Why is China investing in Africa?

Evidence from the firm level

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Abstract

China's increased trade with and investment in Africa has boosted the continent's growth rate but has also generated considerable controversy. In this paper we investigate China's outward direct investment (ODI) in Africa using macro and micro data. The aggregate data on China's ODI in African countries reveal that China's share of the stock of foreign investment is small, though growing rapidly. China's attraction to resource-rich countries is no different from Western investment. China's ODI is uncorrelated with a measure of property rights and rule of law, whereas Western investment favors the better governance environments. As a result, Chinese investment in strong and weak governance environments is about the same, but its *share of foreign investment* is higher in the weak governance states. The micro data that we use is MOFCOM's database on all Chinese firms investing in Africa between 1998 and 2012. We use key words in project descriptions to code the investments into 25 sectors. This database captures the small and medium private firms investing in Africa. Contrary to common perceptions, there are few projects in natural resource sectors. Most projects are in services, with a significant number in manufacturing as well. In our country-sector-level regressions based on firms' transaction-level data, we find that Chinese ODI is profit-driven, just like investors from other countries. In particular, our regressions show that Chinese ODI is relatively more concentrated in skill-intensive sectors in skill-abundant countries, but in capital-intensive sectors in capital-scarce countries. These patterns are mostly observed in politically unstable countries, suggesting stronger incentives to seek profits in tougher environments. Finally, the predominance of Chinese ODI in services appears to be related to the recipient countries' natural resource abundance, which is also consistent with the profit-driven nature of Chinese ODI.

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