

Chinese Investors in Ethiopia: The Perfect Match?



Françoise NICOLAS

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Cover Picture: Chinese locomotive driver Liu Ji (R) trains his Ethiopian counterparts at a railway station in suburban Addis Ababa, Ethiopia, Oct. 1, 2016. © www.news.cn

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Ifri

27 rue de la Procession 75740 Paris Cedex 15 – FRANCE

Tel.: +33 (0)1 40 61 60 00 – Fax: +33 (0)1 40 61 60 60

Email: accueil@ifri.org

Website: ifri.org

Author

Françoise Nicolas is Director of Ifri's Center for Asian Studies. She has been with Ifri since 1990. She also teaches at Langues' O, Sciences Po (Paris) and Sciences Po (Lyon) and is an occasional consultant to the Directorate for Financial, Fiscal and Enterprise Affairs (DAF) of the OECD.

In the past she has been an assistant Professor in international economics at the University of Paris-Est (Marne-la-Vallée, 1993 - 2016) and has taught at the Graduate Institute of International Studies (GIIS, Geneva – 1987-1990), at the *École nationale des Ponts et Chaussées* (1991-1995), as well as at the HEC School of Management (2000-2002).

Françoise Nicolas holds a PhD in international economics (1991) and a MA in political science (1985) from the Graduate Institute of International Studies (Geneva, Switzerland). She has also studied at the University of Sussex (1980-1981) and has spent some time as a visiting fellow at the Institute of Southeast Asian Studies (ISEAS) in Singapore (1999) and at the Korea Institute for International Economic Policy (KIEP) in Seoul (2004).

Executive Summary

Since the fall of the Derg regime in 1991, cordial relations have developed between China and Ethiopia, forming a positive political backdrop in front of which the two countries' interests have increasingly converged.

On the one hand, Ethiopia seeks to replicate the experience of East Asian countries such as Taiwan, Malaysia, or China and to attract foreign direct investment (FDI) in order to accelerate the development of its manufacturing capacities (in particular through an ambitious industrial Park – IP - development program and the acceptance of foreign-owned Special Economic Zones - SEZs). On the other hand, China looks to export its development model (including SEZs), to delocalize its most labor-intensive activities, and to promote connectivity between Asia and the African continent. In this context, the Chinese government identified SEZ projects in 19 countries – including one in Ethiopia (the so-called Eastern Industry Zone - EIZ), located in Dukem some 30 kilometers southeast of Addis Ababa.

Today, China is by far the leading foreign direct investor in the country. In addition to the Chinese-owned EIZ in Dukem, Chinese investors are also present in privately-run SEZs that are not part of the MOFCOM strategy, as well as in government-led IPs and outside SEZs or IPs. Lastly Chinese firms are also extremely active in all kinds of infrastructure development thanks to Chinese funds.

Chinese investment in Ethiopia does not match the standard view of Chinese FDI in Africa, wherein investors are seen as looking for natural resources and plundering the country. Far to the contrary, as Chinese investments in Ethiopia are concentrated in infrastructure and in the manufacturing sector, they were expected to play a transformative role and give rise to a “win-win” outcome.

For the time being, however, the assessment is mixed at best. Although China has certainly played a useful role in Ethiopia by setting up industrial zones, financing infrastructure, and encouraging Chinese firms to move some manufacturing production to Africa, thus contributing to the industrialization process, its transformative power remains limited. Backward linkages (through the purchase of materials and services from the local economy) as well as forward linkages (which refer to a situation where foreign companies sell goods or services to domestic firms) are not

easy to come by. In particular, local inputs are not always up to the standards expected by Chinese producers. Also, skills transfers that may simply occur through labor mobility so far remain limited, as the workers are concentrated in low-skilled jobs. For all these reasons, Chinese investment has not proven to be as transformative for Ethiopia as inbound investment was for China in the late 1980s.

In particular the hope of turning Ethiopia into an international shoe and light manufacturing hub remains elusive so far. Overall, Ethiopia's export pattern remains dominated by agricultural products (coffee/tea, vegetables and live trees and cut flowers), while garments and footwear account for less than one percent of the country's total exports.

Rather than manufacturing investments, Chinese investments in infrastructure may have proven to be more instrumental in transforming the country. The construction of new dams, for instance, has been instrumental in guaranteeing a stable supply of power and helping Ethiopia to realize its plan of becoming a major electricity exporter.

The explanation of this disappointing result in garments, footwear and other light manufacturing sectors lies with policies. The two-pronged approach to SEZs followed so far by the Ethiopian authorities, with government-led IPs coexisting with private foreign-led SEZs, is certainly a good approach since there are more FDI firms wanting to invest or expand in industrial zones in Ethiopia than the government can offer. However, it is important to make sure that the zones' activities are aligned with the country's needs in terms of industrial development. This is less likely to be the case if the state is not actively involved, as in the case of foreign-owned private SEZs.

However, various developments suggest that the situation may be changing soon. First, Ethiopia's strategy has recently shifted in favor of government-led IPs, the logic of which is much closer to that of SEZs promoted in East Asia. Moreover, newly developed projects, such as the Huajian International Light Industry City, are also promising, as the sectoral orientation of the project is in line with the country's industrial objectives. As these developments are still recent, the jury is still out on the reality of backward linkages and the ability of Ethiopian firms to take advantage of the presence of Chinese firms and technology, and hence on the potentially substantial benefits. The prospects look rather good, provided other accompanying measures are put in place so as to improve the overall business environment, and, probably more importantly, to enhance the local labor force's "absorptive capacity".

Table of Contents

INTRODUCTION	6
BACKGROUND ELEMENTS TO THE CHINA-ETHIOPIA ROMANCE	8
The historical context: a long-standing partnership.....	8
Ethiopia’s industrialization strategy: East Asia as a model.....	9
China’s strategy: from “Going out” to “One Belt, One Road”	13
CHINESE INVESTMENTS IN ETHIOPIA	17
An overview	17
Chinese-led special Economic Zones.....	19
Chinese investment in infrastructure	24
ASSESSING THE IMPACTS OF CHINESE INVESTMENTS.....	27
Ambivalent perceptions	27
Economic impacts: win-win, really?.....	28
CONCLUSION: PROSPECTS AND IMPLICATIONS	35

Introduction

“Overseas economic and trade cooperation zones not only promote the investment abroad by our enterprises, but also bring the significant opportunity for local economic development, achieving the mutual benefit and win-win.”¹

China’s interest in Africa is nothing new. It has been engaging the region for a long time, initially for political and diplomatic reasons (so as to gain support in its attempt to regain its seat at the UN in particular), and increasingly for economic reasons, in search of natural resources (oil, gas, and other minerals). The impact of the latter initiatives on host countries is hotly debated. In resource-rich countries, the suspicion is that Chinese investment may be to a large extent self-serving (investment is often said to be part of a grand strategy to secure resources in Africa, as evidenced by resource-backed loans); moreover Chinese investments are often criticized for crowding out local labor by bringing in Chinese workers and for crowding out local products. In other words, China is said by some to be merely practicing a new form of colonialism, making the best of Africa’s natural resources and cheap labor without any major gains for the local population. However, other analysts claim that China may be an ideal partner for development and they see China’s presence as beneficial to both China and Africa.

Although part of the earlier sources of concern may still be valid, China’s involvement in resource-poor African countries is generally thought to be more positive. Ethiopia is one such partner. Despite its lack of natural resources the country has managed to become one of China’s top trading partners and one of its top investment destinations in Africa. Interestingly, Ethiopia is often portrayed as “the next China” or “China’s China” with a substantial number of Chinese firms relocating their production to this part of the world. Lastly Ethiopia is apparently following in China’s footsteps on a number of counts, and in particular in the implementation of Special economic Zones (SEZs), to some extent with China’s help. For all these reasons, it is worth analyzing the rationale and nature of Ethiopia’s partnership with China in more details.

