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*“Scoping Study on China’s Relations  
with South Africa”*

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*For the African Economic Research Consortium (AERC)*

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## **I. Introduction**

### ***b) Brief Description of South Africa***

#### **Basic Facts**

<b>Description</b>	<b>Value</b>	<b>Source</b>
Area	1,219,912 sq km	CIA
population	43,997,828	2006 est, CIA
Life Expectancy	45 years	2006, AfDB
Infant Mortality	59.44 deaths/1,000 live births	2006 est, CIA
GDP	US\$271.779 billion	2006 est, IMF
GDP/capita	US\$5,679.8	2006 est, IMF
GDP Growth	5 %	2006 est, CIA
Government Budget	US\$72.15 billion (revenue) US\$75.93billion (expenditure)	2006 est, CIA
GINI	0.72	2001, SARPN

The beginning of the 1990s signalled the start of a new era as apartheid structures began to disintegrate and previously banned parties such as the African National Congress (ANC) could re-enter the political arena. South Africa's first democratic elections were held in April 1994 which the ANC won with a 62 percent share of the vote under the leadership of Nelson Mandela. Thabo Mbeki became the second democratically-elected president in 1999 and was re-elected in 2004 when the party won almost 70 percent of votes cast.<sup>1</sup> The ANC is currently characterized by factionalism. President Mbeki has failed to consolidate power and marginalised political opponents such as former vice-president Jacob Zuma who was implicated in corruption and sex scandals, was recently elected chairman of the ANC. The ANC-COSATU-SACP Tripartite Alliance that dominates government has become stronger with the election of Jacob Zuma and feelings are that the alliance partners will have greater leverage in influencing South Africa's trade and industrial policy.<sup>2</sup>

Under the Mbeki Administration, economic performance was satisfactory. Overall economic performance is solid, with growth remaining uninterrupted since 1999, averaging 3.5 percent per annum over this period. This coupled by favourable interest rate cuts that brought some relief to domestic consumers following the dramatic increases after the Asian Financial Crisis in 1997. On the foreign earnings side, the volatility of the Rand created highs and lows in export earnings. Yet, in spite of government claims that growth has been steady, critics point out that the main feature of the Mbeki years is jobless growth.

Today Government continues to face a high unemployment rate, vast inequality and poverty of a large percentage of the population and the growing HIV/AIDS epidemic despite opportunities in the infrastructure sector being extended. The country relies heavily on the primary sector, principally mineral resources and agricultural products, for economic growth. It has begun diversifying its output over the past four decades, increasing production of tertiary sector products and value-added exports. While the primary sector, consisting of mining, agriculture, fishing and forestry, constituted almost 25 percent of GDP during the 1960s, it only accounts for around 10 percent today.<sup>3</sup>

The tertiary sector, which includes wholesale, retail, trade, tourism, transport, communication, and services, has grown remarkably. In 2004, service industries contributed 65 percent of gross domestic product (GDP) with the largest contributions coming from wholesale and retail, finance, real estate, business and hospitality services. There are, however, increasing problems associated with the country's infrastructure such as energy provision and transport capacity and there is also a skills shortage currently being experienced in many of the sectors of the economy. A prominent legacy of the Apartheid regime is a strong correlation between race and class, with black South Africans mostly representing the disadvantaged and lower classes of societal structure. Unemployment, lack of housing and service delivery, as well as crime, remain at the top of the government's list of challenges to address, affecting not only disadvantaged communities, but all citizens in some form or another.

While the official unemployment level stands at 25 percent, the real rate is believed to be in the range of between 40 and 50 percent. As a result the informal sector is growing rapidly, with more and more people engaging in alternative economic practices to meet basic needs. HIV/AIDS also represents a fundamental crisis in South Africa with over four million South Africans believed to be HIV positive in 2004. An affirmative action program known as Black Economic Empowerment (BEE) has been implemented to address economic (and social) inequality. Through BEE, the government provides a wide range of benefits and incentives to institutions that ensure the ethnic profile of their employees and shareholders is in line with the national profile. While the program has clearly made some significant contributions, it has proved difficult to implement and is regularly exploited. Corruption is perceived to be increasing across the country although certain Government institutions such as the Department of Home Affairs appear more prone to irregularities than others. Nepotism is rife across all sectors, although relationships often appear to be based on ad hoc associations amongst alumni or work colleagues, rather than ethnic or cultural associations.

This paper explores the economic relationship between South Africa and China and assesses the direct and indirect consequences therein.

### ***b) Historical Background to Sino-South Africa Relations***

The first Chinese arrived in South Africa as indentured labourers in the mid 1800s, and initial Chinese diplomatic representation was established in the early 1900s to support these labourers. Between 1904 and 1910 there were almost 64,000 Chinese working on the Witwatersrand gold mines near Johannesburg. By the late 1950s, the Apartheid government became increasingly nervous about the PRC's solidarity with the colonially-oppressed in the developing world, particularly in Africa. The PRC's participation at the Asia-Africa or Bandung Conference in 1955 served to validate these fears. Furthermore, the Chinese Communist Party (CCP) supported the promotion of anti-colonialism and racial equality, thereby reinforcing Pretoria's fears that the PRC government could lend support to the liberation struggle, and undermine its own economic and security interests inside South Africa, as well as within the region.

Ideologically, the South African government was opposed to the pro-communist stance of China and regarded the Chinese involvement in Africa as potentially harmful to its own agenda. The threat of communism taking root in Africa, and thereby inciting violent uprisings in African states, was in direct opposition to the ideals of the Apartheid government of the time. Official diplomatic relations thus ended in 1960, and Pretoria established relations with Taiwan in 1976. Despite the cessation of official relations between Mainland China and South Africa, economic relations were maintained, albeit on a more furtive level. The CCP supported various liberation organisations throughout Africa, including the African National Congress (ANC) and the Pan-African Congress (PAC).

Despite their communist links, Sino-Soviet relations at the time were poor and the PRC was competing with Russia in terms of funding liberation movements in Africa. This enabled the PRC to promote their own ideological agenda and gain powerful alliances with opposition leaders in Africa. In Cold War terms, such alliances were crucial in securing future cooperation in other areas such as within the United Nations.<sup>4</sup> With Taiwan being a permanent member of the UN Security Council, it was important for Beijing to oust Taiwan, and support from the African bloc was crucial in achieving this goal.

