MASTER OF PUBLIC POLICY
CAPSTONE PROJECT

Chinese Investment in Canada: Trends and Policy Responses

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Capstone Executive Summary

After constructing a novel, transaction-level dataset on China's direct investment into Canada, this paper examines the trends of said foreign direct investment over the past quarter century and places them within the context of their ongoing public policy issues. China's investment into Canada has a controversial history, in large part due to concerns over China's state-ownership of the investors. By presenting the scale and forms of this investment, it is possible both to determine what avenues exist to respond to it, and to assess how founded concerns over ownership are. The dataset reveals that China's investors conducted 783 transactions into Canada for the period 1993 through 2017, for a total of C$86 billion.

State-owned investments have played a significant role in China's investment history in Canada, but have in recent years become less significant than private investment flows from China. Still, the controversy surrounding China's investment activities continues to draw significant attention, with the result being a need for evidence-based responses to the costs, benefits, risks, and opportunities of said investment. Options for amendments to the Canadian *Investment Canada Act* are one such avenue to improve the system, but must balance public and international investment concerns, and need to be conducted alongside enhanced investment monitoring policies.

Background and Issue

Background

Canadian policy responses to China's outbound foreign direct investment (OFDI) require an understanding of the trends in firm-level OFDI flows from China to Canada. Bridging this informational gap will allow policy-makers to offer more adequate analysis of the China-Canada investment context. Additionally, policy-makers can benefit from placing this descriptive analysis within broader trends in both Chinese outbound investment globally and Canadian receipt of inbound investment. Policy-makers seeking to induce additional inbound Chinese OFDI into Canada or constrain this flow of investment require evidence-based, prescriptive avenues for policy change.

Globally, the scale and scope of China's investment has been divisive, and Canada's diverse responses to this flow of investment have been no exception. The debate surrounding China's OFDI, however, is not always informed by data; what data is out there is itself often disputed across the many fora for debate. While there is generally a broad agreement by economists that a country benefits from receiving FDI – via mechanisms such as spillover efficiencies and greater access to global supply chains – there are still issues with assessing the extent of investment. [1] [2] [3] [4]

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[1] Blomstrom, M., Kokko, A., and Zejan, M. 2000. *Foreign direct investment: Firm and host country strategies*. New York: St. Martin's Press Inc.

[2] Resende, Paulo T.V., and Alvaro Bruno Cyrino. "The Transnationalization of Supply Chain Management: the Experience of Brazilian Industrial Companies." In *The Rise of Transnational Corporations from Emerging Markets: Threat Or Opportunity?* Edited by Karl P. Sauvant. Northampton: Edward Elgar Publishing, Inc., 2008. 32-52.

[3] Buckley, Peter J. et al. "Explaining China's Outward FDI: An Institutional Perspective." In *The Rise of Transnational Corporations from Emerging Markets: Threat or Opportunity?* edited by Karl P. Sauvant. Northampton: Edward Elgar Publishing, 2008.

[4] Globerman, S. & Shapiro, D. "Economic and strategic considerations surrounding Chinese FDI in the United States" Asia Pacific Journal of Management (2009) 26: 163.

While national and supranational accounts have the potential to be the most comprehensive sources of FDI data, given the enhanced ability of governments and supranational bodies with respect to data collection, enforcement of compliance, and verification, they have their limitations. As such, while Statistics Canada, the National Bureau of Statistics of China, Organisation for Economic Co-operation and Development (OECD), and United Nations Conference on Trade and Development (UNCTAD) data all exist on China's OFDI into Canada, their utility is limited for two main reasons. The first critical limitation is a propensity to track investment from the most recent source country, and not further registering of FDI to the ultimate source country. The second limitation has to do with the levels of aggregation involved, as privacy considerations typically limit reporting to a mixture of highly aggregated data for many variables, with transaction-level data little more than a public register of entrant investors' names and potential target geographies.

Still, there is value in reviewing the existing systems in order to illustrate the challenges and scope of investment monitoring. According to Statistics Canada, China and Hong Kong's FDI stock in Canada is C$29 billion.[5] Limitations include the lack of detailed information on investment beyond aggregate values, substantial lags in reporting, and issues with tracking investment by ultimate ownership. Conversely, the National Bureau of Statistics of China reports in its China Statistical Yearbook 2017 that China's FDI stock in Canada is US$13 billion.[6] Limitations include a lack of data from Hong Kong and non-reporting of investments through third countries. The OECD

[5] Statistics Canada. Table 36-10-0008-01 International investment position, Canadian direct investment abroad and foreign direct investment in Canada, by country, annual (x 1,000,000).

[6] National Bureau of Statistics of China. *China Statistical Yearbook 2017*.

reports China and Hong Kong's FDI stock in Canada as US$25 billion (C$33 billion); UNCTAD reported China's FDI stock in Canada as US$12 billion in 2012, the last year reported in their Bilateral FDI Statistics report.[7] [8]

In response to this perceived gap, in recent years there has been a proliferation of Chinese investment monitoring datasets. The American Enterprise Institute and the Heritage Foundation's China Global Investment Tracker (CGIT) is the most comprehensive dataset specifically focused on China's global construction activity and investment. CGIT has tracked nearly 3,000 transactions by amount, location, parent company, and industries. Publicly available and with the aim to be comprehensive, CGIT has recorded $1.8 trillion in investments around the world which stem from China. According to CGIT, China's FDI stock in Canada is US$49.67 billion. Limitations of this dataset include its relatively recent coverage (a 2005 start date) and its minimum recorded value threshold of US$100 million. The latter may be especially impactful given the substantial share of flows which stem from smaller transaction amounts.

The Financial Times' fDi Markets Crossborder Investment Monitor tracks worldwide greenfield investments across all countries and sectors, reporting such elements as capital amounts and gross jobs created by each investment.[9] Launched in 2003 and published online, its data is collected and updated in real time and is aimed for a corporate and large agency audience. According to the fDi Monitor, China's greenfield FDI stock in Canada was US$3 billion at the end of 2015. As fDi Markets only records greenfield investment, it does not capture the full scope of investment. Review of the

[7] OECD (2018), FDI flows (indicator).
[8] United Nations Conference on Trade and Development (2014), *Bilateral FDI Statistics 2014*.
[9] Financial Times (2015), *fDi Markets* dataset.

database indicates that its algorithmic collection of transactions has generated false positives (i.e. announced projects which never broke ground) as well as spurious estimations of investment values and gross jobs created.

The Rhodium Group's China Investment Monitor (CIM) tracks Chinese investment into the United States, its ownership, industry, and deal type. According to the CIM, China's FDI stock in the United States is US$138.1 billion.[10] Limitations include CIM's minimum recorded value threshold of US$500,000, lack of recorded portfolio investment, and algorithmic estimation of some greenfield investment data precluding precision.

The University of Sydney and KPMG's Demystifying Chinese Investment in Australia (DCIA) database records Chinese investment into Australia, with reports providing a comprehensive overview for public consumption. According to the DCIA, China's FDI stock in Australia is US$90 billion.[11] Limitations include DCIA's minimum recorded value threshold of US$5 million and lack of recorded portfolio investment.

The Mercator Institute for China Studies (MERICS) and the Rhodium Group (RHG)'s series of reports monitor Chinese investment in the European Union's economies in a similar manner as RHG's CIM, this transaction-level dataset used by MERICS and RHG is not published, but has been used extensively across MERICS and co-published reports. According to recent reports, China's FDI stock in the European

[10] Rhodium Group, *China Investment Monitor* data, 2018.
[11] University of Sydney and KPMG, *Demystifying Chinese Investment in Australia* data, 2018.

Union economies is EUR 35 billion, which is also the amount recorded by the European Commission's Eurostat.[12] [13]

As such, it is evident that investment monitoring with respect to China is still a relatively nascent field, and will require further research. Even so, it is still possible to place the trends which have been monitored into a discussion of historical and institutional backgrounds of Chinese investment in Canada, which are expanded upon in greater detail below.

Issue

China's outbound foreign direct investment has garnered significant policy interest over the past decade. On the one hand, the scale of China's economy and recent Chinese economic reforms have led to China's emergence as a significant, new source of capital for foreign firms and governments; as such, when interests co-align, there are notable incentives for policy-makers to seek to attract Chinese OFDI. In the Canadian context, Chinese investment has been viewed as a means to boost economic activity at the regional- or sectoral- level, and as means of diversification of Canadian economic activity away from the United States.

Conversely, Chinese OFDI has also attracted controversy and raised concerns surrounding potential loss of ownership over Canadian economic sectors, especially with respect to firms or industries viewed as 'national champions'. Second-order concerns are also prominent in policy discussions on Chinese OFDI to Canada, namely

[12] Eurostat (2017), 'The EU continues to be a net investor in the rest of the world', Eurostat News Release, 12 January 2017

[13] European Commission (2017), 'Trade: Countries and regions'

the potential for Chinese state influence of domestic policies and the perception of risks to Canada's national security. These discussions are further fueled by the relative novelty for Canadian policy-makers in crafting appropriate policy responses to investment from firms which may have direct state involvement, or at the very least, tacit encouragement to engage in non-profit maximizing investments.[14] [15] [16]

Policy-makers face choices when it comes to encouraging or discouraging China's investment into Canada, and their preferences may change depending on the form of investment, amounts, locations, sectors, and ownership involved in transactions. This report describes the form and scope of China-sourced investment activity in Canada over the past quarter century, providing firmer evidence for policy-makers' consideration. Additionally, this investment history is contextualized, across Canada's investment history and that of other countries, in order to give observers a better sense of the Canadian experience.

