Survival of the Fittest: A Study of the Effects of Chinese Entrepreneurship in Kenya

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# Abstract

The increasing presence of Chinese players in the Kenyan market is indisputable. Their motivations, business acumen and how that impact on the market has raised debate in various pockets of international business scholars, observers and students (citations required). This paper applies the internationalisation of firm theory, to locate the real and actual effects of the burgeoning Chinese entrepreneurs in Kenya. Using ethnographic interviews of a significant number of Kenyan entrepreneurs the Kenyan players overwhelmingly contend that as a result of hyper competition imposed on their businesses by cheap and low quality alternatives (mainly from China), they are facing business extinction and a case of survival for the fittest.

# Introduction

The number of Chinese living in many parts of Africa has increased to almost 1 million and the number of Chinese corporations doing business in Africa has increased to over 2000 ([Wenping 2012](#_ENREF_43)). Analogously, the number of Africans going to China has surged at a rate of 30-40% annually and it is believed that there are 200,000 Africans in Guangzhou alone ([Wenping 2012](#_ENREF_43)). Based on their mutual history of suffering from colonial invasion and desire for development, Sino-Africa relationship has experienced various development phases in the last 60 years, from infrastructure construction to full development ([Taylor 2009](#_ENREF_41); [Wenping 2012](#_ENREF_43)).

At the same time, economic engagement between China and Sub Saharan Africa continue to deepen and according to [Caulderwood (2014](#_ENREF_12)), trade between these regions is projected to continuously experience significant annual growth. Importantly, in recent years, China motivated by natural resource needs for continued domestic economic development and through state owned corporations, has made significant investments in Sub Saharan Africa ([Alden 2007](#_ENREF_2); [Alves 2013](#_ENREF_5); [Brautigam 2009](#_ENREF_6); [Carmody 2011](#_ENREF_8); [Carmody & Taylor 2011](#_ENREF_11); [Sautman & Hairong 2008](#_ENREF_37); [Segal 1992](#_ENREF_38); [Shinn & Eisenman 2012](#_ENREF_39)). Moreover, according to [Broadman (2013, p. 1)](#_ENREF_7):

*“China’s investments in Africa have become diversified in recent years. While oil and mining remain an important focus, Chinese foreign direct investment (FDI) has flooded into everything from shoe manufacturing to food processing. Chinese firms have also made major investments in Africa infrastructure, targeting key sectors such as telecommunications, transport, construction, power plants, waste disposal and refurbishment. Given the scale of Africa’s infrastructure deficit, these investments represent a vital contribution to the continent’s development”.*

This diversification has seen individual Chinese working on behalf of their corporations, and engage in entrepreneurial activities across numerous cities in Sub Saharan Africa ([Kaplinsky & Morris 2011](#_ENREF_20); [Zafar 2007](#_ENREF_44)). The importance of exploring the effect of such entrepreneurial activities to the domestic market, price stability and quality of products has become apparent. This paper looks at the impact of such engagement to the strength, position and sustainability of local players with similar undertakings. Rather than focus on the entire Sub Saharan Africa region, this study narrows the scope down to Kenya.

The structure of the paper is as follows: a brief literature review, followed by an illumination of the theory that informs the benefits of a firm’s internationalisation. Thereafter, a brief methodology will be highlighted, followed by the discussion of the findings. This paper will conclude by re-enforcing the importance of the voice of local businessmen calling for help to better manage the unprecedented competition imposed on their small to medium business by the Chinese actors.

