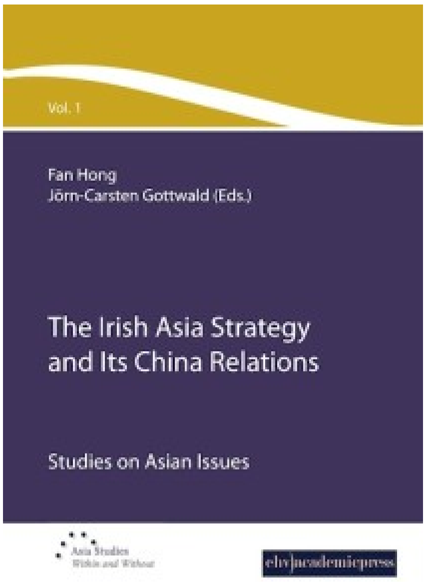
The Irish Asia Strategy and Its China Relations: Appendix II ~ "Ireland & China: Friendship And Cooperation"



Speech by An Taoiseach Mr Bertie Ahern TD at Tsinghua University,

Beijing Tuesday, 18 January 2005

President, distinguished guests,

I am pleased to be here today, at this centre of academic excellence which has educated so many of China 's leaders.

Tsinghua University reflects the energy of China in many ways:
· through its emphasis on change and development;
· through its openness and eagerness for international cooperation;
· through its commitment to high standards, exemplified by its motto of "self-discipline and social commitment";
· and through its recognition of the challenge of balancing carefully the ancient and the modern, tradition and innovation, in a way which generates healthy and sustainable progress.

It is six years since my first visit to China. In that period, China has continued its

remarkable economic and social transformation. China is playing an increasingly important role in international affairs. China is now very much a world power in every sense, with a solid and rapidly growing presence in the global economy.
Ireland is a strong supporter of Chinese engagement in the international community. We were at the forefront in welcoming China ‘s membership of the United Nations some three decades ago. And we recognise that China ‘s entry to the World Trade Organisation in 2001 was both a political and an economic landmark.

After my visit in 1998, I authorized the elaboration of an Asia Strategy, with a particular focus on China.
The aim of this Strategy is to ensure that the Irish Government and Irish enterprise work coherently to develop the important and many dimensional relationship between our two countries. As a result of that Strategy, we have strengthened our diplomatic and trade representation in China , both in Beijing and also through the opening of a Consulate General in Shanghai.
The adoption of the Asia Strategy by the Irish Government in 1999 has contributed in a significant way to the development of the relationship. Trade has increased very considerably.
Education links have also increased and Ireland is now attracting significant numbers of Chinese tourists. There is an active and popular Chinese community in Ireland – Chinese New Year is celebrated in Dublin as well as in Beijing. Cultural contacts have increased in both directions – I am always impressed by the impact that Riverdance has made here in China.

If Ireland ‘s interest in China has developed and expanded, so too has there been a growing interest in Ireland, here in China. This arises from a number of factors, for example:
· Ireland ‘s economic growth and record of economic achievement;
· our status as a knowledge-based high-tech economy with a strong track record of achievement in software, life sciences, and information technology in general;
· our regional development policies;
· and our active role and influence within the European Union.

The healthy and positive development of our relations has been nourished by regular high level visits.

The President of Ireland, Mary McAleese, paid a State visit to China in October

2003.
I have myself had two very friendly and productive meetings with Premier Wen Jiabao in the course of 2004, a year which marked the 25th anniversary of diplomatic relations between Ireland and China and which also saw the sixth Presidency by Ireland of the European Union.
Our Deputy Prime Minister visited China in 2000 and 2004.
Distinguished visitors to Ireland have included former Vice Premier Li Lanqing in 2000, former Premier Zhu Rongji in 2001, and Premier Wen Jiabao in May of 2004. Most recently, Vice Premier Huang Ju visited Ireland in November 2004.

There have also been exchanges at other senior levels.
Relations between China and Ireland are not only deepening. They are also widening.
I see my current visit as a platform for a further boost to the political, human, educational, cultural, trade and commercial relations between our two countries.
We are now taking steps to reinvigorate our Asia Strategy as we enter into the second 25 years of our important relationship with China.
High-level visits should continue to develop, including in new fields. As a keen follower of sport, I look forward to greater contacts in this area as we approach the Beijing Olympics of 2008.

The constructive and friendly economic, human, cultural and trade links between us are based on sound political relations. I am happy to say that the political relationship between the Governments of China and Ireland are both friendly and flourishing.
A sign of a close and growing bilateral relationship is that it can include dialogue on a wide range of issues, including some which have started from different points of view. The question of human rights is a good example. I believe that bilateral discussion of such issues, and also discussion in structures such as the EU/China Human Rights Dialogue, contribute to building enhanced mutual understanding.

Business missions are driving forward our economic links. I hope that Irish and Chinese entrepreneurs will look increasingly at the direct investment opportunities which both countries offer. Education cooperation has an important role to play. The number of young Chinese students in Ireland has grown in recent years.
We want to strengthen contacts between Chinese universities, including Tsinghua

University, and their Irish counterparts. In Ireland we have a respected and high quality English language educational system. This has been one of the chief engines driving our economic success. I would invite the students here today to consider studying at one of our educational institutions in Ireland.
Relations between China and Ireland show that distance and differences in size are no barriers to a warm and friendly relationship. Ireland has some 4 million inhabitants – less than one third of the population of the city of Beijing. China is the most populous nation on earth. The land
area of Ireland could fit into China many times.
But while the differences, particularly of scale, between our countries are obvious, I firmly believe that there are parallels in our respective national experiences which deepen mutual understanding.

Both China and Ireland have long histories and a strong sense of their past. China's recorded history goes back 5000 years. Developed communities in Ireland existed from about the same period. More recently, 1500 years ago, Ireland began its long record of education when Irish scholars travelled and taught throughout Europe. In both countries, as we each develop economically, there is a strong sense of tradition as well as a strong sense of the importance of the correct balance between tradition and modernity.
Both countries worked actively throughout the last century to achieve their respective destinies.
Both countries were successful in creating the conditions in which they could become the subject and not the object of their histories.
In Ireland , as a new state, genuine national control of our destiny meant working to create the conditions for economic and social, as well as political progress. We had to work intensively to address our comparative economic underdevelopment and lack of investment capital.
Moreover, we had the additional challenge of creating enough employment in Ireland to ensure that many of our young people no longer had to emigrate in search of work and a prosperous future.

Indeed, it was an American President descended from Irish emigrants, John Fitzgerald Kennedy, who said on a visit to Ireland that "the achievement of nationhood is not an end, but a beginning".

That beginning presented great challenges to Irish Governments in the newly independent Ireland. That first generation of leaders created a stable and democratic state and skilfully and successfully negotiated the dangerous decades of the 1930s and 1940s. But economic growth was slow in coming. Ireland's record of slow growth and high emigration continued until the 1950s. It was only when Ireland committed to international economic engagement that the trend of underdevelopment and depopulation was reversed.

While Ireland 's size and geographical location are fixed, the present model of the Irish economy – an open, trading economy – was the result of a strategic choice. Essentially it was a recognition by Irish leaders of foresight that, in the changing economic circumstances of the second half of the 20th century, certain conditions and polices were necessary for sustainable economic progress. These included:

· a policy of economic expansion;
· greater access to education;
· recognition of economic interdependence;
· effective regional economic policies;
· the vigorous promotion of trade, encouragement of foreign direct investment, and diversification of markets;
· the need for full involvement with the process of European integration.

This recognition and those strategic choices were central to our decision to seek membership of the European Community, now better known as the European Union. Ireland joined the European Community in 1973, and we have been an active and committed member ever since.

The industrial, economic, scientific, and educational polices adopted by successive Irish Governments have had profound effects on our employment patterns. The demands of a high tech economy have led to greater links between our university sector and enterprise.

In vigorously opening our economy, we created a range of special agencies and policies. For example, special economic zones, of which Shannon is best known. And agencies which worked closely with Irish and foreign enterprises to attract foreign investment and to support Irish exporters. Representatives of these agencies are among the business delegation which has accompanied me on my visit this week. We are ready to share our insights with our Chinese friends. I hope that we will also learn from the Chinese experience of economic and social transformation.

I spoke earlier of the European Union and its importance to Ireland. The European Union, through its economic and social mechanisms, and the access which membership gave to the European markets, was a major element in the process of Ireland's economic and social transformation. European Union agricultural, regional and structural policies, and support for our national regional policies, were of great importance in assisting Irish Governments in developing the national economy.

But Ireland is also important to the European Union. We are a small country, but we have a clear, influential and respected voice within the Union.

The decision to join the European Union, and before that the United Nations, gave new and important platforms to Ireland to play a role in international and multilateral affairs. Not only as an issue of principle, but also as a matter of prudence, Ireland places strong reliance on the maintenance of a stable, peaceful and just international environment. We support a rule-based international order with clearly defined rights and obligations.

Ireland supports the rule of law as the organizing principle of international relations. Our Constitution enshrines Ireland's devotion to the ideal of peace and friendly relations between nations based on international justice and morality.

Ireland, like China, sees the United Nations as the key multilateral framework. Ireland has been a committed member of the UN for nearly fifty years. We have served three terms on the UN Security Council. We will celebrate the fiftieth anniversary of our membership of the UN in December of this year. We have played an active and proud role in peacekeeping operations, and our military and police have been deployed in many such operations since our first involvement in UN peacekeeping over forty years ago. We support the efforts of the UN Secretary General to restructure and retool the United Nations to meet the new challenges it faces.

The importance of clear UN leadership has been amply demonstrated in recent days by the relief and reconstruction challenges posed by the enormous tragedy of the tsunami in South Asia.

China also places great emphasis on multilateral cooperation and peaceful coexistence. I am confident that China, as a permanent member of the UN Security Council with a strong interest in peace and development, will continue to play a leading and positive role in addressing the new and complex challenges that face the UN.

The international community has a duty to address causes of insecurity which have the potential to evolve into catastrophic situations. Many of the new security threats and challenges that we must face in common are vastly different from the

traditional problems of the last century. The 21st century challenges of terrorism, proliferation of weapons of mass destruction, organized and transnational crime, the crippling burden of poverty – all of these can be fertile ground for the generation of cycles of insecurity and mistrust.
As partners in the international community, China and Ireland have a firm belief in the value of international cooperation and dialogue which aims at defusing tensions and preventing conflict.

The Chinese philosopher Sun Tzu said that the greatest test of a general's skill was never to fight a battle. Thus the greatest challenge facing the international community is to prevent conflict and the causes of conflict, as opposed to dealing with its consequences.

I welcome China's growing engagement with the European Union. One of my countrymen, John Hume, a winner of the Nobel Peace Prize, said that the European Union is itself an outstanding example of conflict resolution. Certainly, conflict between the members of the EU is unthinkable. The EU has exported democracy and has imported democracies. The process of EU enlargement has been a stabilizing factor in Europe. Increasingly, the EU is seeking to apply the principles of conflict prevention and support for effective multilateralism and the role of the United Nations. This is an important development as the Union develops its international role across a wide range of sectors – trade, commerce, aid, but also the growing role of the EU in the sphere of international peace and security.

I had the privilege of chairing the European Council when Ireland held the Presidency of the European Union in the first half of last year. I was pleased to conclude negotiations on a new constitution for the European Union, which gives a further boost to the process of European integration and will allow the Union to further develop its role in the wider international community.
The EU and China are becoming increasingly important trading partners. Our relations are entering a new phase. The EU's strategic partnership with China has assumed growing importance. The recent EU Summit of Heads of State and Government, which I attended last month, welcomed the results of the seventh EU/China Summit held earlier in the Netherlands and confirmed the significant recent developments in EU/China relations. I am confident that we are on the threshold of a new and positive phase in EU/China relations. This is a development that we greatly welcome.

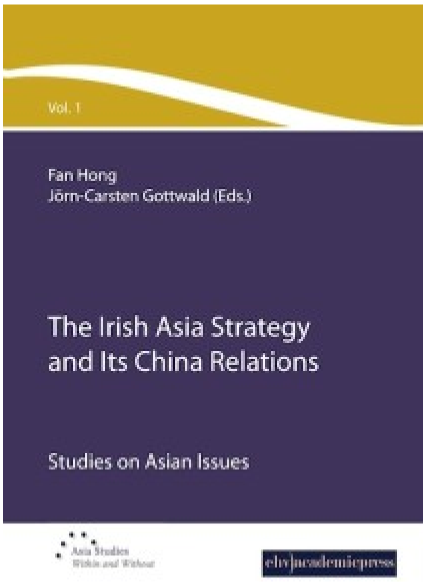
Regional integration and cooperation have been shown to be a potentially important stabilising influence in international affairs. It has been so in Europe. I am aware of China's positive role in supporting regional cooperation in Asia, and in acting in support of multilateral approaches to issues, such as those relating to the Korean peninsula.
From my comments, I think that it will be clear that there are many issues on which Ireland and China have similar views. I am keen to maintain and intensify our cooperation and exchanges in all of the fields that I have mentioned.
In Ireland, literature is a particular focus of our culture and I have been impressed to learn that some of the greatest works of Irish literature have been translated into Chinese.
As a small country, we have been privileged to have four winners of the Nobel Prize for Literature – William Butler Yeats, George Bernard Shaw, Samuel Beckett and Seamus Heaney.

In looking at the great opportunities for cooperation between Ireland and China in all of the areas I have mentioned in my remarks today, I am reminded of what George Bernard Shaw once wrote: some people see things and say why. I dream things that never were, and say why not?

That is the ambitious motto that I believe should underpin the development of further relations between China and Ireland.

Thank you.

The Irish Asia Strategy And Its China Relations: Appendix III ~ Chronology Of Sino-Irish Relations



1979
– Establishment of Diplomatic Relations between Ireland and the PRC 22nd June.

1980
– Exchange of Ambassadors between Ireland and China.