The scope of this research is limited to commercial OFDI from China (here treated as the Mainland, Hong Kong, and Macao). While non-commercial investment activities – namely, personal investments – are often of strong interest within Canadian public debates, they are excluded due to issues of data collection and verification. Much attention has been focused on the extent to which Chinese nationals are investing in Canadian residential housing markets, Vancouver and Toronto in particular, and the impacts of their investment activities on such issues as housing affordability and

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[14] Mintz, Jack, "China's state-owned enterprises will make us all weaker and poorer," *Financial Post*. January 4, 2018.

[15] Mintz, Jack, "Construction group warns of price-cutting if Aecon sold to China," *The Globe and Mail*. February 4, 2018.

[16] Mintz, "Time to put -limits on larger state takeovers," *Financial Post*. September 10, 2012.

available housing stock. However, due to the extremely disaggregated and private nature of these transactions across all sectors, and due to very basic issues of identifying and classifying investors and their transactions at that level, this non-commercial investment is excluded from this study.

Historical Context

China as Emerging Investor

Foreign direct investment, or FDI, has increased in importance for the global economy over the past few decades. This has especially been the case for developed economies such as Canada, which since the Second World War have been the primary targets for FDI, typically from similarly higher-income economies.[17] According to data from the American Enterprise Institute and the Heritage Foundation's *China Global Investment Tracker*, Canada ranks seventh among all recipients of China's FDI, with a stock of US$49.1 billion in investments as of August 2018. [18] If the total of C$84.6 billion (US$77.0 billion) recorded for this paper is used, and absent adjustments to any other country totals, Canada would rank third, behind the United States, with US$178.7 billion, and Australia, with US$111.4 billion.

Turning abroad, there are few comparator economies closely similar to the Canadian context. Most economies, while at similar levels of development, are far less resource focused; conversely, developing economies may have greater resource

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[17] Schularick, Moritz, "A Tale of Two "Globalizations": Capital Flows from Rich to Poor in Two Eras of Global Finance," in *International Journal of Finance & Economics*, John Wiley & Sons, Ltd., vol. 11(4), pages 339-354. 2006.

[18] American Enterprise Institute and Heritage Foundation, *China Global Investment Tracker*, accessed August 1, 2018.

investment, but vary considerably in other areas. Australia has typically been identified as the closest, strongest comparator for Canada to learn from, for reasons stemming from Australia's more extensive experience with China in terms of scope and history, and from its similarities to Canada.

Australia's relative proximity to China geographically, in terms of time zones, and through historical links have aided its investment attraction from China, as has its complementary, resource-endowed economy. In many ways, this more advanced engagement offers lessons to Canada, concerning state-owned enterprise (SOE) activity in the resource sector and Chinese investors in residential real estate and are useful comparators for Canadian policy responses.[19] [20] Canada's policy responses to China's FDI often take the form of reactions to very specific events – and in some cases, sole transactions – whereas Australia's greater experience appears to have resulted in a more integrated awareness of China's FDI throughout Australian policy discussions.[21]

Australian policy observers have suggested improved responses to China's FDI via improvements to institutional and regulatory capacity and capabilities, as opposed to tasking investment review systems to target China's investment directly through investor origin rules, or indirectly through thresholds for review which appear to be designed to target China's investments all the same.[22] Australia's suite of experiences have

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[19] Peter Drysdale and Christopher Findlay, "Chinese foreign direct investment in Australia: policy issues for the resource sector" in *China Economic Journal* Volume 2, Issue 2. 2009.

[20] Dallas Rogers, Chyi Lin Lee, and Ding Yan, "The Politics of Foreign Investment in Australian Housing: Chinese Investors, Translocal Sales Agents and Local Resistance" in *Housing Studies* Volume 30, Issue 5. 2015.

[21] For example, see Australia's central bank directly reporting on China's FDI as part of its monetary policy statements: Reserve Bank of Australia, "Box B: Chinese Direct Investment in Australia" in *Statement on Monetary Policy – November 2017*.

[22] Peter Drysdale & Shiro Armstrong & Neil Thomas, 2016. "Suggestions to Improve Australia's Foreign Investment Review Framework : Submission to the Inquiry by the Senate Economics References Committee," Finance Working Papers 25460, East Asian Bureau of Economic Research.

implications for Canada, which has also struggled with setting up a regulatory system which appropriately responds to China's investments.

Canada as Recipient

Contentious experiences with China's investment have led to much of Canadian policy discussions being focused upon investment restricting policies, and the concerns are feeding these policies are varied. Perhaps most critically, while China is not unique in terms of rousing Canadian sensitivities in sectors framed as 'national champions' or 'jewels', it has been at the forefront of these well-documented and d-disseminated discussions over the past decade.[23] [24] Canadian observers have raised concerns surrounding sovereignty, resource and land security, national security, and reciprocity in access for Canadian investors.[25] [26] [27] [28] Investment activities in specific sectors have also raised discussions on investor adherence to environmental and labour standards and the hiring of foreign workers.[29] That the tone and tenor of China FDI policy discussion often revolves around these concerns is therefore unsurprising, given the breadth of policy areas involved.[30] [31]

These concerns have been well-documented in opinion polling at the national and provincial levels. With specific reference to commercial investments, China's

[23] Nathan Vanderklippe, "Grouse Mountain acquisition just the start for Chinese investment firm, banker says," *The Globe and Mail* July 24, 2017.

[24] Mintz, "Weaker and poorer," 2018.

[25] Douglass Todd, "Does China's money threaten Canada's sovereignty?," *Vancouver Sun* August 1 2017.

[26] Mintz, "Weaker and poorer," 2018.

[27] Josephine Smart, "Canadian Investment in China and Chinese Investment in Canada," *SPP Research Papers* Volume 5, Issue 27. Calgary: University of Calgary, 2012.

[28] Charles Burton, "Engaging China poses potential risk to Canada's national security," in *The Dragon at the Door: The Future of Canada-China Relations*. Ottawa: Macdonald-Laurier Institute, 2017.

[29] Kate Lunau, "Our Chinese oil sands," *Maclean's*, August 8 2012.

[30] Smart, 2012.

[31] Wendy Dobson, "China's State-Owned Enterprises and Canada's FDI Policy," Calgary: 2014

investments are particularly controversial when they gain controlling stakes in existing Canadian firms, when the investing firm is a state-owned enterprise, and when they invest in commercial real estate, technology, and energy and natural resources. Concerns appear driven by issues in resource security, environmental and labour practices, and a lack of trust.[32] [33] [34] Significantly, China-sourced investments are also less popular than investments from all other surveyed sources of investments, an indication of the relative uniqueness of this policy challenge.

The aggregation of concerns into distinct categories is a useful result of these opinion polls, but they should be taken as complementary to narratives built on more discrete concerns, which often cut across these categories. For example, jobs and domestic business impacts are two key, interlinked areas of controversy. There are perceptions that investment from China either replaces jobs and businesses in Canada, or at least lowers the quality of jobs and business activities relative to cases when investment is sourced domestically or from a non-China investor. There are also concerns – primarily voiced in the resource sector – that M&A or greenfield investment projects will bring over Chinese nationals to work on their sites, thereby displacing Canadian labour opportunities and potentially leading to lowered on-site environmental practices.

Reflecting the above, much of the public discourse surrounding China's OFDI in Canada occurs within the media. In this area, commentators have voiced concerns over

[32] Asia Pacific Foundation of Canada, *National Opinion Poll 2018: Canadian Views on Asia*. Vancouver: 2018.

[33] Asia Pacific Foundation of Canada, *National Opinion Poll 2015: Canadian Views on Asian Investment*. Vancouver: 2015.

[34] China Institute, *Annual China Institute Survey 2017: Albertans' Views on China*. Edmonton: 2017.

China's political goals, national security implications, residents migration into Canada, drive to acquire commodities, and history of pollution.[35] [36] [37] [38]

Given the aforementioned concerns, it is no surprise that elected governments at the municipal, provincial, and federal levels have spent considerable time responding to specific cases or trends in those sectors; aside from federal legislation and regulation, these include provincial- and municipal-driven taxes on foreign purchases and empty real estate.

Canada is not unique in its concerns over Chinese investment, and in fact appears to have been an early harbinger of a more general, international push-back against select practices by China, particularly against China's slack intellectual property rights and forced technological transfers.[39] These two issues are in turn part of a larger suite of concerns surrounding the degree to which China's firms may act not out of profit-maximizing interests, but due to ancillary state direction.

Based on the dataset generated for this report, China's SOEs dominated in terms of deal values during the 2005 through 2013 period, and it is apparent that legacies of those first impressions remain. However, more recent skepticism regarding state-influence cannot just be framed as a legacy of earlier these discussions; rather, there are continuing indications that the already significant influence of private sector Party committees is increasing, which is becoming increasingly acknowledged within policy

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[35] Mintz, "Weaker and poorer," 2018.

[36] CBC, "The dangers of Chinese investment in Canada." January 25, 2018.

[37] Younglai, Rachelle, "New rules stem Chinese real estate investment in Canada," *The Globe and Mail*. March 11, 2018.