1. “Led by the Construction of “Belt and Road”, Creating the New Ground of Opening Up” – Gao Hucheng, Commerce Minister of the People's Republic of China, 14 April 2016.

The objective of the paper is to examine why and how Chinese investments have developed in Ethiopia and what may be their impact. It will seek in particular to assess whether Ethiopia is a case of a win-win partnership², focusing in particular on the potential contribution of SEZs.

The paper starts out by explaining the context of the Sino-Ethiopian economic partnership, then moves on to examine the form of Chinese economic presence in Ethiopia in detail before finally assessing its impact on the local economy.

2. Xi Jinping's speech at the Johannesburg Summit of the FOCAC in 2015 stressed the "opening of a new era of China-Africa win-win cooperation and common development". Available at: <http://english.cri.cn>.

Background Elements to the China–Ethiopia Romance

The historical context: a long-standing partnership

The first contacts between China and Ethiopia go back to the mid-1950s, when Chinese Premier Zhou Enlai actively engaged the leaders of 6 African countries – Egypt, Ghana, Ethiopia, Liberia, Libya and Sudan – at the Afro-Asian conference in Bandung (Sun 2014), which aimed to promote Afro-Asian economic and cultural cooperation and to oppose colonialism or neocolonialism under any form. China perceived the neutral position of most African countries between capitalist and socialist blocs as conducive to China's interests.

However, bilateral relations developed cautiously in the 1960s and the two countries were divided in the Eritrean conflict, with Beijing supporting the Eritrean Liberation Front (ELF). When Ethiopia finally established diplomatic relations with the PRC in 1970, it extracted a promise that Beijing would terminate support for the ELF (Shinn 2015).

Bilateral relations soured once again following the 1974 military coup, which toppled the Haile Selassié monarchy and gave rise to the Derg régime, as Moscow shifted its support to Addis Ababa. This development undermined China's goal of strengthening relations with Ethiopia. During the entire period of the Derg régime (1974–1991), however, little changed in the Sino-Ethiopian relationship, as the two countries even signed some economic and technological agreements, and bilateral economic development cooperation continued despite the political tensions. Official visits between the two countries only resumed once the Sino-Soviet conflict came to an end in the mid-1980s.

The fall of the Derg régime in 1991 opened the door to the return of more cordial political relations between Beijing and Addis Ababa. The visit by Ethiopia's then-Prime Minister Meles Zenawi to Beijing in 1995, which was reciprocated by Chinese President Jiang Zemin one year later, ushered in a period of intense political relations, marked by a series of high-level visits to each other's national capitals. But China's activities in Ethiopia

only became visible at the turn of the century, with the launch of the Forum on China Africa Co-operation (FOCAC) in 2000.

As recalled by Cabestan (2012), Ethiopia's interest in a tight partnership with China lies in the latter's active engagement in economic development: PM Zenawi encouraged closer ties with China with a view to tapping its financial resources and balancing close ties with Western countries, particularly the United States. As for Beijing, the presence of several headquarters of international organizations in Addis Ababa (UNECA and African Union) made it an attractive partner. As a symbol of the close relationship, Addis Ababa was chosen to host the second FOCAC in 2003. Moreover, the two partners share the view that economic advancement should be given priority over democracy, and this convergence of views further nurtures their partnership (Dollar 2016).

Overall, despite tensions primarily resulting from external factors, there has been no real break between the two countries ever since the establishment of diplomatic relations in 1970. Against this favorable backdrop, the two countries' interests have increasingly converged over the past two decades. Ethiopia has embarked on an industrialization strategy while China's "going out" policy has been given new momentum through its One Belt, One Road (OBOR) program.

Ethiopia's industrialization strategy: East Asia as a model

Industrialization as a priority

Due to internal problems associated in particular with the war and separation of Eritrea, Ethiopia was unable to concentrate on a genuine economic development effort before the early 2000s. From around 2002-2003, PM Zenawi announced a series of policy initiatives, including the Agricultural and Rural Development Policy and the Industrial Development Strategy. Ever since, Ethiopia's economic development process has been governed by a succession of large-scale government development plans: the Sustainable Development and Poverty Reduction Program (2002-2005), the Plan for Accelerated and Sustained Development to End Poverty (2005-2010), and the Growth and Transformation Plans I and II (GTPI 2010-2015, and GTPII 2015-2020).

Transformation here means industrialization. For the time being, however, the economy is still dominated by agriculture which, in 2015, still

accounted for about 38.8 percent of GDP³, 90 percent of foreign currency earnings and 85 percent of employment. The objective of GTP I and II is to turn Ethiopia into a middle-income country by 2025 and one of the key pillars for reaching the target is the development of light manufacturing activities.

Following the example set by several East Asian economies, such as South Korea, Malaysia, but also by China,⁴ Ethiopian authorities are in favor of government interventions with the state leading the industrialization process.⁵ Although it is difficult to trace the specific moment when Ethiopia officially embraced the developmental state model, the narrative of advocating the developmental state as the best path for Ethiopia started to be heard very clearly in the early 2000s, when PM Zenawi emphasized the need for fast economic growth as a way of ensuring Ethiopia's survival as a country.⁶

Attracting FDI is at the core of Ethiopia's industrialization strategy,⁷ which is supported at the highest level and in particular by the Prime Minister himself (Ohno, 2013). To that end, Ethiopia's investment policy has been reformed at least four times over the past 20 years, making the country increasingly open to FDI.

Focusing on the manufacturing sector, Ethiopia is prioritizing FDI in specific sectors: textile and apparel, leather and leather products, agro-processing, and pharmaceuticals and chemicals. The imperative is to build on the country's agricultural foundations⁸ by moving toward new tradable activities in manufacturing that absorb large numbers of young and semi-skilled workers. Ethiopia's potential in the light manufacturing sector is significant, but faces binding constraints related to access to land, infrastructure, trade logistics, customs regulations and a skills gap (World Bank, 2012). FDI is seen as a way of lifting all these constraints, with an important role to be played by Special Economic Zones (SEZs).

3. The industrial sector accounted for 15.2 percent and services for the remaining 46 percent.

4. In various speeches, Japan, South Korea, Taiwan and more recently China are being explicitly mentioned as examples.

5. This position was clearly stated by Bereket Simon, the chairman of the Commercial Bank of Ethiopia and advisor to the PM, who explained that Ethiopia from the outset defied the Washington Consensus and such policy prescriptions based on the conventional wisdom of "one size fits all" and opted to formulate its own policy based on the objective reality of the country.

6. This is the argument made in his master thesis "African Development: Dead Ends and New Beginnings" where he calls for a paradigm shift away from the predatory state and neoliberal paradigm to a home-grown and more progressive one, i.e. the democratic developmental state.

7. Interestingly, as recalled by Chaponnière (forthcoming), such a strategy was already favored by Emperor Haile Selassie in the 1940s.

8. This is referred to as "agricultural development-led industrialization".

Replicating the SEZ experience

In an attempt to alleviate the constraints highlighted earlier, the Ethiopian government has launched an ambitious Industrial Park development program. Industrial Parks (IPs) are defined as geographically delimited areas that are administered by a single body, and aim to overcome investment barriers at the national level by offering services, infrastructure, and incentives for businesses that locate and operate within the site. The objective is to use IPs as a means of kick-starting Ethiopia's manufacturing sector. IPs are often favored because systematic investment-climate reforms in multiple areas take time to address and are politically challenging to implement.

With this scheme, Ethiopia is seeking to replicate the experience of East Asian countries such as Taiwan, Malaysia, or China, which have made an extensive use of IPs or SEZs to attract foreign investment and push their industrialization.

The GTP identifies IPs (or SEZs) as one of the means for industrialization and includes provisions on the establishment of SEZs for the following manufacturing industries: textiles and garments, leather and leather products, sugar, cement, metals and engineering, chemicals, pharmaceuticals and agro-processing products. The point of selecting these specific sectors is to maximize Ethiopia's comparative advantages.