1982
– Minister for Foreign Affairs Gerald Collins to China in October.

1983
– Minister of Health Cui Yu to Ireland in May.
– Minister of Trade, Commerce & Tourism Frank Cluskey to China in May.
– Minister for Health & Social Welfare Barry Desmond to China in September.

1985
Agreement on Cultural Cooperation between the Government of the People's Republic of China and the Government of Ireland signed by China's Minister of Culture, Mr. Zhu Muzhi and Ireland's Minister for Foreign Affairs, Mr. Peter Barry during Mr. Zhu's visit to Ireland in May.
– Ministry for Agriculture He Kang to Ireland in July.

1986
Agreement between the Government of the People's Republic of China and the Government of Ireland on Economic, Industrial, Scientific and Technological Cooperation officially signed by the two countries during the visit to Ireland by China's Minister of Foreign Trade and Economic Cooperation, Mr. Zheng Tuobin in May.
– State Councilor & Minister for Foreign Affairs Wu Xueqian to Ireland in May.

1988

– President Patrick J. Hillary to China in April.

1993

– Minister for Tourism & Trade Charlie McCreevy to China in April.

1994

– Attorney General Harry Whelan to China in May.

– Tánaiste & Minister for Foreign Affairs Dick Spring to China in September.

– Minister of Civil Affairs Doji Cering to Ireland in October.

1995

– Minister of Foreign Affaires & Economic Cooperation Wu Yi to Ireland in April.

– Vice Premier & Minister for Foreign Affairs Qian Qichen to Ireland in October.

1996

– Vice Chairman of the National Peoples' Congress Standing Committee Tian Jiyun to Ireland in March.

– First meeting of heads of State when Premier Li Peng meets Taoiseach John Bruton at World Summit in Rome in November.

1997

– Minister for Marine & Natural Resources Michael Woods to China in November.

1998

Agreement between the Government of the People's Republic of China and the Government of Ireland Relating to Civil Air Transport signed by China's Vice Minister of General Administration of Civil Aviation, Mr. Shen Yuankang and Ireland's Minister of State at the Dep. of Enterprise, Trade and Employment, Mr. Tom Kitt during the visit to China by Taoiseach Bertie Ahern in September Ministry for Foreign Affairs David Andrews to China in May.

– Premier Zhu Rongji meets Taoiseach Bertie Ahern at Asia-Europe Summit meeting in London in April.

– Minister for Social Community & Family Affairs Dermot Ahern to China in June.

– Irish Speaker Dail Ceann Comhairle Séamus Pattison to China in July.

– Taoiseach Bertie Ahern meets President Jiang Zemin and Premier Zhu Rongji in September.

2000

Agreement between the Government of the People's Republic of China and the Government of Ireland for the Avoidance of Double Taxation and the prevention of Fiscal Evasion with Respect to Taxes on Income officially signed by China's Ambassador to Ireland, Zhang Xiaokang and Ireland's Minister of State for Enterprise, Trade and Employment, Tom Kitt during the visit to Ireland by Vice Premier Li Lanqing in April.
Agreement on Scientific and Technological Cooperation between the Government of the People's Republic of China and the Government of Ireland signed by China's Minister for Science and Tánaiste and Minister for Enterprise, Trade, and Employment Mary Harney during Harney's visit to China in September.
Agreement on Education Cooperation between the Government of the People's Republic of China and the Government of Ireland initiated by China's Ambassador to Ireland and Ireland's Secretary General of the Department of Education and Science in Dublin in October 2000.

2001
– Minister for Arts, Heritage, Gaeltacht & the Islands Síle de Valera to China in January.
– Premier Zhu Rongji to Ireland in September.
Agreement on Education Cooperation Between the Government of the People's Republic of China and the Government of Ireland signed in February.

2002
– *Ireland-China Research Collaboration Fund Agreement* in December.
– Inaugural Shanghai Intern Programme in Ireland – June –September.

2003
– Minister for Justice, Equality & Law Reform Michael McDowell to China in March.
– Shanghai Intern Programme – June – September – visit to Cork in August.
– President Mary McAleese to China in October.

2004
– Lord Mayor, Cork City Council, Cork Chamber and UCC visit to Shanghai in February.
– Irish Tánaiste to China in March.
– Foreign Minister Li Zhaoxing to Ireland in March.
– Premier Wen Jiaobao to Ireland in May.

Memorandum of Understanding on Visa and Related Issues Concerning Tourist Groups from the People's Republic of China signed in May.
– Cork City officials visit Shanghai in June to explore Sister City relationship.
– Shanghai Intern Programme – First Cork-based Interns; first Interns from Suzhou and Wuxi.
– Vice Chairman of the Chinese People's Political Consultative Conference National Committee Ye Xuanping to Ireland in October.
– Visit by Shanghai Municipal Cultural Administration of Culture, Radio, Film and TV – meeting with Cork cultural and arts organizations October.
– Performance by Shanghai Dramatic Arts Centre as part of Cork 2005 European Capital of Culture Programme in October.
– Performance by Shanghai Percussion Orchestra as part of Cork 2005 European Capital of Culture Programme in November.
– Vice Premier Huang Ju to Ireland in November.

2005
– Irish Trade Mission to China led by Taoiseach Bertie Ahern in January. Largest trade delegation have ever left Ireland.
Cork City Council and UCC participate *Memorandum of Understanding on Cooperation in Software Sector between the Ministry of Commerce of China and the Department of Enterprise, Trade and Employment of Ireland* signed in January.
Protocol on Quarantine and Veterinary Health Requirements for Pork to be exported from Ireland to the People's Republic of China signed in January.
Agreement on Cooperation between CCPIT, China International Chamber of Commerce and Ireland Chamber of Commerce signed in January.
Agreement on Cooperation between China National Committee of Natural Sciences Foundation and Science Foundation of Ireland signed in January.
– Cork City twins with Shanghai in May signed by Cllr. Sean Martin, Lord Mayor of Cork, and Mr. Gong Xue Ping, representative of the city of Shanghai, Chairman of the Standing Committee of the Shanghai Municipal People's Congress.
– Shanghai Intern Programme – two Cork-based Interns.

2006
– Establishment of Irish Institute of Chinese Studies at University College Cork and University College Dublin under auspices of the Irish Asia Strategy in January.

– Visit from Changning Huju Opera Troupe to Cork – first time performed outside China.
– Shanghai Intern Programme – two Cork based Interns: programme extended to Hangzhou.
– Mr Zeng Peiyan, Vice Premier of the People's Republic of China, to Ireland in September.
Memorandum of Understanding on Agricultural Cooperation between the Ministry of Agriculture of the People's Republic of China and the Department of Agriculture and Food of the Republic of Ireland signed in September.
Visit of Cork Chamber delegation to Shanghai and Hangzhou; MOU signed with Shanghai Chamber of International Commerce.
– BA in Chinese Studies programme (four years) began at UCC.

2007
– Establishment of Irish Studies Centre at Beijing Foreign Studies University in partnership with NUIM in March.
– Establishment of Confucius Institute at University College Cork in conjunction with Hanban and Shanghai University in November.
– First Annual China Conference: *China in the 21st Century* took place at University College Cork in June.
– Shanghai Intern Programme – two Cork based Interns.
– Visit of eight Cork schools to Shanghai in October.
– Establishment of Confucius Institute at University College Dublin in conjunction with Hanban and Renmin University of China.
– A lecture on 'The EU Through the Eyes of Asia- the Case of China and Hong Kong' took place in UCC.
– *Focus on Asia* lecture series took place in UCC.
– BCom in Chinese Studies programme (four years) began at UCC and UCD.
– Higher Diploma and MA in Contemporary Chinese Culture and Business programmes (one year) began at UCC.

2008
– Shanghai Intern Programme – two Cork based Interns.
– Visit of Chinese Vice Premier Zeng Peiyan in Sept. 2008.
– Visit of nine Shanghai schools to Cork; 9 Memoranda of Understanding signed; October 2008.
– The 2nd Chinese Language Contest in Ireland (Chinese Bridge) took place in

UCC.
– Enterprise Ireland Trade Mission led by Taoiseach Brian Cowen to China in October, the second largest trade mission to China.
– The 10th Session of China-Ireland Economic, Trade and Technological Joint Commission Meeting was held in Dublin, which was co-chaired by Mr. Sun Yongfu, Director General of European Affairs Department of Ministry of Commerce in China and Ms. Clare Dunne, Assistant Secretary General in the Department of Enterprise, Trade and Employment of Ireland in December.
– The 1st Conference of the Association of Chinese Studies in Ireland took place in Dublin. Signing of *Memorandums of Understanding between the Irish Financial Services Regulatory Authority and the China Bank Regulatory Commission and the China Securities Regulatory Commission* during October Trade mission.
– The first group of students of Higher Diploma and MA in Contemporary Chinese Culture and Business programmes graduated at UCC.
– The prestigious European Award for Languages has been awarded to the Irish Institute of Chinese Studies (IICS) at UCC.
– IICS's second annual international conference, *The Rise of Asia and its Challenge for Europe*, was held in Cork by UCC.
– The First Asian Ambassadors Round Table Discussion took place in Cork.
– The Asian Studies Ireland Association (ASIA) was established.

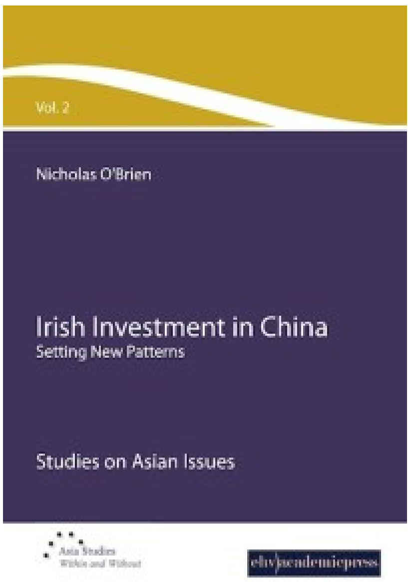
2009
– Visit of delegations from Cork to Shanghai led by Deputy Lord Mayor Patricia Gosch; *Memorandum of Understanding* signed with Vice Mayor Tang Dengjie of Shanghai Municipal People's Government to cover the period to 2014.
– Tánaiste and Minister for Enterprise, Trade and Employment Mary Coughlan, T.D., met with a delegation from Changchun City led by Party Chief Mr. Gao Guangbin in Ireland in May.
– First annual Irish Studies Conference at Beijing Foreign Studies University in December with announcement that Irish language will be taught at the Irish Studies Centre in BFSU.
– Shanghai Intern Programme – two Cork based Interns; Dujiangyan City (Sichuan) joins the programme.
– Visit by Shangha Federation of Industry and Commerce; Memorandum of Understanding signed with Cork City Council.
– *Study in China Summer Camp for Irish University Students* took place at Shanghai University organized by UCC Confucius Institute and IICS (UCC).

– *You Ai Cairde China Cultural Tour 2009* co-organised by UCC Confucius Institute and the Irish Chinese Contact Group took place in China.
– The 2nd Chinese Language Contest in Ireland (Chinese Bridge) took place in UCC.
– Chinese Assistant Minister for Commerce Mme. Qiu Hong led a trade and investment promotion mission to visit Ireland in December.
– University College Cork launches School of Asian Studies in October.
– Enterprise Ireland Trade Mission led By Ministry Billy Kelleher TD to China in October (Financial Services Trade Mission).
– Visit of China National People's Congress Delegation to UCC Confucius Institute and UCC.
– *Post Beijing 2008: Geopolitics, Sport, Pacific Rim International Conference/Workshop* took place in UCC.
– The 2nd Conference of the Association of Chinese Studies in Ireland took place in Dublin.
– The 2nd Annual Conference of the Asian Studies Ireland Association took place in UCC.
– The Irish Association of Chinese Teaching and Learning was established at UCC with its Inaugural Conference.
– The 2nd Asian Ambassadors Round Table Discussion took place in Dublin.
– The Irish Institute of Korean Studies was established at UCC.

2010
– Enterprise Ireland Trade Mission in March to China (Education Trade Mission).
– Three new Asian Studies programmes at postgraduate level began at UCC including: MA in Asian Studies, Higher Diploma in Entrepreneurship and East Asian Affairs and Higher Diploma in East Asian Affairs and Economics.
– Online training programme – Doing Business in China initiated.
– The Confucius Class Room Programmes established in Cork and Ireland.
– *You Ai Cairde China Cultural Tour 2010* co-organised by UCC Confucius Institute and the Irish Chinese Contact Group took place in China.
– The 1st Chinese Language Contest for Schools in Ireland (Chinese Bridge) took place in UCC.
– The 3rd Chinese Language Contest for Universities in Ireland (Chinese Bridge) took place in Dublin.
– The 1st Conference for Korean Studies took place at UCC.
– The inaugural of the Training Centre for Chinese Language Teachers and the

1st Chinese Language Teachers Training Workshop took place at UCC.
– The Cork City Delegation led by the Lord Mayor of Cork visited Cork's sister city Shanghai and the Shanghai Expo.
– The Irish President Mary McAleese visited the Irish Pavilion at the Shanghai Expo.
– The 3rd Conference of the Association of Chinese Studies in Ireland took place in Dublin.
– The 3rd Annual Conference of the Asian Studies Ireland Association will take place in November at UCC.
– The 3rd Asian Ambassadors Round Table Discussion will take place in November at UCC.

Irish Investment In China. Setting New Patterns ~ Contents, List Of Abbreviations & Glossary Of Terms



Now online: Nicholas O'Brien – Irish Investment in China. Setting new patterns.

Consideration of Irish investment in China will be located within the context of investment theory. Accordingly, *chapter two* examines the seminal literatureon foreign direct investment and sets out an appropriate model of investment theory within which this research shall be considered. The limited literature on Irish outward FDI is also considered, with specific emphasis on Barry et al's model on Irish outward FDI.

