

How suppliers penetrate overseas market :
internationalization of Chinese firms from the
value chain perspective

著者	Fujita Mai
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How suppliers penetrate overseas market: Internationalization of Chinese firms from the value chain perspective

Mai FUJITA *

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Abstract

This paper examines how Chinese firms serving the low-end domestic market internationalize into developing country markets abroad. It adopts a value-chain-focused approach to analyze the internationalization of Chinese firms into the Vietnamese motorcycle industry. The analysis shows that it was Chinese component suppliers rather than Chinese motorcycle manufacturers that successfully penetrated low-end market at the destination. Chinese suppliers did so by focusing on production-related expertise to provide key components to many locally-owned firms that undertook end-product assembly and distribution. The findings suggest that the research on the internationalization of Chinese firms needs to be embedded in the context of industrial organization in Chinese industries and its transformation.

Keywords: internationalization, suppliers, China, Vietnam, motorcycle industry

JEL classification: F1; F2; L10; L20, L62

* Director, Southeast Asian Studies Group II, Area Studies Center, IDE
(mai_fujita@ide.go.jp)

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INSTITUTE OF DEVELOPING ECONOMIES (IDE), JETRO
3-2-2, WAKABA, MIHAMA-KU, CHIBA-SHI
CHIBA 261-8545, JAPAN

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1. Introduction

Chinese manufacturing firms have achieved remarkable success in enhancing their global presence. The growing literature has focused primarily on end-product companies that achieved certain success in building internationally recognized brands, highlighting the particular features of their internationalization paths. Companies such as Lenovo, Haier and Galanz adopted an accelerated route to expand internationally via acquisitions with the aim of accessing strategic assets such as technology, research and development (R&D) skills, and international brands (Hong and Sun 2006; Duysters et al. 2009; Liu and Buck 2009; Child and Rodriguez 2005). For these companies, international investments were primarily a means of remedying their competitive disadvantage rather the exploitation of existing firm-specific advantages and to enter large developed country markets (Child and Rodriguez 2005).

In highly segmented Chinese market (Gadiesh et al. 2007), there is another category of Chinese firms that have taken a very different route to internationalize. These are smaller firms without internationally recognized brands that exploit cost advantage to dominate the huge low-end market in China (Brandt and Thun 2010). These firms, pressed by intense competition at home, explore new markets in developing countries that exhibit demand characteristics similar to the Chinese market. Previous studies examined the impact of Chinese exports (Alvarez and Claro 2009; Sonobe and Otsuka 2010) or foreign direct investment (FDI) (Gu 2009, Ozawa and Bellak 2011; Amendolagine et al. 2013; Kubny and Voss 2014) by this type of firms on the host countries. However, to date limited attempts have made to examine how Chinese firms actually operate in the host country. A problem that deserves particular focus in this regard is how Chinese firms organize their value chains as they enter developing country markets. This is because Chinese industries serving the low-end domestic market are characterized by a vertically disintegrated structure, in which large numbers of component suppliers and end-product assemblers engage in arm's-length relationships (Watanabe 2014a). These features raise a series of questions regarding the internationalization of firms in this segment of Chinese industries. How do Chinese firms link among themselves and/or with other firms to reach the end customers overseas? How do Chinese firms compete with competitors at each node of the value chain? This paper explores these questions.

In addressing these questions, this paper looks into historical experience of the internationalization of Chinese firms into the Vietnamese motorcycle industry. This is

because the motorcycle industry is one of the earliest and most dynamic cases of Chinese manufacturing firms' internationalization. Vietnam was the first major destination, where the entry of Chinese firms not only had significant impact on the incumbent manufacturers but also gave rise to new value chains serving the local low-end market. This paper adopts a value-chain-focused approach to examine the role of Chinese firms in the chains feeding into the low-end motorcycle market in Vietnam, including motorcycle manufacturers and component suppliers. Although both Chinese motorcycle manufacturer and component suppliers entered the Vietnamese market, the analysis shows it was Chinese suppliers that successfully penetrated the low-end motorcycle market in Vietnam. They did so by trading with a large number of locally-owned customers at the destination. This paper discusses the factors that give rise to this pattern of internationalization as well as its subsequent decline, and the implications of the findings for the research on the internationalization of Chinese firms.