Relations between the CCP and the ANC became more strained when the ANC decided to align itself with the Soviet Union in terms of ideological, financial and technical support. This was in response to the alliance between the ANC and the SACP, where the latter was more closely aligned to Moscow.<sup>5</sup> In response, the CCP started to develop closer relations with the PAC, however, their aid contributions were never very substantial, and support always remained rather 'meagre and unreliable'.<sup>6</sup>

In the 1980s, when the Soviet Union started experiencing serious political and economic problems, they were unable to continue to support the liberation movements within Africa and encouraged such organisations to look towards alternative sources. The ANC renewed its engagement with the CCP and strengthened ties after 1983, when it was announced that all such liberation organisations would be treated equally and without discrimination.<sup>7</sup>

Following deliberation over the One China Policy, the Mandela Administration decided to switch diplomatic recognition from Taipei to Beijing in 1997. This was viewed as the beginning of a new era in Sino-South African relations. South Africa established formal diplomatic ties with the People's Republic of China on the 1<sup>st</sup> of January 1998. Thereafter relations with the Chinese Mainland developed rapidly, in terms of political engagement, economic ties and social or cultural exchanges.

Both the PRC and South Africa have emerged as key players on their respective continents. The two countries co-operate in many multilateral fora. This, in turn, has also increased their mutual interdependence, which is clearly reflected in their expanding volumes of bilateral trade and other interactions.<sup>8</sup>

### **c) Political Exchanges**

After the re-establishment of diplomatic relations, the South African Vice President, Thabo Mbeki, paid a visit to China in September of 1998, followed by the Speaker of the South African National Assembly, Frene Ginwala, in October. The following year, Chinese Vice President Hu Jintao visited South Africa and President Nelson Mandela paid a state visit to China. At the invitation of President Mbeki, Chinese President Jiang Zemin paid a state visit to South Africa in 2000.<sup>9</sup> During the visit the two signed the "Pretoria Declaration" that provided a framework for closer cooperation and provided for the establishment of the PRC-SA Bi-National Commission (BNC).<sup>10</sup> The two presidents conducted an in-depth exchange of views on bilateral ties along with international and regional issues. China and South Africa are both regarded as developing countries with significant influence in their respective regions. There were also independent talks held with other prominent actors in the South African political scene.<sup>11</sup>

In the following year, contact between the PRC and SA increased, in the form of official visits by foreign ministers, trade ministers and heads of state. In 2001, a large delegation, led by President Mbeki, visited China at the invitation of President Jiang Zemin. During this visit, President Jiang and President Mbeki co-chaired the first meeting of the BNC. President Jiang suggested that this meeting brought forth a new stage in bilateral, friendly cooperation between China and South Africa.<sup>12</sup> The Centre for Chinese Studies (CCS) was created within the framework of this Commission, at the second meeting, which took place in 2004. Some of the other points discussed at the meeting included the reaffirmation of China's policy statement on Africa, and the new ideas and measures to strengthen China-Africa cooperation as elaborated in the Addis Ababa Action Plan (2004 - 2006) of the Forum on China - Africa Cooperation (FOCAC). China's commitment to building a new type of partnership with Africa based on long-term stability, equality, mutual benefit and all-round cooperation were also emphasised. There has also been considerable cooperation between the two countries within the framework of the United Nations. Having regularly met at the UN General Assembly, the countries expressed their commitment to shared interests and each other's foreign policy agendas.

In February 2007, President Hu Jintao started an African tour, visiting eight African countries including South Africa, Cameroon, Liberia, Sudan, Zambia and Mozambique. The tour highlighted China's solidification of the FOCAC commitments made in 2006 and the consolidation of relations between China and South Africa. It underscored China's renewed interest in the continent and provided a platform for new agreements and dialogue with the countries visited. President Hu's stop in South Africa focused on trade, political, development, investment and economic cooperation in addition to cultural exchanges between the two countries and seven agreements were signed.<sup>13</sup> Discussions followed up on the agreements made during the Forum on China-Africa Cooperation (FOCAC) in Beijing in 2006 and focused on four principles; broadening of political mutual trust and strategic consultation, enhancing economic cooperation and trade, enhancing coordination, cooperation and diplomatic consultations, as well as strengthening cultural and personal interaction between Africans and Chinese.<sup>14</sup>

## Agreements and MoU's signed between South Africa and China

- Joint communiqué on the establishment of diplomatic relations;
- Maintenance of the consulate-general of the Republic of South Africa in the Hong Kong Special Economic Administrative Region;
- Establishment of diplomatic relations;
- Civic air transport;
- Trade, economic, and technical cooperation;
- Establishment of a joint economic and trade commission;
- Reciprocal encouragement and protection of investments;
- Scientific and technical cooperation;
- Police cooperation;
- Cooperation in the fields of arts and culture;
- Maritime transport;
- Animal health and quarantine/ phytosanitary cooperation;
- Public health and medical sciences;
- Avoidance of double taxation; and
- Understanding on cooperation between national prosecuting authorities

Source: G. Le Pere and G. Shelton, *China, Africa and South Africa*. Midrand: Institute for Global Dialogue, 2007, p. 27.

