

# **Drivers of Long-Term Growth? Assessing the Impacts of Emerging Countries on Sub-Saharan African Economies**

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## **Abstract**

After the ‘lost decades’ Sub-Saharan African economies have exhibited positive growth rates, which has led donors to conclude that, thanks to emerging countries, stagnation is now a thing of the past. The paper shows the complexity of causalities and imbalances: these depend on: i) channels (trade, investment); ii) the emerging country (China having by far the strongest impact); and iii) African countries’ market structures. On the one hand, this growth relies on structural asymmetries. It is generated by distorted export structures that are based on commodities, whereas emerging countries follow the pattern initiated by developed countries. This growth falls if international prices decline, which necessarily occurs due to the inherent volatility of prices. High prices are moreover driven by the growth of emerging countries. This growth increases the specialisation of African economies in commodities. On the other hand, emerging countries have positive impacts via their investments in infrastructure, which fosters industrialisation and the spillover effects of investments in commodity sectors. Developed countries’ aid, due to the detrimental effects of conditionality, induces far greater asymmetries than does the aid of emerging countries. Asymmetries are dynamic processes and depend on the specificities of African countries - economic structures, geopolitical importance, political economy -, and the strategic policies of emerging economies.

## **1. Introduction**

After the ‘lost decades’ of the 1980s and the 1990s, Sub-Saharan African economies have exhibited positive growth rates in the 2000s. This has led observers – typically

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donors - to conclude that, thanks to emerging countries – China, India, Brazil -, stagnation is now a thing of the past. Sub-Saharan Africa may even offer a “contemporary expression of the emerging economies paradigm” (Bach, 2013). The paper shows the complexity of causalities and imbalances: these depend on: i) channels (trade, investment); ii) the emerging country (China having by far the strongest impact); and iii) African countries’ market structures. On the one hand, this growth relies on structural asymmetries. It is generated by distorted export structures that are based on commodities, where emerging countries follow the pattern initiated by developed countries. This growth falls if international prices decline, which necessarily occurs due to the inherent volatility of prices. High prices are moreover driven by the growth of emerging countries: the growth of African economies depends on factors that are external to them and will decelerate if demand in emerging countries decelerates. This growth increases the specialisation of African economies in commodities, while emerging countries consolidate their comparative advantage in manufacturing and threaten nascent African industrial sectors. As industrialisation is a key determinant of long-term growth, emerging countries may, in the long-term, erode their short-term positive impact on African economies. Asymmetries also stem from the attractive trade and investment policies African countries offer.

On the other hand, emerging countries have positive impacts, via their investments in infrastructure, which fosters industrialisation and the spillover effects of investments in commodity sectors. Developed countries’ aid, due to the detrimental effects of conditionality, induces far greater asymmetries than does the aid of emerging countries. Asymmetries are dynamic processes and depend on the specificities of African countries - economic structures, geopolitical importance, political economy -, and the strategic policies of emerging economies.

The paper is structured as follows. Firstly, it underscores the structural asymmetries that characterise Sub-Saharan African export structures, i.e. their dependence on primary commodities and a growth that is driven by exports, and therefore factors that are external to African domestic policies. Secondly, it explores whether emerging countries, notably China, amplify these structural asymmetries. Likewise examined are their positive (via demand and high prices) and negative impacts (incentives to keep the specialisation in commodities), emerging countries here following patterns that were initiated by developed countries. Thirdly, it shows that foreign direct investment also has complex effects, positive and negative, and that the asymmetries it conveys are similar across emerging and developed countries. Fourthly, it argues that the strongest asymmetry may be found in the aid device and in developed countries’ conditional assistance. Finally, it underscores the dynamical character of these asymmetries and their impacts.

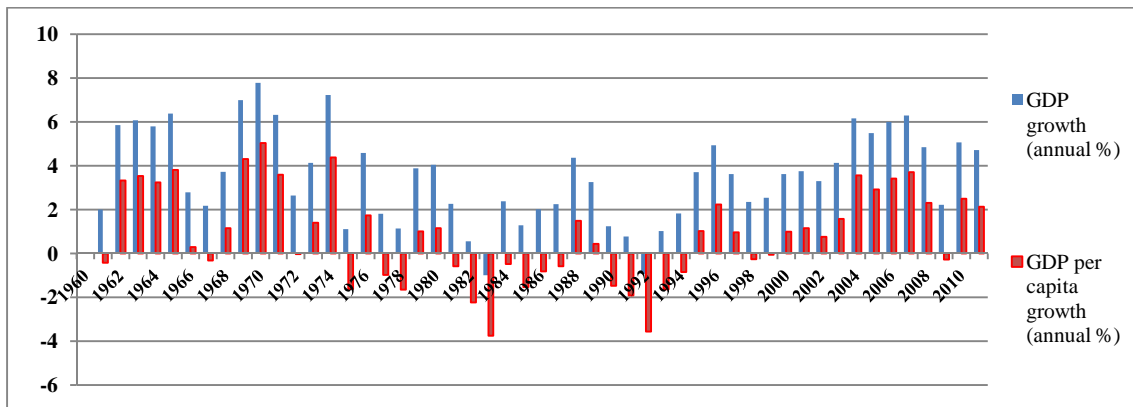
## **2. A growth driven by structural asymmetries: the importance of primary commodities in exports**

### **2. 1. An asymmetric integration in the global economy: commodity-based exports**

Sub-Saharan African (SSA) economies have enjoyed high growth since the early-2000s, with output growing by 5.1% in 2012 (IMF, 2013). Most development finance

institutions use this fact in order to argue that prospects for SSA are good, that the current characteristics of market structures of SSA economies do not constitute insurmountable issues and that the region may be on the verge of structural transformation (AfDB, 2013; IMF, 2013).

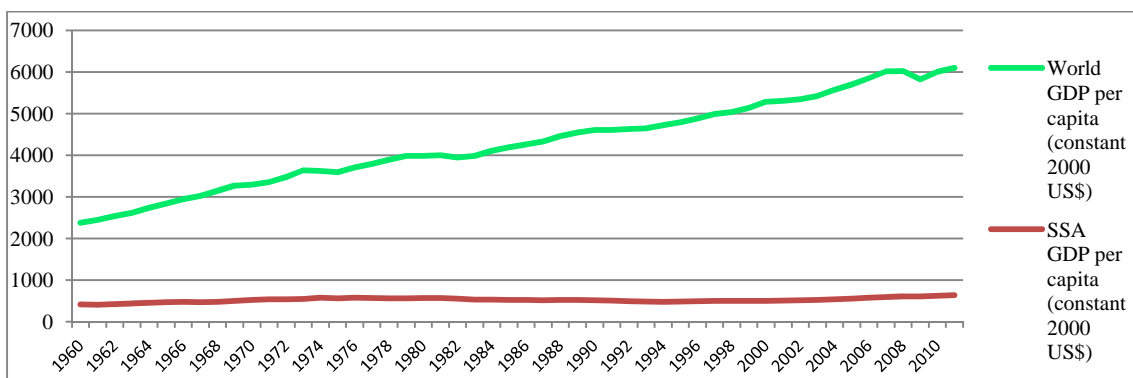
**Figure 1: Sub-Saharan Africa: GDP growth and GDP per capita growth, 1960-2011**



Source: World Bank World Development Indicators, May 2013

Underlying causalities and processes, however, are more complex. SSA growth performances must be put in a longer-term perspective, and in this case, the broad picture is that of a divergence vis-à-vis other regions.

**Figure 2: GDP per capita, Sub-Saharan Africa vs. the world, 1960–2011**



Source: World Bank World Development Indicators, May 2013.

Above all, Sub-Saharan Africa is characterised by a distorted export structure based on the dependence on primary commodities. It is this distorted structure that has been the main driver of growth in the 2000s, because of the dramatic increase in commodity prices since the early-2000s, both fuels and non-fuels prices.

