



# Policy Brief

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## **The Impact of China-Africa Trade Relations: The Case of the Republic of Congo**

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### **Introduction**

#### *Statement of the problem*

The relations between China and Congo are already old since they began in 1963. However since the beginning of the 2000s, the economic relations between the two countries are characterized by an unprecedented dynamism. Congo's exports and imports with China recorded a leap of 179.38% and 309.21% respectively for the period 2001-2005. Such a trend pushed analysts to predict that the relations between Africa and China should have a significant impact and lead to upheavals in the structure of African economies. Two tendencies emerged in the literature: the first predicts that these relations would have a negative impact, in the sense that they would provoke a competition that African producers would not be able to bear. The second predicts that these relations would enable African countries to consolidate their growth, thanks to the diversification of trade and the installation of infrastructures which were lacking - such as roads, bridges, hydro-electric dams, drinking water purification plants, etc.

In sub-Saharan Africa, the Republic of Congo is part of the countries which have rapidly made great strides in trade relations woven with China. Congo's possession of important oil and forest resources on the one hand and China's enormous need for raw materials on the other are the two independent factors which have contributed to the strengthening of trade relations between the two countries (Bounboua Bazika, 2008).

The strengthening of trade between the two countries raises a series of problems which research must elucidate. These problems relate to the incidence of trade on Congo's macroeconomic performance, the possible gains and losses that this trade procures, and the opportunities and challenges for the Congolese economy.

Ultimately, the fundamental question that trade with China raises is that concerning the necessity to establish between the two countries of trade relations established on the win-win principle.

### *Objectives*

The general objective of this research is to assess the incidence of China's strong growth and trade on the Congolese economy.

The specific objectives are as follows:

- To determine the weight of China in Congo's exports and imports;
- To classify Congo's principal trade partners;
- To examine the incidence of trade with China on Congo's macro-economic performance;
- To determine Congo's gains and losses in trade with China;
- To analyse the opportunities and challenges arising from trade between China and Congo;
- To examine the economic policy implications;
- To suggest measures for the establishment of win/win relations.

### *Theoretical and methodological framework*

The analysis is based on the Ricardian theory of comparative advantages which stipulates that a country should import goods from a partner country where costs are lower in order to obtain a gain in the trade. It is then possible on the basis of this idea to carry out comparisons of the average costs (unit) of similar products being traded between several partners to consider the competitive advantage and the possible gains or losses caused by this trade. Let us take textile goods as an example. If a unit of a fabric is less expensive in China in comparison with France, it is more advantageous for Congo to import it China. By doing this it realises a gain. If on the contrary for certain reasons linked to the organisation of the market and trade traditions, the good is imported from France. In this case, this type of trade causes a loss for the importing country. The model described hereafter makes it possible to estimate the gains and losses by multiplying the differences in quantity by the differences of unit price.

The indicators are considered for the period 2006-2007. For exports and imports, it is a question of calculating the competitive advantage as well as the gains and losses of revenue attached to Congo's trade with China. We adopted the Ricardian approach of comparative costs to estimate the gains and losses arising from the exchange of similar products between Congo and China on the one hand and between Congo and other traditional partners on the other. The comparison was made with the main customers for exports and the leading suppliers for imports of similar products. If China became the leading supplier or customer of the product, the comparison was made with the countries which occupied the lower rank. This model that we developed on the basis of the comparison of unit costs made it possible to have an insight into the gains and losses of the exchange.

