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The Impacts of China's Economic Rebalancing on Africa

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Abstract:

The economic development in Sub-Saharan Africa (SSA) indicates an improvement of living standards with an average growth rate hovering around 4.5 percent over the past decade. SSA is experiencing a remarkable change with structural reforms in governmental macroeconomic policies with reliable public institutions supported by private sectors. This has open up the business horizon and prospects of SSA to take part in global business. On other hand China's interest in Africa's natural resources, its external economic policy, inexpensive commodity prices and cheap labor market is germinating a new business platform in many nations of SSA. Thus, China has become the largest trade partner of Africa in 2015. This trade with a modest beginning of about 2.5 percent in 1980s has

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reached to a staggering figure of 25 percent in 2015 and this is expected to grow in near future. China's business interest in Africa is largely concentrated on its growing energy demand in domestic fronts of which 33 percent is imported from SSA. On other hand the heavy infrastructure fund requirement of Africa is made available largely by EXIM Bank of China, China Development Bank and the People's Bank. Further, large numbers of private Chinese enterprises (around 2230) in SSA have not only created a competitive consumer base but also have open up new channels of capital investment in these transition economies (UNCTAD 2014; Shen 2014). The effort of China Africa forum regarding the Chinese business investment in SSA countries has been widely acknowledged. The bilateral and diplomatic relation of Chinese leadership's with SSA countries has also been highly praised recently in Africa.

Key words: FDI inflows, FDI stocks, Trade Projections, Economic Rebalancing, Consumption Oriented Growth Model, Natural Resource Exports

JEL Classification: F17, F21, F34, F35, N77, O55

1.0 INTRODUCTION

The growth rate of China has recently slipped down to 6.7% in first quarter of 2016 after experiencing a series of high growth rate of more than 7% in the past five years. This was because of the strong services and consumption offset the weaker manufacturing and exports. In addition a surplus production potential emerged in Chinese market because of excess of capital stocks during 2005 to 2011 with an exception of 2008, resulting in reduction of net return on capital. The strength of consumption although increased in 2015 is low by international standards. This is a right move if one compares the effort of Chinese government to redirect the economy towards an internal consumption driven sustainable model with substantial participation of competitive private sector instead of an investment and export oriented growth model. The objective of Chinese policy makers is to realize a paradigm shift of internal economy as well as to support the international trade and investment flows for both the advance and transition economies.

China has already established its hegemony in World trade. However, the traditional dynamics that determined China-SSA economic relation is gradually changing. China's growth has exaggerated commodity prices by bringing change in consumption demand imperatives. This has affected the global markets as well. The labor cost in SSA is great attraction for global investors including China beside the availability of virgin market. This has invited many Chinese firms and producers to establish their business in SSA market as the labor rate has increased three folds in China in past eight years. This paper tries to search the new economic rhetoric between China and SSA, the essential dynamics and the effect of China's economic rebalancing on SSA nation's trade and investment. The paper uses available information from the Government of China, China-SSA trade and foreign direct investment (FDI) and database of international organizations such as World Bank, UNCTAD and etc.

2.0 REVIEW OF LITERATURE:

China is one of the biggest trade partners of Africa with a trade value of US$300 billion in 2015 and expected to rise US$400 billion by 2020 (Fourth China-Africa Industrial Forum _CAIF, 2015). Europe was the largest trade partners of Africa for quite a long time. This position was recently replaced by China. African trade either with Europe or with China is not symmetric as African countries imports huge amounts consumer items and capital from while exports mostly agricultural commodities, oils, minerals and some natural resources especially primary commodities. The change in regional dynamics in China with a changing international commodity prices will have certain impact on Sino - Africa trade. Africa has not able to reap of the benefits of its exports of agricultural goods and oil & other natural resources in the Chinese market even though it enjoy certain comparative advantage in these products. China has brought momentum to the increased growth imperative in many African countries especially those bestowed with abandon natural resources. Unlike EU and USA, African countries trade to other countries market has never been affected by awesome Chinese exports. The reason is the wide export profiles of Africa. Rather it has act as a balancing one. But Chinese increased exports to Africa have exerted huge pressure on the African domestic producers although the consumers have been benefited because of varieties, quality and price. There are several reasons of this increased competition. Notable among them are the appreciation of real exchange rate in Africa and pegging of their currencies into certain hard currencies especially to Euro, USD and Pound Sterling, the outpouring exports of natural resources and primary commodities & raw materials as well as huge amount of financial assistance received by SSA countries from international donors including China. Recently African firms are facing the risk of the fierce competition of from their Chinese counterpart.