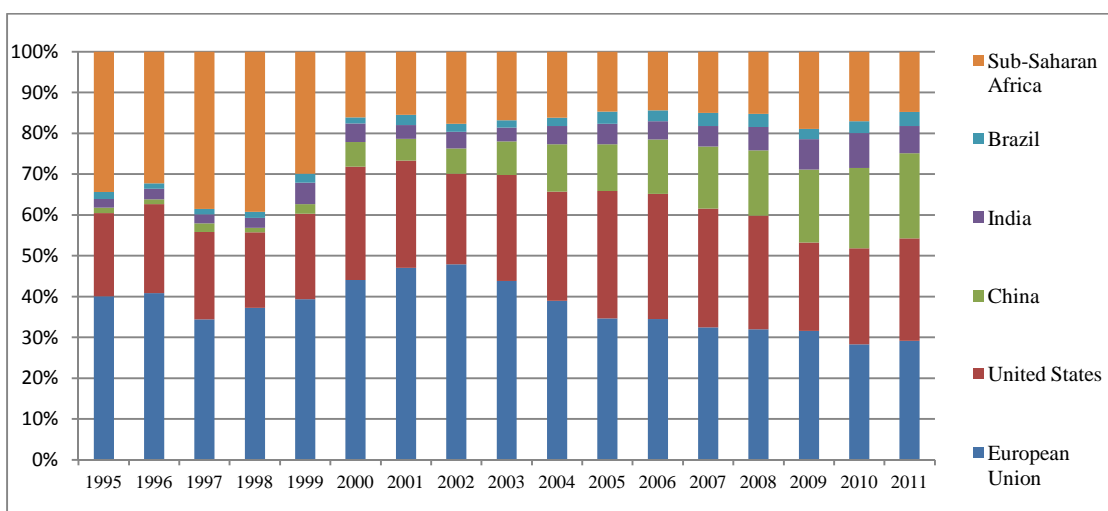
Commodity dependence is a key source of asymmetry: it is a market structure that generates vulnerabilities and that may be detrimental to growth. Commodity prices are

determined by international commodity markets, and increasingly by financial markets (Nissanke and Kuleshov, 2013). They are the result of several causes, e.g., the demand from large emerging countries, the levels of interest rates, of commodities inventories, of the US dollar exchange rate, among others.

These commodity prices are inherently volatile. Price volatility has a negative impact on GDP growth rates for countries whose exports and fiscal balances often depend only on one or two commodities, e.g., oil, coffee, copper, and the like: this is the case not only because prices may decline – as is already the case in 2013 for global metal prices (World Bank, 2013), but also because volatility *per se* is detrimental to long-term growth. Commodity-dependent countries are exposed to repeated price shocks, and their domestic policies may have little effect on their growth rates, in particular on trade and investment policies: growth may just stem from ‘good luck’ – e.g., vis-à-vis external price shocks -, and not from ‘good policies’ (Easterly et al., 1993). Commodity-dependent countries’ growth rates depend on the fluctuations of prices, which are determined by forces that are external to them, on the growth and demand of other countries (the US, EU countries, China) and on the vagaries of the latter’ domestic policies. For example, a unilateral decision that is driven by domestic considerations, such as the reorientation of the United States towards domestic shale gas, has an impact on oil prices, and therefore on SSA oil exporters, as well as these exporters’ direction of exports, as they must look for other oil importing countries.

In this context, the sustained demand for SSA commodities by large emerging countries, China in particular, represents a diversification of partners, which may attenuate the key asymmetry in global trade that is associated with commodity-based exports. All SSA countries export a lower share of their products to their ‘traditional partners’ (the US and the EU countries) than in 1990, and a greater share to emerging countries, in particular China.

**Figure 3: Sub-Saharan Africa: total exports and percentage of exports by partner**



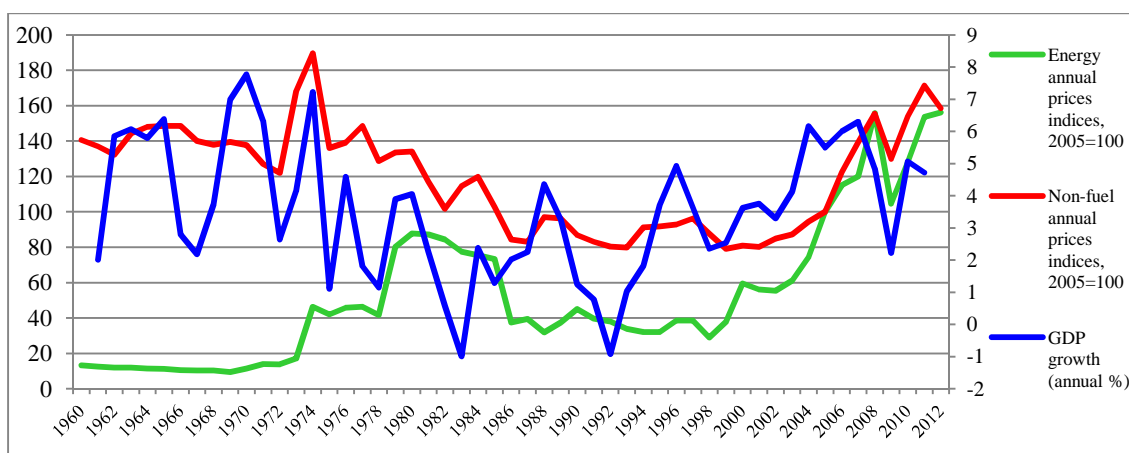
Source: <http://unctadstat.unctad.org>, author's calculations.

In addition, China has become a central driver of high prices in a significant number of commodities (Akyüz, 2012): the price boom of the 2000s stems from the increasing importance of China's demand in commodity price formation. High commodity prices obviously represent a positive gain for SSA exporters of these commodities, as they imply an enhanced fiscal space, hence more space for investment, which is a key cause of long-term growth.

China's demand is especially strong for metals, notably aluminium, copper and iron. While China's impact on world trade and prices varies by commodity, it has become the dominant importer of base metals and agricultural raw materials, and its role in food and energy markets, though small, is growing (Roache, 2012). China is now the number one energy consumer in the world, and its energy consumption is projected to double by 2017 and triple by 2025 from its 2008 level (IMF, 2011a). A one-percentage-point increase in China's industrial production growth induces a two-percentage-point increase in oil and copper prices (IMF, 2011b).

The influence of commodity prices on SSA growth rates, both for fuel and non-fuel exporters, is shown by the figure below. Most SSA countries are oil importers and vulnerable to oil shocks, e.g., in the 1973-79 period. The mid-2000s onwards witnessed a boom in commodity prices and co-movements between energy and non-fuel prices (Baffes and Haniotis, 2010). The debate remains open as to whether the increase in commodity prices of the 2000s is a price 'supercycle', and whether it will last. Assessments depend on the time span that is considered, as food prices remain below the prices of 1960s and the 1970s in real terms.

**Figure 4: Sub-Saharan Africa: growth rate (right scale) and commodity prices (annual price index, 2005=100, real 2005 dollars, left scale), 1960-2012**

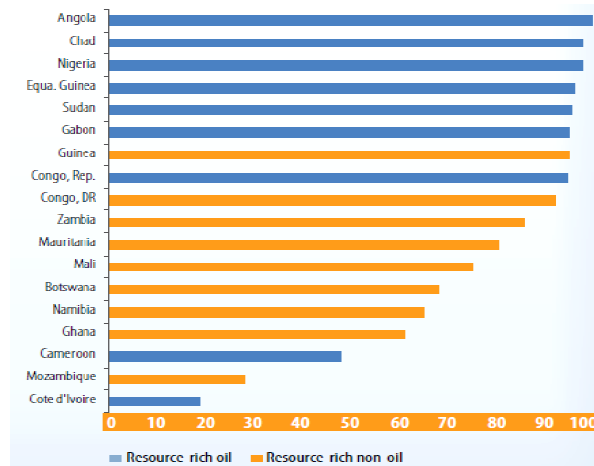


Source: World Bank Commodity Price Data and World Bank World Development Indicators, June 2013.