### ***Data and their sources***

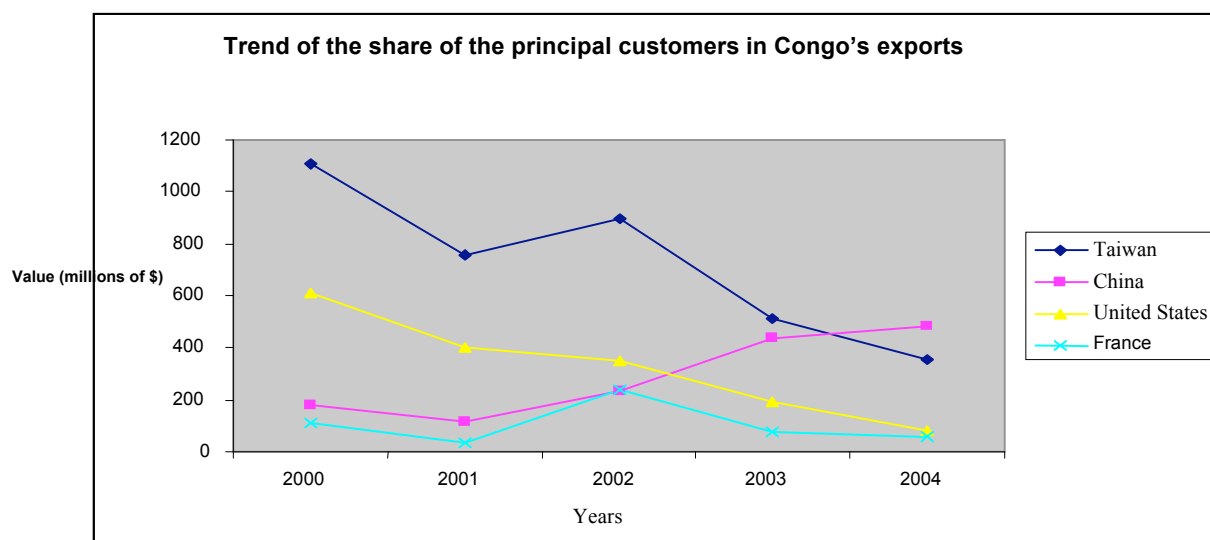
The data are mainly provided by the imports and exports statistical directories compiled by the Customs Service. These data cover 2006 and 2007. They include a nomenclature of several thousands of products of the 11-digit harmonised system (HS). The statistical data relate to the volumes (kg) and the values (CFA francs) of the traded products. The values of imports and exports are respectively CIF and FOB. For the purpose of harmonisation, the values were converted into dollars. The disaggregated data make it possible to know the products traded between Congo and foreign countries in a detailed and exhaustive manner. They also help to better perceive trade within the sectors of production and to have a more accurate view of the capacity of diversification of products and partners. Thus, an analysis of diversification, for example, is more robust when it is based on disaggregated data and the sectors than on a macro-economic approach. Aggregate data coming from National Centre for Statistics and Economic Studies (CNSEE) was also used. These data cover the period 2000-2007. The data collected constitute an interesting basis for considering the competitive advantages by basing oneself on the estimation of the unit costs of exports and imports as well as China's share in Congo's foreign trade according to products and trade partners.

### **Trend of trade with the traditional partners**

#### ***Exports according to the customers***

Export trends clearly show a spectacular growth of China which occupied the third place in Congolese exports in 2000 and which took the first place from 2004, thus dethroning Congo's traditional position of first customer held by Taiwan. If the trend of Congo's exports to the traditional partners (Taiwan, the United States, and France) is downward, on the contrary, China's weight in Congolese exports is increasing and China is the only country to experience this upward trend. The explanation of this trend is the strong increase in oil exports to China from 2001.

### **Graph 1. Trend of Congo's exports to its principal customers**

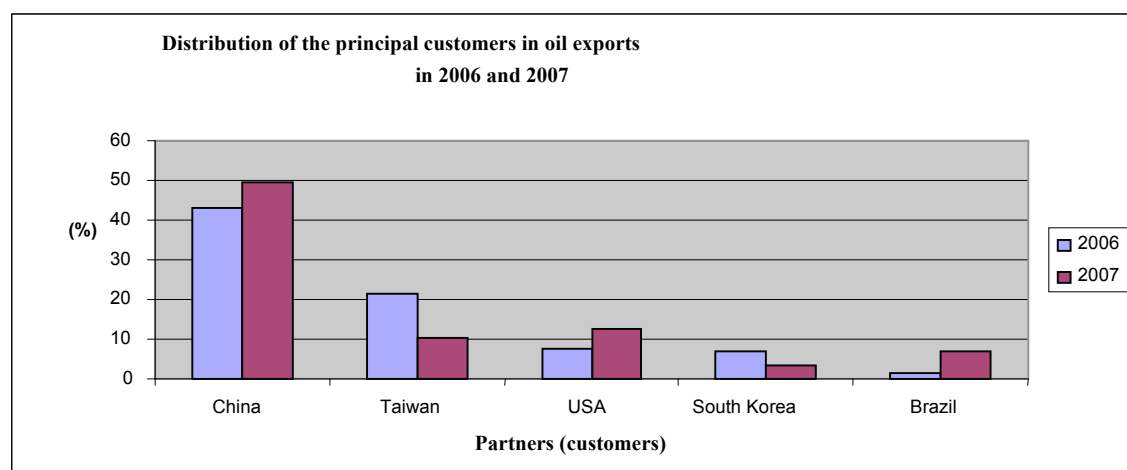


When one observes the trend of the distribution of the principal countries which are Congo's customers in oil sales, one can clearly note the growing weight of China these last years. Its share in exports tends to be strengthened compared to that of the traditional partner countries like Taiwan and the USA.

### *Exports according to products*

The two principal products, oil and wood, are mainly exported to China as the above graph shows.

**Graph 2: Geographical distribution of oil exports**



Concerning wood exports, China is by far the top customer with nearly 70% of exports.

