AFRICAN EAST-ASIAN AFFAIRS
THE CHINA MONITOR

Issue 2
June 2013

Chinese Special Economic Zones in Africa: a new species of globalisation?*

By **Peter Dannenberg**[i], **Yejoo Kim**[ii], **Daniel Schiller**[iii]

Introduction

Establishing 50 Chinese special economic zones (SEZs) is an integral part of the "Going Global" strategy promoted by the Chinese government (Gonzalez-Vicente, 2011). It is the latest addition to earlier pro-active economic internationalisation measures that comprised development aid and concessional loans, access to natural resources, export market development and outward foreign direct investment (OFDI). Africa became the most important host of the initially planned 19 SEZs worldwide with zones in Zambia (2), Nigeria (2), Ethiopia, Egypt, Mauritius, and Algeria. The developers of these zones were selected via two rounds of

We thank Sven Grimm (Stellenbosch) and Tom Mockford (Sheffield) for their valuable comments.

[i] *Peter Dannenberg, is a Senior Lecturer at the Institute of Geography at the Universität zu Köln, Germany*

[ii] *Yejoo Kim is a Research Analyst at the Centre for Chinese Studies, at the University of Stellenbosch in South Africa. Her research focuses on Chinese investment in Africa and its implications.*

[iii] *Daniel Schiller, is a Senior Researcher at the Lower Saxony Institute for Economic Research, Germany.*

competitive tenders held by the Ministry of Commerce (MOFCOM) in 2006 and 2007 (Bräutigam and Tang 2011, 2012).

The promotion of SEZs attempts to build on Chinese domestic experiences. Yet, the implementation of these zones in other countries emerges as a new species of globalisation. In the past, various forms of SEZs, for example export processing zones, free trade zones and industrial parks dedicated to foreign investors, were established globally with particular concentration and successes in the emerging economies of Asia. In these cases, governments of the affected countries usually established these zones as enclave spaces by their own initiative with preferential conditions for foreign investors or export-oriented firms (Sidaway, 2007) . In the case of Chinese SEZs, the programme is initiated by the Chinese government (MOFCOM) and operated by developers and managers of the zones which comprise of Chinese state-owned enterprises (SOEs), private enterprises or public organisations. The re-territorialisation of the Chinese state abroad is, thus, not only governed and implemented by the central government as a monolithic bloc, but involves regional governments and marketised state branches as independent actors (Gonzalez-Vicente, 2011). Thereby, the Chinese SEZs not only seem to become institutional enclaves within the host countries, but also spaces of trans-national governance.

This guest editorial argues that Chinese SEZs in Africa involve at least three relevant research themes for political and economic geographers: 1) emergence of transnational governance and institutions in enclave spaces, 2) investment motives and location choice factors of Chinese actors in Africa, and 3) implications for development and power relations.

Transnational governance: grand plan or grand experiment?

SEZs were a successful instrument to initiate OFDI flows to China during the early reform and opening process. These spatially limited openings allowed for the experimentation with gradual reform steps which could be revoked in case they proved counterproductive. The Chinese overseas zones programme adopted this approach and is organised as an experimental process that resembles the reform strategy of “crossing the river by feeling the stones” (Bräutigam and Tang, 2012).

The experimental approach is reflected by the sectoral focus of the different zones and the selection of host countries. All SEZs are either both resource and market-driven or aimed at serving various sectors and markets (see below); a number of SEZs are even located in landlocked countries. The differences in stages of development, size of the economy, growth rates, and institutional environments of the host countries underline the strategy of a flexible diversification (see Table 1). Furthermore, the investors in Chinese SEZs in Africa do not exclusively consist of SOEs supervised by the central government, but SOEs of regional governments, private companies, and (potentially) even non-Chinese investors are hosted in the SEZs. The multiplicity of actors involved in the ‘Going Global’ policy is part of the Chinese strategy to involve commercial actors in the exercise of transnational power; termed economic statecraft with Chinese characteristics by Norris (2010).

Investment motives: market development or natural resource-seeking?

