

## **How does the routing of FDI to and from tax havens confound our understanding of Chinese MNE identity? A critical review of the empirical literature on Chinese MNEs**

**Abstract:** An extensive empirical literature tests the motivations and characteristics of the outward foreign direct investments of Chinese MNEs. Much of it, however, suffers from serious shortcomings in its treatment and use of foreign investment data. In particular, most research fails to properly account for the ways in which Chinese MNEs route their foreign investments both to and via tax havens and financial centers. As a result, our understanding of the identity of Chinese MNEs still remains embryonic. We outline the nature of the most commonly found problems so as to inform future research.

# **How does the routing of FDI to and via tax havens confound our understanding of Chinese MNE identity? A critical review of the empirical literature on Chinese MNEs**

## **Introduction**

What are the characteristics and features of Chinese MNEs (CMNEs)? Are they different from other MNEs? What, in other words, is their particular identity? Much empirical and conceptual research has explored this question with well over 100 articles published in academic journals to date. A question posed by many scholars, in particular, is whether new theories of the MNE are required to explain their strategy and behavior. For example, does strategic asset seeking (i.e. acquiring foreign technologies and brands via acquisition of developed country firms) contravene tenets of the OLI paradigm or those of transaction cost theory (Hennart, 1982; 2012; Luo and Tung, 2017; Mathews, 2017)? Besides the paradox of strategic asset seeking, considerable research has explored how state involvement and ownership, prevalent in Chinese business, may influence CMNE expansion. Buckley, Clegg, Cross, Liu, Voss and Zheng (2007), for example, asked whether China's state owned MNEs had 'special ownership' advantages, owing to their propensity to invest in politically unstable regions. Many subsequent *JIBS* papers, which we review later, have considered the impacts of state ownership in greater detail (Table, 1). For example, how does state ownership influence entry mode strategies in potentially hostile host countries (Cui and Jiang, 2012; Meyer, Ding and Zhang, 2014) or expropriation risks (Duanmu, 2014)? Does government support reduce the need for foreign investment experience (Hoskisson, Wright and Filatotchev, 2013; Lu, Liu, Wright and Filatotchev, 2014)) and how has this relationship evolved over time (Liang, Ren and Sun, 2014)? How important is state involvement *vis a vis* over industry effects, for example internal competition (Gaur, Ma and Ding, 2018)? Does level of government affiliation affect Chinese outward foreign direct investment (FDI) strategies (Wang, Hong, Kafourous and Wright, 2012) ? Questions have also been asked about how underdeveloped institutions may influence CMNE activities, via for example business group development—widely seen as a response to institutional voids (Sutherland and Ning, 2010)-- or more generally 'institutional arbitrage' (Buckley, Sutherland, Voss and El-Gohari, 2015), in which FDI is considered an 'escape' response (Boisot and Meyer, 2008; Shi, Sun, Yan and Zhu., 2017). These are just some of the types of questions that have been asked about CMNE identity.

However, despite large volumes of conceptual and empirical research, our understanding of CMNE identity remains incomplete. This is mainly because most empirical research on CMNEs has failed to adequately

understand and subsequently account for the ways in which CMNEs route foreign direct investment to and from tax havens and (often offshore) financial centers (hereafter all reference to tax havens incorporates the notion of financial center). To illustrate the nature and extent of the issues involved in accurately capturing CMNE activity we critique nine empirical studies published in the *Journal of International Business Studies (JIBS)* since the influential work of Buckley et al. (2007) (recipient of the *JIBS* decade award prize (Table 1)). We concentrate on these *JIBS* articles as the incorrect approaches used in them are similar to those found elsewhere. These articles, therefore, are fairly representative of the problems encountered in other empirical studies that explore CMNE identity. As such, they provide us with a convenient way of illustrating the challenges associated with understanding their outward FDI strategies, behaviors and, ultimately, CMNE identity.

#### TABLE 1 ABOUT HERE

We first outline how and why tax havens and offshore financial centers (hereafter abbreviated to THOFCs) bias FDI data and consequently limit our understanding of CMNE activity. Second, we provide brief critiques of *JIBS* papers that undertake empirical testing of CMNE outward foreign direct investments (Table 1). We identify two groups of CMNE empirical studies. The first group includes studies which are largely unaware of the ways in which FDI that transit through THOFCs affects Chinese FDI flows. The second group, by contrast, shows some awareness of the problem but, as we will show, generally does not adequately deal with it. To illustrate these points more emphatically, we employ several firm-level CMNE samples developed from the Orbis (Bureau Van Dijk) database as well as recently published OECD inward FDI data compiled by both immediate and ultimate origin. This shows that immediate inward FDI from China to OECD countries is much smaller than when it is measured by ultimate ownership. For example, for the US it is about one half (Table 2). Much Chinese inward investment to the US, therefore, is routed via THOFCs. Countries with favorable tax regimes and institutions, like the Netherlands, which receives over 90% of its FDI from China (over \$22 billion to date) in the form of special purpose entities (SPEs hereafter), serve as transit hubs. We focus on exploring, in particular, the nature of this ‘capital in transit’ (CIT), or what we call ‘onward-journey’ (as opposed to ‘round-trip’) FDI. By way of conclusion, we argue that the misunderstanding of CMNE activity is indicative of a broader problem within the international business community. In general, there appears to be a limited comprehension of how transnational ownership chains associated with the creation of SPEs in THOFCs affects FDI data collection processes and, in turn, our understanding of MNE activity (Beugelsdijk, Hennart, Slangen

and Smeets, 2010). We therefore still have some further way to go to unravel the complexities of CMNEs and their specific identities.

## TABLE 2 ABOUT HERE

### **Background: Why are THOFCs an issue when investigating outward FDI and MNE activity?**

MNEs often diversify their investments geographically through various organizational structures, including through SPEs. SPEs are legal entities (subsidiaries) that “have little or no employment, or operations, or physical presence in the jurisdiction in which they are created by their parent enterprises. These are typically located in other jurisdictions, such as tax havens and/or offshore financial centres” (OECD, 2008, p. 186). They are also often used as devices to raise capital or to hold assets and liabilities and usually do not undertake significant production. Indeed, according to the most recent OECD benchmark definition of FDI, “The core business of SPEs is to channel funds between entities outside the country where they are established.... The role of these SPEs is *merely to serve as a financial turntable for enterprises in other countries*” (OECD, 2008, p. 186) (emphasis added). Compilers of FDI data, moreover, argue that SPEs “hardly affect domestic economic activity and do not reflect genuine investment activities in or of the reporting country itself”. Accordingly, the question for those involved in tracking foreign investment is “how to ensure that the geographical and industrial allocation of such investment is not distorted” (ibid.). Often, unfortunately, FDI data when used for the purposes of understanding MNE activity is seriously compromised as a result of SPE- related foreign investments.