SSA countries enjoy comparative advantage in certain agricultural products, ores and metals. But they are losing their competitiveness in all most all the sectors including agriculture except in certain natural resources. Thus these nations have not been able to take the benefits of this comparative advantage in Chinese export market. The revealed comparative advantage of exports of SSA countries manufacturers is the lowest among all types of export products. This indicates presence of logistic barriers and structural incompetence in SSA market. Further, high tariff rates on agricultural imports in China create additional hindrances for expansions of SSA market in China.

Foreign Direct Investment (FDI) flow to SSA is gradually gaining momentum. Chinese FDI stock in SSA reached nearly US$24 billion in 2013, a 50 percent growth between 2004 and 2013 (MOFCOM 2003-2014; Copley, Maret Rakotondrazaka, and Sy 2014). When majority of foreign investors left Africa at the beginning of 2008 global economic crisis, Chinese firms inspired by the government started investing in Africa. China focused mainly on mergers and acquisitions (M&As), commercial lending and infrastructure financing, making good investment in oil and minerals, financial services and manufacturing. Initially China made huge investment in Nigeria, South Africa, Sudan, and Zambia. Now Chinese investment is found everywhere in SSA. Recently Chinese manufacturing firms have invested heavily in countries like Ethiopia, Kenya, Sudan, South Africa and Tanzania. These investments have made significant contribution to job creation in SSA countries.

The Chinese FDI inflows to SSA was 3.1 billion US$ in 2013 (Ministry of Commerce of People Republic of China). This was 7% of the total FDI flows to the region and second highest after USA with a total FDI flows of 7.3% around that period. Chinese FDI stocks were 5% of the total FDI stocks of SSA with a value of 24 billion US$. The financial transaction of China in Africa is difficult to calculate. But Chinese banks have provided huge credit to Africa approximately US$52.8 billion during 2003–11. This is approximately 2.8 percent of China's GDP. The investment flows from SSA countries to China is negligible although there is an upward tendency. South Africa, Mauritius and Seychelles are the SSA countries with a substantial investment in China. However, Mauritius and Seychelles are offshore financial centers of China. The investment flows from SSA countries to China are mostly characterized by trading concerns.

Chinese investments are diverged in nature and well spread globally. However, big Chinese firm have not established their identities in SSA countries with exception of few big firms such as the Huajian shoe factory in Ethiopia as well as the Yuemei group which processes mineral ores and the produces liquid natural gas in Nigeria. Chinese firm are recently relocating some of their production line in SSA countries as the domestic labor costs in China is gradually increasing. Further, SSA countries not only provide inexpensive labor force but they are strategically located near to many European market. But only few Chinese firms have exploited this advantage. The presence of Chinese manufacturers has not been able to bring the expected economic transformation in many of the SSA countries' economies. The inherent nature of these economies is one of the main reasons as why these economies could not able to reap of the benefit of large economies of scale.

The Chinese private investment in SSA countries although a recent occurrence but expected to bring certain change in the economic development of these nations. However, only few countries such as Nigeria, South Africa, Sudan and Zambia have able to attract private Chinese investments in constructions and manufacturing. In many African countries such as Tanzania and Ethiopia although the Chinese firms are able to create job and enhancing the productivity of the private sectors but at the cost of competition with local market.

