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CHINA AND GLOBALIZATION: INTERNATIONALIZATION OF FIRMS AND TRADE IN SERVICES

Our contribution focuses on the transformations of the Chinese economy, on its growth trajectories, notably its internationalization, which was made possible by the adoption of an export-led growth model followed by a catch-up and export of good to higher value-added.
Foreign direct investment played a decisive role in this process. Inbound capital has contributed to the development of new sectors (automotive, information technology) and new specializations. Financial resources accumulated by China, then, fueled the outflows of capital in the form of acquisitions and greenfield investments around the world, especially towards developed market economies.
After recalling the phases of the transformation of the Chinese economy, the importance of Chinese outgoing FDI and their contribution to the evolution of trade in services between China and the rest of the world, the recent development of trade in services, which are heavily dependent on FDI is analyzed.
JEL: F21; F43; O1; O4; 053

The great Chinese growth that has been going on continuously and regularly for more than four decades is constantly calling on specialists, economists, political scientists, and historians. China, a "developing" economy, the most populous in the world, which introduced a Marxist-Leninist-type political system after a long civil war, went through contrasted experiences of socialism to forge, ultimately, a model of "market socialism with Chinese characteristics" a mix of pro-market reforms with the maintenance of an important state sector, the absence of "pro-Western" political reforms (rule of law, democracy).

Several factors explain this success. Among these, one should emphasize the opening of the Chinese economy and the strategy of specialization that supported it. On the one hand, economic decentralization and the mode of governance, notably the state sector, on the other, the pursuit of an export-led growth model. This has led to rapid economic growth, leading to the specialization of the Chinese economy in the production of low value-added goods ("the world's workshop"). At the same time, in the context of openness, China has attracted foreign direct investment in order to accelerate its economic catch-up in many sectors, leading the country to become an exporter of more higher value-added products

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and services. Over the past four decades, the strategy of openness has borne fruits. China has become the world's largest exporter, changing the structure of its exports in terms of added value, in sectoral terms (from industry to services). Foreign direct investment, both inward and outward, contributed greatly to these changes. The growing importance of trade in services illustrates the development of China's specialization.

After recalling the phases of the transformation of the Chinese economy (Section 1), the importance of Chinese outgoing FDI and their contribution to the evolution of trade in services between China and the rest of the world (Section 2). The recent development of trade in services, which are heavily dependent on FDI is then analysed (Section 3).

1. Reform and New Growth Model

Outward opening of the Chinse economy which has gradually taking place in the early 80s of the last century has had two consequences: the reception of foreign direct investment in priority sectors through the creation of joint ventures with mixed capital in order to favor technological catch-up (electronic, automotive, telecommunication) with a strong impact in terms of diffusion and spin-off in the industrial environment. The export-led growth strategy initially favored low value-added products, using unskilled and heavily exploited labor, gradually replaced by more sophisticated products. The undervaluation of the national currency (Renminbi) has helped to maintain a competitive exchange rate and stimulate export growth, it has encouraged the accumulation of large financial reserves and the creation of sovereign wealth funds, instruments today supporting and financing the strategy of acquiring foreign assets. At the domestic level, these reserves have enabled the financing of overinvestment policies in infrastructure, transport (railways), construction, steel plants.

These policies have had many positive effects. The high and sustained growth rate of about 10% per year over the last forty years has led to a clear increase in the country and in the general population with a significant reduction in the poverty line, particularly in the countryside. It spread unevenly between coastal cities and the interior, between urban and peasant. An urban middle class appears with its consumption requirements, access to new types of goods, which fuels the activity of many new areas. New problems arise concerning social policy (protection system, retirement), the sedentarisation of the mobile workforce (*hukou*). Economic activity regularly produces bubbles (real estate) and macroeconomic regulation must regularly arbitrate between stimulating activity, controlling inflation and halting sectoral imbalances. The informal sector is still deployed and continues to circumvent government regulations (shadow banking), corruption is endemic.

At the international level, the policy of openness and specialization has greatly changed the flow and structure of trade. In just three decades, China has become the world's second-largest economy; It is on the verge of overcoming the United States. It has become the leading producer of cars; It is in the process of acquiring dominant positions in the electronics and telecommunications sectors in terms of market share. Today, Chinese firms are launching the onslaught of the global market both to acquire resources (materials, technologies) to conquer new markets. Workshop of the world (production with low added

value) China intends to become also the office and the financier of the world. China is now present in many markets and is in a position to control and acquire strategic firms in major market economies, commodities in southern economies. Its financial reserves and the importance of its foreign trade allow it to take a growing place in the international capital markets.

Can this growth model continue at this rate? Can China maintain an export-led growth strategy as wage increases increase the cost of exports, as global demand stagnates? Does the ongoing technological catch-up (R & D spending increases) help to reduce the remaining gap and in some cases continues to increase with the most developed economies? Can Chinese leaders support economic activity only by injecting massive amounts of money into infrastructure financing to support growth? Will the necessary pro-market reforms announced by the leaders (interest rate liberalization, capital account liberalization, land reform, capital allocation mechanism, elimination of subsidies, privatization) be applied in whole or in part at a homeopathic dose? These are some questions that arise as the Chinese economy has reached a stage of its development which requires an adaptation of the model that has ensured this great and long economic growth, leading China to become, in volume of production, the first world economy .

To explain the dynamics of Chinese growth, one must look at the "mix" of the reform, both economic and political. Economic first of all by using an abundant and underpaid labor, taking advantage of undervalued prices of products exported through the manipulation of exchange rates. The prevailing social system constrains the workers, a large part of them are exploited workers who have no status, come from the countryside (the *Hukou*), do not benefit from social protection. On the other hand, there are plenty of specialized workers shortage leading to wage increases in many regions, pushing labor-intensive industries to relocate to countries with lower labor costs.