## II. Investment

### a) *Chinese Companies in South Africa*

Chinese foreign direct investment (FDI) in South Africa has been relatively small and accounts for a very small percentage of overall FDI in the country. A senior Chinese diplomatic representative based in Pretoria interviewed in July 2007 suggested that the total cumulative value of China's FDI in South Africa to be around US\$600 million.<sup>15</sup>

### Foreign Investment in South Africa (US\$)

	2003	2004	2005	2006
Total FDI	734,000,000	799,000,000	6,379,000,000	- 323,000,000 *
China	7,300,000	17,810,000	47,400,000	40,700,000

Source: World Investment Report 2007, UNCTAD Report on Asian FDI

Chinese FDI in South Africa is set to increase dramatically and a number of recent initiatives by Chinese companies suggest change is already underway. In October 2007 the Industrial and Commercial Bank of China (ICBC) announced the purchase of a 20 percent share of South Africa's Standard Bank for US\$5.2 billion in a deal that was finalized in March 2008. This represents one of China's largest overseas investments on the continent to date. In February 2008 Sinosteel announced it would invest an additional US\$440 million in South Africa to build a closed electric furnace capable of producing 240,000 tons of ferrochrome and two inclined shafts each with an annual production capacity of 540,000 tons of raw chromium ore.<sup>16</sup>

The primary challenges to Chinese corporations moving into Africa are human resources and problems associated with understanding dynamics at the ground level. South African companies have proved very successful in these areas and have branched out across the continent entering a broad range of industries including mining, construction, energy, telecommunications, transportation, entertainment, food and beverage, retail, and finance. Standard Bank has branches in 17 different countries across Africa and ICBC's recent investment is an effective way for the Chinese to secure the necessary skills and experience to operate on the continent. We can expect to see similar acquisitions in the future and rumours that a Chinese company was looking to buy MTN increased the value of the South African telecommunication company's shares by 7 percent in December 2007.

In addition to finance, the two main areas in which the Chinese have invested in South Africa are in the assembly of electronic goods and the mining industry with a particular focus on chrome. The Chinese company, Hisense, entered South Africa in 1997, with the procurement of a Daewoo electronic factory. The company expanded its facilities in early 2004 and currently produces 200,000 TVs, 50,000 VCDs and DVDs, and 10,000 Hi-Fi home theatres each year. With a staff of over 200 people, it exports its products to ten over countries in the region including Namibia, Lesotho, Mozambique and Botswana.<sup>17</sup> The company is currently planning a 19-million-dollar expansion scheduled for completion by the end of 2009 that will enable it to produce 400,000 colour televisions, 300,000 refrigerators and 100,000 washing machines annually. Since arriving in South Africa, the company has maintained annual production, sales and profit growth averaging 20-30 percent, and in 2006, the South Africa branch of Hisense registered sales income of US\$47 million with a profit of US\$1.26 million dollars.<sup>18</sup>

Sinoprime Investment and Manufacturing South Africa is a subsidiary of Xiamen Overseas Chinese Electronic Co. Ltd (XOCECO) and was established in South Africa in 1998 as a manufacturer and distributor of consumer electronics specializing in CRT TV, Plasma and LCDTV.<sup>19</sup>

Other industries where Chinese companies are involved include First Automotive Works (FAW) Vehicle Manufacturer (Pty) Ltd., which manufactures heavy vehicles. FAW is China's largest and the world's third largest truck manufacturer, but the company had some problems satisfying the South African market's demands on quality, reliability and affordability. The company is seen as an example of China's growing presence in South Africa's business environment and therefore it was imperative for it to succeed, also with the company's eye on the sub-Saharan region. Trucks and cars are brought into South Africa in knocked down form and assembled at a plant in Spartan, Kempton Park<sup>20</sup>.

Currently, the company has 25 dealerships selling FAW Trucks in South Africa, with plans to expand this to 30 by the end of 2007. This strong dealership drive has formed the basis of its success in sales, also providing after-sales service and support to customers. Although the company has experienced some issues with quality control and legal matters associated with the South African automotive industry, it has now begun to show signs of success. The reason for these initial problems was differences between customers in China and those in South Africa. While in China customers are

prepared to sacrifice quality for a cheaper price, South African customers have proved to be less forgiving on such grounds.

Black Economic Empowerment (BEE) group Nulane Investments has recently bought 31 percent of Chinese telecommunications multinational Huawei Technologies Africa and is looking to set up a manufacturing plant and training centre in South Africa. Huawei Technologies sub-Saharan Africa vice-president Kevin Tao said the deal was a result of months of discussions following about three years of research of the local environment. The company is committed to using local skills in the countries to which they are supplying products and will invest in building technical skills, thereby playing a part in bridging the digital divide in Africa. On the continent Huawei has a presence in Angola, Nigeria, Kenya, DRC, Zimbabwe, Egypt, Algeria, Tunisia and Morocco.<sup>21</sup> Zhongxing Communications (ZTE) has offices in South Africa, providing solutions in the fields of mobile network, broadband data network, 3G, optical transmission and multimedia communications.

Chinese gold producer, Zijin Mining, recently acquired a 20 percent share in the South African platinum producer Ridge Mining, which marked the long anticipated entry of China into South Africa's resource market. The company invested just over US\$17 million, a relatively small investment in mining terms, but significant because of the implications it holds for the platinum industry in South Africa. The sector has been experiencing problems consolidating a number of small producers, and through this investment, Ridge might have found an investor with resources and motivation to build the necessary infrastructure such as a smelter or refinery to accommodate the smaller companies' output.

Other mining acquisitions include Sinosteel which bought a 50 percent stake in Samancor Chrome's Tubatse smelter and the Tweefontein chrome mine. State-owned steel producer Jisco bought 29.1 percent of International Ferro Metals and agreed to purchase half of the mine's production after the new expansion project is finished.

The Vaal River Eastern Sub-system Augmentation Project (VRESAP) was initiated as part of the South African government's US\$53 billion infrastructure investment plan. The project is being managed by the Trans Caledon Tunnel Authority (TCTA) on behalf of the Ministry of Water Affairs and Forestry and Vaal Pipeline Consultants (VPC) were selected as the consultants for the project.

In December 2005 China Overseas Engineering Company (COVEC) won a component of the US\$357 million VRESAP project with a US\$61 million bid that was US\$14 million lower than that next highest bidder. VRESAP will consist of a 121km steel pipeline with a diameter of 1.9m that will deliver 160 million cubic metres of water a year. The project was divided into two sections and tenders were issued internationally by the South African Government in line with requirements from the European Investment Bank. While the manufacture and installation of the pipeline was given to the large South African construction firm Murray and Roberts; COVEC won the contract for the civil engineering component. This sent shockwaves through the local construction community, just at a time when it is anticipating a boom on the back of scaled-up infrastructure investment by government.<sup>22</sup> This is also

the first major contract awarded to a Chinese construction company in South Africa, whose construction sector is traditionally very competitive.