## 2. 2. The vulnerabilities induced by this distorted export structure

In particular, in 10 Sub-Saharan countries, commodities exports represent more 75% of total exports (World Bank, 2012). This distorted structure induces important vulnerabilities (Sindzingre, 2012).

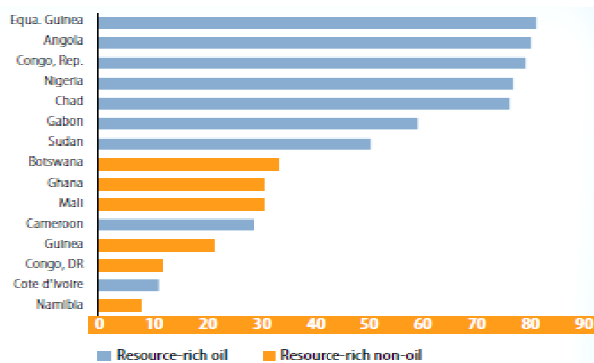
**Figure 5: Sub-Saharan Africa: resources export as % of total exports**



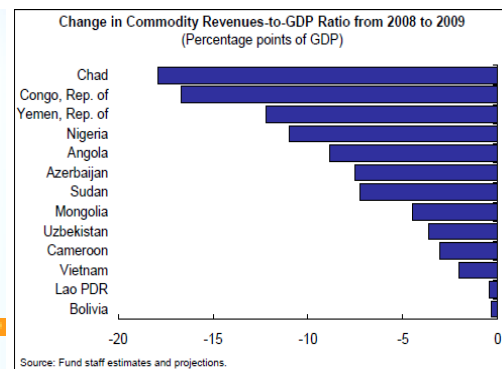
Source: World Bank (2012).

A key vulnerability of commodity-dependent countries is the dependence of their fiscal revenues on commodities with volatile prices. This is confirmed by the impact of the 2008-2010 financial crisis, which has been a major shock on international commodity prices. In oil-rich countries government revenues from natural resources represented 60% of total government revenues in 2011. This obviously makes their fiscal earnings highly vulnerable to any external shock.

**Figures 6: Government revenue from natural resources, 2011 (% general government revenue); the fiscal vulnerability of commodity exporters (to the 2008 crisis shock)**



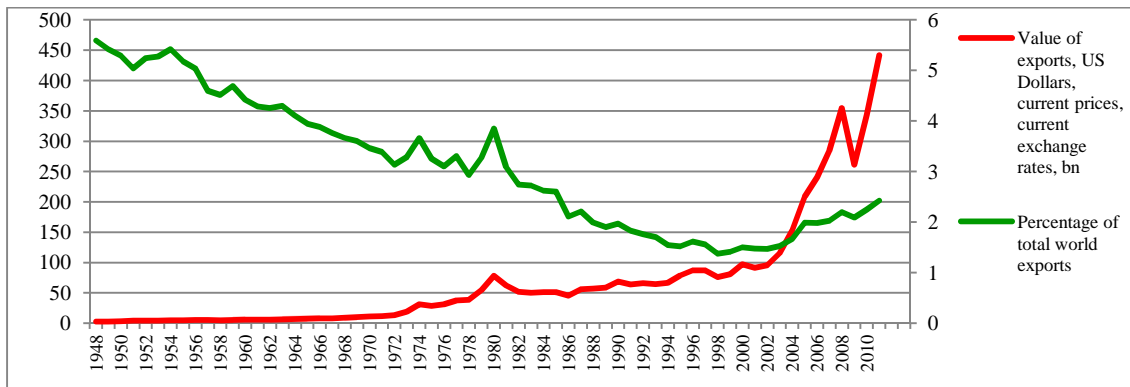
Source: World Bank (2012).



Source: IMF (2009).

This distorted export structure also affects SSA trade over the long-term. In particular, it explains the diminution of the share of SSA in global exports, due to the increase of the trade of other countries, which trade goods with more value-added, despite the increase of SSA exports in absolute value.

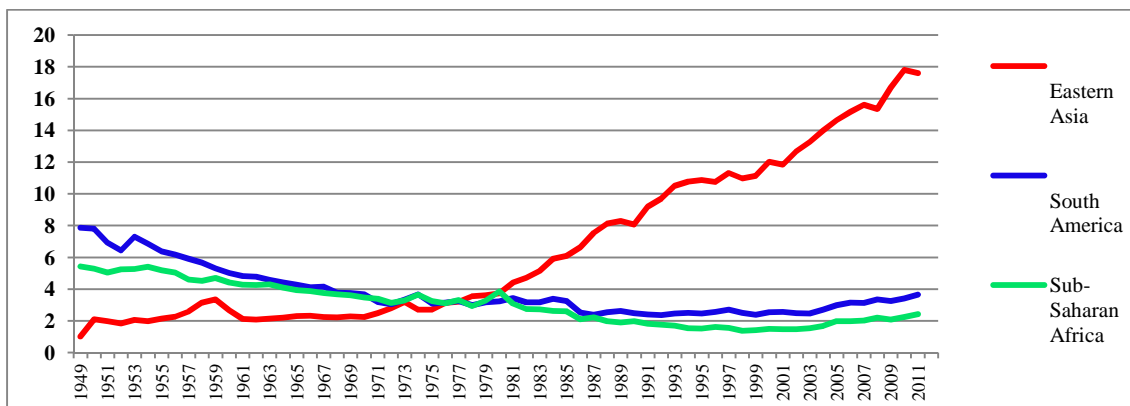
**Figure 7: Sub-Saharan Africa's exports: percentage of world exports (right axis) and value (left axis), 1948-2011**



Source: UNCTAD Statistics: <http://unctadstat.unctad.org>

The long-term forces that undermine Sub-Saharan African international trade and the region's international integration appear to generate more divergence than convergence. Contrasting relative vs. absolute perspectives, however, may give rise to different assessment: East Asia and its exceptional performances may also be viewed more as an 'outlier' in comparison to most developing countries, e.g. those of SSA and Latin America.

**Figure 8: Share of exports in world exports by region, 1948-2011 (percent)**



Source: UNCTAD Statistics: <http://unctadstat.unctad.org>

### 3. Structural asymmetries amplified by emerging countries? Positive and negative impacts

Are SSA distorted market and export structures amplified by the change in global economic balances and the increasing wealth and demand of emerging countries? They are both amplified and reduced. Emerging countries have positive impacts on SSA economies via higher demand for products exported by SSA and high prices for some primary commodities that are exported by SSA, and they have negative impacts via the

incentives, which their demand for commodities generates towards the strengthening of SSA countries' commodity-based structures.

### **3.1. Global trade's asymmetries: no 'exceptionalism' for emerging countries**

Are emerging countries representing unprecedented processes for SSA? In particular, would these processes generate more asymmetries than those created by the patterns of trade and investment that prevailed before emerging countries' increasing global importance? There are specificities associated with emerging countries. Commonalities, however, are numerous, and emerging countries do not exhibit any 'exceptionalism'. In contrast with an abundant literature, it may be argued that this is also the case of China.

With globalisation and since the end of the 20<sup>th</sup> century there has been an increasing trend towards internationalisation of production – the global value chains and global production networks: all countries are increasingly dependent on the demand from foreign markets; all industries use intermediate products from different countries due to global competition in order to enhance productivity and lower costs ('offshoring') (Foster et al., 2013; Baldwin, 2011; EU, 2013). These processes constitute the new features of international trade and affect all countries - be they developed, emerging and developing.

Regarding SSA, its structural asymmetries are generated by causes that characterise all its partner countries and not the developed more than emerging countries: SSA is dependent on forces that are external to its domestic policies, notably international commodities prices, and on external shocks, i.e. shocks on prices, or shocks on the growth of countries which trade and invest in SSA, be they the eurozone countries, the United States or emerging countries. They are all associated with asymmetries and uncertainty for SSA countries' growth. Global imbalances, internationalisation of economies and vulnerability to external markets' fluctuations affect all economies - and for example the prospects of EU growth.

