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CHINA IN AFRICA: COMPETING WITH CHINA



FOREWORD

Africa is becoming an ever increasingly attractive market for investors. This is most notable in the realm of new discoveries in the oil, gas and minerals sectors where 48 out of 54 African countries are currently engaged in prospecting activity.

At FTI Consulting we work with a range of organisations looking to better understand this market. The risk spectrum is broad – security threats, political instability, bribery and corruption all remain uppermost in the minds of investors. As the competitive environment stiffens, an increasingly common concern for investors is competitor risk, particularly in relation to high value opportunities being pursued by the majors and state-linked entities. The phenomenal demand in China for African commodities, minerals and energy has driven significant Chinese investment activity across the continent, which takes many forms and presents significant challenges to competitors seeking to secure advantage.

As a result of this tide of interest, the Africa and Asia Global Risk Investigations Practice (GRIP) at FTI Consulting has developed an analysis of Chinese engagement in Africa. Mapping the various forms of activity witnessed by FTI Consulting, we highlight a number of themes:

- High-level Chinese investment is not necessarily homogenous or always state driven, although certain sectors benefit from state support
- African acceptance of Chinese involvement remains a highly political choice and not necessarily one that all African states are willing to take, either for domestic or geo-political reasons
- In some African countries, the relationship is so deep that it appears hard to break the advantage apparently enjoyed by Chinese companies
- Western companies and consortia have strong cards to play too, both in terms of reputation and the impact they can have in Africa

As Western businesses need to understand the politics and the personalities of the different markets within Africa, so they need to understand the Chinese relationship with the Continent. Chinese and Western companies will increasingly need to act as partners as the challenge of single enterprise success becomes too great.

China is on its own track, with key political changes and a strengthening appetite for reform and transparency looming ever larger. The prizes will be there for those companies who learn to ride the twin tigers of tightening Western business conduct legislation and China's imperative to go out and win.

Philip Boulton
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“China is always Africa’s trustworthy brother, friend and partner”

Yang Jiechi,
Minister of Foreign Affairs

INTRODUCTION

China’s recent intensification of financial and political activity with African states has not passed unnoticed. Over the past ten years, Chinese foreign direct investment (FDI) into Africa is estimated to have exceeded USD 15 billion; and in 2012, bilateral Sino-Africa trade topped USD 115 billion.¹ Having pledged an additional USD 20 billion in finance and assistance to the African continent, China is now Africa’s largest single financier.²

China’s ability to mobilise state owned enterprises (SOEs) and effectively target personnel, resources and its economic largesse at the African continent, is increasingly being received with slight trepidation in policy and business circles. Not only are Chinese companies able to draw on their government’s diplomatic support in new African markets, they can also rely on cheap finance provided by China’s state-owned banks. Moreover, despite expanding the remit of its anti-corruption law in 2011 to include the ability to prosecute Chinese citizens for bribing foreign public officials, Chinese anti-corruption regulations are not as strictly implemented as their US and UK counterparts: the UK Bribery Act and the Foreign Corrupt Practices Act (FCPA).

On this uneven playing field, our clients across sectors continue to encounter significant challenges to market entry and to their existing operations in African states. We have learned of instances where clients feel compelled to place bids to “go through the motions” and reinforce their market presence, despite holding little hope of success against a Chinese competitor offering services at a low rate. Given the difficulties inherent in competing in this environment, understanding China’s engagement strategy, its successes and its failures, is critical to developing an overarching strategy aimed at enhancing a company’s competitive edge. Effectively navigating the challenging political landscape and myriad security concerns that often plague operations in African states requires the following:

- An in-depth understanding of the political dynamics and operational landscape within the target state;
- Sound intelligence as to the human terrain including key decision makers; coupled with,
- An effective top-down and bottom-up engagement and CSR strategy aimed simultaneously at statesman and the grassroots.

¹ http://english.gov.cn/2012-07/19/content_2187290.htm

² Pledge made at the 2012 Forum for China-Africa Cooperation (FOCAC V)

CHINA'S ENGAGEMENT STRATEGY

DRIVERS OF BEHAVIOUR

In its five-year plan for 2011-2015, the government of the People's Republic of China outlined policies to accelerate its "going out" strategy and enhance its competitive edge. This strategy emphasized the need to place equal importance on inward and outward FDI flows, to transform China's international trade and investment models, and to expand outward investment. To that end, China's Development Bank and its Export and Import (EXIM) Bank are financing a string of opportunities in Africa and have provided loans to build highways, schools, hospitals, and other infrastructure in return for rights to African minerals and oil.