The Ethiopian Industrial Parks Development Corporation (IPDC), established in 2014, is mandated to develop and operate the parks, availing developed land and pre-built sheds equipped with all-encompassing utilities and infrastructural facilities. The industrial zones offer land for factories at US\$1 per square meter per month, tax holidays for up to seven years and customs and other services on site for those investing in the country.

The Industrial Parks proclamation 886/2015 provides that industrial parks can be developed by any profit-making public, public-private or private enterprise. Three paths are envisaged for the construction of IPs/SEZs:

- 1) they may be designed and built by government;
- 2) they may be built through public-private partnerships (PPPs) with the IPDC;
- 3) they may be designed and developed by private developers only.
The investment is open to domestic and foreign investors.

The GTPI envisions the establishment of five industrial parks in the country: two in the Addis Ababa area (Bole Lemi and Kilinto Industrial Parks), one in Hawassa, one in Dire Dawa and one in Kombolcha. The country is targeting US\$ 1 billion of annual investment in industrial parks over the next decade to boost exports and make it Africa's top manufacturer.

At the time of writing, Bole Lemi Phase 1 (covering 156 hectares) is the first IP operating under the IP development strategy. It was established in 2012 with the help of a World Bank loan, and started operation in 2014. It now consists of some 20 pre-erected factories (of 185,000 square meters of factory space) rented-out to more than 10 foreign-owned manufacturing companies producing and exporting leather and apparel goods (see Table 1). Bole Lemi Phase 2 (covering 186 hectares) is currently under construction with the financial support of the World Bank.

Table 1: List of Licensed Investment Projects in Bole Lemi Industry Zone (as of July 2015)

Date of permit	Name of investor	Country of origin	Investment activity	Planned investment (thousand US \$)	Investment status	Number of employees	Number of sheds
26/11/2013	New Wide Garment (Ethiopian Branch)	Taiwan	Manufacturing of wearing apparel (including sportswear)	1,000	Operation	340	1
10/01/2014	Shints ETP Garment Plc	South Korea	Manufacturing of garments	7,670	Operation	2,500	5
07/02/2014	Ashton Apparel Manufacturing Plc	India	Manufacturing of garments for export	5,000	Operation	648	2
25/12/2013	C & H Garments Plc (M & M Garments Plc)	China	Manufacturing of wearing apparel (including sportswear)	5,000	Operation	200	1
17/07/2014	Lyu Shoutao Factory Plc	China	Manufacturing of leather products (including gloves)	700	Operation	194	1
18/10/2013	Jay Jay Textiles Plc	India	Manufacturing of wearing apparel (including sportswear)	2,000	Operation	937	3
14/10/2013	George Shoe Ethiopia Plc	Taiwan	Manufacturing of leather shoe	5,750	Operation	1,100	2
11/06/2014	Vestis Garment Production Plc	India	Manufacturing of garments	575	Operation	150	1
17/09/2013	Arvind Lifestyle Apparel Africa Plc (ANF GULF)	India	Manufacturing of garments	4,000	Operation	586	2
01/07/2014	KEI Industrial Engineering Consultancy Plc	US/South Korea	Manufacturing of garments	2,000	Operation	126	1
18/06/2015	Nitton Apparels Manufacturing Plc	China	Manufacturing of garments	4,000	Pre-implementation	–	1
TOTAL				37,695		6,781	20

Source: Ethiopian Investment Commission.

The World Bank also supports the development of the new industrial hub in Kilinto, 20 miles south of the capital (Dollar, 2016). Kilinto aims to be a mixed-use park and the top destination for manufacturers in agro-processing, pharmaceuticals, electric and electronics products, wood and furniture, both for export and to serve local consumers.

Hawassa eco-industrial park (HIP), which covers 300 hectares of land, is the third government-sponsored industrial park, located 275 km south of Addis Ababa. The IP was designed and constructed by the China Communications Construction Company. The park will house 15 textile and garment firms from China, India, the US, and Sri Lanka, in addition to six Ethiopian companies. The park has 38 pre-erected factory sheds and 19 buildings to house these firms. The development of HIP started in mid-2015 and the park was inaugurated in July 2016. Currently, 10 factory sheds are already rented out to foreign companies. The park is principally focused on textile and garment products for exports.

In addition to government-sponsored IPs, several private foreign-owned industrial zones (IZs) have been established. The largest one is the Chinese-owned Eastern Industrial Zone (EIZ) in Dukem, some 40 km east of Addis Ababa. Other private IZs include the Lebu Industrial Zone, which is owned by Huajian Group⁹ (also called the Huajian International Light Industry City), and the Modjo Industrial Zone, owned by Taiwanese George Shoe. The IPDC had also planned to construct another park in Addis Ababa in a joint venture with Turkish Ayka Addis Textile and Investment Group,¹⁰ but the project is apparently stalled due to financing difficulties.

China's strategy: from "going out" to "One Belt, One Road"

Going global and promoting SEZs

In the mid-1990s, the Chinese government began to emphasize a policy of "going out" or "going global" (*zou chuqu*), which encouraged Chinese companies to target new markets, build global brands, and invest abroad. In support of this strategy, the CCP's eleventh Five-Year Plan in 2006 called for a global expansion of Chinese *special economic zones* (SEZs).

The choice of the contractors for the zones is made through a competitive tender led by the Chinese Ministry of Commerce (MOFCOM).

9. Huajian is said to be the world's largest OEM (Original Equipment Manufacturer) of brand shoes.

10. This is one of the biggest foreign investors in Ethiopia, with 7,000 workers.

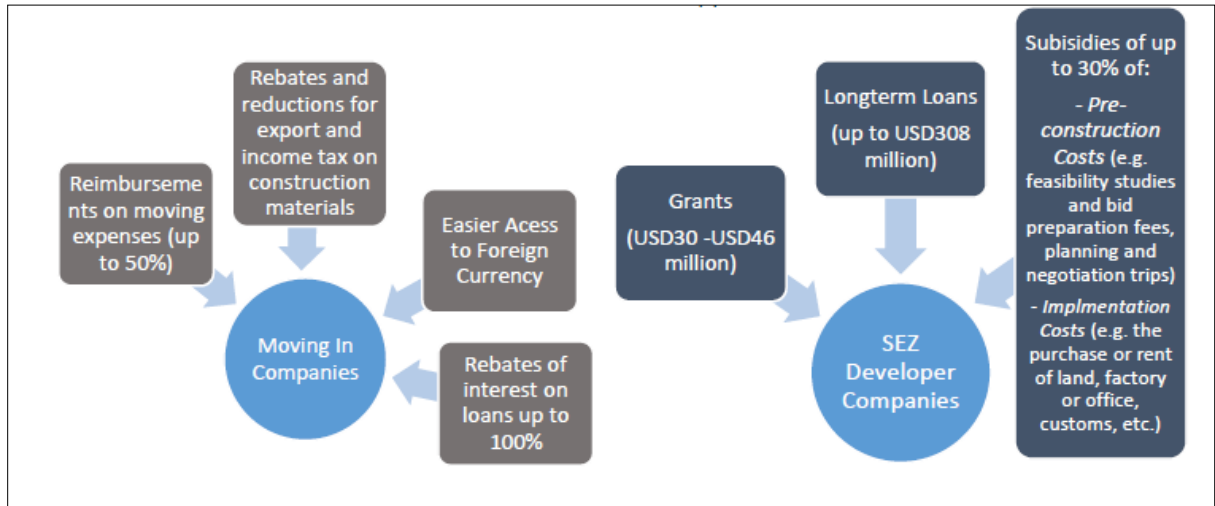
Although the Chinese government is not involved in the design or direct operation of the cooperation zones, it plays a supporting role through the provision of various forms of financial support, including subsidies, so as to reduce the commercial risk for Chinese investors.

To be more specific, Chinese companies working on the development of these zones are eligible for grants, loans and rebates on interests, in addition to subsidies that may cover up to 30 percent of pre-construction and implementation costs (El Rashidy, 2016). It is worth noting that MOFCOM incentives are performance-based: as a result, developers of China's overseas SEZs are expected to submit periodic progress reports to MOFCOM and are also subject to receiving evaluation missions. Companies moving into one of China's overseas SEZs are also offered a similar package of incentives.

