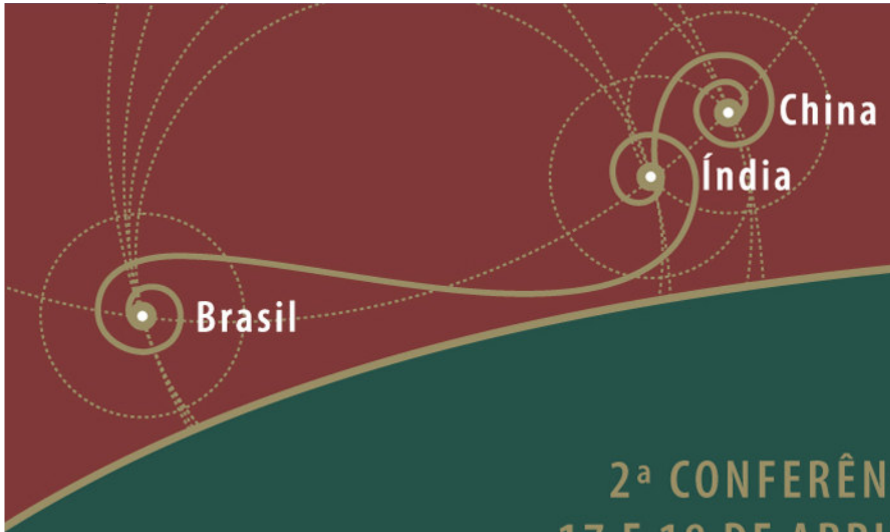

CONSELHO EMPRESARIAL BRASIL–CHINA
中国-巴西企业家委员会

2ª CONFERÊNCIA INTERNACIONAL
17 E 18 DE ABRIL DE 2007 – SÃO PAULO

DESAFIOS EMERGENTES

a ascensão econômica de China e Índia e seus efeitos para o Brasil

China
Índia
Brasil

CONSELHO EMPRESARIAL BRASIL-CHINA
中国-巴西企业家委员会

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The impact of Chinese and Indian Growth:

The African Case

China-Brazil Business Council Conference, 17-18 April 2006

Neuma Grobbelaar

Outline

- Introduction
- Understanding the African context
  - Nature of African economies
  - Recent growth: SA, commodities
  - Response of Investors
- India and China
  - Motivations for investment & economic engagement
  - Differences in engagement
  - South Africa and China
- Challenges in dealing with China
- Conclusion

Introduction

- No doubt that rise of China and India having enormous impact on African continent
- Effect of China felt in each of Africa's 53 states, from Cape to Cairo, Luanda to Mombassa, India less so
- Most visible is penetration of African markets by affordable Indian & Chinese goods, however, resource boom sea-change across Africa
- But also in this area engagement of Indian elephant & Chinese dragon with African lion potential to fundamentally change longer-term development path
- **IF** engagement infused by mutually beneficial relationship based on partnership

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Introduction cont

- Focus on impact of China & India on development of private sector in Africa
- Continent's much neglected and marginal private sector has pivotal role for Africa to overcome developmental backlog, global economic and political marginalisation
- Not grand political scheme – rather interest of Africa's 870 million citizens: sizeable market – problems related political, economic & social fragmentation.
- Two fundamental questions:
  - Is entry of China & India leading to development of African economy in sustainable fashion, or short-term commodity-based business boom leaving Africa depleted and debt-ridden?
  - Deeper, fundamental level: quality & nature of engagement (contributing to robust development of African private sector in line with global best practice?)

African context

- Home to the largest number of LDCs – making Africa most underdeveloped region in the world
- Important: Africa is not homogenous continent, 53 states are diverse: topography, geography, economy & polity
- Tendency to look at Africa as a country instead of the continent that it is **BUT** several characteristics that African economies have in common.
- **First:** Small size of individual markets (number of consumers + low level of disposable income): size of sub-Saharan economy (minus Nigeria and SA), $3.6bn = US town of 60,000, result: foreign business activity highly visible, impact immediate, resonates through entire economy

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African context cont

- **Second:** Dominance of informal sector in most African countries. Informal trading and subsistence agriculture – backbone of African economies, also largest employer, 80% of Mozambican population employed in subsistence agriculture, imp livelihood strategies, not contribute to growth of economic pie – foreign FDI thus welcome.
- **Third:** Neglect of private sector since independence. Private sector in its infancy compared to Asia, Latin America, many gov officials deeply suspicious role of private capital, overhang of centralist & command-driven practices, despite adoption of free-market principles since 1990s. Continue to colour way foreign investors are viewed, out of kilter needs of modern, globally integrated economy of firm.
- **Fourth:** Intersection between aid dependence, trade & investment and their impact on economic development. Trade, aid & investment from North, enforced by preferential trade agreements, continue to wield huge influence on T&I flows in region. Rapidly changing with India & China's expanding economic relationship, but most African economies very aid dependent (60% of gov revenue from aid + borrowing) – introduces dimension to influence + engagement on continent