The remainder of the paper is structured as follows. Section 2 discusses the distinctive organizational features of the Chinese motorcycle industry. Section 3 presents the case study. After analyzing exports and FDI by Chinese motorcycle manufacturers and component suppliers to Vietnam, the section examines the structure and characteristics of in the motorcycle value chains that emerged in Vietnam as a result of internationalization of Chinese firms. The last section summarizes the findings and discusses their implications.

2. Value chain features of Chinese industries serving the low-end domestic market

A growing literature has demonstrated Chinese industries targeting the low-end domestic market up to the early 2000s shared several distinctive features (Watanabe 2014a, 2014b). First, industries tended to be vertically disintegrated; that is, industries tended to be divided into narrower domains and such domains – particularly the assembly of end products and the production of components – tended to be undertaken by separate firms. Second, suppliers tended to provide components that were fully or de facto compatible across multiple end-product firms, rather than components that were customized to particular customers, and end-product firms made extensive use of such components (Marukawa 2007). Third, vertical disintegration, combined with the emergence of specialized suppliers of fully or de facto compatible components, lowered the cost of entry into assembly and distribution of end products, and active entry, in turn,

resulted in low level of concentration. Fourth, the use of components that were compatible across multiple end-product firms enabled end-product firms and component suppliers to engage in arm's-length transactions. Very often, both parties traded with multiple partners and engaged in limited communication or coordination, and partners were switched easily. These features together helped Chinese firms to lower the costs of producing undifferentiated products for the low-end domestic market until the early 2000s.

In the case of the motorcycle industry, the features discussed above started to be observed in the 1990s. Prior to that, the industry had consisted of a limited number of large enterprises that introduced technology from Japanese motorcycle manufacturers under formalized agreements. Then came dramatic transformation in the early 1990s, triggered by sharing of previously introduced Japanese motorcycle models ("base models") and engines by the entire industry (Ohara 2006: 52-53). These highly popular designs became industry-wide de facto standards and came to be replicated by many motorcycle manufacturers and component suppliers. As a consequence, motorcycle manufacturers could now purchase and assemble standard components that were readily available on the market, and this significantly lowered the entry barriers for motorcycle assembly. Likewise, suppliers did not have to invest in equipment, human resources, or skills specific to customers; to operate as a motorcycle component supplier, simple reverse engineering capabilities in terms of reproducing existing components and routine manufacturing sufficed (Fujita 2013a). De facto standardization of base models also made motorcycle manufacturers and component suppliers increasingly independent of each other. Suppliers traded with many customers while manufacturers normally maintained multiple – usually three or more – suppliers of each type of component (Ohara 2001: 18).

As was the case with most industries in China, active entry and expansion of production by new entrants resulted in saturation of the market and intense price-based competition by the late 1990s. A typical response, observed among incumbent players in many industries in China, is to attempt to upgrade from the low-end to the middle-end market by improving product quality and design (Brandt and Thun 2010). This option, however, was not available to incumbents in the motorcycle industry, in which restrictions on motorcycle use in large cities in China meant that motorcycle demand concentrated in low-income population in medium- and small-sized cities and rural areas (Ohara 2006: 32). In this industry, the remaining option for survival was to explore new markets abroad. Chinese motorcycle firms therefore started to internationalize via exports and

FDI by the end of the 1990s, and the first major destination was Vietnam.

3. Case study of Chinese motorcycle firms' internationalization into Vietnam

3.1 Modes of entry: exports vs. FDI

Vietnam was the first major destination for the overseas expansion of the Chinese motorcycle industry. The key actors and the modes of entry changed over time, in response to changes in the Vietnamese government's policies.

The internationalization of Chinese firms into Vietnam started with massive exports of vehicles. Figure 1 shows that China's exports of vehicles to Vietnam surged dramatically in 2000–2001. Vietnam accounted for 65% and 74% of China's total motorcycle exports in 2000 and 2001, respectively¹, and the top exporters in these years included China's leading motorcycle manufacturers (Ohara et al. 2003: 78). The year 2002, however, marked a turning point, when the exports of vehicles declined remarkably. This is because the Vietnamese government has increased its enforcement of import controls and local content rules that had previously been circumvented by Vietnamese importers (Fujita 2011). In subsequent years, Chinese exports of engines and other components increased and remained stable until 2009.