[38] Gillis, Charlie, Chris Sorensen, and Nancy Macdonald, "China is buying Canada: Inside the new real estate frenzy," *Maclean's*. May 9, 2016.

[39] Stephen Nagy, *Twin Trap Challenges – China's Trajectory in the Years Ahead* in Canadian Global Affairs Institute Roundtable series. Calgary: Canadian Global Affairs Institute, July 2018.

discussions.[40] [41] As China's state and Party heavily overlap, the latter's increased influence within the private sector makes it more likely that nominally private firms will act with motives aside from profit maximizing.

China's SOEs have been specifically flagged as engaging in overseas activities to secure resources, with evidence of such strategic activities emerging within their practices in the energy and metals and minerals sectors in particular.[42] [43] [44] While the China-side motivation is not demonstrated within the collected data on the Canadian experience, there is at least evidence that Canada's SOE experience reflects international observations: of the 215 recorded transactions by state investors, 120, or 56%, were in the metals and minerals sector, with another 43 (20%) in the energy sector. This at least implies that China is acting to secure resources in Canada, although further research is necessary. At the same time, as will be discussed below, the role of SOEs in terms of both number of transactions and values of flows have been surpassed by private investor activity since 2012 and 2014, respectively.

While Canada has long been a recipient of foreign investment, it was only in the second half of the 20th century that the debate on foreign investment started in its current form.[45] The policy discussions that would lead to the net benefit test was the Gordon Commission's 1957 report, which raised concerns about foreign ownership of

[40] Wei Yu, *Party Control in China's Listed Firms*. Hong Kong: The Chinese University of Hong Kong, 2009.

[41] Zhang Ye, "Private sector Party committees start to bloom," in *Global Times* 2016/7/1.

[42] Zhang Jian, "China's Energy Security: Prospects, Challenges, and Opportunities." Washington, D.C.: The Brookings Institution, 2009.

[43] Jeffrey D. Wilson, "Chinese resource security policies and the restructuring of the Asia-Pacific iron ore market" in *Resources Policy* Volume 37, Issue 3. 2012.

[44] Theodore H. Moran, *China's Strategy to Secure Natural Resources: Risks, Dangers, and Opportunities*. Washington, D.C.: Peterson Institute for International Economics, 2010.

[45] Andrew Jackson, "The MAI and Foreign Direct Investment," in *Dismantling Democracy: The Multilateral Agreement on Investment (MAI) and Its Impact*, ed. Andrew Jackson and Matthew Sanger (Toronto: James Lorimer & Company Ltd., Publishers, 1998), 251.

Canadian firms within the federal government.[46] Even so, while the report contained recommendations on ensuring Canadian employment, supply procurement, transparency, and leadership remained within Canada, it stopped short of recommending mechanisms to measure and prohibit this behaviour.[47]

A decade later, discussions on FDI took on a sovereignty dimension, with the federal task force behind the 1968 Watkins Report on FDI taking the stance that FDI negatively impacted Canada's sovereignty.[48] Amid these discussions, in 1984 the federal government passed the *Investment Canada Act* (*ICA*), creating a new bureau, Investment Canada.[49] *ICA* has had substantial implications for investment approvals: by 2012, the Canadian government had approved 18,700 transactions under the *Investment Canada Act*.[50]

While there are indications that *ICA*'s existence dissuaded some potential investment in the 1990s,[51] it was not until the past decade that its usage became controversial. The effects of *ICA* on investment were also made more explicit during this time, a result of high-profile applications of the test in the aerospace, potash, retail, and cultural sectors.[52] The increase in discussion and application was in no small part due to an increase in high-profile activities from foreign investors, including SOEs, such

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46 Michael Hart, *A Trading Nation: Canadian Trade Policy from Colonialism to Globalization* (Vancouver: UBC Press, 2003), 301-2.

47 Privy Council, *Royal Commission on Canada's Economic Prospects* (Ottawa: Canada, 1958).

48 A. E. Safarian, *Simplifying the Rule Book: A Proposal to Reform and Clarify Canada's Policy on Inward Foreign Direct Investment* (Toronto: C.D. Howe Institute, 2015), 12.

49 Hart, *A Trading Nation*, 528.

50 Justin G. Persaud et al., "Canada," in *International Legal Developments Year in Review: 2012*, eds. John B. Attanasio et al. (Chicago: American Bar Association's Section on International Law and Practice, 2013), 558.

51 Dornan, "Other People's Money," 55.

52 OECD, *OECD Economic Surveys: Canada 2012* (Paris: OECD Publishing, 2012), 34.

as the United Arab Emirates' Abu Dhabi National Energy Company purchase of Prime West Energy Trust.[53]

Within this environment, in 2007, the federal government set out new guidelines for the Minister of Industry's reviews of SOEs, which added commitments to Canadian laws and practices as a consideration under the net benefit test for SOE applications.[54] [55] The Minister of Industry, flagging a need for new guidelines regarding SOE investments,[56] also floated the idea of an *ICA* national security test, to be administered by the federal government.[57] As a result of the lack of security considerations within the net benefit test, amendments to the *Investment Canada Act* occurred in 2009, creating a new, separate test from the net benefit one.

Further activity surrounding the net benefit test at this time included the federal Competition Policy Review Panel's 2008 recommendation that, given FDI was already of benefit to Canada, and that the global competitive environment had changed since the 1980s, the net benefit test be replaced by a national interest test, conceived as an easier, more transparent policy for investors, with the onus placed on the government to prove an investment was not in the national interest. [58] [59] [60] The year was also a watershed for the net benefit test, as for the first time in its history, the test was used by the federal government to reject an application: Alliant Techsystems Inc., an American

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53 Marcela B. Stras et al., "Canada," in *International Legal Developments in Review: 2007* (Chicago: American Bar Association's Section on International Law and Practice, 2008), 937.

54 Alison L. Dempsey, *Evolutions in Corporate Governance: Towards an Ethical Framework for Business Conduct* (Sheffield: Greenleaf Publishing Limited, 2013), 127.

55 Safarian, *Simplifying the Rule Book*, 9.

56 Susan M. Hutton, *Canada Considers Changes to Foreign Investment Review* (Ottawa: Stikeman Elliott LLP, 2007).

57 Stras et al., "Canada," 939.

58 Stras et al., "Canada," 938.

59 Safarian, *Simplifying the Rule Book*, 2.

60 Philippe Bergevin and Daniel Schwanen, *Reforming the Investment Canada Act: Walk More Softly, Carry a Bigger Stick* (Toronto: C.D. Howe Institute, 2011), 10.

aerospace and defense firm, was prevented from purchasing a space technology firm from Vancouver, MacDonald, Dettwiler and Associates.[61]

At the time, many saw the proposed BHP Billiton-Potash Corp deal as a bellwether for more politicized usage of *ICA*.[62] However, through joint ventures and minority stakes, foreign firms were still able to enter the Canadian upstream resource industries.[63] Additionally, in 2012 the federal government approved both state-owned enterprise China National Offshore Oil Corporation (CNOOC)'s acquisition of Nexen and Petronas' acquisition of Progress.[64] [65] In the case of CNOOC, the acquirer made substantial efforts to pass the net benefit test, yet its acquisition still prompted concerns about misalignments between Canadian and Chinese interests and values which were not adequately captured by the net benefit test. [66] [67]

The CNOOC approval, and to a lesser extent the BHP Billiton-Potash Corporation of Saskatchewan proposal, had wide-ranging implications on the net benefit test, and Canada's investment openness in general.[68] [69] This was not surprising, given that the CNOOC deal was China's largest foreign acquisition at the time, and CNOOC's

[61] Jameson Berkow, "Canada rejects $5.9-billion Petronas bid for Progress Energy," *Financial Post*, October 20, 2012.

[62] Sandra Walker, Jim Dinning, et al., "Canada," in *International Legal Developments Year in Review: 2010*, eds. Alexander A. Jeglic and Anjali Krishnamurthy (Chicago: American Bar Association's Section on International Law and Practice, 2011), 473.

[63] Dempsey, *Evolutions in Corporate Governance*, 128.

[64] Derek H. Burney and Fen Osler Hampson, *Brave New Canada: Meeting the Challenge of a Changing World* (Kingston: McGill-Queen's University Press, 2014), 145.

[65] Note: Burney and Hampson mistakenly refer to CNOOC as "China National Offshore Oil Company," when it should be China National Offshore Oil Corporation.

[66] Burney and Hampson, *Brave New Canada*, 146-7.

[67] Dempsey, *Evolutions in Corporate Governance*, 129.

[68] C. Fred Bergsten et al., *Bridging the Pacific: Toward Free Trade and Investment between China and the United States* (Washington: Peterson Institute for International Economics, 2014), 316.

