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## How can Sub-Saharan Africa turn the China-India threat into an opportunity

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## **HOW CAN SSA TURN THE CHINA-INDIA THREAT INTO A CHINA-INDIA OPPORTUNITY?**

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## 1. INTRODUCTION

The rise of China and India – the Asian Driver economies – is transforming the global economic, political and social landscape. The challenges posed by their rapid growth and global emergence are increasingly at the centre of strategic debates in the large OECD economies. But what of their impacts on other low income economies in general, and sub-Saharan Africa (SSA) in particular? Perhaps these giant Asian economies, confronted with their own challenges in overcoming endemic and deeply-rooted poverty, share common problems and have common interests with other low income economies? Or, perhaps more darkly, the overlap of common interests is thin and the rise of the Asian Driver economies poses more of a challenge than an opportunity for SSA and other low income economies?

The prevailing view is one of mutual interest between China, India and SSA. This is reflected in the widely-used categorisation between North and South (sometimes “the global North” and the “global South” to reflect the fact that both China and India are in the northern hemisphere and Australia is in the southern hemisphere). This broad North-South categorisation captures the divide between high- and low-income countries; it also broadly overlaps with industrial/non-industrial economic structures. It is widely accepted that the inter-group variations (North versus South) are greater than those within groups (within the North and within the South) and that each grouping has broadly common interests. Thus, there are believed to be an identifiable set of interests which Southern economies have in general, and including in their relations with Northern economies.

In this Chapter we will argue that whatever the relevance of this bi-modal North-South configuration in the past, the rapid growth and increasing global presence of China and India challenges the belief in common South-South interests in a number of important dimensions. In particular, we will argue that SSA faces major new challenges to its future trajectories which arise directly as a consequence of the rapid growth of the Asian Drivers. Unless appropriate policy responses are adopted, the “dark side” (that is, threat) may easily overwhelm the “light side” (that is, opportunity).

The discussion begins in Section 2 by identifying four major conventional wisdoms underlying development trajectories in SSA. Section 3 briefly shows how these orthodoxies are affected by the rise of the Asian Drivers. In Section 4 we address the areas in which this new Asian challenge is synergistic for African economies, and contrast these with areas in which Asian Driver-SSA interests are in conflict. Section 5 concludes with a discussion of the broad policy implications for Africa in its evolving relations with the Asian Drivers.

## 2. DEVELOPMENT TRAJECTORIES FOR SSA – THREE ORTHODOXIES

Amongst the range of development orthodoxies governing the policy agenda in SSA, four are both particularly important and are heavily affected by the rapid rise and growing global presence of the Asian Driver economies.

### 2.1. Aid, trade and foreign direct investment should be separated

Economies interact through a variety of different vectors (Kaplinsky and Messner, 2008). The most important of those with regard to low income countries are the three vectors of trade, aid and foreign direct investment. In the Colonial era they were fused and the imperial powers' interests in Africa were closely coordinated. For example, in the immediate post-war period, British Colonies were seen as providers of traded commodities for UK consumers, involving foreign direct investment from UK firms (for example, producing tea in Kenya), with infrastructure to support this trade provided by the UK Colonial Office (roads and ports to transport the tea to the UK). French and Portuguese presence in Africa was coordinated in a similar way. But as Africa was decolonised in the second half of the 20<sup>th</sup> Century, the aid, trade and foreign direct investment vectors were increasingly separated. This separation occurred for a number of reasons. First, there was increasing opposition from African countries who saw this integration as being very costly. For example, tied aid generally led to much higher-cost inputs. Second, new players were entering the field (notably the US) and they complained that the integration of vectors locked them out of the game. Third, there was growing public opposition in the OECD economies against what was seen as a framework for the exploitation of many low income economies. Fourth, multilateral aid grew in importance and the International Financial Institutions (the IFIs) have increasingly insisted on the delinking of aid, trade and foreign direct investment.

### 2.2. Trade liberalisation

The nineteenth century had been an era of rapidly growing trade liberalisation. But after WW1 (which, incidentally was in large part a consequence of the imbalances created by rapid global integration), the world economy turned inwards. From the 1950s, this inward focus was reversed, and the second half of the 20<sup>th</sup> Century saw an era of rapid and sustained global trade growth, in large part arising from, and indeed leading to, the liberalisation of barriers to trade. This trade liberalisation is widely thought to have been one of the major sources of global economic growth.

The intellectual rationale for the positive feedback between trade and growth can be traced back to Adam Smith and David Ricardo (Kaplinsky, 2005). Smith argued that the division of labour was the source of productivity growth, and that the extent of the division of labour was contingent upon the size of the market. Hence a global economy, with very large factor and product markets, provides the ideal context for productivity growth. Ricardo showed how if countries specialised in their areas of relative comparative advantage, countries could gain from international trade.<sup>1</sup> More recently it has been

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<sup>1</sup> The distinction between absolute and comparative advantage is critical here. A country which has the lowest costs of production possesses an absolute advantage. But it may be relatively more competitive in some sectors than others. This is its domain of comparative advantage. Similarly a country may have an absolute

argued that a further benefit derived from global trade is that it spurs technological progress.<sup>2</sup> For these and other reasons, trade liberalisation is at the forefront of current policy agendas.