The counterpart of selling low-cost products leads to financial surpluses that are not firstly redistributed into the economy (social protection financing). They provide funds to sovereign wealth funds to invest in the economic priorities set by the government. If redistribution occurs, it takes place at the margins, it takes the form of corruption (transition from the state sector to the private sector). It is therefore the State Party that is at the heart of the redistribution of resources, which decides which priority sectors to develop, the technologies to be acquired to ensure the catching-up and upgrading of domestic firms. The Chinese financial sector, which is little open (in spite of commitments resulting from WTO accession) and in the hands of the government, facilitates the financing of the big industrial groups in which the economic elite exercises control. Most of the large Chinese firms that invest abroad, especially in the commodity sectors, receive preferential financing.

Over the last decades, China has acquired a hegemonic position in various economic and political fields. Its growing raw material needs translate into foreign direct investment in developing or semi-developed countries (south-south relations), massive purchases of products, which have resulted in some countries in Latin America to reprimarization (Brazil). The non-binding regulation of trade (WTO) favors the entry of Chinese products at lower prices and upsets the specialization of many countries including developed countries. In this context, China has been a great beneficiary at the same time as an active participant in globalization.

2. China and the globalization process

Globalization has led to a new phenomenon which attracts the attention of scholars, namely the internationalization of firms from emerging countries such as China. These firms are still limited in number and the volume of capital invested. But they are entering different markets in the North and the South, in search for production factors (material resources, technology and human capital), as well as sales outlets. The accumulation of financial resources, along with technical and managerial know-how through industrial cooperation with foreign companies operating in these emerging countries and the spin-offs this creates, all favour the investment in greenfield sites, as well as the acquisition abroad of assets that are sometimes prestigious (see for example the purchase of Volvo by the Chinese car producer Geely).

The mainstream press views these trends as a threat. Western firms are seeking to protect their technology, and governments are putting into place rules limiting the entry of foreign capital (the United States). According to the BCG *New Global Challengers* inventory, there are no less than 43 Chinese firms among the top 100 companies from the most dynamic emerging countries, which are operating in several sectors, running from energy to information technology and financial services. These firms are directly or indirectly controlled by States, and some are associated with inter-governmental contracts, especially in Africa which helps their entry into markets.

The internationalization of Chinese firms and the development of their operations in various continents is a new phenomenon which has arisen during the last two decades. This rapid progress is linked to the strong GDP growth recorded by China over several decades, and which has followed its economic reforms and opening. Having been the main recipient of FDI, China is today one of the main new sources of FDI in the South). Outward FDI growth rates from China in recent years have converged on rates of inward (Figure 1)

It must be stressed that this move to internationalization is not unique to China. The BRICs, which are among the main emerging market economies, have a certain number of companies that are spreading internationally, both into the developed economies (South-North), as well as into the developing economies (South-South), via greenfield investments and acquisitions. Most of the Chinese firms are “national champions”. They have expanded thanks to a number of factors: innovation, and specialization in protected markets, the development of internal competencies, market size, favored access to finance from banks that have monopoly positions, the nature of regulation, the exchange rate, specific industrial policies that target certain sectors, research and development (R&D) policies. Furthermore, the continued appreciation of the Chinese Yuan – the Renminbi (RMB) – in recent years, against the US dollar and the euro, before falling back recently has cut the costs of buying up western companies, just as it raises domestic costs which today push Chinese firms that are labor intensive to locate to offshore production (e.g., to Vietnam, and Cambodia).

Figure 1

Chinese inward and outward FDI flows (in $ billions)

Source: UNCTAD.

To be sure, in terms of the numbers of companies and volumes of flows, FDI from emerging countries, including China, are still modest (UNCTAD, 2016). But China accounts for the lion's share today, and outperforms other emerging nations both in the number of new (greenfield investments) and acquisitions: this is true for the sectoral distribution of FDI as well as its location across the five world continents. The *Fortune Global 500* ranking of major global companies includes 61 Chinese firms (including 4 from Hong Kong), 8 Indian companies, as well as 7 firms from Russia and Brazil. The Chinese firms, of which nearly 80% are state enterprises, belong to nearly all sectors, ranging from mining and oil extraction to banking, passing via electronics, capital equipment and transport.

How is this strong growth to be explained? Is there a link to the massive inflow of FDI into China, which played a vital role in technological catch-up and the appropriation of know-how, followed by the rise of Chinese outward FDI? What are the specificities of China's industrial model that favored this expansion, and which allowed the emergence of such a large number of companies capable of competing in certain niches with the major multinationals from the developed world? What are the specificities of these countries in comparison with their counterparts in the developed market economies?

A few Chinese companies today hold dominating market shares in developed world markets (Haier, Huawei). Others are undertaking technological breakthroughs via acquisition strategies, which allow them both to obtain technology and to position themselves in new, competitive market segments that are more profitable, including within China itself (Geely). Other firms, however, have failed or have run into difficulties integrating their acquisitions or greenfield investments within their global strategies.

FDI in China as a vector of modernization

China's hosting of FDI has played a role in accelerating its economic development, even if it has at times been viewed negatively by certain observers (Huang, 2003). In contrast to Eastern Europe, FDI into China has been strongly regulated (in terms of volume, ownership and the control of joint ventures, regional distribution, the search for agglomeration effects, and links with local government industrial policies).