On the mainland, Chinese media continues to justify the government's investment in Africa to an internal audience by emphasising the abundance of Africa's cheap labour, reinforcing the need for African commodities to improve living standards in China, and noting Africa's increased strategic importance as a cooperative partner on development related matters in international fora. Given decreased profit margins in China, the media also highlights Africa's vast and untapped consumer potential as a market for China's low-priced goods, machinery, telecommunication, transport equipment, and services.

METHODS

Due to China's economic might, the state is able to deploy a range of resources simultaneously to enhance its appeal to the target state. Its economic relations with African states are underpinned by a comprehensive political and diplomatic strategy aimed at paving the way for state-owned and private Chinese enterprises. At its core, China's political strategy can be reduced to these key elements:

- **Encouraging bilateral cooperation** including high-level visits between Chinese and African leaders, ministers and politicians. In 2012 China's Foreign Minister Yang Jiechi embarked on a tour of African states including Namibia, Nigeria and Cote d'Ivoire. This came a year following similar high-level visits to other African countries including Kenya, Sierra Leone and Algeria.

- **Deepening economic cooperation** and encouraging practical cooperation in the security domain. For example between 2008 and 2011, China shipped USD 200 million worth of military vehicles and equipment to Zimbabwe and sold USD 24 million in arms and USD 57 million in vehicles and equipment to Sudan between 2003 and 2006.
- **Undertaking aid and assistance projects** and engaging in soft power activities to enhance China's appeal within the State; and,
- **Encouraging political cooperation** on issues of international concern for developing states. In doing so, China is promoting itself as *primus inter pares* in the United Nations, leading developing nations on matters relating to trade, climate change and on wider security concerns. During South Africa's membership of the Security Council between 2011 and 2012, its support of China's policy towards Syria was all the more remarkable given South Africa's historic battle against minority rule and for democracy.