Chapter three outlines the results of this research and emerging themes are identified. This allows conclusions to be drawn as to whether Barry et al's model holds in the case of Irish FDI into China. It should be stressed that this is not in any manner a judgement on Barry et al's model. Rather, it is a reflection on the nature of China as an emerging economy and the unique political economy which it enjoys.

Chapter four draws on the research to explore the opportunities and challenges which China represents. The principal locational advantages and disadvantages which China poses are set out. It is argued that the major potential which China represents for Irish investors lies in market opportunity rather than in low labour costs, an opinion which is supported by the relevant literature on FDI in China. The principal locational disadvantages are identified as existing in the regulatory, cultural and legal environments. This allows conclusions to be drawn on our sub-hypothesis, namely the challenges which China poses for investors.

Chapter five explores the nature of Irish FDI into China. The non-application of Barry et al's model to China is discussed together with our prescriptive research question, namely the desirability of state involvement in outward FDI. This chapter also seeks to explain why Irish FDI into China is different from that in the traditional destinations for outward FDI.

The concluding chapter draws on previous chapters to identify conclusions which can be drawn. Key findings are highlighted and potential areas for further research suggested.

List of Abbreviations

China – This term is used to refer to the People's Republic of China
CSO – Central Statistics Office, Ireland
EJV – Equity Joint Venture
EJVL – Equity Joint Venture Law
EU – European Union
FDI – Foreign Direct Investment
HFDI – Horizontal Foreign Direct Investment
IFC – International Finance Corporation
IMF – International Monetary Fund
IPR – Intellectual Property Right
M&A – Merger and Acquisition
MNC – Multinational Corporation
MNE – Multinational Enterprise
NBER – National Bureau of Economic Research
OECD – Organisation for Economic Co-operation and Development
OLI – Dunning's Eclectic Paradigm model: Ownership advantage, Location advantage and Internalisation advantage
SEZ – Special Economic Zone
UNCTAD – United Nations Conference on Trade and Development
US – United States of America
VFDI – Vertical Foreign Direct Investment
WFOE – Wholly Foreign Owned Enterprise
WFOEL – Wholly Foreign Owned Enterprise Licence
WTO – World Trade Organisation

Glossary of terms

Foreign Direct Investment (FDI) – the value of financial flows from 'home' countries to foreign affiliates in 'host' countries, in which a direct investor has a controlling interest.

Host economy – the country that receives FDI from the foreign investor.

Home economy – the country of origin of the investment.

Inward Direct investment – refers to direct investment by foreign investors in the host economy.

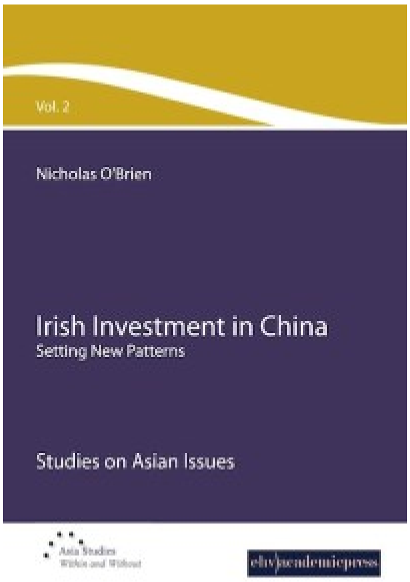
Multinational Enterprise – incorporated or unincorporated enterprise comprising parent enterprise and its foreign affiliate(s).

Outward Direct Investment – direct investment by investors from the home economy Pearl River Delta – Hong Kong and its surrounding hinterland.

Subsidiary – an incorporated enterprise in the host country in which the foreign investor owns at least 50 per cent of the shares or has the right to remove a majority of the board.

Yangtze River Delta – Shanghai and its surrounding hinterland.

Irish Investment in China. Setting New Patterns ~ Abstract & Acknowledgements



Abstract

According to the Industrial Development Path Hypothesis (Dunning, 1981, 1986, 2001), outward Foreign Direct Investment is symptomatic of successful advanced industrialised economies. After a decade of unprecedented growth and prosperity from the mid-1990s, the Irish economy had reached a sufficient level of maturity that Irish firms were beginning to seek new markets in which to invest.

Barry et al's (2003) authoritative work states that Irish outward FDI is disproportionately horizontal and oriented towards non-internationally traded sectors. This study was based exclusively on developed economies – Europe and North America, rather than developing economies or emerging markets. Such countries have not yet featured in the literature on outward Irish FDI. Given the importance of China as the largest global recipient of inward FDI, this book explores the nature of Irish FDI into China and specifically considers whether Barry et al's model on Irish outward FDI holds for current Irish investment into China. This consideration will be conducted within the framework of Dunning's Eclectic Paradigm, which contends that locational, ownership and internalisation advantages must exist for successful investment to occur.

While the level of Irish FDI into China is limited, research was conducted among all Irish firms which had invested in China (this research was conducted in 2006 and 2007). It was found that the nature and scope of Irish FDI into China differs from earlier patterns identified by Barry et al in the case of developed economies. Irish FDI into China is found to be predominately in the traded sector and can be described as only marginally horizontal.

In order to gain a deeper understanding of this development, the locational advantages and disadvantages which China poses are explored. The principal locational advantage is identified as market opportunity. Perhaps the most significant challenge facing investors is the risk to the protection of intellectual property rights (IPR). It is argued that this has the potential to affect the ownership advantage which Irish MNEs possess. Accordingly, there is a need to

utilise internalisation advantage to protect IPR. Consideration is given to the role which the state can play in the provision of 'soft supports' for investors, primarily through the provision of market information.

Acknowledgements
The experience and insight offered by senior business executives offered a valuable and unique perspective on the world of private sector decision making. I am particularly grateful for the level of access and openness which I received. I would also like to thank senior staff in the Irish Government state agencies, Enterprise Ireland and the Industrial Development Agency for the valuable information and assistance provided. Without the openness and positive disposition of my interviewees, this research would not have been possible.

I wish to acknowledge the support and encouragement of my doctoral thesis supervisors Dr. Andrew Baker, Queen's University Belfast and Dr. Michael Mulreany, Institute of Public Administration, Dublin. Their guidance and support were particularly important and insightful in helping me develop my line of argumentation. I should also like to acknowledge the support of the Department of Foreign Affairs for their positive attitude and support towards continuing professional education. A special word of thanks is due to the staff at the Department's library, who aided my search for literature in a professional and helpful manner.

Finally, I should like to thank my wife Caroline who, on a snowy afternoon in Monscheau, Germany, suggested that I pursue a doctorate. Together with my daughters, Ciara and Niamh, she provided support, encouragement and especially the time to facilitate my studies.

Nicolas O' Brien

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For anybody with an interest in investing in or doing business in China, Nicholas O'Brien's scholarly and informative book should be essential reading. Given the growing importance of China in global trade this is a very timely work which I highly commend.
Dick Spring, former Deputy Prime Minister and Foreign Minister of Ireland

This book identifies clear differences between Irish investment into China and that into traditional FDI locations such as the US and UK. It is an authoritative work, particularly in view of the author's experience as a senior diplomat in China and offers clear conclusions as to the benefits and challenges of investing in China".

Dr. Michael B. Murphy, President, UCC

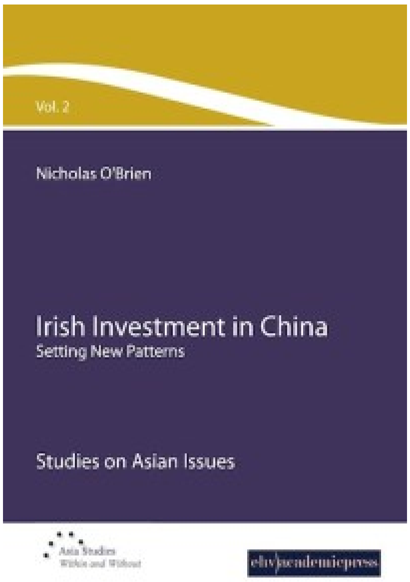
This is a must read for Irish people considering investment in China. The author discusses why considerable challenges still remain. A very comprehensive insight into informed investment in China.
Donal O'Callaghan, former Chairperson, Ireland China Association

Dr Nicholas O'Brien worked at the coalface of the transformation of modern China during his four years as Irish Consul General in Shanghai. His work is a testament to intelligent observation and the insight that experienced observers can have. The sideline sometimes brings more perspective than those on the pitch have. His book greatly expands our store of knowledge on this subject in an accessible manner with lucid division of what he is discussing and crystal clear conclusions.
Richard Barrett, Treasury Holdings

This admirable book charts the experience of Irish investors in China and has valuable pointers and good advice for business investors planning to invest in the Middle Kingdom. Given the author's wide international experience, in particular his unique insight as Irish Consul General in Shanghai, this book is an authoritative source on the challenges and opportunities which China offers.
Dr T P Hardiman, Asia Europe Business Forum

Chapter 1: The Giant Arises ~ Irish Investment in China. Setting

New Patterns



Introduction
The introduction of the 'opening-up' policy by the Chinese authorities in 1979 heralded an era of economic reform and 'symbolised China's sharp turn towards participation in the world market to speed to economic growth and technological modernisation'. (Riskin, 1987: 316) Since then, China's economic story has been a remarkable success, growing on average over eight per cent per annum. Central to this economic success was the attraction of inward foreign direct investment. Such was the success of this policy that in 2003 China overtook the US as the largest global recipient of foreign direct investment (FDI), attracting $53 billion in that year (OECD, 2004).
On the other side of the globe, the Irish economy was also going through its own transformation. The 1970s and '80s were a period of high inflation, unemployment and the presence of large-scale emigration. In contrast, the 1990s was an era of unrivalled economic growth, with double digit GNP increases for most of this decade. Central to this transformation was the high level of inward FDI which Ireland attracted. Building on the strength of the economy, outward FDI continued to grow to such a degree that in 2004 Ireland became a net exporter of FDI for the first time.
Given the importance which both inward and outward FDI plays in economic development, the drivers and patterns of Irish FDI into the surging Chinese economy are worthy of examination. Barry et al's (2003) seminal work on Irish outward FDI focuses on FDI into the US and UK, both of which are developed economies. Barry et al show that Irish outward FDI has been disproportionately horizontal (focused on replicating production facilities in third countries rather than moving an entire component of the production chain) and oriented towards non-internationally traded sectors.

Given the importance of China, as the largest recipient of inward FDI and the world's second largest economy, it is opportune to explore the nature of Irish FDI into China and specifically whether or not the model identified for developed economies by Barry et al holds for Irish investment into China. 'As Dunning (1997) has emphasised, full account must be taken of location factors, such as the structure of the host economy, the policies of the host government and the nature of local business culture, in explaining the comparative success and failure of FDI'. (Buckley and Casson, 1998: 27) However, 'China's size makes it different from nearly all other developing and developed countries'. (Eckaus, 1987: 117) It is important therefore for investors, policy makers and commentators on FDI to be conscious of the challenges and opportunities which China holds. While China displays the hallmarks of a market economy, it is a unique political economy. The State is still heavily involved in virtually all facets of economic life. In addition, China has a strong cultural tradition which places an emphasis on relationship building.

The author conducted research into Irish investment during the period 2006-2007 among the relatively small number of Irish investments in China. In the intervening period, the pattern of investment has not appreciably changed and the findings are still valid. The author had the good fortune to witness at first hand the rapid advances which the Chinese economy is experiencing over a four-year period. The rationale motivating this research is the importance of China in the study of FDI and the potential modifications to theory which China may necessitate, because of its status as a developing economy and its non-adherence to the Weberian concept of contract law.

Consideration of the nature of Irish investment in China also generates a sub-hypothesis. The literature review points to the challenges which the business environment poses, including the persistence of guanxi, and what Jones (1994) describes as the Rule of Relationships rather than Rule of Law. Therefore our sub-hypothesis asks if the investment environment in China poses particular challenges for investors who are accustomed to Western norms and if this is a pertinent fact to be considered when evaluating investment decisions. The nature of such challenges and their impact will be explored in order to evaluate whether or not investing in China is particularly different from investing in economies which Irish firms are more accustomed to. If the market is an inefficient allocator of resources, market imperfections are deemed to exist, because additional costs arise. (Mulreany, 1999) Should this be the case, economic theory holds that a role exists for public policy in overcoming such market imperfections.

The engagement or non-engagement of Irish firms in outward FDI is an important economic governance issue. If Irish firms do not engage and their European competitors do so, there is a risk that Irish firms will lose competitive advantage. ‘Increased openness to trade and factor flows increases international interdependence with important consequences for governance’. (Barry, 2006: 165)

Research Methodology

In conducting research on Irish investment in China, a combination of quantitative and qualitative research was utilised, with the latter dominating. As a means of obtaining first-hand accounts of the experience of investors in China and the associated challenges, research was conducted among three categories of executives – Irish firms which have invested in China (within the meaning of our definition of investment); selected non-Irish firms which have invested in China; and selected Irish firms which have invested in Eastern Europe. Semi-structured interviews were conducted to establish why they invested in China (or didn’t in the case of the latter group) and the challenges which they faced. This data, together with desk-based study, was analysed to allow conclusions to be drawn as to the validity of our primary hypothesis and sub-hypothesis.

As the objective of this research was to establish the perceptions and opinions of key business executives, the relevant data is inherently qualitative rather than quantitative. Quantitative research essentially employs some form of measurement, whereas qualitative research is considered to be the most appropriate form of collecting data on ‘experiences and processes – especially as understood by respondents themselves’. (Alcock, 2004: 57) While a qualitative methodology dominated during this research, limited quantitative analysis was also utilised, primarily in the identification of investment trends and patterns, as part of desk-based research. A note of caution needs to be sounded on the availability of reliable statistics on FDI. ‘There are gaps in the FDI statistics available from the source and host countries on FDI. Most countries do not publish comprehensive information on the foreign operations of their companies, for reasons of secrecy. Because of these problems, inconsistency between measure of FDI flows and stocks are the rule rather than the exception’. (Moosa, 2002: 2-3)

All Irish companies which have invested in China (with a holding of greater than 50% in their Chinese subsidiary) were selected for inclusion in this research. In the case of non-Irish MNEs which have invested in China, purposeful sampling was employed. The Irish Government's Asia Strategy (Government of Ireland 2006) identifies eight sectors as having the potential to deepen their trade links with China. These industries were identified by the Government because of the strength of their Irish base of operation and as such can be assumed to possess ownership advantage, as described by Dunning, and possibly have the potential to invest in Asia. The eight sectors, as set out in the Asia Strategy, were analysed and four of these sectors were identified as having no Irish firm which has invested in China to date.