The distinction between genuine and non-genuine foreign investments has been considered with reference to the biases inherent in FDI data as a measure of MNE affiliate activity. Investment holding companies, financing subsidiaries, conduits, shell companies, shelf companies and brass-plate companies are all examples of SPEs. The currently employed OECD guidelines, outlined in the 3rd Edition Benchmark Definition of FDI (1996) and revised, though not yet implemented by all countries, in the 4th Edition, state that investments in SPEs, even though they undertake little physical production, should be incorporated in FDI data. This inclusion stems from an earlier recommendation by the IMF in its Balance of Payments Manual, which has been followed since the early 1990s:

Whatever the structure (e.g., holding company, base company, regional headquarters) or purpose (e.g.,

administration, management of foreign exchange risk, facilitation of financing of investments), SPEs are an integral part of the structure of the direct investment network as are, for the most part, SPE transactions with other members of the group (IMF, 1993, para. 365)

While many MNEs use SPEs in THOFs (Jones and Temouri, 2016), Chinese MNEs make an exceptionally high use of them. This is due to several factors. Firstly, enterprise income tax law in China favored foreign-invested companies for many years. Foreign investors were offered lower corporation tax rates so as to encourage inward investments (Sutherland and Anderson, 2015). This created incentives for domestic businesses to become ‘foreign’ investors themselves, and to “round-trip” capital back to China. Second, limited access to domestic capital markets has spurred China’s private sector, in particular, to find offshore alternatives. Third, Hong Kong and other tax havens closely linked to it, particularly the British Virgin Islands (hereafter BVI) and Cayman Islands, have been historically linked to Hong Kong as part of the former British Empire. The triad of these THOFs has provided important conduits for offshore financing. Fourth, domestic interference and restrictions on the overseas investments of Chinese businesses have caused some of them to move offshore, where legal institutions are superior and domestic restrictions can be circumvented. Institutional arbitrage, more generally, has attracted Chinese businesses to the offshore world (Buckley et al., 2015). All of these factors have historically leant Chinese businesses towards THOF use.

The problems introduced by THOF use are caused by both direct FDI transfers to offshore SPEs to facilitate round-tripping and institutional arbitrage and by the less frequently discussed though equally serious problem of “onward-journeying” (Sutherland and Ning, 2011). Round-tripping involves moving capital offshore to a SPE only to bring it back onshore again, so inflating outward (and inward) FDI data. Onward-journeying, in contrast, involves establishing an offshore business (often an SPE) and using this vehicle to conduct further FDI in third countries. The initial investment to the offshore SPEs is mistakenly recorded as genuine, value adding activity (particularly in the case of FDI to Hong Kong). Thus, THOFs have consistently figured prominently as major FDI recipients in China’s officially compiled outward FDI data, implying FDI associated with the transfer of assets and equity from mainland Chinese businesses to SPEs in these jurisdictions.<sup>1</sup> The triad of three former British colonies and crown dependencies, Hong Kong, the BVI and Cayman Islands, in particular, stand out. In 2016, for example, Hong Kong, the Cayman Islands and BVI ranked 1<sup>st</sup>, 3<sup>rd</sup> and 4<sup>th</sup> largest recipients of Chinese

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<sup>1</sup> Since 2002 China’s Ministry of Commerce (MOFCOM) has compiled China’s FDI statistics in accordance with the OECD/IMF’s balance-of-payment guidelines.

outward FDI flows (MOFCOM, 2016) (Table 2). The Netherlands, Singapore and Luxembourg also ranked in the top 20.

Investments made via SPEs to third countries, by contrast, are not recorded at all in official Chinese outward FDI data. Rather, they are recorded as outward FDI from the tax haven in which the SPE is formed. These onward-journey investments, however, are also very significant in terms of their size (Ning and Sutherland, 2012). So they cannot be ignored. Indeed, evidence supporting this argument can be found by looking at the flip side of CMNE outward FDI, which is inward FDI data for countries receiving Chinese investments. The OECD/IMF guidelines for reporting FDI have recently been updated (see Benchmark Definition 4<sup>th</sup> Edition, or ‘BMD4’) so that countries are now encouraged to report inward FDI positions (i.e. stock) by both immediate and ultimate investing countries. To date, however, only 13 countries collect such data, albeit inward FDI data from China is not always made publicly available (and is only available for several years, starting in 2014). These data, however, show very significant discrepancies in the two figures, clearly indicating that onward journey-type FDI is a very common phenomenon for CMNEs. Table 3 illustrates the discrepancy between the figures for Chinese inward investments in a number of host countries when recorded by immediate source country vs. ultimate source country.

TABLE 3 ABOUT HERE

The use of SPEs thus creates genuine problems in using officially recorded FDI data to measure MNE activity, both in terms of identifying the ultimate geographical destination of FDI, as well as its targeted industrial sector (i.e. manufacturing, natural resources, services and so on). As the OECD puts it, “where funds are simply channeled through holding companies, major problems are created concerning the geographical and industrial composition of FDI” (OECD, 2008, p. 186). As well as difficulties for studies that use country-level official FDI data, SPE use, where not properly acknowledged and accounted for, may also create serious difficulties for studies that use firm-level data.

### **Research which does not recognize or account for THOFC related FDI**

We now review ten empirical studies exploring CMNE identities which have been published in JIBS over the

past decade (Table 1). We start by looking at those which do *not* acknowledge or recognize the THOFC/OFDI issue, outlining their potential flaws. We illustrate these flaws using a sample of CMNEs extracted from the Orbis database (Bureau Van Dijk). We then consider the studies which do recognize the presence of THOFCs, outlining the inadequate procedures undertaken to mitigate the problem. Both sets of studies, we argue, are likely to give misleading results regarding the strategies and identities of CMNEs.

### **Buckley et al. - inclusion of FDI to Hong Kong (and the Netherlands, Cyprus and Singapore)**

We initially focus on Buckley et al.'s (2007) highly influential JIBS decade award winning paper. In the words of the JIBS decade award review panel this was 'a landmark study' which 'served to establish a very useful template for empirical research in the following years' (Verbeke, 2018, p. 2). Buckley, Clegg, Voss, Cross, Liu and Zheng (2017), however, have recently recognized how they might have done things differently if they had known earlier what they know now.<sup>2</sup> One of these corrections would have been to pay greater attention to the THOFC problem: 'Recrafting our 2007 paper, leaving today's better data availability aside, we would therefore consider the role of OFTHs more deeply' (Buckley et al., 2017). How problematic is it to use FDI project level data (aggregated at the national level) compiled by MOFCOM, the data source for their original article?