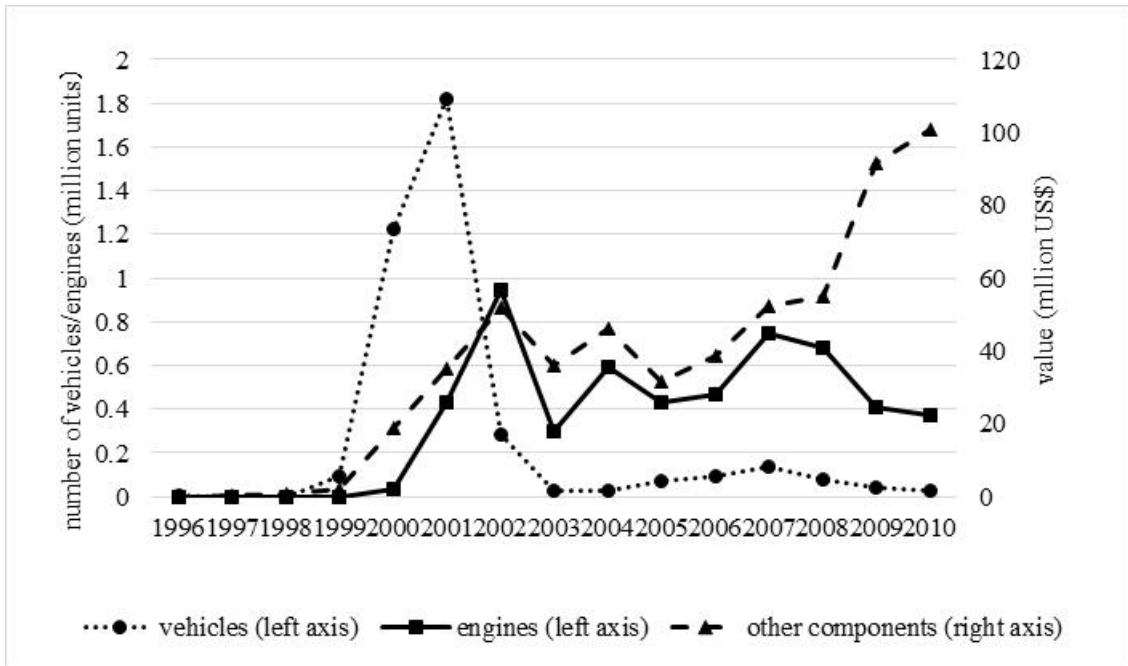
As a result of increased enforcement of import controls and local content rules, many Chinese motorcycle exporters simply left Vietnam and turned to other prospective markets such as Africa². This seems to be at least partly due to the Vietnamese government's restrictive policies towards licensing of FDI projects for motorcycle production. However, one major motorcycle manufacturer, Lifan, established a joint venture with a Vietnamese state-owned enterprise in 2002 for the local production of motorcycles. Chinese firms' FDI focused instead on the production of components. More than 30 such projects were licensed between 2000 and 2005 (Figure 2). Notably, six projects licensed in 2002 and 2003 were joint ventures with capital contribution by Lifan's key component suppliers and Lifan Vietnam. These projects were aimed at the

¹ The author's calculation based on Global Trade Atlas data.

² According to Ohara (2005: 119), Loncin and Yixiang, the first and third largest motorcycle exporters to Vietnam in 2001, subsequently shifted to exporting motorcycles to new markets such as Nigeria and Iran.

production of key components such as engine components, clutches electric components, and plastic components, apparently for Lifan Vietnam.