The South African Federation of Consulting Engineering Contractors (SAFCEC), protested to the Department of Trade and Industry, but to no avail.<sup>23</sup> COVEC has over 30 years experience with an accumulated US\$2.6 billion worth of contracts. The company is listed by the U.S. magazine Engineering News Records as one of the top 225 with project experience across Asia and the Pacific. Over 70 percent of the company's business is in Africa,<sup>24</sup> with projects in Angola, Botswana, Cote D'Ivoire, Kenya, Zambia, Mauritius, Mali, Morocco, Mozambique, Sudan, and Madagascar. COVEC is also about to invest \$300 million in two copper and cobalt mining projects in the Democratic Republic of Congo.<sup>25</sup> Formerly under China's Ministry of Foreign Trade and Economic Cooperation (MOFTEC), COVEC recently joined China Railway Engineering Corporation (CREC) and is one of the 167 SOEs selected for preferential support by China's State-owned Assets Supervision and Administration Commission (SASAC) as a flagship enterprise.

COVEC is generally believed to have won the tender on price alone with no interference or support given by either the South African or Chinese Government. Senior South African officials involved in the project explained that serious problems were evident from the beginning. It was obvious to the majority of observers that the company would be hard pressed to make a profit with such a low quote, though as a senior manager at TCTA explained the low price did not provide adequate grounds to disqualify them.<sup>26</sup> The company clearly underestimated the cost of doing business in South Africa and has had serious problems recruiting senior construction staff. One observer explained that the company had been advertising for professionals with over 20 years experience and only offering around US\$21,000 which is half to a third of the price for such skills in South Africa. In the original contract the Chinese agreed to bring in only 18 Chinese nationals, but faced with the shortage of such skills in South Africa 45 Chinese workers have been approved to date. It has also been suggested that COVEC seriously underestimated the implementation of laws and regulations relating to construction, labour, and the environment in South Africa.

COVEC has had a great deal of experience operating across Africa and approached South Africa in a similar manner. The work practices of the Chinese company and their approach to planning and implementation were also at odds with local practices and the expectations of the consultant and management companies.<sup>27</sup> Apparently the Chinese expected to be left to do the job without interference while in South Africa dialogue between the consultant and contractor is usually constant. The Chinese have been reluctant to provide method statements detailing precise plans, procedures, and specifications for discrete components of work and prefer to simply "wing it." Another serious impediment has been from the local engineering industry. Fearing competition from the Chinese many local suppliers and engineering companies have effectively black listed COVEC and refuse to provide them with support and materials. All of these problems have been compounded by problems associated with language and cultural differences. One senior individual involved explained that communication has been very difficult and described negotiations as tortuous. "It takes hours to decide

on simple points that should take a few minutes and then some weeks after agreeing the Chinese constantly want to renegotiate.”<sup>28</sup>

To pre-qualify, COVEC was required to form a joint venture with a local company. COVEC had previously worked with Mathe Construction (MC) in Botswana on the construction of housing and hospitals and entered into a joint venture with MC taking a 25 percent stake. MC has been involved in construction since 1985; however, its experience in large projects of this nature is limited and the apparent input of the local partner which was well positioned to deal with many of the challenges associated with the procurement of materials and local labor has been negligible. There is also a strong sense that the COVEC head office is not fully cognizant of the problems associated with this project and has not been providing adequate support to the project which has been described by some insiders as being on the verge of collapse.<sup>29</sup>

A consulting company was engaged to consult with all the stakeholders, identify the issues, and develop a strategy to move forward.<sup>30</sup> The consulting company has in effect played the roll of a mediator: focusing attention on the key problems and prompting them to take the necessary action. The last step proposed by the consulting company was to mobilize political pressure within Chinese and South African Governments.<sup>31</sup> The Ministry of Water Affairs and Forestry, the Ministry of Foreign Affairs and DTI have all been informed and the Chinese Embassy in South Africa is also aware of the problem but none have yet been formally requested to respond.<sup>32</sup> Elsewhere in Africa, the Chinese Government has applied pressure and in some instance provided support to ensure that Chinese companies deliver to expectations.

### ***b) South African Companies in China***

South Africa is the only African country to have significant investment in China, although once again it is extremely difficult to ascertain the precise value of the total investment. Several of the companies listed in the box have significant proportions of their investment listed in third countries and Hong Kong. Few of these companies have invested more than US\$5-10 million, with the exception of SAB Miller which is by far the single largest investor and according to a senior representative of the company has a total investment of between US\$500 million and US\$1 billion.<sup>33</sup> One informed industry observer put the total figure of South African investment in China at between US\$1.2 billion and US\$1.5 billion, though acknowledged it could possibly be as high as US\$2 billion if offshore listings were included.<sup>34</sup> A senior Chinese diplomat in Pretoria described these figures as excessive and quoted MOFCOM figures that put the total figure for South African investment in China at between US\$600 and 800 million.<sup>35</sup> He suggested that offshore listings and joint ventures with Chinese companies in Hong Kong and the Mainland contribute to the difficulty of obtaining accurate data.<sup>36</sup>

### **Major South African Companies Operating in China**

<b>Name of Company</b>	<b>Industry</b>
Naspers/ MIH	Media
Metspan	Manufacturing

Freeplay	Manufacturing
Beijing Axis	Consultancy/ Research
Kumba Resources	Mining/ Minerals
AngloGold Ashanti	Mining
AngloCoal	Mining
Anglo American	Mining
Goldfields	Mining
Old Mutual	Financial
Standard Bank	Financial
First National Bank	Financial
Sasol	Energy
SAB Miller	Beverages
African Explosives Limited (AEL)	Engineering
Bateman	Engineering
Landpac	Engineering
Spur	Hospitality and Restaurant