In contrast to Japan and South Korea, China initially based its modernization strategy on welcoming western FDI (from the United States, Europe and other Asian countries), in the hope of acquiring technology it did not have. In Japan and South Korea, company upgrading took place through a process of "reverse engineering", a process based on first mastering, then enriching and developing standard technologies, sometimes by achieving significant technological leaps. This process was also supported by adopting strategic industrial policies, that were targeted and cooperative (State-Enterprises), aimed at growth technologies (electronics). In China, domestic firms were only able to benefit from the spin-offs derived from the presence of western firms, in a second phase, once these firms had been established in the country and had created networks with suppliers. Only then could Chinese firms gain new skills and enter domestic markets which had been dominated by foreign companies. Low entry barriers in many areas, as well as the industrial policies conducted by central, provincial and municipal governments, helped with the process of benefiting from spin-offs, company acquisition and the upgrading of local firms. Lastly and most recently, innovation policies and a significant rise in R&D have sought to accelerate the catch-up of Chinese firms through access to technology, to achieve an increase in their performance in both domestic and international markets.

In the automotive industry, for example, Chinese partner firms have often played a passive role, acting as mere (neutral) platforms, providing grounds, plant, and labour to foreign operators. The foreign partners acted in the market (developing sub-contracting and distribution networks), while the Chinese partners took care of the bureaucracy (relations with authorities). Strongly competitive environments (low entry barriers) and strong market growth facilitated the entry of numerous competitors – public, semi-public and private – into the sector, helping raise supply and reduce costs (Richet & Ruet, 2008).

Inward FDI has played an important role in the adjustment of firms and of trade. It generates more than half of Chinese exports and imports, accounting for 30% of industrial output and creates 22% of profits in the industrial sector, while only employing 10% of labour, given its high level of productivity. Though it is hard to evaluate spin-off effects on other sectors, which are indeed real, industries receiving FDI do have higher levels of productivity. Inward FDI has contributed positively to the strong growth of GDP. The central government has been able to combine a strong policy of regulating FDI, with a certain level of decentralization regarding hosting, attraction, and the adoption of local industrial policies at the regional and municipal level, as shown by the car industry.

It may therefore be asked whether FDI has allowed China to bridge the gap with the developed market economies. It is hard to reach a clear and unequivocal view on this, due to the differences between sectors in terms of their foreign presence, the nature of markets, technologies and the degree of competition.

The impact of industrial cooperation is appreciated in a qualified way by the Chinese authorities. They view it as an essential contribution to the modernization of their economy, while underlining its limited impact on the shift to high value-added production, the appropriation of know-how, and specialization in numerous sectors.

Sino-foreign cooperation through the creation of joint-ventures has not induced a rapid transfer of technology, despite agreements concluded between operators.[3] Chinese firms file less patents than their counterparts and innovate less. A large share of Chinese exports, be they upstream or downstream in the production process, are of low value-added products, even though companies with foreign capital account for nearly three-quarters of high value-added exports (OECD, 2012).

There are several causes of this limited transfer:

- The protection of intellectual property (one of the main points of disagreement between China and its western partners, along with the undervaluation of the RMB). It is notoriously deficient and pushes western firms to limit transfers.
- The nature of agreements and the behavior of Chinese partners. In many cases, Chinese partners have acted passively during the launch phase of cooperation. This reduces internal and external spin-offs (the transfer of knowledge, the appropriation of know-how).
- China's entry into the WTO has allowed foreign firms to protect their know-how better, especially by creating subsidiaries which are 100% foreign owned.

Nearly half of all Chinese exports are of low value-added. Exports also contain a high level of imports: more than 25% for automotive engines and more than 45% in information technology (OECD, 2012). The decision by the government to raise R&D spending substantially (which accounted for 1.83% of GDP in 2011), is aimed at accelerating the acquisition of technologies that China still lacks.

These facts explain why the Chinese government has a selective policy concerning FDI inflows, which focuses on the impact they could have in terms of providing technology to host companies. The Catalogue of Foreign Investments published by the Council of State Affairs sets out sectors targeted by the authorities. Such targeting reveals the level of technical competence reached by Chinese firms in several sectors (chemicals, pharmaceuticals, metallurgy, green technologies, textiles, high-voltage electricity distribution, etc.). It shows the threshold effects concerning technological improvements achieved and the volumes of production envisaged in targeted sectors. Today, FDI constitutes a certain form of subsidiarity in the eyes of the government: how is technology integrated into the capacities of Chinese firms?

These choices draw on the priority of the 12th five-year plan, which sets out seven emerging strategies: alternative energies, new materials, biotechnologies, new generations in the field

[3] The joint-venture format has evolved, especially in less strategic sectors. Thus, in the automobile industry, firms producing component parts may be 100% owned by foreign investors, though for final assemblers the limit is 49%.

of new technologies, environmental industries, and alternative automobiles (electric cars). Today, these sectors account for only 4% of output, but are planned to rise to 15% by 2020 (BBVA, 2012).

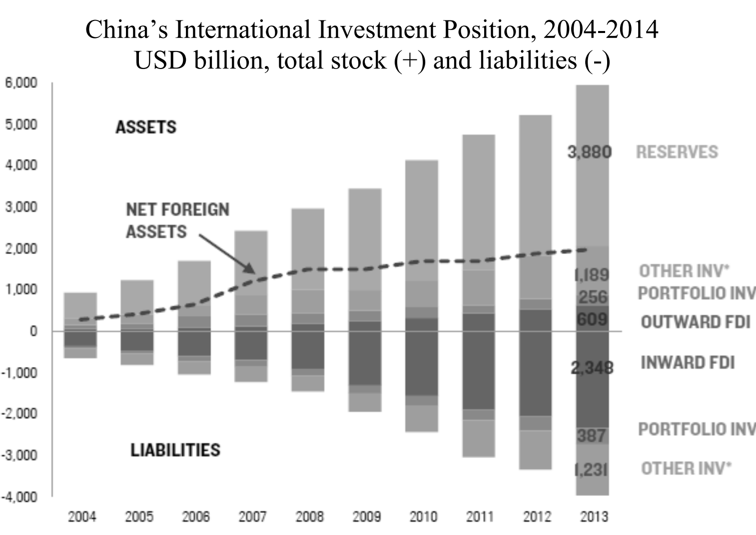
Chinese OFDI: its Growth, Origin, Sectoral and Geographic Distribution

The Chinese economic model which has developed over the last three decades is different to those of Japan and South Korea, at least as far as its first phase is concerned in terms of access to technologies, the accumulation of competencies, the role of the State and the implementation of catch-up policies.