Moreover, in a globalised world where all countries are put in competition for attracting investors, the asymmetries created by the obligation to devise attractive trade and investment policies affect all developing countries vis-à-vis all other countries, developed and emerging ones. When policies are devised unilaterally, outcomes for partner countries are thus always subject to changes over which they have no power. Unilateral trade preferences are an example: some US investors have come to SSA thanks to the AGOA<sup>2</sup>, and China's firms invested in SSA in order to use the AGOA for exporting to US markets: the ensuing growth or firm development may disappear as soon as the developed country decides to change its trade preferences policies (Kaplinsky and Morris, 2009a; Collier and Venables, 2007).

In addition, since the early-2000s, due to their spectacular growth and the stagnation of eurozone countries, emerging countries have been driving SSA trade. Too much may be assigned to emerging countries, which are subject to evolutions as any others. China's dramatic growth started at the end of the 20<sup>th</sup> century but witnesses a deceleration since 2010, which may be the turning point experienced by emerging countries – the so-called

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<sup>2</sup> African Growth and Opportunity Act, a unilateral system of trade preferences granted by the US to a group of SSA countries that meet specific conditions.



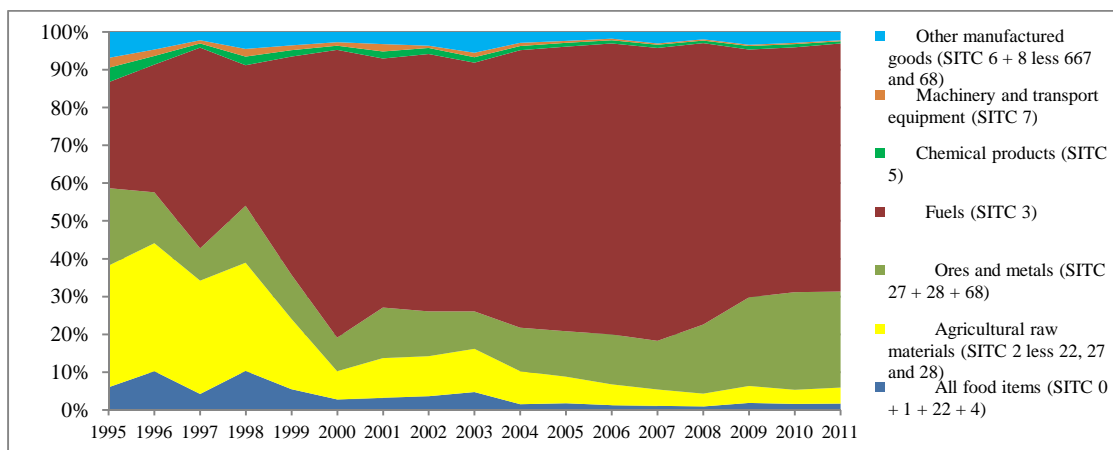
‘middle-income trap’ (Eichengreen et al, 2013). China reorients its growth towards domestic consumption, which is an uncertain process. These changes will have important impacts on the growth and exports of SSA countries and on the demand that China will have towards SSA products as inputs to its own growth – as any global business cycle, a possible deceleration of China’s growth may modify the composition of the SSA products that China will import and alter its investments in SSA. Growth in emerging countries remains fragile in an interdependent world, and the growth of the two other important emerging countries, India and Brazil, may decelerate in the 2010s. The growth rates of Brazil and India have indeed decelerated in 2013<sup>3</sup>.

### 3. 2. China trade relationships with Sub-Saharan Africa

SSA economies have diversified their trade and investment relationships from ‘traditional’ partners – the United States and European countries -, and increase their trade and investment linkages with emerging countries - even if China, India and Brazil constitute the main emerging countries that import SSA exports. This reduces the vulnerability of SSA exporting countries to the business cycles of a single product and the volatility of a country’s growth rates.

SSA exports to emerging countries are characterised by spectacular asymmetries. A first dimension of these asymmetries is that SSA exports mostly commodities to these emerging countries, and in particular fuels (Ye, 2010).

**Figure 9: Sub-Saharan Africa exports to China by key product groups, 1995-2011**



Source: UNCTAD Statistics: <http://unctadstat.unctad.org>; author’s calculations.

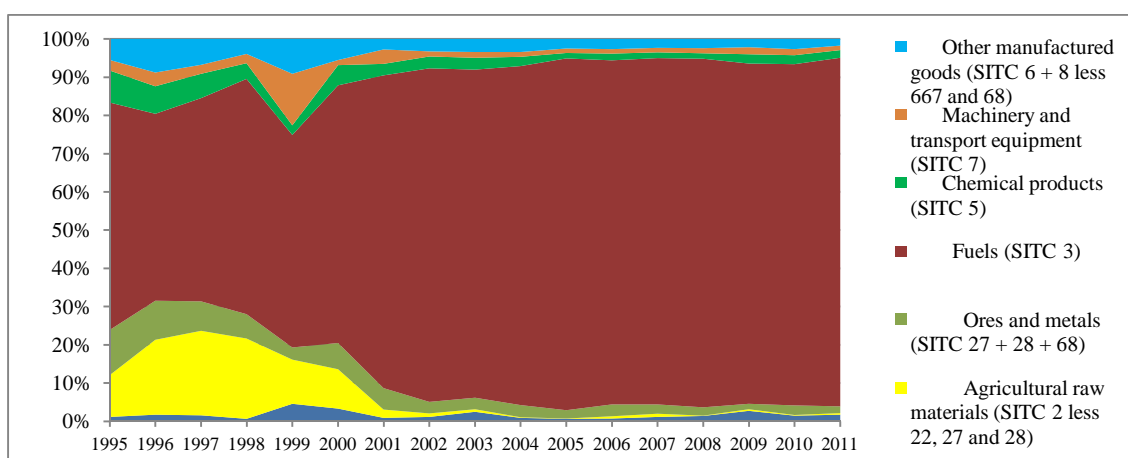
China’s exports to SSA are very different from its exports to developed countries, which is the second dimension of the asymmetry of trade between SSA and China. China exports low-end cheap manufactured products, which are a threat to SSA manufacturing sectors and may strengthen the specialisation of commodity-exporters in this export pattern (Kaplinsky and Morris, 2008).

<sup>3</sup> The OECD Composite Leading Indicators (CLI) indicated in June 2013 that in India, growth is below trend. <http://www.oecd.org/std/clits/compositeleadingindicatorsclisoecdjune2013.htm>

If China's growth rates continue, however, its demand for SSA products will not only be directed towards primary commodities but also towards low-end manufactured products that will no longer be made in China due to increasing local factor costs. The sector of manufactured products with little sophistication— which is usually labour-intensive – is often viewed as a first step towards industrialisation, diversification and therefore long-term growth, and China may be here a factor of structural change for SSA economies.

Other emerging countries interestingly exhibit even deeper asymmetries. For example, SSA exports to Brazil are almost only made of fuels.

