Will China’s Multinationals Succeed
Globally or Regionally?

By

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Abstract

Basic theory suggests that multinational enterprises (MNEs) succeed when they develop knowledge-based capabilities, often called firm-specific advantages (FSAs). In China’s case its large MNEs have few such knowledge based FSAs. Instead, they are building scale economies based on China’s country-specific advantages (CSAs) in relatively cheap labor and natural resources. Thus, China’s MNEs will likely become knowledge seekers as they go abroad, not knowledge takers. Unlike Western MNEs who transfer knowledge and technology through their FSAs, China’s MNEs will lack such FSAs for some years to come. While China’s MNEs will have difficulty in sustaining their initial forays abroad, it is likely that they will expand intra-regionally rather than globally and in a similar manner to other large multinationals.
Introduction

China is home to a set of large firms which can now be classified as multinational enterprises (MNEs). An MNE is defined as a firm with some foreign sales and some foreign production, where the latter takes place in a wholly-owned foreign subsidiary (Rugman 1981, 2006). In the list of the world’s largest 500 companies, ranked by sales for 2001, Rugman (2005) found that there were 11 Chinese MNEs. In 2004, there were 16 Chinese firms in the list of the world’s largest 500. These large MNEs are discussed here as the basic set of firms which will determine the success of China in developing MNEs.

The literature in international business analyzes the growth and foreign expansion phase of MNEs. The starting point of this theory of the MNEs, (Rugman 1981; 1996), is the proposition that an MNE goes abroad to further expand on its firm-specific advantage (FSA). The FSAs are proprietary to the firm, and they can be technology based, knowledge based, or they can reflect managerial and/or marketing skills (Rugman and Verbeke 2003). However, there need to be more than economies of scale in the case of China’s MNEs, as such scale advantages reflect a country factor available to all firms, rather than being an FSA. Further, the large MNEs often serve as ‘flagship’ firms at the hub of large business networks where key suppliers, distributors, and businesses in the non-government infrastructure all come together in a cluster to help promote foreign sales (Rugman and D’Cruz 2000). Again, such cluster advantages reflect knowledge-based FSAs. Are these FSAs being developed by Chinese MNEs or are they simply building on country factors?

In addition to the focus of this paper upon analysis of the FSAs of Chinese MNEs, we will embed the paper within the context of research on globalization and regionalization. Contrary to the previous simplistic viewpoint that economic integration has been occurring
globally, it has been shown by Rugman (2000) that the world’s trade and foreign direct investment take place predominately within the broad triad regions of the EU, North America, and Asia Pacific. Using firm-level data Rugman (2005) confirms that of the world’s largest 500 firms only nine are truly global, whereas the vast majority of them are home-region oriented. Across the 380 firms (out of the 500) for which data on geographic sales and assets are available, the average ratio of intra-regional sales is 72%, see Rugman and Verbeke (2004).

A large literature has now developed exploring the manner in which globalization, in the sense of a world wide commonality that integrates production, marketing, and consumption, is limited such that intra-regional activities are the norm. In addition to the generic study cited above which examines the world’s largest 500 firms, there have been a variety of industry and country studies exploring the regional effect. For example, at industry level it has been demonstrated that retail and merchandising firms are predominately regional, see Rugman and Girod (2003), Sukpanich and Rugman (2007). Similarly the world’s automobile sector is regional not global, see Rugman and Collinson (2004). Finally, the world’s cosmetic industry also operates regionally and not globally, see Oh and Rugman (2006). At country level it has been shown that the largest enterprises in Europe are regional and not global, see Rugman and Collinson (2005). Even UK companies, which are the most internationalized ones in Europe, now operate on average on a regional European dimension, rather than globally, see Yip, Rugman, and Kudina (2006). In an Asian context it has been shown that Asian firms, principally the large Japanese ones, operate on an intra-regional basis rather than globally, see Collinson and Rugman (2007). Within Asia it has been shown that Korean cosmetics firms operate mainly within the Asian region, see Oh and Rugman (2007).
This paper builds in the regional dimension of international business to analysis of China’s largest firms. Based on the literature summarized in the proceeding two paragraphs it is to be expected that China’s firms will follow the normal internationalization pattern, that is, they will grow and expand within the Asia Pacific region, just as the Japanese and Korean firms have done. Thus in this paper we will examine both the nature and extent of international activity of the world’s largest firms, especially those in Asia, in order to set the regional context for the predicted expansion path for large Chinese firms. At this time there are insufficient data provided by Chinese firms, or the Chinese government, for that matter, to fully assess the regional or global nature of Chinese internationalization strategy. Basically, it is necessary to place the examination of the FSAs of Chinese MNEs within the regionalization context rather than to simply assume that global international expansion is available across a homogenous world. Contrary to Friedman (2005) the world is not flat but exhibits profound heterogeneity between the three blocks of Europe, North America and Asia Pacific. Thus this paper is the first to combine analysis of the FSAs and CSAs relevant to Chinese MNEs within the regional dimension of international business.