Dunning’s (1981) investment development path predicts that FDI by countries at a higher stage of development in those at a lower stage has the purpose of gaining access to natural resources or benefitting from low production costs. Thus, vertical FDI, in other words, the relocation of cost-sensitive or resource-intensive parts of the value creation process, are expected to prevail over horizontal FDI, or the relocation of the whole value creation process with the aim to serve the local market (Carr *et al*, 2004). However, Chinese MNCs seem to diverge from the pattern predicted by Dunning’s (2000) OLI paradigm because cost advantages can still be realised in the home market. Natural resource seeking was the dominant motive of Chinese investors in African countries during the 1990s (Asche and Schüller 2008); gaining access to additional markets for Chinese low-cost products became a major investment motive since the 2000s (Bräutigam and Tang 2011). While

Table 1: Location factors of the six African host countries of Chinese SEZs and South Africa

Country		Market Size		Market growth			Institutional environment
	Stage of development	GNI per capita in US$ 2008-12	Population 2011	GDP in billions of USD 2011	population growth rate in % 2011	GDP growth in % 2011	Doing Business (rank) 2012	Corruption Perception Index (rank) 2012
Mauritius	0.728	8,040	1,286,051	11.3	0.71	4.0	19	43
Algeria	0.698	4,470	35,980,193	188.7	0.4	2,4	152	105
Egypt	0.644	2,600	82,536,770	229.5	1.7	1.8	109	118
Nigeria	0.459	1,280	162,470,737	244.0	2.5	7.3	131	139
Ethiopia	0.363	370	84,734,642	30.2	2.1	7.2	127	113
Zambia	0.430	1,160	13,474,959	19.2	4.2	6.4	94	88
South Africa	0.619	6,960	50,586,757	408.6	1.2	3.1	39	69

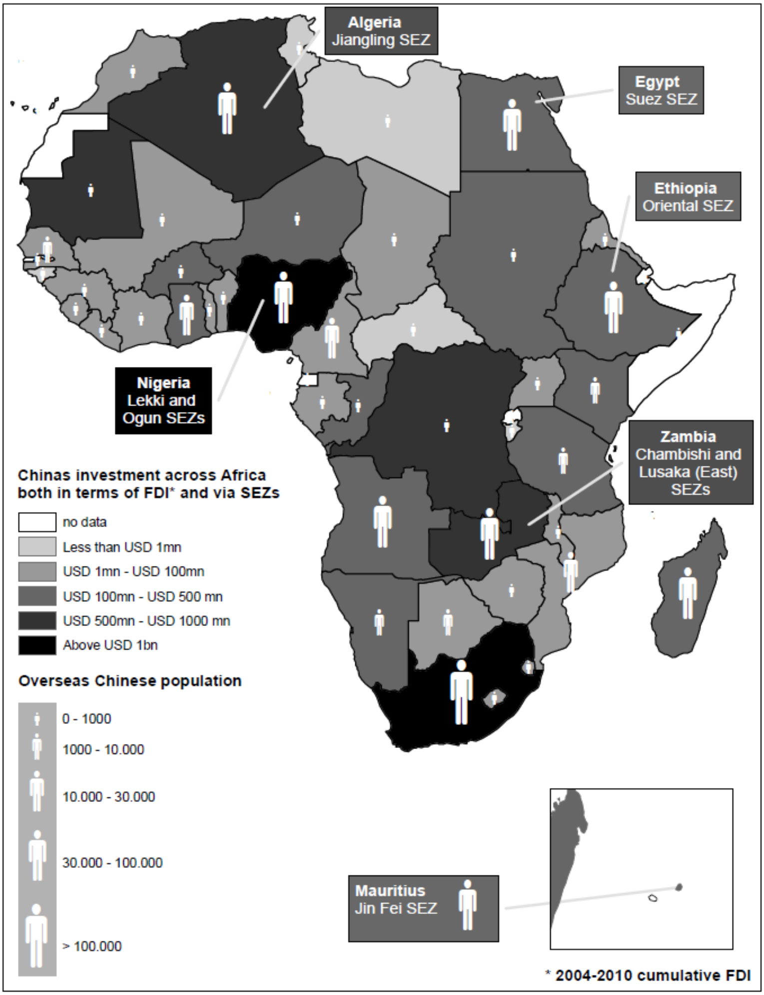
Sources: column 1: hdr.undp.org (2013); column 2-6: worldbank.org (2013); column 7: doingbusiness.org (2013);column 8: transparency.org. (2013)

resource-seeking activities were mainly dominated by large state-owned conglomerates, the market-seeking strategy opened the door for private firms and SMEs, increasing the diversity of Chinese actors in Africa.