### 2.3. Industrialisation is the source of long-run productivity growth

Historically there has been a clear association between countries with high per capita incomes and with developed industrial structures. There are sound intellectual reasons to explain this association. First, there has been a long trend for the barter terms of trade to turn against commodities and in favour of manufactures. In other words, the prices of commodities fell by comparison of those of manufactures (Bleaney and Greenaway, 1993; Cashin, et. al, 2000; Kaplinsky, 2009). Second, the income elasticity of demand for agricultural products is low so unlike manufactures where falling prices may in some cases be compensated by rising demand, in the case of primary commodities, aggregate export receipts were stagnant or falling. Third, almost all of the commodities, and particularly agricultural products which are affected by climate, were affected by very volatile prices. Fourth, manufacturing has many linkages to other sectors and is a source of technological learning and deepening. And, finally, many primary commodities have been hurt by the development of synthetic substitutes.

For these, and other reasons, virtually all of the developing world has targeted industrialisation as the prime building block for long-term and sustainable growth. From the 1980s the orthodoxy was augmented in favour of export-oriented growth, particularly of labour-intensive products such as clothing and furniture.

### 2.4. The pervasive growth of standards and codes of conduct

There has been a pervasive growth of standards and codes of conduct which increasingly govern the extent and nature of inter-country relations. These standards are apparent at a number of levels. At the highest level of aggregation they surface in relation to aid, both bi- and multi-lateral aid, where flows are conditional upon a variety of performance measures. Sometimes these reflect economic policies (for example, the Structural Adjustment Programmes of the 1980s and 1990s), and more recently also affect patterns of governance (for example, Paris Club pressures on the transparency of spending; western pressure on Sudan around Darfur). In other cases, these standards may affect the nature of products (for example organic certification; lead-free toys) and/or processes (for example, child labour; fairtrade certification; ISO standards on quality and the environment; EUROGAP standards on agricultural practices).

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disadvantage in all sectors – that is, there are no sectors where it is the lowest cost producer. But the degree of this absolute disadvantage may differ across sectors, and it is therefore indicated that it should specialise in the areas in which it has the least disadvantage.

<sup>2</sup> This, however, is contested by Greenaway and Kneller (2007), who produce evidence to show that firms raise their technological capabilities in order to participate in global markets, rather than as an outcome of participating in global markets.

There have been a number of drivers of these standards which govern inter-country relations. These include governments with respect to aid-conditionality, firms with respect to quality and environmental standards, and civil society organisations with respect to labour and other process standards. The common factor in these standards has been that they emanate *from* high-income countries and are applied *to* low income countries.

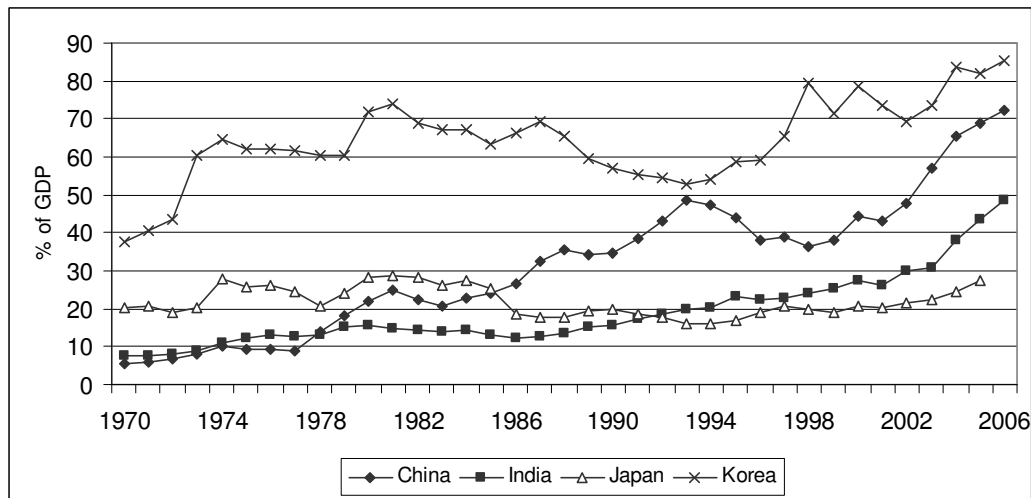
### **3. THE RISE OF THE ASIAN DRIVER ECONOMIES AND THEIR CHALLENGE TO THE THREE ORTHODOXIES**

Each of these four development orthodoxies are challenged by the rise of the Asian Driver economies. Before considering the reasons why this is the case, it is first necessary to explain why, as a general phenomenon, the Asian Drivers are of such historic importance. Since 1979 China has grown at a compound growth rate of 9 percent p.a, and India at a similar rate since the early 1990s. This rapid growth is not unique – Botswana, Hong Kong, Japan, Korea, Singapore and Taiwan had all grown at similar rates for prolonged periods. But all of these rapidly growing economies were small, so that their growth could proceed without changing the basic parameters of production and exchange in other countries. However, China and India together account for almost 40 percent of the global population, so that when they grow very rapidly for prolonged periods, the “small country assumption” has to be suspended. China is likely to become the second biggest economy in the world by 2020, and India the third largest by 2035. Moreover, increasingly this growth has taken a global dimension, and, in particular, China’s dependence on the global economy for both imports and exports has led to a sharp and noteworthy increase in its trade-GDP ratio (Figure 1). The size and the global integration of China (and increasingly India) means that their expansion punctuates and disrupts the equilibrium path of incremental change which has dominated many societies for so long, not least the relatively weak and poor economies in Africa. It is for this reason that these newly emerging very large Asian economies are referred to as the “Asian Drivers”.<sup>3</sup>

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<sup>3</sup> [www.asiandrivers.open.ac.uk](http://www.asiandrivers.open.ac.uk); see Special Issue of World Development, Vol. 36, No. 2, 2008.

**Figure 1: Trade intensity, 1970-2006 (Exports and Imports as a share of GDP)**



Source: Calculated from World Bank, World Development Indicators, Accessed July 30<sup>th</sup>, 2008.