The FSA/CSA Matrix of MNEs
There are two building blocks in a basic matrix used in international business that we can utilize here to analyze China’s MNEs. First, there is a set of firm-specific factors that determine the competitive advantage of an organization. We call these firm-specific advantages (FSAs). An FSA is defined as a unique capability proprietary to the organization. It may be built upon product or process technology, marketing, or distributional skills. Second, there are country factors, unique to the business in each country. They can lead to country-specific advantages
The CSAs can be based on natural resource endowments (minerals, energy, forests) or on the labor force, and associated cultural factors.

Managers of most MNEs use strategies that build upon the interactions of CSAs and FSAs. They do this so that they can be positioned in a unique strategic space. The CSAs represent the natural factor endowments of a nation; they are based on the key variables in its aggregate production function. For example, CSAs can consist of the quantity, quality, and cost of the major factor endowment, namely resources.

The FSAs possessed by a firm are based ultimately on its internalization of an asset, such as production knowledge, managerial, or marketing capabilities over which the firm has proprietary control. FSAs are thus related to the firm’s ability to coordinate the use of the advantage in production, marketing, or the customization of services (Rugman 1981).

Using Porter’s terminology, the CSAs form the basis of the global platform from which the multinational firm derives a home-base “diamond” advantage in global competition (Porter 1990). Tariff and non-tariff barriers to trade and government regulations also influence CSAs. Building on these CSAs, the firm makes decisions about the efficient global configuration and coordination between segments of its value chain (operations, marketing, R&D, and logistics). The skill in making such decisions represents a strong, managerial, firm-specific advantage (FSA).

To help formulate the strategic options of the MNE, it is useful to identify the relative strengths and weaknesses of the CSAs and FSAs that they possess. Figure 1, the CSA/FSA matrix, provides a useful framework for discussion of these issues.

Figure 1 here
In Figure 1, quadrants 1, 2, and 3 can incorporate the three generic strategies suggested by Porter (1980): cost leadership, differentiation, and focus. Quadrant 1 firms are generally the cost leadership ones; they are generally resource-based and/or mature, internationally-oriented firms producing a commodity-type product. Given their late stage in the product life cycle, production FSAs flowing from the possession of intangible skills are less important than the CSAs of location and energy costs, which are the main sources of the firm’s competitive advantage. Quadrant 2 firms represent inefficient, floundering firms with neither consistent strategy, nor any intrinsic CSAs or FSAs. These firms are preparing to exit or to restructure. Quadrant 2 can also represent domestically-based small and medium-sized firms with little global exposure. Firms in quadrant 4 are generally differentiated firms with strong FSAs in marketing and customization. These firms usually have strong brands. In quadrant 4 the FSAs dominate, so in world markets the home-country CSAs are not essential in the long run. Quadrant 3 firms generally can choose to follow any of the strategies listed above because of the strength of both their CSAs and FSAs.

It is useful to note the following two points. First, if the firm has a conglomerate structure it should be more useful to situate each division or product line individually, recognizing that different units of the diversified firm would use different generic strategies. Second, changes in the trading environment, such as the EU 1992 single-market measures, or the EU 1999 single currency, or the United States-Canada Free Trade Agreement and NAFTA, will affect the relative CSAs of the firm. To the extent that CSAs are improved, the firms will tend to move to quadrant 3, and, to the extent that the CSAs are hampered, the firm or some of its product lines may move to exit, as in quadrant 2.
The Theory of MNEs in a Chinese Context

One of the unresolved problems facing the MNE in a foreign country is that it suffers from a liability of foreignness (LOF). From the viewpoint of the MNE’s managers, foreign markets present risks as there are social, political, and economic costs associated with entry to unfamiliar markets. The LOF literature suggests that the MNE has to make an investment in learning about foreign markets. In general, this follows a process of internationalization. The MNE goes to nearby countries. The LOF thereby is consistent with the empirical finding that the great majority of international business is conducted by MNEs in their home region.

The new insight that comes from this literature is that we cannot analyze the role of MNEs in a purely global sense. Instead, the MNEs need to be analyzed in a regional sense. We need to analyze the impact of Asian MNEs, primarily Japanese ones (66 of the 75 largest MNEs in Asia are Japanese) on the rest of Asia. Second, we can analyze the role of Chinese MNEs themselves; we follow this approach in the next section. We need to remember that 320 of the 380 of the world’s largest 500 MNEs (for which data are available) have an average of 80% of their sales in their home region (Rugman 2005). Their distribution of foreign assets is even more regionalized. We conclude that analysis of Chinese multinationals is actually about their regional sales in Asia.

A case can be made that the recent economic development of China is almost entirely due to FDI. The opening of the Chinese economy to foreign MNEs, first in the Special Economic Zones (SEZs) in the 1980s, followed by the opening of most coastal cities in the 1990s, has introduced some market-based efficiency to a previously totally command economy. While China is still dominated by state-owned enterprises (SOEs) and collectives, by 2005 foreign-owned firms accounted for one-third of production and 50% of exports (Thun 2005). The foreign
MNEs operate on a world-class basis of competition, and they have developed efficient supply networks. Much of the privatized sector of small and medium-sized enterprises (SMEs) in China has affiliated to the MNEs. Together the MNEs and SMEs are now driving forward the economic development of China. The inefficient and protected SOEs are beginning to reform and are starting to adopt more market-based strategies in the face of this new type of MNE-led domestic competition (Tan and Tan 2005). Through this process, efficiency-based thinking is spreading from the coastal cities throughout China. In this sense foreign MNEs are the agents of economic development for China.

