Why China matters to Africa: partnership, investment and trade?

By Victor Mathale

China first became involved in Africa during the cold war, when it made friends and did business in parts of the world overlooked by the West and the Soviet Union. Its investment is paying off now in oil and raw material imports and markets for manufactured goods.

A seminar on “China-Africa Partnership in the 21st Century” was held at the Great Wall Sheraton Hotel, Beijing, co-hosted by the United Nations System in China and the China-Africa Business Council.

"This discussion is extremely timely, given the unprecedented expansion in South-South trade, investment and aid flows that has taken place in recent years, in which China’s role has been the major driving force. China has already demonstrated a strong interest and capacity to support MDG achievement in Africa. "

-Mr. Khalid Malik, UN Resident Coordinator in China and UNDP Resident Representative

China’s diplomatic, economic and people-to-people engagement with the nations of Africa has been expanding dramatically in the last five years. Sino-African trade is growing even more rapidly than Chinese trade with the rest of the world, virtually exploding from $2 billion in 1999 to $39.7 billion in 2007. During his recent visit to Africa, Chinese Premier Wen Jiabao signed 71 agreements on politics, economy, trade, infrastructure, science and technology, culture and education. In light of continued challenges faced by a number of African countries in meeting their Millennium Development Goal targets, this growing role for China in Africa offers encouraging opportunities for the region’s economic and social development.

The keynote presentation made by Professor Jeffrey Sachs, Director of the United Nations Millennium Project and Special Advisor to UN Secretary General Kofi Annan on the Millennium Goals spoke on “Africa’s particular challenges and key areas for Chinese assistance”.

Professor Sachs noted that “The People's Republic of China is providing significant assistance to countries across the African continent in meeting the great challenges of disease, hunger, and poverty.

Africa needs to grow more food, fight infectious diseases, and build its infrastructure.

Professor Sachs views are in this case in line with the NEPAD priorities and objectives, namely, peace, security, political and economic governance, human development, infrastructure development, agriculture and market access, environment, culture and science and technology.

The key recommendations are currently being implemented by the UN and partner organizations in Millennium Villages in 10 countries in Africa." He added that "China has made record-breaking progress in the fight against poverty, and is now eager to share its great successes with other low-income countries around the world. Backed by the experience and confidence of its own economic breakthroughs, China is stepping up its efforts to support Africa's economic development. The benefits to Africa are sure to be enormous."

Mr. Khalid Malik, UN Resident Coordinator in China and UNDP Resident Representative noted that "This discussion is extremely timely, given the unprecedented expansion in South-South trade, investment and aid flows that has taken place in recent years, in which China's role has been the major driving force. China has already demonstrated a strong interest and capacity to support MDG achievement in Africa. For decades, South-South cooperation has been a slogan full of lofty vision but short on concrete substance. No longer. China and other developing countries now have the opportunity to reinforce the development process from the South as well.

Trade and investment by and from developing countries are rapidly growing. The challenge now is to ensure that this important development in South-South partnership is equitable and pro-poor. "

China pledged to offer US$5 billion in preferential loans and credits, and double aid to Africa by 2009, while announcing a package of assistance, investment, trade and other key projects for public health and education with Africa. China also unveiled an ambitious target of raising Sino-African trade to US$100 billion by 2010. Bilateral trade reached US$39.7 billion in 2007, almost four times that of 2000.

Chinese companies signed 14 commercial contracts and agreements worth US$1.9 billion with African nations, covering natural resources, infrastructure, finance, technology and communications.

The roadmap for bilateral co-operation in the next three years is in the political, economic and social sectors.

Politically, China and Africa agree to maintain high-level contacts and exchange views on international affairs.

The economic partnership covers agriculture, investment, business co-operation, trade, finance, infrastructure construction, energy and natural resources.

In the social sector, the action plan includes development and assistance, debt reduction, training of professionals, culture, education, public health, environmental protection, and tourism.

In general, this tighter economic friendship has been welcomed. After all, reducing poverty tops the global community's Millennium Development Goals for 2015. But concerns are increasingly being voiced about how China's growing presence might affect Africa's development. Many African nations worry about its possible impact on local industries and employment. And major industrial nations worry about the lack of donor coordination and rebuilding of debt burdens in poor countries that have benefited from their recent debt write-offs.

