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Impacts and Challenges of a Growing Relationship**

Raphael Kaplinsky, Dorothy McCormick, and Mike Morris

African Studies Program
The Johns Hopkins University
Paul H. Nitze
School of Advanced International Studies
Washington, DC



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Raphael Kaplinsky, Dorothy McCormick, and Mike Morris

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For more information about the African Studies Program at SAIS please contact:

African Studies Program
The Johns Hopkins University
Paul H. Nitze
School of Advanced International Studies
1717 Massachusetts Avenue, NW
Office 716
Washington, DC 20036
Phone: 202.663.5676
Fax: 202.663.5683
smjackson@jhu.edu

China and Sub Saharan Africa: Impacts and Challenges of a Growing Relationship

Raphael Kaplinsky¹, Dorothy McCormick², and Mike Morris³

*Introduction*⁴

That China is having an impact on Sub Saharan Africa (SSA) is very clear. What is not clear is the precise nature of that impact. Does it come mainly from trade in cheap manufactured goods? Does it come from China's seemingly insatiable hunger for oil and minerals? What role do Chinese companies operating in Africa play? How beneficial is Chinese aid and/or international cooperation?

Existing literature gives a fair amount of information about the magnitude and effects of trade between China and SSA. It tells us, for example, that trade between China and SSA has increased rapidly, especially since 2001. Available databases can be mined to tell us what is traded and by whom. The literature, however, is less clear about how that trade actually affects Africa. What countries benefit and in what sectors? Who is losing out, and why? It is also clear that trade is not the only form of interaction between China and Africa, and that other interactions may also generate positive or negative impacts. Of the many possibilities, we have identified foreign direct investment, production, and aid as potential channels of impact.

Unfortunately, we know even less about how these affect Africa than we do about the effects of trade. In the following pages, we attempt first to take stock of our knowledge. We do by subjecting the most common forms of interaction between China and SSA to a comprehensive and detailed analysis using a systematic framework. We then use this analysis to identify the gaps in our knowledge and suggest ways of bridging them. The paper uses secondary data from a number of sources, including the International Monetary Fund, the World Bank, the US Department of Commerce, as well as published materials and relevant websites.

The paper is written in five parts. Part 2 presents a framework for analyzing the impact of China on SSA. Part 3 uses available information to examine each of the main channels of impact. Part 4 raises a number of issues arising from this analysis, focusing particularly on the manufacturing sector. Part 5 presents our conclusions.

1. Framework for Analysing Impact

It is important to be systematic in assessing the impact of China on SSA, particularly in the context of uneven data availability. In providing a framework for a coherent and overall evaluation we can distinguish a number of *channels* through which these impacts may be transmitted. Our preliminary examination of the issues suggests three main channels through which China is affecting SSA: 1) trade flows; 2) FDI flows, technology transfer and integration in global value chains; and 3) aid flows. These are not the only channels through which a given country or region may have an impact on another country or region (IDS, 2006). For example, there may be impacts transmitted through the environment, through financial flows, or through participation in institutions of regional and global governance. The three, however, appear to be particularly pertinent at the present time.

In each channel, it is possible for China-SSA relations to be either *complementary or competitive* (or indeed both). In the case of the trade channel, for example, China may provide SSA with appropriate capital goods and cheap consumer goods, and SSA may supply China with the commodities it requires to fuel its continued economic expansion. The relationship is complementary because both countries gain from it. On the other hand, China's export of consumer goods to SSA may displace local producers, leading to competitive impacts on workers and entrepreneurs in these sectors.

This distinction between complementarity and competitiveness is easily understood. By contrast the distinction between the *direct and indirect* impacts is less obvious, and its significance is less widely recognized. The direct impacts are relatively simple and clear. In the case of the trade illustrations discussed in the previous paragraph, for example, both complementary and competitive impacts occur as a result of direct bilateral relations between China and SSA. These impacts can be measured, by charting the direct trade flows between China and SSA, breaking these down by sectors and countries, and over time. The indirect impacts occur as a result of China's relations with third countries, working their way indirectly through to SSA. Staying with the trade example, China's demand for commodities may raise their prices at a global level, and even though a country like Ethiopia does not export animal feed to China (a direct relationship), it sells animal feeds into a global market in which prices have been raised by China's growing imports (indirect impact). As we shall see below, and particularly in the case of trade, the indirect impacts of China on SSA are sometimes much more substantial than the direct impacts. However, almost all of the analysis of the impact of China on SSA focuses on direct, bilateral relations, and hence tends to miss some important issues.

Figure 2 integrates these three sets of factors – channels, complementary-competitive impacts, and direct-indirect impacts – into a synthetic framework which can be used to assess the overall impact of China on SSA. As will be shown below, our attempt to complete this synthetic matrix has resulted in several empty cells, and it is unclear to what extent this represents the pattern of China's impact on SSA or the

underdeveloped state of our knowledge on these impacts. We will return to this issue in the concluding section of the chapter.

Figure 1. A Synthetic Framework for Assessing the Impact of China on SSA

Channel	Impact		
		Direct	Indirect
Trade			
	Complementary		
	Competitive		
Production and FDI		Direct	Indirect
	Complementary		
	Competitive		
Aid		Direct	Indirect
	Complementary		
	Competitive		

3.1 Trade

Assessing the Impact of Direct Trade Links

Trade between China and SSA is a small proportion of each region’s total trade, but its rapid growth suggests that the trade channel is a significant source of impact. Trade values quintupled from close to \$10 billion in 2002 to more than \$40 billion in 2005 and more than \$50 billion by 2006 (Zafar, 2007). The basis for China’s rising trade links with SSA has been the country’s extraordinarily rapid growth of more nine percent per annum since 1979. One of the main features of this growth has been its deepening trade orientation, with the trade-GDP ratio in excess of 70 percent, well above the “norm” for large countries. Within this, China has become a major exporter of manufactures and a significant importer of commodities.⁵