Interestingly, although the Chinese program of overseas SEZs is presented as a state-led initiative, the actual implementation is in the hands of Chinese developer companies: Chinese companies negotiate with the host country government, while the Chinese government (namely MOFCOM) merely intervenes in cases where government-level negotiations are needed, in particular to go over treaties that may benefit the work of the zones, for instance. The responsibility between the stakeholders has been divided so that the Chinese enterprise, with the support of the Chinese government, is responsible for the development within the zone, while the host government is, in principle, responsible for the development of infrastructure outside the zone.

In addition to the host country government, three actors are involved: the Chinese developer, the Chinese government (MOFCOM) and the operating, profit-oriented companies (Figure 1).

Figure 1: China's MOFCOM's Mechanisms of Support to overseas SEZs



Source: Brautigam, 2011.

SEZs in Africa

The Program for China-Africa Cooperation in Economic and Social Development, launched during the third FOCAC Summit in 2006, was conceived as a means to share with Africa China's experience with investment promotion and FDI growth, with SEZs as major tools. Under the 2006 policy, the Chinese government identified SEZ projects in 19 countries – including seven in Africa.¹¹

For the establishment of the SEZs, the Chinese government offered subsidies of up to 200 million RMB (US\$ 33 million) for each zone, with the loan arrangements and equity investment provided by the China-Africa Development Fund (CADF), an equity capital instrument set up in 2007 by China Development Bank.

Although their objectives are primarily China-centered, the projects are claimed to benefit the host country. Chinese companies willing to “going out” would gain closer access to markets, resources and cheap labor in a relatively low-risk environment, thanks to the provision of infrastructure in the zones and preferential regulation. Meanwhile, African host countries would benefit from new waves of foreign investment, knowledge transfer and job creation. In other words, it was hoped that overseas SEZs would both facilitate investment by Chinese enterprises abroad, and transfer China's development experience to other countries.

11. Algeria, Egypt, Ethiopia, Mauritius, Nigeria (two), and Zambia.

These overseas SEZs have now been included in the “One Belt, One Road” strategy (OBOR). OBOR emphasizes the key role of “connectivity” and of infrastructure development in particular, but in addition to investing in transport, telecommunication and energy infrastructure, Beijing is also seeking through OBOR to export its model for industrial parks or zones. In this respect, there is no break of logic between the “going out” strategy and OBOR. The NDRC’s Action Plan on OBOR explicitly stresses: “we should explore a new mode of investment cooperation, working together to build all forms of industrial parks, such as overseas economic and trade cooperation zones and cross-border economic cooperation zones, and promote industrial cluster development” (Tang, 2015).

Although Kenya is officially nominated as China’s African hub for the OBOR initiative, the whole continent is meant to be part of the scheme. OBOR may indeed be a way of enhancing complementarity between China and Africa: on the one hand, there is China, a large per-capita-resource-scarce developing economy with an aging population, excessive savings and infrastructure overcapacity, and on the other hand is Africa, a large, resource-rich developing continent with a mostly young population and which in aggregate terms lacks both savings and infrastructure.

In a nutshell, the convergence of interests is quite clear between Ethiopia, which seeks to attract FDI in order to accelerate the development of its manufacturing capacities (in particular through SEZs), and China, which seeks to export its development model (including SEZs), to delocalize its most labor-intensive activities, and to promote connectivity between Asia and the African continent. The next section examines in detail how China became increasingly involved in Ethiopia and whether the converging interests of the two partners actually translate into mutually beneficial outcomes.

Chinese Investments in Ethiopia

Today, although the Ethiopian government is careful to say that all investors are welcome, the close political relationship between China and Ethiopia – both *de facto* one-party states that have pursued a heavily state-driven development model – has helped to cement China's role as a primary economic partner.

An overview

With a population of about 90 million and a relatively easy access to the sea through Djibouti, Ethiopia is an attractive production location for Chinese firms. According to China's MOFCOM, Ethiopia ranks today among the top destinations for Chinese ODI in Africa (behind Nigeria, and more or less on par with South Africa and Zambia).¹² This is all the more remarkable for two reasons. First, because Ethiopia lagged behind other African countries as an investment destination (it ranked at best number 10 in the mid-2000s) and second, given the absence of natural resources in Ethiopia.

Seen from Ethiopia's perspective, Chinese direct investments barely existed in 2000 but now surpass any other country, reflecting a sharp acceleration over the past few years. According to data provided by the Ethiopian Investment Commission (EIC), over the period 1992–2016, China is by far the first foreign direct investor in the country (even ahead of Turkey and India), be it in terms of number of projects (with 20.7 percent of the total), or of capital invested (17.9 percent). In terms of employment, however, China merely accounts for 14.6 percent of permanent employment and 14.8 of temporary employment, well behind Britain (with 28.6 and 33.2 percent respectively).¹³ According to UNCTAD data (2016),

12. By end 2014, Ethiopia ranked second (behind Nigeria, but ahead of South Africa) in terms of number of Chinese manufacturing projects approved. This ranking order is confirmed by other sources, such as Marukawa, Ito and Zhang (2014).

13. If projects involving multi-partner projects in which a Chinese firm participates are also added, the share of Chinese FDI rises to 24 percent in terms of number of projects, to 22.4 percent in terms of value and to 20 or 17.5 percent in terms of number of employees.

FDI flows from China to Ethiopia increased from just about a US\$ 1 million in 2003 to an annual amount of US\$ 122 million in 2012.

**Table 2: Top 5 foreign direct investors
(August 1992–October 2016)**

(Licensed FDI projects in operation, in percentage of total)

Value	Number of projects	Permanent employment	Temporary employment
China (21.6)	China (23.6)	Britain (28.6)	Britain (33.2)
Saudi Arabia (18.8)	India (9.0)	China (18.5)	China (17.0)
Turkey (8.3)	USA (7.0)	Saudi Arabia (6.9)	Saudi Arabia (9.3)
India (6.3)	Turkey (4.4)	Turkey (5.1)	India (7.2)
Britain/Netherlands (5.3)	Saudi Arabia (3.5)	India (4.8)	Turkey (2.9)
Memorandum items:			
Total value (in thousand birrs)	Total number of projects	Total permanent employment	Total temporary employment
93,541,582	2,547	287,664	306,641

Source: *Ethiopian Investment Commission*.

As of July 2016, there were more than one thousand Chinese projects registered by the EIC. According to the same data source, the bulk (more than 70 percent in terms of amounts invested) of Chinese ODI in Ethiopia is in manufacturing; “Construction”, and “Real estate, renting and business activities” come next (with respectively 22 and 5 percent). This should not come as a surprise: with its inexpensive¹⁴ yet relatively skilled labor force, coupled with the government’s proactive efforts to court foreign (in particular Chinese) investors, Ethiopia has been able to attract substantial investments in labor-intensive industries. A casual look at the list of Chinese firms investing in Ethiopia suggests that garment and shoe production loom large, although investment activities are well diversified.

14. The Ethiopian Investment Commission reports that the average wage of workers in the leather factories is US\$ 45 per month, while the minimum wage in Guangdong is about US\$ 300.

The breakdown differs, however, according to the nature of Chinese investors: while Chinese government-led ODI is heavily concentrated in mining and contracting activities, private-led investment tends to focus primarily on manufacturing and trade.

Over the last couple of years, Ethiopia has attracted 15 major Chinese investment projects in sectors such as textiles and electronics. Beyond abundant and cheap labor, the firms are no doubt attracted by improving infrastructure and by the healthy state of the Ethiopian economy. Moreover the country's attractiveness as a production location has certainly to do with its duty-free access to the U.S. market through the African Growth Opportunity Agreement (AGOA), to the EU market through the Everything But Arms (EBA) mechanism, and to the regional/African market since Ethiopia is one of the founding members of the Common Market for Eastern and Southern Africa (COMESA).