[69] Note: Bergsten et al. mistakenly refer to a "Potash Company of Saskatchewan" in reference to Potash Corporation of Saskatchewan.

investment activity was also raising concerns in the United States, where it faced a United States Committee on Foreign Investment review in November 2012.[70]

As a result of the CNOOC deal, the federal government announced that it regarded the deal as an exceptional case, and that future foreign SOE acquisitions of oil sands would pass the net benefit test only in exceptional circumstances.[71] Then Prime Minister Harper also emphasized that Canada was not "for sale to foreign governments," with a former ambassador to China opining that, with China's SOE acquisitions in Canada, "the consequences go far beyond" just economic ones.[72] As well, the federal government released clarifying guidelines on SOE investment in December 2012 and May 2013.[73] In response to a perceived gap in policy surrounding SOEs not explicitly covered by the net benefit test, the December 7 *ICA* revisions to guidelines on investment reviews introduced a review threshold for SOEs of CAD $330 million.[74] [75] [76] They further stipulated that "the burden of proof is on foreign investors to demonstrate to the satisfaction of the Minister that a net benefit is likely.[77]

While it is impossible to know for certain the impacts of these statements and guidelines, given the impossibilities of proving a counterfactual within a complex investment environment, low investment in the oil sands in 2013 has been linked by some to the restrictions put in place after CNOOC.[78] Foreign investment in Canadian

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70 Persaud et al., "Canada," 559.
71 Joachim Karl, "FDI in the Energy Sector: Recent Trends and Policy Issues," in *Foreign Investment in the Energy Sector: Balancing Private and Public Interests*, eds. Eric de Brabandere and Tarcisio Gazzini (Boston: Brill Nijhoff, 2014), 16.
72 Charles Burton, "Stephen Harper's new trade rules safeguard Canada's interests," in *The Globe and Mail* (December 8, 2012).
73 Safarian, *Simplifying the Rule Book*, 11.
74 Burney and Hampson, *Brave New Canada*, 147.
75 Persaud et al., "Canada," 560.
76 Ibid., 557.
77 Bergsten et al., *Bridging the Pacific*, 317.
78 Burney and Hampson, *Brave New Canada*, 148.

resources did drop from $27 billion to $2 billion between 2012 and 2013, but the long timelines of large deals could mean that the drop was set to occur regardless of the CNOOC decision.[79] For SOE activity in the oil sands in particular, however, there is evidence that the policy did have a statistically significant effect.[80] It also has been noted that joint ventures and other minority investment activities were still far more easily available to foreign oil sands investors even after the 2013 guidelines were released.[81]

The federal government raised the threshold for review for the most common – and generally least controversial – category of investor, private WTO investors, to CAD $1 billion in June of 2017, two years ahead of schedule, which will likely reduce the number of applications facing a net benefit test.[82] Work is also underway to raise the same threshold to CAD $1.5 billion for private investors from both Canada's bilateral free trade agreement partners, and Canada's multilateral free trade partners under the Canada-European Union Comprehensive Economic and Trade Agreement, although no target date has been set as of the time of this writing.

There were 22 approvals under the net benefit test in fiscal year 2016-2017, for a total value of CAD $30 billion in approvals, and an average value of CAD $1.4 billion. Rejections under ICA do not have to be made public. These most recent year approval numbers were up from 15 approvals in both 2014-2015 and 2015-2016.[83]

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[79] Ibid., 149.

[80] Eugene Beaulieu and Matthew M. Saunders, "The Impact of Foreign Investment Restrictions on the Stock Returns of Oil Sands Companies," in *SPP Research Papers* Volume 7 Issue 16. 2014.

[81] Persaud et al., "Canada," 561.

[82] Canada. *Annual Report 2016-2017*.

[83] Canada. *Annual Report 2016-2017*.

However, recent years have also seen the Canadian government once more contend with high-profile investment cases involving China, and their national security implications in particular. The government's reversal of a 2015 decision blocking Hong Kong's O-Net Technology Group from acquiring ITF Technologies led to a bevvy of criticism, although the government was satisfied by the conditions it attached to the deal.[84] Yet, after different security concerns led to the halting of a deal involving state-owned China Communications Construction Company Ltd. acquiring Canada's Aecon Group, concerns were raised surrounding impacts on the broader Canada-China trading relationship.[85] As such, the issue of China's investment clearly remains both pressing and controversial.

Trends and Policy

The data analysis portion of this project utilizes a novel dataset constructed from existing transaction-level data compiled within the China Institute at the University of Alberta's China-Canada Investment Tracker, the Asia Pacific Foundation of Canada's Investment Monitor, and the Financial Times' fDi Insights datasets, cross-referenced with the American Enterprise Institute and the Heritage Foundation's China Global Investment Tracker and existing statistical data from Canada.

The Asia Pacific Foundation of Canada and School of Public Policy's Investment Monitor tracks Asia Pacific-Canada investment, with frequent reports published by the Asia Pacific Foundation. The Asia Pacific Foundation hosts a publicly available web

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[84] Steven Chase, "Liberal green light for Chinese takeover deal a turning point for Canada: experts," *The Globe and Mail*, 2017.

[85] CBC, "Federal government blocks sale of construction giant Aecon to Chinese interests," 2018.

portal and seeks to inform public discussion on investments across the region. With plans to expand coverage down to the city-level across the Asia Pacific, the Monitor will be the most comprehensive publicly available information for the region. The Monitor's core strengths are the ability to compare both inbound and outbound investment between Canada and the Asia Pacific, and to compare between economies. According to the Investment Monitor, China and Hong Kong's FDI stock in Canada is C$62.53 billion.

The China Institute at the University of Alberta's China-Canada Investment Tracker records, verifies, and publishes a comprehensive dataset on Chinese FDI into Canada going back as far as 1993. Publicly available data visualization tools are available for the public to learn about China's investment stock, sectoral and regional distribution, and ownership in Canada, while a more comprehensive dataset has been used by academic and government researchers. As a China-focused policy centre, the China Institute has been able to track investments not recorded anywhere else in public, English-language sources. According to the China-Canada Investment Tracker, China and Hong Kong's FDI stock in Canada is US$73 billion (C$80 billion). Limitations are primarily due to its exclusive focus on China, and thus its comprehensiveness is not directly comparable to other information. Its methodology results in zero values for any unverifiable information, as opposed to estimates, with the result being a likely understatement of total investment.

Trends of Chinese Investment in Canada

Following the merger and verification of transactions across the China Institute at the University of Alberta's China-Canada Investment Tracker, the Asia Pacific

Foundation of Canada's Investment Monitor, and the Financial Times' fDi Insights datasets, the total for tracked Chinese outward foreign direct investment into Canada totalled C$84.610 billion (US$76.958 billion) by way of 783 transactions for the period 1993 through 2017.[86] [87] [88] [89]

Over the past quarter century, the value of annual flows of Chinese OFDI into Canada has generally shifted from a period of slow increases from relatively small investment values up until 2009, largely indicative of China's slow but substantial emergence on the international economic stage. This was then followed by three years of much higher investment flows during the Global Recession and across the 2010 through 2012 period. A peak in 2013, almost entirely driven by the one, energy-driven investment by CNOOC into Nexen, was followed by two years of much smaller investment flows. Recently, there has been a return to higher investment flows in 2016 and 2017, possibly reflecting a new wave of investment driven by shifts in China's domestic policies and investment targets.

The number of deals per year presents a similar story, with few investments in 1993 through 2004, followed by increases from 2005 through 2010, and then a plateau in number of deals across 2011 through 2013. The period 2013 through 2015 saw a return to increasing numbers of deals, with 2016 and 2017 the two most voluminous years to date.

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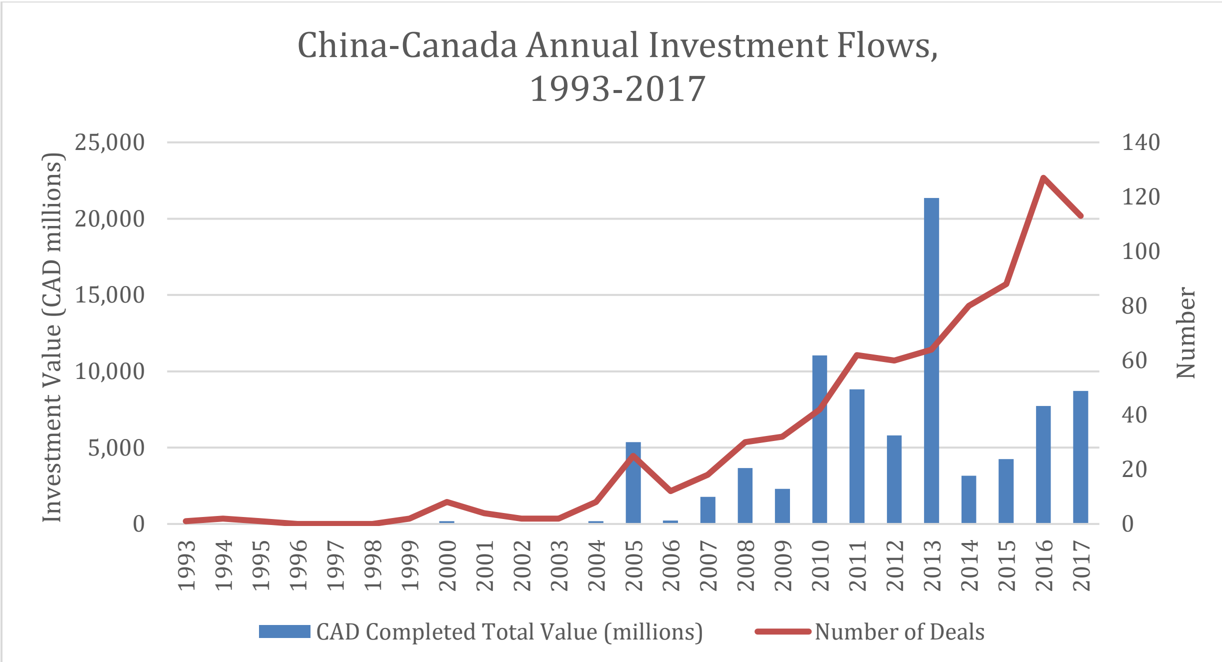
[86] Currency conversions calculated for the date of deal closing or greenfield project groundbreaking.

