Chinese Investment in Australia

Unique Insights from the Mining Industry

Xueli Huang and Ian Austin

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Foreword

The growth of Chinese outward direct investment (ODI) is a relatively recent and somewhat controversial phenomenon. So recently has it become important that, not unexpectedly, there are very few studies that provide reasoned analysis of the context in which Chinese ODI had grown so rapidly, what the pattern of investment has been, what the response has been in countries that have hosted it and what the effect of investment has been – economically, politically and socially – in those countries.

This book helps to redress that deficiency.

In 2009, China's ODI was running at US$48 billion, and ranked sixth, behind only the United States, the United Kingdom, France, Japan and Germany, with more than 5 per cent of global foreign direct investment (FDI) in that year. By the end of 2009, the stock of Chinese ODI in Australian amounted to almost A$6 billion, a 70 per cent increase on 2008. Between 2007 and 2009, the Australian government had given approval to 110 projects and around A$39 billion worth of Chinese investment, largely in the mining sector.

As China has opened up to engagement in the global market economy, Australia, it turns out, has been an important destination for Chinese outward foreign direct investment (OFDI). In the 1980s, when the first large-scale Chinese investments were undertaken abroad, in Rio's Channar iron ore mine in Western Australia (WA) and in the Portland aluminium smelter in Victoria, Australia was the largest destination for Chinese investment abroad. With the remarkable growth and industrialisation of China over the subsequent 30 years, the focus on resource procurement as Chinese demand for raw materials drove international commodity prices spirally upwards, and the recent policy of "going out" (or encouraging investment abroad) by large, Chinese state-owned enterprises, which was adopted by the Chinese authorities, Australia has again become a major centre for Chinese OFDI activity, mainly but not only in the minerals and energy sector. Indeed, tax-haven investments excluded, Australia can properly be regarded as China's largest overseas investment destination once again.

The experience of Chinese ODI in Australia, therefore, is of major interest both because of what it reveals about China as a major new player in international direct foreign investment and because of what it reveals about the policy, business and public response to Chinese investment in a major developed-country recipient of FDI.

Australia has perhaps the most efficient mining sector in the world. This is, importantly, due to its openness to foreign investor competition and participation, because that brings with it, and fosters, the technology, management know-how and market links that are essential ingredients in the development of a world class, internationally competitive industry. Australia has a long record of global competitiveness, and a strong policy regime, characterised by openness towards foreign investment in its resource industries. Yet Australia's foreign investment policies and foreign investment review process (through the Foreign Investment Review Board (FIRB)) – put in place to cushion the political impact as well as to capture the economic benefits of FDI – was buffeted by the surge of Chinese FDI and created some initial uncertainty about how the regime would deal with it.

The rise of Chinese investment in Australia, of course, caught many by surprise. This alone does not explain the elevation of policy and public interest in Chinese investment in the Australian mining sector or the discomfort of various Australian governments in dealing with the issue. The nature of Chinese ODI, dominantly from state-owned enterprise, the inexperience of Chinese investors in investing abroad and dealing in unfamiliar policy and political settings and a series of particular events and circumstances in the early stages of investment in Australia also contributed, all of which are reviewed in some detail in this book.

Xueli Huang and Ian Austin have done a splendid job in assembling information about Chinese ODI experience thus far in the Australian mining sector. The volume provides an excellent compendium of Chinese investments in the sector, the experience of Chinese investors in the sector and how investment has been managed by the Australian policy authorities. It is an essential handbook on the subject for those in business, those concerned with policy-making and for the interested public.

The book is not only an invaluable primer on Chinese ODI in the Australian mining sector. It also offers useful comment on the challenges that Chinese investors face in operating abroad, with illustration from the important Australian case. The context is one of the rapid growth and evolution of Chinese corporations, as state-owned enterprise finds its way in the global marketplace. A key issue is the practice and expectations of corporate governance in mature market economies such as Australia. Chinese firms lack experience in corporate governance as the concept of corporate governance in China is relatively new. Many Chinese companies are not familiar with standard corporate governance practice. Huge differences exist between the corporate governance system in China and that in countries like Australia. Although China has been gradually developing its market-based corporate governance system (the European or Japanese "insider" system of corporate governance with concentrated shareholders rather than the Anglo-Saxon system), it finds it a challenge to comply with the Australian system. The Australian government puts much (appropriate) emphasis on corporate governance of foreign investors. The authors provide anecdotal evidence that success in investment in Australia may be dependent, importantly, on whether Chinese investors can absorb local management know-how and practices and, through endogenizing learning about all aspects of corporate behaviour in that way, establish a foundation for both profitable and welcome business abroad.

The book also touches upon the huge learning process of government in managing the surge of Chinese investment abroad: for the Australian government in managing Chinese investment and the questions it raises, in the case of state-owned enterprise, about the relationship between the state and economic enterprise; and for the Chinese government and its strategies for encouraging and approving investment abroad. Here there is much research to be done, not only on the dynamic of national policy development and political economy, but also on the interaction between the two governments and between the Chinese government and its growing international enterprise abroad.

This book will whet the readers' appetite for continuing updates on developments in the Australian mining sector and very much more.

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The Australian National University
Canberra
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1
Introduction

China's economy has been growing rapidly over the past three decades. Since it implemented its "open-door and economic reform" policy in 1979, its gross domestic product (GDP) has increased rapidly from $175.6 billion in 1979 to 4.91 trillion in 2009 (National Bureau of Statistics of China, 2010), which trailed only the US ($14.256 trillion) and Japan ($5.07 trillion) in the world (International Monetary Fund, 2010). China's average GDP growth rate over the past three decades is about 9.5 per cent. It is expected that the Chinese economy will grow by 9.5 per cent in 2010 based on the forecast by the World Bank in June 2010 (The World Bank, 2010) and will, for first time, become the world's second largest economy, surpassing Japan.