Chinese economic rebalancing with a more focus on domestic consumption rather than external investment will require certain policy design which in long term may be able to create comparative advantage in SSA. But at present only few African countries have been able to take advantage of large Chinese investment with exception of resource sectors. It is expected that the shifts in Chinese economy will also pull down the resource imports such as oils and mineral from major resource based African economies. The rebalancing of Chinese economies is oriented towards an increase in wage rate in domestic market in China. SSA countries can take benefits by making substantial investments in cheap labor- intensive industries, the benefit of which Ethiopia is already deriving. However, this requires relatively skilled labor force, a proactive government policies towards Chinese investments in infrastructure. This paper focus on how SSA countries could take advantage of the abundance of opportunities provided by Chinese government through trade and investment ties.

3.0 OBJECTIVE:

The objective of this paper is to find out the effect of economic rebalancing of Chinese economy on the trade and FDI flows to SSA countries.

4.0 METHODOLOGY:

A theoretical approach has been adopted to study the trade and investment between China and SSA.

4.1 Projection of China -SSA Trade:

China- SSA trade is projected taking into account the compound average annual growth rate of trade for the past periods and applying the projected growth rate formula as mentioned below:

$$\boxed{\mathbf{T_{pn} = T_{n-1} + (T_{n-1} * X\ \%)}}$$

Where T_{pn} = Trade Projection for n –year
T_{n-1} = Trade in n-1 year
X % = Compound Average Growth Rate of trade for a time period.

5.0 CHINA - SSA TRADE

China is a major trading partner of SSA along with European Union and the United States. SSA trade was more oriented towards western markets since a long time. However the equation is now tilting more toward China as its products are less expensive in comparison to USA and Europe. The trade flow of China to Africa is enormous. It has grown vigorously in the last decade with a CAGR of 22.7 percent during the time period 2004 to 2014. The total value of trade has increased tremendously to188.8 billion USD in 2014 from a meager amount of 3.01 billion USD in 1995 as presented in Table 1. However, from Table 2 it is clear that the share of SSA in Chinese trade is abysmally low and is only 3 percent even though the growth of SSA's export to China is faster than the growth of its imports. Chinese exports to SSA are more varied although SSA's export to China is still concentrated upon the primary commodities and renewable and non-renewable resources. Resources exports from SSA to China constitute more than 75 percent in between 2007 to 2014. This creates a more asymmetric trade relationship between China and SSA. Chinese imports from SSA are concentrated on natural resources such as oil, uranium, aluminum, zinc, phosphates, copper, nickel and gold and certain other renewable sources. The agricultural commodities category includes timber, rubber, cocoa, coffee, cotton, fish and cashew nuts. But SSA's imports from China varied from consumer goods, clothing, textiles, and consumer electronics to capital goods such as machinery, commercial electronics, transport equipment and etc. In certain categories of exports such as primary agricultural commodities, oil and minerals and certain non-oil energy products, SSA enjoy comparative advantage in Chinese market. However, in manufacturing products SSA has negative comparative advantage in Chinese market.

Table 1: China's Trade with SSA during 1995 to 2014

Year	*China's Import share in total product of SSA*		*China's Export share in total product of SSA*		*China's trade in total product of SSA*
	In %	*Value in Billion USD*	*In %*	*Value in Billion USD*	*Value in Billion USD*
1995	11.92	1.24	51.29	1.77	3.01