China has specialized in the production of low value-added goods, and has applied a mercantilist policy. As a result, it has been able to accumulate in a few decades financial and monetary surpluses which it can use to achieve other objectives. These surpluses include sovereign wealth funds, the purchase of foreign securities, and FDI. The latter still only accounts for a small share of these assets (Figure2)

Figure 2

China's International Investment Position, 2004-2014
USD billion, total stock (+) and liabilities (-)



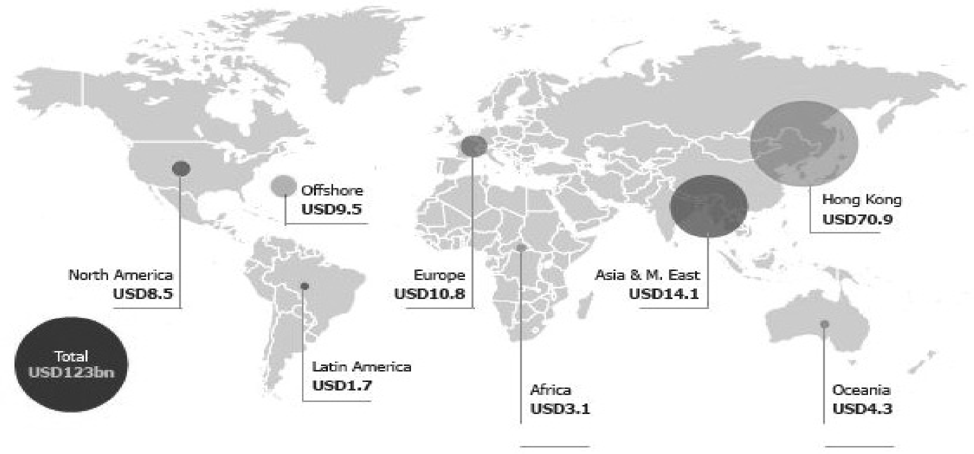
Source: Rhodium Group

Despite the strong growth of OFDI in the developed economies, levels still remain low. In contrast, the rise of China's OFDI has led to worries about its control of strategic assets, which are often considered as national, industrial jewels in some countries, such as the purchase of Volvo by the Chinese car firm Geely (Balcet, Wang, Richet 2012), and worries about China's growing influence in the major developed. The acceleration of the pace of Chinese OFDI is due to a number of factors including the strong growth of the Chinese economy which requires increasing raw materials and fossil fuels (oil and gas).

Over the last twenty years, inward FDI for the developed market economies (DMEs) has continued to rise, accounting for 69.9% of the global IFDI stock ($12,501 billion), compared to 27.9% for the developing economies. The Asian economies account for 16.3% of this total, and China alone for 2.7%. For OFDI, the DME's share fell from 93% to 82.3%, whereas the developing countries' share rose strongly from 6.9% to 15.3%, with Asia's share of the world stock rising from 3.2% to 11.5%, and China's from 1.1% to 4.5% (UNCTAD).

Figure 3

The Evolution of Chinese FDI Abroad



Source: Ernst & Young, China Outlook, 2015.

The growth of Chinese outward FDI has been marked by several phases (Hanemaan & Rosen, 2012) (Figure 4). Each phase has been linked to political choices and central government incentives ranging from strict control, to gradual relaxation and then encouragement with adoption. At the start of the 2000s, proactive policies known as "going global" were adopted as part of the 10th development plan. In the second half of the last decade, these policies contributed to accelerating the internationalization of Chinese companies across all continents.

Box 1

Chinese Round Tripping Investments

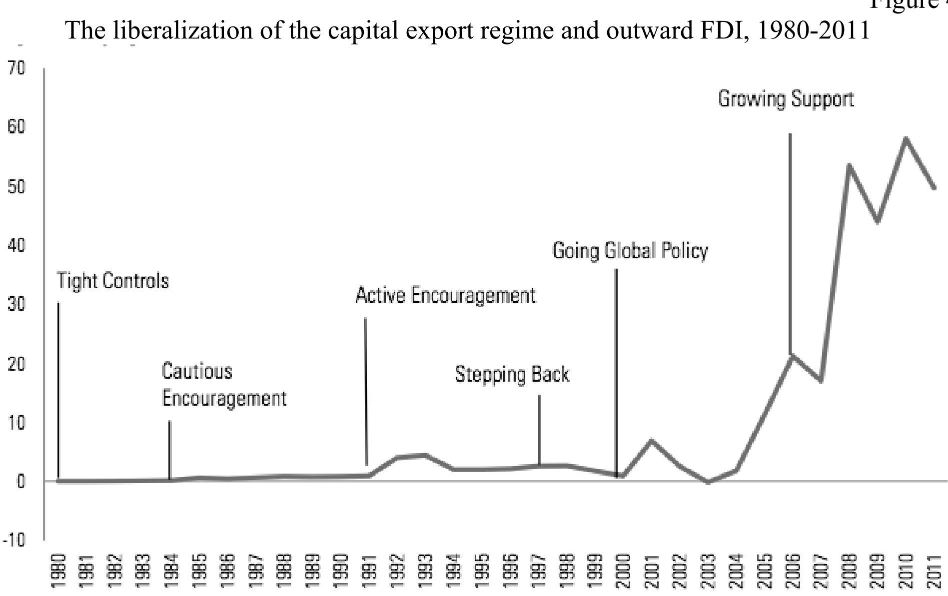
There is a statistical bias when analyzing the flow of Chinese outward foreign investments and assessing the reality and importance of round tripping investments (Sutherland and Matthews, 2009). An important part of Chinese outward FDI is located in tax heavens. Chinese investors use these locations (Hong Kong, Cayman Islands, British Virgin Islands) in order to take advantage of either of local taxation policies, to escape capital control on the home market. Reintroducing capital in China favours the change of original companies into foreign-invested firms with tax advantages.

