



# CENTRE FOR CHINESE STUDIES

## Report Summary

### **China's Interest and Activity in Africa's Construction and Infrastructure Sectors**

The People's Republic of China (PRC) has become an important and influential player in Africa. It is increasingly a source of political and financial support for many African governments, particularly in countries with many natural resources. A number of incentives are driving the commercial engagement of China with Africa. Principal among these is China's increasing need for energy sources and raw materials to fuel its rapidly growing economy.

Another motivation has been the development of markets for Chinese goods. Except for the relatively small number of resource-rich countries such as Angola and Zambia, the majority of African economies have mounting trade deficits with China. The Chinese have sought to offset these deficits with more favourable terms of trade for African products and the provision of aid in the form of infrastructure.

China's involvement in Africa's construction and infrastructure sectors has proved most effective in building relations with African governments—increasing influence and expanding access to natural resources on the continent. Chinese state-owned enterprises (SOEs) and private companies are making strategic inroads into the construction and infrastructure sectors of many African economies. This is at the expense of European and South African companies which previously dominated these sectors. Naturally, the traditional actors are alarmed by this phenomenon and there are concerns that China's politically determined business models do little to build local capacity.

The Centre for Chinese Studies conducted research in four countries to evaluate the market entry models of Chinese construction firms in Angola, Sierra Leone, Tanzania and Zambia. The study was funded by the UK Department for International Development (DFID). Particular attention was paid to the methods of engagement and the impact on the local construction industries. Chinese activity in the four case studies was examined and then compared across five areas: 1) tendering, 2) access to capital, 3) labour, 4) procurement, and 5) quality of workmanship. Trade and bilateral relations between China and the countries concerned were also taken into consideration.

### **Market Entry Strategies**

China's Africa focus is undoubtedly geared towards resource-rich countries such as Angola, Nigeria, Sudan, Tanzania, and Zambia. However, China is rapidly expanding its presence across the African continent, with a strong preference for larger and/or more stable economies. Prior to 1979, state-owned construction enterprises were among the few Chinese institutions permitted to leave the mainland and conduct business in the outside world. The experience of these companies in the construction of large-scale infrastructure projects, often in extremely isolated areas, has proved invaluable. With access to substantial liquidity, it is no surprise that Chinese SOEs are at the forefront of China's engagement with Africa.

Winning the bid for a government-endorsed contract enables Chinese companies to secure low-cost capital from Chinese banks to deal with the expensive start-up costs associated with moving the necessary equipment into place. Before leaving China, these companies regularly engage a host of private Chinese sub-contractors specializing in different areas of construction such as plumbing, electrical engineering and air-conditioning which they take with them. Once the project is undertaken within the respective country, the companies use the opportunity to gain first-hand knowledge and experience of the local environment and identify additional opportunities. While these companies clearly prefer large-scale government projects, they will also engage in small-scale private projects and make full use of their access to relatively cheap capital from Chinese banks when necessary. It is at this juncture that the Chinese companies first encounter competition with local companies.

### **China's Edge**

The competitiveness of Chinese construction companies may largely be attributed to their access to cheap capital, low labour costs, hands-on management style, high degree of organization, and general aptitude for hard work. Chinese worksites are usually highly organized and all the personnel, from the executive down, invariably live and work on the site full-time. This "hands on" style of management saves considerable time and provides all levels of management with a profound understanding of the project and the ability to handle challenges as they occur. While local and foreign construction companies operate on profit margins of 15-25 percent, Chinese companies usually operate on margins of 10 percent or less making them extremely competitive.

The Chinese government is very supportive of Chinese construction companies. All the Chinese diplomatic representatives interviewed for this study were however adamant that this support is in line with free trade practices and limited to "political support".

Travel between China and Africa is increasing steadily. The number of flights between the two regions is rising steadily and Chinese Embassies in Africa are streamlining the visa application process to facilitate greater travel between China and Africa. At the same time, access to European and North American markets, networks, and academic institutions for African businesspeople is becoming increasingly difficult. Immigration policies are being tightened, further encouraging increased commercial engagement with China.

### **Competition with Traditional Players**

In countries specifically targeted by the Chinese government such as Angola, Zambia or Tanzania, the initial arrival of the Chinese construction companies has had an enormous impact on the local industry. Foreign companies, mainly from Europe and South Africa, which had traditionally dominated the construction sector, were the first to experience competition with the Chinese. In Zambia and Tanzania, Chinese construction companies have rapidly gained approximately 30 and 40 percent of the respective markets over the past five to ten years. Chinese companies have only just entered Angola and are expanding rapidly causing considerable alarm as many of the traditional players find themselves unable to compete. Given the scale of China's investments in Angola, we can expect it will be some time before the market adjusts to the entry of Chinese companies. This is in marked contrast to Sierra Leone where the construction market remains small and only a small number of Chinese construction companies are operating.

Very few local companies in the countries surveyed have the capacity for large-scale projects and rarely find themselves competing with Chinese companies in the early stages of the latter's market penetration. We observed a number of cases where Chinese companies regularly subcontract local companies, albeit with strong reservations. Many of the Chinese company representatives consulted expressed dissatisfaction over the quality of the work done by local contractors. They cited concerns over local firms' ability to manage finances and keep to deadlines. Western companies maintain a slight competitive edge over their Chinese competitors when it comes to specialized or technical areas of construction such as airports and harbours, especially in finishing and reliability as well as quality and timeliness, which enables them to secure work and access finance, especially from local sources. The gap is, however, closing.

### **China on China Competition**

Competition between Chinese companies is fierce and the diversity of Chinese construction companies operating in Africa is enormous, ranging from multi-billion dollar SOEs from mainland China to small single-person operations established by Chinese nationals living in-country.