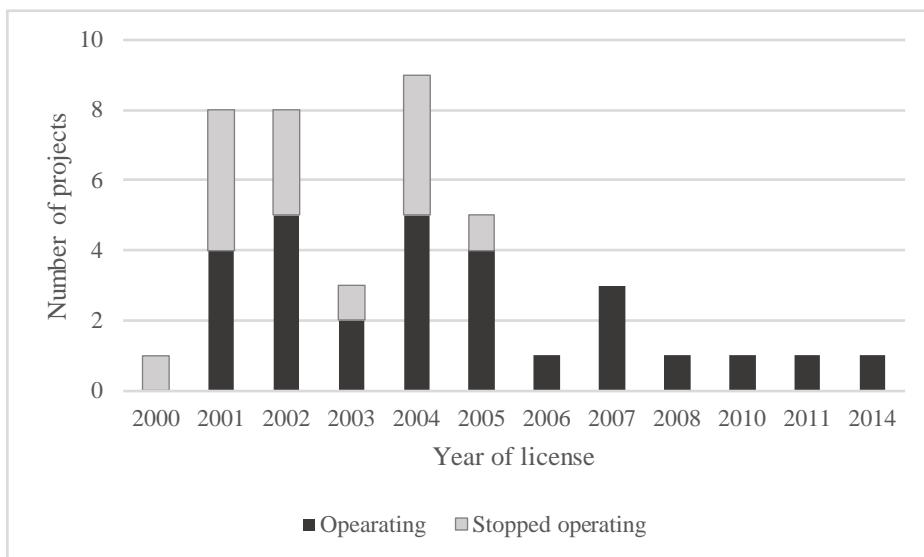
Figure 1. China’s Exports of Motorcycles and Components to Vietnam



Note: Motorcycles are limited to those with a cylinder capacity over 50cc but under 250cc (HS 871120), the types most commonly used in Vietnam.

Source: Data from Global Trade Atlas.

Figure 2. Number of Chinese-invested projects in motorcycle component production in Vietnam by year of license



Note: The status of projects is as of September 2016.

Source: Data from the Ministry of Planning and Investment.

3.2 Emergence of local production serving the low-end market at destination: Value chain analysis

Exports and FDI by Chinese motorcycle manufacturers and components suppliers had significant impacts on the Vietnamese motorcycle industry. Prior to the entry of Chinese firms, the industry consisted of a handful of Japanese- and Taiwanese-invested motorcycle manufacturers that produced sophisticated yet expensive models that were beyond the reach of majority of the country's population under heavy protection by the government (Fujita 2011). However, massive inflows of Chinese vehicle imports discussed above resulted in a loss of market share for the incumbent Japanese and Taiwanese companies. In particular, Honda's market share declined sharply from 67.2% in 1998 to 11.9% in 2001³ (Institute for Industry Policy and Strategy 2007: 38). Honda nevertheless responded by launching a new model priced nearly one-third of its previous products in 2002, which helped the company to recover its market share in the subsequent period.

In the meantime, the shift in the entry mode of Chinese firms from vehicle exports to component exports and FDI by motorcycle manufacturers and component suppliers gave rise to new value chains serving the low-end motorcycle market in Vietnam. The following provides an analysis of the key features of the emerging value chains focusing on the situation around 2007. This is the timing when value chains that emerged out of Chinese exports and FDI had a dominant position in the Vietnamese motorcycle industry. More recent situation of the industry in the 2010s will be discussed briefly in the concluding section.

Motorcycle assemblers: Domestic assemblers outperform a major Chinese-invested firm

As a result of the internationalization of Chinese firms and the Vietnamese government's policies to increase the enforcement of import controls and local content

³ The difference between these figures and data in Table 1 is explained by the following factors. First, these are sales data collected by surveying the manufacturers, whilst the data in Table 1 are registration data. Second, the sales data in the text include both motorcycles produced locally by Honda Vietnam and imported Honda-brand motorcycles, primarily from Thailand.

rules, local production catering to the low-end motorcycle market in Vietnam started to be undertaken by two groups of motorcycle assemblers. One group comprised a Chinese-invested firm, Lifan Vietnam. Although this company launched local production of motorcycles under its own brand name, its products essentially imitated popular Japanese models and were sold at prices similar to its local competitors.⁴ The other group consists of locally-owned companies, which amounted to more than 50 in 2001. Many of them started as importers of Chinese motorcycles in the early 2000s. In response to the increased enforcement of import controls and local content requirements in 2002, motorcycle assembly and even in-house production of components was launched.