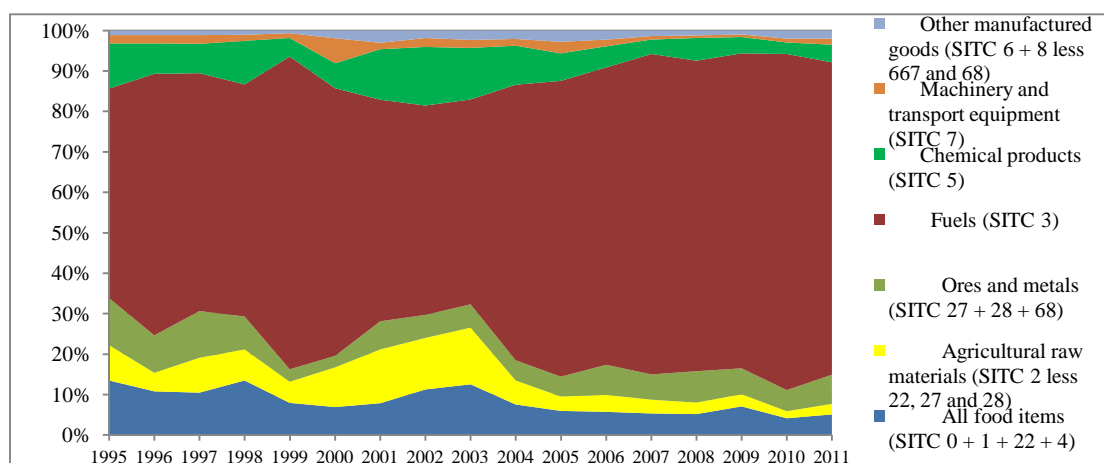
**Figure 10: Sub-Saharan Africa exports to Brazil by key product groups, 1995-2011**



Source: UNCTAD Statistics: <http://unctadstat.unctad.org>; author's calculations.

Exports of SSA to India are similarly mostly made of fuels.

**Figure 11: Sub-Saharan Africa exports to India by key product groups, 1995-2011**



Source: UNCTAD Statistics: <http://unctadstat.unctad.org>; author's calculations.

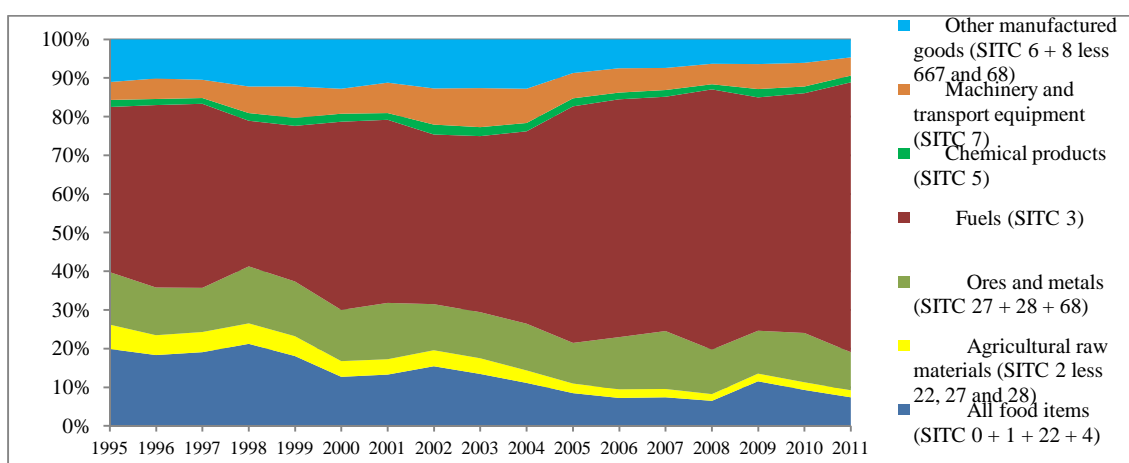
As industrialisation is a key determinant of long-term growth, emerging countries may, in the long-term, erode their short-term positive impact on SSA economies.

### 3. 3. Do developed countries do better? The similarity of emerging and developed countries trade structures

Emerging countries' trade structures with SSA do not exhibit any 'exceptionalism': it is similar to the relationships that have been developed by western countries over the 20<sup>th</sup> century. Western countries' trade commodities with SSA since the colonial period and their trade patterns still broadly follow the model of the 'small colonial open economy' - exporting commodities, importing manufactured products - coined by Hopkins (1973).

These relationships are all characterised by asymmetries, and all trade partner countries of SSA, developed countries, and then emerging countries, follow a similar pattern, where SSA exports primary commodities and imports industrial products (Wang and Bio-Tchane, 2008).

**Figure 12: Sub-Saharan Africa exports to G8 countries by key product groups, 1995-2011**



Source: UNCTAD Statistics: <http://unctadstat.unctad.org>; author's calculations.

In addition, even if China's trade may be viewed as an expression of broader political and diplomatic policies, this does not constitute a specificity: as has been underscored for ex-colonial powers (France in particular), trade and investment from developed countries are similarly backed by political economy contexts.

## 4. Foreign direct investment: complex effects, and similar asymmetries

### 4. 1. China's investment in Sub-Saharan Africa

Emerging countries, and China in particular, constitute important drivers of foreign direct investment (FDI) in SSA. Chinese FDI to SSA as a share of total FDI to the

region climbed from less than 1% in 2003 to 16% by 2008 (IMF, 2011b). China's FDI in SSA does not represent an important part of total Chinese outward investment, but for SSA it represents a rising share of its total inward FDI. This is a dimension of asymmetry between the two regions.

Investment in SSA countries exhibit wide variations and differences. Chinese investment may represent an important share of inward FDI in some countries. Yet in a large and diversified economy such as South Africa, the stock of Chinese investment at the end of 2010 amounted to between \$4.153bn and \$5.616bn. China is only the 6<sup>th</sup> largest investor in South Africa, with 3.7% of FDI stock (90% being a single investment, ICBC in Standard Bank of South Africa) (Gelb, 2013).

According to the criteria developed by Dunning (2000; 2002), the motives of FDI may be market-seeking, efficiency-seeking, resource-seeking, and strategic-asset-seeking motives. China has been viewed a mainly driven by resource-seeking motives.

A great share of FDI is directed towards primary resources, in particular oil. China multinationals, mainly state-owned enterprises or backed by the state, thus invest in the resource sectors, such as oil and mines (Kragelund, 2009). Much of this type of FDI consists in a contractual package that 'exchange' commodities for investment by Chinese firms, often in infrastructure – the so-called 'Angola model' (Alden and Alves, 2009; Corkin, 2008, 2011a). These 'commodity-for infrastructure' deals imply a risk of lock-in SSA structure in the production and exporting of commodities. The FDI of other emerging countries, Brazil and India, is more limited than that of China. It is more diversified and may include investment in agriculture and financial services.

Emerging countries' investment exhibit similar asymmetries and is driven by motives that are similar to developed countries. Developed country FDI in SSA is similarly more important than SSA investments in developed countries. Likewise, developed countries' investors invest in the resource sector: for example, in Angola, the United States is by far the leading investor in the oil sector (GAO, 2013). Furthermore, large Chinese investments are often backed by China's government: this may be the case for large western firms, e.g. French utilities investing in SSA, large investments abroad often being a dimension of foreign policy.

#### **4.2. Emerging countries as promoters of structural change for Sub-Saharan African economies?**

Emerging countries, however, have the potential of reducing these asymmetries. The entering of emerging countries into trade and investment relationships means more players and more capital inflows towards SSA, which is positive. Also, the growth of emerging countries implies increasing wages and costs in these countries, hence the opening of windows of opportunities for certain SSA countries that can be substitutes, where FDI can outsource activities of the low-end segments of production networks

Moreover, emerging countries invest in SSA industrial sectors, which is an opportunity for structural change since industrialisation is a key determinant of long-term growth (Rodrik, 2009). Besides oil and mining, Chinese investment is directed toward manufacturing, construction, finance, agriculture, services (IMF, 2011b). Motives of FDI may go beyond the traditional resource-seeking or market-seeking motives, and emerging countries FDI appears to be increasingly moved by the 'linkages' driver, in

which firms invest in order to augment their competences by learning from their overseas investments – ‘leveraging’ FDI (Kaplinsky and Morris, 2009b). Motives of efficiency are also present (such as the buying of Standard Bank, the largest bank of South Africa<sup>4</sup>).