The rapid economic growth in China over the past three decades has been propelled by three drivers: domestic consumption, investment and export. With the rapid economic development, the GDP per capita has been increased to $3677 by 2009 (International Monetary Fund, 2010). Although this was just about 8 per cent of Australia's GDP ($45,586), China has become the largest market – owing to its huge population of 1.3 billion – for many products, including luxury goods. For example, new car sales in China reached more than 13 million in 2009, which exceeded those sold in the US in the same period. In fact, the average growth rate of China's domestic consumption was 13 per cent between 2000 and 2009, reaching $1.838 trillion in 2009 (National Bureau of Statistics of China, 2010).

China's urbanisation and industrialisation over the past three decades have driven its investment. Over the past decade, China's urbanisation rate has increased from 35.8 per cent in 2000 to 46.1 per cent in 2009 (United Nations, 2010), which means that more than 10 million people moved from the rural areas to the cities every year. This trend is expected to continue in the next decade as China's urbanisation rate in 2009 was lower than those in many developing countries, not to mention those in developed countries, such as Europe (80%) and Japan (67%) (Liu & McDonald, 2010). Such a huge number of migrants from rural to urban areas has substantially increased Chinese demand for infrastructure such as housing, transportation and electricity. The United Nation predicts China's urbanisation rate will reach 55 per cent by 2020 and 73.2 per cent by 2050 (United Nations, 2010).

Many foreign multinational corporations (MNCs) have considered China to be their key market, so are investing heavily. FDI inflow into China has increased from $57 million in 1980 to $95 billion in 2009, a 1500-fold increase over the three decades (UNCTAD, 2010a). China is therefore one of the largest destinations for FDI in the world.

China is also one of the largest export countries owing to its strong manufacturing sector, surpassing Germany for the first time in 2009 to become the world largest export country (Department of Foreign Affairs and Trade, 2010). The Chinese manufacturing industry accounted for 46.8 per cent of its national GDP in 2009 (National Bureau of Statistics of China, 2010). This, coupled with its cheap labour, has been the driving force for its exports, which have been growing at double-digit figures since 2002, with the exception of 2009 when the world economy was hit by the global financial crisis. Many Chinese manufacturing firms now compete with their foreign counterparts in both Chinese and global markets.

China has increasingly been committed to integrating its national economy into the world. China gained access to the World Trade Organisation (WTO) in November 2001, and was consequently obliged to open more of its industries and markets to the world. At the same time, WTO membership provides many opportunities for Chinese firms to integrate their business activities into the global economy.

At the organisational level, the "open door and economic reform" policies implemented since 1979 have changed not only China's national economic structure, but also various enterprises' ownership. As China's planned economy has been gradually transformed into a market-oriented economy, the ownership structure of Chinese firms has been changed. With the privatisation of state-owned enterprises (SOEs) and the deregulation of many domestic industries, an overwhelming majority of Chinese firms are now privately owned. By the end of 2008, the number of private firms was over 3.5 million, increasing from 1.98 million at the end of 2004 and accounting for 72.5 per cent of the total number of enterprises in China. At the same time, SOEs decreased from 179,000 to 143,000, only accounting for 2.88 per cent of firms (National Bureau of Statistics of China, 2009). However, these SOEs, although less than 3 per cent of firms, held 23 per cent of the total assets of all enterprises in China, while the private firms only held 12.7 per cent.

Chinese firms, both state-owned and privately owned enterprises, have improved their competitiveness over the past three decades as they have acquired and developed a huge amount of modern technology, learnt a large range of new managerial competences, gained a deeper understanding of international financial markets and mastered a great deal of knowledge and experience in competing in markets (Nolan, 2002). Moreover, they have accumulated many financial resources and gained a great deal of experience in competing with foreign firms, particularly in their domestic markets. However, they still face a critical challenge in global business as there are still big gaps in competitiveness between the Chinese firms and the world's leading firms.

China's emergence as an important source of investment is a new phenomenon, as underpinned by rapid development in the national economy, significant improvement of competitiveness of its domestic firms and a huge accumulation of foreign currency reserves ($2.45 trillion by the end of June 2010) (Zhang, 2010). In 2009, China's ODI reached $56.5 billion (Ministry of Commerce, 2010), and was ranked fifth in the world. It only trailed the US ($248 billion), France ($147 billion), Japan ($75 billion) and Germany ($63 billion), and accounted for over 5 per cent of the global ODI in that year (UNCTAD, 2010b). This is a significant achievement for China, considering its relatively short history of ODI, which started first in 1979 with a three-stage process: introduction and experiment between 1979 and 1997; development and fluctuation from 1997 to 2002; and rapid growth since 2002 (Huang, Austin, Zhang, & Grainger, 2009). China's ODI has touched many industries including car manufacturing, services and minerals and energy, and many countries (Ministry of Commerce, 2010).

Australia has become one of the largest destinations for Chinese ODI (Ministry of Commerce, 2010) because of its abundance of natural resources, geographical proximity to China, favourable economic environment and stable political institutions. On the one hand, China's rapid economic development, underpinned by its urbanisation, export and investment, has substantially increased its demand for natural resources. For example, China produced 567.8 million tonnes of steel