The majority of Chinese companies in the initial phase of market-entry are SOEs, although the number of private Chinese construction companies is growing rapidly. The study found that while SOEs receive greater assistance from the Chinese government in terms of access to African governments and information on market tenders, private construction companies appear to be more efficient in project implementation. Where Chinese construction companies are properly established, the only serious competition they face is from one another. Such competition serves to streamline operations, reduce costs and improve quality. However, the low profit margins accepted by Chinese companies are likely to be unsustainable in the medium-term, thereby exposing them to a range of risks including currency fluctuations and rising energy, transport and commodity prices.

### **Quality and Standards**

The level of standards among Chinese companies varies. While there are instances of Chinese companies completing work of substandard quality, they have clearly proved themselves capable of achieving extremely high quality work as observed in Zambia, underlining the importance of supervision with regards to quality and standards. In countries such as Sierra Leone and Angola where the government authorities lack the capacity or political will to enforce building codes, structures of sub-standard quality are considerably more common than in countries where the authorities effectively enforce the law.

### **Procurement of Materials**

Chinese-made construction materials are increasingly popular due to their more competitive prices. Opinions on the quality of these Chinese materials vary, but the majority of respondents agreed that the quality is improving. China now has the capacity to produce extremely high-quality building materials at a corresponding price. In smaller markets such as Sierra Leone only lower quality materials are available. This has led to a situation where lower-end quality Chinese goods have pushed out many foreign competitors and high quality Chinese products are simply not readily available due to perceived lack of demand. Although several knowledgeable respondents insisted that demand for better quality materials exists, the market appears to judge otherwise.

Chinese companies in each of the countries surveyed have been granted tax breaks on importing construction materials. Yet there were widespread reports that these tax breaks are being abused. Consumer goods such as clothes and electrical items for local distribution are allegedly smuggled in along with construction materials. Such allegations remain difficult to verify.

## **Labour**

Labour has been an extremely contentious issue in all the countries surveyed. The general perception is that Chinese companies are bringing in their own labour and underpaying the local workers they do employ. Except in Angola, local personnel accounted for between 85-95 percent of the total workforce of most of the Chinese construction companies examined for this survey. While predominantly employed as unskilled casual labourers, there were many instances of locals employed in administration and managerial positions – a phenomenon more common in companies with a longer in-country presence.

Without exception, all the Chinese construction companies commented on the lack of skills and extremely high turn-over of local workers. Aside from Angola, where the price of local labour is already relatively high, Chinese companies in the other three countries surveyed appear to be gradually increasing salaries to retain “good” employees. Stories of Chinese construction companies using Chinese prison labour are widespread in all countries surveyed, but no evidence was found to support such rumours.

## **Joint venture business models**

There are very few examples of joint ventures between Chinese companies and local firms in the countries surveyed. Although several joint ventures were identified in Angola, there were none in Tanzania and only one in Zambia that was reportedly successful. In Sierra Leone one example of a joint-venture was discovered, although details were very unclear. Very few of the Chinese construction companies consulted were even remotely interested in entering into such an arrangement with a local partner. The main problem they envisaged with joint ventures was lack of trust, while several suggested that local partners have very little to offer. Their preferred mode of engagement with local entities is through sub-contracting arrangements for discrete sections of projects.

## **Capacity building**

Many respondents suggested that Chinese technology is “appropriate” for Africa. The techniques and practices many of the Chinese companies bring are low-tech and relatively easy for African construction companies to emulate, as opposed to the often specialized and capital-intensive equipment used by Western companies.

The technologies and methodologies employed by Chinese companies are generally easier to transfer to local industry. While some Chinese companies maintain the use of low-level technology, others are slowly adopting more sophisticated methods and technology, utilizing

comparatively cheap equipment within the reach of the larger local firms. This bodes well for future technology transfer from Chinese construction companies to local firms.

With the exception of Angola where the majority of Chinese companies import all their equipment, materials and labour directly from China, the Chinese construction companies interviewed in the other three countries surveyed claimed that they provide employees with on-the-job training focusing particularly on machine operation. Local engineers have also remarked that they have learned new techniques on site visits to Chinese construction projects.

### **Conclusion**

Though historic and ideological ties provided a base for China's initial relations with the continent, China has increasingly sought stronger commercial relations with Africa. The Chinese government and companies are looking further than quick profit. They are focussing on areas where they perceive medium to long-term benefit in terms of acquiring natural resources. This prompts them to pursue strong relations with countries such as Angola, Zambia and Sudan. Construction companies, both SOEs and the growing number of private companies, earn hard currency and provide a convenient platform to penetrate new markets and secure access to natural resources through investment, trade and military assistance. In this respect, Chinese companies are not very different from Western multinationals.

Even though Africa's markets present a new frontier for Chinese products and services, access to raw materials appears to be the underlying force in China's engagement with the continent. We can expect the location of oil and minerals to dictate the geographic focus of China's future engagement on the continent. China's diplomatic presence is spread across the continent and continues to grow. It was observed that substantial (re)construction of Chinese diplomatic missions was being undertaken in at least three of the four country case studies. The Chinese are now well positioned to take advantage of new opportunities wherever they might occur.

Neglected until the late 1980's, the contribution of infrastructural development to broader economic and social development is now widely acknowledged. Despite the enormous challenges the Chinese face concerning their own development, China's focus on infrastructural development with the construction of roads, bridges, hydroelectric and irrigation schemes, schools hospitals, health centres and an array of government buildings is making a clear contribution to development in Africa.

For a copy of the full report, please email: [ccsinfo@sun.ac.za](mailto:ccsinfo@sun.ac.za) or download the full report at:

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