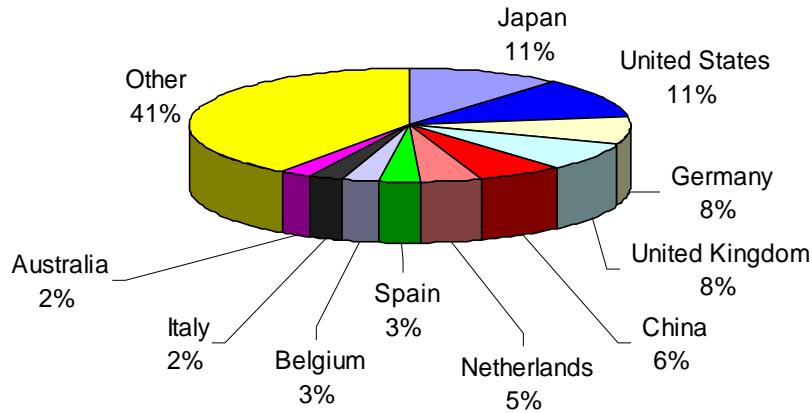
South African companies have proved particularly successful in China. It has been suggested that their experiences operating in similar environments across Africa with extremely poor infrastructure and limited levels of governance have provided them with a strong competitive advantage over Western companies. The South African government does not appear to provide any support to South African corporations operating in China beyond consular assistance to South African nationals present in the country.

### **III. Trade**

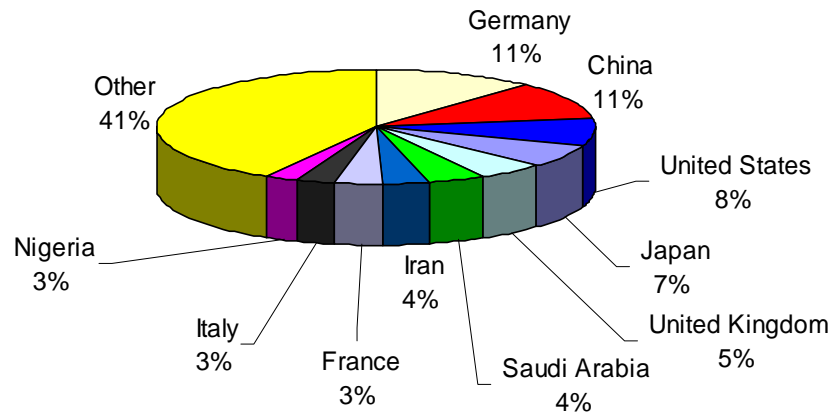
#### ***a) South African Trade***

South Africa exports consisting primarily of platinum, gold and other minerals in addition to coal, cars and machinery were valued at approximately US\$52 billion in 2007 while its imports comprising petrochemical, cars, mechanical components and telecommunications equipment was approximately US\$66 billion. As the graphs below show, South Africa's primary trade partners were all Western countries with the exception of which China accounted for 6 percent of exports and 11 percent of imports.

### SA Trading Partners 2007 - Export



### SA Trading Partners 2007 - Import

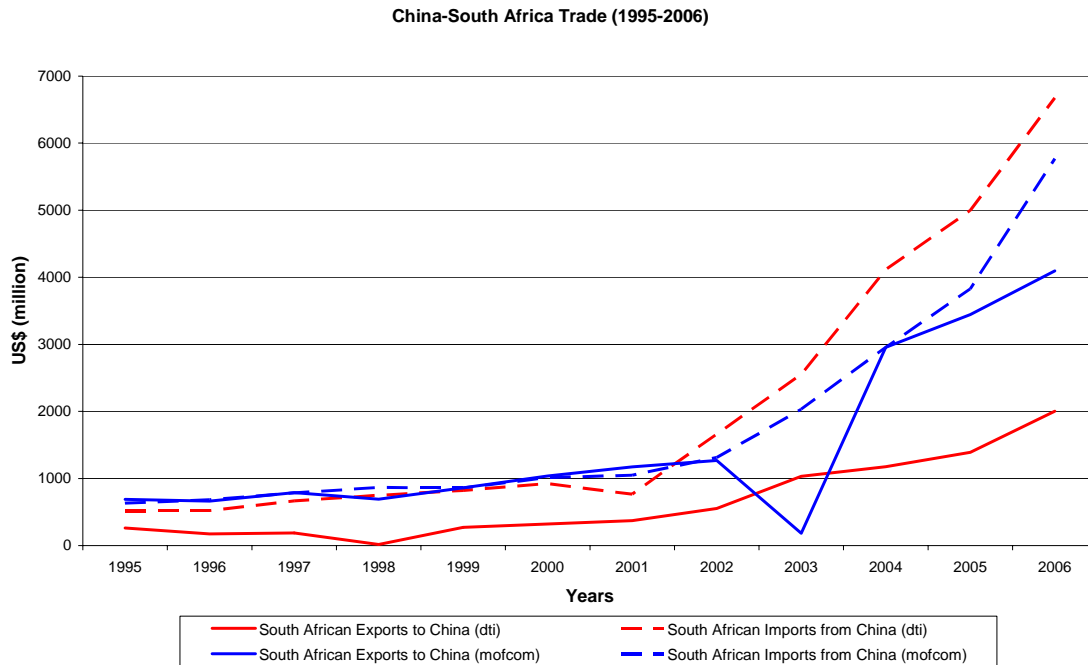


This represents a significant change from 2003 when China accounted for 2 percent of South Africa's exports and six percent of imports. South African imports from China were valued at US\$7 billion in 2007 making it the second largest source of imports after Germany which supplied US\$7.9 billion worth of imports in that year.

#### ***b) Anomalies in Trade Data***

As seen in the graph below, there is a substantial difference in the trade figures declared by MOFCOM and DTI. The discrepancy in these figures may be attributed to a broad range of factors including

smuggling and corruption; however, the Chinese economic and trade counsellor suggested that the reasons for the discrepancy are “technical” rather than political.<sup>37</sup> Ron Sandrey explains, “The variance in such figures can be attributed to currency fluctuations, different valuation methods (fob versus cif)<sup>38</sup>, timing differences, the role of a third port such as Hong Kong and intermediaries such as the European diamond market.”<sup>39</sup> The trade imbalance presented by the South African government’s DTI data is accentuated by the fact that South Africa records cif values for imports and fob values for exports. The sudden trough in South Africa’s imports from China in 2003 is a result in the drop in the value of the Rand at that period.