[87] China Institute, *Canada-China Investment Tracker*, University of Alberta. 2018.

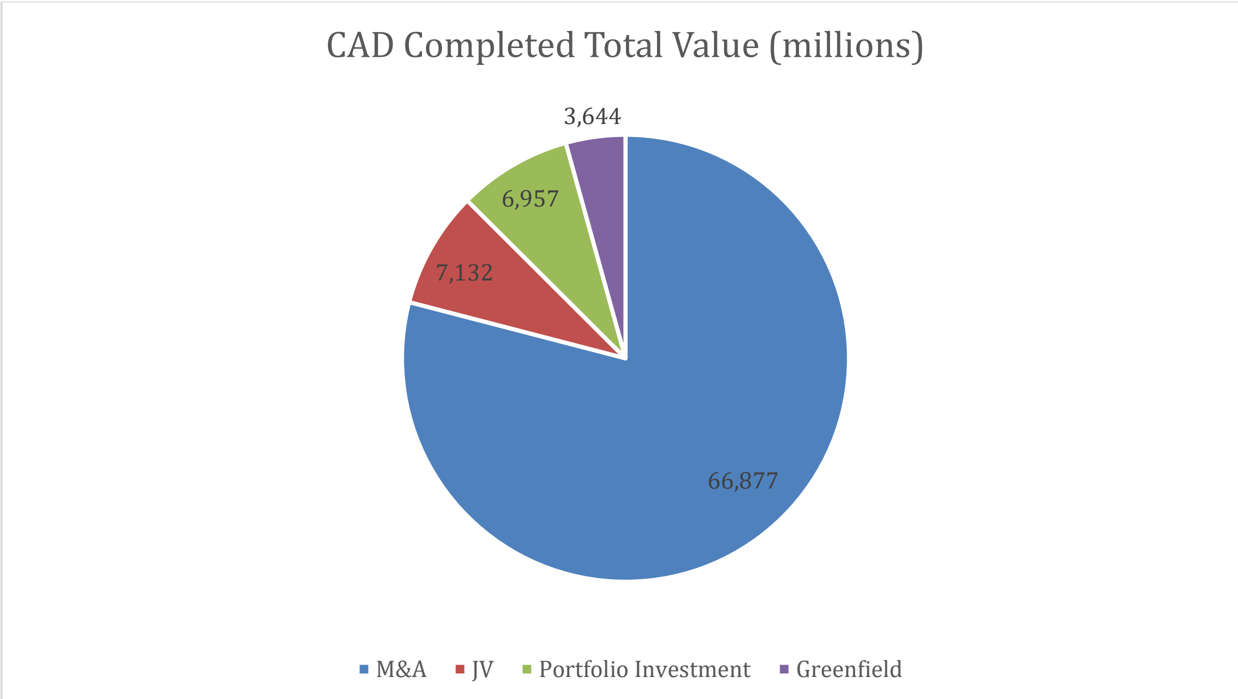
[88] Asia-Pacific Foundation of Canada, *Investment Monitor*, 2018.

[89] Financial Times, *fDi Insights*, 2017.

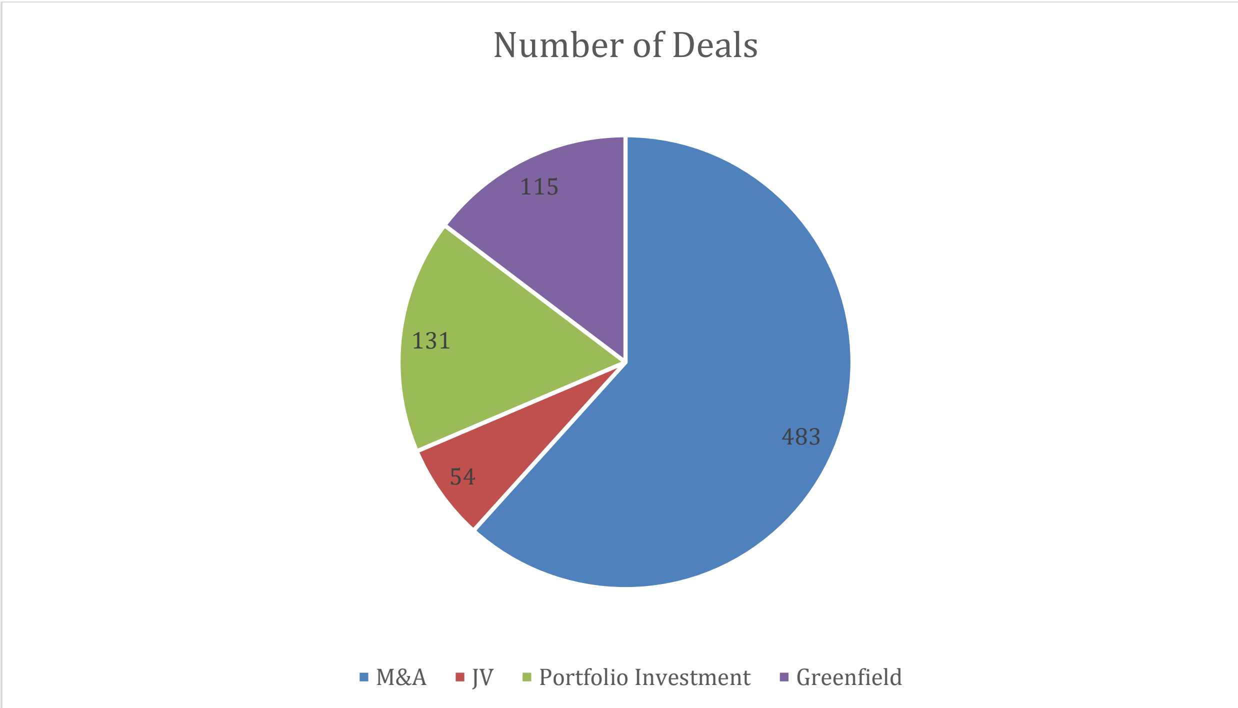


Source: Dataset constructed from China Institute, Asia Pacific Foundation, and fDi Markets data

A focus on just the past decade illustrates that while the annual flow of investment increased fourfold between 2007 and 2017, the intervening years have seen marked changes, including four years with investment flows higher than 2017's. A more apparent trend amidst these changes is the number of transactions occurring, with transaction numbers six times higher in 2017 than a decade prior, and rising between all but two years.

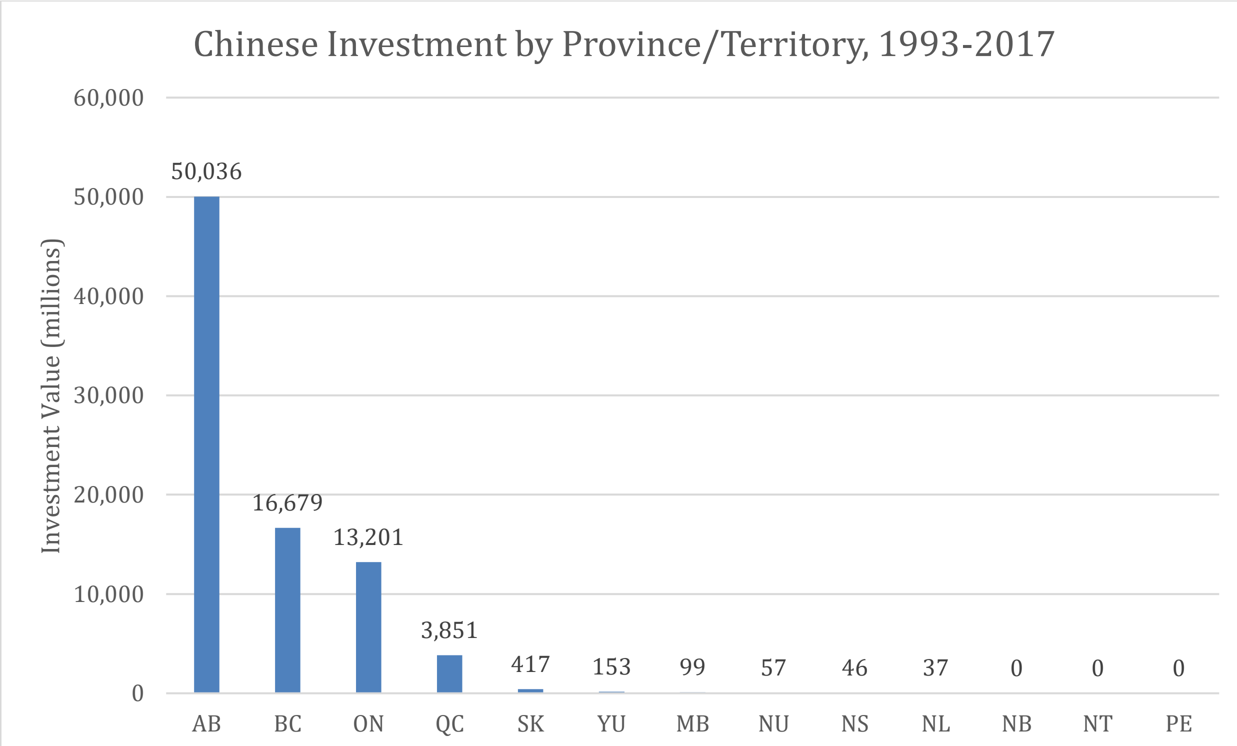


In terms of ownership, over four fifths of the dollar value of Chinese investment stock in Canada by the end of 2017 is via merger and acquisition (M&A) transactions. The share of merger and acquisitions, or M&As, in the transaction numbers is somewhat smaller than its share of dollar value, yet it still comprises two thirds. Nearly one fifth is via portfolio investment.

