AFRICA RETURNING EAST

Can the China Development Model Travel To Africa?

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16 September 2005

A minor dissertation submitted in partial fulfilment of the requirements for the award of the Degree of Master in Social Sciences (International Relations)

Declaration

This work has not been previously submitted in whole, or in part, for the award of any degree. It is my own work. Each significant contribution to, and quotation in, this dissertation from the work, or works, of other people has been attributed, and has been cited and referenced.

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Abstract

Africa is returning to the strategic agenda of both old and new powers. A number of new opportunities and alarming missteps will be possible in the coming decades. Since the fall of the Berlin Wall, the neo-liberal agenda has been unchallenged allowing little flexibility for developing countries to alter their macro-economic policies and closely coupled development agenda. However, the successes of economies to the east of Africa are providing an alternative to following the prescriptions and rules set by the 'Western' economies. Because of these geopolitical changes and Africa's continued socio-economic problems, the policies of China and the surrounding economies are gaining attention. Africa is no longer completely reliant on trade and aid from the predominant powers and the rise of the Indian Ocean and Asian economies is loosening the grip and associated consequences of following (or not following) predetermined economic policies. These changes in the international order lead to the central purpose of this thesis, which is to explore the influence of China's development model in Africa.

This thesis will argue that African governments are beginning to challenge the 'Washington Consensus' by shifting towards a model based on China's development gains. However, the political economy of African countries does not support a complete adoption of China's socialist, state-centric model. The null would suggest African governments are committed to a 'Washington Consensus' defined development model, however the evidence suggest the contrary.

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Introduction

"The transfer of power from West to East is gathering pace and soon will dramatically change the context for dealing with international challenges – as well as the challenges themselves."[1]
James F. Hodge, Editor, *Foreign Affairs*

The Geo-Economics of the Indian Ocean

To Africa's east, the ascent of Indian Ocean and subsequent Asian economies is perhaps the most significant geopolitical event of the 21st century.[2] These nations have developed into legitimate economic engines soon capable of rivalling the western nations of North America and Europe. While many of these developing countries are still facing the vast problems of unemployment and poverty, they are experiencing unforeseen growth levels and are quickly developing geopolitical ambitions. The two striking stories of these eastern economies are China and India, for they have both managed prolonged gross domestic product (GDP) growth and are now deeply affecting the global marketplace.

China's gradual emergence as a global power is no longer an undercurrent unnoticed by the masses. The debate about China's future and its global agenda has quickly reached inexplicable levels with varying and uncertain discourse among scholars and political leaders. Business professionals are mainly indifferent to the political implications, for they are seeing enormous potential profits from a strikingly populated country (1.3 Billion or 20% of the world's population!). Media and other international observers are producing a litany of shocking statistics about China's potential. Here are a few, choice selections:

- As the South Africa Institute for International Affairs calculated, "if the Chinese were to reach the American level of car ownership and oil consumption, it would require 80 million barrels of oil per day. Current global production is a little more than 64 million barrels."[3]
- Or *The Economist*'s startling observation , "If China's real income grows by 8% a year and its income distribution remains unchanged, by 2020 the top 100m households will have an average income equivalent to the current average in western Europe."[4]

The story of India's accession has attracted less attention but is none-the-less important to global standing. Stephen Roach noted within his weekly column, "Up until now, it's been a China-centric journey – some 25 trips since 1997. But I have long suspected that there's far more to Asia's remarkable story. India convinced me that my instincts were right."[5] Where China has grown through low-end manufacturing, India has aggressively provided professional services for multinationals found mainly in the United States and Europe. The product 'value-chain' is no longer domestically based and has been strewn globally. Information technology services is

[1] Hodge, 2004
[2] Africa is defined as Sub-Sahara or Southern Africa.
[3] South Africa Institute for International Affairs, 2005
[4] *The Economist*, 30 Sept 2004
[5] Roach, 14 February 2004

where India initially focused but they are now performing a number of back-office processes for companies who had previously never considered the risky notion of moving operations to a developing country. Through this strategy, India has been able to side-step its woeful infrastructure problems while taking advantage of its highly educated and English speaking population. The future is always uncertain, but many respected analysts have noted that if India sustains its current economic growth rate for the next 50 years, it will rival or pass China.[6]