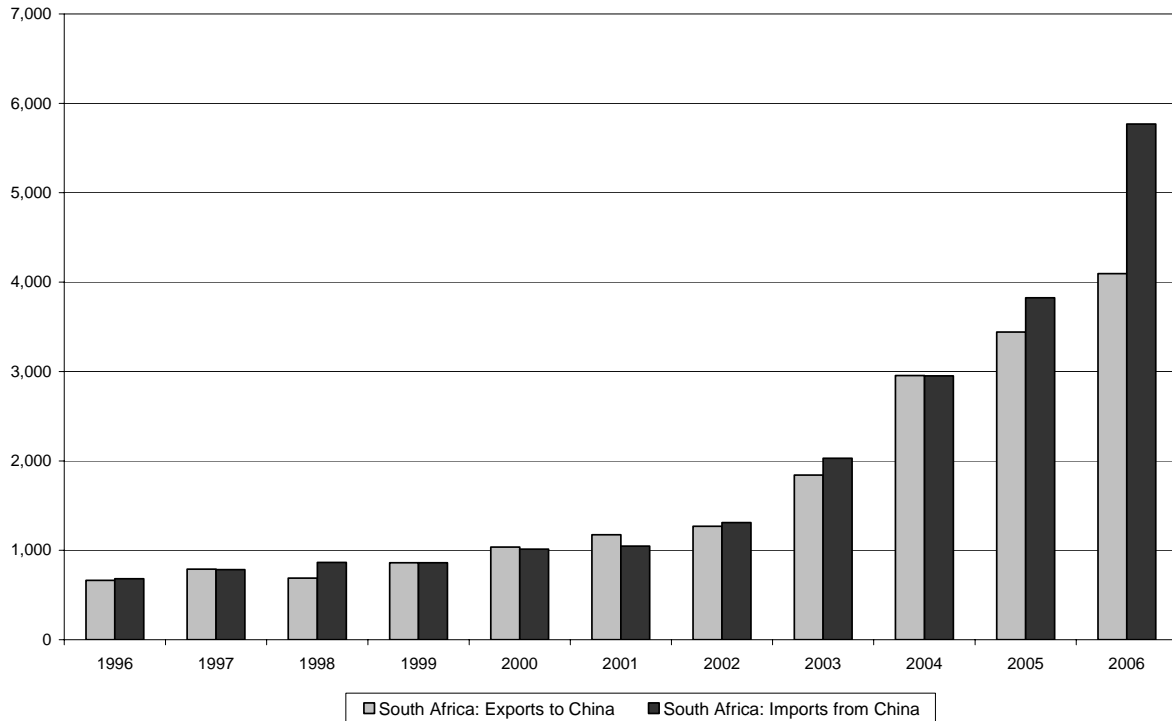


While the precise dimensions remain difficult to ascertain, all data shows that trade between the two countries is growing rapidly, and that South Africa is experiencing a trade deficit that began to spike around 2002. Chinese figures put the total value of trade at almost US\$9.9 billion in 2006, up from US\$1.3 billion in 1995, while the South African Government suggests trade has grown from approximately US\$770 million to US\$8.7 billion over the same period.

### **c) South Africa’s Trade with China**

South Africa is China's second largest trading partner in Africa, after Angola. The trade volume between China and South Africa accounted for 20 percent of the total trade volume between China and Africa. The direct bilateral trade between the two countries started in the early 1990s. South Africa granted China market economy status in 2004 is in fact one of the first countries to do this.

South Africa: Value of Trade with China, millions of US\$ (1996 - 2006)



South Africa runs a large trade deficit with China, but the same can be said for its trade with the rest of the world, due to its resource dependence and development trajectory. Because South Africa's main exports to China are raw materials and semi-processed goods, the value-added component to exports is limited resulting in trade terms that are not as beneficial as they could be. There are still untapped opportunities for South African products in the Chinese market, outside of natural resources. This is yet unfulfilled.

The textile, clothing and footwear industry is South Africa's sixth largest domestic industry and eleventh largest exporter of manufactured goods. The industry directly employs around 143,000 people, with an additional 200,000 workers from related industries such as transportation and packaging. In 1997, total South African retail apparel sales exceeded US\$ 117.1 billion, with the textile industry sales reaching US\$57.8 billion.<sup>36</sup> This total rose to about US\$190.4 billion in 2004, with textiles contributing US\$ 97.4 billion and clothing the remaining US\$ 92.9 billion<sup>37</sup>. In 1992, the government instituted a program to drastically reduce tariffs for textiles and apparels over a twelve-year period. Textile tariffs were to be reduced from 100 percent to 45 percent on clothing, from 50 percent to 25 percent on fabrics, from 35 percent to 17.5 percent on yarn, from 15 percent to 10 percent on fibers, and from 60 percent to 30 percent on household textiles. At present, the clothing industry is protected by a 40 per cent tariff.

In the post-1995 period, as the Multifibre agreement began to be phased out, the South African textile industry became stagnant and even began to decline in certain areas. Local clothing manufacturers

lost an estimated third of all market share while Chinese imports increased from US\$55 million to around US\$870 million between 1995 and 2006 according to Chinese Government reports.<sup>40</sup> The footwear and textiles industries have followed similar patterns, with Chinese imports growing 370 and over 19,000 percent respectively. China produces the majority of garments imported into South Africa and has put a serious strain on domestic markets as a result of China's undervalued currency, efficient production, and cheap labor costs that South African manufacturers claim make them less competitive both locally and internationally. The effect has been a massive loss in jobs for workers across the industry, and although the precise figures are difficult to calculate, estimates range from 23,000 to 85,000. According to an application filed by South African Textile and Clothing Workers Union (SATCWU) to the International Trade Administration Commission (ITAC) in 2005, more than 75,000 jobs have been lost since 1996.<sup>41</sup> In a country where unemployment and poverty are major socio-economic challenges, this number total is perceived by many as unacceptable.

Trade Unions have always played a prominent role in South African politics, with vocal leaders, powerful alliances with the governing party and an active membership that is organised and historically unified. The most important union that represent workers in the textile and clothing industry is the SATCWU, which is an active member of COSATU and has a membership of over 110,000. SATCWU have actively engaged with relevant stakeholders in business and government, forming a task team that is convened by the Minister of Trade and Industry (Mandisi Mphahlele) within which was formulated various proposals for industry restructuring. The reason for union's significance in influencing policy formulation is the cross-over of senior members and leadership between unions and the ANC, the current ruling party.