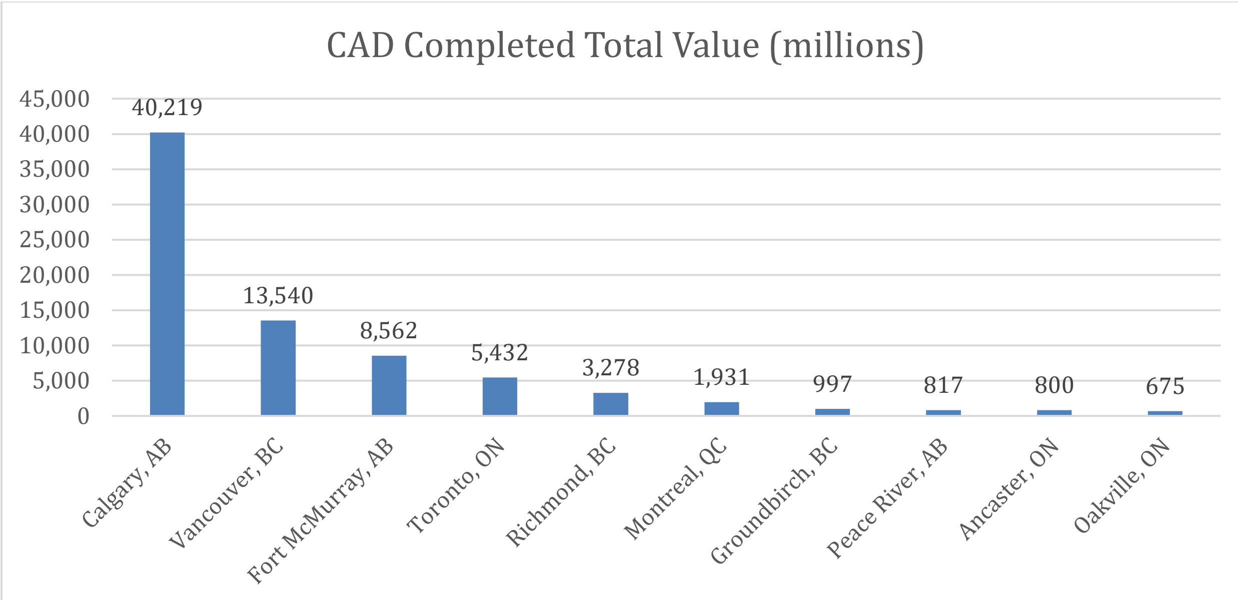


Across the past 25 years, M&A is dominant in terms of both annual dollar flows and transaction numbers. Recent mid-decade increases in activity among portfolio and greenfield investment were still eclipsed by the increases seen in M&A. Note that 2010 was the only year since 2004 where recorded M&A investment value did not make up the majority of investment value, due to the especially large portfolio investment by China Petrochemical Corp into Syncrude, as well as the similarly large joint venture involving China National Petroleum Corp in the MacKay River and Dover oil sands projects.

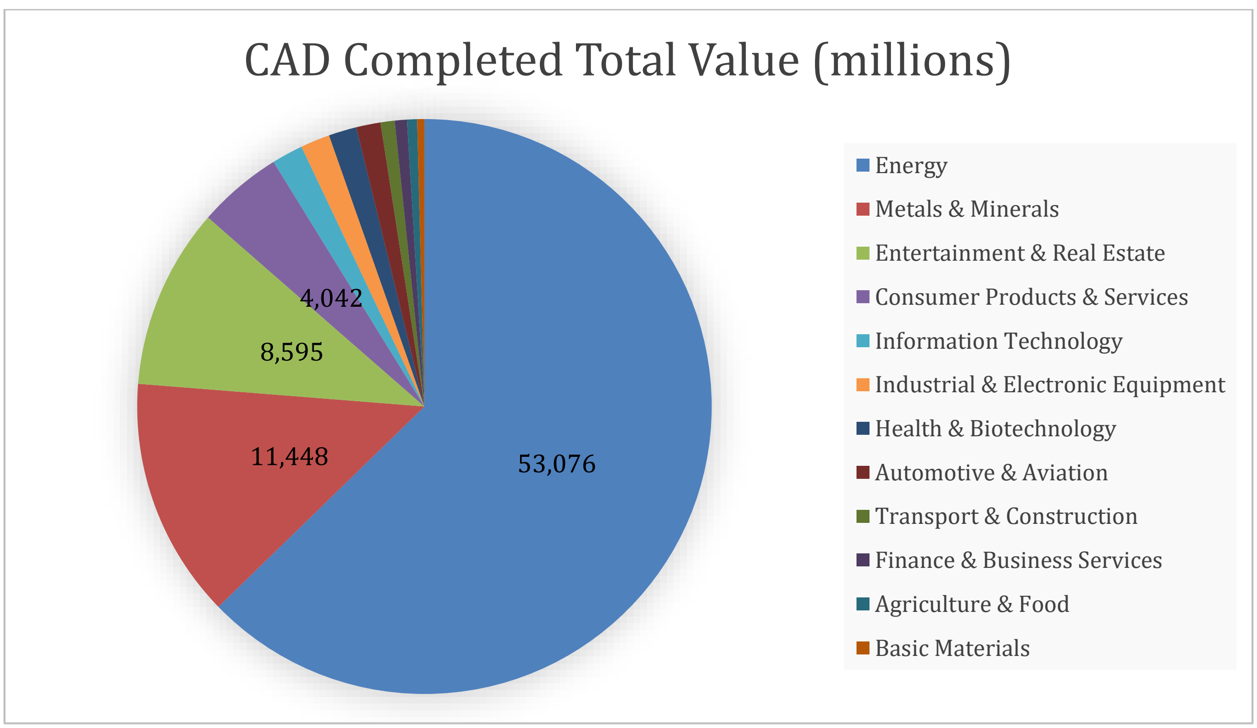
While provincial- and territorial-level investment data exists, caution should be used when interpreting the exact amounts invested. Still, they offer some information on the relative amounts of investment across jurisdictions. Alberta has received the lion's share of Chinese investment over the past quarter century, followed by British Columbia and Ontario, with Quebec and Saskatchewan also receiving substantial investment.



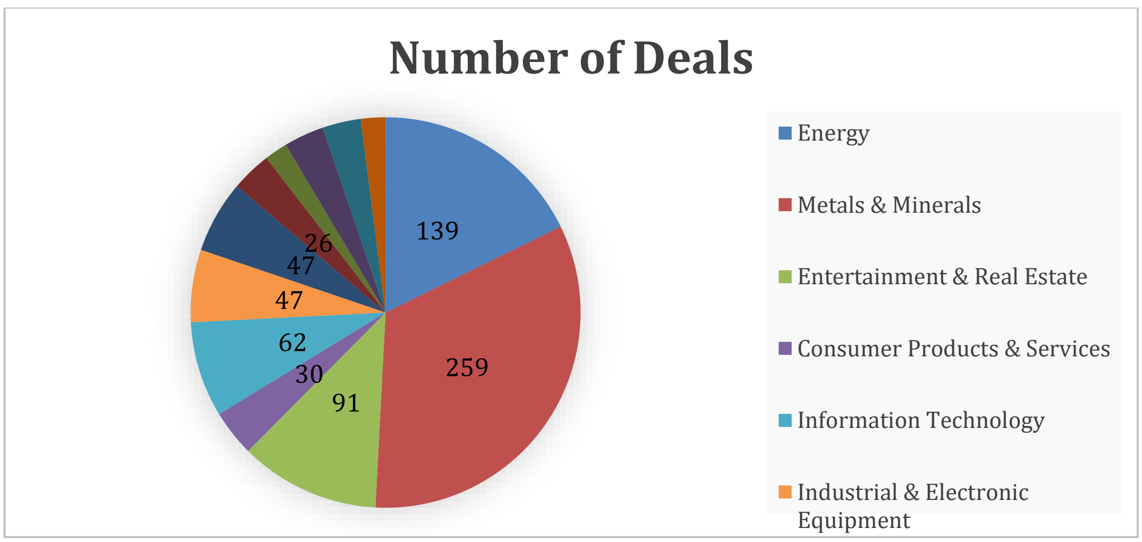
As numerous resource-based firms are headquartered in Calgary and Vancouver, it is unsurprising to see these two locations as having received the largest volume of investment value. Fort McMurray receiving nearly double the amount of Toronto further highlights the influence of resource investment. Several locations are notable due to their placement relative to their population size: generally, these locations have been the target of one, large investment, as is the case with Groundbirch, BC, which saw China National Petroleum Corp acquire the Groundbirch Shale-Gas Project.



The bulk of the dollar value invested into Canada by China between 1993 through 2017 is in the energy sector, a recipient of nearly two thirds of total Chinese OFDI into Canada.