**Graph 3: Geographical distribution of wood exports**

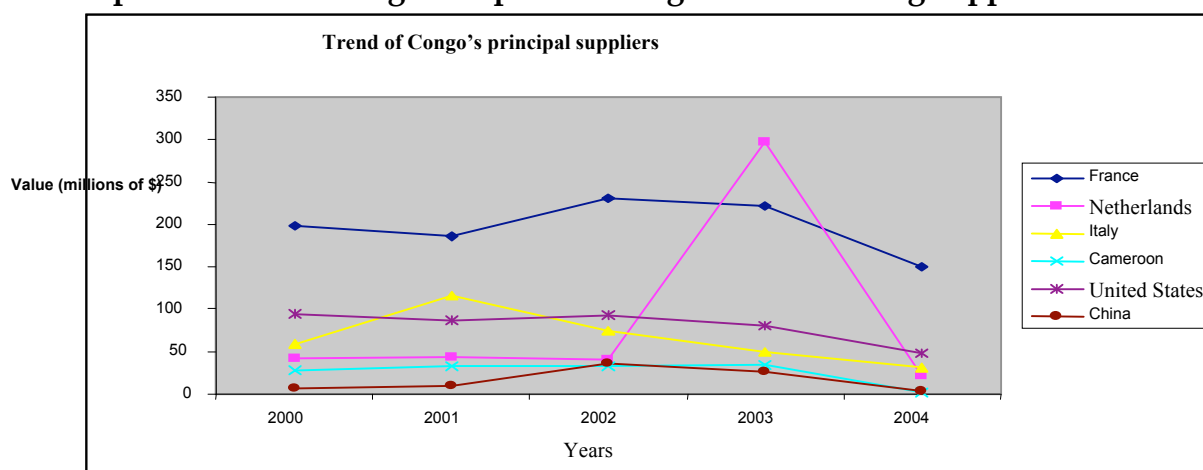


## Imports

Congo's imports have not experienced disruptions like exports. In fact, the same trends are noted; France continues to be the principal continuous traditional partner to hold a dominant position as a supplier of Congo. The United States occupies the second position, but far behind France. China's share experienced a slight increase from 2001 to 2003 and thereafter recorded a fall. In general, imports coming from China remain marginal.

Thus, if the impact of China in the area of exports from Congo is significant and is leading to a modification of the geographical structure of Congolese exports in favour of China. This impact is on the contrary low, indeed nil regard to the geographical orientation of Congo's imports. The traditional partners preserve their former position and the China's weight is very low.

**Graph 3. Trend of Congo's imports coming from its leading suppliers**



## Gains and losses of Congo's foreign trade

As following tables show, in 2007 Congo realised some gains in its imports coming from China and some losses in its exports to China. These trends are explained by the higher or lower unit costs of products traded with China compared to those of the other partner countries with which similar products were traded.

**Table 1: Unit price and gain of exports to China in comparison with other partner countries (2007) (in US dollars)**

Destination (partner)	Number of categories of similar products (HS)	Average unit costs of China's exports	Average unit price of exports to the partner	Congo's competitive advantage (%)	Gain obtained by Congo (in dollars)
Cameroon	5	0.342	0.342	100.12%	81.736.031
France	15	0.296	0.286	103.75%	576.342.910
Portugal	6	0.246	0.234	104.87%	-669 464.750
Germany	10	0.32	0.288	111.29%	427.981
The Netherlands	2	0.246	0.272	90.04%	-606 235.698
Italy	12	0.284	0.278	102.74%	-683 311.559
Belgium	5	0.326	0.326	100.07%	-61.100
Taiwan	11	0.302	0.304	99.46%	-78.536.529
South Korea	1	0.298	0.446	66.89%	-1.157.051 418
The USA	2	0.348	0.372	93.64%	-422 410.707

Sources: Calculations of the author on the basis of the data of the DGD

**Table 2: Unit costs and gain of imports coming from China in comparison with other partners (2007) (in US dollars)**

Origin (partner)	Number of categories of similar products (HS)	Average unit costs of imports coming from China	Average unit costs of imports coming from the partner	China's competitive advantage (%)	Gain obtained by Congo
Cameroon	29	2.10	7.37	28.45%	61.945.122
Italy	41	1.80	13.95	12.92%	145.773.421
France	76	2.02	8.86	22.74%	480.082.680
Belgium	42	2.05	7.98	25.71%	113.045.587

**Economic policy implications and challenges to be taken up to minimise losses and to maximise gains**

Because of the foregoing, four areas of policy implications can be identified which are as much challenges to be taken up. The challenges firstly revolve around the limitation of losses and the maximisation of gains in exports to China. They secondly revolve around the strengthening of imports which contribute to economising the outflows of foreign currency while taking care of the quality of imported goods. The challenges thirdly revolve around the need to benefit from China's expertise and industrial capacity so that Chinese enterprises which are setting up realise processed products and thus contribute to technology transfer and to improving the capacity to export products of strong value added.