# Literature Review

China officially established diplomatic relations with Kenya in 1963 and since that time, almost 50 Chinese companies have invested in more than 96 projects, estimated to be valued at USD 400 million ([Mbendi 2013](#_ENREF_29)). These companies include the Chinese electronic company that set up a television assembly factory in Kenya with USD11.7 million worth of investment. This facility has the capacity to assemble 800 television sets per day and employs 52 people ([Mbendi 2013](#_ENREF_29)). Other companies are Huawei Technologies which has signed a contract with the Kenyan Government for the Kenya Rural Telecommunications Development Project ([Mbendi 2013](#_ENREF_29)), and Chinese automobile manufacturers who teamed up with Trans Africa to market vehicles in Kenya. In 2005, China signed an agreement with Kenya to boost the coffee trade while at the same time undertaking to help Kenya to curb imports of counterfeit goods from China ([Mbendi 2013](#_ENREF_29)). At the same time trade between Kenya and China remains unfavourable and unbalanced, with Kenyan exports to China standing at USD 50 million while Chinese exports to Kenya stand at USD 3.2 Billion ([Kimani 2014](#_ENREF_21)).

By May 2014, the Chinese and Kenyan government signed further trade, infrastructure and joint co-operation agreements ([Kimani 2014](#_ENREF_21)) while at the same time arranging to finance infrastructure development, agriculture and wildlife conservation projects. During these negotiations the Chinese Prime Minister Li Keqiang pledged USD 10 million in additional aid to Kenya ([Kimani 2014](#_ENREF_21)) for a standard gauge railways line worth Kenya Shillings 327 billion in USD? ([Masinde 2013](#_ENREF_28); [Olick 2014](#_ENREF_33)). This railway line is intended from Mombasa on the Kenyan coast to Uganda, Rwanda and South Sudan and is billed as one of the largest infrastructure projects ever to be seen in the East Africa region ([Masinde 2013](#_ENREF_28); [Olick 2014](#_ENREF_33)). According to [Mukoya (2014](#_ENREF_31)), the new standard gauge railway will supplement and eventually replace the current old, restricted and slower narrow gauge line that now runs only to Uganda. The project is seen as part of the Chinese effort to reduce the costs of trade between east African countries, which have traditionally relied on an unreliable road network and colonial era narrow gauge railways ([Mukoya 2014](#_ENREF_31)). At the same time, the Chinese company that has been designated to complete this projects - China Roads and Bridge Corporation (a subsidiary of China Communication Construction) has not only been blacklisted by The World Bank but has also been the subject of widespread concerns in Kenyan circles that the tendering process was neither competitive nor open ([Mukoya 2014](#_ENREF_31)).

In addition, China’s Jiangxi International won a tender to develop National Social Security Fund (NSSF)’s shopping mall in Nairobi, billed as the tallest real estate project in Kenya, while other Chinese corporations were busy enhancing efficiencies at Kenyan port of Mombasa ([Masinde 2013](#_ENREF_28); [Oketch & Mwahanga 2013](#_ENREF_32)). At the same time, other Chinese firms were contracted to construct power lines for Kenya Electricity and Energy Transmission between Rabai and Lamu, through Malindi and Garsen ([Oketch & Mwahanga 2013](#_ENREF_32)). Moreover, Chinese archaeologists have been engaged in excavations at Lamu and Malindi to retrieve ancient sunken ships in an attempt to rediscover the connection between the Kenyan coast and China during antiquity ([Oketch & Mwahanga 2013](#_ENREF_32)). The issue of greatest concern to Kenyans was that almost all of the above projects utilised Chinese rather than Kenyan expertise and labour (Oketch & Mwahanga 2013).

While the above development is taking root, Kenya’s foreign debt has continued to grow and in 2013 was in excess of 50 per cent of the country’s Gross Development Funding (GDP), a level at which experts suggest a country should question the sustainability of such a burden ([Masinde 2013](#_ENREF_28)). Moreover, the Kenyan Government already faces a major challenge in financing domestic debt, which currently stands at more than USD1 billion ([Masinde 2013](#_ENREF_28)), with the cumulative interest and other charges on this debt rising to USD10.17 billion by May 2013, compared to USD7.42 billion over a similar period in 2012 ([Masinde 2013](#_ENREF_28)). Sadly, in the same period, Kenya’s debt to China has grown exponentially and with the additional USD5 billion (for standard gauge railway) made available by China, the net debt owed to China is almost USD50 billion ([Masinde 2013](#_ENREF_28)).