African context cont

- Other characteristics: export of primary goods, skills deficit, vulnerability to shocks, absence of hard & soft infrastructure, political and regulatory uncertainty – very challenging business environment
- But: many countries have worked on political and economic governance, emergence of more reformist, technocratic political elites in conjunction democratic wave since Cold War, has lead to slow, but remarkable change.
- **African Growth improved:**

  From 2.1% (1985-1995) to 3.7% (1995-2003); 4.1% (2003); 5.1% (2004); 5.6% (2005); 5.4% (2006); forecast 6.2% (2007) – average of 4.5% in 1st 5 years of millennium, strongest, consistent performance since 1970s.

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What is driving African growth?

- **South Africa:** largest + most diversified economy doing well, GDP of $239bn 40x larger than average sub-Saharan economy, 25% of African economy, 1/3 of SSA, 2/3 of SADC, breached 5% GDP growth in 2005 (1% slowdown in SA, ½-3/4 % slowdown in rest of Africa), SA significant investor in rest of Africa
- **Oil & mineral commodity boom:**
  - oil exporters(2000-05): Angola (9.8%), Chad (13.9%), E Guinea (24.6%), Nigeria (5.3%), Sudan (6.1%)
  - non-oil exporters: 10 countries average growth rate about 5%
- **Market reform** since 1990 important, **BUT** resource hunger of China & India, best terms of trade for oil +mineral exports in many decades

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Foreign Investor Response

- WIR total FDI inflows to Africa increased to $31bn (2005), historic year-on-year increase 78% **BUT** still only 3% of global FDI flows. Africa still at margins of global economy.
- How about Asia? Asian FDI flows to Africa $1.2bn per annum (2002-04); Singapore, Malaysia & India top sources of FDI, however, China increasing in prominence.
- China FDI stock of $1.6bn in 48 African countries (only 3% of total Chinese FDI outflows), whereas India $1.9bn (2004).
- What is all the fuss about?

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Why is Africa important to India & China?

- **First:** offers an underdeveloped market for low-technology, but cost-effective goods + services. 87% of China's exports = equipment, machinery, textiles, clothing; 51% of India's exports manufactured products; but also preferential access to third markets (US & Europe)
- **Second:** important source of resources, China = net crude oil importer in 1993, 2nd largest oil importer globally, 25% of oil & gas from Africa. India = sources 70% of oil on int market (50% from Africa). China's African imports: oil + gas (62%), ores + metals (17%), agri (7%). India's African imports: ore + metals (61%) - gold (52%), agri (19%)

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Why is Africa important to India and China?

- **<u>Third:</u>** Weight of Africa in multilateral institutions. China = permanent UNSC member, India is aspiring. China's peaceful rise suggests 'system maintainer', rather than 'system wrecker', but both mooted interest in becoming 'system shapers'.

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The Status Quo

China

- Engagement part of 'going global' strategy
- Part of high-level shuttle diplomacy, kick-started in 1996 (Jiang Zemin), 5 principles of Sino-African engagement, high point FOCAC
- By 2005: 700 projects, only small number $10 million

India

- Significant diaspora – East + Southern Africa, West Africa
- Engagement shaped by own developmental challenges + democratic value system
- Technical assistance: health, education

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The Status Quo

China

- Debt relief of $1.2bn without any conditionalities, preferential access to LDCs
- 11 trade + investment promotion centres across Africa
- Bilateral credit lines in the form of tied aid

India

- Exim Bank policy (2002-2007) launched ‘Focus Africa’ - export promotion
- India only 6 small missions covering West & Central Africa, against 22 large Chinese missions in same region, India closed 4 missions

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The Status Quo

China

- Sino-African trade grown from $11bn (2000) to $40bn (2005), China hopes to grow bilateral trade to $100bn (2010)
- China far less risk averse

India

- Indian-African trade has grown from $976m (1990) to $9.14bn (2005), 10-fold increase
- India admits at least decade behind
- Relies on Indian diaspora & much more risk conscious

South Africa and China

- As Africa's largest economy, preferred strategic partner for China
- Diplomatic relations only established in 1998
- China has grown from 16th most important trading partner (1995) to 5th position (2004)
- SA holds substantial trade deficit with China of \$2.5bn (2nd largest after Germany) - China disputes this
- Chinese investment in SA (figures disputed), but driven by attractive, sophisticated market in own right + platform to service operations in rest of Africa

South Africa and China

Chinese investments:

- Commercial banking (4 Chinese banks servicing clients in the region); electronics + telecommunications equipment; light manufacturing; mining (Sinosteel in chrome mining in Limpopo province* Xstrata alloys); shipping & automobiles

- Reasons for low investment:
  - SA is not oil-rich
  - China does not need to own resources in SA market to gain access because of country’s strong legal + physical infrastructure
  - SA opportunities already well-developed, SA capital & expertise