The first challenge concerns the fixing of the oil price. This price is different from that of wood. For wood, the price is uniform on the market independently of the purchaser. On the contrary, the oil price seems not only volatile but variable according to the customers. In 2006, the unit price of oil sold in China was higher than that of 2007. Moreover, if in 2006 it was higher than that paid by a large number of partners in 2007, it was the opposite situation. This in addition is what explains the tendency to deterioration of losses for this period. The challenge to be faced up to is considerable. China has become a big customer and in addition an important investor in Congo. This position could have a great influence in the negotiations of prices.

The second challenge requires that the departments in charge of the quality control of imports be strengthened so that goods imported from China are of better quality and give full satisfaction to the consumers. Low prices allow a massive access of the poor to Chinese products. However, it is important to ensure that the products consumed are not of poor quality so that they have a positive incidence on the standard of living of households.

The third challenge necessitates the strengthening of the institutional mechanism and the improvement of the macro-economic environment and the business climate. Chinese enterprises, in particular those established in the forest sector, must be better controlled and the legislation requiring that most of the barks be processed on the spot should be better adhered to. In Cameroon, for example, the government has succeeded so that nearly 80% of the barks are processed on the spot. In Congo, the threshold of 80% fixed by the regulation is still far from being reached. The failures in the implementation of the legal mechanism must be corrected. In addition, the industrial and trade policy must be strengthened in order to improve the capacity to produce and to diversify products in production sectors like that of wood. This implies the improvement of the airport, road, railway and river infrastructures. The administrative procedures in the customs and others require to be reduced.

The fourth challenge revolves around the efficient management of the large monetary resources generated by exports of natural resources to China. Exports of raw materials, mainly of crude oil, to China have generated large monetary reserves from which the country should benefit to diversify the economy, to improve public services and to contribute to the reduction of poverty, which remains high with 50.7% people living below the poverty line (Ministry of Plan, 2006). The improvement of the management of public finances is a necessary condition for

benefiting from these monetary reserves. A project of reform of public finances is ongoing with the support of the World Bank, the European Union and the French Development Agency. This project consists in rationalising public expenditure, to computerising the expenditure chain, and improving the procedures of government contracts.

Congo's trade with China represents a formidable opportunity not only for strengthening export earnings and minimising the costs of imports, but also diversifying partners as well as production and exporting capacity. An improvement of the environment could constitute a factor of attraction of China's investments in the manufacturing production in Congo. Congo can also benefit from China's experience in the manufacturing industry by developing mixed joint ventures in sectors having a large export capacity on the regional and international market.

### **Conclusion and recommendations**

Trade between Congo and China has recorded a considerable increase these last years. China has in the five-year space become Congo's top partner at the level of oil and wood exports. Congo's trade with this country was a key factor in the strong economic growth of the period 2000-2007 recorded by the country. Imports coming from China have remained marginal. Congo's traditional suppliers, in particular the countries of the European Union and mainly France, have preserved their former positions. With regard to gains and losses, exports to China have resulted in losses and gains according to the trade partners to whom goods are exported and according to the period. With regard to wood, exports to China have procured Congo a competitive advantage and contributed to procuring the country substantial gains. With regard to oil, Congo recorded gains and losses according to the periods because the unit prices of exports of this good in China were at a lower level compared to the selling prices of oil to customer countries like the USA, Taiwan and South Korea. From 2006 to 2007, the losses were increased because the unit price of oil sold in China dropped. This is the essential reason that explains the losses in the trade. If the price were equal or higher than those of the other purchasers, the export earnings would have been definitely higher than those obtained.

Imports coming from China made it possible to save large resources. The low prices of imported Chinese products explain this favourable situation of Congo's foreign trade.

Trade with China has also highlighted the limitations of the capacity to diversify as well as the constraints to intra-regional trade. The tendency to export raw products and to import low-cost manufactured goods are at the root of the non-diversification of the wood sector and reduces imports coming from the CEMAC countries.

The challenges to take up consist in the application the regulation on the on-the-spot processing of wood, improving the business climate in order to attract Chinese enterprises in the manufacturing production and establishing an efficient management of public finances.

From the foregoing, the following are the economic policy recommendations:



- To negotiate advantageous prices in the sale of oil in China in order to align the prices to the level of the highest bidders and to maximize public revenue;
- To ensure compliance with the environmental rules in forestry development;
- To ensure quality control of imports coming from China;
- To anticipate the possibility of attracting Chinese manufacturing and construction enterprises by establishing joint ventures with them with a view to favouring the knowledge and technology transfers and guaranteeing the diversification of production and exports on the regional market;
- To improve the business climate thanks to the improvement of the administrative procedures of creation of enterprise as well as infrastructures and public services.