It has been suggested that one of the ways in which Kenya might be able to repay Chinese loans and grants would be to allow China to have unlimited access of Kenya natural resources ([Luesby 2013](#_ENREF_27)). Kenya has resources far greater than oil and gas, including significant deposits of rare earths metals ([Luesby 2013](#_ENREF_27)) used extensively in mobile phones, and modern light bulbs. China secured more than 95 per cent of the world’s rare earth supplies ([Luesby 2013](#_ENREF_27)), which strongly suggests that China views its infrastructure developments as a means to access African resources ([Alden & Alves 2010](#_ENREF_3); [Alves 2010](#_ENREF_4), [2013](#_ENREF_5)), with the infrastructure developments in Kenya aimed at accessing rare earth deposits ([Luesby 2013](#_ENREF_27)). Detailed figures estimate that these deposits are worth USD95 billion ([Luesby 2013](#_ENREF_27)) and may be the largest single resource available to the country. For this reason it may be in Kenya’s interest to secure these resources from outsiders.

Besides the allure of infrastructure and resources engagement between China and Kenya, is the reality of Chinese entrepreneurs playing their everyday merchandise and trade in most Kenyan Cities. The effect of this trade to the Kenyan market and players is the focus of this paper. However, the context of Chinese entrepreneurs engagement in Kenya is illuminated by foreign direct investment (FDI) and its benefit to the host nation.

# FDI Theory

According to [Ozawa (1992, p. 6)](#_ENREF_34), the role of firms in the context of international investment should be that of creators and traders of tangible asserts with the firms themselves constituting major generators and disseminators of technology, skills and market demand channels, moderated by competition. Moreover, FDI (foreign direct investment) theory suggests that firms will behave in a particular way when competing for international resources. Thus [Hymer (1976](#_ENREF_18)) (as cited by [Ozawa (1992, p. 6)](#_ENREF_34) concludes that:

“*FDI draws on the role of firms as creators and exploiters of intangible corporate assets”*.

Also, in the effort to appreciate Kojima’s contribution to the growth of FDI theory, [Dunning (1988, p. 9)](#_ENREF_15), argues that:

“*The theory of international firm views multinational enterprises (MNE) as instruments by which the comparative trading advantage of a nation state may better be advanced*”.

Kojima also suggested that a home country should invest abroad in sectors that require intermediate (but internationally mobile) products that the country is well suited to supply but that this needs to be combined with non-transferrable inputs with which the host country is well endowed. Hence, FDI acts both as a catalyst to trade and as arbitrage for improving the international allocation of economies ([Dunning 1988, p. 10](#_ENREF_15)). Furthermore, Kojima as quoted in [Ozawa (1992, p. 6)](#_ENREF_34) also defines the role of FDI as:

*“To transplant production technology through training of labour management and marketing, from the advanced industrial country to lesser developed countries and therefore, acting as the starter and the tutor of industrialization in less developed countries”.*

This however assumes that firms are independent of their national states, an approach negated by the active role played by the Chinese government in supports of its corporations through financial subsidies and overall ownership and does not accurately portray the role of Chinese state owned enterprises investing in Sub Saharan Africa ([Alden 2005](#_ENREF_1); [Carmody 2011](#_ENREF_8), [2013](#_ENREF_9); [Carmody, Hampwaye & Sakala 2012](#_ENREF_10); [Carmody & Taylor 2011](#_ENREF_11); [Taylor 2008](#_ENREF_40); [Zafar 2007](#_ENREF_44)).