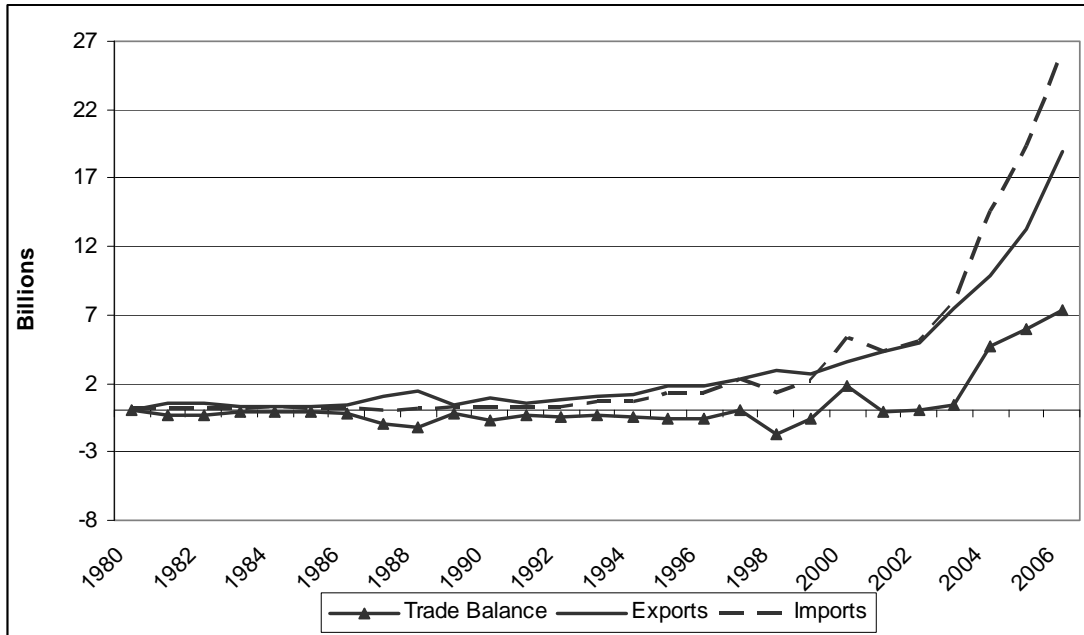
Table 1. Trade with China (Mainland) as a Proportion of Trade with Industrialized Countries

	1990	1997	2001	2004	2005	2006
SSA Exports to China	0.3%	2.3%	3.9%	8.8%	9.5%	11.3%
SSA Imports from China	1.1%	2.3%	3.9%	6.0%	6.6%	8.1%

Source: Calculated from IMF Dots, Accessed 25th November 2007.

In 1990 Sub Saharan Africa’s exports to China were less than one per cent of its exports to industrialized countries, but by 2006 this percentage had risen to 11 per cent. Similarly SSA’s imports from China, which were 1.1 per cent of its imports from industrialized countries in 1990, had risen to over 8 per cent by 2006. Since 2001, imports from China have been expanding more slowly than exports, allowing SSA’s trade balance with China to turn from negative to positive (see Figure 2).

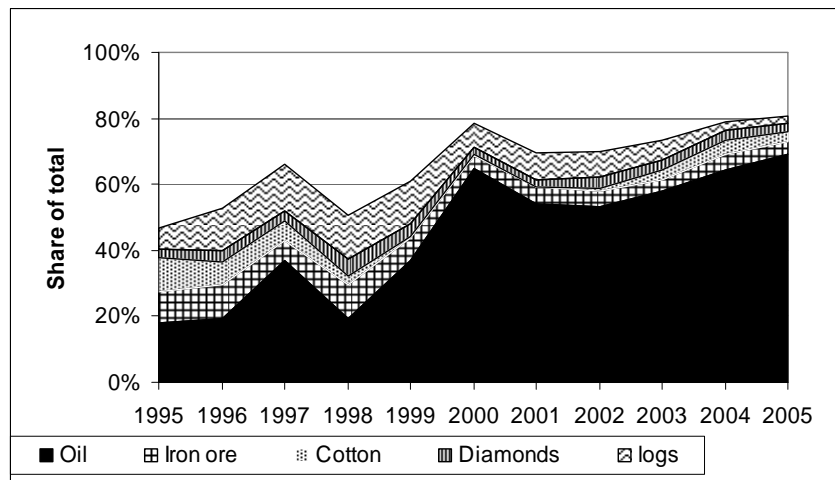
Figure 2: Balance of Trade between China and SSA, 1980-2006



Source: Calculated from IMF Dots, Accessed 25th November 2007

SSA's exports to China are mainly fuelled by China's growing demand for commodities. As Figure 3 shows, the share in total SSA exports to China of five families of commodities (oil, iron ore, cotton, diamonds and logs) grew from less than 50 percent to more than 80 percent between 1995 and 2005. The overwhelming bulk and most rapidly-growing export was oil so that while the growth of other commodity exports was at a high level, the proportion of the total which they accounted for fell during the decade after 1995. SSA manufactured exports to China were mostly from South Africa. But even in this case, nearly all products were derived from basic metals.

Figure 3: Composition of Chinese Imports from SSA



Source: Derived from Sandrey (2006)

For some SSA economies, the importance of China as a direct destination of exports grew particularly rapidly. In the case of oil, for example, exports to China account for between 86 and 100 percent of all oil exports for Angola, Sudan, Nigeria, and Congo. A similar picture is true for the DRC, which sends 99.6 percent of its basic metal exports to China. On the import side, only seven SSA countries source a significant share of their total imports from China. Sudan, which has growing and policy-related energy links with China (see below) stands out, with 14.2 percent of its imports coming from China, followed by Ghana and Tanzania (9.1 percent), Nigeria (7.1 percent), Ethiopia and Kenya (6.4 percent) and Uganda (5.1 percent) (Jenkins and Edwards, 2005). Almost all of these imports were manufactured products.

With that historic picture as background, we look forward to areas of potential bilateral trade between China and SSA. The World Bank, using its own “Trade Complementarity Index”, concluded that on the basis of existing economic specialization, the potential for future bilateral trade growth with China was not strong, but could become so if China’s growing demand for commodities were to be sustained (World Bank 2004a). This evidence on the direct trade links between China and SSA, suggests that on the export side SSA gains from China’s demand for commodities, and on the import side, it gains cheap and appropriate consumer and capital goods. Outside of textiles, timber and cotton (see below), there appears to be little trade between China and SSA in intermediate goods and little incorporation of China and SSA into coordinated global value chains. Jenkins and Edwards (2006) argue that most of these imports into SSA have substituted for imports from outside of SSA, with the possible exception of Ethiopia and Nigeria, suggesting little displacement of domestic production and few negative impacts on employment and local production. These conclusions suggest a synergistic link between SSA and China and help to explain the high sense of optimism which prevails in some circles in SSA on the potential opportunities opened for SSA by China’s rapid trade expansion.