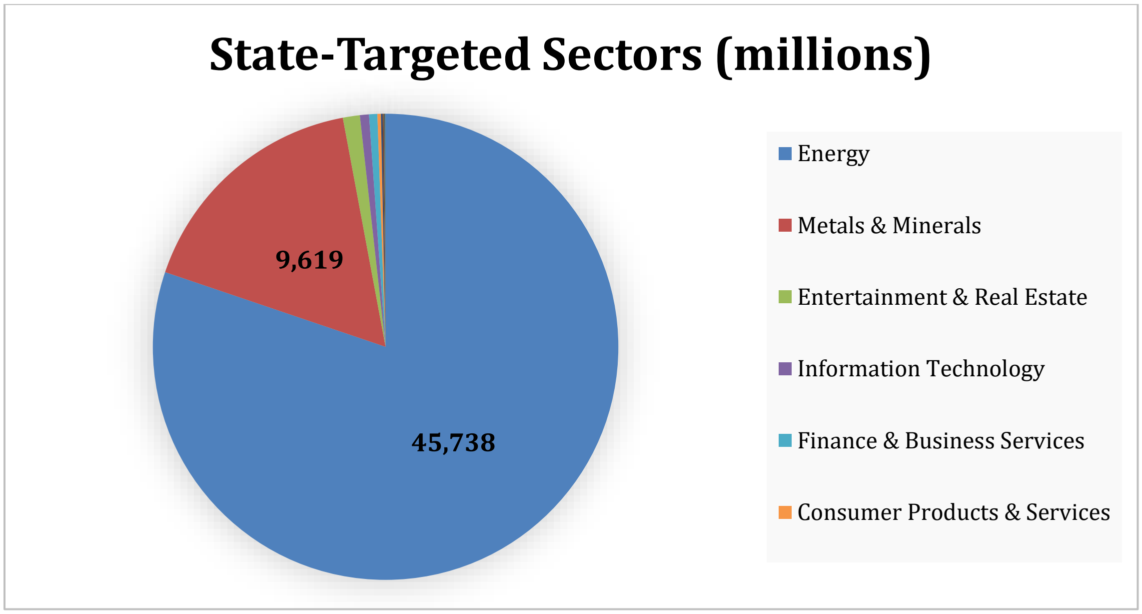
However, when breaking down the number of transactions by sector, it becomes apparent that these investments into energy are relatively large, as fewer than one in five transactions have been into energy. Meanwhile, over a third of the transaction activity in this period was into the metals and minerals sector. Even so, both deal values and transaction numbers should be taken as significant metrics for discussion, as policy-makers should be cognizant of why these sectors are being selected. Within Canada, there is evidence to indicate that China's SOEs select Canadian sectors within which Canada offers some comparative advantage with respect to China and alternative investment destinations – this in turn implies that, in China's eyes, Canada's resource sectors have been this country's comparative advantage.[90]



Notably, of the C$57 billion in China's investment by SOEs, C$55 billion has been in two natural resource sectors: C$46 billion in energy, and C$10 billion in metals and minerals. Aforementioned concerns to do with direct state-owned enterprise involvement, then, should be considered in light of this sectoral distribution: clearly,

[90] Dobson, 2014.

state-ownership is biased towards certain industries, and should not be taken to be the norm across all sectors.



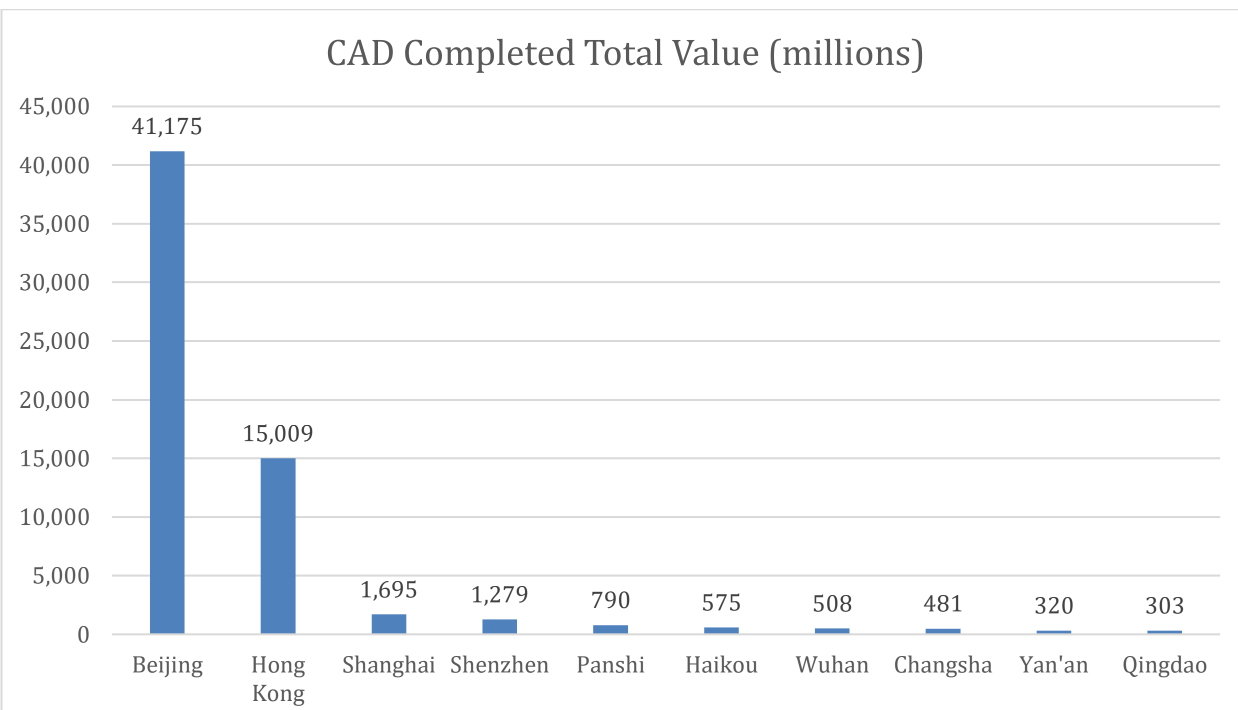
State-Owned Dollar Share of China's Investment by Sector

Sector	State-Owned Share
Energy	87%
Metals & Minerals	86%
Finance & Business Services	59%
Information Technology	24%
Basic Materials	19%
Entertainment & Real Estate	10%
Transport & Construction	6%
Agriculture & Food	6%
Consumer Products & Services	3%
Health & Biotechnology	3%
Automotive & Aviation	2%
Industrial & Electronic Equipment	0%

However, concerns also consist with respect to the concentration of investment in one sector – in other words, the amount of activity by China which is state-owned, regardless of the total value in the sector. When this is assessed, the energy, metals and minerals, and finance and business service sectors all have a majority of China's investment activity driven by SOEs.

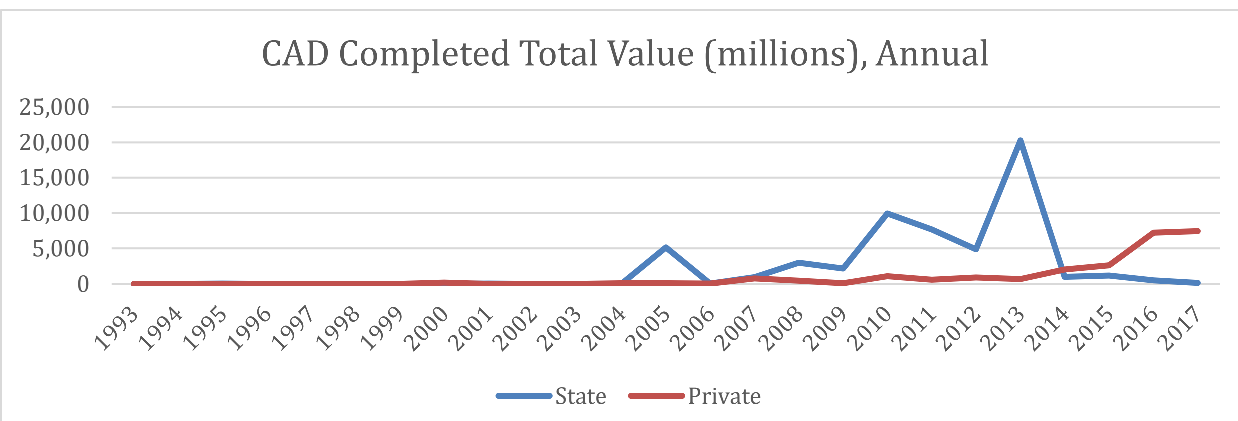
Transaction data also reveals that China's investments have both historically and recently led to controlling stakes: the average stake acquired between 1993 through 2017 was 55.47%, a figure that drops slightly to 55.27% for the period 2013 through 2017.