This raised the question: when will China generate its own MNEs? To answer this question, we need to examine first the development of FSAs of Chinese firms.

The Development of FSAs in Chinese Firms

What, then, is the current status of FSAs of Chinese firms and what is the extent to which inward and outward FDI have helped improve the FSAs of Chinese companies? The development of FSAs of local Chinese firms affects productivity and new product development, relative to foreign companies in China (including international joint ventures and wholly owned subsidiaries). According to the data in the *Annual Census of Industrial Enterprises* published by the State Bureau of Statistics of China, between 1998 and 2002, the average labor productivity of local Chinese firms has increased by 45%. The productivity gap from foreign companies in China, measured by the ratio of the average productivity of foreign firms to that of local Chinese firms, has dropped from 5.25 to 3.29. These figures suggest that although local Chinese firms have improved their FSAs over time, they still lag behind foreign companies in productivity.
Based on firm level studies, Nolan (2004) also finds that Chinese firms are lagging well behind Western firms in the development of FSAs, especially in their lack of technology. Nolan finds little evidence that Chinese firms can develop knowledge of the systems integration skills that characterize successful Western MNEs. The Chinese firms tend to be protected, resource based, labor intensive, low technology, and inefficient firms. How to improve the FSAs of Chinese firms therefore poses a great challenge for both the Chinese government and the local Chinese firms.

One first way to improve Chinese FSAs is through collaboration with foreign firms in international joint ventures (IJVs). In developing countries collaborating with foreign firms provides significant technology transfer benefits for local firms (Lane, Salk and Lyles 2001; Lyles and Salk 1996). Yet, while there is no doubt about the benefits from technology transfer, engaging in IJVs may induce some indigenous Chinese firms to depend on their foreign partners for technological contributions to the IJVs and thus limit their endogenous efforts in innovative activities. For example, Gao (2004), based on a survey of the Chinese automobile industry, finds that collaborating with foreign automobile companies in IJVs induces a reliance upon foreign partners for sophisticated technology and new products. IJVs thereby hinder the development of technological capabilities of the Chinese firms. Furthermore, utilizing a longitudinal dataset consisting of 474 industries in China during 1998–2002, Li and Zhou (2008) show that the presence of IJVs in an industry has an inverted U-shape impact on innovative capabilities of Chinese firms, which suggests the co-existence of both positive and negative impacts of IJVs on indigenous Chinese firms. Since improving technological capabilities is ultimately an endogenous and accumulative process, which requires substantial endogenous efforts (Kim
A second way to improve the development of FSAs in Chinese firms is through an open market environment with the enhancement of domestic market competition by foreign firms. This is an effective way to facilitate FSA development because when facing fierce competition by foreign companies, indigenous firms have more incentives to develop their FSAs in order to survive in the local market (Caves 1996). This positive effect of foreign competition is particularly salient in industries where the indigenous firms are already equipped with high absorptive capacity and are capable of competing with foreign firms. Despite the fact that China continues to commit to an open market economy, the government keeps strong protection over certain industries such as banking, natural resources, telecommunications, and utility. Such protection will in turn reduce the incentives of local companies to build up their FSAs.

A third alternative to establish FSAs is through international acquisition of technology, although the benefits will take a long time to realize. One important reason for the Chinese firms to acquire companies from more advanced economies is to acquire knowledge in the form of technological capabilities, management, and strategy skills. For example, Lenovo bought the PC line of business from IBM; Baosteel bought up iron ore supplies in Brazil; Shanghai Motors bought Rover of the UK; TCL Group bought Thomson TV. The problem is that these acquisitions mainly reflect China’s CSAs rather than FSAs. Thus, it will take a long time to obtain knowledge and capabilities during post-acquisition integration. There are three reasons for this.

First, the Chinese acquirers’ lack of experience in innovative activities makes it difficult to recognize and absorb all the potential value of the acquired companies. Second, lack of
experience in international acquisition likely delays the knowledge transfer and integration process. Last, the Chinese MNEs still lack the internal managerial capabilities to integrate foreign acquisitions to develop anything resembling dynamic capabilities. They suffer from a Penrose (1959) effect of a lack of top management talent. This competitive disadvantage in management will take about a decade to remedy, before Chinese firms are competitive with Western MNEs. The integration failure between Thomson TV and TCL Group can be used to illustrate the above points. Recently, the CEO of TCL has admitted that acquiring Thomson’s TV segment was a failure. TCL did not have the capability to absorb knowledge and assets in Thomson so as to realize synergy because 1) TCL lacked international experience in acquisition; 2) TCL did not have capable managers that could help improve the communications between the Chinese acquirer and the acquired French company; 3) TCL was not able to transfer its competitive advantage in cost to France due to different labor practices between China and France. Due to the lack of longitudinal data, we cannot conclude whether acquiring knowledge and capabilities through international acquisition is a success or failure in the long term. But there is no doubt that it will take much more time than was anticipated for the Chinese firms to realize synergies through international acquisition.