China's SEZ strategy reflects the shift towards sectoral diversification and market orientation. While African host countries of Chinese SEZs differ strongly in their location factors (see Table 1), their market is either characterised by a comparatively high development stage for African standards (Mauritius, Egypt, Algeria) or strong economic growth (Nigeria, Ethiopia, Zambia). Resource seeking is still an important motive for Chinese FDI in Nigeria (oil) and Zambia (copper), but production plants for consumer goods (example home appliances, textiles) and investment goods (machinery, construction materials) emerged more recently. The implications of these investments for local firms, the diversification of host economies and their integration in value chains of Chinese firms remain yet unanswered.

Apart from the support of market-seeking FDI, it is likely that geo-political considerations of economic statecraft are also an important driver for the decision of where to establish a SEZ (Norris, 2010). Except for Mauritius and Zambia, all zones are located in countries with large populations and high regional political importance. Good economic and political relations with these countries potentially support China's long term strategic ambitions in Africa as a whole. However, the interpretation of these facts is debatable and offers room for future research as illustrated by the following two examples. First, no zone developer submitted a proposal for a zone in Tanzania despite the country's long standing relations with China (Bräutigam and Tang, 2012) . Second, South Africa was not chosen as a location for an SEZ, even though it possesses all the attributes necessary to qualify for an attractive FDI destination. A possible explanation is that the institutional environment in South Africa is sufficiently reliable to allow for FDI outside of institutional enclaves; additionally, the political climate towards Chinese

Figure 1: Chinese special economic zones, investments and population in African countries



Sources: Baynton-Glen (2012); wikipedia.org/wiki/Overseas_Chinese (2013) investors in South Africa was unlikely to be supportive of special economic enclaves.

Location choice and bargaining power: do formal or informal institutions matter?

Institutional factors determine the attractiveness of a location for FDI and the efficiency of different entry modes. Meyer et al. (2009) have shown that MNCs cope with unreliable institutional environments by entering host markets via mergers & acquisitions and joint ventures instead of wholly-owned subsidiaries. The strategy of creating institutional enclaves in the host market by setting up SEZs could be interpreted as a way of dealing with institutional uncertainty. The institutional support provided by SEZs seems to be of higher importance for market-driven investments by SMEs and private firms than for large SOEs that are able to create their own institutional environment and have direct access to negotiations with host country governments.

While SEZs provide advantageous formal institutions, many Chinese firms still capitalise on informal institutions and personal networks (Yeung 2006), particularly SMEs and private enterprises. Both, personal networks and SEZs can lower the transaction cost related to FDI in unfamiliar institutional environments, but may also limit the interactions with local actors. In that sense, SEZs could be an indicator of weak institutions and a manifestation of power asymmetries.

The indicators for institutional quality, in Table 1, support the expectation that SEZs are used as a market entry strategy if economic factors are promising but institutions are weak. In addition to measurements of formal institutions, Figure 1 reveals that the host countries for Chinese SEZs are among those that possess the biggest Chinese populations in Africa. Even though the identification of causality for this correlation is still an area for further research, it seems likely that Chinese zones and diasporas are attracted by the same economic interest.

The fact that South Africa does not host a Chinese SEZ is even more notable due to the fact that it possesses the largest Chinese population in Africa. South Africa is the leading recipient of Chinese FDI, but the rare combination of a comparatively high stage of development, a big market and rather good institutions probably gives it a stronger bargaining position in negotiating the general conditions of FDI (Mlachila and Takebe, 2011). Indeed, South African politicians and labour unions fear that the establishment of Chinese SEZs could lead to low labour standards and the displacement of domestic firms (van der Westhuizen and Grimm, 2013). While this concern also exists in other African countries, local actors might not possess sufficient negotiating power to negotiate the terms for FDI. However, the conclusions of existing studies on the implications of China's activities in Africa are ambiguous. Yan and Sautman (2013) analysed the Western discourse of Chinese copper mining in Zambia and showed that inaccurate stereotypes are produced since the conditions in Chinese mines are often not worse than in comparable mines of other owners.

