

The Impact of China-Africa Investment Relations: The Case of Nigeria



Infrastructure project in Nigeria

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The Problem

Historically, Nigeria's traditional development partners are mainly from Europe and the Americas (U.S. A. and Canada). Indeed, these groups have dominated the flow of trade, investment (in terms of foreign direct investment – FDI) and grants and financial as well as technical aid to the country over the years. Although Nigeria and these countries have come a long way in their relationship, it is contestable if such has in any significant way assisted the country in its quest for development. The relationship appears to be exploitative at least from the trend in the structure and pattern of FDI inflow to the country.

Although China-Nigeria relationship dates back to 1971, recent dimension and nature of economic interactions between the two countries demand a careful and detailed analysis of this relationship with a view to

establishing its potential impact on the economies. Interestingly, the growing relationship between China and Nigeria is induced by the fact that the two countries have economic complementarities. On one hand, a major development challenge in Nigeria is infrastructure deficiency, with huge investment need. Complementarily, China has developed one of the world's largest and most competitive construction industries with particular expertise in the civil works considered critical for infrastructure development coupled with its ability to provide the necessary financial assistance to the countries in need including Nigeria. Again, China's industrialization drive and massive inflow of FDI into the Chinese economy led to fast growing manufacturing economy which requires oil and mineral inputs that are outstripping the country's domestic resources, hence the need to source them from abroad including Nigeria which is well endowed with these resources.

Of late, positive developments have been recorded in respect of the net FDI inflow from China to Nigeria,

as it has doubled from US\$3 billion in 2003 to more than US\$6 billion in 2005. However, the share of the oil and gas sector was about 75% indicating the expressed and explicit desire of China in Nigerian oil and gas resources. It further reinforces the prevalence of a link between Chinese FDI and trade in the context of China-Nigeria investment relations. Granted that FDI constitutes a key channel through which impacts of China's economic growth can be transmitted to the typical African economy, ensuring that existing and future FDI inflow from China to Nigeria is beneficial requires that some questions must be attended to. Such questions include, but are not limited to, the following:

- To what extent is China different from other exploitative practices?
- In what sectors is FDI from China directed?
- Does this FDI augment productive capacity, or do the funds represent a change in ownership?
- Is incoming Chinese FDI resource – or market-seeking, and is the output targeted at the domestic or external market?
- What economic benefits arise from Chinese FDI in terms of exports, import-substitution, contribution of value added and employment?
- Outside of the specific investments, what are the spread effects to the domestic economy in terms of skill development and capability building, the use of local inputs, supply chain management and technology transfer?

The rationale for this research is the all-important necessity to provide answers to the questions raised above as well as other related ones with a

view to evolving policies that will help to optimize China-Nigeria investment relationship.

Method of Analysis

The study covers 1997-2007 and the main objective is to analyze the economic relation between China and Nigeria in the area of foreign direct investment (FDI) with a view to determining its developmental impacts. Sequel to the review of the theoretical and empirical literature, the investment development path (IDP) framework emanating from the work of Dunning (1981, 1986) and Dunning and Narula (1996) is adopted for the study. The central thesis of the IDP framework is that a country or region's international investment position is systematically related to its level of economic development. This framework, formalised in the concept of the investment development path, proposes that there is a U-shaped relationship between economic development and a country's international investment position. This implies that as economic development proceeds, net inward direct investment will first grow and then decline. In the earliest phase, the country's infrastructure will be inadequate to support even vertical ("low labour cost seeking") inward investment. Such investment will grow however as the economy develops. It will take longer for firms from backward regions to accumulate the firm-specific assets that would allow them to engage in outward direct investment; Caves (1996); Dunning (1988). Over time, learning-by-doing will allow this process to evolve and outward FDI will emerge. At the same time, the country's absolute cost competitiveness will be eroded, reducing the incentive for vertical inward investment. The incentive for horizontal ("market seeking") and technology-sourcing investments may expand however as the economy becomes wealthier, and domestic firms will seek to maintain their competitiveness by engaging in outward vertical investments.

The choice of this theoretical framework is borne out of the fact that, the IDP is a dynamic concept and it draws on Dunning's eclectic paradigm of international production and is shaped by the OLI variables (ownership, locational and internalization advantages). The framework assumes,

first, that development induces significant structural change to the economy and, second, that such change has a systematic relationship with the pattern of FDI (Lall, 1996). It goes further to contend that the change in the locational advantage of a country as well as in its firm's ownership and internalization advantages vis-à-vis other economies explains how its international investment position evolves from only receiving inward FDI to exporting FDI.