The close ties between the two organisations are formalised through the tripartite alliance within the South African government which gives unions some leverage in engaging with government.<sup>42</sup> As a very vocal and large constituency within the voting public, COSATU holds considerable bargaining power with which to shape government action. It is, however, important to mention that although formal ties exist between the organisations, and leadership does have close relations, it remains uncertain how far the influence of unions stretches, purely because of the fact that all government decisions have not been in favor of union policies and lobby. The head of SATCWU commented on this fact after the agreements were signed in 2006, saying that it was "too little, too late" since a large number of jobs had already been lost in the years leading up to the signing of the agreement.<sup>43</sup>

In 2006, labor and manufacturers successfully lobbied government to initiate discussions on import limitation with China. As a founding member of GATT and the WTO, the South African government is bound by their agreements. It has offered to implement 'safeguard measures' which are compliant with the WTO's code of behavior. The decision by the Chinese government to accept the request was described by a senior Chinese diplomatic official as a political decision to promote good will between Beijing and Pretoria.<sup>44</sup> The Memorandum of Understanding (MOU) was initiated in June 2006 during the Chinese Prime Minister's visit to South Africa. The Chinese agreed to place voluntarily restrictions on 31 categories of export products for two a two-year period to allow the South African industry to restructure and prepare itself for direct competition with China. It is also interesting to note that the

Chinese were receiving considerable pressure from the EU and US concerning the undervaluation of the RMB and the impact on China's trade competitiveness. Trade Unions have recently demanded that the country's retailers maintain a 25 per cent ceiling on all imported goods. Measures were also put forth to government in order to restructure various tariffs and quotas that will enable more competitive prices and quality. The South African wholesalers and retailers were reportedly not consulted by the DTI and were concerned at the sudden implementation of such a program as they were preparing for the busy Christmas season. They successfully applied to have the implementation of the quotas delayed until 31 December 2006. A number of South African wholesalers continued to import Chinese garments beyond the limits of the quota through third countries such as Dubai while others immediately began to source products from countries such as Vietnam and India.

There have been no apparent increases in the demand for local produced textiles and 8 months into the implementation of the quota system the garment industry has apparently made no attempts to restructure or increase capacity in preparation for competition with China. Evaluating the effectiveness of the quota has proved extremely difficult with no effective methods for monitoring the number of garments being imported into the country; however it appears unlikely that the industry will use this opportunity to restructure and the compromise made by the Chinese Government to implement the quota appears to have been wasted. The Chinese Government has approached the South African textile industry with an offer to train workers and build capacity in preparation for the resumption of competition, but has to date, received no response. The funds are currently being used to build capacity in other industries and there are no signs that the South African garment manufacturing industry will be competitive in the international market in the short to medium term future.

South Africa and China have committed to work together to create favourable conditions for growth in relations between the two countries and to balance trade. China has pledged to further open up its market to Africa, by increasing the number of export items to China eligible for zero-tariff treatment, from 190 to over 440. This is applicable to the least developed countries (LDCs) in Africa that have diplomatic relations with China.

As South Africa aims to improve the value-added and technology levels of its exports, China poses a major challenge, both because of competition in these areas, and because China's growth itself raises the relative prices of raw materials on international markets.

#### **IV. Indirect Impacts**

The Standard Bank deal mentioned above is indicative of attempts by Chinese companies to broaden and deepen their investment portfolios across Africa through mergers and acquisitions. South African companies have established a presence in most African markets leaving these companies vulnerable to takeovers and direct competition from Chinese companies entering Africa. While in conventional terms this maybe interpreted as indirect competition in third markets for South Africa business interests, in other respects it also seen as enabling them to become more competitive beyond the

African market where they have concentrated their investments to date. South African companies also stand to gain from injection of capital from China through such mergers and acquisitions. They will also benefit from access to Chinese technology, research and development.

The impact on local labour in third markets is less clear. South African corporates have been criticised for using their African operations to circumvent employment quotas under the Affirmative Action policy back home, especially at the senior management level. Yet, evidence on the ground, particularly in Uganda, suggests that major corporates like MTN and Shoprite Checkers have successfully implemented an employment portfolio that incorporates senior management from the local labour market. Therefore, it is not clear whether the expansion of South African companies through mergers and acquisitions by Chinese firms will lead to closures and job losses in the African market for both the local labour force as well as senior South African executives in these operations.. For the time being, however, the ICBC appears to be taking a hands-off approach in its involvement in the way that Standard Bank conducts its business. Moreover, indications are that it is unlikely to bring in very many Chinese personnel into the Bank whether at Executive or branch level. This could change and might prove different for corporates in other sectors; however, Chinese companies in operating in Africa have demonstrated a strong preference for local labour despite widely held perceptions to the contrary.

Chinese exports to South Africa neighbours such as Swaziland, Lesotho, Namibia and Mozambique have reduced the demand for South Africa's exports to these countries and this has had a detrimental effect on South African producers that have not been able to compete. The Chinese also appear to be expanding control of supply chains in both the formal and informal sectors.

## **V. Aid**

South Africa, in comparison to other African countries, is not a large aid recipient. While most multilateral and bilateral donors provided significant development assistance to the post-apartheid state after 1994, this was primarily aimed at assisting democratic South Africa with its reconstruction and development programme. In this regard most of the development assistance programmes were short-term, having a shelf life of five-years. As South Africa moved into the second phase of its democracy after 1999 most donors re-evaluated their programmes and restructured them according to the government's national development plan. In most cases this remained aligned to the reconstruction and development programme but focusing more sectors including vocational training, SME development, education, and civil service training.

A study commissioned in 2003 by the South Africa National Treasury, NORAD and the Norwegian Embassy in Pretoria and conducted by the Chr Michelsen Institute (CMI) to evaluate Norwegian development assistance to South Africa noted that "foreign aid only constituted 1% of the budget and 0.3% of GDP". Even though aid as a percentage of the national budget remains negligible, the same study found that aid "assisted in transformation of institutions, in developing new policies, in

implementation and delivery of services and in exposing South Africa to lessons and experiences from other countries” which without such assistance would have been much slower. In terms of hierarchy of donors, western multilateral institutions and bilateral partners have dominated the aid relationship with the new South Africa.