To date, there have been relatively few systematic studies of the growing economic relations between China and Africa. That is why the IMF has undertaken a study to quantify— pulling together available information, which is far from complete—China's economic engagement with Africa. The hope is that through a better understanding of the relationship, we can identify how African countries might best position themselves to reap the biggest possible gains.

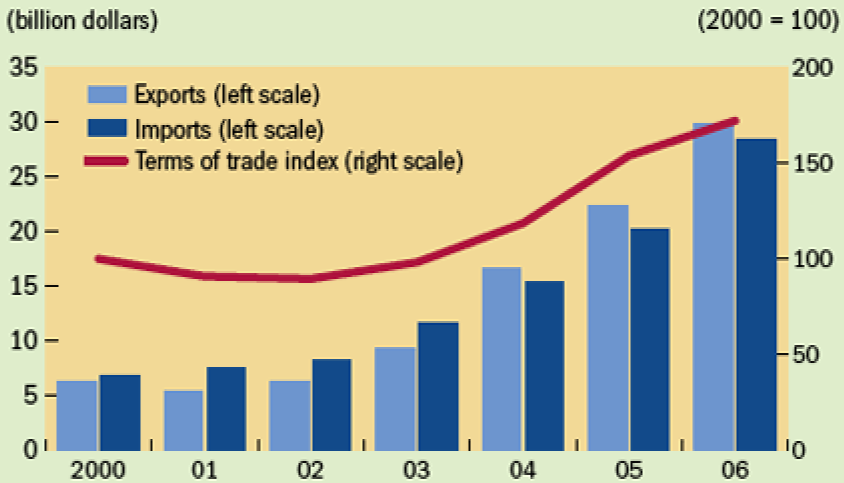
Trade is growing

Two-way trade flows between Africa and China has been growing rapidly. Between 2001 and 2006, Africa's exports to and imports from China rose on average by more than 40 percent and 35 percent, respectively, significantly higher than the growth rate of world trade (14 percent) or commodities prices (18 percent). In dollar terms, for both imports and exports, the increase in that period was from about $10 billion to more than $55 billion (see Chart 1). China is now Africa's third largest trading partner after the United States and the European Union. Its share in Africa's annual export growth has almost doubled since 2000 (see Chart 2).

Chart 1

Surging trade

Africa's exports to China are soaring as its terms of trade improve.



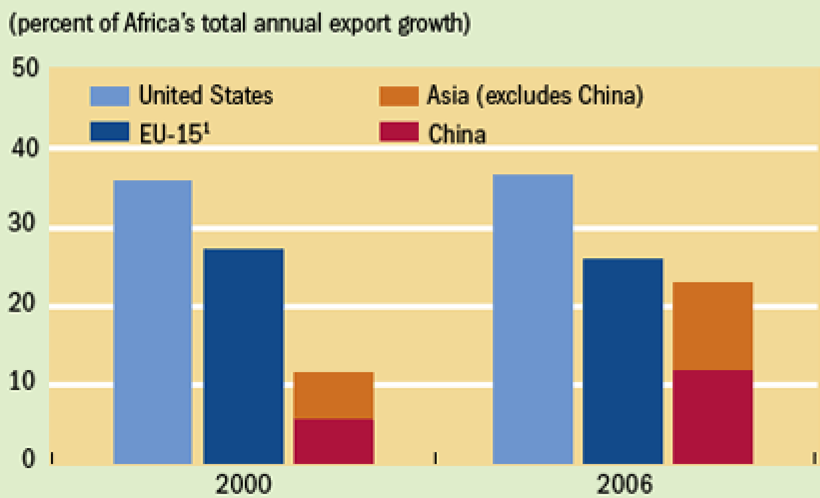
Sources: IMF, *Direction of Trade Statistics*; authors' calculations.

Note: Terms of trade are prices of Africa's exports to China relative to the prices of its imports from China.

Chart 2

The partnership deepens

China is increasingly contributing to Africa's export growth.



Sources: IMF; authors' calculations.

[1]Original EU members before the 2004 expansion: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden, and United Kingdom.