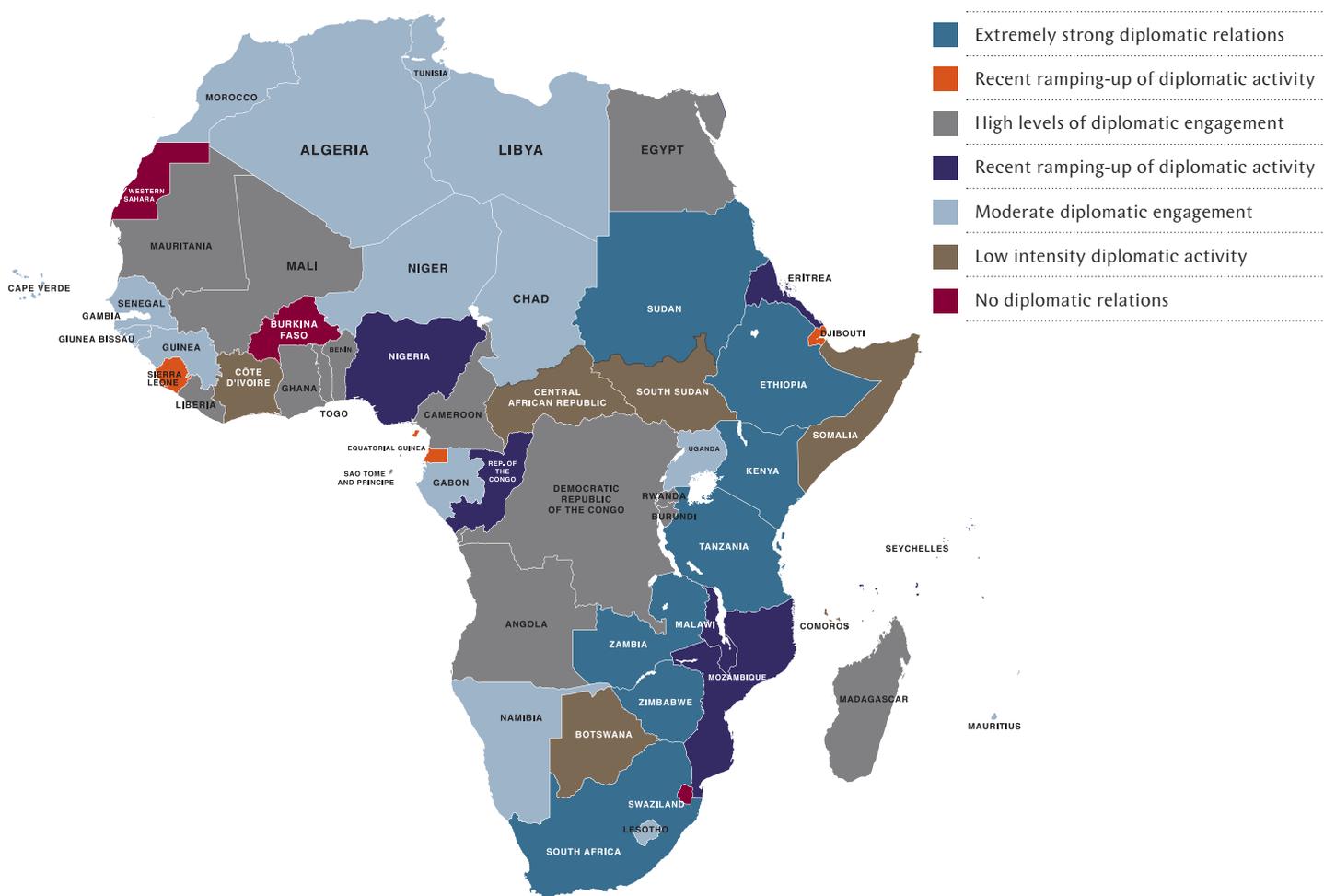
China's political strategy has so far been successful. Its policy of non-interference continues to appeal to African governments who are traditionally censured on issues of corruption and governance by the West. Their appeal is particularly strong for autocratic regimes that are often ineligible for financing from International Financial Institutions such as the International Monetary Fund (IMF) and other western donors. In 2002 Angola, for example, agreed an infrastructure investment package with the Chinese government after their application for funding from the IMF was rejected due to concerns over financial transparency. Countries such as Zimbabwe have issued similar requests to the Chinese government following the implementation of sanctions prohibiting western companies from investing in key strategic areas.

“Its economic relations with African states are underpinned by a comprehensive political and diplomatic strategy aimed at paving the way for state-owned and private Chinese enterprises”

The map below captures the strength of China’s bilateral relationship with each African state based on an analysis of the following factors:

- The frequency of high-level visits between government officials and heads of state;
- Military and security cooperation, both explicit and inferred from a wider range of activities;
- The volume of aid and assistance projects;
- The volume of cultural and political exchanges between the two states; and,
- Import and export activity determined by China’s ranking as a trade partner with each African state;

This is the product of analysing all official documents and activities listed by China’s Ministry of Foreign Affairs between 2010 and August 2012 (approximately 349 activities). The map aggregates the unpublished data to convey the wide variances in the strength of bilateral relations with each state.



CRITICISM AND FAILURE

While the increase in competition and the so-called “win-win” partnerships that Chinese companies were thought to herald was initially welcome by the general public, the quality of services and operational approach adopted by these companies has eroded public support. We list some of the commonly voiced concerns below.