Year	*China's Import share in total product of SSA*		*China's Export share in total product of SSA*		*China's trade in total product of SSA*
	In %	*Value in Billion USD*	*In %*	*Value in Billion USD*	*Value in Billion USD*
1996		1.36		1.87	3.23
1997	12.26	2.32	53.60	2.32	4.64
1998	12.41	1.29	58.17	2.99	4.28
1999	13.97	2.18	61.19	2.75	4.93
2000	18.35	5.34	66.26	3.55	8.89
2001	18.96	4.50	69.14	4.37	8.87
2002	21.32	5.09	70.98	4.96	10.05
2003	22.94	7.88	73.68	7.42	15.30
2004	25.64	14.53	75.74	9.85	24.38
2005	27.89	19.22	76.92	13.29	32.51
2006	27.35	26.31	79.40	18.88	45.18
2007	30.63	39.96	80.74	26.45	66.41
2008	31.12	51.55	81.77	36.53	88.07
2009	30.63	37.97	81.58	33.21	71.19
2010	34.41	59.88	82.69	43.78	103.66
2011	31.96	87.00	84.24	55.78	142.78
2012	33.54	100.95	83.91	61.51	162.45
2013	33.11	108.59	83.65	67.40	175.99
2014	32.8	110.21	84.69	78.59	188.79

Source: World Integrated Trade Solution Data, World Bank, March 2016.

Table 2: SSA's Import and Export with China during 1995 to 2014

Year	*SSA Share in China Import (in %)*	*SSA Share in China Export (in %)*
1995	0.94	1.19
1996		
1997	1.63	1.27
1998	0.92	1.63
1999	1.31	1.41
2000	2.37	1.42
2001	1.85	1.64
2002	1.73	1.52
2003	1.91	1.69
2004	2.59	1.66
2005	2.91	1.74
2006	3.32	1.95
2007	3.45	2.17
2008	4.55	2.55
2009	3.78	2.76
2010	4.29	2.78
2011	4.99	2.94
2012	5.55	3.00
2013	5.57	3.05
2014	5.63	3.36

Source: World Integrated Trade Solution Data, World Bank, March 2016.

Even though there exist many asymmetries in SSA and China regarding the nature and characteristics of trade but the future volume of China and SSA trade is expanding. The China-SSA trade, if projected at the current decadal growth rate (presented in Table 3) indicates a robust figure. This robustness implies China's interest in SSA economies even though there is a rebalancing in Chinese economies more towards internal consumption rather than external orientation.

Table 3: China SSA Trade Projection*
During 2015 to 2020

(In billion USD)

Year	*Projected Trade (approx.)*
2015	231.68
2016	284.30
2017	348.88
2018	428.13
2018	525.38
2020	644.72

Authors' calculation

**NB: Calculated at existing compound average growth rate of 22.7% during 2004 to 2014*

China has a genuine interest in SSA's metals, minerals and oils. SSA has also benefited from exports of these commodities to Chinese market. Chinese exports in Europe or in USA market are either unrelated to SSA's exports or comes as a complementary although there is certain evidence where it has created negative impact in SSA countries regional market. Even though SSA's export to China has brought economic development in China, evidence also suggests that China's solid permeation in manufacturing sector in SSA economies has negatively affected the diversification of manufacturing sector in SSA economies instead of bringing an industrial growth. This may in long run pull down the economic growth of SSA. But certainly it has benefitted a major chunks of African consumers and producers those who relied on less expensive

Chinese imports and capital inputs. There is a huge price gap between Chinese products and SSA countries products. Sometime this gap is around 50 percent. When technology transfer takes place from developed countries to transition economies (where wage rate is less) through its subsidiary in the form of inputs or components, it is generally meant to make a finished product so as to export it to another country's market or back to the country from where the input has originated. This helps in building up the capital technology in developing countries as well as introducing the product of these transition economies to an international value chain or to World market. This is a question of helping these countries by presenting their products to bigger market and recognising the dynamics of comparative advantage these countries enjoy. It has a long term benefits for to the manufacturing sector of developing countries. When we analyse China - SSA trade even though the finished product exports from SSA countries to US consumer market is positive, still it is only a tiny percentage of the total trade. This bottleneck is an indication of China's lack of initiative and interest to introduce SSA market in the international value chain.