Most Chinese projects are medium-sized investments of US\$5 million to US\$ 20 million by private firms. Chinese investors are present in the existing government-led Industrial Parks, such as the Bole Lemi IP (Table 1), and some also plan to establish themselves in Hawassa IP. A final interesting feature of Chinese investment is the establishment of fully Chinese-controlled SEZs, which is examined in the next section.

Chinese-led Special Economic Zones

The privately-run Eastern Industrial Zone (EIZ), located 35 km south-east of Addis Ababa in the town of Dukem, Oromia Regional State, about 900 kilometers from the port of Djibouti, is one of the first six Chinese SEZs established in Africa under the FOCAC framework to date (UNDP, 2015).

In 2007 a Chinese consortium, the Jiangsu Yongyuan Investment Corporation, was selected by China's MOFCOM through a competitive tender process as the developer for the EIZ. This consortium originally consisted of two steel companies, Jiangsu Yonggang Group and Jiangsu Qiyuan Group from the city of Zhangjiagang in Jiangsu Province, the former was the major partner and the latter a minority partner.¹⁵ Due to financial difficulties caused by the global economic crisis, the Yonggang Group left the project in 2008, leaving the Qiyuan Group in charge of the zone's development and management (Bräutigam and Tang, 2011).

15. The Yonggang Group is among China's largest iron and steel producers with over 10,000 employees and an annual revenue of US\$ 4.5 billion in 2010. The Qiyuan Group is a steel pipe and aluminium producer with approximately 1,000 employees. The Group consists of twelve subsidiaries in China, two in the United States and five in Ethiopia. The Ethiopian subsidiaries are all invested in the EIZ (UNDP, 2015).

Interestingly, the Chinese government did not intervene to support any of the players at the time of the crisis. Today the EIZ is entirely owned and managed by the Qiyuan Group, a private Chinese investor.

In 2011, the EIZ was approved by MOFCOM as one of China's flagship SEZ projects overseas, which, subject to an official site inspection at the completion of the project, could entitle it to a significant amount of financial subsidies of up to 40 percent of its total investment. With the guarantees provided by two coastal municipalities, Suzhou and Zhangjiagang, the investor obtained a long-term loan of US\$ 36 million from the Exim Bank of China.

The EIZ is regarded by the Ethiopian government as a key component of the "sustainable development and poverty reduction program" (SDPRP) and listed as a priority project of Ethiopia's national industrial development (Eastern Industry Zone website). However, in contrast to common practice, where the host government is responsible for off-site infrastructure (in particular infrastructure leading to the SEZ), under the Memorandum of Understanding signed by the Ethiopian government and the Qiyuan Group, the latter has been asked to develop infrastructure, such as power transmission lines, water supply and waste water treatment to and from the EIZ with a 30 percent reimbursement of the costs by the Ethiopian government (UNDP, 2015).

The Administration and Management Committee of the Zone provides various services to the companies in the Zone, including consultation of investment policy and law, investment and work permits, business license registration, customs declarations, commodities inspection, product storage and transportation, exhibition, coordination with the local government, brokerage and security services etc.

In line with the most common preferential policies offered to investors in any given SEZ, the government of Ethiopia has set up a package of incentives whereby EIZ investors shall be exempted from: 1) import custom duties on capital goods, raw materials and spare parts (up to 15% of the value of the imported capital goods) only if they are not available in the local market; 2) export taxes; 3) income taxes within a period from two to seven years; and 4) taxes on remittance of capital.¹⁶

Although the EIZ has been off to a difficult start, probably due to the lack of experience of the developer, things seem to have settled and at the time of writing, there are more than 30 companies operating on the site,

16. El Rashidy (2016).

with approximately 15,000 workers.¹⁷ Except for one (Be Connected, a Dutch garment printing and labeling company), all companies are Chinese; they operate in a wide range of activities, spanning textiles and garments, food processing, metal works, electrical materials, automotive, steel pipes, cement and various services. The extension of the EIZ (2.6 additional square kilometers) is currently under construction.

A final point worth noting is that the location of the zone is far from ideal given its distance from the capital and its limited transport links to international transport routes (UNDP, 2015). The recent construction of the Addis-Djibouti railway line may to some extent improve the situation.

Table 3: List of Chinese companies operating in the Eastern Industry Zone

Cluster	Company	Type of Business	Year of establishment
Textiles and clothing (10)	Chang Cheng Packaging Co Ltd	Production of woven bags and packaging material	2010 (operation)
	Huajian Shoe Co Ltd	Leather shoes	2011 (operation)
	Dongfang Spinning, Printing and Dyeing	Textiles and garments	2013 (operation)
	Linde Clothing	Manufacturing of garments	2014 (operation)
	KEPA Textile Plc	Weaving, finishing and printing of textiles	2014 (operation)
	Yuechen Textiles	Manufacturing of woven fabrics	2015 (operation)
	Haibo Manufacturing Plc	Manufacturing of children's clothes and adult suits	2016 (operation)
	Kaipu Manufacturing Plc	Production of school bags, travelling bags	2016 (implementation)
	Shuaije Textile Plc	Textile products	2016 (pre-implementation)
	Wuzhen Miao Textile	Textile products	2016 (pre-implementation)

17. Interview with the Zone management in October 2016. The initial plan, however, was to bring in around 80 projects that would generate 20,000 job opportunities.

Metal works (3)	Eastern Steel Co	Manufacturing of basic iron and steel	2006 (operation; expansion 2014 and 2016)
	LQY Pipe Manufacturing Co. Ltd	Steel pipe production	2010 (operation)
	Zhen Zhen Iron & Steel Manufacturing Plc	Manufacturing of basic iron and steel	2015 (operation)
Construction Material (7)	East Cement	Cement production	2006 (operation)
	L&J Engineering Co. Ltd	Production of bricks, pipes and cement products	2010 (operation)
	Yulong Technology Building Materials Co. Ltd	Production of gypsum boards and related products	2010 (operation)
	Zhong Shun Cement Manufacturing Co. Ltd	Cement production	2008 (operation)
	Hansom Kinfengda Manufacturing Plc	Manufacturing of electrical wires or cables	2015 (operation)
	TY Wood Manufacturing Plc	Manufacturing of plywood boards, timer doors, floors and furniture	2016 (implementation)
	Di Yuan Ceramics	Ceramic products	2016 (pre-implementation)
Machinery (8)	Yangfan/Lifan motors	Motor vehicle manufacturing and assembling	2013 (operation)
	Shadeka Spare Parts Manufacturing Plc	Manufacturing of spare parts and accessories for motor vehicles	2013 (operation)
	Changfa Agricultural Equipment Manufacturing	Tractors, harvesters and other agricultural equipment	2011 (operation)
	Yuechen Industry Plc	Manufacturing of special purpose agriculture machinery	2014 (implementation)
	Yema Auto	Pick-up assembling	2011 (operation)
	E-truck Motors Manufacturing Plc	Heavy vehicles	2016 (pre-implementation)

	Higer Pickup	Pick-up production	2011 (operation)
	Ejia Metal Products Manufacturing PLC	Manufacturing of screws, nuts and other metal products	2014 (operation)
Miscellaneous manufacturing (3)	Aisai Recycled Plastic Manufacturing	Manufacturing of plastics and/or synthetic rubber	2013 (operation)
	Hul Huang Industrial Plc	Manufacturing of plastic products excluding plastic shopping bags	2013 (operation)
	Jili Electric Plc	Home appliance manufacturing	2016 (pre-implementation)
Packing (2)	Great Wall Packing Material	Packing materials production	2011
	Pure Wood Pulp Paper and Packing Plc	Production of pulp, paper and packaging materials	2017 (pre-implementation)
Services (3)	East Cement Leasing Company	Construction equipment rental service	2008 (operation)
	East Cement Share Company	Administrative services, personnel management, sales, billing, etc.	2006 (operation)
	Eastern Hotel	Hotel services	2008 (operation)

Source: Author's own compilation.