'The Halo Effect'[7]

Evaluating China and India does not draw the complete picture of the geo-political landscape, especially when specifically measuring China's emergence globally. The once isolated nation is now largely propelling the global economy. As the *New York Times* Columnist Thomas Friedman recently exclaimed, "If you're the leader of Japan, America, Australia, Taiwan, Malaysia, Russia, Thailand, Indonesia, Singapore, the Philippines or the European Union and you're not going to bed each night saying the following prayer for China, then you're not paying attention."[8] Over the last twenty years, China has averaged nearly 8% GDP growth per annum and is now the 6th largest economy (based on market exchange rates). China's economy is also unusually open to trade and investment. In 2004, total exports and imports of goods and services was nearly 75% of China's GDP.[9] This is especially daunting when reviewing other large economies; the United States and Japan were less than 30%. In terms of trade, China's total worldwide share in 1979 was less than 1%, it now accounts for nearly 6%. This huge expansion has paid enormous dividends for the world's economy during the recent recession. From 2001-2003, China accounted for nearly 1/4th of the world's growth.[10]

Not surprisingly, China's economic successes are casting wealth across the entire region. An explosion of trade between the countries bordering the Indian Ocean and Asia has been gaining momentum for some time. Total exports from Asia into China grew from $72 Billion in 1995 to $161 Billion in 2002.[11] Japan has been slowly edging out of a decade long recession and the 'Asian Tigers' have rallied from the 1997 financial crisis. Even Australia is benefiting through increased demand for exports and China's quest for resources. China's success is a global affair, but with a greater concentration of benefits for the Indian Ocean and Asian economies.

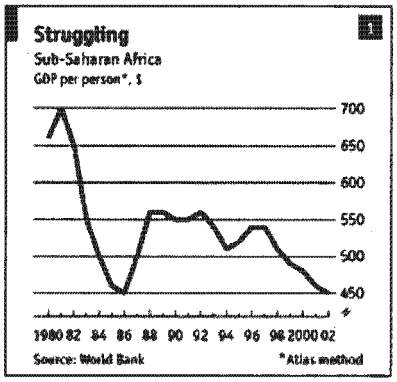
[6] Roach, 4 February 2004
[7] *The Economist*, 30 September
[8] Friedman T., NY Times, 2 April 2005
[9] IMF, 2004, 232
[10] Hale D. and Hale L., 2003, 47
[11] Ibid, 51

From West to East – A New Scramble?

How do these new geo-economic trends affect Africa's development?[12] Africa's troubles are no secret. Brief periods of hope have been trailed by despair and crippling conflict. The socio-economic statistics are startling: 45% of the continent's population lives below the poverty line and according to the World Bank, only 15% of Africans today live in "an environment considered minimally adequate for sustainable growth and development."[13] Where globalisation has spurred an increase in world trade levels, Africa's share has actually been shrinking for the last 25 years. Africa accounts for less than 2% of the world's GDP. Beyond altruism, the paltry domestic markets provide little incentive for the international community to get involved. Due to population increases and the sheer number of impoverished, economic growth rates in excess of 7% are now necessary to reach the United Nations millennium development goals. In simplistic economic terms, Africa neither provides the supply nor offers much demand. Thus, the wealth gap between Africa and the international community has expanded (see Figure 1).

While this unpromising story is often told, some hope does exist, especially in Sub-Saharan Africa. Except for Zimbabwe (albeit a broad exception), stability is allowing for new optimism and finally providing some economic tools necessary for governments to review their domestic political and economic situations. South Africa's continued political success is driving economic growth for the entire Southern region and signs of real per capita GDP progress are present. Southern Africa has been relatively conflict-free with nearly all of the countries showing positive growth rates for the last few years. Average incomes in Mozambique have nearly doubled in the last decade and both Uganda and Rwanda had GDP growth rates over 6% last year.[14] Even the recent awarding of the 2010 FIFA World Cup to South Africa should be interpreted as a sign of confidence for this embattled part of the world.