5.1 Chinese FDI in SSA

As per the UNCTAD 2014 data (Table 4), the major source of SSA's FDI inflows comes from European Union (26%) followed by USA (9%) followed by South Africa, China, India, Singapore and Japan. UNCTAD 2014 reveals a total of 2158 million USD FDI inflows to Africa from China. There is a difference between FDI data of Ministry of Commerce of the People's Republic of China (MOFCOM) and FDI data of Organization of Economic Cooperation and Development (OECD) as MOFCOM data includes private and public financial flows from the mainland China while OECD definition of FDI inflows consider the private investment inflows. MOFCOM 2014 data shows FDI inflows to SSA from China as 3.1 billion USD (2013) which is almost 7% of the total global investment in SSA. Similarly stocks of Chinese FDI in SSA is indicated as 5% of the total FDI stocks of SSA and is valued at 24 billion USD in 2013 (MOFCOM 2014). However, the UNCTAD (2014) data revealed a total of 21730 million USD Chinese FDI stocks in Africa in 2012. This is presented in Table 6. Chinese FDI inflows to SSA have increased substantially from a meager 0.1% of the total GDP of SSA in 2003 to 1.5% of the SSA GDP in 2012. But the FDI stock has increased from 0.37% to 0.78% during the above-mentioned period. Chinese FDI inflows to SSA although is gradually increasing over the years but is concentrated more in few resource countries such as South Africa, Zambia, Nigeria, Angola and Zimbabwe. This is presented in Table 5. State Council of China 2013 data revealed that Chinese investment in SSA is more concentrated in extractive industry (30.60%), finance (19.50%), construction (16.40%) and manufacturing (15.30%). Other sectors accounts for 18.20%. In Other sectors important one are commercial services (5%), scientific research, technology and geological prospecting (4.1%), wholesale and retail commerce (2.7 %), agriculture (2.5%) and real estate (1.1%).

Table 4: FDI inflows to Africa during 2001 to 2012

Year	FDI inflows to Africa in million USD											
	China	Japan	USA	EU	France	UK	Germany	Italy	Denmark	Luxembourg	Portugal	Spain
2001	-	-183	2439	3570	1791	1658	-260	48	23	-	140	-529
2002	-	227	-578	4955	855	3291	-328	42	25	152	-608	429
2003	76	120	2697	9407	1096	5639	-319	51	50	-6	-3	2156
2004	298	382	1612	17359	1346	10735	1367	111	197	269	110	755
2005	292	44	2564	17127	4639	10624	-625	139	345	133	249	1006
2006	417	926	5157	7384	3115	-432	267	1657	-8	438	309	1571
2007	1359	1147	4490	17365	4653	9456	2470	166	-313	1087	-1070	1163
2008	5416	1541	3837	23150	16311	1620	1018	1780	117	1039	-883	1856
2009	1100	-229	9447	15704	-3049	10266	1247	1723	261	1837	-1128	661
2010	1883	-314	9281	18612	4643	12086	1163	1508	480	83	149	-449
2011	2932	522	5127	6904	2010	-5105	1870	3919	242	345	302	503
2012	2158	115	3706	12562	2096	7450	258	3564	-35	10	272	-637

Source: UNCTAD 2014.

Table 5: Chinese FDI inflows to SSA Countries in 2013

Year	*(in million USD)*										
	South Africa	**Zambia**	**Nigeria**	**Angola**	**Zimbabwe**	**Sudan**	**Congo DR**	**Mauritius**	**Ghana**	**Ethiopia**	**Others**
2013	4400	2164	2146	1635	1521	1507	1092	850	835	772	7030