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South Africa and China

South African investment in China

- Reached R4.5bn in 2005
- SA flagship companies: Kumba Resources (built iron ore terminal Qingdao Port in China in 1994), Naspers (instant messaging service + largest Beijing-based newspaper), SABMiller (2nd biggest brewer in China – 33 breweries), Standard Bank (service clients in mining sector with project financing & risk trading from Hong Kong
- Petro-chemical giant, Sasol in talks to establish two coal-to-liquid plants in Shaanxi Province & Nigxia Hui Autonomous region, technology cost-effective with high crude oil prices, but intellectual property rights

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China, South Africa & Africa

- China's engagement in Africa offers biggest potential for collaboration, but also conflict of interest with South Africa
- SA construction companies complain about uneven playing field, consistently outbid by Chinese companies – now tend to focus on Middle East & Gulf + have urged SA government to introduce tied aid policy
- SA government is resisting – important to note that SA investment-drive is private sector- led, companies are expected to shoulder all risk, even DBSA funds are untied, because of SA gov fears of being labeled as new colonisers of Africa
- Is the complaint warranted?

Chinese Construction in Africa

- 2003: 48 688 construction companies in China, employing over 24 million, 7% of GDP, further 50% of economic activity, no surprise that China has begun concerted expansion drive
- Competitiveness in Africa driven by low wages & use of Chinese labour
- Food & housing + $1 stipend a day vs food & housing + $3-4 stipend day for low-skilled local Angolan worker, Chinese engineer earns $130 a month in contrast to $120-150 per month for Angolan construction worker
- Other reasons: Shift system (1 bed, 2 workers policy), low absentee levels (other companies 20%, increase cost by 1/5), better levels of training

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China, South Africa and Africa

- SA retailers have to work more innovatively and smartly to find niche between expensive European products & cheap Asian imports, invest in establishing reputation for good quality, but cost-effective goods & services
- There is role for cost-effective Chinese + Indian inputs, MTN relied on Chinese telecoms infrastructure to roll out network in Nigeria in more cost-effective manner with spectacular benefits for the company & good service to customers
- Room for synergistic collaboration, but SA companies insist on equality of treatment of bidders + best corporate practice to labour practices, operations, environmental and social impact and standards – good for companies + business environment in the long run

Challenges in dealing with China

Labour

- Persistent use of lowly-skilled Chinese labour in labour-intensive construction projects, inexplicable
- Little transfer of technology or skills
- Influx of 'illegal immigrants'
- Angola: Minister of Energy claimed 3m Chinese workers may move in because of number of projects – counterbalance against total population of 13m
- Became election issue in Zambia

Infrastructure

- Many projects geared towards facilitation of extraction of raw materials
- Building of 'presidential palaces' not productive
- However, rebuilding of Africa's railways, roads, ports at cost & completion levels that outperform others – making important contribution to opening-up of African economies
- Chinese companies also willing to take on projects avoided by other investors, despite profitability concerns

Challenges in dealing with China

Dumping of products

- Chinese companies criticised for flooding markets with cheap products and undermining light manufacturing sector
- However, important role to play in providing more cost-effective products to customers who could not previously afford them

Engagement in oil-producers

- Biggest concern about manner of engagement in autocratic oil states in Africa
- In Sudan criticised for purchase of Chinese arms for use against civilian population from oil revenue (Southern Sudan & Dafur)
- Granting of concessional loans to Sudan described as immoral, to Angola in face of IMF pressure as amoral

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Challenges in dealing with China

- Concern that this heralds development of a two-tier approach to Africa versus the rest of the world
- E.g., China created two companies PetroChina and Sinopec that has listed successfully on NYSE with its stringent environmental and social responsibility requirements – thereby ringfencing African operations from rest of the world
- However, came under scrutiny from US shareholders in mutual investment insurance funds who called for divestments from both companies because of the involvement of parent companies in Sudan
- This might see change as China becomes more integrated into global economy and is forced to address these concerns
- However, while China is blocked from acquiring larger Western oil majors, such as publicised bid for US-owned Unocol, will continue to follow high-risk acquisition and investment strategy.

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Conclusion

- Chinese & Indian engagement comes at time where Africa is giving much more attention to good political and economic governance
- Release of China's Africa Policy in 2006 seems to be a response to growing African concerns
- But for Africa to avoid being stuck in the raw material corner known for its boom and bust cycles, needs to engage China & India more effectively
- Chinese & Indian infrastructure providing platform, but African governments need to focus more attention on positive spillovers & linkages with domestic economies

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Conclusion

- Africa has opportunity to fundamentally change course of its development trajectory.
- However, will only happen if Africans insist that the best practice private sector model becomes the norm rather than the exception.
- Will only happen if Africa does more to improve investment climate: corruption, regulatory uncertainty, political stability, transparency & bringing down costs and risks of doing business on the continent.

Thank you

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