However, this optimistic picture of opportunities opened up by growing bilateral trade links between SSA and China may be misplaced. There are three major reasons for suggesting a more cautious set of conclusions. First, the analyses of Jenkins and Edwards and the World Bank are conducted on 3-digit SITC trade data. Whilst this shows notable aggregate trends, it hides some important specific impacts which only show up with different, firm-level methodologies. In a study conducted for DFID, Kaplinsky and Morris report that domestically produced clothing and furniture manufactures in both Ghana and South Africa are being displaced by imports from China (Kaplinsky and Morris, 2008). Similar anecdotal evidence can be found with regard to clothing and footwear manufacture in many SSA economies. For example, in Zambia the trades unions assert that imports of Chinese clothes have undermined the clothing and electrical sector, and in Nigeria trades unions blame Chinese imports for the loss of 350,000 jobs (<http://www.nzherald.co.nz/>). 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 micro enterprises fell from 7 to 4.8 employees, and of SMEs, from 41 to 17 (Tegegne 2007).

However damaging these impacts might be, a matter of greater concern is the potential effects on future production. Here, particularly in the case of light consumer goods, there are important and adverse long-term implications for SSA industrialization (Kaplinsky and Morris 2008). What “spaces” will they be able to move into as their economies grow and they seek to diversify?

However, the third and by far the most important indicator of caution arises in regard to the *indirect* impact of China’s trade with SSA. That is, it is not so much in the growth of direct bilateral economic trade links that we must look for impact, but on the indirect links. Both China and SSA trade in global markets. But China’s trade footprint is so large that it is in itself altering global prices, and this has significant impacts on SSA. The problem is that these indirect trade impacts are much more difficult to analyze than the direct impact, which is why almost all of the analysis so far has been on the growth and impact of direct trade links.

Assessing the Impact of Indirect Trade Links

A number of attempts have been made to assess the impact of indirect trade links. They have focused on their effects on product prices (Kaplinsky and Santos-Paulino 2006), the similarity (or lack of it) between SSA’s and China’s exports (Jenkins and Edwards 2006), and the identification of winners and losers from trade with China (Stevens and Kennan (2006). Each of these studies has provided useful insights into the indirect effects of China’s trade on Africa, but the fact that most of the analyses have been done at fairly high levels of trade aggregation tends to mask the severity of China’s indirect impact on SSA manufactured exports. The actual impacts are better seen by examining particular sectors and products.

By far the most significant manufactured export from SSA in recent years has been in the clothing and textile sector, largely as a result of United States Africa Growth and Opportunity Act (AGOA) preferences. Table 2 shows not just significant export growth, but growing reliance on the US market. For some SSA economies, these rapidly-growing exports have become especially significant. In 2002 clothing and textile exports accounted for 50 percent of Lesotho’s GDP. In Kenya, in 2004 employment in the clothing EPZ enterprises was equivalent to 20 percent of formal sector manufacturing employment.

Table 2: Growth of SSA Clothing and Textile Exports, 2000-2006

Supplier	Year	Exports(\$ '000)		
		World	USA	US Share
Kenya	2000	54,195	46,962	86.7%
	2004	309,579	295,851	95.6%
	2005	284,466	271,145	95.3%
	2006	290,071	279,690	96.4%
Lesotho	2000	152,646	146,371	95.9%
	2004	494,474	481,866	97.5%
	2005	404,922	390,827	96.5%
	2006	418,759	407,347	97.3%
Madagascar	2000	382,209	116,040	30.4%
	2004	577,107	346,363	60.0%
	2005	536,769	277,720	51.7%
	2006	592,244	254,227	42.9%
Swaziland	2000	46,920	33,407	71.2%
	2004	198,737	188,588	94.9%
	2005	168,377	161,005	95.6%
	2006	147,304	142,121	96.5%
South Africa	2000	496,237	187,222	37.7%
	2004	561,090	191,728	34.2%
	2005	406,115	102,540	25.2%
	2006	370,993	95,811	25.8%

Source: Calculated from COMTRADE, accessed via WITS on 25th November 2007.

The primary driver for these growing clothing and textile exports has been trade preferences in general and the US AGOA preference scheme in particular. However, within AGOA, there has been a key derogation on the rules of origin which allows SSA exporters to import inputs from outside of the AGOA region or the US.⁶ This derogation was initially limited to September 2004, was extended to September 2007, and in December 2006 was extended again, this time to 2012. Its intent is to encourage backward integration into the textile sector, but the only significant case of the development of a textile industry in a Lesser Developed Country has been the construction of a \$100m denim plant in Lesotho, which came on stream in mid-2004.⁷ Nevertheless, the derogation has been important because it has allowed countries with weak or non-existent textile industries to boost employment and exports through clothing production.

The final integration of the textile sector into WTO rules involved the removal of all quotas, effective 1 January 2005. This opened the US market to imports from a number of countries, notably China, which had previously been subject to quotas. All of the countries that had been exporting textiles under AGOA experienced a decline in

exports following the removal of quotas, though the precise impact varied from country to country. Nevertheless, the outcome of quota-removal has not been quite as catastrophic as many had anticipated. By value, overall AGOA textile exports fell by 22 percent between 2004 and 2006 (www.agoa.info). The major casualty of quota removal was South Africa, whose AGOA exports collapsed to only 50 per cent of their 2004. Kenya fared best, with its 2006 exports at 95 per cent of their 2004 value. Lesotho, Swaziland, and Madagascar had 2006 exports of 85, 75, and 73 per cent of 2004 values respectively. By contrast, partly as a result of falling unit-prices, China's share in the same product markets increased, suggesting a direct exclusionary impact by China on SSA in third-country markets (Kaplinsky and Morris 2008).⁸

The main reason why SSA's overall export performance was not as bad as expected relates to the degree of effective subsidy offered to AGOA producers in the US. The nominal rates of tariff on the clothing products which AGOA countries export to the US range between 16 and 32 percent. However, in nearly all cases AGOA clothing products can use (duty-free) fabrics and other inputs from outside of SSA in manufacturing their clothing. These imported inputs account for up to 60 percent of costs. Therefore, the implicit "effective rate of subsidy" is substantially higher than the nominal rates of protection would suggest. These effective rates range between 27 and 84 percent for representative exported products (Kaplinsky and Morris, 2008).

This rate of subsidy is required for AGOA clothing producers to compete in the US market. This is because scales are low in SSA plants, and many SSA economies suffer from poor bureaucratic and physical infrastructure. But there is also pervasive evidence that many SSA clothing plants have low levels of productivity because of poor organizational procedures, low levels of skill and inadequate management within plants (Manchester Trade Team, 2005; Barnes, Morris and Gastrow, 2006).