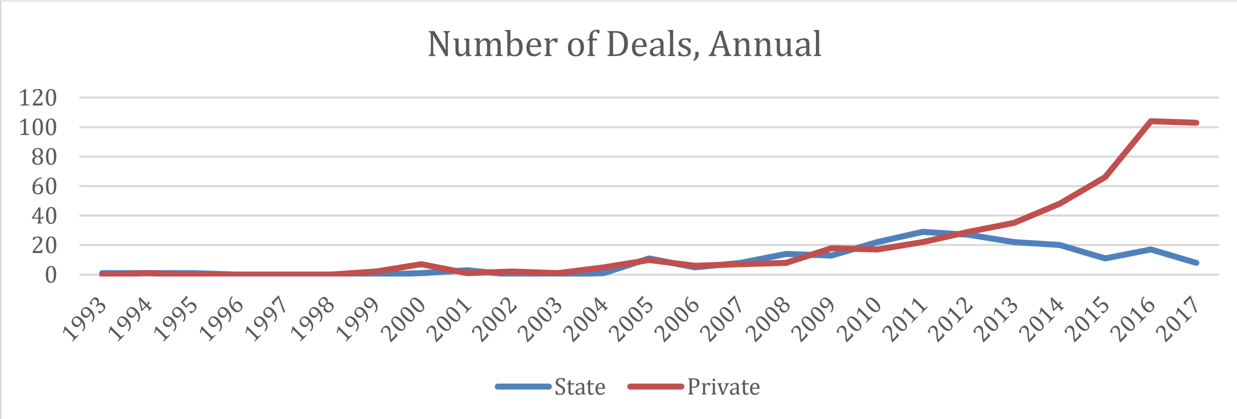
The top source cities for acquirers are Beijing, Hong Kong, and Shanghai; while the latter two are viewed as China's major financial centres, it is evident that the country's capital is vastly more significant for investments in Canada, making up approximately half of China's investment stock. While not a direct indicator of state-involvement, the large number of Beijing-sourced transactions is reflective of its role as the host city for most of China's national-level state-owned enterprises.



While concerns surrounding SOE investment has dominated most discussion regarding China's OFDI into Canada, the record over the past 25 years illustrates that both SOE and private investors have played significant roles. The volume of state-owned investment remained relatively low between 1993 and 2004, with slightly higher annual flows in the 2005 through 2009 period leading to a drop across the 2010 through 2012 period. Following 2013's peak, nearly entirely due to state-owned China National Offshore Oil Corp's purchase of Nexen, state-owned investment has remained remarkably low.

Nominally private investment dollar value flows also remained low between 1993 through 2009, rising in 2010 before dropping to a slightly lower range for the years 2011 through 2013. The years 2014 and 2015 saw an uptick in annual flows of investment value to the point where private investment flows overtook state-owned ones, with 2016 and 2017 the two highest years to date for private investment.





This private investment trend is notable, as it contradicts two generally held beliefs on the current state of investment in Canada. First, China's private investment has for several years been larger than its state-owned investment in terms of both deal values and deal numbers, contrary to popular perceptions of a purely state-owned investment drive. Again, it is crucial to note the degree to which the Chinese state can influence its private firms, too, and this certainly cannot be ignored. Even recognizing this, however, it is evident that this private investment now plays a larger role than directly state-controlled investment, providing opportunities for a potentially less-sensitive bilateral investment relationship moving forward.

Second, private investment from China is rising at a time when there is growing concern over Canada's ability to attract international investment from any source, a significant outlier given the potential pool of private capital which China could provide.[91] While China should not be construed as a panacea for all of Canada's FDI attractiveness ills, it could offset some of the lowered growth stemming from Canada's declining FDI attractiveness; perhaps more importantly, this form of investor presents a

[91] Conference Board of Canada, "Inward FDI Attraction." Ottawa, 2018.

useful case study of a success within relatively turbulent economic times, and should at least be drawn upon when examining broader investment policy options.

Policy Discussion

As demonstrated above, the scale of China's investment in Canada is significant, and any policy responses must acknowledge that there are benefits associated with this investment. Thus, it follows that the net benefit test itself should be re-examined, to ensure that it captures as many benefits as possible, and in manner which inspires the trust of both the general public and potential investors.

Enhancements to the test can be devised to create clearer criteria through explicit metrics and a transparent process through the *Investment Canada Act*, the Investment Canada Regulations, guidelines, and interpretation notes. With respect to amending *ICA*'s net benefit test provisions, the current text is primarily concerned with the process of review. Amendments which increase the review process' transparency could be added, so that future applicants may best interpret the test based on past precedent. Given section 36's treatment of "all information" on applications and approvals as privileged, there is room for improvement.[92] As a model, the *Special Import Measures Act* (*SIMA*) also legislates on federal review of foreign business and confidentiality, with *SIMA* section 85 disaggregating between confidential and non-confidential information.[93] The Canada Border Services Agency, which administers *SIMA*, discloses review information "in order that all parties can understand the reasons

[92] *Investment Canada Act*, RSC 1985, c 28, s 36
[93] Special Import Measures Act, RSC 1985, c S-15, s 85

and bases of fact on which decisions are made, while guaranteeing the protection of confidential information."[94]

The introduction of published metrics can be accomplished through utilizing sections 35 and 38 of *ICA* to issue and publish regulations, guidelines, and interpretation notes.[95] In practice, the Investment Canada Regulations contain procedural information and expanded paragraphs defining variables for calculations for non-Canadian applicants.[96] This could be expanded to include metrics for section 20 of *ICA*.

ICA guidelines describe obligations and requirements to applicants; these could be expanded to include more exhaustive descriptions on section 20 criteria. Interpretation notes handle terminology, and could be expanded to include definitions for section 20 criteria, including metrics for measurement when applicable. This is not without precedent: state-owned enterprises (SOEs) were given additional guidelines on criteria surrounding the net benefit test in 2007.[97] As Cabinet creates ICA regulations and the Minister composes guidelines and interpretation notes, there is still room for Ministerial and Cabinet discretion; however, publishing the criteria used to assess net benefit would lessen concerns over political interference.

A third option exists via a recently used mechanism: amending ICA's thresholds for review to the point where their application is nullified. Earlier this year, two acts received royal assent, raising thresholds through amendments to sections 14.1 through

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[94] Canada. Canada Border Services Agency, *Statement of Administrative Practices for the Special Import Measures Act* (Ottawa: Canada Border Services Agency, 2017).

[95] Investment Canada Act, RSC 1985, c 28, s 35, s 38

[96] Canada. *Investment Canada Regulations* (Ottawa: 2017).

[97] Canada. Industry Canada, *Guidelines – Investment by state-owned enterprises – Net benefit assessment* (Ottawa: Industry Canada, 2007).

14.3.[98] [99] The threshold for review for non-SOE World Trade Organization investors was raised from $800 million to $1 billion, and will be adjusted annually to reflect GDP; a new threshold for select free trade agreement investors were set at $1.5 billion.[100] [101] [102] While data is limited to approved applications, the average value of applications in 2016-17 was $1.38 billion; thus, there is evidence that new thresholds could result in lower demand for review.[103]

Aside from explicit benefits, Canada should also recognize the potential opportunities that China's investment could provide. The sectoral and regional breakdown of investment presented above presents one potential road-map for policy-makers to identify opportunities for investment promotion activities. Aside from assessments within Canada, opportunities-tracking should also compare Canadian competitiveness to the policies of comparable investment destinations, many of which present higher barriers to China's investment.[104]

However, tightened restrictions on China's investment by other investment destination jurisdictions should also be indicative of the risks, real and perceived, of China's outbound investment. Just as Canada needs to assess its competitiveness against other jurisdictions, and look for potential investment promotion opportunities within Canada, there is also scope to learn from other investment recipient jurisdictions

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[98] Canada-European Union Comprehensive Economic and Trade Agreement Implementation Act, SC 2017, c 6, s 80

[99] Budget Implementation Act, 2017, No. 1, SC 2017, c 20, s 192

[100] Canada. Innovation, Science, and Economic Development Canada, *Annual Report 2016-2017* (Ottawa: Innovation, Science and Economic Development Canada, 2017).

[101] Canada-European Union Comprehensive Economic and Trade Agreement Implementation Act, SC 2017, c 6, s 80

[102] Budget Implementation Act, 2017, No. 1, SC 2017, c 20, s 192

[103] Canada. Innovation, Science and Economic Development Canada, *Annual Report 2016-2017* (Ottawa: Innovation, Science and Economic Development Canada, 2017).

[104] Don Weinland, "Chinese state tech investors face higher US barriers," *Financial Times* (2018).

and from previous Canadian policies. While the Canada-China Foreign Investment Protection Agreement is only three years old, there is still a case to reassess what future trends in investment Canada expects to see, and what it would seek to encourage and discourage. Doing so would be especially relevant in the lead up to any free trade agreement discussions, a topic which continues to be raised by officials on both sides.[105]

Additionally, sectoral breakdowns and other, metric-based breakdowns of China's investment which disaggregate SOE activity from the rest provide another tool for risk assessment. While protecting so-called 'national champions' of industry is not without its consequences, attempts to at least mitigate perceived negative impacts in such sectors as energy or metals and minerals could be presented in response to the sectors' higher state-owned attention. The apparent lack of comparative advantage in many other sectors, at least in the eyes of China's SOEs, means that risk avoidance efforts could be more effectively targeted along sectoral lines.

Further research should also be conducted to accurately capture and model any costs of China's investment on Canada. Tracking transaction-level investment flows remains critical to Canada's understanding of the nature of this investment, but it needs to be complemented with other impact assessments. Evidence-based, clear-headed discussions on contentious investment may only be resolved with accurate and timely reporting of other metrics associated with investment, be they on Canadian business, labour, the environment, and so on. Only then can policy-makers ensure that any

[105] Naomi Powell, "China says it's 'always ready' to restart free trade talks with Canada," *Financial Post* (August 20, 2018).

adjustments to the Canadian system will retain the confidence of Canada's public and of the international investment community.

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