To briefly illustrate the prevalence of MNE subsidiaries in offshore locations and the issues they may cause, we created two samples of CMNEs using the Orbis database. This is a widely used firm-level commercial database that holds details on over 220 million companies worldwide and the immediate and ultimate ownership of their subsidiaries. From this database it is possible to piece together an accurate picture of where CMNEs own subsidiaries, including details on subsidiaries in foreign jurisdictions.<sup>3</sup> We are initially interested in establishing the extent to which FDI from China is: (i) directed towards tax havens and; (ii) subsequently routed via tax havens to other foreign (i.e. onward-journeying) and domestic destinations (i.e. round-tripping). We wish to do this for a general sample of CMNEs as well as for a sub-sample of this group including only state-owned CMNEs (the focus of the Buckley et al.'s (2007) original study). By showing that there is a very high prevalence of SPE related FDI in state owned CMNEs as well as CMNEs as a whole, we may get a better picture of the

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<sup>2</sup> Their admission is surprising, as at the time round-tripping via Hong Kong (and other offshore jurisdictions) was widely known about (see Fung et al. (2011) for a more recent discussion). The creation of offshore vehicles in Hong Kong was associated with the corporatization procedures required for the offshore listing of state owned enterprises. Many SOEs have therefore established offshore vehicles for the purpose of, among other things, raising capital.

<sup>3</sup> Our data looks at the current situation. However, we are confident it is indicative of earlier historical patterns.

extent to which standard FDI data has become tainted by SPE use in tax havens.

#### *All CMNEs*

We focus initially on CMNEs with a 10% ownership threshold required to lock in subsidiary control. This is a standard and commonly used cut-off employed in collecting official FDI data (OECD, 2015). We also stipulate that the Chinese company must be incorporated in China and also have a Chinese global ultimate owner. We do this to exclude non-Chinese firms (i.e. foreign controlled but Chinese incorporated). We initially screen the data and remove foreign subsidiaries involved in sea and coastal passenger water transport and marine coastal freight and marine fishing (NACE sectors 5010 and 0311). We do so as many ocean going vessels are owned via offshore companies but are not the focus of our interest. This left 2,728 CMNEs owning a total of 27,439 subsidiaries (both foreign and domestic). Of these 27,439 we identified 2,926 foreign subsidiaries (i.e. firms with ISO country codes which are not China i.e. not ‘Cn’). We include here Hong Kong as a ‘foreign’ jurisdiction.<sup>4</sup>

#### TABLE 4 ABOUT HERE

Table 4 summarizes our firm-level findings with regards to point (i). It highlights the most important geographical locations of CMNE subsidiaries (columns one and six) as well as their sectoral categorization by NACE code in ranking order (both geographical location and NACE code rankings are independent of one another here, i.e. there are 931 subsidiaries in Hong Kong and there are 251 retail/wholesale trade companies reported (see row one) but these are not necessarily all found in Hong Kong). In line with official MOFCOM data we find that a great many subsidiaries are registered in tax havens. Singapore, the Cayman Islands and BVI, the Netherlands and Hong Kong all figure prominently. While many of the CMNE subsidiaries in our sample lack NACE codes, it is evident that many are officially recorded as ‘investment holding companies’ (i.e. NACE code 6420). Only 1,312 of the 2,926 identified foreign subsidiaries provide a NACE code. Of these 1,313, 156 or around 12 % were in the ‘activities of investment holding companies’ category (NACE code 6420).<sup>5</sup> This

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<sup>4</sup> At this point, it is worth noting that a number of these subsidiaries do not have ISO codes (i.e. around 4,602 of these subsidiaries report no ISO code, perhaps owing to their small size and lack of detailed data collected on them – some of these 4,602 appear also to be foreign subsidiaries, i.e. in Hong Kong).

<sup>5</sup> In this regard, it is interesting to note that use of these SPEs in THOFCs also creates industrial composition biases. Investment holding companies (i.e. SPEs that hold investments in other corporations) are considered to be financial corporations and therefore are classified as firms providing business services. This is despite the



made it the second largest four digit NACE code category, after wholesale and retail trade. The establishment of investment holding companies, therefore, has been a central motive for CMNE outward FDI. Other important categories are business services (NACE 8299, 42 subsidiaries), other business and management consultancy activities (NACE 7022, 25 subsidiaries), financial service activities (except insurance and pension funding) (NACE 6499, 17 subsidiaries) and head offices (NACE 6499, 17 subsidiaries). Combined these business services subsidiaries totaled 254, exceeding the number of trade related subsidiaries.

Business service activities also provide an excellent mechanism for CMNEs to engage in transfer pricing and, more generally, the routing (or tunneling) of profits offshore (i.e. by charging ‘service’ fees of various types) (Fung et al., 2011) . It is also of interest to note that service activities generally do not figure prominently in the NACE codes of the parent firms, suggesting the services being undertaken are related to intra-MNE firm activities (i.e. providing services within the MNE group).<sup>6</sup>

*Do state-owned CMNEs have the same prevalence of FDI to THOFs and investment holding companies?*

Table 4 also includes data on a further sub-sample of CMNE, namely those that are state owned. The criteria for selecting these is identical to our initial sample, with the exception that we screen also for state-owned firms, i.e. firms owned by public authorities, the central government, provinces, and municipalities. This returns 873 state owned CMNEs with a total of 1,428 foreign subsidiaries. As with the full sample, there is a strong tendency towards incorporation in THOFs. Over one third are registered in Hong Kong (Table 4). Singapore, BVI and the Cayman Islands are important as well. Only 702 of the 1,428 foreign subsidiaries report NACE codes. From this we see that investment holding companies are the largest single group of foreign subsidiaries of state owned CMNE. State owned CMNEs, the focus of Buckley et al. s (2007) paper, are therefore also highly active in establishing SPEs. While our sample focuses on a later period to theirs, the evidence suggests that state-owned CMNEs have been setting up offshore SPEs in THOFs for many years and that it is not a recent phenomenon (Sutherland and Anderson, 2015).

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fact that they do not sell such services but are vehicles used to own businesses in different industries, such as manufacturing or mining.

<sup>6</sup> Beyond investment holding, the largest categories appeared in the retail and wholesale businesses (NACE codes 4500 to 4791). This is in line with the findings of Sutherland and Ning (2012), who also note in general the high prevalence of foreign trade related subsidiaries in CMNEs

### *Onward-journeying in CMNEs*

While outward FDI to THOFCS is common, onward investments from offshore SPEs/THOFCS may also be significant. The triad of THOFCS jurisdictions, including Hong Kong, the BVI and the Cayman Islands, figure prominently in the offshore structures of CMNEs (Tables 2 and 4). The NACE codes of CMNE subsidiaries also reveals that investment holding companies are common in other jurisdictions such as Singapore, Bermuda, the Netherlands, Luxembourg and Switzerland. To explore the levels of onward journeying in CMNEs, we therefore look at the outward FDI undertaken from these offshore jurisdictions. How many of these first tier subsidiaries (which we will call ‘level 1’ subsidiaries), owned their own subsidiaries (which we will call ‘level 2’ subsidiaries) in other countries? We include these additional locations and focus on the number and types of companies owned by the 669 level 1 CMNE foreign subsidiaries identified in six tax havens (see Table 5).