The impact of competition from China in third-country markets on poverty and livelihoods is very substantial. Some of this is positive, insofar as reduced prices of clothing imports enhances the consumption power of consumers. But the negative impacts are very large, and focused, and hence command attention. Since there are so few backward linkages into textiles, the major conduit for income-dispersal in the clothing industry has been through direct employment. The scale of job-losses arising from the end of MFA quotas is alarming (Table 6).⁹ It is not just the degree of job loss (particularly in Lesotho and Swaziland) which is of concern, but the nature of the jobs which have gone. Most workers are women, and the impact on their families is severe. For countries without alternative sources of employment, this employment decline has major poverty implications. We also know from global experience that rapid economic growth can be a significant factor in reducing poverty levels, and the loss to both GDP and exports arising from a sharp contraction of the clothing sector will have a further negative impact on poverty levels.

Table 3. Employment Decline in Clothing Sector, 2004-2005

	2004	2005	% decline
Kenya	34,614	31,745	9.3
Lesotho	50,217	35,678	28.9
S Africa	98,000	86,000	12.2
Swaziland	32,000	14,000	56.2

Source: Kaplinsky and Morris, 2008

The figures in Table 3, stark as they are, are incomplete because they largely omit employment in micro and small units. Although exact numbers are not readily available, this employment no doubt also fell. The entry of Chinese clothing imports into many countries has not only reduced domestic production, but has also displaced imports from neighboring countries, many of which were previously produced by small-scale tailors, dressmakers, and knitters (for Kenya, see McCormick et al. 2007).

3.2 FDI and Production

Chinese Investment in Africa

In tandem with the surge in trade, Chinese investment in Africa has also increased dramatically, driven by both resource and market considerations. Although our data on FDI is more limited than data on trade, available information allows us to piece together a rough picture of Chinese investments in Africa.¹⁰

There was little Chinese foreign direct investment (FDI) in Africa until around 1990. Then from \$20 million per year in the early 1990s, Chinese FDI in Africa jumped to close to \$100 million in 2000 and reached more than \$ 1 billion in 2006 (Zafar, 2007). This represents a growth rate higher than Chinese FDI to any other part of the world. According to UNCTAD (2007), China's FDI stock in Africa had reached \$1.6 billion in 2005. If this figure and Zafar's (2007) estimate are correct, then 2006 alone witnessed an increase in Chinese investment in Africa of 62.5 per cent.

Chinese FDI is qualitatively different in kind from European and North American sourced FDI. Historically, Western and Japanese FDI in SSA has come from privately-owned corporations focused on profit maximization, generally with relatively short time-horizons. By contrast, much of Chinese FDI in SSA comes from firms which are either wholly or partially state-owned. They have access to very low-cost capital, and hence can operate with much longer time-horizons. Moreover, many of these investments are either explicitly or implicitly linked to achieving strategic objectives, often those which are focused on long-term access to raw materials, and are closely bundled with Chinese aid.

Furthermore, Chinese FDI is at least partly driven by an active government policy (UNCTAD 2007). In the late 1990s, the Chinese government began encouraging outward FDI and announced its “going global strategy.” The policy has been developed and strengthened over the years, until at present Chinese companies enjoy four types of incentives: special and general tax incentives, credit and loans, foreign exchange allowances, and a favorable import and export regime. China’s FDI to Africa has been further supported by common efforts by the Chinese and African governments. The most visible of these have been high level visits and meetings such as the visits to China by African leaders, visits to Africa by the former president and ex-premier of China, and summits, such as the Summit of the China-Africa Cooperation in November 2006. Such high profile events have received encouragement from behind the scenes through joint committees, bilateral agreements, and various investment promotion activities, including visits by both the Chinese and African business communities to their counterparts.

Chinese FDI mainly takes the form of equity joint ventures with local entrepreneurs and/or national parastatals (Economist Intelligence Unit 2005; UNCTAD 2007). In some cases these are multi-million-dollar joint ventures with local counterparts. The most obvious examples are in the energy and resource sectors, which China has invested heavily in Sudan, Nigeria, Gabon, Angola, Mali, and Zambia. China also has a few large joint ventures in manufacturing, including textile factories in Tanzania and Nigeria, and soya and prawn processing in Mozambique (UNCTAD 2007; Bosten 2006).

In other cases, the investment and scale of operations are much smaller. In some SSA economies, small-scale entrepreneurial investment is presaged by the construction of specialized shopping malls retailing Chinese goods. One country for which there is fragmentary evidence is Sierra Leone. Here, Chinese FDI has become very prominent, particularly in a context where more traditional European and US investors have been wary of political risks and are subject to pressures to support good governance. Investments in Sierra Leone include a joint venture with the government in an industrial estate where small-scale private investors make mattresses, tiles, hair lotions and other light industrial products (Financial Times, 16th March 2005). It appears, however, that very little manufacturing is going on at this industrial estate apart from assembly and goods storage at a bonded warehouse.

Despite the image of Chinese investment as driven by hunger for resources in general and oil in particular, the reality over the longer term is slightly different. Nearly half the amount invested between 1979 and 2001 (46.3 per cent) was in the manufacturing sector (World Bank 2004a). Resource development accounts for just over one quarter of the investments (27.5 per cent), though this share is probably increasing. The balance of the investments went to services (18.3 per cent), including construction services. Agriculture (7.1 per cent) and other (0.9 per cent) claimed the balance.

The Chinese have become highly visible in infrastructure construction and rehabilitation. This is one area where it is sometimes not clear how much Chinese economic activity in SSA comprises FDI, how much is a result of winning commercial tenders, how much is linked to Chinese aid, and how much is part of integrated

production networks between Chinese and SSA firms. Participation in infrastructure and construction projects ranges from stadiums in West Africa, to Presidential Palaces (in Kinshasa), dams (a \$650m tender for Nile River Merowe Dam project), pipelines (Sudan), roads, railways and government buildings.

By 2005, the Chinese had invested in 48 African countries (UNCTAD 2007). Table 4 shows the number of projects and investment amounts for the top fourteen recipients. Zambia, South Africa, Mali, and Tanzania top the list, with the remaining countries receiving relatively small amounts.