Executives of MNEs from these four sectors (telecoms, financial services, education and healthcare) were included in this research in order to identify the experience of investors and relate these findings to the Asia Strategy. A further four MNEs were identified because of the hi-technology nature of their industry, a high susceptibility to intellectual property violation, the strength of the industry in the Irish economy, and a consumer products MNE. In addition, consultations were held with a consultancy company which assists in the setup of MNEs in China, and with representatives of two leading Chinese law firms.

As a means of gaining an understanding of the relatively low number of Irish firms which have invested in China to date, analogous situations were considered to assess if a comparative dimension could be introduced. In the recent past, Eastern Europe was presented as a low-cost, high market-potential destination for FDI. '[EU] Enlargement will also bring forth new investment opportunities for EU15 firms'. (Barry, 2004: 829) One might assume that firms which have already invested in Eastern Europe would also be attracted by the prospect of investing in China, given the strong locational advantages which China offers. Accordingly, a selection of Irish MNEs which have invested in Eastern Europe were selected for inclusion in this research.

The study of the perceptions of business elites on investing in China does not lend itself to a narrow scientific study with its associated definitive findings. Based on the information available on inward FDI into China and the limited information on Irish outward FDI, a decision was taken to use a qualitative approach through the medium of semi-structured interviews.

The questions around which the semi-structured interviews were conducted were formulated with reference to issues identified during the literature review and areas of specific study in this research. The core research was conducted among executives of MNEs which have invested in China, supplemented by the views of those which have invested in Eastern Europe but not in China.

Outline

Consideration of Irish investment in China will be located within the context of investment theory. Accordingly, chapter two examines the seminal literatureon foreign direct investment and sets out an appropriate model of investment theory within which this research shall be considered. The limited literature on Irish outward FDI is also considered, with specific emphasis on Barry et al’s model on Irish outward FDI.

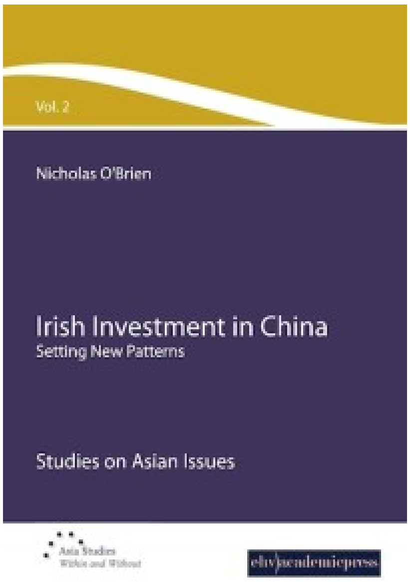
Chapter three outlines the results of this research and emerging themes are identified. This allows conclusions to be drawn as to whether Barry et al’s model holds in the case of Irish FDI into China. It should be stressed that this is not in any manner a judgement on Barry et al’s model. Rather, it is a reflection on the nature of China as an emerging economy and the unique political economy which it enjoys.

Chapter four draws on the research to explore the opportunities and challenges which China represents. The principal locational advantages and disadvantages which China poses are set out. It is argued that the major potential which China represents for Irish investors lies in market opportunity rather than in low labour costs, an opinion which is supported by the relevant literature on FDI in China. The principal locational disadvantages are identified as existing in the regulatory, cultural and legal environments. This allows conclusions to be drawn on our sub-hypothesis, namely the challenges which China poses for investors.

Chapter five explores the nature of Irish FDI into China. The non-application of Barry et al’s model to China is discussed together with our prescriptive research question, namely the desirability of state involvement in outward FDI. This chapter also seeks to explain why Irish FDI into China is different from that in the traditional destinations for outward FDI.

The concluding chapter draws on previous chapters to identify conclusions which can be drawn. Key findings are highlighted and potential areas for further research suggested.

Chapter 2: Literature Review And Issues To Be Addressed ~ Irish Investment In China. Setting New Patterns



Introduction

There is a considerable amount of material on FDI, the multinational enterprise (MNE) and the role of China in today's globalised economy, and the literature considered in this chapter reflects the key issues under discussion. Initially, investment is defined and competing views on investment theory are considered, with the most suitable one for this study identified. Given the inter-twined linkage between FDI and multi-national enterprises (MNEs), the role of MNEs is explored, followed by an analysis of how FDI occurs at the level of the firm.

The limited literature on Irish outward FDI is also set out. Specifically, Barry et al's model on Irish outward FDI is examined, so that the application of their hypothesis to the Chinese economy can be considered. This is followed by a consideration of the rise of FDI in China and the influence which China's unique culture has on the FDI environment.

Investment Defined

The International Monetary Fund (IMF) offers a definition of foreign direct investment.

Direct investment is the category of international investment that reflects the objective of a resident entity in one economy obtaining a lasting interest in an enterprise resident in another economy. (The resident entity is the direct investor and the enterprise is the direct investment enterprise.) The lasting interest implies the existence of a long-term relationship between the direct investor and the enterprise and a significant degree of influence by the investor on the management of the enterprise. (IMF, 1993: 86)

The IMF goes on to define a direct investment enterprise 'as an incorporated or unincorporated enterprise in which a direct investor, who is resident in another economy, owns 10% or more of the ordinary shares or voting power'. (IMF, 1993:86) This definition is aimed at providing a standard by which balance-of-payments data is compiled. However, it does not adequately address the issue of control.

The OECD (2006: 2) defines direct investment as a category of international investment made by a resident entity in one economy (direct investor) with the objective of establishing a lasting interest in an enterprise resident in an economy other than that of the investor (direct investment enterprise). 'Lasting interest' implies the existence of a long-term relationship between the direct investor and the enterprise and a significant degree of influence by the direct investor on the management of the direct investment enterprise.

Again, this definition is not precise enough for use in this research, as the issue of control is couched in terms of a 'significant degree of influence'. Moosa (2002: 1) comes close to a workable definition when he defines FDI as 'the process whereby residents of one country (the source country) acquire ownership of assets for the purpose of controlling the production, distribution and other activities of a firm in another country (the host country)'.

Lipsey (2001) contends that the United Nations System of National Accounts, which governs the compilation of national income data, appropriately addresses the concept of control. The UN System of National Accounts defines foreign controlled enterprises as subsidiaries of which more than 50% are owned by a foreign parent. (United Nations, 1993) This definition focuses on control and is the one which shall be used as our reference point. Investments below 50 per cent of a firm's stock are either of a portfolio nature or offer the investor a minority shareholding. In seeking to explore potential Irish investment into China and gain a fuller appreciation of the complexities and challenges of FDI, the scope of this research includes only those firms which have a controlling interest. MNEs holding 50% of stock or less are, by their nature, restricted in the scope of their decision-making and influence. 'The distinguishing feature of FDI, in comparison with other forms of international investment, is the element of control over management policy and decision'. (Moosa, 2002: 2)

For the purposes of this research, therefore, control is a central concept. The FDI relationship consists of a parent enterprise and a foreign affiliate which together form a multinational enterprise (MNE). Given the importance of MNEs and the central role which they play in FDI decisions, their role and structure is explored later in this chapter.

Having set out our working definition of FDI, it is important to distinguish between the two principal forms in which FDI takes place. Firstly firms can invest abroad to supply a market directly through a subsidiary, whereby production processes from the home economy are replicated in the host economy, and this is described as horizontal FDI. This form of FDI is often undertaken to exploit more fully certain monopolistic or oligopolistic advantages, such as patents or differentiated products. (Moosa, 2002) The second form, vertical FDI, is undertaken to locate low-cost locations for components of the production process, whereby certain elements are moved in their totality from the home to the host economy. Horizontal and vertical FDI should not be seen as competing theories. Rather, they seek to explain different rationale underlying
investment decisions.

All investments necessarily entail trade-offs and compromises. Horizontal FDI avoids trade costs but foregoes economies of scale, as production is diversified. Vertical FDI incurs the costs of splitting production over various geographic locations. 'Theory suggests factors that are important in these tradeoffs; some of these factors are firm or industry specific (e.g. the importance of economies of scale), some are country characteristics (e.g. the market size or factory prices)'. (Navaretti and Venables, 2004: 127) It would appear that horizontal FDI is by far the major component of outward FDI. Moosa (2002) argues that horizontal FDI may be in the region of 70% of the total. Jim Markusen, one of the leading FDI scholars, states that horizontal exceeds vertical, but acknowledges the difficulty in quantifying this. Reliable data on the breakdown between horizontal and vertical FDI is difficult to obtain. While it can be assumed that horizontal FDI still dominates, the extent of such pre-eminence is unquantifiable.

Having defined FDI for the purposes of this research, it is appropriate to move to a consideration of the body of literature which exists on FDI theory. This literature provides an appropriate investment theory within which to locate our consideration of Barry et al's model and the potential challenges and opportunities facing Irish investors into China.

Dunning's Eclectic Paradigm Investment Theory

Our consideration of Irish outward FDI and its applicability to China should be considered within a framework of investment theory. While there is no universally accepted investment theory, this section will provide an analysis of the framework within which this research is considered.

Investment theories emerged in the post-war period, with the increasing importance of FDI and multinational enterprises (MNEs). Indeed, FDI theories have developed with MNEs at their core. Researchers sought to find theories to explain the actions of MNEs and the expansion of international production. The first such approach was Ohlin's (1933) neo-classical theory, which focused on international trade theory and classic location theory. It was argued that international fund flows are caused by differences between resource endowments among competing countries. Therefore, investment should flow from capital-abundant countries to relatively capital-scarce countries, where higher marginal productivity can be achieved. Interest rate differential is seen as the variable which causes cross-border capital movements, which will cease when the marginal productivity of labour in competing countries is equalised. However, this approach has several defects. It fails to distinguish between direct and portfolio investments, so it does not address the issue of control. (Aliber's (1970) capital-markets approach also fails to incorporate this distinction.) This theory assumes that production technologies are equally well-known in all trading countries and are characterised by constant returns to scale. Also, it is constructed on the premise of a perfect market, which assumes zero transaction costs. (Eckaus, 1987) These assumptions greatly weaken the theory. Perfect competition is a useful theory for economic analysis but rarely exists, if ever. For these reasons, this theory is of limited value in seeking to analyse FDI flows and the motivation of MNEs.

Vernon (1966) developed the product-cycle theory in order to explain the existence of international production as well as international trade. He argued that, as a product moves through its life-cycle, the characteristics of the product will move through three distinct stages, from a newly developed product to a mature product to a standardised product. Each stage has implications for production. In the development stage, production must be located close to markets. During the mature stage, a higher level of capital intensity is required. In the final stage, the standardisation of production means easier imitation and increased competition. Consequently, the firm has to search for low-cost labour in overseas production locations as a means of further reducing unit costs. Vernon's theory was a response to the observation that US firms were among the first to develop new labour-saving techniques in response to the high cost of skilled labour and a large domestic market. (Du Pont, 2000) This theory proposes that the MNE needs to exploit its firm-specific advantages by moving from its home market to produce overseas in a low-cost location. Vernon made a significant contribution to the development of FDI theory, as he could explain most of the outward FDI from the USA in the 1960s. While this theory holds for some FDI, notably the movement of low-value manufacturing facilities from developed to developing economies, it does not provide an explanation for the flows of FDI between developed economies. Also, the focus on innovation makes it difficult to explain FDI in industries where innovation is not at its core.

Responding to the weaknesses in Ohlin's (1933) neo-classical theory, Hymer (1960) developed the Industrial Organisation theory. Hymer argued that FDI is a result of market imperfections, which can be caused by either the market or government, particularly tariffs and trade barriers. (Mundell (1957) had earlier recognised that FDI develops when trade in goods is impeded.) Hymer went on to argue that companies operating in a foreign country face certain disadvantages in comparison with domestic companies, such as information costs, the business culture, and the political or economic operating environments. Domestic companies are likely to have lower operating costs. Therefore, in order for FDI to occur, foreign companies must have firm-specific advantages which allow them to compete with domestic firms. These advantages, which are of an intangible nature, include superior technology, brand names, financial strength, managerial or marketing skills. It has to be assumed that the firm's intangible advantages are not available to local companies for some time after the foreign firm invests, otherwise the incentive to invest would be negated. Kindleberger (1969) developed this theory further when he argued that the comparative advantage has to be firm-specific, transferable to foreign subsidiaries, and large enough to overcome these disadvantages.