#### TABLE 5 ABOUT HERE

Using Orbis we found that these level 1 subsidiaries in turn owned a further 4,503 subsidiaries. Of these, the largest number, 1,688, was found in China – suggesting a high prevalence of round-tripping by our level 1 subsidiaries located in tax havens. These 1,688 level 2 subsidiaries were owned by 141 level 1 subsidiaries, so each level 1 subsidiary owned on average over 10 level 2 subsidiaries. A number of these level 2 subsidiaries were held in tax havens such as the BVI (740 subsidiaries), Hong Kong (670 subsidiaries) and the Cayman Islands (200 subsidiaries). Furthermore, many of these level 2 subsidiaries were investment holding companies. Many had a 6420 NACE code (investment holding) (Table 5). This, of course, points towards complex ownership chains in CMNEs, usually involving at least one THOFCS jurisdiction and several SPEs. This finding is in line with earlier firm-level research on CMNEs, documenting a high prevalence of international ownership chains, with THOFCS figuring prominently (Ning and Sutherland, 2012; Sutherland and Anderson, 2015).

While round-tripping is clearly common, analysis of the Level 2 subsidiaries shows in addition that onward journey type FDI is also prevalent. One hundred and twenty-six Level 2 subsidiaries are found in the United States, accounting for the considerable difference in immediate inward FDI and ultimate inward FDI figures reported for the United States in Table 3. There were also 96 Level 2 subsidiaries in the United Kingdom, 44 in Australia, and 87 in the Netherlands (Table 5). Official MOFCOM FDI data does not capture these investments. Again, this undermines their use as a proxy for CMNE international activity. From a measurement perspective,

as noted, the problem with FDI undertaken from an offshore jurisdiction is that it will be counted on a bilateral basis from the home country (i.e. Hong Kong, BVI etc.) to the target country (i.e. UK, US, etc.). This onward-journeying phenomenon is therefore common. Some attempts have been made elsewhere to explore its extent and nature (Sutherland and Ning, 2011). It is clearly significant, as the recently released OECD data confirm (Table 3).

### *Summary*

As Buckley et al. (2017, p.4) have noted in reevaluating their contribution, ‘Offshore financial centres and tax havens are playing a significant role in the way Chinese firms structure and execute their internationalization regardless of whether they are SOEs or privately owned’. Our data support the idea that both state-owned CMNEs and other CMNEs frequently use THOFCs to coordinate their business activities. Great care, therefore, must be exercised when using both official aggregated and firm-level data to investigate where and how much CMNEs invest and in which industry. Since 2002 China’s Ministry of Commerce (MOFCOM) has compiled China’s FDI statistics in accordance with the OECD/IMF’s balance-of-payment guidelines (Cheng and Ma, 2007). China’s MOFCOM therefore makes no attempt to distinguish between foreign subsidiaries established as shell companies (i.e. SPEs) and those that undertake more genuine OFDI projects to serve foreign markets, to acquire strategic assets, or to export back to China. It is therefore not helpful to use this FDI data to understand CMNE activity. One significant problem raised by Buckley et al. (2007) is the thorny question of how to deal with FDI flows to Hong Kong which is an important destination for various types of FDI, both SPE related (as it is an important transit point) as well as of a more genuine type, particularly trade and market serving operations.

### **The influence of Buckley et al (2007): Ignoring SPEs?**

We initially focus on Buckley et al. (2007) as it has become a highly influential paper. In the words of the JIBS decade award review panel:

‘Buckley and his colleagues provide a truly comprehensive treatment of Chinese investment abroad making it a landmark study in understanding OFDI.....The study was among the first of its kind to tackle the measurement and estimation issues related to Chinese OFDI, and as such *it served to establish a very useful template for empirical research in the following years.*’ (Verbeke, 2018, p. 2) (emphasis added)

Indeed, many later studies that empirically explore the foreign direct investments of CMNEs take a similar approach in their use and treatment of Chinese FDI data. Wang et al (2012), for example, explore how government involvement affects the international expansion of CMNEs, focusing on the level at which the firm is affiliated to government as well as its degree of state ownership.<sup>7</sup> Their information on foreign direct investments is again taken from MOFCOM (2006 to 2007). In specifying their dependent variable, the annual amount invested by the firm in foreign projects, they note that they ‘followed a large number of similar studies (e.g., Buckley et al.2007) and used the actual amount of annual OFDI by each firm’ (Wang et al. 2012, p.665) (emphasis added). While little descriptive data is provided on where these funds are invested, we can assume that investments in Hong Kong and other tax havens (like the Netherlands, Cyprus and Singapore, which Buckley et al. (2007) also include) figure prominently (see Table 4). As in Buckley et al. (2007), however, there is no attempt to explain how they deal with SPEs in these locations. We can only presume that their dependent variable captures all tax haven-related investments.

In a later study, using a somewhat different dependent variable, Liang et al. (2014) construct a ‘degree of globalization’ index for CMNEs (or ‘DOG’).<sup>8</sup> DOG is the average of three firm-level ratios: (1) foreign sales to total sales; (2) foreign assets to total assets; (3) number of overseas branches and subsidiaries over total branches and subsidiaries, both domestic and foreign. This measure, they argue, ‘depicts the extent of geographical-operations dispersion across countries (Stopford & Wells, 1972) and is widely applied in globalization research’ (Liang et al. 2014, p. 8). However, there are clear problems with parts (2) and (3) of the index. Both will be strongly influenced by SPEs which, as Table 4 shows, are among the most common type of CMNE foreign subsidiary. One would presume that (3) in particular would be severely skewed by the large number of

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<sup>7</sup> Different types and levels of governments, they argue, prioritize different objectives. Each exerts different institutional pressures. They find that ‘Government involvement influences the level of overseas investment, its location (developed vs developing countries) and its type (resource- vs market-seeking). These effects depend on firms’ own resources and capabilities, suggesting that not all firms possess equal ability to internalize government-related advantages and respond to institutional pressures. By demonstrating that resource-based and institutional constructs are highly dependent on one another, we enhance understanding of how EMEs succeed in expanding overseas, and why governments matter.’