The performance of these two groups of assemblers shows striking contrast. Lifan Vietnam never obtained a substantial market share. The combined share of Lifan Vietnam and two foreign-invested assemblers that are neither Japanese or Taiwanese in the country's total motorcycle registration was 2.5% at most during the years 2001-2006 (Table 1), which means that Lifan Vietnam's share was even smaller. Despite being a subsidiary of a fully-fledged motorcycle manufacturer, Lifan Vietnam eventually shifted its focus to the supply of components to local assemblers in Vietnam (Motorcycle Joint Working Group 2007), which as we shall see emerged as a promising area of business for Chinese firms in Vietnam. In contrast, Vietnamese motorcycle assemblers dominated the low-end market since 2001. Despite Honda's entry into the middle-end motorcycle market with the new low-priced model in 2002, these local assemblers maintained a combined share of 45.5% even in 2006 by catering primarily to the demand of low-income consumers mainly in rural areas. While as many as 43 Vietnamese assemblers continued to operate as of 2005,⁵ this segment of the industry showed signs of consolidation. The market share of local assemblers producing more than 40,000 units per year increased consistently, whereas those producing less than 10,000 units per year continued to survive (Table 1).

⁴ Details of models launched by Lifan Vietnam were obtained from Vietnam Register website (http://www.vr.org.vn/vaq/Xecogioi_sxlr/Xecogioi_sxlr.asp). Lifan Vietnam's 100cc and 110cc models were priced between 6.8-7.4 million dong in July 2004, which was comparable to prices of models of a Vietnamese assembler (*Oto-xe may*, July 2004) as well as four other local assemblers surveyed by the author in the same year.

⁵ Institute of Industry Strategy and Policy (2007: 36), citing Vietnam Register data, mentions that there were 51 motorcycle manufacturers and assemblers. If we exclude foreign-invested companies (three Japanese, two Taiwanese, one Chinese, and two Thai), then there were 43 Vietnamese companies.

Table 1. New Registration of Motorcycles and Shares by Assemblers

	2001	2002	2003	2004	2005	2006
Number of newly registered motorcycles (Unit: 1,000 vehicles)	2,486	1,819	1,790	2,139	2,188	2,554
Foreign-invested assemblers	12.9%	42.4%	47.6%	51.7%	53.6%	54.5%
Honda Vietnam	6.8%	21.0%	23.7%	23.9%	28.6%	31.6%
Yamaha Vietnam	0.9%	3.8%	6.8%	9.8%	11.7%	13.7%
Vietnam Suzuki	1.0%	2.3%	2.9%	3.6%	3.9%	1.7%
VMEP *	3.2%	13.6%	11.8%	12.0%	7.8%	5.9%
Others **	1.0%	1.7%	2.5%	2.5%	1.6%	1.7%
Local assemblers (categorized by scale)	87.1%	57.6%	52.4%	48.3%	46.5%	45.5%
More than 40,000 units/year (6 firms in 2005)	8.1%	10.2%	12.6%	19.4%	22.4%	27.1%
20,000-40,000 units/year (10 firms in 2005)	40.5%	31.1%	30.6%	24.6%	13.4%	7.4%
10,000-20,000 units/year (14 firms in 2005)	21.1%	10.0%	9.2%	4.2%	8.8%	5.5%
Less than 10,000 units/year	17.4%	6.3%	0.0%	0.2%	1.8%	5.6%
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Note: * Vietnam Manufacture and Export Processing Co., Ltd. (VMEP) is a motorcycle manufacturer wholly invested by Chinfon Group of Taiwan.

** Others include Lifan Vietnam (China), Vina Siam (Thailand), and GMN (Thailand and Laos).

Source: Institute for Industry Policy and Strategy (2007:37).

The question that follows is what types of Vietnamese assemblers eventually expanded their sales. The results of the author's fieldwork-based research in 2008–2009 (Fujita 2013b) show contrasts in product strategies among local assemblers. Some assemblers prioritized price-based competitiveness. These assemblers made little effort to develop own brands or to improve product quality. Their products essentially carried designs that imitated a limited number of most popular Japanese models, but they launched increasing varieties of products by making minor cosmetic modifications to the original Japanese designs and sold such products under a large number of imitated brand names. Other assemblers opted for the improvement of product quality, developing own product designs and/or brands even at the expense of higher prices. A clear difference from the former group is that this group launched much smaller numbers of new models sold mostly under a few fixed brand names.