Chinese investors are also present in privately-run SEZs that are not part of the MOFCOM strategy. Capitalizing on its experience in the EIZ¹⁸, the Huajian Group has recently chosen to further develop in Ethiopia by establishing its own SEZ, the so-called “Huajian International Light Industry City” in Lebu, on the outskirts of Addis Ababa. The zone, which is projected to require a US\$ 2 billion investment and yield a US\$ 4 billion return over 10 years, aims to eventually employ 100,000 workers and provide housing, hospitals and schooling on site. Other producers of footwear, handbags and accessories will be allowed into the zone. The declared, very ambitious objective of the project is to turn Ethiopia into a global hub for the shoe industry, supplying the African, European and

18. The Huajian Group it has set up two production lines in the EIZ, with a production capacity of 2,000 pairs per day, exporting to the US and the EU markets.

American markets. The initial funding for the zone came from the Huajian Group, and interested investors include the CADF and the World Bank's IFC. The groundbreaking ceremony for the project took place on 16 April 2015, but at the time of writing the zone is still in its very early stages, with only four factory buildings operational.

Chinese investment in infrastructure

In Ethiopia, as in the rest of Africa, Chinese firms are also extremely active in all kinds of infrastructure development thanks to Chinese funds. Estimates show that China has outpaced the World Bank as the leading funder of Africa's infrastructure (OECD, 2011), and Chinese firms are also often building the infrastructure projects (roads, railways, telecommunications, etc.). In Ethiopia, at least, these investments cannot be taken as FDI as such, since they are basically carried out by or on behalf of the Ethiopian government. However, given that most of these projects would not have been realized without Chinese financing and engagement, they may be referred to as quasi-FDI.

Although some of these projects may be real game changers for Ethiopia's development, they are also favorable to Chinese interests. Projects backed by concessional loans must be executed by Chinese contractors, which are often selected through a non-competitive negotiation process, and a significant share of the goods and services embodied in a project must usually be sourced in China (Dollar, 2016).

Chinese companies are particularly active as developers of industrial zones. The IPDC of Ethiopia has awarded construction of several new industrial parks for the textile and garment industry to Chinese firms: CGCOC will construct the Bole Lemi II industrial park (US\$ 155 million), an extension of the Bole Lemi I; China Communication Construction Company (CCCC) will build the Jimma industrial park (US\$ 66 million); CTCE (a subsidiary of China Railway) has been tasked to build Kilinto IP (US\$ 240 million); and China Civil Engineering Construction Corporation (CCECC) concluded a US\$ 246 million deal for the construction of the Hawassa Industrial Park.

Similarly, Chinese companies have dominated the Ethiopian scene in the construction of roads and railway lines. Dozens of Chinese firms are currently engaged in the construction of roads throughout the country, carrying out nearly 70 percent of the road works in the country with funding by Chinese banks (Shinn, 2014). Similarly, the Addis Ababa light rail system and the 753 km Djibouti – Addis Ababa railway line were

funded by the Exim Bank of China and built by the China Railway Engineering Corporation (CREC).

Lastly, Chinese companies are playing an increasingly significant role in the development of the power sector in Ethiopia, primarily with the construction of hydroelectric power plants, but also of wind farms and biomass plants (IEA, 2016). As the latest FOCAC in 2015 in Johannesburg emphasized greater co-operation in energy and natural resources, further Chinese involvement may be expected in this sector in the coming years.

Table 4: A selection of Chinese-funded and contracted infrastructure projects

	Chinese contractor	Chinese lender	Loan amount (US\$ million)	Total cost (US\$ million)
Addis Ababa Light Railway	China Railway Engineering Corporation (CREC)	Exim Bank of China	403	475
Addis – Djibouti Railway line	China Railway Group, China Civil Engineering Construction Corporation (CCECC)	Exim Bank of China, China Development Bank, Industrial and Commercial Bank of China	2,400	3,400
Addis Ababa – Adama Expressway	China Communications Construction Company (CCCC)	Exim Bank of China	800	1,400
Bole International airport expansion	CCCC	Exim Bank of China	225	340
Tekeze Dam	China Gezhouba Group Corporation (CGGC), Sinohydro Company Ltd	Exim Bank of China	50 (initially)	365
Finchaa-Amerti-Neshe (FAN) hydro-electric power dam	CGGC	Exim Bank of China	119	140
Geba hydroelectric power project	CGGC, Sinohydro Company Ltd	Exim Bank of China	466	583
Genale Dewa III hydroelectric power project	CGGC	Exim Bank of China	326	408
Gibe III Hydropower project	Dongfang Electric Corp (as sub-contractor for electro-mechanical work) in collaboration with Italian Salini Impregilo)	ICBC	470	1,580

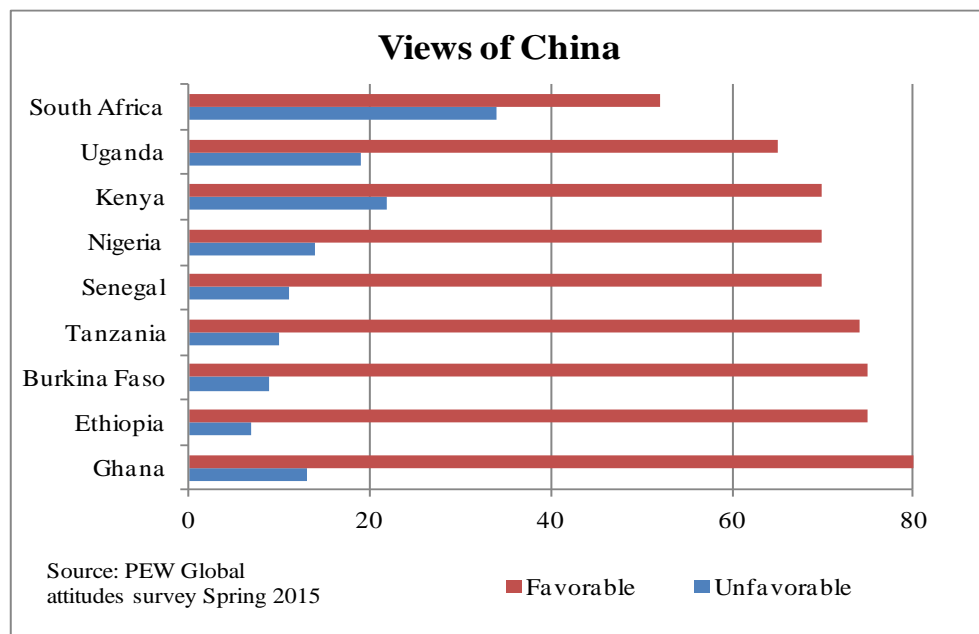
Source: author's compilation.

Assessing the Impacts of Chinese Investments

Ambivalent perceptions

Interestingly, perceptions of Chinese presence tend to be more positive in Africa than in most other regions. In the Pew Global Attitudes survey for 2015, African respondents had a significantly more positive view of China (on average 70 percent with a favorable view) than respondents in other regions such as Europe (41 percent), Asia (57 percent), or Latin America (57 percent). Ethiopians have a particularly favorable opinion of China (75 percent of them)¹⁹ with a very low percentage (7 percent) having a negative view (Figure 2).

Figure 2: Views of China



Source: PEW Global attitudes Survey Spring 2015.

19. Only Ghana is ahead of Ethiopia with 80 per cent of favorable opinions.

This favorable vision may be due to the perceived positive impact of Chinese investment on economic growth in African countries. But this is not unanimously shared; some dissenting voices, illustrated in press articles in particular, point to the exploitation of the country's resources by Chinese companies, to neo-colonialism, etc.