### 3.1. The threat of the Asian Driver to the separation of vectors

It is easy to overestimate the degree of strategic integration of China's advance into the African continent. There are an increasing number of Chinese constituencies who are involved. The role of the central government and state-owned enterprises is evident and widely recognised. But less widely recognised at the provincial governments who are often the drivers of large firm involvement in African infrastructure development. Even lower below the surface are the very many migrants, often in Africa illegally, or filtering away from large companies after infrastructural projects have been completed (Mohan and Kale, 2007). These migrants are rapidly spreading into a range of small scale formal and informal sector activities throughout the continent.

Nevertheless despite this heterogeneity of Chinese actors in Africa, there is an over-riding sense of strategic focus. Particularly in the case of large scale infrastructural and mining projects, this takes the form of the strategic integration of various inputs from China. It is for this reason that it is virtually impossible to unbundle what constitutes "aid" and "foreign direct investment". China's EXIM Bank provides a line of credit, at apparently advantageous interest rates, for a certified set of large Chinese firms to draw on in bidding for large infrastructural projects, such as those in Angola which cover mining, oil and railways. Most of these funds are tied to the use of Chinese inputs, and make intensive use of Chinese skills. Typically, the costs of these large infrastructural projects are 20-30 percent lower than those of western, South African and Brazilian competitors. In the same countries China provides aid for politically sensitive and prestigious projects such as parliamentary buildings (for example, in Mozambique), sports stadia (for example in the Congo) and police training college (for example, in Namibia). Indian operations in Africa are increasingly beginning to take a similar form.

What these strategic operations do is to undermine the accepted wisdom that aid, foreign direct investment and trade need to be unbundled in order to protect the recipient countries (although, as remarked above, it also reflects the demand by those western economies without a colonial presence in Africa to be allowed to sit at the table).

### 3.2 What does the rise of the Asian Drivers do for the logic of trade liberalisation?

As we saw in Section 2.2 above, there are powerful analytical arguments in favour of trade liberalisation. The pursuit of specialisation, coupled with trade in comparative advantage, provides economies with the capacity to increase productivity, growth and employment. It is accepted in this framework that, especially in the case of rapid technological change, there will be frictional costs as firms, regions and countries adjust to meet the challenge of specialising in their areas of relative competence. But these are seen as temporary and as areas where (limited) government support may promote appropriate forms of restructuring.

However, this intellectual edifice is built on two related assumptions, both of which are central to Ricardo's theory of comparative advantage (Kaplinsky, 2005). The first is that production and exchange occurs in the context of full employment. It is this which forces all economies to choose – which sectors should they specialise in? The second is that capital is immobile. If these conditions do not apply, then production tends to gravitate towards the site of absolute advantage, where the costs of production are lowest. At the theoretical extreme, a single economy may produce everything it needs, and indeed supply the world for all these products (if the world can afford to buy them).

Which one of these scenarios is accurate? Are we in a world of mutual complementarity (the textbook outcome) or sustained structural imbalance? A key to answering this is to look at the structure of trade and finance balances in the global economy, and the evolution of global shares in manufacturing.

Looking at the contemporary world, we can observe significant trade and financial imbalances in the global economy. These imbalances surface most clearly at the macro level with regard to the balance of payments flows between China and the western world. China's current account trade surplus has grown from a mere £1.6bn in 1996 (0.3 per cent of GDP) to \$239bn in 2006 (9.1 per cent of GDP) (IMF Balance of Payments Statistics, accessed 24<sup>th</sup> June 2008). A related imbalance is in financial stocks. By mid-2007 China held foreign exchange reserves in excess of \$1.4trillion, with India holding in excess of \$200bn. These reserves compare with the total value of foreign direct investment stock in the US of \$1.7trillion. The flip side of this equation is that both in the case of the US and the UK, the balance of payments deficits are more than six percent of GDP. China is now also the EU's largest trading



partner and ruins a substantial surplus in its trade with Europe.<sup>4</sup> This trade surplus is both a cause and a reflection of the competitiveness of producing in China. It is often associated with the transfer of production from Europe and North America to Asia, hence reinforcing this growing structural imbalance in the global economy.

Table 1 shows how rapidly and significantly Chinese industrial competences have grown over the past two decades (Table 1). In a very short period of time (remember how many decades it took continental Europe to catch up with England, and North America to catch up with Europe), China's share of global manufacturing value added almost doubled from 5.1 percent in 1995 to 9.8 percent in 2005. What this means for SSA, as we shall see in the following section, is that it is being squeezed out of global markets in very many sectors.

**Table 1: Distribution of global manufacturing value added at Constant 2000 Prices**

	Share of the World		Share of developing countries	
	1995	2005	1995	2005
South and East Asia	12.9	19.7	59.5	69.4
of which: China	5.1	9.8	23.6	34.7
Latin America	6.9	6.4	31.5	22.6
Sub-Saharan Africa	0.3	0.3	1.3	1.0
North Africa and West Asia and Europe	1.7	2.0	7.7	7.0

Source: Data provided by Statistics Office, UNIDO, June 2008.