The study employed the use of quantitative (descriptive analysis such as ratios, percentages and correlation as well as cross tabulations), qualitative (key informant interviews and surveys) and case studies involving projects handled by the Chinese. The use of surveys assisted to generate firm-level data that allowed the analysis of China-Nigeria investment relations with respect to concerns such as effects of employment effects as well as the competitive and/or complementary effects of Chinese firms to local firms. Use of content analysis of relevant documents and reports from various sources was equally involved to corroborate the results from primary data. Documents containing investment policy regime in both Nigeria and China were reviewed so as to capture the policy adequacy and the need to fine-tune policy to make FDI flows from China beneficial to Nigeria.

In addition, in-depth interviews of key informants/stakeholders (both Nigerians and Chinese; representatives of government, embassies; National Planning Commission, Central Bank of Nigeria, Ministry of Finance, Nigeria Investment Promotion Council, Chamber of Commerce, National Association of Small and Medium Enterprises, etc) and case studies of some selected Chinese firms in Nigeria provided the database required for the qualitative impact analysis of China-Nigeria investment relations.

Key Findings

Nigeria occupied the 12th position as host countries of Chinese outward FDI between 2003 and 2006 with the sum of US\$191.01 million. Chinese FDI to Nigeria increased from an average of \$0.55 million in 1999-2000 to about \$5.5 million in 2006. Structurally, Chinese investment covers mainly manufacturing and construction activities, particularly in the area of infrastructure and services.

The composition of Chinese investment in Nigeria is highly fragmented. China has set up over 30 solely – owned companies or joint venture in Nigeria in the construction, oil and gas, technology, services and education sectors of the Nigerian economy (Ogunkola, Bankole and Adewuyi, 2006).

Chinese economic interests in Nigeria can be broadly classified into two: private and public. Information from the Nigerian Investment Promotion Commission (NIPC) revealed that Chinese private FDI are mostly in agro-allied industry, manufacturing and communications sectors. Correspondence is observed between countries with large Chinese natural resource investments and those with large Chinese infrastructure financing for power and transport. Reason: the need to link mining deposits with power required for processing and rail and port infrastructure required for export. Nigeria, though a major recipient of Chinese infrastructure finance, received relatively small volumes of Chinese infrastructure finance during 2002 and 2005. However, in 2006 there was a major surge when China made almost US\$5 billion of infrastructure finance commitments to Nigeria, which accounts for 70% of China's total commitments to Sub-Saharan Africa that year. Sectoral spread of Chinese infrastructure finance in Nigeria is a little different from the entire Africa, with transport infrastructure projects amounting to 65.0% of all commitments followed by power with 24.0%.

Chinese investment is concentrated in a few sectors that are of strategic interest to China, especially in the extractive industries. They are carried out largely by state-owned enterprises or joint ventures. Chinese FDI in Africa is typically accompanied by Chinese workers and most of the supplies are sourced directly from China. Chinese outward FDI is often associated to "pull" factors such as a host country's favourable investment policies, including incentives and other location-specific advantages.

In pursuit of practical evidence regarding impacts of Chinese FDI in Nigeria, five case studies were captured, namely, Kajola Specialised Railway Industrial Free Trade Zone, Ofada Vee Tee Rice Limited, and Ogun Guangdong Free Trade Zone (OGFTZ), China Town in Lagos, and Lekki Free Trade Zone (LFTZ). Major findings from the case

studies are presented below:

Kajola Specialised Railway Industrial Free Trade Zone

- The zone is a joint venture of the OGS&G and the Chinese Civil Engineering Construction Company (CCECC). The company's investment was estimated at about \$775 million.
- Aim of the project: Facilitate rapid industrialization of the State and deepen foreign direct investment inflow to the state.

Ofada Vee Tee Rice Limited

- The company has a designed capacity of 225,000 (9,000 bags) tons of rice per day and the capital outlay is estimated at about \$2 billion.
- The local farmers are to supply paddy rice to the company to be processed (de-husking, de-stoning, parboiling, sorting, polishing, packaging and marketing) by the company. About 30,000 farmers are to supply the paddy rice.
- The backward linkage of the company is important for the economy in terms of employment and rural livelihood.
- Other beneficiaries are: transporters and traders of the raw materials and the finished products.

Ogun Guangdong Free Trade Zone (OGFTZ)

- A tripartite project of two Chinese companies: Guangdong Xinguang International of Guangdong Province in China and China-Africa Investment Limited; and the OGS&G. Cost of the project estimated at about \$500 million: to be financed by the Chinese consortium. The First Bank of Nigeria Plc is collaborating with the consortium in areas of investment banking, project financing, business advisory services and correspondent banking relationship.
- When completed, the FTZ will consist of about 100 firms mainly engaged in light to medium manufacturing activities including footwear and rubber production, ceramic processing, furniture, hardware and household appliances, real estate development, and light and heavy manufacturing plants.