<sup>8</sup> They discuss two types of state control that may influence the globalization decisions of SOEs (and their degree of globalization): the degree of state ownership and the political connections of executives. They argue that the impact of these two factors is influenced by the home country’s evolving institutional environment. Using a two-step corporate globalization decision model and 17,272 firm – year observations of nonfinancial, Chinese-listed companies, they find a strong impact on globalization for these two factors. Impacts, however, differ between the periods before and after domestic governance reform and across different globalization decision steps. The diminishing impact of executives’ political connections and the increasing impact of state ownership on firms’ DOG demonstrate the evolving relationship between the state and the managers.

investment holding companies incorporated offshore to facilitate round-tripping and onward journeying. In fact, this is largely confirmed by another *JIBS* article published only a few months earlier (in May 2014). Lu et al. (2014) use an identical approach to identify foreign subsidiaries, drawing from listed firms in Shanghai and Shenzhen. They find that the most common locations by far for the ‘foreign’ subsidiaries of listed firms are Hong Kong (278 subsidiaries), the BVI (58 subsidiaries), Singapore (26 subsidiaries), the Netherlands (25 subsidiaries), the Cayman Islands (19 subsidiaries), Luxembourg (4 subsidiaries) and Bermuda (4 subsidiaries). Thus 414 of the total 702 subsidiaries owned by Chinese listed firms are potentially SPE-related (i.e. are set up for the purposes of round-tripping or onward-journeying). Should these types of foreign subsidiaries really be counted when measuring DOG? Perhaps they could be - depending upon exactly what questions one was trying to explore. If so, however, the authors should justify and explain any such inclusion. If they are going to be excluded greater explanation is required regarding how they are actually excluded. Given the difficulties involved in fully identifying SPE-related subsidiaries this is not a trivial matter.

Some studies would appear at first view to be less impacted by SPEs, but in fact this is not the case. Gaur et al. (2018) and Cui and Jiang (2012) fall into this category. Gaur et al. (2018), for example, collect survey data from Chinese firms which identified themselves as MNEs-- presumably because they have a foreign subsidiary of some type.<sup>9</sup> Cui and Jiang (2012) also survey managers of CMNEs. They rely on MOFCOM foreign investment data to identify their sample of MNEs: ‘We collected data from a survey conducted in 2006 targeting Mainland Chinese firms with outward FDI projects. The population was identified from the 2005 Statistical Bulletin of China’s Outward Foreign Direct Investment published by the Ministry of Commerce of China’ (p.271). Neither Gaur et al. (2018) nor Cui and Jiang (2012) discuss the potential issues surrounding SPEs in jurisdictions like Hong Kong, the BVI or the Cayman Islands. While this may seem on first reflection somewhat of a technicality, it is in fact an important issue. This is because there are many CMNEs that are multinational *only* by virtue of having one or more SPE-type subsidiary in these locations. In other words, they are not really MNEs in any meaningful, conventional sense of the word since they do not engage in foreign value-adding activities.

In our firm-level CMNEs sample taken from Orbis we identified 328 CMNEs that were MNEs only by virtue of owning at least one subsidiary in a THOFC (i.e. Hong Kong, the Cayman Islands, Singapore or the BVI). It is

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<sup>9</sup> They employ institution- and industry-based views to examine how the degree of support of the domestic government and the situation of the domestic industry influences overseas foreign direct investment and compare the relative strengths of these two influences.

questionable as to whether these are the type of MNEs that both studies claim to be investigating. While these studies do not have a problem with their dependent variable, they suffer from a serious sampling bias, as they potentially include as CMNEs firms that are not traditional MNEs since they *only* own subsidiaries in THOFCs.

### **JIBS articles which recognize THOFC-related FDI but do not adequately address the problem**

Alongside the four articles above, which generally overlook THOFC-related FDI and the associated issues, we identified a number of later studies that do acknowledge the problem, but fail to adequately deal with it. Their findings, therefore, are also likely to be misleading.

Meyer et al. (2014), for example, explore how institutional pressures on state-owned firms influence their foreign entry strategies. They argue that SOEs may want to reduce potential conflicts and increase their legitimacy when making foreign direct investments. They empirically test how listed state-owned Chinese firms alter their entry mode compared to private firms and how conditions in host countries impact these strategies.<sup>10</sup> Their empirical methodology, however, does not adequately address the THOFC problem. They note, for example, that ‘subsidiaries in Hong Kong, Macao and the tax havens of British Virgin Islands and the Cayman Islands serve primarily as holding organizations or as financing instruments for operations in third countries, or in fact in China itself (Ding, Nowak, & Zhang, 2010; Hong & Sun, 2006), and hence fall outside the scope of our research’ (Meyer et al., 2014, p. 1012). Hence while the authors move in the right direction by at least acknowledging the complexities of the THOFC issue, their approach still remains unsatisfactory. They assume, for example, that all investments in Hong Kong are SPEs or tax haven-related. In our Orbis CMNE sample, however, we find that this is a considerable oversimplification. Many subsidiaries in Hong Kong, for example, engage in real, value adding activities, such as trading.

Besides the exclusion of all Hong Kong subsidiaries, a further problem in their approach is the inclusion of all subsidiaries in other recognized tax haven jurisdictions. Chinese subsidiaries in the Netherlands, Singapore, Luxembourg, Cyprus and Switzerland, for example, are all included in their sample. This is problematic because these countries receive significant volumes of SPE-related investments from China. Newly reported country-level FDI data collected by the OECD following its Benchmark Definition 4, which separates SPE from non

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<sup>10</sup> They find these differences are larger where pressures for legitimacy on state-owned firms are stronger.

SPE investments, shows, for example, that over 92% (\$22.1 billion out of \$23.8 billion) of the FDI stock into the Netherlands from China at the end of 2016 was SPE related (OECD, 2018). While similar OECD data for Luxembourg and Switzerland and other tax havens remain unpublished, our Orbis firm-level data show that all of these aforementioned jurisdictions are home to Chinese investment-holding subsidiaries. Why not then exclude these subsidiaries as well? As a point of fact, these subsidiaries accounted for 15 % of their observations (57 out of 386). This is clearly inconsistent. A better solution would have been to weed out all SPE-related subsidiaries—regardless of their location, based on the descriptions of their activities or on their NACE or SIC codes, which are often stated in annual reports, particularly for Hong Kong listed firms. Excluding firms by virtue of their country of incorporation is evidently a blunt tool for excluding SPE-related subsidiaries. Lu et al. (2014) make a similar mistake in a study published around the same time. In their sample of 702 investments (taken, as noted, from listed firms) they exclude all 278 Hong Kong subsidiaries, all 26 Singapore-based subsidiaries, as well as subsidiaries in the BVI (58), the Cayman Islands (19), Macau (5), and Bermuda (4). Of the 316 remaining subsidiaries, which they include in their sample, 25 are incorporated in the Netherlands, 5 in Liberia, 4 in Luxembourg, and 4 in Panama. Hence over 12% of their sample remains potentially SPE-related, while their blanket exclusion of all subsidiaries in Hong Kong, Singapore, the BVI, the Cayman Islands, Macau and Bermuda means that they are excluding some genuine value-adding subsidiaries. Again, how reliable are results based upon this type of data likely to be? The Netherlands alone is the second largest home to Chinese subsidiaries in their sample (after the US). It is, however, clearly an important transit hub for CMNEs investing in Europe via SPEs. A further anomaly in the Meyer et al. (2014) study is their inclusion of direct investments in shipping: ‘We kept investments in Panama and Liberia in our sample because they are in the shipping business and are not for tax purposes’ (Meyer et al., 2014, p. 1012). Our CMNE sample shows, however, that direct investments in shipping often involves the incorporation of companies which directly own individual vessels, in Panama for example.<sup>11</sup> It is not clear if it makes any sense to include vessels as genuine direct investments.