Table 4. Top 14 SSA Countries Receiving Chinese FDI (1979-2001)

Country	Investments		Investment Amount	
	No.	%	Thousand US\$	%
Zambia	17	3.8	134,126	18.5
South Africa	83	18.5	110,849	15.3
Mali	5	1.1	58,122	8.0
Tanzania	14	3.1	39,483	5.4
Zimbabwe	11	2.5	33,257	4.6
Nigeria	33	7.4	31,144	4.3
D.R. Congo	7	1.6	24,242	3.3
Ghana	17	3.8	19,212	2.6
Kenya	21	4.7	18,475	2.5
Gabon	11	2.5	17,045	2.3
Benin	4	0.9	16,723	2.3
Mauritius	20	4.5	16,657	2.3
Cote d'Ivoire	13	2.9	16,033	2.2
Cameroon	15	3.3	15,851	2.2
Africa total	448		726,532	

Source: World Bank, 2004a

SSA FDI in China

FDI has contributed significantly to the Chinese economy. According to UNCTAD (2007), its share in fixed capital formation has been consistently over 10 per cent since 1993. SSA has, however, accounted for very little of that investment. Most of SSA investment in China comes from South Africa, with a number of large South African firms having a growing presence. This includes SABMiller (now the world's second largest brewing company), which has invested more than \$400m in China since 1994, and has equity in 30 local breweries (Goldstein, 2004). Other large investors are SASOL, which is about to join local Chinese investors in two very large coal-to-petroleum plants (each at more than \$3bn) in the North West Province of China, Kumba Resources (part of Anglo American) in the production of zinc, SAPPI (also owned by Anglo American, in paper), Polifin in chemicals and ABSA and NEDCOR in the financial sector.

Aside from these South African investments, there are a few isolated cases of firms whose origins lay in SSA investing in China. Chandaria Holdings, with its roots in Tanzania and Kenya, has for example a number of manufacturing plants in China which it sees as the focal point for its new investments in developing countries (Interview with Dr Manu Chandaria, June 2004). Although a number of African companies, mostly from South Africa and Nigeria, have been set up to conduct investment promotion activities in China, these seem to be mainly aimed at attracting Chinese capital into Africa rather than at establishing production in China (UNCTAD 2007).

3.3 *Aid*

Formal aid links between China and Sub-Saharan Africa go back to the Bandung Conference in 1955. Until the mid-1990s, much of this aid went towards liberation movements and the attempt to isolate Taiwan. Since the 1990s, this appears to have changed, with aid being increasingly directed towards broader strategic goals, especially the development of links with resource-rich SSA economies (Muekalia 2004; Kaplinsky et al. 2007; Brookes and Shin 2006; Pan 2006; Tull 2006). In October 2000, the China-Africa Cooperation Forum, which was held in Beijing, emphasized the need to enhance co-operation between China and financial institutions in Africa.

During the Forum, China also expressed willingness to reduce Africa's debt burden, promote investment, and assist in the development of human resources in Africa (Muekalia 2004). China's Africa Policy, adopted in early 2006, states that China-Africa relations are to be based on five principles: Sincerity, equality, mutual benefit, solidarity, and common development. The policy also reiterates that the one-China principle is the political foundation for the establishment and development of China's relations with African countries and regional organizations (China 2006a; Guoqiang 2007). This was further elaborated in the Beijing Summit of November 2006, which affirmed "a new type of strategic partnership" between China and Africa (King 2006).

Chinese aid to SSA can be grouped into six categories. The first is financial assistance for key investments. As of mid-2005, the Chinese government had provided aid to approximately 800 individual projects, including flagship projects such as the 1,860 km TAZARA railway linking Zambia and Tanzania in the early 1970s. Second, and linked to the first, China cancelled \$1.2 billion in debts owed by 31 African countries in 2004, and has continued to use debt relief as an aid tool. The third form of aid provided has been a growing training programme (China 2006b). China's African Human Resources Development Fund had provided training in China to 9,400 Africans by the end of 2004, and a further 3,800 places were planned for each of 2005 and 2006. 15,600 scholarships were offered to 52 SSA countries in 2005.

Fourth, China has provided technical assistance to SSA – more than 600 teachers and more than 15,000 Chinese doctors have worked in 52 SSA countries, including 1,100 present at the end of 2004. Fifth, in an initiative announced at the second ministerial

meeting of the Sino-African Co-operation Forum held at the end of 2003 China has instituted a programme of tariff exemption for 29 SSA economies, covering 190 products, including food, textiles, minerals and machinery. The policy took effect at the beginning of 2005, and coverage has since been extended to 400 items. Finally, China has in very recent years begun to provide peace-keeping forces to SSA, with 1,500 troops currently being deployed.

Infrastructure development and debt relief are the most widely useful, but also the most controversial of these forms of aid. Infrastructure aid is useful to almost every African country because of Africa's general need for rehabilitation, expansion, and updating of infrastructure. Debt relief is valuable because it is akin to general budget support, in that the resources freed up can be applied to other needs at the discretion of the government. The widespread usefulness of these two aid forms differs from, for example, tariff exemptions which depend on the country's export capability, or technical assistance which is always subject to problems of cultural understanding or the lack of it. Nevertheless, both infrastructure assistance and debt relief have proved to be controversial, with some observers arguing that they create more problems than they solve.

Many infrastructure projects have been linked to resource extraction, and have been subject to criticism on environmental grounds. Some construction projects, like stadiums and government office buildings, have been seen as contributing little to long-term development or poverty reduction, not only because of the nature of the project, but also because they are tied to Chinese inputs and/or do not adhere to good labour practices. Debt relief, like general budget support, is most useful when the country has a clear development agenda into which the freed resources can be channeled. In the absence of such an agenda, debt relief runs the risk of wasting resources or worse, of propping up governments that oppress their people.

More generally Chinese aid has been criticized for its failure to pay attention to a range of issues pertaining to good governance, human rights, environmental protection, and social justice (Bosshard 2007; Zafar 2007; Oya 2006; Tull 2006). There is evidence that this is beginning to change. China EXIM Bank, the country's official export credit agency and major lender to Africa, adopted an environmental policy in November 2004 (Bosshard 2007). Although it is still general and needs to be further specified, it is clearly a step in the right direction. The Chinese government is also moving cautiously towards greater collaboration with Western donors, especially around issues of environmental sustainability (Lancaster 2007). At the same time, it is clear that China does not want to lose its distinctive character as a donor with a special understanding and sympathy for Africa's development challenges. How this will be worked out, especially in the areas of human rights and social justice, remains to be seen. More research is needed. Not only does this need to be systematic, but since China is changing rapidly, studies also must be designed to capture the dynamics of change (McCormick 2008).

3.4 Channels in Aggregate

In assessing the overall impact of these links between China and SSA, we return to the architectural classifications set out in Section 2. We began by observing that China's impact on SSA can be gauged in relation to three primary channels: trade, production and FDI, and aid. Each of these channels, as we have seen in Section 3, is inter-related. China's trade impact (direct and indirect) in clothing and textiles, for example, is closely linked to the integration of SSA and Chinese firms in coordinated global value chains, and China's growing aid programme appears to be closely related to its need for traded commodities. We saw in Section 2 that these links may be both complementary and competitive, and direct and indirect.