Candidates for Successful Chinese MNEs

The above analyses show that although Chinese firms have achieved some level of development of FSAs through spillovers and knowledge transfer from inward and outward FDI, the benefits are only limited. Essentially, to develop FSAs requires that the Chinese firms devote tremendous efforts and resources to continuously improving their absorptive capacity and managerial capabilities. However, as shown in Table 4, the Chinese firms in the world’s largest
500 are mainly state owned and often lack strong incentives to develop their FSAs due to government protection and control (Park, Li & Tse 2006; Buckley, Clegg & Wang 2002). They are still largely in the protected banking, natural resources, and telecom service sectors; they show few signs of developing strong proprietary FSAs which would allow them to compete internationally even on an intra-regional basis. As shown in Table 5, none of these companies are truly internationalized. Indeed, these large Chinese firms are mainly SOEs and have well over 95% of their sales within China (although only partial data are available for eight firms).

Indeed, the more promising candidates for successful Chinese MNEs are companies in industries with strong domestic competition and little government intervention and control. These firms are more willing to improve R&D, managerial, and marketing capabilities and to take risks for long term development. Indeed, several firms have started to show their global competitiveness. For example, Huawei Technologies Co. has continuously invested 10% of sales on R&D for the past several years, dedicated almost half of its employees to R&D, established R&D centers in advanced countries, and has now become a world leader in providing next generation telecommunications networks.¹ Haier has established design centers in more than 30 countries and has now become the world’s fourth largest white goods home appliance producer. Haier has grown to a company ranked No. 1 among China’s Top 10 Global Brands (by Financial Times in 2005) and 86th among the World’s 500 Most Influential Brands (by World Brand Lab in 2006).²

Related Literature on FSAs and CSAs in Asian MNEs

¹ http://www.huawei.com/corporate_information.do
² http://www.haieramerica.com/en/aboutus
The World Bank (1993) categorized eight Asian countries into three groups: first, Japan; second, the first-generation, newly industrialized countries (Republic of Korea, Hong-Kong, Taiwan, and Singapore); third, the second-generation, newly industrializing countries (Malaysia, Indonesia, and Thailand). Even though those Asian countries have experienced fast-growing and export-oriented economic growth, they have different MNEs based on country-specific advantages (CSAs).

Debrah, McGovern, and Budhwar (2000) show that Singapore’s CSAs lie in skilled labor, advanced technology, advanced physical infrastructure, and advanced commercial infrastructure, while Indonesia and Malaysia have advantages in cheap (unskilled) labor and natural resources. The three other first-generation countries (and Japan) have similar advantages to Singapore.

Nelson and Pack (1999) explain the successful growth of the Republic of Korea and Taiwan by using technology assimilation. They argue that individual firms had strong incentives to improve their FSAs in efficiency to enable them to export rather than to engage in rent seeking in the domestic market. Brouthers, O’Donnell, and Hadjimarcou (2005) show that emerging market firms achieve higher level of export performance when they mimic the product strategies of Western MNEs in triad nation markets rather than when they enter emerging markets or when they develop other product strategies in triad nation markets.

Due to geographical, cultural, institutional, and historical similarities the internationally successful Korean and Japanese firms can be models for Chinese firms. For example, as discussed earlier for Chinese firms (Haier, Lenovo, etc.), Korean MNEs have acquired foreign technologies (but not really strong FSAs) by acquisition; for example, Samsung Electronics acquired Harris Microwave Semiconductor in 1993, and LG Electronics purchased 57.7% of the stock of Zenith Electronics in 1995.
Japanese firms are linked to firms in the new industrialized Asian countries as markets for final electrical and electronic products and as customers for Japanese made components. The first generation newly industrialized countries developed their technological capabilities relying on Japanese firms’ FSAs. Korea and Taiwan electronic firms acquired technology mainly through licensing and contracting arrangements with Japanese firms such as Sony, Sanyo, Matsushita, etc. in 1970-1980 (Hobday 1995). We now relate this theoretical work on FSAs and CSAs, applied to analyze Chinese MNEs, to the data available on the nature and performance of such Asian MNEs. We shall conclude by examining the available data on China’s MNEs.