Another study, by Shi et al. (2017), also acknowledges some of the potential issues surrounding THOFs. The authors hypothesize that ‘Institutional fragility in a province is positively associated with the outward foreign direct investment by the firms headquartered in that province’ (p.457). To address this question they create an index capturing the institutional development of each province in China, as well as the evolution and change of

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<sup>11</sup> There are a large number of shipping foreign subsidiaries. These are often vessels registered as offshore companies. Of the 6,700 or so foreign subsidiaries found in our initial CMNE sample, many were involved in shipping. These, in our view, are often not standard investments.

this index over time, to capture ‘institutional fragility’.<sup>12</sup> The paper is rather unusual, insofar as it excludes tax haven-related foreign investments, though it is very vague as to exactly how it does this – a challenge which to us would appear a significant achievement in its own right. However, as the study is basically looking at the determinants of institutional arbitrage, it might be argued that THOFC-related investments *should be included* in their study. Most authors seem to agree that THOFC-related investments can partly be explained by institutional arbitrage (Buckley et al., 2015). It is thus ironic that one of the few papers that should include THOFC-related FDI does not actually do so. Again, this highlights the confusion that surrounds exactly how THOFC and SPE-related investments should be treated in international business research.

### **Summary**

While lip-service is sometimes paid to the problems created by SPE-related investments in THOFCs and elsewhere, they are seldom addressed properly. The work of Buckley et al. (2007), as the *JIBS* decade award panel point out, has provided a template for authors—and referees--of those studies. Unfortunately, there has been a lack of critical evaluation of Chinese foreign investment data, at both the country and firm levels (Sutherland and Anderson, 2015). Studies that use country-level official aggregated outward FDI data suffer from quite obvious weaknesses, about which comparatively little can or could have been done. One should note that is not the approach taken in the *JIBS* papers reviewed here, but that it is common elsewhere. A cursory analysis of this data shows that havens like the Cayman Islands and BVI are major recipients of outward FDI. At a sectoral level, ‘business services’ also figure very prominently in the data, while they account for a very small share of domestic value-added. This all points to one conclusion – that Chinese outward FDI figures capture high levels of SPE-related THOFC investments. Moving to the firm-level (the approach predominantly used in the *JIBS* papers reviewed here), makes it easier to identify SPE-related FDI. However, researchers and journal referees have in general lacked a proper understanding of how such subsidiaries are created and used by CMNEs. As a result the findings of most extant studies of CMNEs are likely to be heavily contaminated by the incorrect inclusion of some SPE-related subsidiaries as well as by the exclusion of some genuine value-adding ones.

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<sup>12</sup> This latter construct reflects the fact that different institutional dimensions do not progress at equal speed, which in turn ‘creates internal friction and conflict during institutional development’ (Shi et al. 2017, p. 455).



The problems identified in these *JIBS* papers, it should be noted, can be found in a great many other research papers that empirically explore CMNE activity, as well as in those studying the investments of MNEs from other regions, including developed countries.

### **What lessons can be learned?**

Firstly, a general lesson from the empirical literature on CMNEs is that using officially collected outward FDI data is likely to lead to highly misleading results. Such data is typically highly skewed by FDI flows to THOFs (Tables 2, 3, 4, 5). While the Chinese case may seem extreme, in reality many countries, both developed and emerging, have quite high levels of FDI into and from THOFs (OECD, 2015). The problem stems from the original purpose of collecting FDI data, namely for balance of payments estimates. An investment into a THOF has implications for the national capital account – so it should be recorded as FDI if the purpose is to measure a country’s balance of payments on a bilateral basis. It does not, however, necessarily reflect real MNE activity (Beugelsdijk et al., 2010; Lipsey, 2007). Unfortunately, there are no easy ways of cleaning official FDI data so that it may give a more accurate representation of MNE activity. Some CMNE studies, Kolstad and Wiig (2012) for example, have excluded OFDI to Hong Kong and other THOFs. The problems with this approach, however, are also evident. Firstly, many real foreign investments are excluded. Secondly, all onward-journey investments are excluded, and yet they are substantial (Sutherland and Ning, 2011).

Secondly, studies that use firm-level data as their dependent variable, for example counts of foreign subsidiaries, fail to properly account for SPE-related subsidiaries. A surprisingly large number of them completely ignore the issue. They typically include *all* foreign subsidiaries, even those which may be clearly labeled ‘investment holding’ companies in the notes to the consolidated financial statements of listed companies. Because CMNEs own a large number of such holding companies, this is likely to adversely impact empirical results. More careful studies attempt to exclude SPE-related subsidiaries. These studies, however, tend to drastically oversimplify the matter. They typically make very strong assumptions about which specific jurisdictions are SPE hotspots (see for example Meyer et al., 2014; Lu et al., 2014). The problem here is that it is incorrect to assume that all subsidiaries in a tax haven (Hong Kong, for example) are SPE-related. By the same token, many CMNE investments to seemingly legitimate destinations are actually SPE-related. For example, the US State of Delaware is a recognized low tax jurisdiction. It also receives a considerable number of Chinese subsidiaries, many of which are likely to be SPE-related. Similarly, a developed country like the Netherlands is a SPE

hotspot. Thus, when counting subsidiaries, an optimal solution is to identify all SPEs, regardless of their location. Of course, this problem is made more difficult by the fact that many holding companies may not be registered as such, but instead as providers of a range of ‘business services’. So when they are provided in annual reports—and often they are not—detailed descriptions of a subsidiary’s business and its NACE codes may not reveal its true purpose.