Hymer brought a new dimension to the consideration of FDI, which future researchers built on. Prior to his influential work, it was customary to treat equity investment on a par with capital flows, thereby failing to distinguish between equity and investment flows. (Du Pont, 2000) From a conceptual standpoint he introduced an analysis of the MNE as being central to our understanding of FDI. While Hymer's theory introduces the notion of a spatial dimension it does not address the location advantages which certain economies possess or how the decision to invest is reached by the individual firm. One problem with this approach is that it fails to explain why the firm does not utilise its advantages by producing in the home economy and exporting abroad, which is an alternative to FDI. Even if one accepts the impetus to invest abroad because of lower input costs, Moosa (2002: 32) contends that this theory 'does not explain why firms choose to invest in country A rather than country B'. Hymer's theory does not

provide a workable hypothesis for large MNEs which dominate international production. (Du Pont, 2000) Its only acknowledgement of location is that firms may invest in a third country in order to overcome tariffs, but the advantages which a particular location may or may not possess are not considered.
Buckley and Casson (1976) proposed an internalisation theory whose basic hypothesis is that multinational hierarchies represent an alternative mechanism for organising the firm across international boundaries. Firms are likely to engage in FDI whenever they perceive that the net benefits of ownership of foreign subsidiaries exceed those offered by international trading. (Du Pont, 2000) This theory moved away from explaining why an MNE invests abroad to the consideration of why MNEs decide to retain certain activities within the enterprise when undertaking FDI, rather than sub-contracting or licensing production. This approach centres on the logic that the market for intermediate products is difficult to manage and control, so manufacturing can be handled more efficiently within the firm. Therefore, an MNE is created when the firm decides to internalise such production across different markets. Internalisation theory negates the regulatory costs associated with operating in external markets i.e. tariffs can be avoided through local manufacturing. Thus, multinational companies prefer internalising production rather than exporting or licensing as a means of reducing transaction costs. (Williamson, 1985) However, Rugman (1980) argues that the hypothesis underlying this theory cannot be tested directly. Buckley and Casson (1989) acknowledge that statistical tests are bound to be based on simplifying assumptions and lead to the conclusion that the process of internalisation is concentrated where high incidences of R&D occur. While the internalisation theory contributes to the development of a theory of FDI and specifically that of the MNE, it fails to provide a comprehensive approach to the firm's decision to invest abroad, specifically by lacking an analysis of the locational advantages and disadvantages which a particular country can offer. This theory is of use in analysing why MNEs decide to retain production within the firm rather than to sub-contract, and will be of benefit when considering the optimum means of protecting intellectual property rights when investing in China.

While the investment theories cited above make a contribution to our understanding of investment theory, they focus on partial elements of FDI. Dunning (1979a) built on earlier models of investment and set out a comprehensive explanation of FDI and the MNE. He combined the firm-specific ownership advantage which Hymer had identified with Buckley's internalisation theory, and added a locational dimension. He built on Hymer's hypothesis that for foreign firms to operate in a different environment requires the firm to have a firm-specific advantage which offsets potential disadvantages. Bringing together the strengths of earlier theories, Dunning (1977, 1979a and 1980) provides a conceptual framework in his eclectic paradigm model (also known as OLI Advantage).

Dunning sets out three basic advantages as preconditions for MNEs to successfully undertake FDI: Ownership-specific Advantage, Location-specific Advantage and Internalisation Advantage (OLI). Dunning argues that FDI occurs when these three conditions are met. Ownership-specific advantage is based on the concept that companies possess internal advantages which are specific to the firm and related to the accumulation of intangible assets, such as advanced technology, product differentiation, product innovation, financial strength, marketing expertise or managerial skills. These advantages come in the form of an asset which reduces the firm's production costs and allow it to compete in foreign markets despite the increased costs associated with such a move. As economies have developed and globalisation has intensified, Dunning argues that there is a need for 'firms to undertake FDI to protect, or augment, as well as to exploit, their existing O [ownership] specific advantages'.(Dunning, 2000a: 169) For FDI to occur, the ownership advantages have to be transferable to a foreign country and possible to use simultaneously in more than one location. Dunning's ownership advantage is a restatement and expansion of Hymer's industrial organisation theory. Where Dunning adds to Hymer's theory is with the integration of location and internalisation advantages into one comprehensive model.

Dunning (1979a: 273) states that consideration of the questions associated with the choice of location was "not wholly satisfactory" as this issue has not been integrated with other theoretical approaches. Locational advantage refers to the institutional and productive factors available in a particular geographic area. 'More often, they are related to market characteristics, trade barriers, cost conditions and the institutional and business environment'. (Van Den Bulcke et al, 2003: 13) Locational advantage determines whether or not a particular location is attractive to inward FDI, and a strong locational advantage will reduce the firm's production costs. In the absence of locational advantage, the firm will produce in the home economy and export to the host economy.

Buckley (1989) contends that locational advantage enables MNEs to gain maximum advantage from differential prices of non-tradables in particular locations, particularly labour costs. These advantages are accentuated when they are combined with the inherent strengths of MNEs such as advanced technology, financial strength or marketing expertise. Dunning (2000a) points to the trend that many countries are endeavouring to provide the most appropriate economic and social infrastructure.

…a country or region's comparative advantage, which has been traditionally based on its possession of a unique set of immobile natural resources and capabilities, is now more geared to its ability to offer a distinctive and non-imitable set of location bound created assets, including the presence of indigenous firms with which foreign MNEs might form alliances to complement their own core competencies.(Dunning, 2000a: 178)

Internalisation advantage determines how a firm uses its ownership advantage. In deciding to enter a third country it can decide either to license production to another firm or to establish a manufacturing facility itself. If the firm does not possess internalisation advantage, then it is more profitable for the firm to exploit its ownership advantage by licensing production to an external firm. Internalisation refers to the structure of the firm and its ability to meet the demands of interacting with the market place. Internalisation theory states that as long as the transaction and coordination costs of using external arm's length markets in the exchange of intermediate products, information, technology, marketing techniques etc. exceed those incurred by internal hierarchies, then it will pay a firm to engage in FDI, rather than conclude a licensing or another market related agreement. (Dunning, 2000a: 179)
The reality is that foreign companies incur additional costs as compared with indigenous companies. These extra costs range from a culturally unfamiliar environment to legal and political uncertainties. Internalisation also avoids the difficulty of what Buckley (1987) terms 'buyer uncertainty problem'. This can occur when a firm licences another enterprise to produce its goods. The licensee obtains a transfer of information. Once it has such information, there is a risk that the receiving firm no longer considers that it should continue to pay for it.

FDI occurs only when the firm possesses ownership and internalisation advantages and the host economy offers locational advantage. While possession of ownership advantage is required for a firm to operate in a foreign market, it is the existence of location and internalisation advantages which determines the manner in which the foreign market should be entered. Buckley and Casson (1998) found that all advantages are interconnected. They contend that within these three advantages ownership-specific advantage is the main determinant of why FDI is undertaken; location-specific advantage determines where to undertake FDI; and internalisation advantage determines how FDI should be undertaken. Ietto-Gillies (2005) contends that the strength of Dunning’s approach is the contemporaneous analysis of these three variable advantages.

Dunning’s contribution to FDI theory is that he provides a comprehensive framework for discussion of the motives underlying FDI. ‘The eclectic paradigm was developed by Dunning by integrating the industrial organisation hypothesis, the internalisation hypothesis and the location hypothesis’. (Moosa, 2002: 36) He also explains the choice of entry into foreign markets. The strength of Dunning’s model, as compared with earlier theories, is that it offers an inclusive and complete framework within which to analyse FDI and the role of the MNE.

This being said, Dunning has his critics. Ietto-Gillies (2005) argues that the original eclectic paradigm hypothesis is too wide to be useful in practice, with at least 20 possible ownership advantages, 11 internalisation advantages and 16 locational advantages to be considered. In later works Dunning acknowledges the difficulties which the number of variables can pose and uses terms such as ‘systemic framework’ or ‘paradigm’ rather than ‘theory’. ‘The eclectic paradigm is more to be regarded as a framework for analysing the determinants of international production than as a predictive theory of the multinational firm’. (Dunning, 2000b: 126) Dunning suggests that the key to operationalising his paradigm lies in contextualising the variables e.g. the contextualisation of the ownership advantage can be achieved by reference to the kind of multinational enterprise which is most appropriate to the activity, be it resource seeking, market seeking, efficiency seeking or asset seeking.

Dunning’s framework commands strong support within international business theorists. ‘Any conference on international business is likely to have a number of papers using Dunning’s framework. It has certainly been successful in introducing the taxonomy of OLI advantages’. (Ietto-Gillies, 2005: 117) ‘A striking feature of this [FDI] literature is its overwhelming reliance on the OLIparadigm framework’. (Du Pont, 2000: 21) Ietto-Giles accepts that the strongest point of Dunning’s approach is that he highlights how internationalisation and locational issues are interlinked. This means that issues specific to firms and their competitive advantages must be seen in conjunction with issues related to local conditions and to issues of markets and industrial organisation.

Given the diversity of opinion within academic writing, there is unlikely to be consensus on the most appropriate theory to explain FDI. ‘There is not one but a number of competing theories with varying degrees of power to explain FDI’. (Agarwal, 1980: 740) Most theories of FDI are under-determined and deal only partly with observed trends. (Du Pont, 2000) However, Dunning provides a framework within which to evaluate both the firm and the location chosen for FDI. Other theories consider these aspects in isolation. Du Pont (2000: 14), while a keen supporter of Hymer’s approach, acknowledges that:

Dunning offers a rich conceptual framework for explaining not only the level, form and growth of MNC activity, but also the way in which such activity is organised. Furthermore, the paradigm offers a robust tool for analysing the role of FDI as an engine of growth and development as well as for evaluating the extent to which the policies of source and host governments are likely both to affect and be affected by that activity.

In response to criticism that the eclectic paradigm is a static rather than dynamic analysis, Dunning developed the Investment Development Path (IDP) hypothesis:

The basic hypothesis of the IDP is that as a country develops, the configuration of the OLI advantages facing foreign-owned firms that might invest in that country, and that of its own firms that might invest overseas, undergoes change, and that it is possible to identify both the conditions making for the change and their effect on the trajectory of the country’s development. (Dunning, 2001: 180)

The IDP hypothesis ‘proposes that there is a U-shaped relationship between economic development and a country’s net outward investment position’. (Barry et al, 2003: 342) The IDP identifies five stages of development through which a country will pass. The first stage is one of pre-industrialisation, when a country has little or no inward or outward FDI because it does not possess sufficient locational advantages. As government policy develops or natural resources are exploited, the first wave of inward FDI will concentrate on the natural resource sectors, labour intensive industries, construction and possibly tourism. ‘Depending on the extent to which the country is able to create a satisfactory legal system, commercial infrastructure and business culture, and to provide the business sector with the transport and communication facilities and human resources they need; and depending on its government policy towards inward direct investment, its locational attractiveness will increase’. (Dunning, 2001: 181) This second stage sees the development of some location specific advantages which leads to inward FDI targeting the emerging domestic market in consumer goods and infrastructure.

The improvement in the locational advantage of a country may help indigenous firms to upgrade their own ownership advantage. As countries move along their development path, the OLI configuration facing outward and inward investors continues to change. Some foreign (and domestic) firms, which earlier found a country attractive to invest in because of its low labour costs or plentiful natural resources, no longer do so. In other cases its L [locational] advantages have become more attractive as an indigenous technological infrastructure and pool of skilled labour is built up. This, in turn, makes it possible for domestic firms to develop their own O [ownership] advantages and begin exporting capital. (Dunning, 2001: 181)

Stage three witnesses a modest rate of growth in inward FDI, which is eventually overtaken by outward FDI. The fourth stage sees the country become a net outward investor with location advantage based on created assets and indigenous firms' ownership advantage. Dunning contends that whether this happens or not depends on the strategy of individual firms and the policies of national governments to generate the competitive advantage of domestic firms and by making the location attractive to both domestic and foreign investors.

The final stage sees the net FDI flow position approaching zero with permanently high stocks of both inward and outward FDI. The net FDI flow position will be determined by short-term trends related to exchange rates and economic cycles. Dunning and Narula (1996) argue that this stage of development has been reached by the more advanced industrialised economies, whose wealth creation and productivity growth are increasingly based on the ability to utilise intellectual capital. It is possible to identify the Irish investment experience in several of the stages identified by Dunning. We shall return to this below when we consider the composition of Irish outward FDI.

Dunning sets out a theory which is broadly accepted internationally, and which provides a strong analytical framework in which to locate this research. No other theory offers such a holistic and dynamic approach or can so adequately encompass the characteristics of the firm and the specific attributes of the location chosen for inward FDI. For this reason, it is chosen as the framework for the analysis in which the nature and scope of Irish outward FDI into China is explored.

The Role of the Multinational Enterprise in FDI

It was the attempt to explain the actions of MNEs and the expansion of international production which led to the development of FDI theory. Indeed, FDI and MNEs are so intertwined that the motivation for FDI may be used to distinguish between MNEs and other firms. (Moosa, 2002) An understanding of why investment by a foreign firm differs from that made by a domestic firm assists in our appreciating the dynamics which underlie FDI. As FDI entails higher costs for the investing firm, MNEs must possess an advantage over local firms sufficient to offset the costs of international coordination, or the locational benefits will be captured instead by indigenous firms. (Froot, 1993) FDI has been described as the highest commitment a firm can make in international business as it involves not only the infusion of capital but also the transfer of personnel and technology. (Daniels and Radebaugh, 1995) Research in the areas of MNEs and FDI provides a theoretical underpinning which suggests that the MNEs' ability to organise their unique, firm-specific assets and resources over many countries and exploit the advantages of operating in these countries fundamentally alters their approach to business, the nature of their assets and resources, and accordingly the impact they have on host countries. (Scott-kennel, 2004)

In seeking to understand the role of MNEs, Hymer 'is regarded as a seminal figure in the establishment of the theory of the multinational enterprise'.**[i]** (Buckley, 2006: 140) Hymer clearly distinguished between portfolio and direct investment, with the latter offering managerial control.

Hymer focused on the specific advantages which the firm possesses, which enable it to engage in outward FDI. Hymer borrowed D.H. Robertson's description of MNEs as 'islands of conscious power in an ocean of unconscious co-operation'. (Hymer, 1970: 441) He forecast that increasing specialisation by MNEs would force the global economy to become spatially specialised with a hierarchy of specialised locations emerging. However, Graham (2006) points to Hymer's lack of success in arriving at a dynamic model of the MNE. Buckley and Casson (1998) argue that there is a need for a new agenda in models of the MNE based on dynamic analysis and a move away from Hymer's static analysis. Such a new agenda 'highlights the uncertainty that is generated by volatility in the international business environment. To cope with flexibility, corporate strategies have to be flexible'. (Buckley and Casson, 1998: 22)

Navaretti and Venables (2004) see such a dynamic existing in Dunning's eclectic paradigm. In analysing Dunning's work they outline three defining questions underlying a firm's decision to internationalise – what are the costs and benefits to the firm of splitting production; whether the firm's foreign activities should be internal to the firm or outsourced to independent operators; and what are the effects of multinational activity on the home and host countries. These three issues are now examined in turn.