The Regional Performance of Asia’s Multinational Enterprises

The performance of the world’s 500 largest MNEs has been examined in Rugman (2005). The world’s largest 500 firms, ranked by revenues, account for approximately 90% of the world’s stock of FDI. They also account for over half of the world’s trade, (Rugman 2000). Recent research has shown that the vast majority of these large MNEs operate on an intra-regional basis. This information is summarized in Table 1. The geographic basis for the broad regions of the triad are developed and explained in Rugman (2005). Of the world’s largest 500 firms a total of 379 provide data on the geographic dispersion of their sales across the three broad regions of the triad. As shown in Table 1, the 75 MNEs from Asia have an average of 77.9% of their sales in their home region. This is somewhat above the average for the 379 MNEs which is 74.6%. Otherwise the 75 Asian MNEs have an average revenue of $27.4b which is only slightly less than the average for North American MNEs for $28.8b and the $31.1b for the European MNEs. In summary, the regional performance of Asian MNEs parallels that of the regional nature of business of their competitor MNEs from North America and Europe.
Table 2 refines the data of Table 1. A smaller set of 174 MNEs is considered. These are the firms which fully report their sales in each of the three broad regions of the triad. The resulting information confirms the patterns observed in Table 1. For example, the 45 Asian MNEs average 73.2% of their sales in their home region; however, we can now see that they average 16% of their sales in North America and only 7.6% of their sales in Europe. Again, this focus on home region sales is paralleled by MNEs from North America (which average 77.7% of their sales in the home region, and 12.5% in Europe, with only 6.3% in Asia). The 58 European MNEs average 69.1% of their sales in their home region, nearly 20% in North America and only 6.7% in Asia.

In Table 3 we identify the country home base of the 45 Asian MNEs providing data on their sales in each region of the triad. This list is dominated by the 37 MNEs from Japan which average 74.6% of their sales in Asia, 14.8% in North America, and 7.3% in Europe. While there are 11 Chinese MNEs in the 2001 dataset analyzed by Rugman (2005), none of them report their geographic sales across each region of the triad. The only firm from China-Taiwan reporting has 100% of its sales in Asia. We would anticipate that the other 11 MNEs from China would also have close to 100% of their sales in Asia.

Table 4 lists the 16 Chinese firms in the top 500 for 2004, arranged by industry group. The average size of these 16 firms is $29 billion, up from an average size of $22 billion for the 11 firms listed in 2001.
Based on the annual reports of the Chinese MNEs, Table 5 shows data on the geographical dispersion of sales of eight Chinese MNEs. In Table 5 we can see that China Telecom and China Southern Power have 100% of their sales in Asia (indeed, virtually all of these within China itself). The Bank of China has 98.4% of its sales in Asia. The other five Chinese firms have over 90% of their sales in Asia. Overall these 8 large Chinese firms, most of which have the potential of being classified as MNEs, average 93.1% of their sales in Asia. We do not see that this number will fall below 90% for many years. Indeed, it is likely to be at least 10-15 years before the largest 15 Chinese firms have intra-regional sales close to the world average of about 75%. Until then the Chinese MNEs will continue to experience strong sales within China itself, with a gradual increase in foreign sales, but mostly within the Asian region.

Table 5 here

Table 6 presents the approved Chinese FDI outflows to NAFTA, EU, and Asia Pacific countries between 1990 and 2003. Average outward FDI is about US$10 billion in 2002-2003 and has increased nearly six fold from 1990 to 2003. Asia Pacific and NAFTA are the major destinations for Chinese outward FDI, which account for 62.88% and 14.43% of the total outward FDI from China in 2002-2003. The absolute value of outward FDI to all three regions has increased. The percentage of FDI outflows to Asia Pacific has remained stable during 1990-2001 but increased substantially in 2002 and 2003 (mainly due to a substantial increase to Hong Kong), whereas the percentage to NAFTA has decreased over time since 1990. These data indicate the importance of Asia Pacific countries in developing China’s trade and FDI. Hence, Chinese MNEs, in developing their internationalization strategies, should pay close attention to
their home region in order to be internationally successful. Chinese MNEs will likely expand on an intra-regional basis (like most of the world’s other MNEs) rather than globally.

**Conclusions**

Based on the foregoing theoretical and empirical analysis the following three major conclusions can be drawn about the nature, extent, and future of outward FDI by Chinese MNEs.