China’s export bank, Exim Bank, had approved a $2bn line of credit to enable Angola to reconstruct infrastructure - including electricity, railways and administrative buildings - destroyed during 30 years of civil war. In return China would receive 10,000 barrels of oil a day

The terms of trade have moved in Africa’s favor. It is estimated that Africa’s export prices relative to the price of imports from China improved by 80–90 percent between 2001 and 2006, the result of rising world prices for oil and raw materials, Africa’s main exports. Those increases have been driven in part by strong demand from China. Bilateral trade, meanwhile, has been fairly balanced. Africa in 2004– 06 ran a small, $2 billion a year trade surplus with China.

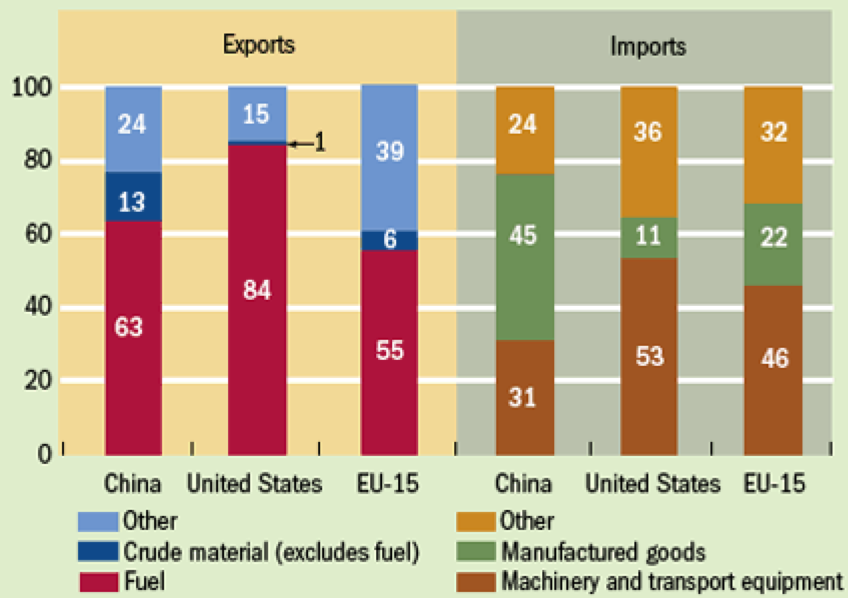
The composition of goods traded between Africa and China is similar to that between Africa and its other major trading partners (see Chart 3). In 2006, oil and gas accounted for over 60 percent of Africa’s exports to China, followed by non-petroleum minerals and metals at 13 percent. Africa’s imports from China comprised mainly manufactured products and machinery and transport equipment, which together accounted for about three-fourths of total imports. The similar composition of goods traded between Africa and its main trading partners suggests that the recent surge in Africa-China trade largely reflects the comparative advantages of each partner, given their stage of economic development, rather than any unilateral interest by China in exploiting natural resources.

Chart 3

Familiar trade pattern

Africa's trade with China in 2006 was similar in composition to its trade with other partners.

(billion dollars)



Source: UNCOMTRADE.

Commerce dominating aid

Merchandise trade is only one aspect of the booming economic relations between Africa and China. There are fewer reliable data on the other important factors in the relationship—such as aid, debt, and direct investment. But on the basis of the information available, it appears that China has played a variety of roles in Africa—trading partner, donor, financier and investor, and contractor and builder. The data also show that trade, investment, and other commercial activities combined have outpaced official development assistance (ODA) and become dominant in financial terms (see Table 1).

Table 1

Aid, trade, and investment

The level of transactions between Africa and China has burgeoned since the turn of the century.

(billion dollars)

	2001	2006
Total trade	10.8	55.5
African exports	4.8	28.8
African imports	6.0	26.7
Official development assistance (ODA)	...	2.3
Chinese ODA	...	1.0
Chinese debt relief	1.3	1.3
Foreign direct investment (FDI)		
Chinese FDI to Africa	...	0.9
African FDI to China	0.3	1.1
Contracted projects		
Chinese projects in Africa	1.8	9.5

Sources: Trade data are from China customs statistics. All other data are from Wang (2007).
Note: ... denotes not available.