The decision on whether to concentrate production in a single country or disperse it across several countries has associated costs and benefits. The cost of splitting off production to a third country also entails costs in terms of the efficient use of factors of production. Multinationality is most likely to occur when there are high firm-scale economies, combined with relatively low plantscale economies. Navaretti and Venables (2004) argue that the gain in market power will be even greater if the investment takes the form of a merger or acquisition, which directly eliminates a potential rival. 'Market power considerations are a major motivation behind both domestic and international M&A activity'. (Navaretti and Venables, 2004: 28) But this form of market entry poses particular challenges in China, a matter we shall return to later.
A perceived benefit of investing abroad is the incentive to reduce production costs.

MNEs will gain from moving unskilled labour-intensive activities to countries where unskilled wages are low, R&D-intensive activities to places where scientists are relatively cheap and so on. The expansion of EU investments in Central and Eastern Europe countries, US investments in Mexico, and the investments in software companies in Bangalore are all driven by the aim of reducing costs of production.(Navaretti and Venables, 2004: 29)

They qualify this statement by pointing out that factor prices have to be adjusted for the quality of the factor input. 'The evidence suggests that FDI rarely goes to the lowest-wage economies, going in preference to countries that have abundant labour with basic education… Firms look at the cost of labour, not its abundance'. (Navaretti and Venables, 2004: 29)

From an organisational perspective, FDI is a choice to retain functions internally within the firm rather than relying on other actors in the market. There is also the option of licensing the franchising. There are costs and benefits associated with retaining the function internally or relying on market transactions. 'Internalising may bring a direct cost penalty, but avoids problems of contractual incompleteness in dealing with outside agents'. (Navaretti and Venables, 2004: 25) Internalising production also has the advantage of better protecting one's intellectual property. The protection of intellectual property is an on-going challenge in the Chinese economy, an issue which will be considered in chapter four.

The decision to internationalise one's production has an effect on both the host and the home economies. Navaretti and Venables (2004) identify three channels through which the effects on host (receiving) and home (sending) countries are transmitted: product market effects, factor market effects and 'spillover effects'. In the case of product market effects, the firm undertaking FDI will change the quantity of goods it buys and sells in the host and home country when it undertakes FDI. In the case of substitute products in the host economy, local firms may be unable to sell as much produce as heretofore and crowding-out can occur. Consequently, consumers may not be any better off and local firms may be forced to sell less or perhaps leave the market. Alternatively, the MNE may increase competition in the marketplace and perhaps also increase quality or variety, which will subsequently raise consumer welfare. If the MNE has higher productivity than local enterprises, then consumers may see a price reduction.

Factor market effects can occur in both labour and capital markets. In general, when a MNE sets up in a host country, there is an inflow of funds. It is not normal practice to raise the funds on the local market (this is a pertinent issue in the construction sector in China, an issue that we will return to, given the strength of this sector in traditional Irish outward FDI). In the case of the labour market, a range of situations may occur. The demand for different categories of labour will increase in the host economy and may fall in the home economy, depending on the type of investment undertaken. The establishment of an MNE may also have an impact on skilled labour in both economies. If the jobs being established in the host economy require a certain degree of skill and such skill is in short supply, then wage levels will increase as employees move between companies. This phenomenon is currently evident among English-speaking educated Chinese executives, for whom there is an ever-increasing demand, particularly in areas such as Shanghai and Guandong. As stated above, this issue features in our research.

It is argued that the most important benefits to accrue from FDI are a variety of 'spillovers', which may be technological or pecuniary externalities. The former arise when FDI imposes costs or benefits that are not directly transmitted through markets. The latter arise when effects transmitted through markets are not fully paid for, so parties to the transaction may receive economic surplus. (Navaretti and Venables, 2004: 41) Technological externalities include technology transfer and the acquisition of labour skills. 'It [FDI] can bring not only capital but also new technologies and skills that might not otherwise be obtainable'. (Eckaus, 1987: 127) Technological changes have not simply altered the ways in which firms conduct their overseas business activities, but they have made possible the creation of a new infrastructure for carrying out diverse operations within a unified structure. (Du Pont, 2000) The insistence of the Chinese authorities on obtaining a transfer of technology through FDI will be considered during our research. Also considered will be the potential impact which this has for firms seeking to protect intellectual property rights.

… the overwhelming evidence for MNEs both operating abroad (foreign subsidiaries) and at home (headquarters and home plants) is that they perform better than fully national firms… The analysis of firm-level data for the UK, the US, Italy and various other developed and developing countries reports that average labour productivity in foreign subsidiaries of MNEs is between 30% and 70% higher than in national firms and for the home activities of MNEs it is approximately 30% higher'. (Navaretti and Venables, 2004: 42)

MNEs do not perform better simply because they are multinational players. They are larger in scale, engage in R&D, use more capital and generally employ more skilled labour. Vaupel (1971) compared US MNEs as with domestic US firms. He found that MNEs incurred higher R&D expenditure, had higher net profits, had higher average sales, paid higher wages in the US, and had a higher export/sales ratio. Using an econometric model, Grubaugh (1987) obtained results supporting the importance of R&D, product diversity and size as characteristics of MNEs. The emphasis on R&D confirms the link with Dunning's ownership advantage. By pursuing R&D, the firm increases its internal advantage and affords itself higher levels of technology than its rivals.
Policy makers should be reassured by the evidence that when a national firm transfers part of its production to cheap-labour countries or is bought out by foreign investors, its performance is generally better than if the firm had not invested abroad or had stayed national. Moreover, MNEs often have features (size, R&D, investments, brands etc.) that national firms do not have and which in themselves are important, as they enrich the domestic production structure and

they improve its average performance. (Navaretti and Venables, 2004: 43)
This is an important consideration and one which we shall return to in chapter five, during our discussion of public policy on outward FDI.

Why FDI Occurs?

Dunning offers a theoretical framework within which investment occurs and which will guide the consideration of our hypothesis. However, it is also important to explore the specific motivation which leads to the individual firm's investing in a third country.

Hewko (2002) argues that if a country offers significant business opportunities and does not present any formal barriers to investment it will attract foreign investment. As the market size grows to a critical value, FDI will start to increase with further expansion. Navaretti and Venables (2004: 141) contend that 'the larger the host market the greater the likelihood that MNEs will be able to recoup the fixed cost of their foreign plants'. Secondly, a stable political and social environment is conducive to the attraction of FDI. Conversely, large and unexpected modifications of legal and fiscal frameworks may drastically change the economic outcome of a given investment.

Studies indicate that the effect of labour cost on FDI is controversial. Goldberg (1972), Saunders (1983), Schneider and Frey (1985), Culem (1988) and Moore (1993) found that a rise in the host country's wage rate would discourage FDI. On the other hand, Nankani (1979), Kravis and Lipsey (1988) and Wheeler and Mody (1990) found the opposite. A possible explanation for these conflicting results is offered by Lucas (1993), who shows that a rise in the wage rate of the host country means an increase in the costs of production, which should discourage production and consequently inward FDI. However, the increase in wage levels may cause a movement to more capital-intensive means of production, which may result in higher inward FDI. It is fair to assume that in the case of low-skill, high-volume manufacturing, labour costs are an important determining factor. However, as companies increase the value of their output, skill levels increase and the manufacturing process becomes more complex. Quality skilled labour is then likely to assume a higher degree of importance, with less emphasis on labour costs. Navaretti and Venables (2004: 140) contend that the reason for the mixed results is because of the need to differentiate between horizontal and vertical FDI. '[W]e expect VFDI to increase with differences in factor endowments and factor costs, as this is precisely what investors are looking for'. Reuber et al (1973) assert that low labour costs in developing countries provide the basis for high rates of return on export-oriented products. This assertion will be examined later in the case of China, specifically in the case of Irish FDI into China.

A country's degree of openness to international trade should have a direct relationship to the level of FDI. Kravis and Lipsey (1988) report a strong positive effect of openness on FDI. Wheeler & Mody (1992) observed strong evidence in the manufacturing sector, but a weak negative link in the electronics sector. This points to the lack of homogeneity in FDI. There are various submarkets for FDI depending on the level of skill, value of output etc. This issue will be revisited when determining which sectors of the Irish economy hold the most potential in terms of inward FDI into China. Allied to this is the question of tariffs.

Studies find that tariff jumping is an important motive for investments in the US and EU. For example, Barrell and Pain (1999b) examine the determinants of aggregate flows of Japanese FDI into both the European Union and US in the 1980s. They find that Japanese FDI into a particular country is strongly influenced by the extent of that country's trade protection measures and, in particular, by its extent of antidumping activities.' (Navaretti and Venables, 2004: 137) Countries that are more open to trade tend to provide and receive higher levels of FDI. (Lipsey, 2000) Bajo-Rubio and Sosvilla-Rivero (1994) found a significant effect of the tariff rate on FDI. Indeed, Blonigen and Feenstra (1996) suggest that FDI may be induced by the threat to introduce protectionist measures. A further consideration is the relative strength or weakness of the host economy's currency. The weaker the currency of a country, the less likely are foreign firms to invest in that location. This is because an income stream from a country with a weak currency is associated with exchange rate risk, and an income stream is therefore capitalised at a higher rate by the market when it is owned by a weak currency firm. Chakrabarti (2003) states that a strong currency is often interpreted as an indication of the greater competitiveness of the host country.

Intercultural transaction costs are inevitable when cultures meet. They are produced by mistrust, miscommunication, language difficulties, clashing values, conflicting senses of propriety etc. Prejudice or ignorance may distort the investor's perception of the foreign market. The host-country consumer may have a disdain for goods made by a particular country. Cultural compatibility can enhance a destination for foreign investors, but cultural estrangement can nullify the attractiveness. The importance of Chinese culture will be considered further in this chapter, given its strong influence in Chinese society.

Another consideration is the efficiency and transparency of the legal system. A transparent legal system reduces transaction costs for economic actors and is of considerable benefit in attracting FDI. Needless to say, an arbitrary legal system will be relatively uninviting for investors. In the latter case, there may be some investors who are willing to invest on the basis of very high potential returns, but generally investors require legal certainty.
Finally, most governments adopt policies aimed at encouraging inward FDI by offering incentives. Moosa (2002) identifies the incentives which governments offer as tax reductions, exemption from customs duties, accelerated depreciation, grants, loan guarantees, market preference (including monopoly rights) and low cost infrastructure. The effect of incentives in successfully attracting FDI is far from clear. It is arguable that incentives benefit a firm which would have made the investment in any event. The results of Agarwal's (1980) empirical studies show that incentives have a limited effect on the level of FDI, as investors base their decision on risk and return considerations. Reuber at al (1973) found that incentives can play a role in encouraging small firms with limited experience, but their overall impact is small.

Views diverge on the effect of taxation on FDI. 'Hines (1999), in his survey of empirical studies, concludes that "the econometric work of the last 15 years provides ample evidence on the sensitivity of the level and location of FDI to tax treatments"…. There is also evidence that responsiveness to tax has increased in recent years, as might be expected if VFDI, which is not tied to serving a particular market, has increased in importance'. (Navaretti and Venables, 2004: 139) Buckley (1987) argues that the urge to avail oneself of transfer price manipulations may induce a bias towards low tax countries. Devereux and Griffith (1998) contend that differences in taxation policies have an impact once the decision to invest overseas has already been made, but not in the making of the decision itself. Newman and Sullivan (1988) conclude that the modelling and estimation limitations of existing studies make it difficult to reject the hypothesis that taxes influence business location, but the results are not clear. The views of commentators on the effect of taxation are mixed. Taxation is part of a package of measures which investors find attractive. It is the overall environment of a particular country, as constituted by its political, social and economic conditions, which attracts FDI. (Moosa, 2002) Common determinants of FDI emerge from the above literature: market size, labour costs, trade barriers, the growth rate, openness, the exchange rate, political certainty, culture shock, the legal system and business opportunities. Theoretically, the size of the host market, low labour costs, fiscal incentives, a favourable business climate, and trade openness should have positive impacts on FDI, while high transportation costs, bureaucratic red tape, and political instability should act as disincentives. *Table 1* gives some useful pointers in determining the likelihood of whether a firm will invest in a particular country or not.

Table 1: Determinants of FDI: Theoretical Predictions

Determinants	Prediction by type of investment Horizontal	Vertical
Determinants relating to types of firms or industries		
Firm-level economies of scale	+	+
Plant-level economies of scale	-	?
Production-specific trade costs	+	-
Difference in factor intensity between stages of production	?	+
Determinants relating to type of country		
Trade costs (distance, trade barriers etc.)	+	-
Market size	+	?
Factor cost differentials	?	+

Source: Navaretti and Venables (2004: 31)

Table 1: Determinants of FDI: Theoretical Predictions
Source: Navaretti and Venables (2004: 31)

These factors should be borne in mind when considering the determinants relating to which sectors of the Irish economy should focus their attention on China. Vertical FDI is likely to occur when factor cost savings are large relative to the costs of fragmenting activities in two or more locations. The table shows a clear prediction in the case of horizontal FDI and market potential. This will emerge as one of the key rationale for Irish firms investing in China.

Having set out the theoretical framework within which this research will be conducted and the role of MNEs in today's globalised economy, the literature on Irish outward FDI is now considered.

Irish Outward FDI

By way of introduction, it is important to point out that there is a limited amount of literature on Irish outward FDI. While Forfás, the Irish Government's national policy and advisory board for enterprise, trade, science and technology, has conducted one study on Irish outward FDI, the key published work in mainstream academic journals is Barry et al (2003). Both Barry et al's and Forfás' analyses have focussed on the US and UK as a destination for outward FDI. The findings of a survey undertaken by the Irish Business and Employers Federation (IBEC, 2006) on trade and investment with Asia will also be considered. While most of the data refers to trade, some interesting observations are made on investing in China. In addition, the perceptions of firms on trade issues may be of benefit in corroborating the findings of this research e.g. in the domain of intellectual property rights.