First, as Chinese MNEs develop and go abroad their primary geographic focus will be within the Asia Pacific region. Here their main competitors will be from other Asian MNEs based in Japan, Australia, South Korea, Singapore, and other Asian Tigers. The empirical evidence on the performance on the world’s largest 500 MNEs, as summarized in Rugman (2005), shows that the great majority of these firms operate on an intra-regional basis. Of the 380 firms providing data on geographic sales, the largest set of 320 average 80% of their sales in their home region. These firms have an even higher proportion of their foreign assets in their home region. There are extremely few “global” firms, and only three dozen bi-regionals. The Chinese MNEs are highly unlikely to become global or bi-regional firms in the next ten to twenty years. However, this is not a problem since there is no evidence showing that global and bi-regional firms are more profitable than the home region MNEs. This conclusion has strong implications for government policy and firm strategy. Since the late 1990s, Chinese government has strongly encouraged Chinese companies to go abroad and become global firms. Such a “go global” policy may be ineffective and misleading without making Chinese firms aware of the difficulty and costs of overseas investments. Indeed, being a global firm per se should not be an objective for Chinese firms. They should be careful in assessing costs of overseas investments in planning international expansion and pay more attention to the regional business opportunities.
Second, the theoretical literature indicates that MNEs expand abroad based upon a complex interaction between firm-specific advantages (FSAs) and country-specific advantages (CSAs). The successful MNEs from North America, Europe, and Japan, in general, expand abroad in order to exploit FSAs which they have developed in their large internal home markets. The activities of their foreign subsidiaries, to an overwhelming degree, tend to replicate for local distribution the FSAs developed in the home market. This explanation of MNEs was developed in Rugman (1981), and is still true today on the 25th anniversary republication of that book (Rugman 2006). Only to a minor extent do MNEs go abroad to gain access to knowledge and technology. In this respect a few Japanese MNEs doing asset-seeking FDI in North America are the main exceptions to the rule whereby the knowledge and technology is usually developed in the home market. Similarly, only a small set of Western MNEs go abroad to exploit natural resources. These are MNEs in the energy, mining, and forestry sectors. They go abroad to exploit host country CSAs, but they retain proprietary control over managerial and marketing FSAs, where the latter are identified with their home countries. The implication of this for China is that its MNEs are likely to develop by exploiting China’s CSAs in cheap, unskilled, and skilled labor. It is highly unlikely that Chinese MNEs will go abroad in any significant numbers over the next five to ten years on the basis of FSAs. In general China lacks firms with FSAs in knowledge and systems integration, especially in comparison to Western MNEs in the world’s top 500.

Third, SOEs in protected industries are poor candidates for internationalization because they have been slow to engage in the realities of market driven efficiency. As they go abroad their domestic monopoly protection, with its resulting inefficiency, will serve them badly in competitive foreign markets. Indeed, firms that face strong domestic competition and little
government protection and that emphasize development of R&D, managerial capabilities and brand names, such as Huawei Technologies and Haier, are better candidates for globalization. Yet, these companies have a long way to go to become competitive in the international market because of the intense competition and the lack of experience. At this stage, Chinese firms should learn actively from successful foreign multinationals while devoting tremendous efforts to improving capabilities of R&D, production, marketing, and management.

Last, the major impact of the growth of Chinese outward FDI, and the development of Chinese based MNEs, will be to enhance the internal efficiency of the Chinese economy. Only the best Chinese firms will succeed abroad. Thus a prerequisite for international success is domestic efficiency. As the Chinese government has supported the establishment and improvement of domestic markets, so economic efficiency within China has improved. The key agent for change in China has been the entry of foreign direct investment. Over the last ten years Western MNEs have greatly improved efficiency of the Chinese economy. They have established clusters and business networks with links to new and regenerated Chinese businesses. Indeed, many small to medium sized Chinese firms are now affiliated in business networks with foreign multinationals. Hence, the role of the Chinese government is to facilitate continuous improvements in the domestic market system. The government should continue to improve basic infrastructure, but a faster pace of liberalization in the service sector, especially financial services, is required to develop a competitive Chinese business system. As China’s economy improves the most efficient firms will be able to expand abroad. Initially they will build on China’s CSAs, but eventually they will start to generate home grown FSAs in knowledge and technology. Then Chinese MNEs will be on an equal footing with foreign MNEs in the world’s list of the 500 largest firms.
Figure 1
The CSA/FSA Matrix

Country-Specific Advantages

Firm-Specific Advantages

Weak  Strong

1  3

2  4

Weak  Strong

Source: Based on Chapter 8 Rugman (1981, 2006)
## Table 1 Regional Sales of the World’s Largest Firms

(Units: Billions of US dollars, %)

<table>
<thead>
<tr>
<th>Region</th>
<th>Number of MNEs</th>
<th>Average Revenue</th>
<th>Intra-regional Sales (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total</td>
<td>379 (500)</td>
<td>29.2 (28.0)</td>
<td>74.6</td>
</tr>
<tr>
<td>N. America</td>
<td>186 (219)</td>
<td>28.8 (28.5)</td>
<td>78.6</td>
</tr>
<tr>
<td>Europe</td>
<td>118 (159)</td>
<td>31.1 (29.0)</td>
<td>66.4</td>
</tr>
<tr>
<td>Asia</td>
<td>75 (122)</td>
<td>27.4 (25.8)</td>
<td>77.9</td>
</tr>
<tr>
<td>Third World</td>
<td>5 (34)</td>
<td>23.3 (21.8)</td>
<td>70.4</td>
</tr>
</tbody>
</table>


Notes: Values in parentheses are for entire set of the largest 500 MNEs in 2001. Only 379 MNEs’ intra-regional sales can be identified. The third world countries only include Brazil, China, Malaysia, Mexico, Republic of Korea, Russia, Singapore, and Venezuela.
Table 2 Triad Sales of Large Firms