- In addition, the development of the host community is expected to be positively enhanced. Two related projects are in this direction:
 - a \$700,000 primary school project; and
 - dualisation of the road linking Igbesa (the FTZ site) to Badagry express way.

China Town in Lagos

- Chinese enterprises prevalent in the market, about 120 shops. Chinese own about 75%.
- Average of two Nigerians engaged as shop attendants
- Enterprises in the market deal in products such as textiles and apparels, lace materials, baby wears and toys, foot-wears, handbags, household utensils, personal effects, items for decorations, electrical appliances, art works, among others: light manufactures
- Investigation revealed that some products are produced by Chinese firms in Nigeria, while majority are imported from China
- Other participants in the market are the transporters, food sellers and the market management. There is a branch of the Intercontinental Bank (Plc.) at the market and this is expected to facilitate financial transactions of the market participants.

Lekki Free Trade Zone (LFTZ)

- A joint venture between the LGSG (represented by Lekki Worldwide Investment Limited-LWIL) and the Chinese Government (represented by Nanjing Jiangning Development Zone in the Jiangsu Province and the China Railway Construction Corporation)
- The main missions of the LFTZ include the following: to develop an offshore economic growth zone; attract foreign investment; promote export; create job opportunities; minimise capital flight; and establish a one-stop global business haven.
- Opportunities and access of investors to supply raw materials particularly for activities such as agro-processing, clothing and textiles, food and beverages, forestry, mining and pharmaceuticals to be created by the zone

Impacts: Potential Gainers and Losers

All economic agents (producers, consumers and government) in Nigeria stand to benefit from China's transformational investment finance in Nigeria, particularly in the area of infrastructure and social amenities. Adequate infrastructure in Nigeria through China's financial resources will improve investment climate and welfare in the country. Consequently, improved output, export, employment and government revenue should be expected. Establishment of China's export processing zone should promote export and increased foreign exchange earnings. It is noteworthy to argue that anticipated gains are premised on the condition that all projects are completed and there are no white elephant projects or corruption in the process.

It is doubtful if Chinese FDI in Nigeria will bring about positive revenue effect because of many taxes and other fiscal incentives as well as the possibility for tax evasion/avoidance by Chinese firms. Massive influx of Chinese FDI into the country to produce goods and services at cheaper prices coupled with import of cheap commodities from China will enhance the welfare of Nigerians.

Granted that Nigerian firms are not competitive, massive influx of Chinese FDI into the country to produce goods and services may lead to closure of domestic competing firms, with adverse effects on employment particularly where Chinese firms are fond of bringing in workers from their country. The fact that Chinese firms in Nigeria bring in inputs from their own country and set up their own market outlets implies that there may not be any (or major) backward and forward linkages between Nigerian and Chinese firms. Domestic firms operating in sectors of interest to China (such as oil and gas, power, construction, manufacturing and services) may lose as a result of lack of competitiveness.

Arising from increased investment relationship with China are a number of sector specific opportunities and challenges to be faced by Nigeria.

The table below catalogues these specific opportunities and challenges along sector line.

A OIL AND GAS SECTOR		
	OPPORTUNITIES	CHALLENGES
	Availability of funds and expertise for exploration and production	The likely increased environmental problem and the crises in the oil producing areas
	Increased production to meet the rapidly growing world demand for energy products	Limited absorptive capacity and lack of linkages of this sector with the rest of the economy since the activities in this sector is highly capital intensive. Non-encouraging local labour absorbing tendencies and incentive system and the need for regulation to promote local employment, skill acquisition and technology transfer
		Dominance of foreign investment and influence of foreign investors on the economy
B SERVICES SECTOR		
	OPPORTUNITIES	CHALLENGES
	Availability of funds, expertise and technology for services infrastructure development	Intense competition with local firms producing similar services and the associated job losses.
	Availability of funds, expertise and technology for improved service delivery	Exploitative tendencies of foreign firms providing services.
	Competition promotes efficiency in service delivery and affordability	Inadequate infrastructure to cope with the rapidly growing demand for services
	Promotion of employment, skill acquisition and technology transfer	Non-encouraging local labour absorbing tendencies or practices and incentive system and the need for regulation to promote local employment, skill acquisition and technology transfer
		Avoidance and evasion of taxes
C MANUFACTURING AND CONSTRUCTION		
	OPPORTUNITIES	CHALLENGES
	Availability of funds, expertise and technology for industrial development	Intense competition with local firms producing similar products and with local contractors
	Production of cheap goods for domestic consumption and export	Assurance of the quality of investment
	Promotion of employment, skill acquisition and technology transfer	Non-encouraging local labour absorbing tendencies or practices and incentive system and the need for regulation to promote local employment, skill acquisition and technology transfer
		Environmental pollution and other associated problems
D INFRASTRUCTURE AND SOCIAL AMENITIES		
	OPPORTUNITIES	CHALLENGES
	Availability of funds, expertise and technology for economic and social development	Avoidance of white elephant and abandoned projects
	Aid element of the investment promotes social development	Corruption in the awards of infrastructure contracts