Overall, in Ethiopia, as explained earlier, the government's stance tends to be very positive vis-à-vis China while public opinion, in contrast, complains for instance about the quality of Chinese infrastructure²⁰ and of Chinese products, but also about the excessive number of Chinese present in the country, about the limited opportunities for local unskilled labor and the lack of technological transfer. Moreover, Chinese firms are also accused of using their connection with top government officials to crowd out domestic firms.

The most serious issue, however, certainly has to do with the accusations of poorly compensated land-expropriations. An oft-heard argument is that the recent socio-political unrest that led to the imposition of the state of emergency in the fall of 2016 is the result of the excessively fast expansion of industrial zones at the expense of the local population.

Economic impacts: win-win, really?

Chinese investment in Ethiopia does not match the standard view of Chinese FDI in Africa looking for natural resources and plundering the country. Far to the contrary it is concentrated in infrastructure and in the manufacturing sector. The hope was that China's growing outbound investment ambitions could be as transformative for today's poor African countries as inbound investment was for China in the late 1980s. But is it really the case?

Static gains: investment and employment

The establishment of the EIZ has undoubtedly helped put Ethiopia on the radar screen of Chinese companies and FDI inflows have been on the rise ever since. The gap between overall figures and FDI inflows attracted in the zone is substantial, indicating that the creation of the EIZ was not the only reason for the surge, although it certainly contributed.

In this respect, the case of the Chinese shoe producer, Huajian, is particularly telling. As explained earlier, Huajian started producing in the

20. The rapidly degraded ring-road in Addis Ababa is one such example. But complaints are also quite frequent about the poor quality of the AA light railway operation.

EIZ in Ethiopia in 2012, and then decided to expand its production by creating its own industrial zone in 2015. Although still in its early phase of development, the Huajian International Light Industry City started operating in 2016.

Another positive impact is through employment creation. In spite of frequent allegations about Chinese companies bringing their own labor force, in Ethiopia, Chinese firms tend to employ local workers, except in management positions. According to a World Bank survey (2012), 87 percent of the permanent workforce in Chinese firms in Ethiopia was local.

Dynamic gains: linkages and spillovers

Proponents of SEZs usually argue that these schemes will benefit the local economy because of business linkages between foreign and local companies. Foreign investors may purchase materials and services from the local economy, invest in infrastructure built by local companies and bring new technology into the zones that will be transferred to the rest of the economy. But linkages between foreign firms and local firms are not easy to come by, while spillovers do not happen automatically and may need to be encouraged through specific policy interventions.

Prospects for the SEZs to build backward linkages within the local economy are usually rather weak both because the raw materials and intermediates needed in assembly-type operations may not be available locally, and because of the known propensity of Chinese companies to source inputs through their own networks. Moreover, local firms may also lack the capacity or “absorptive capacity” to adopt any spillover that does take place. At the same time, forward linkages, which usually involve the provision of diverse ancillary services to the zones, may be constrained by deficient infrastructure and logistics and lack of competition in the host economy.

In Ethiopia, backward linkages are usually thought to be important in light manufacturing (T&G and leather garment industries, for instance). The reason for such an optimistic stance is that, in contrast to what may be observed in many LDCs such as Cambodia, for instance²¹, Ethiopia also grows cotton and has a spinning, weaving, and knitting history, making local sourcing possible. Moreover Ethiopia’s industrial policy has focused

21. In Cambodia, foreign investors in the textile and garment industry openly admit that they have only a rare connection with the local economy. This may be easily explained by the way the industry is organized and by the absence of a domestic textile industry.

on incentivizing exports and developing domestic value chain linkages between cotton, textile, and apparel firms (Staritz *et al.*, 2016). As a result, Ethiopia is not only integrated in the global value chains at the downstream end through cut, make, trim (CMT) activities.

Similarly, in the leather garment sector, the potential for backward linkages is substantial because of the existence of associated industries. With one of the largest untapped livestock resources in the world and an ancient tanning industry able to turn cattle, sheep and goat hides into a variety of leather, there is no denying that the country should be an attractive place to make shoes using local inputs.

A casual look at the list of Chinese companies already operating in the EIZ suggests that the chance for the emergence of major backward linkages is rather weak, since companies in the machinery or construction equipment industries tend to be dominant. A World Bank survey (2012) showed that in 2011, 61 percent of the total material inputs and supplies used by Chinese firms in the EIZ were sourced abroad.

Nevertheless, the recent rise in the number of T&G producers is encouraging. Five new Chinese T&G producers have entered the zone and should start operation very soon (see Table 3). With 10 companies belonging to the sector, clustering effects may be achieved, thus strengthening the chances for deeper backward linkages. The impact of Chinese producers will, however, remain limited because of their relatively small number, compared to Turkish investors for instance. Chinese firms are also much more small-scale and diverse compared to other Asian investors. Thirteen Chinese firms²² account for 5 percent of total employment in the sector, compared to only 6 Indian firms accounting for 8 percent (Staritz *et al.*, 2016).

In the leather garment industry, some backward linkages may also be expected. Chinese leather garment manufacturers such as Huajian are indeed reported to use local raw materials such as skins and hides as inputs for their production. The establishment of Huajian International Light Industry City, the objective of which is to serve as an Ethiopian supply chain cluster should help the development of more substantial backward linkages, provided local producers are allowed into the zone and can benefit from clustering effects.

22. Six in textile, five in apparel, and two are integrated.

The snag is that local inputs are not always up to the standards expected by the producers.²³ As a result, foreign final producers were induced in the past to invest in upstream activities, posing a risk of crowding out local suppliers. The risk is all the more important since local authorities did not seem to be very concerned with the protection of local supply industries, as reported by Braütigam *et al.* (2011) and Chaponnière (forthcoming). It remains to be seen whether they will adjust their policy.

Another potential channel for dynamic gains is through transfers of technology, or of know-how. According to a World Bank survey (2012) 69 percent of surveyed Chinese firms provide formal training programs in Ethiopia. Further anecdotal evidence confirms this point: Huajian has been reported to provide vocational training to its employees, including training of local technicians in China (for 3 to 12 month periods – Zeng, 2015). Skill transfers may also simply occur through labor mobility, but they remain limited if the workers are concentrated in low-skill jobs.

A number of other factors may also limit the potential spillovers. In particular, the fact that local investors are not allowed in the Chinese-led SEZs is one such inhibiting factor, since local SMEs for instance cannot take advantage of working in partnerships with the larger firms in the zones. Moreover, joint ventures, which could facilitate such transfers, are not frequent. As is often the case, the tendency is for SEZs to work as enclaves; and yet the Chinese domestic experiences show how important it is to synchronize the zones and the local economy, including local suppliers (and even local universities). One of the fundamental goals of FDI is to boost local competitiveness through active interaction with advanced foreign businesses (Kim, 2013). Absent such interaction, the host country cannot benefit as much.

The limited transformative power of Chinese investments

The much hoped for contribution of China-led SEZs to the structural transformation of the Ethiopian economy is also limited at this stage. In particular, the diversification of Ethiopia's manufactured exports is mixed at best.