## Host Country Benefits of Inward FDI

Developing and nations in transition have liberalised their FDI regimes and have adopted policies favourable to foreign investments. This is in part because FDI can make positive contributions to the host economies by making available much required capital ([Kurtishi 2013](#_ENREF_26)). Also, multinational corporations take risks by investing in long term projects, and repatriate profits only when the projects yield the desired returns ([Kurtishi 2013](#_ENREF_26)). By virtue of their large sizes, strong reputation and huge financial muscle, many Multi National Corporations (MNC) have access to financial resources that are not available to firms in the host country. Such strong capital positions enable a firm to seek out the highest rate of return ([Kurtishi 2013](#_ENREF_26)). On the other hand, according to [Feldstein (2000](#_ENREF_16)), international flows of capital reduce the risk faced by investors and allow them to diversify their lending and investment. In addition, internationalisation has also promoted the integration of capital markets which has led to spillovers of best practices of corporate governance, legal traditions and accounting practices ([Feldstein 2000](#_ENREF_16)). FDI has also enhanced technological transfer to host countries, which has helped propel economic growth and industrialisation in these developing countries ([Kurtishi 2013](#_ENREF_26)). Due to the fact that most developing countries do not have R&D resources required to develop their own local products and process technology, most multinational corporations have filled this gap resulting in increased industrialisation and economic growth ([Kurtishi 2013](#_ENREF_26)). Importantly, technologies transferred tend to be modern and more environmentally friendly ([Kurtishi 2013](#_ENREF_26)). In light of this, this paper proposes the following proposition:

**Proposition 1:** *FDI in host country deposits spillovers such as: technology, skills, R&D and industrialisation*

Another benefit of FDI is its ability to promote the transfer of knowledge to host countries through labour training, new managerial and organisational practices and skills transfer. Additionally, local personnel are often trained to take up managerial, operational, financial and technical posts in the subsidiaries of foreign MNCs ([Feldstein 2000](#_ENREF_16)). In addition, training by foreign firms is of higher quality given they are potentially the most productive firms and hence, the entrepreneurial capabilities of the local personnel are also heightened as they seek out for investment opportunities locally ([Kurtishi 2013](#_ENREF_26)). In host nations, mostly developing countries, FDI is also associated with employment either directly or indirectly. In most of these nations, financial capital is relatively limited but labour is available in large supply; so the creation of employment comes as an opportunity ([Jordin & Vahlne 1981](#_ENREF_19)). The benefits are realised directly when an MNC absorbs and employs individuals from the host country, while indirectly, jobs are created in both the local supply chain system and the economy due to the rise in public spending ([Jordin & Vahlne 1981](#_ENREF_19)). Also, FDI affects the host country’s balance of payment account when MNCs establish subsidiaries. This reflects positively in the capital account of the host country. Moreover, in instances where FDI replaces imports of goods or services, the host nation’s current account is substantially improved ([Kurtishi 2013](#_ENREF_26)). Importantly, the host nation’s balance of payment accounts is improved when a subsidiary firm in a foreign country (host country) produces goods for export to other countries ([Vernon 1966](#_ENREF_42)). Therefore, this paper proposes the following proposition:

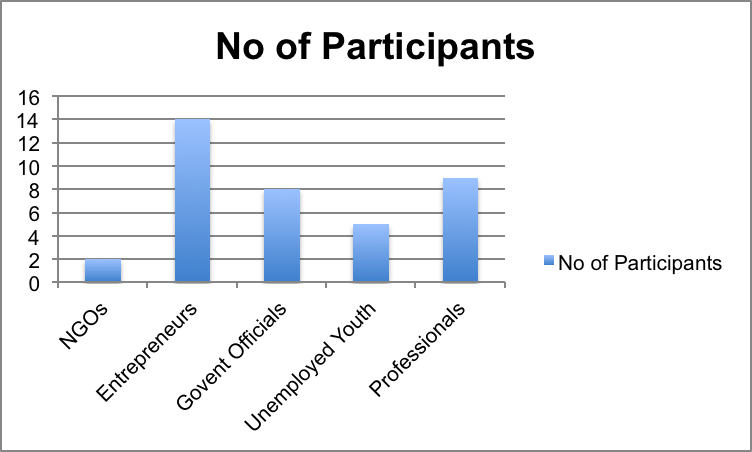
**Proposition 2:** *Entrepreneurial capabilities of the local personnel are heightened and hence seek out for more local investment opportunities.*

In summary,internationalisation has made it possible for MNCs to operate freely. To reap the maximum benefits from FDI, countries have made efforts to create healthy and enabling environments for foreign investors. The net benefits of FDI take time to accrue and may differ from one country to another, and the type of MNC may also influence the benefits to both home and the host country. The benefits of FDI to the host country include transfer of technology, skills, R&D and industrialisation. Also, FDI also provides employment opportunities to people in management positions and enables them to share knowledge with personnel in the host country ([Morgan 1997](#_ENREF_30)).