Historically, aid was of major importance in China's economic engagement with Africa. Aid flows relative to trade were about 20 percent in the early 1990s. That ratio declined to 3–4 percent in 2004–05, even though China has stepped up its ODA to Africa since the first China-Africa Cooperation Forum was held in 2000. Indeed, in dollar terms, annual ODA flows from China to Africa increased from about $310 million in 1989–92 to an estimated $1–1.5 billion in 2004–05 (Wang, 2007; Taylor, 1998). However, there are major difficulties in estimating Chinese aid disbursements because of a lack of official time series and problems in valuing Chinese technical assistance and in-kind aid.

Recently China has twice provided debt relief on its own terms to African countries. In 2000–02, it wrote off overdue obligations totaling 10.5 billion Yuan ($1.3 billion), and in 2006 it announced that it would cancel another 10 billion Yuan in debt owed by 33 heavily indebted and least developed African countries that have diplomatic relations with China. Incomplete data make it hard to compare the terms on which China provided debt relief with the terms of the

Heavily Indebted Poor Countries Initiative—the debt relief program jointly run by the IMF and the World Bank.

Trade credits, including medium and long term, are an important part of the financial flows from China to Africa. Here the Export-Import Bank of China (China Exim Bank) is a major player. Though China Exim Bank does not report annual activities by region, there is clear evidence that it is expanding its operations in Africa. Based on information collected by Moss and Rose (2006) and Broadman (2007), China Exim Bank supports mainly infrastructure projects in Africa, the financing for which is surely much larger than ODA flows.

China's Ministry of Commerce puts China's direct investment to Africa for 2000–06 at $6.6 billion, but the official statistics may not fully capture foreign direct investment (FDI) by Chinese enterprises, which tend to rely on retained earnings and, in the case of private enterprises, informal arrangements to finance investments. Chinese FDI has increased sharply in the past year. In October 2007, for instance, the Industrial and Commercial Bank of China agreed to purchase 20 percent of Standard Bank Group of South Africa, the largest bank in Africa, spending $5.6 billion on that one investment. FDI between Africa and China flows both ways; there are indications that African FDI to China has also expanded significantly in recent years.

In services, Africa is quickly becoming a key market for Chinese construction and engineering enterprises. Official Chinese statistics show the sum of "contracted projects," "labor cooperation," and "design consultation" in Africa as being less than $2 billion in 2001. In 2006 the turnover on contract labor went up to $9.5 billion, representing 31 percent of China's offshore contracted projects (PBC and CDB, 2007). Within trade in services, two-way traffic is growing particularly fast in tourism.

The ascending private sector

It was two decades ago that China dismantled the state's monopoly on foreign trade. Since then, Chinese private and joint-venture firms have become dominant forces in exports and imports. That has been the case in Africa, where China's private sector is at the forefront of trade, direct investment, and the contracted construction business (Wang, 2007). In recent years, when China's state-owned oil companies struck large deals, Chinese private enterprises were also investing millions of dollars in Africa, most obviously in textiles and mining but also in services, agriculture, and processing and manufacturing. The number of private Chinese construction companies is growing rapidly, as are their size and capacity. They compete actively for construction contracts in Africa.

Reaping the benefits

As economic relations between China and Africa become increasingly commercial rather than aid driven, future relations between the two will be shaped more and more by shifts in comparative advantages and changes in global supply chains. How can African countries benefit from these developments? The key will be to leverage expanded foreign trade and investment to achieve sustainable private sector–led growth. Several domestic policy areas will need particular attention.

Reducing the cost of investing and doing business. African countries can attract and use more capital only if they significantly reduce red tape and other regulatory impediments to private activity. Although progress has been made in recent years, sub-Saharan Africa lags other parts of the world in terms of investment and business climate (see Table 2). According to the latest assessment of the International Finance Corporation—which tracks indicators of the time and cost to meet government requirements in business start-ups, operation, trade, taxation, and closure—24 of the 30 countries with the most costly business environment are in sub- Saharan Africa. A business-friendly environment would also incorporate nondiscriminatory taxation, customs regimes that facilitate the movement of goods and services, and regulations that make the labor market more flexible while safeguarding the rights of labor. Because the poor quality of its infrastructure—particularly energy and transportation—is one of the major constraints to doing business in Africa (World Economic Forum, 2007), improving infrastructure is critical if African countries are to benefit from the globalization of business and industry.