In some SSA countries Chinese FDI is more concentrated in the manufacturing sector than in primary commodities. An example is Ethiopia (IMF, 2011b), e.g., its shoe sector, where one of the largest shoe exporters in China has started an important investment in 2013: Chinese manufacturers increasingly invest in SSA in order to benefit from preferential trade tariffs and lower labour costs<sup>5</sup> (Dinh et al., 2012). China established several Special Economic Zones (SEZs) in SSA with the aim of promoting manufacturing. An increasing number of private medium and small enterprises from China operate in SSA in the sectors of manufacturing, infrastructure, agriculture and services (Shen, 2013; Gu, 2009). Moreover, even if emerging countries’ trade and investment would mostly target the sector of primary commodities, this is not necessarily an obstacle to industrialisation. It may be argued that investments in commodity sectors induce positive effects in other sectors, including the manufacturing or the service sectors, via forward and backward linkages in Hirschman’s (1958) sense (Morris et al., 2011; 2012). Sub-Saharan African countries, however, differ among themselves; for example, as shown by Corkin (2011b), China’s investment in Angola’s oil sector generated little spillovers. Such impacts are subject to wide variations across SSA.

In addition, emerging countries invest in infrastructure, and infrastructure is a key determinants of growth (Calderon and Serven, 2010; Foster and Briceño-Garmendia, 2010). Indeed, the low levels and quality of infrastructure - power, electrification and transport - generate huge transaction costs on the circulation of goods and people, and impede competitiveness, trade and therefore diversification and growth. China has a long history of provision of infrastructure in SSA, and the enhancing of infrastructure by investors from China and other emerging countries is undoubtedly beneficial for SSA countries’ growth.

## **5. An important difference: conditionality in development cooperation**

### **5. 1. A key cause of asymmetry: Sub-Saharan African countries’ dependence on foreign aid**

Some SSA countries are excessively dependent on aid, e.g., for budgets, investment, maintenance, infrastructure, health, education. There are several indicators of aid dependence: notably, the percentage of GNI; the percentage of gross capital formation; the percentage of imports of goods, services and income; and the percentage of central government expenses.

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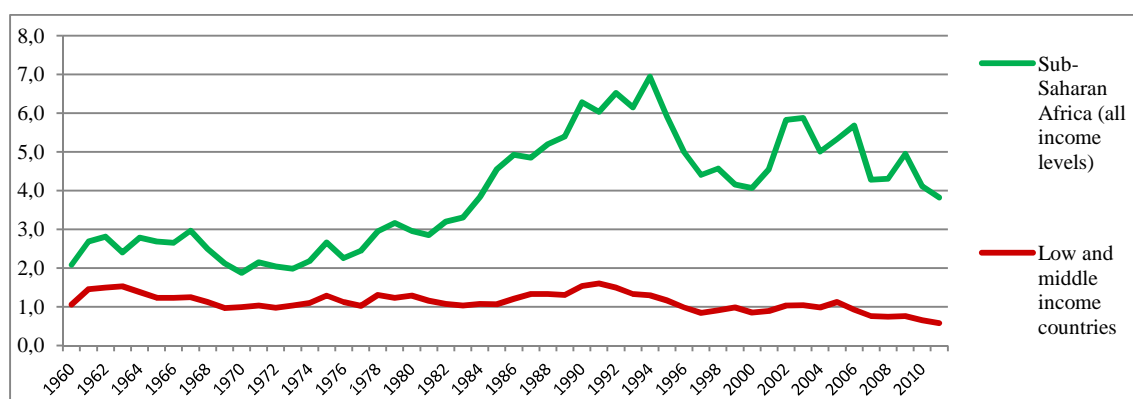
<sup>4</sup> The Industrial and Commercial Bank of China (ICBC) concluded the largest foreign direct investment deal in South African history in 2007, when ICBC paid \$5.5 billion for a 20 percent stake in Standard Bank, Africa’s largest bank (China Daily, 25 March 2013).

<sup>5</sup> William Wallis, China plans multimillion Ethiopia investment, *Financial Times*, 3 June 2013.

All these indicators are very high for SSA. Net official development assistance (ODA) to SSA represented \$20 per capita in 2000 or 4.1% of GNI; \$54 per capita and 4.3% of GNI in 2010 (World Bank Development Indicators/WDI, 2012). In 2000, ODA represented 23.1% of gross capital formation, and 18.8% in 2010. In 2000, ODA represented 11% of imports of goods, services and income; in 2010, 9.9% (WDI, 2012).

Despite important variations within SSA, besides the small-island economies of Oceania, SSA is the region of the world that is the most dependent on aid, and much above the average of low-income countries (LICs) and middle-income countries.

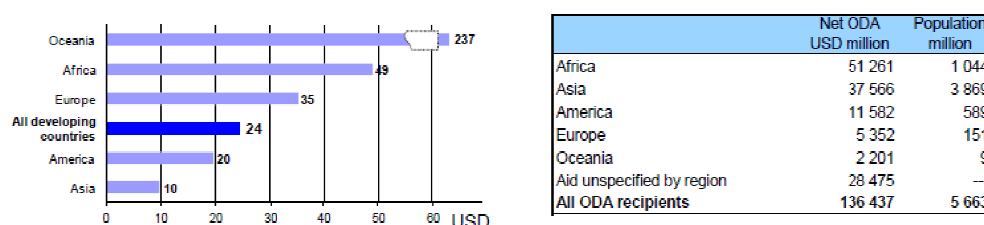
**Figure 13: Net Official Development Assistance (ODA) received, in percentage of Gross National Income (GNI)**



Source: World Bank World Development Indicators, May 2013.

This poor performance is more driven by SSA low-income countries than by SSA middle-income countries. Indeed, for the general category of low-income countries, in 2010 the ratio net ODA/GNI was 9.6%; the ratio net ODA/gross capital formation was 40.9%; and the ratio net ODA/imports of goods, services and income was 24.6%.

**Figure 14: Net ODA receipts per person (US\$) and net ODA and population of aid recipient countries by region (2011)**



Source: OECD (2013).

As shown by Easterly (2009), the argument that aid per capita to SSA is in fact not excessively high is misleading because aid is characterised by a bias towards small countries: countries with large populations get little aid as percent of GDP (Nigeria, South Africa), while the opposite prevails for many small SSA countries, and the

median SSA country is more aid dependent than the median non-SSA developing country.

Aid dependence induce well-known negative effects, e.g. Dutch disease (Killick and Foster, 2007; Harrigan, 2007), intrinsic negative effects of volatility - as aid is very volatile, even more than earnings due to the volatility of commodity prices (Bulir and Hamann, 2008) -, and the undermining of institutions, in particular tax institutions (Moss et al., 2006, Auty, 2007).

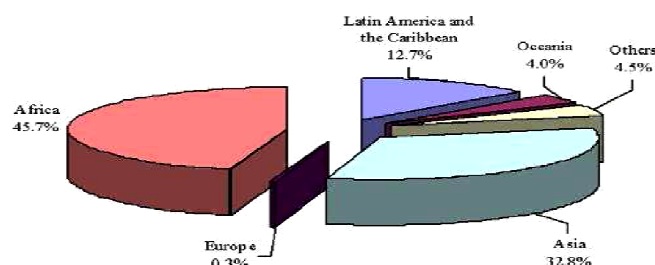
## 5. 2. China's specific mode of development cooperation: a trade aid-investment-nexus

As analysed by Brautigam (2009; 2010), Chinese aid to Africa, which began in the 1960s, is not a recent phenomenon. Chinese aid includes subsidising infrastructure, including rehabilitating former aid projects, direct finance to Chinese companies, and resource-backed infrastructure loans). China's aid is distributed via several channels, the Ministry of Commerce, the Ministry of Foreign Affairs, the export credit agency of the EximBank and the China Development Bank (Davies, 2008).

China's aid consists of grants and zero-interest loans from the Ministry of Commerce and concessional loans from China EximBank – although levels of concessionality between China and other donors cannot be compared, because of missing information (Christensen, 2010). China's aid is indeed not easy to compute: loans are difficult to distinguish from export credits, and Chinese statistics do not use the OECD Development Assistance Committee (DAC) criteria that define Official Development Assistance (ODA)<sup>6</sup>. It is difficult to disentangle Chinese aid in the sense of official development assistance (ODA) from other flows, notably commercial flows.