The location abroad can also enjoy several financial benefits: valuation of assets, access to external financial markets, greater facilities for raising capital in other financial centers.

63% of the total Chinese FDI in 2010 went to Hong Kong (87% of Chinese FDI in Asia). The second largest regional stock is Latin America and the Caribbean (14%) with both tax havens mentioned hosting for 92% share of the Chinese FDI in this region.

Figure 4

The liberalization of the capital export regime and outward FDI, 1980-2011



Source: Hanemaan & Rosen, 2012.

Table 1 illustrates the recent sectoral growth, and Figure 3 shows the geographical distribution of Chinese outward FDI. These figures raise a few points. The first concerns the two types of investments, notably *round tripping investments* from Hong Kong made by Chinese firms. These concern capital flows which are not repatriated to China, but which stays in Hong Kong to avoid foreign currency controls by the central government. Such

Hong Kong investments are largely understated in official Chinese statistics, only 4.9% (*China Daily*, 31/9/2012). Subsequently, the search for tax havens in the Caribbean (the British Virgin Islands and the Cayman Islands) has led to the creation of platforms for investments in third countries, notably in Latin America, which is a favored destination of Chinese outward FDI, especially in the raw materials sector, as well as in agriculture.

Table 1

Growth of Chinese Outward FDI by Sector

	2014 YoY	CAGR (2011-2014)
Secondary industry		
Mining	- 33.3%	4.6%
Manufacturing	33.2%	10.8%
Construction	-22.2%	27.2%
Supply of electricity, gas and water	159.3%	-2.0%
Tertiary industry		
Wholesale and retail	24.9%	21.0%
Transport, storage and post	26.2%	17.6%
Hotels and catering services	3rd 197.9%	27.9%
Financial intermediation	5.4%	37.9%
Real estate	67.1%	49.6%
Leasing and business	36.1%	12.9%
Health, social security and social welfare	1st 800.6%	1st 188.5%
Culture, sports and entertainment	67.0%	2nd 70.4%
Information transmission, computer services and software	126.3%	3rd 59.8%
Scientific research, technical service and geologic prospecting	-6.9%	33.2%
Management of water conservancy, environment public facilities	2nd 280.6%	29.3%
Other services	68.4%	43.0%

Source: KPMG, China Outlook 2016.

The sectoral distribution of Chinese OFDI involves a large variety of sectors, with four leading sectors accounting for 75% of all investments and the importance of the recent shifting toward the tertiary sector.

Part of China's outward FDI is directly linked to the expansion of commercial activities related to exports (transport, insurance and financial services). The search for raw materials,

especially hydrocarbons, is also important. China's top multinational firms in terms of capitalization and turnover are operating in these sectors. They are present in Asian markets, the Middle East and Canada. The search for strategic assets is being carried out to meet the supposed limits, as far as China is concerned, of the transfer of technology and appropriation of know-how provided by foreign multinationals based in China. This seems to have slowed down since China's accession to the WTO, because of the greater possibilities of protecting intellectual property.

Lastly, as far as the legal form of companies is concerned, they are mostly State-owned enterprises (nearly 70%), or publicly listed companies in which the State has a share, influencing the internationalization strategy of these firms.

The Motives of Chinese Companies' Internationalization

The internationalization of Chinese firms as part of a slow process, linked to the phases of economic reform and openness, two choices by the central government and to incentives that have been introduced regularly. There is a strong correlation between institutional reforms, political liberalization and the development of outward FDI as shown in Figure 4.

Four major motives have pushed Chinese firms to internationalize

- *Access to markets*

Access to markets, especially when nearby, follows trade flows and the penetration of markets by Chinese exports. Entering a market is made easier thanks to accumulated know-how. It is a way of circumventing tariff barriers, creating local or regional distribution networks, and getting close to regional markets which are expanding strongly. Another motivation is linked to strengthening competition and the rise in domestic overcapacity, which reduces firms' profit margins. Through local investments, Chinese firms acquire new know-how (which is produced outside the domestic market) and can experiment with their internationalization strategies by limiting risks and costs in case of failure. The accumulation of competencies acquired in the market in areas of medium technology (consumer goods) or high-technology (ICT) has acted as a springboard for the internationalization of certain firms, some of which have become world leaders in their field, such as Haier, Huawei and Lenovo, which are amongst the best known. In contrast, other companies which had the same levels of competence domestically, sometimes with government help, partly failed in their internationalization strategy via acquisition (TCL, and SAIC in Korea). Such failures have been due to the fact that acquisitions have been difficult to integrate into groups' strategies, or because the acquiring company pursued and an asset stripping strategy (acquiring firms with the aim of only controlling a part of them).