Were the benign mainstream economics model to be correct, this would be a source of only passing concern. The world needs to adjust to Chinese manufacturing prowess and other countries (including those in SSA) should produce products in which the Chinese are relatively uncompetitive, or in time Chinese costs will rise and they will in turn vacate the low-wage labour intensive products for SSA and other even poorer countries to produce. The problem with this model is that the Chinese do not have to choose. Total employment in Chinese formal sector manufacturing is less than 85m and is falling, despite growing manufacturing value added and exports. In the same economy, the numbers of unemployed exceed 100m, with an even larger reserve army of labour in India and other populated Asian economies which are waiting to enter the global market. Put bluntly (since space constraints

<sup>4</sup> These broad numbers hide a larger story, and space constraints meant that this cannot be considered in this chapter. In fact, China is in trade deficit with its region, so the major imbalance in the global economy is not so much between China and the west, but east Asia and the rest of the global economy. Products which surface as "made in China" are often only assembled from capital goods and components sourced from other parts of its region.

limit a more nuanced discussion), China, India and other Asian Driver economies do not have to choose between different sectors of economic activity, but can cover most of the range themselves. For much of their economic life, they live in a world where absolute advantage triumphs over comparative advantage. It is for this reason that global foreign direct investment in emerging markets has crowded into China. Hence – both in regard to a structural surplus in the labour market and the mobility of capital – the win-win outcome of mainstream economics and policy loses its intellectual scaffolding.

In this environment, as we shall see below, trade liberalisation has disastrous consequences for SSA (and for many other economies and groups of workers in other economies). Full trade liberalisation makes it very difficult for most other regions to cope with Asian competition in general, and Chinese competition in particular. The oft-expressed mantra that “all the developing countries need is a level playing field” looks the wrong way. It focuses on agricultural protection in the rich northern countries, and ensuring access to developing country exporters of agricultural commodities to European and North American markets. It fails to recognise the rapidly growing dominance of Asian Driver economies in manufacturing and many service sectors, in which case a “level playing field” may not so much open the game to SSA exporters, but lead to their decimation.

### 3.3. The rise of the Asian Drivers and the threat to African industrialisation

How has SSA fared in its attempts to industrialise, bearing in mind that a key component of policy orthodoxy is that industrialisation is the key stepping stone to long-term sustainable income growth. In recent years, the African continent has seen revived growth. Yet, despite this rapid economic growth, there has been little change in economic structure in the continent. Manufacturing value added as a share of gross domestic product is not only much lower than in the rest of the world (including in many developing economies), but its share remained unchanged between 1996 and 2004 (Table 2).

**Table 2: Share of manufacturing value added in GDP (Constant 1995 Prices) (%)**

	1995	2000	2004 <sup>a</sup>
Africa <sup>b</sup>	12.1	12.3	12.1
China	34.7	36.7	39
India	16.3	15.7	15.0
Developing Group excl China	19.2	20	20.4
WORLD	19.8	20.1	19.9

Source: UNIDO International Year Book 2006

a Estimate

b For Africa and not SSA.

The rise of the China and its growing competences in manufacturing and presence in global markets for manufactures is an important factor contributing to this malaise of African manufacturing. Chinese competition is experienced both with regard to African manufactured exports and in regard to manufacturing destined for local markets. Beginning with manufactured exports, excluding South Africa from the picture (since South Africa is a very special case in the African context), clothing accounted for more than one half of all SSA manufactured exports in 2005. In the same year, global trade liberalisation began to allow China and other Asian economies more access to the US and EU markets, markets in which AGOA (the African Growth and Opportunities Act of the US) and other preferences had favoured SSA (and other non-Asian low income producers). Following quota removal, between 2005 and 2007, SSA clothing exports to the US fell by 26 percent, whilst those of China surged. In some very low income SSA economies such as Lesotho and Swaziland the impact on employment was devastating with a fall in employment in the clothing sectors of 26 percent and 43 percent respectively (Kaplinsky and Morris, 2008).

But it is not just in export markets that Asian Driver competition is squeezing SSA industrialisation. In Ethiopia, although competition from Chinese shoe imports has led to an upgrading of processes and design by many domestic firms, it has simultaneously had a negative impact on employment and domestic output. A study of 96 micro-, small and medium domestic producers reported that as a consequence of Chinese competition, 28 percent were forced into bankruptcy, and 32 percent downsized activity. The average size of microenterprises fell from 7 to 4.8 employees, and of SMEs, from 41 to 17 (Egziabher, 2006). In South Africa, imports from China grew from 16.5 percent of total clothing imports in 1995 to 74.2 percent in 2005 (Morris, 2007). Including imports from Hong Kong, China-sourced clothing were 78.8 percent of total clothing imports in 2005. The expansion of clothing imports was associated with a period of rapid decline in formal sector manufacturing in both clothing and textiles. In clothing, employment fell from 97,958 in 2004 to 78,694 in 2006, and in textiles from 21,380 in 2003 to 16,800 in 2005. These two examples are replicated throughout the African continent as many manufacturing enterprises are unable to compete with low cost and superior products imported from China (Kaplinsky, 2008)..

#### 3.4. What does the rise of the Asian Drivers portend for global standards?

Consider three sets of standards which arguably are meant to protect African citizens, consumers and producers from the negative impact of growth and globalisation. The first of these are those standards affecting SSA governments, notably in regard to issues of governance and transparency. Two examples show the impact of China in this domain. In Angola, the attempts by the Paris Club of donors to insist on transparency in the spending of aid inflows were scuppered by loans sourced from China. In the Sudan, a range of pressures exerted by Western Powers on Darfur have been rendered toothless by Chinese aid and foreign direct investment.

A second set of standards are those which reflect the nature of final products, and their associated production processes. Under pressures from high-income western consumers and NGOs, many African products are required to meet product standards with regard to their organic content, their safety and the conditions in which workers in these value chains produce. Each of these standards reflects the generally high-income environment in which western consumers and citizens live. China's global presence is likely to subvert these standards. One reason is that Chinese firms operating in SSA do not incorporate these standards in their own operations. So that as Chinese foreign direct investment is increasing in SSA, the likelihood of these firms adopting these standards is low. A second reason is that insofar as China and other Asian Driver economies become a market for African products, the nature of these external final markets is very different from that which African producers have been used to serving. Products destined for China are aimed at a very different set of consumers. Hence timber exports to China from Gabon, Mozambique and other countries are not sourced from sustainable plantations and nor do they meet the standards of the Forestry Stewardship Council certification schemes which provide for environmentally and socially sustainable practices throughout the value chain. Put bluntly, Chinese and Indian consumers don't care.