Policy Implications/ Lessons

Against the background of the findings of this study, a number of policy implications, lessons and agenda for the future China-Nigeria economic relations are worth noting. One, attempts to compromise the benefits of FDI should be persistently resisted by the Nigerian Government through active engagement and negotiation with

the Chinese government and investors. Second, good governance and stable macroeconomic environment in Nigeria is a necessary to promote productivity and sustainability of investment. Three, Nigerian Government needs to institute policies aimed at maximizing the direct and indirect benefits as well as in minimizing the possible negative impacts. A litmus test for gauging the motive of FDI is to classify investments into resource-seeking, market-seeking or

efficiency-seeking. Efficiency-seeking FDI is preferred to other forms, at least from the perspective of the host country.

Furthermore, there is need to ensure implementation of laws and regulations in Nigeria and to ensure compliance by the Chinese investors. Such laws include labour law, social responsibility law and local content requirement. The Nigeria Labour Congress and its counterpart in the private sector should ensure the Nigerian labour law

is followed by all firms including the Chinese-owned firms. Similarly, the Raw Material Development Council (RMDC) should see to compliance of local content requirements (in terms of human and physical materials) by all firms especially the foreign ones. The Nigerian Investment Promotion Council (NIPC) and other relevant organisations such as the Nigerian Extractive Industry Transparency Initiative (NEITI) should ensure compliance with the social responsibility law in Nigeria.

Again, given that the positive revenue effect of Chinese FDI may not be realized by the Nigerian Government, there is need to generate in a scientific manner, a number of scenarios on the level or number of incentives that can be given to foreign firms without jeopardising the economy. Accurate data on the number, location and tax liabilities of all firms including the Chinese firms should be generated by the Federal Inland Revenue Service in collaboration with the NIPC and the Corporate Affairs Commission, while tax offenders should be sanctioned.

It is important to note that widespread investment and contract awards to Chinese firms can cripple domestic contractors. Thus, the Nigerian Government must be conscious of the high level of unemployment prevalent and thereby give local contractors some considerations in the award of contracts with a view to creating jobs for Nigerians. Local contractors can equally be encouraged to partner with Chinese firms.

The issues of negative externalities associated with investment including those of Chinese in Nigeria is worth mentioning. Oil exploration and production as well as manufacturing activities have been known to be associated with a series of environmental problems. This is a major cost of Chinese investment to be borne by the host communities and producers in which such activities are carried out. There is therefore the need to ensure compliance of all firms including Chinese firms with social responsibility laws in Nigeria (if any). Thus, Nigeria can establish a body or an agency that will audit the performance of the organisations in terms of social responsibility. This will enable it to reward those that are performing well and sanction those that are not.

The importance of data for the purpose of periodic and continuous monitoring and evaluation of the impact of Chinese FDI in Nigeria cannot be overemphasized. Hence, the government has the responsibility to enforce the relevant law that will enable government agencies that gather data such as the National Bureau of Statistics (NBS), Nigerian investment promotion Council (NIPC), Federal Ministry of Finance and Central Bank of Nigeria (CBN) have access to important and necessary information for the evaluation of the benefits and costs of investment relation between Nigeria and China. It is on record that Chinese firms have the tradition of trying to hoard information on their activities in the host countries. The relevant ministries and departments

should be supported financially to gather information including those on China-Nigeria relations.

China-Nigeria investment relation just like any bilateral relationship has some advantages and disadvantages. This suggests that optimal outcome of the relationship will depend on the policies and institutions that are put in place particularly by Nigeria to maximize the complementary effects and to minimize the competing effects. China is virtually everywhere in Nigeria but information about its engagement and activities are fragmented. There is therefore, need to establish a coordinating body on China. This body, preferably a technical arm of an existing body, should be empowered to scrutinize and evaluate agreements, memoranda and any other articles of association between Nigeria and China. The ultimate objective of the proposed body is to spell out the cost as well as the benefits of Chinese-proposed projects and/or programmes. This is similar to what a legal department would do to an agreement before initialising/signing. The proposed technical committee in its assignment must have taken into consideration domestically available resources including skills and ensure that as much as possible, the local content of the agreement is high enough not only for the purpose of generating employment for Nigerians, but also to develop their technological capability.



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