- *The search for efficiency*

This factor was less important at the start of the internationalization process, given China's low production costs. The rise in domestic costs in recent years, however, has led to firms relocating to other Asian countries (Vietnam and North Korea), in labour-intensive industries (textiles). Today, in the province of Guangdong, the rapid and consequential rise

in wages (up more than 20% within 2 to 3 years) has contributed to offshoring to neighbouring economies with lower labor costs.

- *The Access to resources*

This is certainly a leading motive of internationalization by Chinese firms. The Chinese economy has to ensure the availability of resources needed for double-digit growth, taking into account both the limits and depletion of national resources (with the exception of coal) and its plant and equipment, which are largely run down and which consume high levels of raw materials. The technological choices set out within the framework of the 12th plan (2011 to 2015) stress the use of substitutable energies, but the energy transition risks taking a long time. There are several State-owned enterprises among all the top internationalized firms, which are actively supported by the central government, and which operate in oil and natural gas extraction. The access to resources is not constrained by proximity. Chinese companies are working at a global level: in the Americas, Africa, the Pacific, and Central Asia. Nationalist conflicts in the China Sea, between China, Vietnam, the Philippines and Japan have been sharpened by the discovery of oil reserves under the seabed.

- *The search for strategic assets*

The search for strategic assets has become one of the leading preoccupations of Chinese firms, both to consolidate their strengths in foreign markets as well as to acquire technologies they have not been able to obtain through cooperation with foreign MNCs present in China, or due to the weaknesses of China's innovation system. The financial reserves which China has accumulated, along with the liberalization of regulations on outward FDI (reductions in controls on capital exports) on the one hand, and the fall in foreign asset values due to the international financial crisis on the other hand, have greatly increased opportunities for acquiring firms abroad. Accordingly, the "shopping list" of Chinese investments has lengthened, especially in Europe and the United States, which in turn has led to protectionist policies concerning certain sensitive assets (telecommunications). The acquisition of technology and of foreign brands has been a means to accelerate the rise of Chinese companies and improve their foreign reputation. Chinese firms have been able to obtain assets entirely in this way (companies and their networks), or just segments, which often have a technology content and which can be repatriated and integrated into production in China (sometimes accompanied by the temptation of asset stripping). This is an advantageous means of entering markets, allowing Chinese firms to acquire reputation and accede to technologies they do not have. Through mergers and acquisitions, Chinese companies have thus been able to acquire assets they seek to integrate in their global strategy.

By compiling data on outward FDI undertaken over a number of years, Chinese economists have highlighted the motives of Chinese firms. Two motivations standout in particular: the search for resources, and the search for strategic assets.

Some theoretical interpretations of the internationalization strategies by Chinese firms

For many specialists, the internationalization of Chinese firms can be explained by the

domestic institutional context in which it is occurring. This process seems to confirm the "international investment path" paradigm of Dunning, who established a link between domestic growth and increasing FDI. The other explanatory factor follows from technological and managerial spin-offs introduced by the presence of numerous Western foreign direct investments in China over the last three decades.

The internationalization of companies can be understood within a threefold context:

i)the profound reform of the Chinese economy, ii) the internationalisation strategy expected and encouraged by the state and applied to companies, and lastly iii) the importance of institutional changes, the interactions they have provoked by providing actors with greater room for manoeuvre. Companies which internationalize benefit from direct support, profit from opportunities, and know how to use their autonomy by drawing on experience accumulated over the years, within a competitive environment created by economic reforms.

The growth of Chinese FDI is very recent. It only really took off in volume terms, both in the number of acquisitions as well as greenfield investments, when China joined the WTO in 2001. This phase of acceleration was preceded by the accumulation of competencies within the framework of successive reforms concerning Chinese regulations governing foreign investment. State policy has changed considerably in recent years. It has created a favourable environment, rather than fixing strict rules to guide firms wishing to internationalize.

A distinctive characteristic of Chinese MNCs lies in the way firms acquire skills, as the necessary prerequisite to undertaking internationalization. To Dunning's OLI paradigm (*Organisation, Localisation, Internalization*) should be added to the LLL model (*Linkage, Leverage, Learning*) by Mathews (2002), to account for this process. The latter shows how cooperation with high value-added firms, on a contractual basis stretching out over time, has allowed Chinese firms to take advantage of leverage and accelerate their apprenticeship and skills' development.

In the context of globalization, which is characterized by the globalization and disintegration of the international value chain, the apprenticeship and accumulation of competencies have become easier. Despite their lack of resources compared to Western multinational companies, Chinese firms have accomplished their internationalization successfully.

Williamson and Yin (2010) complete the analysis of institutional factors favouring the internationalization of these firms. The authors integrate two dimensions: positioning in the market and the mobilization of resources to explain how firms generate their competitive advantage. Companies which internationalize mobilize three types of capacities:

- cost innovations by using cost advantages of domestic firms (i.e., the capacity to produce while cutting production costs), yet still maintaining quality;
- combined capacities in offering markets redefined products to integrate technology, leading to low costs;

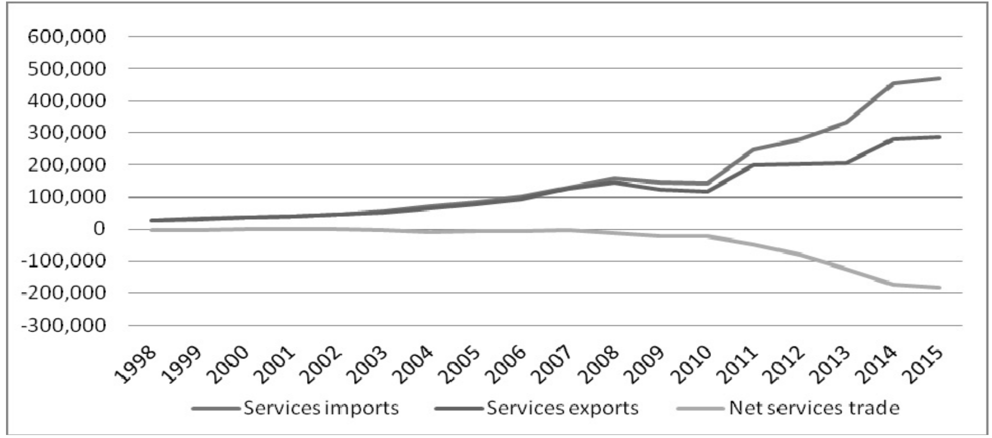
- dynamic capacities in terms of adjustment in the face of uncertainty by drawing on the high levels of flexibility, a quick learning curve.