A third set of global standards threatened by the advance of the Asian Drivers are those which operate within global value chains and which have been a vehicle for upgrading for many African producers. Typically, most western companies have extensive supplier development programmes which have been used to incorporate and improve the competences of local firms. These programmes operate by setting "QCD" (quality cost and delivery) standards for their suppliers, and using these as benchmarks for improvement. In South Africa, for example, together with local service-providers, the Japanese and US auto firms have systematically addressed the performances of their metal-working suppliers with spread effects to many other sectors of the economy (Barnes and Morris, 2008). In Kenya, similar outcomes can be observed (UNCTAD, 2005). By contrast, Chinese firms in Africa appear to source much less from their local environment (Burke and Corkin, 2006, for Angola) and when they do source locally, there is little evidence of similar standards-based supplier-development programmes.

#### **4. THE ASIAN DRIVERS AND SSA – WIN-WIN OR WIN-LOSE?**

Hitherto we have focused on the negative impacts on SSA of the rise of the Asian Drivers. But this is too restricted a focus, and misses the opportunities which are opened-up by the rapid growth and global presence of the Asian Driver economies. Three major opportunities can be identified for SSA – the policy space which is opened; the supply of cheap and appropriate products, and the boom in commodity prices

#### 4.1. The Asian Drivers open-up important policy space for SSA

It is relatively easy to identify the central tenets of the Washington Consensus, both in its original formulation, as in the case of Structural Adjustment Programmes (Williamson 1990), and in its augmented form (Rodrik, 2002). The “Beijing Consensus” is more difficult to identify. However, after a series of discussion with senior Chinese stakeholders, Ramo defines it usefully as consisting of two distinct components. The first is that every country must take its own route – one size does not fit all. The second is that reform should be staged and carefully managed over time (Ramo, 2005).

In a sense the precise significance of the Beijing consensus is that it lacks content, which is of course in sharp distinction to the Washington Consensus. What this does, as is graphically and perhaps unfortunately shown in the case of Sudan and Darfur, is to provide Africa economies with the capacity to withstand western pressure. Increasingly, African governments are saying to the international financial institutions that Chinese experience shows that there is an alternative route, that they do not have to swallow the prescriptions of western-dominated bi- and multi-lateral aid agencies, and that one size does not fit all. There is a tangible sense of this growing policy space across a variety of stakeholders in Africa, in both the private and public sectors. On the other hand, civil society organisations – whose operations in China are heavily circumscribed in China – are perhaps less happy about the ability provided to African governments to withstand pressures and standards emanating from high income economies.

#### 4.2. The Asian Drivers area a source of cheap and appropriate products

We have seen the impact of Chinese competences in manufacturing and their impact on African producers operating in both the domestic and external markets. But the very same competences also simultaneously benefit African consumers of capital goods, intermediate goods and final goods. Asian Driver machinery producers offer equipment at much lower prices, and often with much greater appropriateness to African conditions than do the historically dominant machinery suppliers from the west. Similarly, Asian Driver intermediate products are also very attractive to African producers, and, indeed, the rapid rise of SSA clothing exports to the US has largely been made possible by the sourcing of cheap textiles from China, India and other Asian economies (Kaplinsky and Morris, 2008).

A third set of beneficiaries are African consumers. For example, in South Africa, between 2000 and 2005, the overall price index increased by 30 percent. By contrast, the price index for clothing fell by five percent. Significantly, as in the case of the Ethiopian shoe industry, competition from Chinese manufactures forced local manufacturers to upgrade their competitiveness. As Table 3 shows, price deflation occurred both with regard to imports and locally produced apparel, and was reflected in both lower consumer prices and lower costs to the retailer.

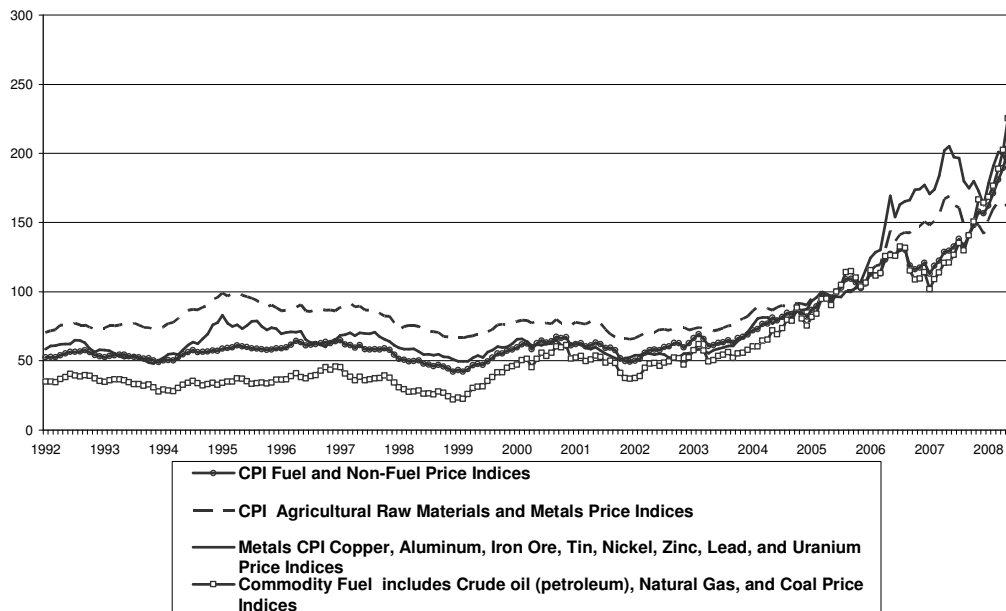
**Table 3: Changes in retail price by major retailer for imported and locally produced clothing products in South Africa, 2004-2006.**