Forfás (2001) refers to Ireland's successful track record in attracting inward FDI. It also acknowledges the growing trend of outward FDI by Irish multinationals but points to the absence of analysis of this issue. It points out that traditionally the bulk of Irish FDI outflows came from a relatively small number of Irish firms. 'While these "old economy" firms still dominate the stock of Irish-owned direct investment assets overseas, a small number of "new economy" high-technology firms have recently started to make significant overseas investments' (Forfás, 2001: 4).

Forfás (2001) alludes to the lack of statistical data on Irish outward FDI. There are three reference sources, the Central Statistics Office (CSO), Eurostat and the UN Conference on Trade and Development (UNCTAD). However, both UNCTAD and Eurostat source their data from the CSO. The information available is limited and does not provide a comprehensive time-series on Irish outward direct investment flows and stocks by sector of origin or country of destination. Accepting this caveat, an analysis of the data for recent years points to an interesting change in patterns in Irish investment.

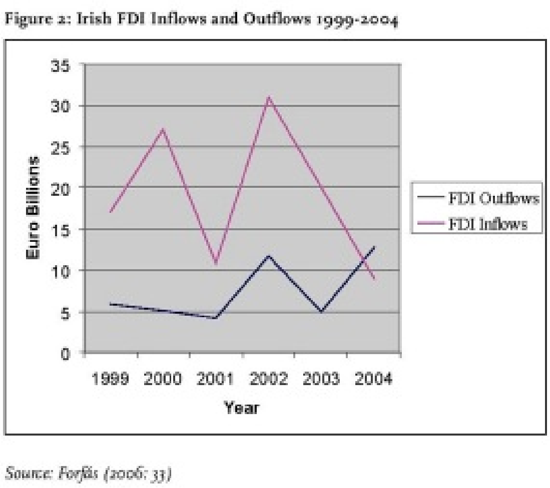


Figure 2: Irish FDI Inflows and Outflows 1999-2004
Source: Forfás (2006: 33)

The most interesting data available is the significant change in FDI flows since 2001. FDI outflows have increased significantly since 2001, and in 2004 were the largest ever recorded at € 12.7 billion. (Forfás, 2006) *Figure 2* gives a representation of the changing trends in Irish FDI.

This graph identifies a sharp decline in inward FDI and a gradual increase in outflows.

Ireland was previously characterised by exceptionally high inflows and average outflows for a developed country. The trends of 2004 may signal a departure from this trend. Inflows of € 9.1 billion in 2004 represented a sharp decline from the peak of € 31.2 billion achieved in 2002, even though inflows still remain high relative to other similar countries. Much of this decline was due to particularly large repatriation of profits by multinationals in 2004. This trend is likely to continue in 2005 and 2006, as changes to US tax law subject earnings by US companies based in Ireland to considerably lower tax rates. (Forfás, 2006: 39)
We can say that an important milestone was reached in 2004 when outflows exceeded inflows for the first time by € 3.6 billion. (CSO, 2006) Barry et al (2003) have examined this trend and argue that it provides evidence of Ireland's conforming to Dunning's IDP hypothesis.

The cumulative Irish stock of FDI invested abroad is estimated to be € 61 billion in 2004. This is equal to 41% of GDP, which is similar to the ratio for the EU-15 as a whole. (Forfás, 2006) However, three years earlier Forfás (2001) pointed out that the ratio of stock of outward FDI to the stock of inward FDI was lower in Ireland than in any other advanced economy and was significantly lower than in most other small EU countries. 'Ireland's rather unique direct investment relationship with the rest of the world reflects not only the high levels of inward investment into Ireland compared with other advanced countries, but also very low levels of outward investment flows from Ireland'. (Forfás, 2001: 8)
The low levels of outward FDI reflect a number of historical factors. With the exception of financial services, Ireland has few large indigenous firms in the industries that generally generate the bulk of global FDI flows, such as oil, cars, telecommunications, electronics and pharmaceuticals. 'Other factors included Ireland's relatively recent industrialisation, the historically heavy focus of development policy on inward investment, and the more active promotion and facilitation of outward investment by other EU governments'. (Forfás, 2001: 10)

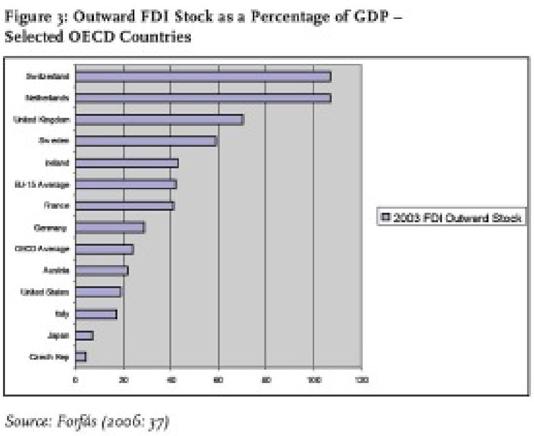


Figure 3: Outward FDI Stock as a Percentage of GDP – Selected OECD Countries
Source: Forfás (2006: 37)

Detailed official statistics are not available on the destination of Irish outward FDI. The most informative information available is provided by LOCOmonitor (2006), a global database that tracks greenfield projects internationally and identifies 212 instances of Irish outward FDI in the period 2002 to 2006 (two months only). *Table 2* sets out the regional destination of Irish outward FDI.

This data should be treated with caution as it relates to Greenfield investments only and does not include mergers and acquisitions (M&A). Accepting this caveat, this data shows that the most important destinations for Irish outward FDI are Western and Eastern Europe and North America. 'Within Western Europe, FDI to the United Kingdom is by far the most important destination, accounting for two-thirds of Irish FDI to Europe… It is also notable that Asia, including developed countries such as Japan and developing countries like China, attracted less than 10% of Irish FDI projects in the period 2002-2006'. (O'Toole, 2007:392) A detailed breakdown by country is not available, but the provision of such information in future years would add greatly to our ability to analyse outward FDI flows.

Barry's model on Irish outward FDI
As set out above, the Investment Development Path (IDP) hypothesis proposes that the changing pattern in FDI flows is systematically related to a country's level of economic development. With increasing economic prosperity, a country evolves from being a net recipient of investment to being a net outward investor.
Barry et al (2003) contend that Ireland is an interesting IDP test case because of its rapid economic development and the heavy reliance of Ireland on inward FDI

as compared with other EU countries. They examine if, given the magnitude of inward FDI, the pattern predicted by the IDP concept is realised. Pointing to the unavailability of time-series data over a considerable period on outward FDI flows, they show that Ireland in the late 1990s had the third largest stock of inward FDI in the EU, after Belgium/Luxembourg and the Netherlands**[ii]**. On the other hand, Ireland's stock of outward investment was the third lowest. 'This suggests that until recently outward FDI flows from Ireland were not very large, as the IDP concept would suggest'. (Barry et al, 2003: 342)

While acknowledging the lack of consistent time-series data on outflows from Ireland, Barry et al (2003) argue that there is evidence of increasing outflows, which is consistent with the Investment Development Path hypothesis. Using CSO data and material from the US Department of Commerce (the only source of a comprehensive time-series on both FDI inflows and outflows by nationality), Barry et al (2003) point out that Irish FDI into the US grew more rapidly than US FDI into Ireland in the 1980s and 1990s, to such a degree that they were broadly similar by the end of the 1990s. Their analysis of US data 'provide[s] evidence of a U-shaped relationship between Irish GDP and the country's net outward FDI position with the US, a pattern consistent with the IDP concept'. (Barry et al, 2003: 345)

Table 2: Regional Destination of Irish Outward FDI

	2002		2003		2004		2005		2006 (Jan-Feb)		2002-2006	
Region	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Africa	1	2.0	2	4.3	2	4.3	1	1.7	-	-	6	3
Developed Asia	2	3.9	-	-	2	4.3	2	3.4	-	-	6	3
Europe	34	66.7	25	54.3	21	45.7	36	61.0	7	70.0	123	58
Developing Asia	2	3.9	5	10.9	2	4.3	4	6.8	-	-	13	6
Eastern Europe	4	7.8	3	6.5	13	28.3	10	16.9	1	10.0	31	15
Latin America	1	2.0	2	4.3	2	4.3	2	3.4	-	-	7	3
Middle East	-	-	2	4.3	1	2.2	-	-	-	-	3	1
North America	7	13.7	7	15.2	3	6.5	4	6.8	2	20.0	23	11
TOTAL	51	100	46	100	46	100	59	100	10	100	212	100

Source: O'Toole (2007: 393)

Table 2: Regional Destination of Irish
Outward FDI
Source: O'Toole (2007: 393)

While the IDP concept is silent on the distinction between vertical and horizontal FDI, Barry et al (2003) predict that as production costs rise there is an incentive for domestic firms to engage in vertical FDI, moving labour-intensive components to countries with a locational advantage in low-cost labour.

Later in the process, firms are able to compete in overseas markets and so engage in horizontal FDI. The incentive for horizontal outward FDI may develop as the economy becomes wealthier and domestic firms seek to maintain their competitiveness. (Barry et al, 2003) Also, economic development results in rising labour costs in the home economy, leading to a reduction in inward investment flows, and creates an incentive to engage in vertical FDI.

Turning to the composition of Irish outward FDI, Barry et al (2003: 345) analyse the available global data on the sectoral destination of Irish acquisitions overseas and identify that "the bulk of Irish outward FDI is of the horizontal type." They also point out that outward FDI is predominately in non-traded sectors. Their work is a valuable and important contribution to our understanding of Irish outward FDI as it identifies the nature and composition of Irish FDI in the case of the largest markets in which Irish investment is made, i.e. the UK and US. This research, which focuses exclusively on China, adds further to our knowledge as it is examines Irish outward FDI to a developing economy.

Table 3 sets out the sectoral distribution of overseas acquisitions in the US by EU firms, by all countries and by Irish firms. **[iii]**

The second column shows the sectoral composition of acquisitions by all overseas firms in the US. Data for this group is broadly similar to that for acquisitions by EU firms, with the exception of the financial services sector, which has a greater dominance among EU acquisitions. What is striking is the divergence of Irish acquisitions from these two groups. The most important sectors for Irish acquisitions are financial services;

Table 3: US M&A activity by sector, average annual share1993-99: (1) by EU firms; (2) within the US; and (3) by Irish Firms

Sector	Cross-border M&A by EU firms	Cross-border M&A by all firms	Cross-border M&A by Irish firms
Food, drink and agribusiness	5.9	5.7	17.5
Print, paper and publishing	2.8	4.5	16.2
IT, Telecoms and electronics	5.1	7.8	4.0
Chemical and Pharmaceuticals	14.4	17.0	9.5
Other manufacturing	24.2	20.5	5.8
Construction, property	1.0	1.8	22.2
Financial Services	32.4	22.5	22.5
Services (consulting, retail etc)	14.3	20.2	2.0
Total	100.0	100.0	100.0

Source: Barry et al (2003: 345)

Table 3: US M&A activity by sector, average annual share1993-99: (1) by EU firms; (2) within the US; and (3)

by Irish Firms
Source: Barry et al (2003: 345)

construction; food, drink and agribusiness; and print, paper and publishing. The result for the financial service sector is broadly in line with the data for all investment in the US, approximately ten per cent below the EU data. Barry et al (2003) point out that as the food, drink and agribusiness sector accounts for 27% of Irish manufacturing employment compared to 12% within the EU15, the result for this sector is not greatly surprising. However, the figure for the construction sector is notable and reflects the traditional strength of this sector in the Irish economy with outward FDI having a historical basis. 'Expansion abroad in such largely nontradable sectors entails horizontal rather than vertical FDI. If companies in these sectors expand abroad they do so for market-access reasons i.e. in order to penetrate and grow in new markets'. (Barry et al, 2003: 345)

Barry et al (2003) point to a large increase in 2000 by Irish firms in hi-tech sectors such as information technology and the pharmaceutical industry. The IDP concept would indicate that this development is a consequence of economic convergence. This points to a new generation of Irish MNEs investing abroad and supports the trend identified by Forfás (2001).

Barry et al (2003) question why there is so little outward Irish vertical FDI to lower-cost production locations. Recalling that firms invest abroad because they possess firm-specific assets (ownership and internalisation advantages), it is suggested that 'R&D and superior product differentiation through advertising are generally found to be the most important firm-specific assets associated with multinationality'. (Caves, 1996; Markusen, 1995)… 'Irish multinational companies do not appear therefore to follow the standard pattern associated with multinationality'. (Barry et al, 2003: 346) They propose that the predominant proprietary assets which Irish firms possess are in the fields of management and expertise, mainly in non-traded sectors.
Barry et al suggest that proprietary assets other than R&D and advertising appear to be associated with the horizontal multinationalisation of Irish firms. 'The fact that the proprietary assets of Irish MNEs do not lie in these areas serves as an illustration of the difficulties facing firms in late-developing regions in surmounting the entry barriers that characterise more conventionally multinational sectors'. (Barry et al, 2003: 346)

Ireland's development along the Investment Development Path and the nature of its outward FDI has implications for Irish investment in China. This research analyses the relevance of Barry's model that Irish outward FDI flows are disproportionately horizontal and oriented towards non-internationally traded sectors, for Irish FDI into China by undertaking research among all Irish companies (employing ten or more staff) which have invested in China. This permits an analysis of whether or not such FDI is disproportionately horizontal. Furthermore, the composition of Irish FDI in China to date is examined to analyse whether it is to be found in the internationally-traded or non-traded sectors.