- Despite proclamations to the contrary, many infrastructure deals signed by Chinese firms make little use of local labour. These contracts continue to mandate the use of Chinese workers for the majority of the work, and for highly skilled work in particular. The importation of foreign labour creates resentment in African countries where, in aggregate, the World Bank estimates that 50.2% of young people are unemployed.
- When local workers are hired, criticism surrounding the treatment and exploitation of labour is abundant. Managers are reported to have ignored contracts and prohibited unions and protests. At times, safety and security measures have not been properly implemented. For example, at Chinese-run Zambian copper mines, labourers “are made to work without safety helmets, below ground ventilation is poor and deadly accidents occur regularly”.³ To avoid censure, Chinese managers are said to bribe union bosses. In 2010 Chinese mining bosses in Sinazongwe, Zambia shot and wounded 11 local employees protesting over pay and working conditions. Politicians were put under intense public pressure to close the mine and arrest the managers.
- Chinese companies are accused of sub-par construction and, on occasion over the past few years, infrastructure and buildings erected by Chinese firms have fallen apart. In 2010, cracks appeared in the walls of a hospital built by a Chinese company in Luanda, Angola, which subsequently had to be closed down due to poor construction. Parts of a 130 km long Chinese-built road from Lusaka, Zambia’s capital, to Chirundu were also swept away by rain. As such, sources indicate that states are increasingly aware that while deals with Chinese companies initially appear lucrative, particularly where infrastructure projects are concerned, countries are tied into expensive future upgrades raising the overall lifecycle cost of the product.
- Companies are criticised by local populations and the international community for routinely ignoring local sensitivities. In 2007 the Nigerian government leased land belonging to ethnic Tuaregs to China Nuclear International Uranium Corporation. Local Tuaregs were displaced without compensation and the few jobs on offer to them were dangerous and badly paid. Sinopec, a state-owned oil firm, conducted explorations in a Gabonese national park and another state oil company has created lakes of spilled crude oil in Sudan.
- China’s actions are perceived to undercut local business to the detriment of the local economy. The influx of cheap Chinese-manufactured products and commodities into the African marketplace has depreciated the cost of local produce, adding to popular dissatisfaction among the general population. This serves to perpetuate the view that China is systematically depriving locals from accessing the potential benefits to be derived from their investments in the given state.

³ See The Economist (2011) ‘The Chinese in Africa: Trying to pull together’ [20 April] <http://www.economist.com/node/18586448>

SOFT POWER: CHINA'S ATTEMPTS TO REVERSE NEGATIVE PERCEPTIONS

In an effort to win the hearts and minds of the public and promote its “ideals culture and policies”, the Chinese government has recently embarked on a charm offensive launching quick-turnover, high-impact aid projects, such as free cataract operations. It has also invested in soft power initiatives and has launched English news channels and radio broadcasts by China Radio International (CRI). In July 2012 President Hu Jintao announced the various benefits that China is bringing to Africa:

“China has built over 100 schools, 30 hospitals, 30 anti-malaria centres and 20 agricultural technology demonstration centres in Africa. It has met the pledge of providing USD 15 billion of lending of a preferential nature to Africa....China has trained close to 40,000 African personnel...and provided over 20,000 government scholarships.”

“China’s political initiatives continue to fail to address the root-cause of discontent which relates to how Chinese companies operate”

However, China’s emphasis on attracting the public buy-in is more apparent in democratic states. In South Africa, for example, China’s activities, which include university exchanges and cultural activities, are heavily geared towards the general population. In Sudan however, efforts are directed at political institutions: scholarships and courses at China’s Confucius Institute are provided exclusively to “officials of the Sudanese government and the Ministry of Minerals”, and not to the wider public.

Ultimately, China’s political initiatives continue to fail to address the root-cause of discontent which relates to *how* Chinese companies operate. In autocratic states, China’s emphasis on directing activities towards the elite has arguably undermined their long-term interests. During the Libyan uprising, for example, Chinese companies had to suspend billions in investments in Libyan projects including housing and railway construction projects. Moreover, the Libyan National Transitional Council overtly stated that Chinese companies will be discriminated against due to Beijing’s strong support for Muammar Gaddafi.

In more democratic African states, civil society is putting pressure on their governments to take a tougher line on China. Increasingly, signs of grassroots resentment that may undermine China’s long-term ability to operate in Africa are becoming evident.⁴ Moreover, politicians have recently latched on to nationalist anti-Chinese sentiment.

In 2011, an opposition candidate in Zambia presidential elections, Michael Sata, ran his campaign with the slogan “Zambia for Zambians,” a thinly veiled call for an end to Chinese influence in the country. Sata was elected President in what the US magazine Foreign Policy described as “a vote of no-confidence against China’s existing projects in Zambia”. We note that following his election Sata openly welcomed Chinese investment in Zambia.

⁴ 2011 tour of five African countries where Yang Jiechi signed a \$7.6 million aid grant to Zimbabwe.

More recently, in July 2012 Jacob Zuma warned that the unbalanced nature of Africa's growing trade links with China is "unsustainable in the long term". In a speech in Beijing Zuma noted that:

"Africa's past economic experience with Europe dictates a need to be cautious when entering into partnerships with other economies".⁵

This statement comes despite the fact that Zuma's political party, the African National Congress (ANC) is believed to be a significant recipient of Chinese financial largesse, and the two nations built close ties as South Africa sought to market itself as China's gateway to other African countries. Comments such as these reflect that African politicians are increasingly aware that their citizens are concerned that the relationship with China is becoming too one-sided.