	Imports	Locally produced
Number of sectors	65	27
% categories experiencing price deflation	61.5%	29.3%
% categories experiencing price inflation	23.1%	22.2%
% categories experiencing no change	15.4%	18.5%
Average % price change	-16.8%	-7.3%

Source: Morris, 2007.

#### 4.3. Making the most of the commodities boom

Whilst historically there has been a long-term decline in the commodities terms of trade against manufactures, there have been periods in which commodities prices have boomed (Figure 2). However, the previous price spikes in the 1950s and the 1970s were short-lived since the primary drivers of rising commodity prices (the Korean and Middle East Wars) were temporary in nature. This time round, the rise in commodity prices is fuelled by growth in major consuming economies, particularly China, but India is also about to enter the global market for commodities. Both these giant Asian Driver economies are at the early stages of their commodity-intensive growth paths and short of a major collapse in their growth trajectories, their thirst for energy and mineral products is likely to be sustained for some time (Kaplinsky, 2006). Moreover, as incomes in these two economies rise, food consumption patterns are changing in favour of meat products and this, and the associated drive for global energy security and biofuels has now also led to a sustained increase in agricultural prices. The current commodity price boom – since around 2001 – is already more prolonged than the price spikes of the 1950s and 1970s, and there seems little chance of it running out of steam in the near to medium-term future.

**Figure 2: Index of Commodity Prices, 1992-2006 (2005=100).**

Source: <http://www.imf.org/external/np/res/commod/index.asp>, accessed 18<sup>th</sup> July 2008

Africa is especially well favoured by these developments, not so much in terms of its existing commodity exports, but rather in terms of its potential exports. Table 4 shows that in many mineral commodities, Africa is the primary resource base for the future. In energy, it is not so much Africa's share of global reserves which is so strategically important, but its reserves of unallocated reserves. New hydrocarbon discoveries off the west coast of Africa, as well as in Uganda, and the potential for oil discoveries in other parts of Africa, make it an exceptionally attractive region for countries with rapidly-growing energy needs.

**Table 4: Africa's Share Of Global Production And Reserves ( percent)**

Mineral	Production	Reserves
Platinum Group Metals	54	60+
Gold	20	42
Chromium	40	44
Manganese	28	82
Vanadium	51	95
Cobalt	18	55+
Diamonds	78	88
Aluminium	4	45

Source: African Development Bank (2007)

But although Africa stands to gain from the commodities boom in the future because mineral potential is widespread in the continent, the current pattern

of resource exploitation is very concentrated. Only five countries account for more than 90 percent of all energy exports, and only 12 countries account for more than 90 percent of all mineral exports (Kaplinsky, 2009). Moreover, although agricultural exports are more widely-diffused in Africa (22 countries account for 90 percent of exports), this excludes more than half of all African countries, most of whose populations live in rural areas. Moreover, in the main, Africa lacks decisive agricultural comparative advantages (Bloom and Sachs, 1998).

## 5. THE POLICY RESPONSE

The challenge for SSA is therefore to confront the threat arising from the rise of the Asian Driver economies in order to minimise the potentially harmful outcomes. At the same time, the impact of the Asian Driver economies on the global economy provides substantial opportunities. Left to the market alone, the likelihood is for an adverse impact on Africa. Thus there is an urgent imperative for SSA economies to develop an appropriate policy response, and perhaps also for traditional western aid donors to assist in the African-defined reaction to the Asian Driver challenge.

In developing an effective response, two key changes in focal lens are required. The first is that that Africa increasingly has to look east, rather than west or north. The second is that whilst south-south solidarity must remain an important dimension of policy, it must be critically examined to recognise that there are key respects in which Africa's major problems lie with its southern, rather than its traditional northern partners.

Five key policy agendas can be identified. These are in regard to developing strategic capabilities, limiting trade liberalisation in global markets, protecting domestic producers, travelling the high road in the commodities boom, and taking advantage of Asian Driver markets outside of the minerals and oil sectors.

### 5.1 Developing strategic capabilities

A Kenyan academic reviewing the rapid advance of China into Africa observed – “the trouble is that China has a strategy for Africa, but Africa doesn't have a strategy for China”. SSA, as we have seen, is not without its attractions to the Asian Driver economies, particularly with regard to its potential as a provider of commodities.

The key, therefore, is for Africa to use this power in commodities to its best advantage in its relations with the new emerging powers, particularly in the exploitation of these mineral resources and in the provision of related infrastructure. The agreement which the DRC reached with China in 2007 and 2008 shows the potential for using this power to leverage advantageous terms, particularly as China and other emerging economies seek to muscle their way into territories which were previously the domain of western economic powers. As Box 1 shows, it is not just that the DRC was able to



crowd-in aid-assisted Chinese investments in infrastructure and training, and to ensure minimum local content, with local co-ownership in mineral exploitation, but also that it was able to use this leverage provided by China to force the renegotiation of more than 60 35 year mining agreements which had previously been reached with western firms.