As regards the performance of the two groups of assemblers, the former group of assemblers grew rapidly, while the latter stagnated. Two assemblers belonging to the former group accounted for as much as 23.1% and 8.3% of total sales recorded by all

local assemblers that operated in 2006 (Fujita 2013b: 60). The latter group experienced difficulties in competing with Honda's low-priced model as Vietnamese consumers increasingly opted for quality and reliability, while the former group concentrated on low-income consumers in rural and remote provinces for whom Honda's low-priced model was still out of reach. For the sake of comparison, Lifan Vietnam's market share was comparable to those in the latter category, and substantially smaller than the largest local assemblers in the former group.

Suppliers: Chinese imports and Chinese-invested suppliers dominate

Having analyzed the strategies and performance of key players in the end-product market, we now turn to suppliers. We already saw that China continued to export significant quantities of engines and other components after 2002 (Figure 1) and that more than 30 Chinese FDI projects in component production were licensed in the early 2000s (Figure 2). While local assemblers outperformed Lifan Vietnam in the low-end Vietnamese market, these firms in fact depended heavily on components imported from China or components sourced from Chinese-invested suppliers in Vietnam to assemble motorcycles that imitated a few – in fact, just two – very popular Japanese models. Chinese suppliers, whether based in China or in Vietnam, produced components that were de facto compatible with such focal models in large quantities and supplied them to a large number of customers in this segment of the Vietnamese motorcycle industry. In effect, these suppliers formed a “shared supply base” (Sturgeon and Lee 2005) for assemblers operating in the low-end Vietnamese market.

The relative roles played by Chinese imports and FDI differed by the types of components. Exports played particularly crucial roles with respect to engines. Vietnam's engine imports from China remained at above 400,000 units per year between 2004 and 2007 and reached 750,691 units in 2007 (Figure 1). Given that Japanese- and Taiwanese-invested assemblers did not import engines from China, at least in large quantities, in these years⁶ and Lifan Vietnam assembled engines in-house, engines imported from China are likely to have been used largely by Vietnamese assemblers. The number of Chinese-imported engines in 2007 is equivalent to 82.7% of the number of motorcycles sold by these assemblers in the same year. Apart from Lifan Vietnam,

⁶ The Taiwanese-invested manufacturer, VMEP, achieved a local content ratio of 70% for engines and exported engines in 2004, which means that they assembled engines in their factory in Vietnam (The Motorcycle Joint Working Group 2007: 20). According to the survey of Japanese assemblers, only 0.9% of engines were imported from countries other than Japan, Thailand, Malaysia, and Taiwan in 2007 (ibid.: 21).

two Chinese-invested suppliers are known to have invested in production of engines, and neither of them achieved substantial shares.⁷ These data suggest that local assemblers depended largely on imported Chinese engines.

Chinese FDI, in contrast, played key roles in supplying components other than engines, particularly the following two types of components. The first includes components that require technologically sophisticated production processes and are, therefore, produced by few local suppliers. Clutches and electric components are examples of such components. The author's fieldwork-based research found Chinese-invested suppliers specialized in these types of components traded with a large number of Vietnamese assemblers (Fujita 2013b: 62). However, these types of components were also imported in large quantities from China, as observed in Figure 1.

In the meantime, much greater success was achieved by Chinese-invested suppliers producing the second type of components, namely, frames, plastic covers, and lamps. Although these are not technologically difficult to produce, these components determine the external appearance of motorcycles. Local assemblers that grew rapidly by prioritizing low prices came to attach increasing importance to these components to meet changes in consumer demands. Supplier A achieved a very high market share in these components; in 2007, this supplier sold over 860,000 units of plastic covers and frames, which roughly accounts for the total number of motorcycles produced by local assemblers in that year, to 43 local assemblers – close to the total number of local assemblers operating in the year (Fujita 2013b: 62, 70).

Supplier A was established in 2001 as a wholly foreign-invested firm with capital contribution of four Chinese motorcycle component suppliers in Chongqing (Ohara et al. 2003: 84). With the initial registered capital of US\$10 million, which was larger than that of Lifan Vietnam (*ibid.*), the firm initially produced not only frames and plastic covers but also other types of components such as engine components and wheels⁸. While other Chinese-invested companies produced frames and plastic components *independently*⁹, Supplier A rapidly expanded sales to local assemblers by providing both

⁷ Author's interviews of the two Chinese-invested suppliers in November 23, 2007 and September 12, 2016, respectively.

⁸ The author's interview with a former manager of Supplier A on July 22, 2017. The total number of employees in 2004 was around 2,400.