3. Evolution of China's trade of services

China's participation in the world trade of services has seen rapid growth in the past few years, making China now the second largest economy in terms of total services imported and exported. According to the MOFCOM[4] (Ministry of Commerce of China), China's services trade reached $770 billion in 2016, with an annual growth rate of 14.2%. However, the deficit on its services trade balance has also grown significantly, as an increase in imports continued to exceed the increase in exports (Figure 5). In 2015 China's services deficit was 1/3 of the size of the trade surplus, up from less than 1% in the early 2000s, making it an increasingly important component of the current account balance. As an example, the services trade deficit between China and the US, China's first trade partner, reached $52.3 billion in 2016. The services trade deficit between China and the US has existed since years, which in fact contra-balanced the goods trade surplus between the two countries.

Figure 5

Evolution of China's trade of services (1998-2015)



Source: OECD.

For the year 2015, according to the MOFCOM[5], China's total import and export services amounted to $713 billion, with an increase of 14.6% over 2014; of which services exports amounted to $288 billion, with an increase of 9.2% compared to 2014; services imports were $425 billion, 18.6% higher than 2014; services deficit was still considerable, at $136 billion. In terms of proportion, services accounted for 15.3% of the total trade (import and

[4] http://tradeinservices.mofcom.gov.cn/g/2017-03-01/295405.shtml

[5] http://zhs.mofcom.gov.cn/article/Nocategory/201605/20160501314855.shtml

export of goods and services), 3% higher than in 2014. Exports of services contributed to 11.2% of total exports and imports of services to 20.2% of total imports, both higher than in 2014. In 2015, China ranked the world 2nd after the US regarding the services imports and the world 3rd for services exports after the US and the UK (Table 2).

Table 2

Global trade of services in 2015

	Export ($ bn)	Share (%)	Import ($ bn)	Share (%)
World	4675	100.0	4570	100.0
USA	690	14.8	469	10.3
UK	341	7.3	205	4.5
China	288	6.1	425	9.6
Germany	246	5.3	292	6.4
France	239	5.1	224	4.9
Japan	158	3.4	174	3.8

Source: WTO, MOFCOM.

China's trade in services is mainly concentrated in the US, the EU, Japan, Hong Kong and ASEAN. Hong Kong is the largest services export destination for China, accounting for 10% of the total in 2015, followed by South Korea and the US (both around 6%). Tourism is the largest sector of services exports to Hong Kong and the US, accounting for nearly 50% and around 30% respectively. It is followed by transport services, owing to China's strong goods trade linkages with both. In general, at present, China's service industry is concentrated in the transportation, tourism, construction and other labor-intensive and resource-intensive traditional sectors. The technology-intensive modern service industry in China has started not long ago. Therefore the relative weight of services in information technology, R&D design, process management, finance and insurance, technical advice outsourcing is still very limited in China's services exports. Meanwhile, since the last five years, the weight of China's offshore service outsourcing in total exports has begun to rise slowly, thanks to the strong promotion at all levels of government.

Table 3 shows the sector distribution of China's services imports and exports in 2015. Travel and tourism present the largest services exports sector in China, taking up to 40% of the total services exports in 2015, with an average growth rate of 14% since 2000; arrivals from Hong Kong accounted for 60% of overall visitor arrivals in 2015 (HSBC). Given its geographic dimension, ethnic diversity, history and cultural heritage, and the fast modernization of its society and the development of some of the world's biggest mega metropolitans, China has been attracting more and more foreign tourists and businessmen. However, travel services imports more than doubled the exports in 2015 compared to 2014, taking up to 62.5% of total services imports and contributing significantly to the services trade deficits. From 2000 to 2015, China's tourism and travel imports have risen on average by 23% a year; over this period, China accounted for 25% of the expansion in global outbound tourism and travel spending (HSBC). Having been the 8th for the size of its tourism industry in 2000, China is now the world's biggest market. Travel services imports

are mainly concentrated in Hong Kong, China Taiwan, Japan and South Korea, accounting for 60% of the total volume.

Table 3

Sector distribution of China's trade of services in 2015 ($100 million)

	Import		Export	
	Amount	Growth %	Amount	Growth %
Total	4248,1	18,6	2881,9	9,2
Transportation	873	-9,3	385	0,5
Travel and tourism	2386,4	26	1149	8,1
Management and consulting	139,4	1,3	291,3	13,6
Construction	101	99,9	163	5,7
Insurance	80	-64,4	50	9,1
Financial	26	-52,7	22	-52,2
Computer and information	114	15,6	269,9	25,1
Royalties and license fees	219,9	-2,2	10,8	64,9
Technical	114,3	6,7	123,7	-4,5
Cultural	170,6	14,1	200,2	37,2
Other business	23,5	-22,5	217	-2