In line with above Chinese aid to South Africa has been minimal. The reason being is that China's historical relationship with South Africa has influenced this engagement and notwithstanding that formal diplomatic relations was only established after 1997 when most donor partners were reaching the end of their phase of assistance. Nevertheless, the fruition of relations between Pretoria and Beijing is now beginning to mature, which is signalling the latter's intention in supporting South Africa's development agenda. Currently, this is largely restricted to education and training and is being managed through the Bi-National Commission between the two countries.

Under the BNC, both countries have signed bilateral agreements that include the following:

- Exchange of Notes Exchange of Notes regarding Funding of Edenvale / Modderfontein Low-cost Housing Project
- Agreement on Trade, Economic and Technical Cooperation
- Agreement on Scientific and Technological Cooperation
- Exchange of Notes regarding the Participation in the Integrated Fish Farming Technology Training Course
- Exchange of Notes on the Provision of Water Supply Materials

As a senior Chinese official explained, his Government identifies the shortage of skilled labour as a major impediment to South Africa's development.<sup>45</sup> During the visit of Prime Minister Wen Jiabao in July 2006, the Chinese government announced that approximately US\$6.3 million dollars would be made available for technical training in South Africa, and President Hu Jintao promised an additional US\$25 million during his visit to the country in February 2007. The Chinese initially approached the textile industry and the SETAs under the Department of Labour for input on the most appropriate way to make use of these funds, but have received no response to date.<sup>46</sup>

They have since approached the Deputy President's office and have begun dispersing the funds through the Accelerated Shared Growth Initiative for South Africa (ASGISA)<sup>47</sup> and the Joint Initiative for Priority Skills Acquisition (JIPSA). Interestingly none of the money is being spent on the development of the textile industry, as originally intended by the Chinese; but rather on technical training in agriculture, tourism, defence and foreign affairs.

In so far as supporting South Africa's skills development, which offers the South African government to draw on lessons from the Chinese technical experience and investment, the Chinese government has also expanded the number of scholarships for South African nationals to study in China. This has recently increased from 3 every two years to five annually under the BNC. Moreover under the BNC various government departments are exploring opportunities of developing exchange programs for the civil service.

It should be noted that while China appears to becoming an emerging development partner to South Africa, the trend and patterns identified in other countries does not apply to South Africa. In so far as China recognises South Africa as a strategic partner, it does not employ the attraction of soft loans to underwrite its development relations with Pretoria. This is for two reasons. On the one hand South Africa is considered as a middle income country with a large modern economic sector, strong public and private sectors and a fairly robust infrastructure that can lay down the foundations for economic growth and poverty reduction. In this regard the Chinese model of using the soft loans, which has become a framework in its other African engagements, is more difficult to apply.

On the other hand, the South African government is careful not to incur external debt. The apartheid debt inherited by the democratic state was small and the current South African government is careful not to burden its development and human challenges, which is still vulnerable by the legacy of apartheid. Therefore the Chinese model of using soft loans as part of the aid arsenal is not something that is evident in terms of China's aid relationship with South Africa. The more utilitarian point of engagement for China is for Beijing to identify areas of mutual collaboration like skills development, socio-economic service delivery and more generally reconstruction and development projects as entry points to garner and harness its development partnership with Pretoria.

Nevertheless as China augments its development assistance to South Africa, there are growing signs that South Africa is moving towards taking on an increasing donor role in Africa. This definitely raises significant issues about whether Pretoria's shift towards a donor position will have an indirect impact on China's engagements in this regard. With other traditional donors, like the EU, supporting Pretoria's endeavours in this regard, China may have to consider how its aid for trade framework may or not be compromised in the continent.

## **VI. Conclusion**

Since 1997, relations between South Africa and China have steadily grown, as both countries aim to develop and grow as leaders in their respective regions. Today, South Africa is one of China's most important trading partners on the African continent with 20 percent of the total trade volume between China and Africa coming from South Africa. Various political exchanges have facilitated greater interdependence and cooperation, as China realises the strategic importance of South Africa as a springboard for their companies and products into Africa. The relationship has also grown because of the rising demand for raw materials in China, a demand that can only be satisfied by the vast reserves of minerals, oil and gas, agricultural and manufactured goods.

Although Chinese companies have been slow to invest in the South African market due to difficulty entering the competitive environment, those that have, have largely been successful in their various industries. The steady increase in trade volume between the two countries, as well as the increasing cooperation and interaction shows China's increased interest in South Africa and Africa as a whole.

South African companies have also shown remarkable capacity to adjust to the Chinese market, with a certain measure of success achieved by companies such as SAB Miller, banks such as First National and Old Mutual as well as Sasol. Sasol is particularly interesting since this company is a leader in energy technology and can thus help the Chinese improve energy efficiency and solve the current energy crisis facing this developing state.

China is now South Africa's fifth largest trading partner and although it is difficult to ascertain the exact figures trade between the two nations is growing rapidly. South Africa is currently experiencing a trade deficit that began to spike around 2002. South Africa imports from China consist mostly of high-tech manufactured products while it exports goods such as raw materials and minerals. Chinese figures put the total value of trade at around US\$9.9 billion in 2006, up from US\$1.3 billion in 1995, while the South African Government suggests trade has grown from approximately US\$770 million to US\$8.7 billion over the same period.

Beijing willingness to implement quotas on its exports to South Africa clearly under-scores the importance it attaches to this African country. South Africa is considerably more developed than the other countries in Africa and while the various organs of Government and the private sector make a significant contribution to the country's engagement with China; relations remain heavily dominated by the presidency.

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- <sup>36</sup> Interview, Pretoria, 20 July 2007.
- <sup>37</sup> Interview, Pretoria, 20 July 2007.
- <sup>38</sup> Cost, Insurance and Freight (cif) includes the cost of the goods, the freight or transport costs and the cost of insurance while the Free On Board (fob) price is simply the value of the goods excluding the transportation and associated costs.
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