⁹ From the list of licensed FDI projects from the Ministry of Planning and Investment, the author could identify, apart from Company A, at least three Chinese-invested projects for the production of frames and two for manufacturing plastic components.

of these components as complete, fine-tuned modules, incorporating minor cosmetic modifications, processing them with reasonable quality and at low costs, and delivering them in a timely manner to the customers (Fujita 2013b: 71). Each year, Supplier A launched new designs incorporating minor modifications to these necessary modules, and this enabled local assemblers to renew their product designs regularly to meet changing consumer preferences (ibid., p.73).

As a consequence of the growing importance of components imported from China and supplied by Chinese-invested suppliers, local Vietnamese suppliers lost their space in the value chains serving the low-end domestic market. These local suppliers grew since the early 2000s primarily by supplying simple components that did not require specific product- or production-related expertise, such as metal stamped components. By 2008–2009, many had shifted away from supplying local assemblers and seeking opportunities to serve other customers, such as first-tier suppliers to Japanese motorcycle manufacturers or customers in industries other than the motorcycle industry (Fujita 2013b).

Arm's length assembler-supplier relationship

Vietnamese assemblers essentially engaged in market-based relationships with their suppliers. Since most of these assemblers came from trading background, they had limited product- or production-related knowledge needed for providing detailed product and process specification to suppliers, monitoring suppliers' performance, and managing relationships with them. For these technologically weak firms, the use of components that were de facto compatible with a few popular focal models was vital as this substantially reduced the need for coordination with suppliers. Local assemblers thus placed orders on an *ad hoc* basis without detailed specifications, engaged in limited monitoring of supplier performance, and switched them whenever they found quality, prices, or other terms of transactions unsatisfactory (Fujita 2013b). Although repeated duplicative imitation of components using different measuring methods with varying degrees of precision and often incorporating minor adaptations meant that the components were only de facto compatible, this sufficed for the purpose of serving low-income consumer market in the early 2000s (ibid).

The rise of Supplier A, discussed above, brought about some changes to the nature of the inter-firm relationship discussed above. This supplier initiated new flows of knowledge by incorporating market information obtained from customers when making

minor adaptations to the designs of popular Japanese models and assisting customers in cases where problems arise after delivery (Fujita 2013b). Such knowledge flows were crucial in addressing the requirements of local assemblers to respond to consumer demands for product variety and improved quality in the face of competition with Honda's low-priced model (ibid.). Nevertheless, the assembler-supplier relationships are arm's-length to the extent that neither side was locked into particular relationships, which allowed Supplier A to realize economies of scale by serving many small customers.

4. Discussion and conclusion

This paper was set to analyze the internationalization of Chinese firms serving the low-end domestic market. To this end, it started by highlighting that the segment of the Chinese industries in question was characterized by vertical disintegration, extensive use of fully or de facto compatible components, low concentration, and arm's length relationships between end-product assemblers and component suppliers. By adopting the value-chain-focused approach to analyze the internationalization of Chinese firms into the Vietnamese motorcycle industry, this paper provided crucial insights into how Chinese firms serving the low-end domestic market internationalize into developing country markets overseas.

Not surprisingly, internationalization started with massive exports of end products, i.e., motorcycles. However, when policy changes made vehicle exports difficult, Chinese firms started to turn to other modes of entry. Lifan, one of the largest motorcycle manufacturers in China, invested in local production. However, the company never obtained substantial market share and even lost out to local assemblers in the low-end market. This can be explained by the following three factors. First, numerous safety-related problems caused by low-quality motorcycles imported from China in massive amounts in the early 2000s seriously hurt the Vietnamese consumers' perception of Chinese motorcycles. This severely affected Lifan, which was among the most prominent Chinese motorcycle brands in the Vietnamese market in those years¹⁰. Even after engaging in local production, the company did not succeed in redressing this

¹⁰ In these years, Chinese firms prioritized expanding exports without attention to quality (Ohara et al. 2003: 72). Lifan, along with Loncin, were the two most prominent Chinese brands that opened the way into the Vietnamese market in the early years (An Nhi 2013a). For Vietnamese consumers' perception, also see An Nhi (2013b).

situation. Second, unlike local assemblers that eventually expanded sales, Lifan Vietnam was unable to launch varieties of new models and thus failed to respond to local consumer demand, which not only differed from China but also changed rapidly (Fujita 2013b). Third, as a foreign-invested firm, Lifan Vietnam is likely to have been disadvantaged in its capacity to develop networks of dealers throughout the country and manage relationships with them. This capacity was particularly crucial for firms focusing on the low-end market, which overwhelmingly concentrated in rural and remote provinces.