Thirdly, related to the above, it is important to be clear about what a Chinese MNE actually is. Many CMNEs are transnational only by virtue of having one or more SPEs held in offshore jurisdictions. Are these businesses really MNEs? Should MNE theories be tested or created using them? We would argue they are not MNEs in any conventional sense. This problem is particularly acute in the Chinese case. For many Chinese businesses, particularly those in the private sector, developing a legal presence in Hong Kong and in its related THOFC networks is a first step in accessing deeper pools of capital and a superior institutional environment, and potentially lowering tax bills—the original rationale for round-tripping. So, as our Orbis sample shows, many CMNEs are multinational only by virtue of this close relationship to Hong Kong. Such businesses, in reality, are far more concerned with the domestic Chinese market, than with foreign countries, going offshore only to improve their position back home.

Related to the above point, it is important to note that corporate inversions, whereby a corporation's legal domicile is moved to another country while all its material operations (including management, functional headquarters and majority shareholders) remain in its country of origin, also pose significant challenges to the use of ‘Chinese’ FDI data. Such inversions hide the true provenance and origins of MNEs and have become increasingly common (Whichard, 2008; Hanson et al., 2015).<sup>13</sup> Using the Orbis database, for example, we identified hundreds of inverted CMNEs. These Chinese businesses have an ultimate controlling corporate owner in the Cayman Islands and BVI. Nearly all of their real operations, however, are in China. Examples include well-known companies, like Tencent, Alibaba, Xiaomi, Baidu, Geely, Li Ning, Goodbaby International, China Mengniu Dairy, WH Group, Tianyun International and Nine Dragons Paper. While we do not discuss the issue in greater detail here, suffice to say that corporate inversions create further serious problems in tracing down and

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<sup>13</sup> US corporations, for example, have been highly active in allowing their onshore affiliates to be acquired by offshore companies (which are often far smaller). This significantly inflates inward FDI to the US and outward FDI from the countries where the ultimate owners are based (i.e. often Ireland in the US case). This has had a large impact on the US FDI position, as well as on geographical patterns and volumes of FDI flows (Whichard, 2008).

understanding CMNE identity. This is because firm-level analyses (using databases like Orbis, for example) typically assume that the geographical location of the ultimate parent in its presumed country of origin. In other words, a Chinese MNE is presumed to have an ultimate owner in China. This, however, is not always the case. Moreover, the OECD newly updated FDI data collection procedures, which advise collecting FDI data on the basis of ultimate ownership, may also struggle to pick up such inverted CMNEs (Whichard, 2008; Hanson et al., 2015).

Fourthly, even when the SPE problem is acknowledged, there often appears to be a general lack of rigor and detail in explaining how it is dealt with. Many research papers typically dismiss the issue with just one or two sentences – as a minor problem of no consequence. They may, for example, note that ‘during the raw data cleanup process....we exclude tax haven cases’ (Shi et al., 2017, p. 460). How? Which tax havens are excluded? Does that include all investments in Hong Kong? How exactly are the cases excluded? Are only investment holding company SPEs in THOFCS excluded? In general, one has to be somewhat skeptical of papers that make such claims, owing to the actual complexities involved in the problem they claim to be solving.

Finally, a further problem involves the incorrect *exclusion* of SPE related investments in some papers when the theoretical underpinnings of the research may suggest inclusion. It probably does make sense to include THOFC-related investments when investigating institutional arbitrage. In these cases more light might be shed on why CMNEs use THOFCS, how they engage in institutional arbitrage, and how these trends are evolving. In fact, it may be argued that research in this area is sorely needed, as it may help us better understand the real identities of CMNEs.

## **Conclusion**

Direct investments to THOFCS as well as the routing of investment flows via THOFCS is a real problem for international business scholars. While the problem has been given some lip-service, in general it has been poorly understood and given inadequate attention. This is evident in the research on CMNEs, where THOFC use is common owing to a number of historical factors. The problems we have illustrated here with respect to CMNEs, however, also affect MNEs from many other countries, both emerging and developed (Beugelsdijk et al., 2010; OECD, 2015). This is why the OECD has now heavily revised its standards for collecting FDI data, asking national agencies to report SPE-related FDI and inward FDI by both immediate and ultimate investor.

Buckley et al.'s (2007) JIBS decade award winning paper has had a major influence on CMNE research. Unfortunately, it seems to have legitimized the casual use of FDI data to measure MNE activity. We have shown here how many papers since then have committed similar errors, insofar as they have not adequately scrutinized and critically evaluated the validity of Chinese FDI data. This is true of studies which have relied upon the broader, aggregated data, published by MOFCOM at the national level, as well as those which have focused at the firm-level. Even a preliminary critical evaluation of MOFCOM data suggests serious potential issues with the routing of investments via tax havens which accounts for the heavy geographical concentration in THOFs like the Cayman Islands and BVI, as well as the strong industrial composition bias towards business services – an area in which China is not known to have any comparative advantage. Unfortunately most, if not all, of the JIBS papers published over the past decade are based upon the questionable use of various types of FDI data. It is important that international business as a discipline become less complacent about this problem, as ignoring it is likely to lead to wasted research efforts, and more worryingly, to unreliable and potentially biased findings, setting us back in our understanding of CMNE identity (Beugelsdijk et al., 2010).

So far, CMNE identity is considered to be strongly shaped by a number of unusual factors which may imbue these firms with distinct and unique characteristics, such as state ownership and the importance of business/government political relationships; the need for rapid firm-level catch-up via strategic asset seeking--including high risk investments in psychically distant developed market economies; home market imperfections and institutional voids which create large diversified business groups; and institutional arbitrage and capital flight as CMNEs look to exploit better and safer institutional environments. How does our understanding of CMNE identity change as a result of our findings on the use of tax havens by CMNEs and how does it affect investment statistics? In truth, it is impossible to be certain. We do not know how the inclusion of potential Dutch SPE-linked subsidiaries affects the results of Meyer et al. (2014), or those of Buckley et al. (2007) and Lu et al. (2014). Similarly, we cannot say how the inclusion in the sample used by Liang et al. (2014) of over 400 SPE-linked subsidiaries, which probably make up more than half of their sample if one extrapolates from Lu et al. (2014), affects their results. Short of replicating these studies with a sample that excludes SPE-related subsidiaries, it is impossible to know. Future research, might consider the feasibility of replicating some of these studies using improved FDI data, so that we may come to a more reliable understanding of CMNE identity. Beyond this, perhaps greater weight and attention should be given to qualitative studies of CMNEs when

assessing CMNE identity.

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**Table 1:** Post Buckley (2007) empirical papers on CMNEs.