<table>
<thead>
<tr>
<th></th>
<th>Number of MNEs</th>
<th>Average Revenue</th>
<th>Regional Sales (%)</th>
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<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>N. America</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>174 (500)</td>
<td>30.4 (28.0)</td>
<td>42.6</td>
</tr>
<tr>
<td><strong>N. America</strong></td>
<td>71 (219)</td>
<td>30.1 (28.5)</td>
<td>77.7</td>
</tr>
<tr>
<td><strong>Europe</strong></td>
<td>58 (159)</td>
<td>29.0 (29.0)</td>
<td>19.8</td>
</tr>
<tr>
<td><strong>Asia</strong></td>
<td>45 (122)</td>
<td>32.4 (25.8)</td>
<td>16.0</td>
</tr>
</tbody>
</table>

Data are for 2001.
Source: See Source in Table 1.
Notes: Values in parentheses are for entire set of the largest 500 MNEs in 2001. Only 174 MNEs report their regional sales for each of the triad regions.
### Table 3 Regional Sales of Asian Firms

(Units: Billions of US dollars, %)

<table>
<thead>
<tr>
<th>Country</th>
<th>Number of MNEs</th>
<th>Average Revenue</th>
<th>N. America</th>
<th>Europe</th>
<th>Asia</th>
<th>Unidentified</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total</strong></td>
<td>45 (112)</td>
<td>32.4 (25.8)</td>
<td>16.0</td>
<td>7.6</td>
<td>73.2</td>
<td>3.1</td>
</tr>
<tr>
<td><strong>Australia</strong></td>
<td>4 (6)</td>
<td>13.9 (14.1)</td>
<td>21.9</td>
<td>7.2</td>
<td>68.8</td>
<td>2.1</td>
</tr>
<tr>
<td><strong>Japan</strong></td>
<td>37 (88)</td>
<td>35.9 (27.9)</td>
<td>14.8</td>
<td>7.3</td>
<td>74.6</td>
<td>3.3</td>
</tr>
<tr>
<td><strong>Korea</strong></td>
<td>2 (12)</td>
<td>26.3 (21.2)</td>
<td>21.2</td>
<td>5.4</td>
<td>69.0</td>
<td>4.5</td>
</tr>
<tr>
<td><strong>Malaysia</strong></td>
<td>0 (1)</td>
<td>n.a. (17.7)</td>
<td>n.a.</td>
<td>n.a.</td>
<td>n.a.</td>
<td>n.a.</td>
</tr>
<tr>
<td><strong>Singapore</strong></td>
<td>1 (1)</td>
<td>13.1 (13.1)</td>
<td>46.3</td>
<td>30.9</td>
<td>22.4</td>
<td>0.4</td>
</tr>
<tr>
<td><strong>Taiwan</strong></td>
<td>1 (2)</td>
<td>11.6 (11.2)</td>
<td>0.0</td>
<td>0.0</td>
<td>100.0</td>
<td>0.0</td>
</tr>
<tr>
<td><strong>China</strong></td>
<td>0 (11)</td>
<td>n.a. (25.0)</td>
<td>n.a.</td>
<td>n.a.</td>
<td>n.a.</td>
<td>n.a.</td>
</tr>
</tbody>
</table>

Data are for 2001.
Source: See Source in Table 1.
Notes: See Notes in Table 1. n.a. stands for not applicable.
Table 4 Chinese Firms in the World’s Largest 500

(Units: Billions of US dollars)

<table>
<thead>
<tr>
<th>Industry</th>
<th>Company Name</th>
<th>Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>Banking and Insurance (5)</td>
<td>China Life Insurance</td>
<td>25.0</td>
</tr>
<tr>
<td></td>
<td>Industrial &amp; Commercial Bank of China</td>
<td>23.4</td>
</tr>
<tr>
<td></td>
<td>China Construction Bank</td>
<td>19.0</td>
</tr>
<tr>
<td></td>
<td>Bank of China</td>
<td>18.0</td>
</tr>
<tr>
<td></td>
<td>Agricultural Bank of China</td>
<td>15.3</td>
</tr>
<tr>
<td>Utility (4)</td>
<td>State Grid</td>
<td>71.3</td>
</tr>
<tr>
<td></td>
<td>China Mobile Telecommunications</td>
<td>24.0</td>
</tr>
<tr>
<td></td>
<td>China Telecommunications</td>
<td>21.6</td>
</tr>
<tr>
<td></td>
<td>China Southern Power Grid</td>
<td>18.9</td>
</tr>
<tr>
<td>Natural Resource Manufacturing (3)</td>
<td>Sinopec</td>
<td>75.1</td>
</tr>
<tr>
<td></td>
<td>China National Petroleum</td>
<td>67.7</td>
</tr>
<tr>
<td></td>
<td>Shanghai Baosteel Group</td>
<td>19.5</td>
</tr>
<tr>
<td>Other Manufacturing (3)</td>
<td>Sinochem</td>
<td>20.4</td>
</tr>
<tr>
<td></td>
<td>COFCO</td>
<td>14.2</td>
</tr>
<tr>
<td></td>
<td>China First Automotive Works</td>
<td>13.8</td>
</tr>
<tr>
<td>Other (1)</td>
<td>Hutchison Whampoa</td>
<td>17.3</td>
</tr>
<tr>
<td>Total (16)</td>
<td></td>
<td>29.0</td>
</tr>
</tbody>
</table>