Source: MOFCOM

The second largest services export sector in China is transportation, accounting for over 13% of overall services exports in 2015, up from below 5% in 2000, with an annual growth rate at 17%. Transport service exports have grown fast since China's entry into the WTO which boosted both goods trade and transport sector. Since a decade ago, the Chinese government has put strong support to the building of its national transport expertise, especially through the construction of the Chinese high-speed railways. Chinese SOEs in transportation have benefited from technology transfers and working experiences along with some of the world's leading infrastructure constructers and transport manufacturers. Business management and consulting services account also for a significant share in services exports, representing 10% of total services exports, as Chinese firms are increasingly looking abroad for business opportunities and take a more active part in the global economy. Computer and information services exports contribute to a solid 9.4% of the total services exports in 2015, accompanying the huge material export in the sector from Chinese firms to the world. It is interesting to notice the weight and fast increase of services exports in the cultural sector, which is a positive confirmation of China's growing "soft power". The sector of intellectual property, although still relatively insignificant, shows the strongest growth potential. According to the 2016 HSBC China Trade Report, China's financial services exports have seen the fastest growth since 2000, rising by 28% a year, and the total assets of Chinese banks have more than six-folded since the early-2000s (HSBC, 2016). MOFCOM's data, however, show that both exports and imports of financial services in 2015 were less than the half of their size in 2014[6]. In fact, the size of financial

[6] http://zhs.mofcom.gov.cn/article/Nocategory/201605/20160501314855.shtml

services exports is still very limited as China's capital account remains relatively closed and the capital outflows are highly controlled.

HSBC's latest Global Trade Outlook survey in December 2016 shows that benefiting from the transformation and upgrading of China's economy, service trade contribution to the Mainland's economic growth will keep increasing and China's position in the global service trade will also advance. The report predicts that by 2030, China's service exports will grow to $818 billion, nearly 3 times the current volume, still ranking the world's 3rd service exporting countries after the US and the UK. At the same time, China's service imports will keep the sustained growth with the development of a middle-class consumer-driven economy and the increasing internationalization of the demand for services. According to its prediction, by 2030 China will become the world's largest importer of services, with a global share of 13.4%, ahead of the US (7.7%) and Germany (5.8%).

While the services deficit is still considerable, China's service trade environment is constantly improving and its development potential is huge. The rapid growth of the service industry in the domestic market, especially technology-driven modern services, will provide a strong basis for service export. In 2015, China's service sector accounted for 50.2% of GDP and in the first quarter of 2016 56.9% of GDP. China is in the critical stage of economic restructuring and industrial upgrading. With Chinese firms working up in the global value chain through technology innovation and strategic investment, the industrial base of service trade is also growing. Besides, new forms of business models based on the internet, telecommunications and cloud technology are emerging in China and they quickly integrate with traditional sectors, offering more efficient and high-quality services and solutions. In particular, the offshore service outsourcing business and cross-border e-commerce are developing very fast.

The Chinese government, at both central and local levels, has recently adopted a more proactive attitude in the promotion of new initiatives to boost the expansion of the service industry and the export of services. In February 2016, the Chinese State Council started a two-year services trade innovation pilot program in ten provinces and cities, including Tianjin, Shanghai, Hainan, Shenzhen, Hangzhou, Wuhan, Guangzhou, Chengdu, Suzhou, Weihai, and five state-level new development zones in Harbin, Chongqing, Guizhou and Shaanxi. Under this pilot program, the government has envisaged policy guidance and favorable conditions to increase the central financial support, improve the preferential taxation (tax abatement from 25% to 15% for eight business categories), strengthen financial services innovation and sustain services trade through the development of guiding funds. The relevant policies will enhance both the scale and quality of China's trade in services and help reduce the services deficit. Results communicated by MOFCOM seemed to confirm the program's efficiency: the total size of services trade in the 15 pilot cities and regions in 2016 took up 50.8% of the national level, with an average growth rate of over 20%.

Furthermore, with the implementation of the "One Belt One Road" (OBOR) initiative started in 2013 and through the recent active development of China-EU railways and maritime roads, Chinese firms are offering more and more technical advice, engineering assistance, business consultancy and financial services to related projects in countries involved. China's market share in construction service outsourcing has already seen a fast

rising. Newest data from MOFCOM show that in 2016 China's services trade with countries concerned by the OBOR initiative totaled $122.2 billion, increasing 3.4% from 2015; among which 21.5% were services exports, 11% higher than in 2015[7]. At the same time, the global services exports have been slowing down: during 2012-2015, the average growth rate was only 2.2%. There is great growth potential given the huge infrastructure and financing needs in the region. Therefore, it is obvious that in order to compete with the US and Western Europe, in the next step of the evolution of its services trade, China will focus on its neighbors, especially the two strategic core areas of the OBOR – ASEAN economies and the Central East European countries. China will further promote cooperation with OBOR countries in international production and equipment manufacturing and deepen its services offering in project contracting, R&D design, operation and maintenance, as well as third-party consulting and certification, financial services and insurance, logistics services. This will help to build the China-led regional industrial and services value chains.

Conclusion

Today, the Chinese economy is confronted with important choices concerning the inflexion of its growth model, the search for new specialization and its increasing integration into international value chains. Over the last few years, it has accumulated skills and has been able to develop strategies that enable it to both upgrade its product range, modify the structure of its exports, and move, at a domestic level, toward a service economy and to significantly increase its trade in services. The growth of this sector in both Chinese GDP and foreign trade is expected to grow strongly in the future.

In this contribution, the importance of China's integration into world trade, in particular, the internationalization of its firms, was assessed. Chinese MNC are vectors of the growth of services in trade. The strong growth in Chinese FDI in Europe and the United States is reflected in the services sector. Moreover, China's recent commitments to open the services sector to foreign investor should contribute to the strong growth of trade in this between China and the rest of the world.

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