Conclusion

The discussion above has shown that the Chinese strategy to establish SEZs in Africa has the potential to become a new species of globalisation. It is unique in its experimental and evolutionary approach towards transnational governance and institutional enclaves. It deviates from existing FDI theories that predict the predominance of vertical FDI at early stages of development. While natural resources were the reason why China became involved in some countries in the past, they are insufficient as an explanation for the recent location of zones. Chinese MNCs focused on market-seeking FDI happens much earlier than expected by theory. Market size and growth potential clearly increases the likelihood for hosting a Chinese SEZ. Despite the positive relationship between institutional quality and FDI in other empirical studies, Chinese SEZs in Africa seem to concentrate in countries with weak institutions. The hypothesis for further research is that there is a negative influence of institutional quality on the likelihood of hosting a Chinese SEZ, because these institutional enclaves become obsolete if a certain level of institutional quality is reached in the host country and/or the bargaining power of the host country government increases.

The multiplicity of actors involved in or operating alongside the establishment of Chinese SEZs in Africa and the diverse and sometimes contradictory implications for development and power relations leads us to conclude that Chinese SEZs are an important topic on the research agenda of political and economic geography.

Bibliography

Asche, H. & Schüller, M. 2008. *China's Engagement in Africa – Opportunities and Risks for Development*. Eschborn: gtz.

Baynton-Glen, S. 2012. *Beyond trade – China-Africa investment trends*. Hong Kong: Standard Chartered.

Bräutigam, D., & Tang, X. 2012. Economic statecraft in China's new overseas special economic zones: soft power, business or resource security? *International Affairs*, 88(4), 799-816.

Bräutigam, D., &Tang, X. 2011. African Shenzhen: China's special economic zones in Africa. *Journal of Modern African Studies*, 49(1), 27-54.

Carr, D.L., Markusen, J.L. & Maskus, K. 2004. Competition for Multinational Investment in Developing Countries: Human Capital, Infrastructure, and Market Size. In R.E. Baldwin & L.A. Winters (Eds.), *Challenges to Globalization: Analyzing the Economics* (pp. 383-409). Chicago, University of Chicago Press.

Doing Business. 2013. [Online]. Available: http://www.doingbusiness.org/rankings [2013, February 12]

Dunning, J.H. 1981: Explaining the international direct investment position of countries: towards a dynamic or developmental approach. *Weltwirtschaft-*

liches Archiv, 117(1), 30-64.

Dunning, J.H. 2000. The eclectic paradigm as an envelope for economic and business theories of MNE activity. *International Business Review*, 9, 163 -190.

Gonzalez-Vicente, R. 2011. The internationalization of the Chinese state. *Political Geography,* 30, 402-411.

Human Development Reports. 2013. [Online]. Available: http://hdr.undp.org/en/reports [2013, February 12]

IMF Working Paper WP/11/178.

Meyer, K.E., Estrin, S., Bhaumik, S.K., & Peng, M.W. 2009. Institutions, resources, and entry strategies in emerging economies. *Strategic Management Journal,* 30(1), 61-80.

Mlachila, M. & Takebe, M. 2011. FDI from BRICs to LICs: Emerging Growth Driver?

Norris, W. J. 2010: *Economic Statecraft with Chinese Characteristics: The Use of Commercial Actors in China's Grand Strategy*. Cambridge: MIT.

Overseas Chinese. 2013. [Online]. Available: wikipedia.org/wiki/Overseas_Chinese [2013, February 12]

Sidaway, J.D. 2007: Enclave space: a new metageography of development. *Area,* 39(3), 331-339.

The World Bank. 2013. [Online]. Available: http://data.worldbank.org [2013, February 12]

Transparency International. 2013 [Online]. Available: http://transparency.org/whatwedo/publications/doc/ar [2013, February 12]

Van der Westhuizen, J. & Grimm, S. 2013, forthcoming. Riding the Dragon or

Being Its Pet? South Africa's Middle Power Ambitions and China's Rise. In B. Gilley & A. O'Neil (Eds.). *Reshaping China – Why Middle Powers Matter* (pp. 148-167). Washington: Georgetown University Press.

Yan, H. & Sautman, B. 2013. "The Beginning of a World Empire"? Contesting the Discourse of Chinese Copper Mining in Zambia. *Modern China,* 39 (2), 131-164.

Yeung, H.W.C. 2006. Change and Continuity in Southeast Asian Ethnic Chinese Business. *Asia Pacific Journal of Management,* 23, 229-254.