Table 2

Investment climate

Sub-Saharan Africa is the most difficult region in the world in which to do business.

Economy	Ease of doing business rank
Top-ranked countries	
Mauritius	27
South Africa	35
Namibia	43
Botswana	51
Kenya	72
Ghana	87
Bottom-ranked countries	
Burundi	174
Republic of Congo	175
Guinea-Bissau	176
Central African Republic	177
Democratic Republic of Congo	178
Average by region	
East Asia and Pacific	77
Latin America and Caribbean	87
South Asia	107
Sub-Saharan Africa	136

Source: *Doing Business 2008*, International Finance Corporation.

Note: The higher the ranking, the higher the cost of doing business in the 178 economies covered. The rankings do not take account of such variables as quality of infrastructure or crime rates.

Leveling the playing field. During the 2006 Forum on China-Africa Cooperation, African and Chinese leaders reiterated their intention to forge a new type of strategic partnership based on equality and mutual benefit. It is thus important for African countries to ensure that competition for their projects is fair and to treat all foreign investors equally. Increasing the transparency of all state-sponsored transactions by implementing the Extractive Industry Transparency Initiative and similar international initiatives will be particularly helpful in fostering sound governance and ensuring more efficient use of Africa's valuable resources.

Managing public finances efficiently. This would include prioritizing all infrastructure projects—including those proposed by others—using best practice cost-benefit analysis, separating project development from financing, ensuring that bidding on tenders for projects is truly competitive, and making financing decisions on the basis of a careful assessment of the most favorable terms. Favorable terms means, among other things, avoiding the use of side transactions that make it difficult to compare financing options.

Preventing the accumulation of unsustainable debt. African countries face a dilemma: they need major financing to build their infrastructure and productive capacity, but their inadequate production and export bases limit the amount of external financing they can handle. Addressing this constraint will require prudent debt management and closely linking debt finance to the potential for productive, possibly foreign-exchange-generating, capacity. Clearly, both debtor and creditor countries have a responsibility to minimize the vulnerabilities arising from debt-creating capital flows to African countries.

Safeguarding the environment. The international trade of many African countries is based on rich but largely nonrenewable natural resources. As illustrated by China's own development path, a country may pay a heavy price unless the environmental impact of exploiting resources is dealt with early on and is mitigated by good planning, high standards, and firm regulatory oversight (World Bank, 2007).

Moving up the value chain. Achieving sustained growth will require African countries, particularly in sub-Saharan Africa, to diversify exports and move from being pure exporters of raw materials to processing or otherwise adding value to those raw materials. There are no substitutes for reforms to reduce domestic barriers to entry and exit and to address critical supply constraints. Many Chinese enterprises have fresh experiences in moving up the value ladder in their own fields of business. Partnerships between African and Chinese firms may facilitate technology transfer, add value to African exports, and help African firms position themselves to benefit from world markets, not least the rapidly expanding Chinese market.

At the same time that Africa has a responsibility to maximize the benefits of its economic relationship with China and other nations; China has an important role to play in ensuring that its economic partnership with African countries is mutually beneficial. After all, China's spectacular growth has made it an increasingly important player in global commerce and finance, and responsibilities come with influence. In particular, increasing disclosure about aid flows would help African countries harmonize donor activities. Aligning assistance with the priorities those countries have identified in their poverty reduction strategies would also make aid to them more effective. Lending terms and volume need to be consistent with the low-income country debt sustainability framework many African countries now use. Finally, increasing local sourcing of parts, equipment, and labor to promote effective technology transfer would help boost income growth in sub-Saharan Africa and hence the size of that market, benefiting both China and Africa.