According to the government of China's White Paper on foreign aid (Chinese Government, 2011), China's financial resources provided for aid fall into three types: grants (aid gratis), interest-free loans and concessional loans. The first two types come from China's state finances, while concessional loans are provided by the EximBank. This demonstrates the close links between trade, investment and aid. For Brautigam (2009), Chinese aid to Africa is much less important than EximBank export credits.

**Figure 15: Geographical distribution of China's foreign aid funds in 2009**

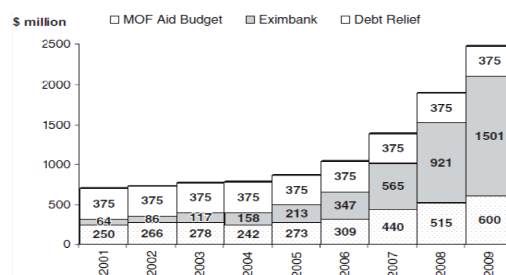


Source: White Paper on China's Foreign Aid (2011).

<sup>6</sup> See also Brautigam's very informative and relevant blog: <http://www.chinaafricarealstory.com>

China's aid to SSA nevertheless exhibits a clear increase (Brautigam, 2009; Mlachila and Takebe, 2011).

**Figure 16: China's aid to Africa, US\$ millions**



Source: Brautigam (2009).

There are important variations of aid flows across countries. Despite the difficulty of comparisons due to the heterogeneity of flows and lack of data, in some countries China's aid may be substantial. The United States Government Accountability Office (GAO) has compared of bilateral aid flows from China and the US case in Angola, Ghana and Kenya (GAO, 2013). In Ghana for example, US grant commitments to Ghana exceeded China's during the period 2006-2010. From 2001 to 2010, the US committed about \$1.6 billion in aid in the form of grants to Ghana, and China committed approximately \$18 million in grants in 2007, 2008, and 2011. In contrast, the US government committed smaller amounts of loans for Ghana than China: China committed, or agreed to, more than \$3 billion in loans to Ghana between 2006 and 2011. China's loans were primarily for infrastructure construction, the repayment of some loans being tied to commodities (oil, cocoa) (GAO, 2013). In Kenya, the US government committed more grant assistance to Kenya than China did in 2009 and 2010, but the GAO acknowledges that China has become one of the top donors to Kenya since 2009, primarily providing highly concessional loans (GAO, 2013).

Chinese aid differs from that of other donors. A substantial part of Chinese aid consists in 'packages' associating aid, trade and investment, where contracts organise the exchange of financing for a given commodity, e.g. oil. As underscored by Christensen (2010), in contrast with developed countries' donors, Chinese financing is largely focused on infrastructure investments; part of export credits and other financing for infrastructure investments are linked to extraction of natural resources through 'infrastructure for natural resources' deals. Such financing is less concessional than aid from traditional donors and resembles rather exports credits. China's aid differs from 'traditional' donors by its close ties with the state banks and state enterprises, often involved in the implementation of China's foreign policy vis-à-vis SSA (Christensen, 2010). China's model of 'economic cooperation' has in fact followed the one practised by Japan in Asia, linking aid, investment and trade, despite important operational differences between Japanese and Chinese aid (Nissanke and Söderberg, 2011).

There are other differences between developed countries' and China's ODA. As underscored by Brautigam (2009), Chinese aid has not suffered from volatility in amounts, paradigms and fads that have characterised Western aid (e.g., since the 1960s,



a succession of focuses on infrastructure, then agriculture, then poverty reduction, then public expenditure reform, etc.).

A key point is that this mode of development cooperation made of a nexus of aid, trade and investment does not include conditionalities on particular policies - economic or political. This is a major difference with western aid, multilateral or bilateral. Whether it is made of loans or grants, the development assistance of OECD-DAC countries, of international financial institutions (IFIs) or of a major donor such as the European Commission is conditional to economic, and often, political reform (e.g. ‘good governance’).

In contrast, China’s aid is more a development cooperation driven by diplomatic and political economy relationships, which go back to the period of independence of SSA countries in the late 1950s-early 1960s and Cold War context, and its motives are broader than strictly economic ones, as they explicitly include the support of Chinese firms (Brautigam, 2009; Rotberg, 2008; Shinn and Eisenman, 2012; Taylor, 2009). China’s aid also involves relationships of barter. China’s claims non-interference with recipient countries domestic affairs and its cooperation therefore deals with all regimes, be they illiberal democracies or even ‘pariah’ regimes (Alden, 2007). Chinese aid is therefore often criticised for supporting dictatorships and corrupt political regimes.

### **5. 3. Developed countries aid as based on conditionality: the most detrimental asymmetry?**

Many dimensions of developed countries’ ODA, however, convey aspects that do not compare positively with China. This is particularly the case with the key difference between China and developed countries, which, for the latter, is financial assistance that is conditional on recipient countries’ domestic reforms. The latter may be very intrusive and prescribe drastic changes in recipient countries economic and political equilibria. Given their very asymmetric position – exemplified by the ‘donor’-‘recipient’ relationship - aid-dependent low-income countries have little possibility to refuse these reforms.

There is no doubt that the absence of conditionality on financing may induce many problems, e.g., the support of certain types of political regimes, opaque deals, corruption and the like. It may be argued, however, that conditional aid as practiced by developed countries – multilateral or bilateral -, also includes these problems, in addition to other negative effects that are inherent to conditionality itself. While for non aid-dependent middle income countries, developed countries and China’s cooperation may not exhibit large differences, as this cooperation is driven by more balanced bargaining power and common interests, for low-income aid-dependent countries, theoretical debates are complex: i.e. theoretical assessments of trade-offs between business-based unconditional finance and conditional aid for dependent countries. The latter may be the most asymmetrical device.

The detrimental aspects of conditionality are inherent to the mechanism of conditionality itself - committing aid ex ante and making aid conditional on reform. They have long been demonstrated since the first programmes of stabilisation and structural adjustment prescribed to SSA governments by the international financial institutions – the IMF and the World Bank. When SSA governments were obliged to

call the IFIs for financial rescue from the 1980s onwards, due to the price shocks that affected them in 1979 - stemming from their distorted commodity-based export structure -, notably a severe drop in non-energy prices, the IFIs implemented policy-based lending. Loans were conditional on government policy and institutional reforms in the borrower country, aid here being a lever to encourage policy reform, i.e. the conditions that are attached to the aid. As SSA countries' performance did not improve in the 1980s and 1990s – the 'lost decades' -, the IFIs reacted in augmenting their conditionalities in the 1990s. The latter became increasingly structural and extended to non-economic issues, e.g., 'governance'.

The effectiveness of conditionality and the extent to which the reforms demanded by donors are in fact implemented, is obviously mediated by the recipient government's willingness to accept the conditions and its ability to implement them (Morrissey, 2004). Conditionalities, however, by definition express the existence of tensions, imply a limitation of sovereignty and trigger resistance: borrowers do not comply with conditions or do it with reluctance. Conditionality inherently induces policy reversals (stemming from the 'if no compliance, no money', the 'exchange of reform for financing', the 'buying of reform'). It paves the way of the 'aid game' that has been described as a 'ritual dance'. A reaction of the IFIs in the 2000s was to promote the 'ownership' of reforms by recipient countries: conditionality, however, by definition cannot enhance 'ownership' of reforms that are prescribed in exchange for finance - conditional reform's 'ownership' being here paradoxical prescriptions<sup>7</sup>. The persistent failure of conditional IMF stabilisation programmes has led, on the donors side, to a repetition of lending since the 1980s onwards, and on the recipients side, to the continuation of dependence on donor lending, which has been acknowledged by the IMF (the 'prolonged users', IMF-IEO, 2002).