# Methodology – Discursive Interviews

Discursive interviews were conducted with 76 participants across various economic sectors in Kenya. The sectors (broken down in figure 1) include: financial, small to medium entrepreneurs, academics, bankers, journalists, government of Kenya representatives, construction, unemployed youth, NGO representatives, retail and manufacturing.

**Figure 1. Breakdown of Discursive Interview Participants (this Figure needs to go at the end and it is not clear. This needs to be at least 1/3 of a page)**



*Source: Okumu (2016) – Unpublished Thesis*

***Note:*** *NGOs participants are projects managers, one from Mombasa (female) and the other from Nairobi (male). Entrepreneurs are all CEOs of various SMEs in Nairobi – 6famele and 8male. Government of Kenya officials are the third tier and head of departments in Nairobi – 2female and 6male. Unemployed youth are all male – 2 in Nairobi and 3 in Mombasa. Professionals are all in various capacities in their respective organisations – 4female and 5male.*

However, for the purposes of this paper, only responses from the entrepreneurs were considered. The themes of interest that emerged from this sector include: mode of entry in to the Kenyan market; industry type targeted; motivation; and trade effects. The summary of the key findings as articulated by various Kenyan entrepreneurs is summarised in Table 1.

**Table 1: Summary of Response to Chinese Entry and Activities in Kenyan Market**

|  |  |
| --- | --- |
| Mode of Entry | The Chinese actors never partner with the locals. They bribe their way to win the entire tender for big jobs. Through government-to-government agreements, they are able to come in and bring in all their materials and labour. |
| Industry Type | All types of industries including agriculture, farming, fishing, infrastructure, technology, retail, real estate, banking and general trade |
| Main Motivation | To make maximum profits. Have seen opportunity and are aggressive. To seek for employment for their Chinese nationals. Market to dump their cheap products. Resource and market seeking |
| Trade Effects | The Chinese are seen hawking in the streets of Nairobi and Mombasa undercutting Kenyan hawkers on price and hence sending the locals out of business. Their cheap products drive out local manufacturing companies. Their cheap products are not durable hence driving up consumerism without cleaning or recycling facilities and so the environment is not well taken care of. |

*Source: Okumu (2016) – Unpublished Thesis*

# Discussion

The Chinese entrepreneurs’ mode of entry in Kenya has not had any variations from their entry to other nations in Sub Saharan Africa. As various authors have contended ([Carmody 2011](#_ENREF_8); [Konings 2007](#_ENREF_25); [Zafar 2007](#_ENREF_44)), they are reluctant to partner with the locals and are willing to bribe their way in to the African markets, as it is the case in Kenya. The trading enhancing ([Kojima 1977](#_ENREF_22), [1978](#_ENREF_23); [Kojima, Chokusetsu & Ron 1977](#_ENREF_24); [Ozawa 2006](#_ENREF_35)) mode of entry employed by the Japanese in the last century employed partnership with local players guided by ethical business principles.

Unlike their fellow Asians - the Japanese who targeted particular economic sector in their internationalisation ([Kojima 1977](#_ENREF_22), [1978](#_ENREF_23); [Kojima, Chokusetsu & Ron 1977](#_ENREF_24); [Ozawa 2006](#_ENREF_35)), the Chinese entrepreneurs have no special economic sectorial targets in their Africa strategy. In Kenya, they entered in to all sectors including: agriculture, farming, fishing, infrastructure, technology, retail, real estate, banking and general trade. This has imposed unwarranted and unprecedented competitive pressure to the local players. As various scholars have argued ([Carmody 2011](#_ENREF_8); [Sanusi 2013](#_ENREF_36); [Zafar 2007](#_ENREF_44)) and has been confirmed by interviews, the Chinese players are driven by an insatiable appetite to accumulate as profit. This is done with little regard for locals’ environment, social capital and way of life. Most interviews concede that China-Kenya economic relationship has insignificant benefit to locals and therefore not sustainable in the long run. One interviewee succinctly captured this position thus:

*“ I don’t think our relationship with them is sustainable because this is not a healthy one. It is where we are, we have allowed them to come in and threaten our economy and they have seen that we don’t have any standards or any ethics on how we work, so if we keep going this way, the Chinese will continue coming and making a mess out of Kenya. So a 'Kenya-China relationship is not sustainable” – Entrepreneur 1 interviewee*

In regards to the trade effect as it related to the study’s two propositions, while the outcomes in specific geographic areas may be subject to debate, there can be little doubt that Chinese entrepreneurs are found in many parts of Kenya hawking their merchandise door-to-door. The complaints from entrepreneurs in the major towns of Kenya is that this form of market intercourse destroys not only the local entrepreneur’s ability to plan, organise and implement a structure market plan but also the low prices and poor quality of products destabilises the market equilibrium to the detriment of the local players. This is reflected in numerous studies such as [Konings (2007](#_ENREF_25)), [Zafar (2007](#_ENREF_44)) and [Kaplinsky & Morris (2011](#_ENREF_20)).

The effect of such market disorder and disillusionment of the local actors is that foreign players limit the space to engage and offer benefits to the hosts as articulated in the FDI theory. Indeed, Kenyan interviewees were not hesitant to point out that: one, because the Chinese players are apprehensive of and less trusting of local partnership, spillovers such as skills and technological knowhow to fund transfer impediments. At the same time, the collaboration needed to facilitate training to the local players is restricted and hence local human resource development fails to emerge. However, although interviewees and literature contends that the Chinese players exhibit diminished interest to impart positive spillover, the study’s participants and various authors ([Collier 2011](#_ENREF_13); [Cuerro-Cazurra 2006](#_ENREF_14); [Gregg 2010](#_ENREF_17)) converge at a common understanding that out of hand corruption embedded in the local institutions and governance actors has more substance in explaining the reluctance on the Chinese actors.

In summary therefore, the realisation of both propositions 1 and 2 is contingent on various factors, some of which include: ethical and incorruptible governance in the host nation ([Collier 2011](#_ENREF_13); [Cuerro-Cazurra 2006](#_ENREF_14); [Gregg 2010](#_ENREF_17)); transparency and accountability in the process of licensing of foreign actors; and support through subsidies or level playing from the government of the local entrepreneurs. As it is at the time of writing, local entrepreneurs are undergoing a more survival for the fittest mantra, which in itself breeds a win - lose scenario with the Chinese winning against the local as opposed to a win-win situation.

# Limitations

This study was not without limitation and key to this was the fact that none of the numerous Chinese merchants in both Nairobi and Mombasa agreed to be interviewed. This is an enormous research bias that needs to be rectified with future research. Other interviews need to be conducted in other countries in East Africa and sub-Saharan Africa to see if these findings are replicated. The lack of adequate representation of Chinese voices in this study obscure the reality on the ground. Further research is necessary to find out the further motivations for both market disruption and lack of substantial spillovers in the country.

Conclusion

Internationalisation theory underpins the importance of spillover effects and history has not been deprived of cases where this has been the case. From Kojima’s trade enhancing theory to Ozawa’s flying geese, several East Asian nations have been at the forefront in re-defining and advancing FDI. However, the contemporary rise of China and its outward FDI has attracted numerous contestations. This paper sought to determine the effects of Chinese entrepreneurs in Kenya both to the market and the local players. As it stands, this paper shows that Chinese players in Kenya endeavour to destabilise the market equilibrium by offering low quality products and at very low prices. The net effect heard from the voices of local entrepreneurs is that the unprecedented competitive edge contained by the Chinese continues to create a market scenario where only the fittest can survive. This is together with the fact that, the form of internationalisation experienced in the process from the Chinese, does very little to enhance positive spillover effects of the investment.

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