China's commitments in Africa

Project	Country
14 commercial agreements	Various countries
Preferential Loans & Credits	Sino-Africa trade
Credit line in return for 10 000 barrels a day	Angola exports 25% of its oil production to China Direct flights to Beijing are being discussed Establishment of Chinatown in Luanda
Tanzam railway	Tanzania & Zambia
Muglab Oilfields	Sudan Imports 50% of oil
Chambezi copper mines	Zambia

Exhausted oil reserves	Gabon
Telecommunications	Ethiopia
Space satellite	Nigeria
Road Mombasa-Nairobi	Kenya

He Wenping is deputy director of the Department of International Relations in the African Studies Section of the Chinese Academy of Social Sciences in Beijing. “Common sense about human rights and sovereignty is only one of the common values shared by China and Africa,” she said. “There is no doubt that China’s success in Africa has partly benefited from it, and those common values have laid solid foundations for further promoting bilateral relations in future.”
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Rwanda’s former minister of finance and economic planning and President of African Development Bank, Donald Kaberuka, says: “It’s a different way of doing business” - an alarming prospect for NGOs already fighting cynical western practices in Africa. In the past international organisations such as the World Bank have been criticized for making loans to countries in need conditional upon non-negotiable demands. Now the situation is reversed, with China granting unconditional, instant credits that encourage white elephant projects, without concern for financial transparency.

Chinese arms sales are a cause for concern. In the late 1990s China made more than $1bn out of the war in Eritrea. It has also been suspected of using Sudan as an outlet for military technology. It is still militarily involved in Zimbabwe, another country cold-shouldered by the West (10). Chinese military attachés have been concentrated in member states of the Southern African Development Community. According to a US analyst: “During the cold war, Chinese arms transfers to Africa were motivated by ideology. Now, profit is the main objective”

What the Chinese see as a win-win situation - a new economic game in which neither partner can lose - can also be seen as fresh neocolonialism disguised as South-South development. Some African analysts are wondering about the limits of Chinese trade policy and the direct competition to Africa’s economy from specific Asian products, from textiles to steel. South Africa was China’s first African partner and, as a gesture of solidarity, broke off relations with Taiwan in 1997. Now, according to the deputy chairman of the South African Institute of International Affairs, Moeletsi Mbeki, China represents “both a tantalizing opportunity and a terrifying threat”. It is a familiar story: “We sell them raw materials and they sell us manufactured goods with a predictable result - an unfavourable trade balance against South Africa”

South Africa’s trade deficit with China has risen from $24m in 1992 to more than $400m. In September 2004 a member organisation of the powerful Congress of South African Trade Unions threatened to boycott anyone selling Chinese products, which it blamed for rising unemployment. The problem can be seen in the market stalls of the Senegalese capital Dakar, where cheap Chinese imports, from shoes to medicines, elbow rival products aside, while the textile workshops of Lesotho are threatened by the expiry of the multifibres agreement last January

The line of credit given to Angola - at 1.5% over 17 years - might look disadvantageous to China in the short term, but Chinese companies will secure the lion’s share of lucrative contracts for national reconstruction. Local people are unhappy. As independent economist José Cerqueira pointed out: “There is a condition in the loan that 30% will be subcontracted to Angolan firms, but that still leaves 70% which will not. Angolan businessmen are very worried about this, because they don’t get the business, and the construction sector is one in which Angolans hope they can find work”

China has responded with promises, handouts, allusions to the spirit of Bandung (see Bandung’s lost illusions, page 14) and symbolic gestures: since 2000 it has cancelled $10bn in bilateral debt. The Chinese government’s African Human Resources Development Fund pays for 10,000 Africans to be trained in Beijing

From Liberia to the Democratic Republic of Congo, China is increasingly involved in peacekeeping operations: in 2004 it contributed more than 1,500 troops to the UN presence across the continent. While acknowledging that any final decision rests with the African Union, China has publicly supported the three African candidates - South Africa, Egypt and, in particular, Nigeria - for a permanent seat on the security council.

China will concentrate its cooperative efforts in countries where it recognises high potential, whether it is a matter of raw materials, potential markets or diplomatic influence”

How will Africa’s traditional partners adapt to the Chinese presence, and how far will they be prepared to go? “It is normal and natural that China’s involvement in Africa could lead to some conflict of interest with the former colonial rulers,” He Wenping says. “I don’t think we should worry too much about it. To help African people become better off and benefit from globalisation is the common object and aim of people and countries around the world. The Chinese people and government would very much like to contribute to this aim. And history shows that this must be a hard and long journey.”
According to the IMF, Africa should experience growth of 5.8% in 2007, the highest for 30 years. In part this will be due to China. But is Africa, once a sideshow in the cold war, destined to be at the centre of an intensifying trade war?

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