, careful monitoring and evaluation processes, including requisite research must be carried out regularly to ensure that Chinese and, indeed, FDI from other sources and in any sector are beneficial to Nigeria.

As stated earlier, the idea that provision of infrastructure in Nigeria through China's financial resources will improve investment climate and welfare in the country and thereby leading to growth of output, export, employment and government revenue presupposes that all projects are completed and there is absence of white elephant projects and corruption in the process. This is because some people may hide under the financing arrangement or connive with some Chinese firms to stash away the country's funds. The issue of debt accumulation and servicing is important because Chinese financing or loans may not be as

generous as we might thought and induce to contract. Therefore there is the need to always employ technical experts that will conduct cost analysis so that contracts are awarded at minimum cost. Also, cost- benefit analysis of projects must be conducted to be able to be more scientific and realistic about our dealings with foreign investors and multilateral institutions.

Again, as mentioned earlier, the positive revenue effect of Chinese FDI may not be realized by the Nigerian Government because of too many tax and other fiscal incentives as well as tax evasion/avoidance by Chinese firms coupled with the permission to repatriate profits and incomes. Therefore there is need to generate in a scientific manner, a number of scenarios on the level or number of incentives that can be given to foreign firms that will not jeopardise the interest of the economy. Accurate data on the number, location and tax liabilities of all firms including the Chinese firms should be generated by the Federal Inland Revenue Service in collaboration with the Nigerian Investment Promotion Council and the Corporate Affairs Commission, while tax offenders should be sanctioned.

Widespread investment and contract awards to Chinese firms will cripple activities of domestic contractors. All these have to be considered by the Nigerian Government in a country characterized by high level of unemployment. Therefore some considerations have to be given to local contractors. They may be encouraged to partner with Chinese firms.

The issues of negative externalities associated with investment including those of Chinese in Nigeria is worthy of mention. Oil exploration and production as well as manufacturing activities have been known to be associated with series of environmental problems. This is a major cost of Chinese investment to be borne by the host communities and producers in which such activities are located. There is therefore the need to ensure compliance of all firms including Chinese firms with social responsibility laws in Nigeria (if any). Thus, Government can establish a body or an agency that will audit the performance of the organisations in terms of social responsibility. This will enable it to reward those that are performing well and sanction those that are not.

Owing to paucity of data at both the Federal and State levels to carry out detailed and comprehensive study of this nature. there is the need to enforce the relevant law that will enable the data gathering agencies of government such as the National Bureau of Statistics (NBS), Nigerian investment promotion Council (NIPC), Federal Ministry of Finance and Central Bank of Nigeria (CBN) to have access to important and necessary information for the evaluation of the benefits and costs of investment relation between Nigeria and China.

Chinese firms have been noted for hoarding information. The relevant ministries and department should be supported financially to gather information including those on China-Nigeria relations.

The analysis clearly shows that the engagement with China just like any bilateral relationship has some advantages and disadvantages and that optimal outcome of the engagement will depend on the policies and institutions that are put in place to maximize the complementary effects and to minimize the competing effects. The study shows that China is virtually everywhere in the country but information about its engagement and activities are fragmented. This is manifested the more in government, ministries, departments and agencies. There is therefore, the need to establish a coordinating body on China. This body, preferably a technical arm of existing body, should be empowered to scrutinize and evaluate agreements, memoranda and any other articles of association between Nigeria and China. The ultimate objective of the proposed body is to spell out the cost as well as the benefits of the proposed project and/or programme. This is similar to what a legal department would do to an agreement before initialising/signing. The proposed technical committee in its assignment must have taken into consideration domestically available resources including skills and ensure that as much as possible, the local content of the agreement is high enough not only for the purpose of generating employment for Nigerians, but also to develop their technological capability.

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## Appendices

**Appendix Table 1: Largest 15 Host Countries of Chinese Outward FDI, 2003-2006, Current USD (Mill) and Shares**

Country	2003	2004	2005	2006	Total	Share
					2003-2006	2003-2006
Cayman Islands	806.61	1286.13	5162.75	7832.72	15088.21	0.39
Hong Kong, China	1148.98	2628.39	3419.7	6930.96	14128.03	0.37
British Virgin Islands	209.68	385.52	1226.08	538.11	2359.39	0.06
Korea, Republic	153.92	40.23	588.82	27.32	810.29	0.02
Russian Federation	30.62	77.31	203.33	452.11	763.37	0.02
United States	65.05	119.93	231.82	198.34	615.14	0.02
Australia	30.39	124.95	193.07	87.6	436.01	0.01
Sudan		146.7	91.13	50.79	288.62	0.01
Germany	25.06	27.5	128.74	76.72	258.02	0.01
Algeria	2.47	11.21	84.87	98.94	197.48	0.01
Singapore	-3.21	47.98	20.33	132.15	197.25	0.01
Nigeria	24.4	45.52	53.3	67.79	191.01	0.00
Mongolia	4.43	40.16	52.34	82.39	179.32	0.00
Indonesia	26.8	61.96	11.84	56.94	157.54	0.00
Kazakhstan	2.94	2.31	94.93	46.0	146.18	0.00
Total (All Countries)	2854.64	5498.01	12261.17	17633.97	38247.79	1.00

Source: Kolstad and Wiig (2009), P.4

**Appendix Table 2: Chinese FDI to African Countries, USD (Million)**

Country	2003	2004	2005	2006	Total
					2003-2006
Sudan		146.7	91.13	50.79	288.62
Algeria	2.47	11.21	84.87	98.93	197.48
Nigeria	24.4	45.52	53.3	67.79	191.01
South Africa	8.86	17.81	47.47	40.74	114.88
Zambia	5.53	2.23	10.09	87.44	105.29
Congo, Democratic Republic of	0.06	11.91	5.07	36.73	53.77
Guinea	1.2	14.44	16.34	0.75	32.73
Ethiopia	0.98	0.43	4.93	23.95	30.29
Egypt	2.1	5.72	13.31	8.85	29.98
Mauritius	10.27	0.44	2.04	16.59	29.34
Angola	0.18	0.18	0.47	22.39	23.23
Congo, Rep.		0.51	8.11	13.24	21.86
<b>Total</b>	<b>74.81</b>	<b>317.43</b>	<b>391.68</b>	<b>519.86</b>	<b>1303.78</b>

Source: Kolstad and Wiig (2009), P.5