In developing this strategic agenda, African countries need to adopt a similar strategy of integrating the aid, trade and foreign direct investment vectors to that which is being pursued most clearly by China, but increasingly also by India. Meeting the trade needs of the Asian Drivers – Africa as a source of primary commodities and, to a lesser extent, as a market for their exports – should be conditional upon their providing aid to exploit these commodities, as well as to meet Africa's complementary developmental and infrastructural needs. Where appropriate, it should also incorporate foreign direct investment from the Asian Drivers, and participation in Asian Driver firm value chains which serve global markets. For example, Chinese and Indian firms providing their fabric to African countries for onward export, through the marketing channels of these Asian Driver firms, to the US and the EU.

**Box 1. The Strategic integration of aid, trade and foreign direct investment: China and the DRC, 2007-8.**

The context is one in which the DRC possesses extensive mineral resources, but lacks the resources or technology to exploit these. (The total DRC state budget in 2007 was only \$1.3bn, most of which was used to pay salaries). Before the elections in 2006, the DRC government had approved a large number of 35-year mining contracts in processes which were not transparent. Reacting to international concern, the new incoming government began a process of reviewing 61 mining contracts entered into between 1997 and 2003. The ability to review these contracts was strengthened by the existence of an alternative path to exploiting the DRC's extensive mineral deposits, in large part by the Chinese aid-trade-foreign direct investment package signed in 2007 and 2008..

This constituted two large, but related, initiatives. The first, entered into in late 2007, involved a loan for \$8.5bn from the Chinese EXIM Bank. This was to promote exploitation of the mining sector, and was supplemented with a further \$5bn loan in early 2008. Together, these loans were securitised by providing China with access to, and security provided by \$14bn of copper and cobalt reserves. This aid was tied to an investment package to exploit these mineral resources by a jointly owned company, Socomin, owned by Chinese (68 percent) and Congolese (32 percent) state-owned companies. The \$3bn investment in the mines will be repaid out of future profits. By agreement, not more than 20 percent of the workforce can be Chinese, 0.5 percent of investment will be allocated to training, a further one percent will be spent on social investments and three percent on environmental projects in the surrounding areas. In addition, at least 12 percent of the work will be sub-contracted to local firms.

In addition to these investments in mines, China will provide support for investments in five key areas identified by the DRC state – in water, electricity generation, education, health and transport. \$8.5bn will be allocated to a variety of projects which include a high-voltage power distribution network, highway and railway extensions, and the construction of 31 hospitals, 145 health clinics, 5,000 houses and two universities. Additional resources are allocated to rehabilitate and expand water supplies. Supplementing all of this are a range of additional aid projects, including training programmes in China for poverty reduction and subsidised loans to construct the national People's Palace (the parliament) and the Stadium of the Martyrs outdoor and sports complex.

Source: Vandaele, 2008; Komesaroff, 2009.

## 5.2. Limiting trade liberalisation in global markets

What SSA does not need is a liberalised and even playing field in the major global importing markets. This terrain will play to the strengths of the Asian Driver economies and lead to the exclusion of non-commodity SSA producers from many important segments of the global trading economy. SSA needs a world of preferential access in order to build its capabilities

In some cases these preferences need to be both significant and sustained. Africa's recent experiences in the clothing sector are indicative of this. As observed, the surge in Asian Driver clothing exports to the US led to a 26 percent fall in SSA clothing exports under the AGOA scheme between 2005 and 2007. At the same time, and comparing like-for-like products, Chinese

exports into the US grew by 85 percent, on the back of a halving of unit prices. However, this surge was only a result of the removal of quantitative restrictions on Asian Driver exporters. (In the past many exporters of clothing were limited by quotas on the number of items they could export to the Northern economies). Once these quotas were removed Asian Driver exports surged, and SSA's clothing exports fell, despite the fact that Africa continued to benefit from preferential access into the US.<sup>5</sup>

### 5.3. Protecting domestic producers

An analogous policy agenda can be identified for the protection of SSA producers in their domestic markets. Patently, in many sectors, and particularly in manufacturing, African producers are unable to withstand competition from Asian Driver producers. Where appropriate – and of course this revisits the discussion on industrial policy – SSA countries will need to have the capacity to protect themselves from this competitive onslaught from the Asian Drivers. But in doing so, five important and related considerations will need to be borne in mind.

The first is that the interests of consumers need to be balanced against those of producers. This is not just a matter of the consumers of final products (for example, shoes and clothes imported from the Asian Drivers), but also those of the users of intermediate goods (for example, sourcing textiles from the Asian Drivers) and capital goods. Second, selectivity will be required. It is clearly undesirable to protect all sectors from competition, only those where it is deemed that SSA can develop a distinct advantage over time. Third, and related, over what time horizon should these advantages be developed and for how long and in what form should this preferential regime be sustained? Fourth, should this protective regime be tilted against all competition from external firms, or only those from the Asian Drivers? And finally, in previous eras of protection, progress was limited due to the absence of competition. Markets in individual countries were too small to allow for a combination of the protection *and* competition which is required to spur productivity growth, and this may indicate the need for a regional approach towards protection.

An important related policy agenda here is that of regional integration, On the export side, trade with China and, to a lesser extent India, is disproportionately geared to primary commodities. It is significant that intraregional exports are more technology intensive than those destined for non-SSA markets, and that the degree of technological intensity has been growing (Table 5). Hence a regional approach towards protection from Asian Driver competition may simultaneously also have important learning externalities

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<sup>5</sup> SSA's exports into the US were duty-free. China's exports (as well as those from India and other Asian countries) faced a weighted average tariff for textiles of 6.93 per cent, and 11.36 per cent for apparel (TRAINS data based accessed through <http://wits.worldbank.org> on 24<sup>th</sup> January 2007).