We also noted earlier that there is a great danger of focusing on the present, the known and the measurable impacts. Moreover, partly because there is a great need to search for a solution to SSA's problems, and partly because the direct bilateral links are easier to see than the indirect, there is a danger of focusing unduly on the positive opportunities and neglecting the potentially negative disruptive impacts of China's growing impact on SSA.

With these caveats in mind, what can be said in aggregate about China's impact on SSA? Figure 5 is an elaboration of the synthetic framework which we set out in Figure 2 above. It presents some of the major conclusions which emerged from our review of what is known about the three key channels. A number of tentative conclusions can be drawn, although the major point of Figure 4 is not so much to provide a comprehensive overview, but rather a framework for thinking through the issues and the range and extent of potential impacts.

The conclusions which we draw are as follows:

- We are not able to fill all the "cells" in this framework. For example, it is possible that there will be indirect complementary effects in the FDI/production channel, and it is conceivable that Chinese-coordinated global value chains producing in the Middle East may source inputs from plants located in SSA. But we can find no evidence for this type of linkage. Does this inability to fill cells reflect the absence of impacts, unmeasured impacts or poorly-manifested impacts?
- Direct impacts are easily evidenced, both with regard to complementary and competitive effects. By contrast, indirect impacts are more difficult to evidence and much more difficult to measure.
- Data on the trade channel is much better than that on the production/FDI and aid channels. Is this a function of our lack of knowledge on production and aid and/or the availability of global trade data, or does the trade impact assert itself first and most significantly?

- With the exception of indirect competitive effects in manufacturing through the trade channel, the balance of existing evidence tends to support the view that the positive impacts (“opportunities”) are probably more important than the negative impacts (“threats”). But it is unclear whether this is a function of the availability of evidence, or the reality of the real world.
- It is difficult to generalize across countries and sectors. They might experience the impacts in each of these three channels in very different ways. For example, commodity exporters in SSA may gain from rising commodity prices (complementary indirect effects), whilst SSA commodity importers may suffer from the very same price rise (competitive indirect effects).
- We have no available methodology for providing a “net outcome”, even for individual countries and regions. This is partly because some impacts are not measurable, and partly because they involve trade-offs between winners (consumers buying cheap clothing imports) and losers (displaced domestic producers of clothing), often within the same country.

Figure 4: China and SSA: An Elaborated Synthetic View of Three Main Channels, and Complementary-Competitive and Direct-Indirect Impacts

Channel	Impacts		
		Direct	Indirect
Trade	Complementary	<ul style="list-style-type: none"> • Inputs for industries • Cheap consumption goods 	<ul style="list-style-type: none"> • Higher global prices for SSA exports
	Competitive	<ul style="list-style-type: none"> • Displacement of existing and potential local producers by cheap Chinese products 	<ul style="list-style-type: none"> • Competition in external markets – falling prices and falling market shares
Production and FDI		Direct	Indirect
	Complementary	<ul style="list-style-type: none"> • Chinese FDI in SSA, particularly in fragile states • Cheap and appropriate capital goods • Technology transfer • Integration in global value chains, particularly in clothing • Low-cost infrastructure 	
	Competitive	<ul style="list-style-type: none"> • Displacement of existing and potential local producers • Less spin-off to local economy than other foreign contractors • Use of scarce resources 	<ul style="list-style-type: none"> • Competition for global FDI and production platforms • Disinvestment and relocation by other foreign investors (for example, clothing and furniture)
Aid		Direct	Indirect
	Complementary	<ul style="list-style-type: none"> • Grants and concessional finance • Technical assistance • Training • Tariff exemptions • Debt relief 	
	Competitive		Chinese aid to Latin America creates productive capacity which competes with SSA producers and lowers export prices

4 The Issues

What follows from this analysis of the impact of China on SSA? How in particular is the manufacturing sector being affected, and how does this inform major policy choices?

In the discussion which follows in this section, we address the implications for policy in five key areas. We do not offer detailed prescriptions for change but, instead, as in the case of the synthetic framework used to assess the impact of China on SSA, aim to see these as promoting the basis for discussions with key stakeholders, within SSA and

China, and with interested organizations and multi-lateral agencies elsewhere. The key issues are:

1. The challenges posed to industrial policy and sectoral choice
2. Reacting to changing patterns of poverty and income distribution
3. Global and regional links
4. Thinking about the future
5. Filling the knowledge gaps

4.1 Challenges posed to industrial policy and sectoral choice

It is in the industrial sector that SSA is most clearly challenged by the growth of the Chinese economy. In the absence of Chinese demand for SSA manufactured exports (with the marginal exception of South Africa) China's impact on SSA industrialization arises from its growing exports. This affects SSA on two related and threatening fronts – competition in internal markets for domestically-oriented manufacturers, and competition in external markets from export-oriented industry.

It is in the clothing, textiles, furniture and footwear sectors that most is known about these issues. With regard to domestic markets, imports from Asia generally, and China in particular, are making life very hard for domestic manufacturers. Ghanaian furniture and clothing exporters find it increasingly difficult to compete with Chinese imports, as do South African manufacturers (Kaplinsky and Morris, 2008). A similar pattern can be found in the Ethiopian footwear sector (Tegegne 2007) and the Kenyan clothing sector (Kamau 2007). Although data is scarce, discussions with manufacturers and retailers in a number of SSA economies with domestic manufacturing sectors suggest that import penetration is increasing in all markets, and in most of the traded-goods manufactured sectors.

However, the challenge to SSA industry is much more substantial than these current impacts might suggest. This is because for much of SSA, industry is currently poorly developed, and is often largely confined to the food-processing industry (where products degrade over time and have a high transport-to-value ratio), building materials (a high transport-to-value ratio and producing customized products) and the informal manufacturing sector (producing to low levels of quality and largely using waste materials). The real policy challenge is not to existing industry, but to potential industry. That is, what space is there for SSA manufacturing to expand in the future? And, what implications does this have for the growth of dynamic capabilities, learning externalities and structural transformation?

What can be done? First, there is scope for improving the productivity of existing industries, often by working with value chains (for example, forestry, timber and furniture) rather than individual firms or sub sectors. Detailed firm-level analysis of productivity in the clothing sector in South Africa (Barnes, Morris and Gastrow, 2006) and in COMESA (Manchester Trade Team, 2005) reveal the nature of these productivity gaps. Kaplinsky and Morris (2006) also report evidence of significant productivity improvements following the introduction of training schemes in Lesotho. Competitiveness in all sectors is a moving target, and for various reasons, few SSA industries have hitherto been able to address this challenge of building dynamic capabilities. There is, however, no intrinsic reason why this should be the case, and there is thus considerable scope for effective industrial policies.