Another reaction of IFIs has been to add 'selectivity' to conditionality, where donors lend to governments that already have good policies and institutions (Thomas, 2004). As a result conditionalities appear to be effective mostly in countries that wish to reform (Dreher, 2008). It may be noted that despite lessons that emerge after decades of questions on this device, conditionality has interestingly been kept intact by the European Commission for its programmes vis-à-vis EU member countries since the onset of the eurozone crisis in 2010, with similar detrimental consequences.

Attempts to reform conditionality have met with mixed success, e.g. budget support, 'output-based' aid, ex post incentives for the donor to reward good policies, etc. The devising of ex post and ex ante conditionalities or incentives do not change the intrinsic asymmetry of the device of conditionality, i.e. the relationships between the one who has the power to give money and therefore impose conditions, and the one who needs it.

Conditionality indeed demonstrates the inherent divergence of interests and asymmetry between the aid-providing IFI and an aid-receiving government, including domestic interest groups (Mayer and Mourmouras, 2005). These divergences between donors and recipients, which are intrinsic to the mechanisms of conditionality, entail negative effects. Donors may impose conditions on unwilling recipients, while recipients may be willing but unable to implement conditions. Aid is typically affected by the 'Samaritan dilemma' (Gibson et al., 2005). For example, if the recipient government knows that donors condition their aid on a reduction of poverty, it has little incentives to exert high

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<sup>7</sup> For example, 'own!', 'be sovereign!', 'be a partner!'...

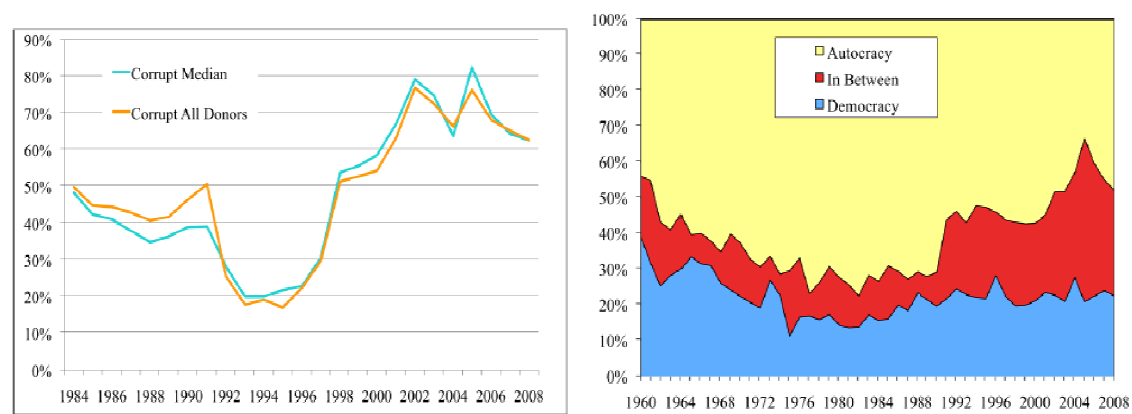
effort toward this objective, as in doing so it will receive less aid in the future; and the ‘Samaritan’s dilemma’ is aggravated by moral hazard: the donor can never know if a poor outcome is the result of low effort (‘bad policies’) or ‘bad luck’ (Svensson, 2005). Conditional aid indeed inherently exhibits important coordination failures (including information problems on other donors’ aid).

On their side, donors did not enforce the conditions, due to their own institutional incentives to lend. Loans may also be given to enable old aid loans to be repaid. The device of conditionality has therefore contributed to the erosion of the credibility of the IMF vis-à-vis borrowing countries (Svensson, 2000; Villanger, 2003). Marchesi and Sabani (2007) thus show that the fact that the IMF is both creditor and monitor of reforms explains the lack of credibility of its threat of sanctioning non-compliance: the IMF's desire to preserve its reputation as a good monitor is an incentive to distort its lending decisions towards laxity, which is reinforced by the length of the relationship with borrowing countries. It may even be argued that aid is ineffective because it firstly expresses the objectives of the bureaucracy of aid (Martens, 2005). In being non-conditional, China’s aid avoids these pitfalls. It may therefore be more effective and reduce a key cause of asymmetry between donors and ‘aided’ countries.

In addition, aid – be it conditional or not - has always been a dimension of the foreign policy of developed economies, whatever the needs of developing countries (Alesina and Dollar, 2000). Aid delivered by developed countries’ donors has also allowed for the maintenance in power of autocratic, corrupt and neopatrimonial regimes, which use aid as a rent and for redistribution to clientele and manipulate donors’ conditions as instruments for the implementation of their own domestic politics - according to a ‘double-edged diplomacy’ (Putnam, 1988), or a strategy using donors as ‘scapegoats’ (Vreeland, 1999). Developed countries have delivered aid to corrupt governments as much as to less corrupt (Alesina and Weder, 2002).

The share of OECD-DAC countries’ aid going to corrupt countries has actually increased since the early 1990s, despite conditionalities and the rhetoric of ‘good governance’ (Easterly and Pfutze, 2008), and aid to autocracies and mixed regimes of autocracies and democracies has not diminished (Easterly and Williamson, 2011). All this is an obvious cause of aid failures (Dreher et al., 2013).

**Figure 17: Aid to corrupt countries, 1984-2008, and by political regimes, 1960-2008**



Source: Easterly and Williamson (2011).

#### 5. 4. Asymmetries as outcomes of dynamic processes

Asymmetries appear therefore to be a feature of SSA external relationships, be they trade, investment and aid flows, and the relationships of emerging countries with SSA follow this dominant pattern. However, while the contribution of emerging countries to the structural transformation of SSA faces important constraints in the short-term, emerging countries may have the potential of fostering this transformation via multiple channels, high commodity prices and the fiscal space they represent, demand for SSA products, investment and infrastructure (Sindzingre, 2013).

Outcomes also always result from combinations of elements: emerging countries, or developed countries, do not ‘cause’ alone any outcome, it is the combination of particular channels, flows and SSA domestic features and policies that produce particular outcomes. External forces are always ‘processed’ and transformed by internal features. *In fine*, SSA countries have a capacity for agency, whatever the constraints analysed above (Mohan and Lampert, 2013). There is room for manoeuvre for domestic policies.

Initial asymmetries may combine with other elements and reinforce themselves. This is typically the case of political economy and institutions. In a world of global competition, domestic political economy creates the difference between countries that will be able to harness the demand for lower cost and investors’ trade-offs towards lower cost countries when China’s production costs will become too high, e.g. in the textile sector. Investment may not go to certain SSA countries due to internal political instability or predatory regimes (World Bank, 2013). This maintains these countries in the production of primary commodities, hence fostering traps and vicious circles – the persistence of low equilibria – made of the nexus of commodity dependence, predatory regimes, and economic stagnation.

Sub-Saharan African countries must indeed be differentiated, and figures regarding growth may also be inaccurate (Jerven, 2013). Middle income countries may differ from low-income commodity dependent countries: the latter are often caught in poverty traps, whatever their trade and investment partners, China or western countries: in LICs, there are improvements (e.g. infrastructure) as there may be no improvements. Short term and long term must also be differentiated. In some countries path dependence may prevail, while, as shown by Arthur (1989) and David (2000), small bifurcations may always occur and produce wide unexpected effects.

## 6. Conclusion

This paper has examined the many structural asymmetries that characterise Sub-Saharan African export structures. It has shown that emerging countries, and particularly China, follow the patterns that have been initiated by developed countries but do not necessarily amplify these structural asymmetries: emerging countries’ trade and foreign direct investment have complex effects, positive and negative.

The paper has also shown firstly that more than trade or investment, aid relationships convey the greatest differences between developed and emerging countries, notably

China. Secondly, despite the recurrent critiques of unconditional aid in the literature, it has revealed that that developed countries' aid may be among the strongest determinants of asymmetry between Sub-Saharan Africa and other countries, because of the mechanism of conditional financing.

It finally insists, however, on the fact that despite commonalities, Sub-Saharan African countries differ in their economic structures, as well as in their political and institutional capacities: asymmetries are generated by multiple channels, and they are historical and dynamic processes.

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