**Table 5: Technological Intensity of SSA's trade: Share of exports and imports comprising different categories of products, 2005 (%).**

	<b>World (excl. China, India)</b>	<b>China</b>	<b>India</b>	<b>Intra-SSA</b>
<b>Primary Commodities</b>				
Exports	67	81	38	17
Imports	8	3	13	36
<b>Resource Based</b>				
Exports	16	15	46	35
Imports	17	9	24	27
<b>Low Technology</b>				
Exports	4	1	3	13
Imports	10	40	22	11
<b>Medium Technology</b>				
Exports	9	2	11	23
Imports	46	33	28	20
<b>High Technology</b>				
Exports	1	0.1	1.1	5
Imports	18	16	12	4

Source: Calculated from COMTRADE (Accessed through <http://wits.worldbank.org>) in January 2007

#### 5.4. The high road to the commodities boom

it is possible to distinguish a low and a high road to resource exploitation. Either Africa can remain a simple source of raw materials, providing little else but basic ores and oil, or it can become a source of knowledge built around the resource sector. This high road is a path trodden by the USA in the 19<sup>th</sup> Century and by Australia and Norway in recent decades, where the National System of Innovation was oriented to making the most of the commodity resources (Wright and Czelusta, 2004). Whilst it may appear to be a long way from Africa's current low-tech road to the commodities sector, "the longest journey begins with the first step", and key long-term investments in knowledge and human resources related to the commodities sector needs to be made now if Africa is to thrive in the future.

#### 5.5. Accessing Asian Driver markets

The Asian Drivers are of course an important source of demand for Africa's commodities exports. Even if the commodities are not directly consumed by the Asian Drivers, they are sold into global markets whose prices have been raised by demand from the Asian Drivers. In other words, it does not matter so much if Nigeria sells oil directly to China, but that it sells oil into global markets whose prices have been radically affected by demand from China.

There are other products, however, in which the direct export relationship is potentially more important and where Africa can benefit directly from augmented demand in the Asian Drivers. Here trade preferences for African

exporters have a role to play, although on their own, this may have little impact. For example, in recent years China has provided duty-free access to a range of African manufactures, but given the weakness of supply capacity on the continent, there has been little increase in manufactured exports to China. Thus, recent initiatives to link trade opportunities with production support are important such as the planned investment of \$800m in Mozambique's agriculture sector by aid-assisted Chinese producers. This targets an increase in rice production from 100,000 tonnes to 500,000 tonnes a year by 2013. (<http://www.bizchina-update.com/content/view/1128/2/>, accessed 24 July 2008)

## 6. POLICY ACTORS

The issue is who in Africa is going to drive this strategic agenda? At the most basic level, this must necessarily involve individual African governments. Although they do not generally directly control inward foreign direct investment and trade flows, they hold the key levers which determine access to their economies. Each of the governments needs to make a cool, informed assessment of its specific attractions to the emerging economies and then to coordinate an integrated strategic response to offer access to the emerging economies in a way which best meets the needs of their domestic economies. This will involve extensive background analysis, but also the convening of appropriate stakeholder groups to ensure an integrated approach providing clear signals to emerging country partners. But formal written strategies which are not implemented effectively are much less use than dynamic and active coalitions of local interests interacting effectively amongst themselves and with emerging country partners.

Another arena for integrated response is in regional and all-Africa fora such as SADC, ECOWAS, NEPAD and the AU. These multi-country organisations are important for three major and related reasons. First, by aggregating African countries in the bargaining process, they help to avoid contradictory bargaining positions and wars of incentives. As has been evident for many decades in the diamonds sector, there is enormous power in cartelised bargaining. This is not just a matter of achieving the best price for Africa's resources, but also to ensure that wider objectives can be met, such as the construction of regional infrastructural networks to provide access for non-commodity exporters. Second, and related to this, as observed earlier, not all African countries have extensive commodity deposits or are significant commodity producers. Their interests need to be protected by those economies who do have primary resources and markets of interest to the emerging economies. Including these marginalised economies is not just a matter of altruism for the commodity exporters. As we have seen, intra-regional trade may be a primary area for the development of the capabilities which are required for long term and sustainable growth so that it is in the interests of all parties – commodity exporters and non-commodity exporters alike – that these intra-regional links are strengthened as a consequence of engaging with the emerging economies. A final reason why the multi-country organisations are important is that the emerging economies themselves see

these as important organisations for bargaining access to Africa's resources and markets. This is most evident in the case of the FOCAC (Forum for China African Cooperation), but it is also relevant for other emerging economies as well.

What role is there for the EU in this? This all depends on whose interests in the EU are being considered. The private sector clearly is affected by the rise of the Asian Drivers, their presence as suppliers in SSA, and their competition for increasingly scarce global resources. From this perspective, the agenda would be to strengthen the opposition to an increasing Asian Driver presence in SSA. Here there may be common interests with the EU NGO community who, in general, are likely to see an increasing Asian Driver presence in SSA as being inimical to the agenda which they are pursuing.

However, both of these EU interest groups are perhaps a little blind to the opportunities opened up for SSA by the global rise of the Asian Drivers. It is true that without appropriate interventions, SSA stands to lose a great deal from the unchecked advance of the Asian Drivers. But at the same time, real and important opportunities are opened up. SSA's abilities to grasp these net benefits depends on its strategic capacities to act in a focused way, and in concert with others. The real test of EU development assistance is whether it can assist SSA in this endeavour in a disinterested way, in the knowledge that in many respects, the greater SSA's capacities are to work effectively with its Asian Driver partners, the more likely it will be that EU corporate interests will suffer.

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