A second area of policy intervention arises with respect to trade policy. Here there may be a need for selective protection on the import side. But, as we saw in the earlier discussion of AGOA exports, SSA requires continued preferential treatment against China (and other Asian economies) in external markets. With regard to the US, the derogation on rules of entry in the clothing sector has been extended to 2012, but this remains a temporary solution. SSA governments would do well to develop active industrial policies that provide incentives to deepening value added in the textiles sector. EU rules of origin are so tightly specified and restrictive that they provide little scope for least developed country exports of manufactures from SSA, particularly in the clothing and textiles sector.

A further important lesson which emerges from China's growing trade presence is for SSA producers to be less concerned about the sector of production (for example, manufacturing versus services versus agriculture) and more focused on identifying niches where they can build barriers to entry to Chinese producers through the development of innovative capabilities. In manufacturing this may be increasingly difficult as Chinese competences grow, whereas in horticulture and services, including knowledge-intensive services, relative capabilities may be high, as in the case of Kenya's horticulture sector, South Africa's medical sector, and East Africa's wildlife tourism sector.

4.2 Reacting to changing patterns of poverty and income distribution

Trade-related income poverty and distribution impacts can be significant (McCulloch, Winters and Cirera (2002)). Although little is known about the detailed impact on China's trade on SSA patterns of income distribution, there are reasons to believe that it could be substantial.

On the positive side, one of the major implications of growing imports of manufactures from China is the benefits which this provides to consumers, particularly to low-income consumers. This is not just a phenomenon affecting SSA, since the decline in prices of basic manufactures is a primary factor holding inflation at bay in many OECD economies. As we have seen, many SSA manufacturers complain that Chinese products

are displacing locally-produced commodities. In many countries, the primary displacement effect is on imports of manufactures from other, non-SSA economies, with wholesalers and retailers switching their sourcing to cheap Chinese suppliers (Jenkins and Edwards 2006). This switching almost certainly has major positive impacts on consumer welfare. It is however an unmeasured impact and we have little idea of its overall significance in consumer welfare, or in which sectors the primary benefits are being felt. This is because most household consumption studies do not collect data at a sufficiently disaggregated basis, failing even to distinguish between food- and non-food purchases, let alone different types or sources of manufactures.

There are also rapidly-emerging negative consequences of Chinese trade on income distribution. On the one hand, employment in many labour-intensive manufacturing sectors is being lost, not only in export-oriented enterprises, but also in micro and small units targeting the local market. On the other hand, the rise in commodity production is associated both with capital-intensive technologies, and because of the large-scale of commodity production, to highly-concentrated forms of ownership. This is not an intrinsic problem of all primary production, since many soft-commodities (such as tea, coffee, cotton and horticulture) are labour-intensive and locally-owned. But, hitherto, most commodity exports to China have been oil and hard commodities, particularly basic metals.

There is an additional global dimension to these emerging patterns of income distribution, since manufacturing incomes are either largely local within SSA (labour) or flow to firms based in low- and middle-income Asian economies. By contrast, with the exception of South Africa, commodity production almost exclusively occurs through the operations of foreign transnational firms. A mitigating factor with regard to the distributional consequences of commodity production is that it is relatively easy to tax, providing revenues to governments. But as we shall see, the use of these state revenues does not necessarily suggest that their poverty and distributional impacts are positive.

4.3. Global and regional integration

Historically, most of SSA's trade links have been with the former metropolitan powers, either directly with the UK (in the case of Anglophone countries) and France (for Francophone countries), or more generally with Europe and North America. These links have been strengthened through the development of various forms of preferential trade arrangements (Lome-Cotonou, AGOA, EPAs and FTAs). It is not surprising therefore, that currently most of SSA's trade is with the historically industrialized countries.

Two major developments are disturbing these historical patterns. First, and this conclusion emerges from the data on trade patterns, there appears to be a naturally growing regional market in southern Africa, as is occurring in the case of Mercosur in Latin America, reflecting regional externalities in production (Evans, Kaplinsky and Robinson, 2006a). But, secondly, the rapid growth in trade between SSA and China (and

to some extent India) evidenced in Table 1 suggests a growing “magnetic pull” from the East. This poses a major policy challenge to SSA economies. In the context of stretched policy and administrative systems, and given the growing importance of regional ties in the global economy, who should they link with, and what forms of linkage might this involve? Should they aim to go North, go East or stay local?

Here it is possible to distinguish between what might be termed “Negative Integration” and “Positive Integration” (Evans, et al., 2006b). The former refers to the removal of barriers to trade, as in the case of FTAs and WTO-orchestrated multilateral trade liberalization. In contrast, positive integration involves targeted policies focusing on particular forms of market imperfections (for example, promoting learning about China and its language), strengthening poor infrastructure constraining particular geographical links, and actively seeking to develop various forms of “deep integration” in China-SSA global value chains. It may also involve the development of particular patterns of trade preference, as in the recent Chinese initiative to lower tariffs on imports of manufactures from the least developed SSA economies.

Increasingly, SSA economies are going to need to develop explicit policies in these areas. It will necessarily involve a “joined-up” mix of economic and political initiatives. As SSA loosens its links with Europe and North America, it will also be necessary for countries, to determine how much weight they wish to place on intra-continental regional links, and how much on forging new regional links with China and other Asian countries.

4.4. Thinking about the future – developing “dynamic capabilities”

As we have seen, economic and political links between China and SSA are changing very rapidly. From the perspective of SSA economies, therefore, it is the capacity to change, to grasp opportunities and to minimize threats that is key. In the business literature, this is referred to as the development of “dynamic capabilities”. It involves a combination of search capabilities, strategic-formulation capabilities and implementation capabilities, as well as the capacity to change continually as new threats and opportunities arise.

Many of the dynamic capabilities which are required to meet these challenges are prefigured in the policy-related issues discussed above. There is however one additional capability which is required, and that is the ability of SSA producers to anticipate future opportunities and threats opened up by sustained Chinese expansion. For example, one emerging opportunity is the promotion of Chinese tourism. By the end of 2006 China had granted tourist destination status to 26 African countries (People’s Daily Online, 6 November 2006). The number of Chinese tourists to Africa reached 110,000 in 2005, doubling the 2004 figure, according to government sources. With the growth in Chinese per capita incomes, there is likely to be more growth in tourism in the future. Such growth has clear links to the manufacturing sector in the form of opportunities for

producers of hotel furniture, textiles, uniforms, processed food and beverages, soaps and cleaning supplies, and the many other items needed to establish and operate a tourist destination.