### Table 5 Regional Sales of Eight Chinese MNEs

(Units: Billions of US dollars, %)

<table>
<thead>
<tr>
<th>Company Name</th>
<th>Revenue</th>
<th>Regional Sales</th>
<th>N. America</th>
<th>Europe</th>
<th>Asia</th>
<th>Unidentified</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sinopec</td>
<td>75.1</td>
<td>n.a.</td>
<td>n.a.</td>
<td>&gt; 90.0</td>
<td>&lt; 10.0</td>
<td></td>
</tr>
<tr>
<td>China Telecom</td>
<td>21.6</td>
<td>n.a.</td>
<td>n.a.</td>
<td>100.0</td>
<td>0.0</td>
<td></td>
</tr>
<tr>
<td>Sinochem</td>
<td>20.4</td>
<td>n.a.</td>
<td>n.a.</td>
<td>&gt; 90.0</td>
<td>&lt; 10.0</td>
<td></td>
</tr>
<tr>
<td>China Const. Bank</td>
<td>19.0</td>
<td>n.a.</td>
<td>n.a.</td>
<td>&gt; 90.0</td>
<td>&lt; 10.0</td>
<td></td>
</tr>
<tr>
<td>China SouthernPower</td>
<td>18.9</td>
<td>n.a.</td>
<td>n.a.</td>
<td>100.0</td>
<td>0.0</td>
<td></td>
</tr>
<tr>
<td>Bank of China</td>
<td>18.0</td>
<td>n.a.</td>
<td>n.a.</td>
<td>&gt; 98.4</td>
<td>&lt; 1.6</td>
<td></td>
</tr>
<tr>
<td>Hutchison Whampoa</td>
<td>17.3</td>
<td>14.0</td>
<td>33.0</td>
<td>53.0</td>
<td>0.0</td>
<td></td>
</tr>
<tr>
<td>Agri. Bank of China</td>
<td>15.3</td>
<td>n.a.</td>
<td>n.a.</td>
<td>&gt; 90.0</td>
<td>&lt; 10.0</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>20.1 (29.0)</td>
<td>n.a.</td>
<td>n.a.</td>
<td>93.1</td>
<td>5.2</td>
<td></td>
</tr>
</tbody>
</table>


Notes: Values in parentheses are for all 16 Chinese MNEs in largest 500 MNEs in 2004. Only six of them report their regional sales. n.a. stands for not applicable. If values are larger than 90%, 90% is used for calculation.

Technical Notes:
1) Sinopec - Annual report notes that Sinopec has less than 10% of sales and investment in foreign areas, and it does not need to report its geographic sales following international financial reporting standards (IFRS).
2) China Telecommunications - Annual report shows that all the group’s operating activities are carried out in the PRC.
3) Sinochem - Based on Sinochem’s sales composition, exports makes up 10%. Sinochem’s regional sales would be larger than 10%.
4) China Construction Bank - Annual report explains that the company follows IFRS, but it does not specify geographic segment data. It is possible to presume that China Construction Bank has less than 10% of foreign sales and assets.
5) China Southern Power - The website of China Southern Power shows that the company covers Guangdong, Guangxi, Guizhou, Yunnan and Hainan, which is also connected with the power grid in middle China, Hong Kong, and Macao. It is possible to presume that the portion of home region sales and assets are 100%.
6) Bank of China - Annual report explicitly shows that the portion of sales from China, Hong Kong, and Macau is 98.41% and that of assets is 94.5%.
7) Hutchison Whampoa - Annual report shows the value of geographic sales.
8) Agricultural Bank of China - The values are not explicitly noted in the annual report, but it is possible to predict that the domestic sales would be larger than 90% from the geographic data on deposit, borrowing, etc.
Table 6: Approved Chinese FDI Outflow (Amount and Destination), 1990-2003

(Units: 10,000 US dollars, %)

<table>
<thead>
<tr>
<th>Year</th>
<th>Total FDI outflow</th>
<th>EU</th>
<th>North America</th>
<th>Asia Pacific</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Amount</td>
<td>Percentage</td>
<td>Amount</td>
<td>Percentage</td>
</tr>
<tr>
<td>1990-1992</td>
<td>133,847.53</td>
<td>2.29</td>
<td>55667.188</td>
<td>41.59</td>
</tr>
<tr>
<td>1993-1995</td>
<td>176,010.77</td>
<td>2.38</td>
<td>70157.893</td>
<td>39.86</td>
</tr>
<tr>
<td>1996-1998</td>
<td>235,466.77</td>
<td>2.01</td>
<td>73583.366</td>
<td>31.25</td>
</tr>
<tr>
<td>1999-2001</td>
<td>377,761.70</td>
<td>1.58</td>
<td>89416.194</td>
<td>23.67</td>
</tr>
<tr>
<td>2002-2003</td>
<td>1,038,208.76</td>
<td>4.08</td>
<td>133098.36</td>
<td>12.82</td>
</tr>
</tbody>
</table>

Sources: Adapted from Buckley et al. (2007).
References


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