



The Rise of China and India What's in it for Africa?*

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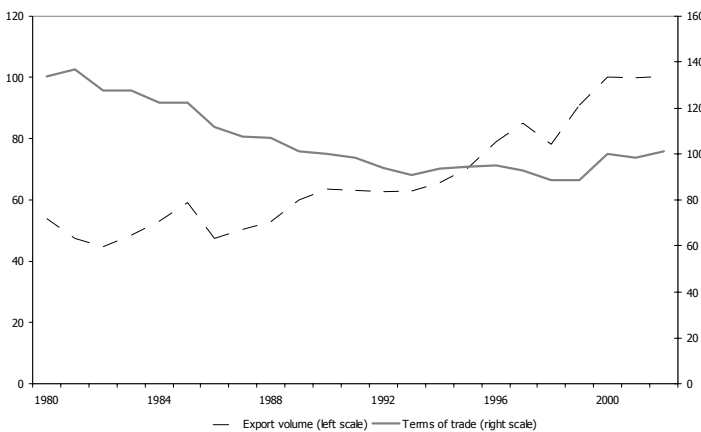
- ◆ China's and India's strong appetite for energy and metal has boosted international prices and the volume and value of African exports.
- ◆ China in particular has become the main trade partner for a number of African countries providing cheap manufactured goods and reducing Africa's dependence from its traditional trading partners.
- ◆ Despite the push for exports, terms of trade and growth that the Asian giants provide to Africa, risks for sustainable poverty reduction are visible in higher raw material dependence and rent-seeking activities.

Since 2001, China and India have jointly contributed approximately 30 per cent to global output growth and helped hold world output growth above the 4 per cent threshold level crucial to improving the terms of trade for primary commodity producers. By investing huge foreign exchange reserves in US securities, Asian investors have also contributed both to low US interest rates and to higher raw material prices.

As a result, sub-Saharan commodity producers benefited from a higher global demand for their exports and from improved terms of trade (Figure 1). This fuelled growth performances in sub-Saharan Africa's over the period 2001-2004 (4.2 per cent on yearly average) compared to the period 1996-2000 (3.3 per cent). In parallel, China's and India's growing demand for commodities turns them into major outlets for African commodities, helping to diversify Africa's export destinations (Figure 2). Sub-Saharan Africa's imports from China (and to a

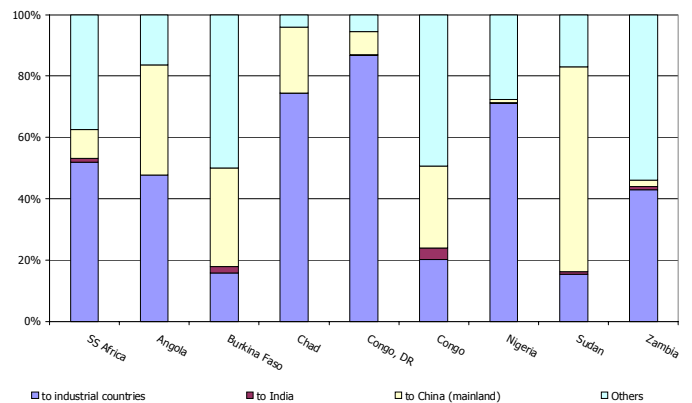
lesser extent India) have also grown fast benefiting urban consumers (who gain from cheaper consumer goods) and enterprises (which can source cheaper capital goods).

Figure 1. Terms of Trade and Export Volumes in Developing Economies, by Region, 1980-2002

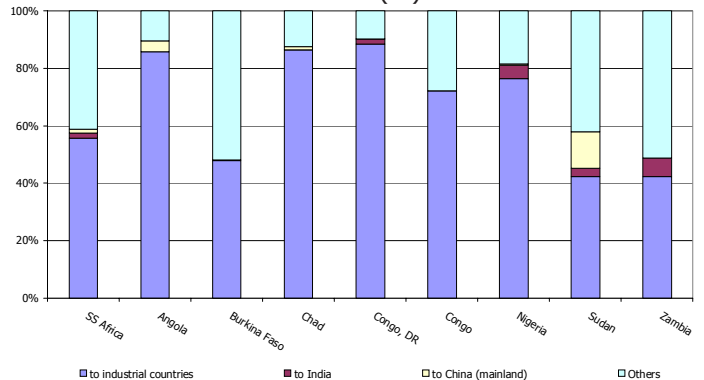


Source: Authors' estimates.

Figure 2. Destinations of Exports for Selected African Countries in 2004 (%)



Destinations of Exports for Selected African Countries in 1995 (%)



Source: Authors' estimates.

* Policy Insights No. 19 is derived from the forthcoming study of the same name www.oecd.org/dev/publications/chindaf

Is this scenario an unqualified blessing for sub-Saharan Africa? There is no doubt that any shot in the arm of this magnitude is positive for the continent, which trails behind the rest of the world when it comes to economic development and poverty alleviation. However, policy responses to what is ostensibly a boon must also be tailored in a careful and comprehensive manner to facilitate sustainable development in a region which is socio-economically fragile.

Africa is endowed with extractive industries such as oil, mining, and timber that are very capital-intensive. Yet, deepening this pattern of specialization can impede the development of the manufacturing sector by consuming all available financial resources and contributing to real exchange appreciation (the so-called Dutch disease). Furthermore, economic development strategies based solely on raw commodities risk having a very limited effect, if any, on poverty levels – although national incomes may increase, natural resources exploitation generate preciously few job opportunities for the low-skilled. In order to avoid the Dutch disease, resource-rich Africa needs to find ways to capitalise on windfall gains arising from resource-extraction and promote job-rich sectors.

Improving the macroeconomic policy mix is crucial. To avoid remaining stuck in the unpromising corner of vulnerable, capital-intensive and high-risk dependence on raw materials with little local-labour content, Africa will have to carefully manage the windfall gain generated by higher commodity prices. This is needed to avoid compromising the future development of labour-rich manufacturing and services activities. Monetary authorities will have to lean against real currency appreciation in order to avoid penalising importing-competing industries and exporters outside the resource sector. A proper policy mix must be

in place and fiscal authorities are required to limit public consumption to keep non-tradable prices in check. Investing abroad part of the export proceeds may be a solution to insulate local economies from “Dutch Disease” effects.

Diversification of economic activities is key as well. India and China are encroaching in the low-tech, labour-intensive sectors such as apparel where Africa had started being globally competitive. Still, there is room for capitalising on opportunities created by the economic ascent of the Asian giants. For example, West African cotton exports to China have been boosted by the phasing out of the Multi-Fibre Agreement and the rapid growth in the Chinese textile industry. Cotton cultivation in Africa is normally carried out by smallholders and this can have strong spill over effects for the whole economy. Thanks to an educated workforce and reliable infrastructure, Mauritius has managed to attract huge investment from Indian software houses which have set their recovery centres there. East African exporters of fresh fruit and vegetables can intercept the forthcoming changes in Chinese and Indian dietary habits, which are likely to converge with those of industrial nations. South Africa can be an important supplier in agribusiness, wine, the automotive industry, harbour wharfs, coal-to-liquid technologies, and chemicals.

Beside diversification, creating vertical and horizontal linkages with other productive sectors and removing development bottlenecks are also important. Natural-resource sectors, such as mining and forestry, can encourage the development of related industries, as well as generating opportunities for sectors such as services. Resource-based sectors can be a channel for knowledge and technology transfers.

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