Another possibility is in regard to China's food needs. At 3,040, China's per capita calorie consumption is on average 90 percent of that in the high income economies (Chen et al., 2006), so future import needs are likely to reflect a change in the composition of food consumption rather than a significant increase in its volume (FAO 2002). So far, China has sourced very little food from SSA (or, indeed, from elsewhere), partly because it has imported intermediates such as animal feed to support its own meat-producing sector. Most of the feed imported so far has been soya, and the primary origin of these imports has been from Latin America (Jenkins, Dussel Peters and Moreira, 2006). Although this has had knock-on effects of Ethiopia's exports of sesame (a substitute in some markets for soya), SSA has gained little from this trade in animal-feeds.

This raises a series of strategic issues for SSA food producers, which require careful consideration, informed by data rather than wild speculation. Will China continue to produce its own meat? Will its growing per capita income lead it to import horticultural products, fish and chicken? If they do, will these imports come directly from eastern and southern African economies which have a demonstrated comparative advantage in some of these sectors, or will SSA gain indirectly from China's growing imports from a supply-constrained global economy? As we saw above, Chinese investors are beginning to pioneer soya production in Mozambique and this may be a sign of future prospects.

These examples of tourism and soya are just that – examples. They represent future possibilities. At the same time, it is also necessary to anticipate future threats. A major potential problem for many SSA economies lies in the escalation of energy prices. Constrained global supplies and rapidly growing demand from China and India are already pushing prices far above previous estimates. So, too, the prices of other SSA imports, including food, might climb to new highs. What pressures will a rapidly diversifying Chinese economy place on economies such as South Africa who have become successful exporters of automobiles and auto components?

4.5. Filling the knowledge gaps

It is abundantly clear from the discussion above that we know more about the questions which have to be addressed on China's impact on SA than on the nature of these impacts. There are significant knowledge gaps, and unless these are filled, policy and capability development will be undermined and may be misdirected.

We can conclude with some confidence that the three primary channels of transmission are indeed trade, FDI/production and aid, and that we know more about the

direct impacts than the indirect impacts. We can also conclude that in order to understand China's growing involvement in SSA, it is as important to focus on the geostrategic and political imperatives, as on the narrow pursuit of financial gain. But, other than this, we cannot at present draw any conclusions with confidence. We cannot assess whether on balance China's impact is likely to be positive or negative, and for which countries and regions, and for which particular stakeholders in particular countries and regions.

In order to establish a good foundation for policy development, key knowledge gaps need to be addressed. These in turn suggest at least six different types of research that needs to be undertaken:

1. Base-line studies to assess the changing future impact of China on SSA
2. Analyses of the determinants of SSA competitiveness and the steps required to enhance productivity (for example, in clothing, textiles, footwear and furniture, as well as in export-oriented food crops).
3. A more thorough assessment of indirect impacts of China's trade on SSA, facilitating the development of appropriate policies for providing special and differential treatment to low income SSA economies in global markets.
4. Studies aimed at determining the impact of China on consumer welfare, income distribution and absolute poverty levels in SSA, through an analysis of the consumer benefits derived from cheaper imports, and the distributional implications of a switch in specialization away from labour-intensive manufactures to capital intensive commodities.
5. Studies that distinguish generic from sub-regional and country-specific impacts, aiding the classification of different types of SSA economies
6. Research into likely future areas of threat and opportunity

5 Conclusions

The detailed analysis presented in this paper has supported the growing realization that China's present and potential impact on SSA is both far-reaching and complex. The synthetic framework proposed in Section 2 has been helpful in disentangling the impact channels and their various effects, but even this systematic approach has produced only a partial picture of China's impact on SSA. This is at least partly because of gaps in our knowledge. Some of these gaps result from lack of data, but others arise because the organization of Chinese society means that the channels are intertwined in ways not immediately obvious to outsiders. This appears to be especially true of the production and aid channels, but may also apply to trade. The result is that some potentially important areas of impact may be misunderstood or missed altogether.

China's public pronouncements convey a desire for a relationship of South-South cooperation, of one developing country helping another (King 2006). Such a two-way relationship can only be fruitful if both parties respect one another and are ready to listen and learn from each other's experience. The relationship also needs to be underpinned by an understanding of how the actions of one are likely to affect the life of the other. Only then will genuine partnerships be possible.

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¹ The Open University, UK

² Institute for Development Studies, University of Nairobi, Kenya

³ University of Cape Town and University of Kwa Zulu Natal, South Africa

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⁵ This has major implications for the global manufactures-commodities terms of trade. See Kaplinsky (2005 and 2006)

⁶ Only four countries – Mauritius, South Africa, Gabon, and Seychelles – do not meet the criteria for “Lesser Developed Countries” under AGOA. Neither Gabon nor Seychelles is a significant clothing exporter, so effectively only South Africa and Mauritius are excluded from the derogation on the rules of origin (see www.agoa.gov or www.tralac.or.za for details of the rules and the derogation). Mauritius received a one-year derogation in 2004-05, but South Africa has had to abide by the rules of origin since the inception of AGOA. It should be noted that AGOA’s “Lesser” Developed Countries are not identical to the UN’s “Least” Developed countries, though the two lists are overlapping. In particular, Kenya and Swaziland are “Lesser” Developed Countries for purposes of AGOA, but are not on the UN’s LDC list.

⁷ Mali has also added to its spinning and weaving capabilities in 2004 and 2005, but this does not appear to be related to AGOA, as its textile exports to the US have remained virtually unchanged since 2004 (AGOA.info, 2008).

⁸ Although China was the major “winner” in global markets following quota-removal, it was not the only one. Other Asian countries – notably India, Bangladesh, Cambodia and Vietnam also prospered.

⁹ Table 7 significantly underestimates the loss of employment in South Africa since it only focuses on the impact of quota removal in 2005. However, job loss in South Africa has been much greater since 2001, reflecting the inability of its clothing manufacturers to source fabrics from Asia and growing import penetration in both textiles and clothing, much of it sourced from China.

¹⁰ There are two official sources of data on FDI from China: the Ministry of Commerce (MOFCOM) and the State Administration of Foreign Exchange (SAFE). The most recent detailed analysis of Chinese outward FDI has been provided by UNCTAD (2007) using both of these sources.