In the meantime, Chinese firms played much more important roles as component suppliers. Although some suppliers followed Lifan to invest in local production in Vietnam, many more Chinese suppliers internationalized independently and penetrated the low-end market at the destination by developing business with local assemblers. These suppliers focused on production-related competencies to process key components to decent quality at low cost, which were in short supply in Vietnam. Moreover, they capitalized on de facto component compatibility to serve many local assembling firms, which utilized their knowledge of local demand characteristics and trading background to promptly respond to market changes and distribute their products to consumers in rural areas. In the end, the low-end motorcycle market was dominated by technologically backward local Vietnamese assemblers that depended heavily on components imported from China and sourced from Chinese-invested suppliers.

The above analysis has highlighted a path of market-seeking internationalization of Chinese firms – one which in which suppliers penetrate developing country markets by connecting with local end-product firms at the destination. While this path emerged specifically out of the analysis of the Vietnamese motorcycle industry, similar phenomenon may be observed among Chinese firms in other industries where they face barriers to exports of end products, subject to a number of factors. The first set of factors concerns market characteristics. Most importantly, the suggested path is likely to be observed in large low-income countries with sizeable low-end market. It is also likely where Chinese end-product assemblers face competitive disadvantage over locally-owned competitors; that is, where consumer demand characteristics differ from those in China and/or change frequently, Chinese brands are not highly recognized, and distribution channels are difficult to be handled by foreign entrants. The second set of factors has to do with the entrepreneurial dynamism in the host country. The suggested pattern is likely to emerge in countries that are equipped with numerous entrepreneurial consumer-facing firms or potential entrants willing to exploit profit-making

opportunities but have a limited pool of technologically competent component manufacturers.

The above sets of factors have implications for long-term sustainability of the suggested path. While this path provides a quick route for Chinese firms to expand business by catering to the low-end developing country market abroad, the sustainability of this route depends on a number of factors. First, there is the issue of whether the sizeable low-income market would continue to exist in the longer run. Where rising consumer incomes lead to the contraction of the low-income market, local assemblers at the destination and their Chinese suppliers might lose their space in the market, unless they succeed in acquiring improved product and/or production capabilities that enables them to tap into the growing middle-income market. The second factor concerns the capabilities of the local assemblers. Where consumers at the destination start to opt for improved product quality and/or design, local firms would eventually be pressured to acquire improved technological capabilities – as had been the case with firms in China (Brandt and Thun 2010). In the Vietnamese motorcycle case, the market for low-priced motorcycles had shrunk considerably by the early 2010s, almost a decade after its emergence, and local assemblers and Chinese suppliers failed to keep up with the changes in consumer demand. By then, the five foreign-invested manufacturers from Japan, Taiwan and Italy accounted for a 98% share, including Honda's 63% (Nguyen Thi Thu Ha and Ho 2013).

This study has implications for the literature on the internationalization of Chinese manufacturing firms. First, the paper provided new systematic insights into how Chinese firms serving the low-end internationalize. These firms are likely to opt to export the end products. However, where the export of the end products is not possible or desirable, an alternative is that Chinese suppliers develop business with downstream firms at the destination, via exports or FDI, to penetrate the low-end market at the destination. Second, research on the internationalization of Chinese firms needs to be embedded in the context of the multi-layered industrial structure in China (Brandt and Thun 2010). This paper showed that internationalization paths differ substantially between major branded firms serving the middle-end market and non-branded firms in the low-end market. While the present analysis demonstrated that the internationalization path of the latter group of Chinese firms is closely related to the distinctive organizational characteristics of the corresponding segment of Chinese industries, this might also be the case with the former group of Chinese firms. The tendency of larger branded firms to pursue acquisitions of overseas companies to access

advanced technologies and R&D skills may at least partly have to do with their historical dependence on external suppliers of key components and the urgent need to achieve technological upgrading to compete domestically and internationally.

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