<b>Paper</b>	<b>Data</b>	<b>Type/purpose of Study</b>	<b>THOFCS/SPEs discussed?</b>	<b>Inclusion of SPEs and THOFC countries probable?</b>
Buckley et al. (2007)	MOFCOM OFDI, project level data	A location choice study	No	Yes: HK, Cyprus, Netherlands, Singapore
Cui and Jiang (2012)	CMNE survey, CMNEs identified via MOFCOM 2005 OFDI projects	Questionnaire directed at CMNE managers	No	Yes: HK, Cayman Islands, BVI, Singapore etc.
Duanmu (2014)	Greenfield FDI data	Looks at expropriation risk of FDI by CMNEs	No	Not clear
Pan et al. (2014)	Listed company data, uses all foreign subsidiaries.	Looks at the influence of government ownership and political connections	No	Yes: HK, Cayman Islands, BVI, Singapore, etc.
Wang et al. (2012)	MOFCOM, 1,231 manufacturing firms with 1390 overseas projects, uses ARIES data as well.	Explores how government involvement (and level) effects international expansion	No	Yes: HK, Cayman Islands, BVI, Singapore etc.
Liang et al. (2014)	Listed firms, Shanghai and Shenzhen Stock Exchanges, Datastream, WIND, CSMAR, etc.	Explores how political connections influence OFDI	No	Yes: HK, Cayman Island, BVI and Singapore etc.
Lu et al. (2014)	Firm-level, taken from reports of listed firms on Shanghai/Shenzhen stock exchanges	Looks at how government support of FDI projects and host country institutional environments interact with prior entry experience	Yes	Yes: the Netherlands, Luxembourg, Liberia, Panama, Switzerland
Meyer et al. (2014)	Firms listed on the Shanghai and Shenzhen Stock Exchanges in 2009	Explores how state ownership influences strategies for legitimacy in host country	Yes	Yes: Netherlands, Luxembourg, Switzerland, etc.
Shi et al. (2017)	NBS and Directory of Chinese Outward FDI Database (MOFCOM),	Study OFDI in 2000-2009 period to explore impact of institutional fragility	Yes	Not clear how THOFCS are excluded
Gaur et al. (2018)	Survey of CMNEs	Questionnaire directed at CME managers, mixed methods	Yes	Yes: HK, Cayman Island, BVI and Singapore etc.

**Table 2: Top host countries for China's outward FDI in 2016, MOFCOM (US\$ billions)**

No.	Host country	Outward FDI flow	percentage (%)
1	Hong Kong	114.2	58.2
2	United States of America	17.0	8.7
3	Cayman Islands	13.5	6.9
4	BVI	12.4	6.3
5	Australia	4.2	2.1
6	Singapore	3.2	1.6
7	Canada	2.9	1.5
8	Germany	2.4	1.2
9	Israel	1.9	0.9
10	Malaysia	1.9	0.9
11	Luxembourg	1.6	0.8
12	France	1.5	0.8
13	United Kingdom	1.5	0.7
14	Indonesia	1.5	0.7
15	Russian Federation	1.3	0.7
16	Vietnam	1.3	0.7
17	Netherlands	1.2	0.6
18	Korea	1.2	0.6
19	Thailand	1.1	0.6
20	New Zealand	0.9	0.5
	Total	186.7	95.0

Source: China's Outward Foreign Direct Investment Bulletin (2016)

**Table 3:** Chinese FDI stock in selected host countries by immediate and ultimate owner in 2015 (US\$ millions)

Country	(a). Immediate FDI from China	(b). Ultimate FDI from China	Column (a)/(b)
US	16,769	33,522	2
France	2,034	6,413	3.2
Germany	3080	4,723	1.5
Italy	107	624	5.8
Hungary	234	1947	8.3
Czech Republic	268	371	1.4
Poland	218	928	4.3

Source: OECD, 2018.

**Table 4:** Geographical and sectoral distribution of level 1 foreign subsidiaries of CMNEs and state-owned CMNEs

All CMNEs					State owned CMNEs				
Country	No.	NACE description	NACE	No.	Country	NACE description	NACE	No.	
Hong Kong	931	Wholesale and retail activities	4500-4791	251	Hong Kong	Investment holding companies	6420	97	
Singapore	170	Activities of investment holding companies	6420	156	United States	wholesale and retail activities	4500 to 4791	75	
UK	166	Other monetary intermediation	6419	45	Singapore	Other monetary intermediation	6419	47	
BVI	156	Other business support service activities	8299	42	United Kingdom	Other business support service activities	8299	19	
Cayman Islands	110	Service activities incidental to water transportation	5222	34	BVI	Business and other management consultancy activities	7022	14	
Germany	105	Agents specialised in the sale of other particular products	4618	32	Australia	Engineering activities and related technical consultancy	7112	11	
France	81	Manufacture of communication equipment	2630	30	Japan	Manufacture of electronic components	2611	10	
Australia	71	Business and other management consultancy activities	7022	25	Germany	Other financial service activities, except insurance and pension funding	6499	9	
Japan	45	Manufacture of electronic components	2611	19	France	Production of electricity	3511	9	
Korea	43	Other financial service activities, except insurance	6499	17	Cayman Islands	Activities of head offices	7010	6	
Italy	41	Production of electricity	3511	15	Canada				
Netherlands	41	Activities of head offices	7010	14	Netherlands				
Brazil	38	Construction of residential and non-residential buildings	4120	12	Italy				
Canada	35	Agents involved in the sale of machinery, industrial equipment, ships and aircraft	4614	11	Bermuda				

Note: the full CMNE sample has 2, 926 foreign subsidiaries in total, state-owned MNE sample has 1,428 foreign subsidiaries. Here we report only major NACE code categories and major recipient countries.

**Table 5:** Industrial and geographical composition of onward-journey investments (i.e. level 2 subsidiaries) held via selected THOFCs (i.e. Hong Kong, BVI, Cayman Islands, Singapore, Bermuda and Switzerland).

Nace code	Number	Country	Number
6420 (investment holding)	243	China	1688
6831	116	BVI	740
3511	42	Hong Kong	670
7735	33	Cayman Islands	200
2529	31	Singapore	130
4652	30	US	126
7022	30	GB	96
7490	30	Netherlands	87
6619	29	Bermuda	61
8299	28	Ireland	44
6499	26	Australia	44
2611	25	Germany	43
7010	25	Malaysia	33
5223	23	Switzerland	32
7112	23	Mexico	27
6190	20	Luxembourg	25
6399	20	Canada	25
6612	17	Macao	24
4618	16	Brazil	23
5229	16	Zambia	21
6419	15	South Korea	16
6492	14	Japan	16
2620	13	Indonesia	15
4519	13	Russia	14
6810	13	Spain	14
4651	12	Italy	13
4671	12	Belgium	12
7911	12	Thailand	11
0729	11	SL	11
1107	11	RO	10

Notes: there are 251 level 2 subsidiaries in NACE 5020 which are excluded.