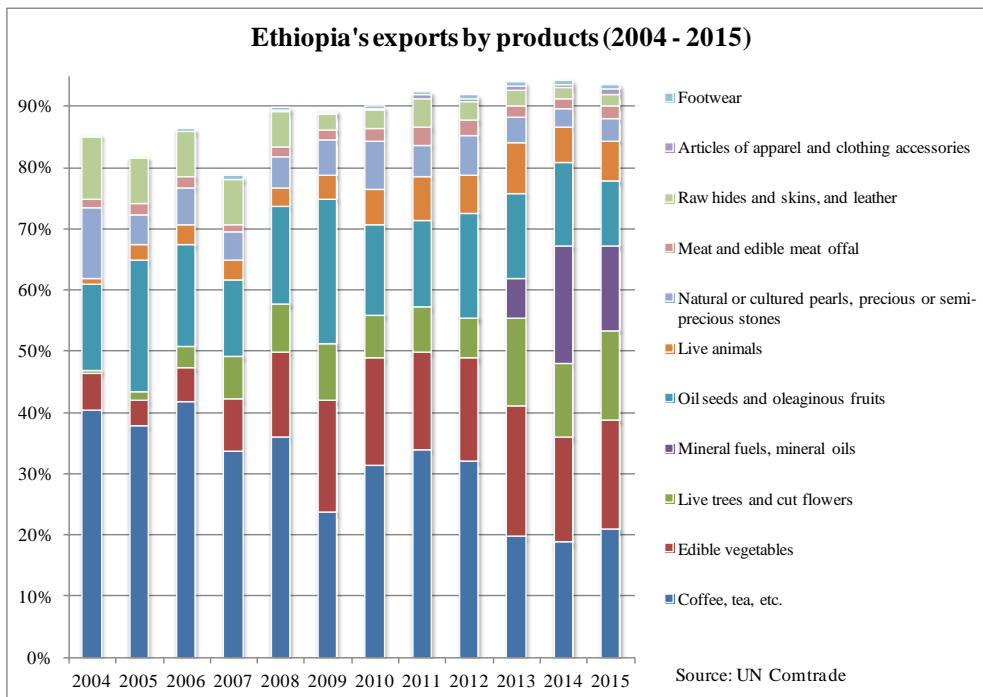
Thanks to the presence of Chinese and other foreign investors actively engaged in the apparel and garment, and footwear industries, Ethiopia is seeking to make a name for itself in the world of mass-produced footwear

23. As recalled by Oqubay (2015), "comparative advantage in natural endowments does not automatically lead to sustained competitive advantage".

and garments. Under AGOA, leather shoes export from Ethiopia has reportedly exploded. However, turning Ethiopia into an international shoe and light manufacturing hub remains elusive so far. Ethiopia has failed to reach the targeted 15-fold increase in textile and leather exports to US\$ 1.5 billion in the first GTP Plan that ended in 2015. One explanation lies in the role of the domestic market, which is still important not only for domestic firms but also for foreign-owned firms – even though the government aims at pushing the latter group solely into exporting (Staritz et al. 2016).

The rise in shoe production is anecdotal and garment and footwear exports still account for a minor share (less than 1 percent) of the country’s total exports. The major changes in Ethiopia’s export pattern (rise in the share of cut flowers and fuel minerals in particular) are not due to SEZ-related activities by Chinese investors. Overall, Ethiopia’s export pattern remains dominated by agricultural products (coffee/tea, vegetables and live trees and cut flowers), although their respective shares have substantially changed.

Figure 3: Ethiopia’s exports by products (2004-2015)



Source: UN Comtrade.

This does not mean, of course, that China has not played a useful role in Ethiopia by setting up industrial zones, financing infrastructure, and encouraging Chinese firms to move some manufacturing production to Africa (Dollar, 2016). The zones have no doubt contributed to the industrialization process but this has not been translated into trade figures yet and the connections with the rest of the economy remain weak.

Rather than manufacturing investments, Chinese investments in infrastructure may have proven to be more instrumental in transforming the country. The construction of new dams, for instance, has been instrumental in guaranteeing stable power supply and making a reality out of Ethiopia's plan of making electricity one of the country's greatest exports into reality. Similarly, the construction of a new railway line connecting Addis Ababa to Djibouti, officially inaugurated in Djibouti on 10 January 2017, may turn out to be a game changer: the new 750 km railway line will turn a week-long drive through a winding pot-hole filled road into a smooth 12-hour ride to the coast, facilitating the transport of goods to and from the Port of Djibouti and cutting costs accordingly.

Shortcomings of Ethiopia's SEZ strategy

The two-pronged approach to SEZs followed so far by the Ethiopian authorities, with government-led IPs coexisting with private foreign-led SEZs, is probably a good approach since there are more FDI firms wanting to invest or expand in industrial zones in Ethiopia than the government can offer.

But it is important to make sure that the zones' activities are aligned with the country's needs in terms of industrial development. And this is less likely to be the case if the state is not actively involved. In the case of the foreign-owned private zones, the government simply allocates zones to foreign investors who promise to mobilize a large number of investors from their home country, facilitating in particular their renting of land. But the government does not have much of a say about the choice of investing firms and their sectoral orientation. In the case of the EIZ, for instance, the Chinese developer sought to help the development of the country through the provision of construction materials and capital goods for the fast-growing local construction industry, but it did not pay any attention to the development of the light manufacturing industry which was (and still is) one of Ethiopia's priorities. In this regard, the EIZ cannot really be compared to SEZs in China (or even in other East Asian countries).

One exception in the EIZ is the Chinese shoe producer, Huajian. Interestingly, the investment by this specific company was made at the invitation of then PM Zenawi, who went personally to Dongguan in August 2011 to invite the Chinese shoe manufacturer to invest in Ethiopia. Reciprocating the visit, Huajian's CEO, Zhang Huarong, came to Addis Ababa a couple of months later, and opened a shoe factory in the EIZ in January 2012. Having a first experience in the EIZ proved particularly useful, allowing Huajian to test Ethiopia as an investment location. The further expansion of its activities, through the establishment of its International Light Industry City, although it is a fully-private Chinese project, is also perfectly in line with the government's industrial policy.

The recently launched government-led IPs, in contrast, should be seen as real instruments of industrial policy, with the government choosing to favor some sectors of activity rather than others, in line with its own objectives.

But neither SEZs nor IPs should be used as a substitute for other policy actions. The government should build on its strategic FDI attraction policies, focusing on carefully targeting lead firms and manufacturers willing to invest in higher value added activities and build linkages to local input providers. Moreover, the government should also put more efforts on improving the overall business environment, including infrastructure, and consider "smart incentives" that encourage skills training, technology transfer/upgrading and local economic linkages (Zeng, 2015).

Conclusion: Prospects and implications

Cordial relations have developed between China and Ethiopia over the past two decades, and the convergence of interests and of ideological visions between the two countries has led to various forms of cooperation, with surging Chinese FDI flows in manufacturing and in infrastructure supported financially by the Chinese government. And yet Chinese contribution to the transformation of Ethiopia's economy remains limited so far. To be sure, there is scope for further expansion of Chinese FDI and for more substantial positive spillovers, but for that to happen some conditions must be met.

Although Chinese investment was hoped to contribute to the country's industrialization, there is no discernible sign yet. Ethiopia has registered high growth rates but little transformation. For the time being, the winners are all on the same (Chinese) side: Chinese investors are seizing the opportunity in Ethiopia to move some of their manufacturing offshore from China to lower-cost production sites. But the SEZs, which were expected to play the same transformative role as SEZs in China's southern provinces (or in other East Asian countries, such as Korea or Malaysia) seem to have failed. This can be easily explained: the fully Chinese-controlled economic zones (such as the EIZ) reflect a very different logic where the priority is given to the interests of foreign investors rather than to those of the host country.

However, various recent developments suggest that the situation may be changing soon. First, while the strategy followed so far by Ethiopia had given priority to Chinese-owned SEZs, it has shifted recently in favor of government-led IPs, the logic of which is much closer to that of SEZs promoted in East Asia. Moreover, newly developed projects, such as the Huajian International Light Industry City, are also promising, as the sectoral orientation of the project is in line with the country's industrial objectives. As these developments are still recent, the jury is still out on the reality of backward linkages and the ability of Ethiopian firms to take advantage of the presence of Chinese firms and technology, and hence on the potentially substantial benefits. The prospects look rather good, provided other accompanying measures are put in place so as to improve

the overall business environment, and, probably more importantly, to enhance the local labor force's "absorptive capacity".

But this is unlikely to be smooth sailing. Recently, the government has been faced with violent protests on the part of local communities complaining in particular about ill-compensated land expropriation and population relocation due to the further expansion of industrial zones. In this context it is all the more important for Ethiopian authorities to be able to show the benefits the country can derive from the presence of foreign, and in particular Chinese, investors in SEZs and/or in IPs.

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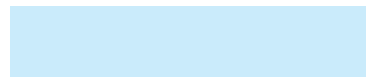
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