China and Inward FDI

Wei and Liu (2001) identify China's decision in 1979 to accept FDI as being the result of a fundamental shift in political leadership and economic policy. The new Chinese leadership recognised that attracting FDI was important for several reasons. It would introduce foreign capital without increasing China's external debt. It would introduce advanced technology, equipment and managerial expertise. It would help improve technology levels in existing industry and introduce export-oriented practices. It would increase China's social capital through training and skill transfer. Finally, it would create additional jobs, probably at higher wage levels.

There have been four distinct phases of development of FDI in China since 1979: the experimental period (1979-83); the gradual development period (1984-91); the peak period (1992-98); and the adjustment period (1998-present). In the experimental period (1979-1983) a limited amount of FDI was introduced into four special economic zones (SEZs) – Shenzhen, Zhuhai, Shantou and Xiamen. Foreign investors had no experience of investing in China since 1949 and were likely to be reluctant. However, these regions enjoyed strong links with Hong Kong and Taiwan. Accordingly, investors from Hong Kong and Taiwan were more likely to avail themselves of the opportunity to invest.

Over the past twenty-five years Chinese GDP and per capita GDP have grown at an annual rate of 9% and 8% respectively. In the last few years economies such as China and India have become the most favoured destinations for FDI as investor confidence in these countries has soared. According to the FDI Confidence Index (A. T. Kearney, 2005), China and India hold the first and second position respectively, whereas the United States has slipped to third position.

Until recently the dominant source of inward FDI in China has been Hong Kong, followed by Japan, the United States and Taiwan. Approximately 59% of FDI has gone to the manufacturing sector, much of which is in labour-intensive industries such as textiles and mechanical and electronic products. (Wei and Liu, 2001) With structural changes in the Chinese economy the composition of inward FDI has also altered. In 1989, 83.3% of FDI was in manufacturing sectors. By 1993 this figure had dropped to 45.9%, while the share of real estate and utilities had risen from 9.4% to 39.3% in the same period. (Du Pont, 2000) This sharp increase in real estate and utilities is of interest to commentators on Irish outward FDI given the level of outward Irish FDI in the construction sector. The movement away from manufacturing in favour of the service sector should be of benefit to Irish investors given the predominately non-traded nature of Irish outward FDI, as identified by Barry et al. This issue will be re-examined following the elucidation of the results of our research.

Li and Li (1999) explore the reasons why MNEs invest in China. They identify two categories of investors in China. Firstly investors from developed economies, such as EU countries, USA and Japan, who tend to invest in the larger cities such as Shanghai, Guangzhou, Tianjing, Dalian and Beijing. They tend to introduce new technology, new management styles, the scale of investment tends to be larger and the focus is on exploiting market opportunity.

The second category comprises mainly Asian investors (excluding Japan), such as Hong Kong, Macau, Singapore and South Korea. Investments from this category are mostly in labour-intensive industries with production geared towards exporting. The size of the investment tends to be smaller and few investments bring new technology to China. Li and Li (1999) argue that while cheap labour is an important determinant for MNEs in this category, companies in the first category are likely to be attracted by the large and growing consumer market and the significant potential for future development. This phenomenon will be explored in our research to examine whether or not Irish MNEs conform to this categorisation.

While FDI is still concentrated in the coastal region, the Chinese Government currently has a policy of ‘opening up the west’. This will see a strong push to open up central and western regions of the country with associated government incentives, and can be expected to be a dominant theme in the next phase of China’s FDI history. This policy has a bearing on inward investment decisions and will be explored later within the context of our consideration of the regional dimension of FDI in China.

While Chinese society has undergone profound changes in the past twentyfive years and has made unprecedented gains in economic growth, traditional values still exert a strong influence. The investment challenges which China holds will be explored fully in chapter three, but two areas, relationships and contract law, are of particular importance to the conduct of business in China. Accordingly, they will be considered at this stage in order to provide a foundation for our later discussion.

Relationships and Contract Law

At the inter-cultural level, networking can bridge the gap between business people of different nations and cultures, hence stimulating trade and investment (Luo, 1998). Networking at both a personal and corporate level in China has its roots in Chinese culture and Confucianism. A particular form of networking has developed over the centuries and is referred to as Guanxi. This refers to the concept of drawing on connections so as to secure favours within a structure of personal relations. It is an intricate and pervasive relational network which Chinese cultivate energetically, with a history of more than 2,000 years. (Luo, 1998) The difference between guanxi and western business networking is that the former also includes social as well as commercial contact. Chinese businesspeople believe that one should develop a relationship and, if this is successful, business will follow. In contrast, western business people believe that a relationship may develop following the conclusion of successful business transactions. (Ambler and Styles, 2000; Tsang, 1998) Both guanxi and western networking emphasise that relationships are not discrete events in time, but are of a continuing nature. A notable difference is that guanxi leads to a strengthening of social relations, which may or may not be called upon in the future.

Guanxi also exists at an organisational level. Inter-organisational guanxi (guanxi hu) builds upon personal relations. Commentators such as Xin and Pearce (1996) argue that, since the cradle-to-grave provision of social services by one's employer (referred to as the 'iron rice bowl') was broken in the early 1980s with the advent of foreign companies, the application of guanxi at the organisational level has become more pervasive and intensive. Any firm in Chinese society, be it local or foreign, inevitably faces guanxi dynamics. (Luo, 1998) Guanxi requires business people to develop relations not only with suppliers and customers, but also with key government officials. 'Such personal connections are imperative to managers in China given the absence of the stable legal and regulatory environment that would facilitate impersonal business activities. Institutional uncertainty during economic transformation has been quite high'. (Luo, 1998: 172)

Jones (1994) argues that business practice in China relies on guanxi rather than on law and legal institutions as the basis of security of expectations. She states that guanxi provides a crucial role in business activities, being the basis for trust. It is therefore a source of stability, certainty, predictability and risk-reduction. Guanxi can serve as a substitute for legal enforcement and fills the void left by the absence of a developed legal system. (Jones, 1994) Guanxi provides a 'substitute form of trust that can improve the profitability of investment and reduce the risk of arbitrary bureaucratic interference that is not in the interests of investors'. (Smart, 1993: 398)
Jones (1994) contends that a distinctive form of capitalism has developed in China and she asks how one can explain the success of an economy dominated by the 'rule of relationships' rather than the 'rule of law', as predicted by Weber's hypothesis.
According to Weber, the operation of market capitalism depends on the existence of incentive to engage in economic activities, and the security of expectation of economic benefit flowing from such activities is an essential element of such incentive. Such security can only be provided by the predictable application of state coercion through logically formal and rational law… [This] type of legal system constitutes a favourable, and almost essential, condition for market capitalism. (Chen, 1999: 99)

Jones states that, when the spectacular success of Hong Kong is repeated in Singapore, Taiwan, South Korea and now China (which she labels the 'fifth tiger'), the possible common denominator is their shared cultural emphasis on familial and business networks as opposed to legal institutions. (Chen, 1999) These are 'the very things Weber regarded as barriers to capitalism'. (Jones, 1994: 197) Weberians tend to distinguish between the universalistic West and the particularistic East, depicting the Western model as being favourable to capitalism and the particularistic East as inimical to it. Jones (1994) argues that in China particularism is in the ascendant (in the form of guanxi and familism), defying theories that associate Western universalistic values with the growth of capitalism. '[D]espite its lack of formal legal rationality, mainland China also seems able to provide sufficient predictability, calculability and stability for

capitalism to thrive. It can be argued that guanxi facilitates rather than hinders this process'. (Jones, 1994: 200)
Jones (1994) suggests that the rule of law is relatively absent from China and that guanxi is frequently preferred. She draws on Unger's differentiated notion of law to identify the legal and quasi-legal forms found in modern China, which may be either interactional, bureaucratic/regulatory or full legal order**[iv]**.

The final category is what one normally associates with the Western concept of the Rule of Law. Jones (1994: 204) argues that 'while law in China is primarily of the second sort (that is regulatory/bureaucratic), China is a legally pluralistic society in which guanxi plays a central role but "full legal order" is absent'.
Guanxi therefore enables business to be done with strangers in a context of mutual trust and certainty; those who break this trust show 'bad faith' and stand to lose an important form of social capital, that is their reputation or 'face'. In a society which places great importance on 'face' and trust, breaking faith may mean expulsion from guanxi-networks and exclusion from future business deals. (Jones, 1994: 205)

Contemporary China suggests that the existence of a rational legal system, in the Weberian sense, may not be a necessary or highly relevant condition for the development of a market economy. (Chen, 1999) Indeed, the Chinese authorities have stated clearly that, while the Western model of economic development was adopted, it was never intended to adopt the Western notion of the Rule of Law. (Deng Xiaoping speaking in 1988) The notion of the separation of powers was anathema to Deng Xiaoping, the architect of the opening-up policy – once a decision has been taken it could be implemented without 'one branch of government holding up another'. (Xiaoping, 1988, cited in Jones, 1994) 'Chinese law is an instrument of politics to be interpreted not by an autonomous judiciary but by the National People's Congress'. (Jones, 1994: 208)
This leads one to ask if normal business can be conducted where a pervasive network of relationships exists. In particular, do western investors face challenges given the lack of the legal certainty which they would be accustomed to in areas such as contract law? But is contract law an absolute reference point in the conduct of commercial activity in Western society? In his seminal study on non-contractual relations in business, Macauley (1963) sets out a view of contract law**[v]** in the West which is open to interpretation, contestation and modification. His study outlines a scenario where relationships are central to business

transactions, with little recourse to legal sanctions. 'Business exchanges in nonspeculative areas are usually adjusted without dispute'. (Macauley, 1963: 60) Business people try to solve conflicts themselves and in so doing they do not refer to the content of the contract. (Roxenhall and Ghauri, 2004) Indeed 'law suits for breach of contract appear to be rare'. (Macauley, 1963: 60)
Macauley (1963) asks why contracts and legal sanctions appear relatively unimportant in the business world. He identifies the understanding of an agreement by both sides as ensuring that the nature and quality of a seller's performance is understood. This understanding is facilitated by experienced professionals who are familiar with industry specifications and standards. In addition, there are alternatives to legal sanctions associated with the firm's standing in the industry, such as the honouring of one's commitments and the perception that the quality of one's product is to be trusted. 'At all levels of the two business units, personal relationships across the boundaries of the two organisations exert pressures for conformity to expectations'. (Macauley, 1963: 63) The ultimate non-legal sanction is the desire to maintain a successful business relationship.

Businesspeople often prefer to rely on informal agreements, such as a handshake, rather than to agree to a formal contract. Roxenahall and Ghauri (2004) argue that this occurs because parties want to continue to do business with each other in future. Macauley (1963: 64) contends that 'not only are contract and contract law not needed in many situations, their use may have, or may be thought to have, undesirable consequences. Detailed negotiated contracts can get in the way of creating good exchange relationships between business units'. Pointing to the negative dimensions of contracts, he argues that the existence of a contract may result in performance being satisfied only to the letter of the contract. Businesspeople at times want a degree of vagueness so that they can react to changed circumstances. In addition, resorting to litigation will inevitably mean an end to the business relationship. Nevertheless, Macauley (1963) envisages situations where the threat of legal sanctions will have more advantages than disadvantages. These include the internal needs of an organisation, where pressure is required on departments within the firm to ensure that standards are achieved, where complex performances are agreed over a long time period, and where default is thought to have potentially serious repercussions.
Overall, Macauley (1963) identifies a reluctance among businesspeople to engage in negotiating contracts. Even when they do and one party defaults, there is a

marked reluctance to pursue legal avenues. This is because businesspeople see a relationship as more important than one particular transaction. Given the importance of establishing a strong network of relationships in China (guanxi) and the relative lack of importance of detailed contracts in the conduct of business among western business people, one would assume that investors in China should not be particularly interested in concluding formal and detailed contracts with Chinese partners. This issue will be explored in our research with the executives of firms which have invested in China, to discover if, given the strength of guanxi in China, trust and credibility play a more salient role than legal contracts. (Tsang, 1998)

Conclusion

This chapter provides an overview of the most pertinent literature on key issues which will guide our future discussion. The definition of investment which has been adopted centres on management control and this will inform the selection of firms for inclusion in our research. While there are several theories on investment, it is argued that Dunning's eclectic paradigm provides a comprehensive and dynamic approach. It builds on the work of earlier theorists such as Hymer. It sets out three preconditions which must exist for FDI to be successful – ownership-specific advantage; location-specific advantage; and internalisation advantage. FDI theories such as Dunning's have developed with the role of MNEs as central to our understanding of foreign direct investment.

As the largest recipient of inward FDI, China exerts a key influence in international economic decisions. FDI in China has made remarkable strides since the 'opening up' policy was introduced in 1979. In the space of one generation it has become a magnet for FDI. That said, the business environment holds challenges, particularly in the deep culture of relationships and the underdeveloped nature of the legal system.

Barry et al (2003) have developed a model of Irish outward FDI by analysing FDI outflows to developed economies, the traditional destination for such FDI. However, as a developing economy China exhibits particular traits and characteristics. Research among executives of MNEs which have invested in China will identify the locational advantages and disadvantages which China holds and enable us to draw conclusions as to whether Barry et al's model is applicable in the case of China.

NOTES

[i] This reputation is based on the hypothesis advanced in his doctoral thesis in 1960 (published in 1976 only). He moved through three phases during his short life: the first was based on his thesis; the second was a neoclassical phase, and the final was his Marxist period.

[ii] The general unavailability of statistical data on outward FDI flows is also highlighted by Buckley and Castro (1998), who cite this as a reason for researchers' apparent reluctance to test the IDP hypothesis.

[iii] US data is used as the US Department of Commerce makes data available on the nationality of inward FDI on a time-series basis.

[iv] 15 Unger's concept of 'law as legal order' is almost identical to Weber's rational law. (Chen, 1999: 99)

[v] Contract is defined by Macauley (1963: 56) as consisting of two stages: (i) rational planning of the transaction with careful provision for as many contingencies as can be foreseen and (ii) the existence or use of actual or potential legal sanctions to induce performance of the exchange or to compensate for non-performance.