⁵ This speech, presented at the FOCAC V meeting in Beijing was all the more noteworthy as it followed China's pledge to increase its assistance to the African continent by USD 20 billion.

COMPETING WITH CHINA

“African governments are increasingly aware that Chinese companies behave in a less ethical manner than their Western counterparts, and that costs are cut”

To date, China has gained competitive advantage through an active policy of courting the favour of top government officials. However, African officials appear to increasingly recognise that this relationship is increasing their dependency on China. Moreover, the Chinese government’s emphasis on engaging top government officials, coupled with their willingness to overlook the needs of local communities, systematically disregards the potential importance of community groups as long-term enablers or spoilers.⁶

African governments are increasingly aware that Chinese companies behave in a less ethical manner than their Western counterparts, and that costs are cut. Chinese companies have also been criticised for their lack of engagement with local companies and for paying the local workforce a low salary. As such, in competing with a Chinese company, a competitor’s ability to adopt a more sustainable operational approach is necessary to enhance their competitive edge.

Effectively understanding the local and national decision-making structure, as well as the drivers and motivators of behaviour, is key to engaging at the right level and with the right actors, both within central government, and with local stakeholders. Gaining accurate political intelligence ensures that the operating environment is thoroughly scoped out in advance and is imperative for effectively navigating the complex socio-political dynamics within states in a sustainable manner.

At an early stage in discussions with the host state, it is incumbent on foreign competitors to articulate a long-term plan to illustrate their vision for partnership with the state. This should address the company’s legacy and include plans for technology transfer, local technical training and capacity building. CSR initiatives responsive to local needs and devised in partnership with the host country at an early stage in discussions, will tangibly convey the company’s willingness and commitment to partner with the state and contribute to its long-term economic and social well-being.

In preparing a bid which conveys the benefits that a project may bring to locals and which includes plans to hire local workers, the company should distance itself from the Chinese operating model, aiming instead to demonstrate an alternative and more sustainable long-term partnership with the state.

In order to garner support for the project, it is then necessary to devise a public communications strategy conveying the social and economic benefits of the company’s presence to key local and central decision-makers. Ultimately, this should be informed by a sound understanding of the internal political dynamic within the state taking into account the nexus between local society and the national government.

⁶ In 2011, China’s indifference to local sentiment led to the suspension of the Myitsone dam project: a key hydroelectric project perceived to be the solution to the energy crisis in South-West China. China had disregarded environmental concerns and had overlooked the region’s cultural and spiritual significance to the minority Kachin. Some analysts suggest that the ruling elite’s decision to trigger economic and political reforms in order to attract western businesses reflected a recognition of their increased reliance on China and a desire to diversify relationships.

CONCLUSION

Through deploying an array of political and financial resources to complement its attractive rhetoric, China is slowly accumulating strategic advantage on the African continent. In building bilateral relationships with African states, China is paving the way for the success of its companies in Africa. This advantage has been enhanced by the companies' access to cheap finance by state-owned banks, and by virtue of the fact that the Chinese anti-bribery legislation is less stringently enforced than equivalent measures in the UK and the US.

In this landscape, Western counterparts find it difficult to compete. However, while the continent has benefited from unprecedented levels of investment, China's presence in the market has reduced competition and resulted in poor work quality. In particular, China's approach, which is primarily geared towards the elite, continues to overlook the importance of engaging on a local level. This has resulted in widespread dissatisfaction among local populations who feel excluded from the benefits of Chinese investment. States traditionally welcoming of Chinese investments are increasingly aware that they are increasingly being drawn into a relationship of dependency on China, as opposed to the "win-win partnership" initially promised.

China's failure to address these concerns presents an opportunity for competitors that are able to devise a well-informed strategy that responds to facts on the ground. Taking into account the dynamic between local society and national government, a public diplomacy strategy pitched at a local level and at decision-makers, and aimed at garnering support for the project is necessary. Ultimately, this should highlight the benefits to the local community and economy that can be derived from the company's operations.

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CRITICAL THINKING
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