Source: MOFCOM 2014

Table 6: FDI Stock to Africa during 2001 to 2012

Year	FDI Stock to Africa in million USD											
	China	Japan	USA	EU	France	UK	Germany	Italy	Denmark	Luxembourg	Portugal	Spain
2001	-	623	15574	31653	6235	12978	3768	-	534	-	1720	-
2002	-	1227	16040	44821	8372	21785	4441	-	822	-	1097	-
2003	491	2049	19835	60339	11407	30410	5576	-	818	-	1284	2301
2004	900	1623	20356	64448	12760	33510	6842	-	1212	-	1356	2536
2005	1595	1326	22756	69856	16104	35874	6697	-	1116	-	1469	3015
2006	2557	2700	28158	76466	23112	29651	7585	-	1320	-	1810	6304
2007	4462	3865	32607	104134	35385	37095	9293	4866	1222	-	2411	6177
2008	7804	7287	36746	111388	39126	37066	8694	6652	1211	1602	5162	6168
2009	9332	5738	43924	150024	50837	47853	11391	9594	1522	1932	3868	7099
2010	13042	6149	54799	158694	55792	47189	13521	10349	1977	2536	4868	6205
2011	16244	8065	57213	161810	53036	47694	13067	13200	2280	1999	5744	6871
2012	21730	6874	61366	175288	57984	58937	8576	15845	2898	-	6846	6255

Source: UNCTAD 2014.

5.2 SSA's FDI in China

The major FDI flows between SSA and China till now flows from China to SSA and not in the other direction. FDI from SSA to China valued at US$1.4 billion in 2012, which is 1.2 % of the total FDI inflows to China. SSA's FDI to China mainly concentrated in Mauritius, Nigeria, Seychelles, and South Africa. The major sectors of investments are petrochemicals, manufacturing, wholesale and retail industries and other sectors. Mauritius which ranks 15th largest foreign investors of China is the only largest African investor. There is a double taxation agreement between Mauritius and China. Mauritius is also an offshore financial center of China (MOFCOM 2013). Mauritius has the largest numbers of investment projects in China with a total 1657 projects which accounts 54.76% of the total projects of SSA in China as per MOFCOM 2012 data. Other SSA countries those who have major investment projects in China includes Seychelles 877 projects (28.98% of the total projects of SSA in China), South Africa 201 projects (6.64%), Nigeria 67 projects (2.21%), Liberia 20 projects (0.66%), Angola 17 projects (0.56%), Zambia 15 projects (0.50%), Madagascar 11 projects (0.36%), Sudan 11 projects (0.36%), Ghana 10 projects (0.33%), Namibia 10 projects (0.33%) and Others with 4.31% of the total SSA projects in China. All these projects are between the periods 2002 to 2012.

Earlier China interest in Africa was directed basically to avoid the restrictions on Chinese manufacturing products in USA and EU and to secure an easy entry to the Western countries markets through Africa. There were stringent restrictions for Chinese manufacturing products in USA and EU. However, the manufacturing product of SSA countries gets preferential trade treatments in western countries market. But now Chinese focus in Africa is different. The market in China is gradually becoming saturated. Therefore China's interest in Africa is concentrated upon potential utilization of the untapped local consumer markets in Africa rather facing stiff competition in domestic market and also to curtail the cost of production. The cost of production in Africa is low because the labor cost is cheap in China. These conclusions have been mentioned in the 2012 report of China Council for the Promotion of International Trade (CCPIT). Further in China the wage rate of semi-skilled worker is much higher than the wage rate in Africa. Thus China is interested in investing in labor intensive manufacturing sector in Africa as the investment cost is very low in Africa in comparison to China and other Asian countries

6.0 CONCLUSION:

There are opportunities as well as challenges of China's rebalancing. It possesses enormous potential to bring long term payoff to SSA countries economy. As China is reorienting its economy, the demand for certain commodities such as oil, aluminum, iron ores and copper will definitely come down in the World market as China was the major import markets for these commodities for the last 15 years. With decline in demand, price of these commodities are expected to fall in future. This will have an adverse effect in African market and on producers of these commodities. However, Africa needs to restructure and transform its economy. Thus, this rebalancing by China is expected to open up a new platform and horizon for these countries. African nations will be forced to look for re-modelling their growth pattern and diversify their industrial and primary sectors leaving behind the excessive reliance on natural resource exports. This will definitely have a negative impact on government expenditure in these countries. But this is the right opportunities for SSA countries to bring necessary policy changes to enhance the effectiveness of manufacturing and other sectors facing stiff import competition from other countries especially China.

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