Figure 1: Africa GDP Per Capita



Much of this optimism can be related to China; Africa is rich in natural resources and China's emergence has amplified their demand. Commodity prices have been on a blistering course for nearly 4 years and this has provided badly needed capital and investment across Africa. Oil is the obvious target and Africa is producing 3.4 million barrels a day extracted from fields in

[12] The term 'development' is rife with rivaling definitions and associated ideologies. The paper defines it broadly as economic growth coupled with distributed wealth across a society, or equitable growth. For a overview of definitions see, John Baylis and Steve Smith, *The Globalization of World Politics* 2nd Edition (New York: Oxford University Press, 2001) p. 562-564
[13] *The Economist*, 11 May 2000
[14] *The Economist*, 14 August 2003

Nigeria, Angola, Equatorial Guinea and Gabon. This production could double in the next five years and more, untapped sources are expected to be discovered.[15] China is not alone in pursuing oil in Africa. India, the United States, and the European Union have all increased their business interests and diplomatic squabbling between the powers has heightened in the last few years. Beyond oil, Africa has extensive reserves of copper, coal, gold and numerous other raw materials that are highly desired by advance economies.

However, not all of this is good news for Africa. China's realist policies of currency manipulation and cheap labour have deeply cut into Africa' manufacturing industry. Due to China's extraordinarily cheap labour, African countries are struggling with their export-led growth strategies. This is more damaging to the poor, for low-skilled positions common in low-cost manufacturing are simply being filled within China and neighbouring economies. Increased trade through commodities is providing benefits but the breadth of African economies could be diminished. What occurs when a down-cycle in commodity prices is not counter balanced with growth in industries like manufacturing and agriculture?

Returning East – History of Indian Ocean Trade

Finally, Africa realigning with the eastern economies is not unknown in history...a precedent unquestionably exists. Africa's first trading partners did not arrive from the western shores of Africa but from the Indian Ocean. Africa has a strong history of trade with the Indian Ocean cultures and communities. Asian and Arab traders were first to the African shores. Artefacts from Great Zimbabwe and modern Mozambique show an extensive trade network beginning around 700 AD, with this being the dominant trade of southern Africa until the arrival of the Europeans in the 16th century. De Gama's passage around the Cape of Good Hope introduced Europe to the Indies spice industry and trade levels soon turned West for the last 400 years. As the Indian Ocean and European trade routes expanded. "India led to China. When Europeans entered the Indian Ocean, they found a flourishing network of trade linking Asia from east to west. from China, Japan, and the Philippines to the caravan

The Mozambique 'Dhow' sail boat design is often mistakenly thought to be borrowed from the Portuguese, but is of Arab descent having dating much earlier than the arrival of Portuguese explorers

[15] Hale, 2005, 8

stations and ports of the Levant and East Africa."[16] Trade levels have since remained skewed towards North American and Europe, but they have been quickly shifting east for the last five years.

As Thomas Pakenham wrote in *The Scramble for Africa* about the visions of the European explorers, "There were dreams of El Dorado, of diamond mines and goldfields criss-crossing the Sahara...There might be new markets out there in this African Garden of Eden, and tropical groves where the golden fruit could be plucked by willing brown hands."[17] The destructive idealism of development forays into Africa is well known, but perhaps the re-emergence of rival trading partners and Africans managing their own development will bring about a renewed renaissance.

Research Question and Methods

Africa is returning to the strategic agenda of both old and new powers. A number of new opportunities and alarming missteps will be possible in the coming decades. Since the fall of the Berlin Wall, the neo-liberal agenda has been unchallenged, allowing little flexibility for developing countries altering their macro-economic policies and closely coupled development agenda. However, the successes of economies to the east of Africa are providing an alternative to following the prescriptions and rules set by the 'Western' economies. Because of these geopolitical changes and Africa's continued socio-economic problems, the policies of China and the surrounding economies are gaining attention. Africa is no longer completely reliant on trade and aid from the predominant powers and the rise of the Indian Ocean and Asian economies is loosening the grip and associated consequences of following (or not following) predetermined economic policies. These changes in the international order lead to the central purpose of this thesis, which is to explore the influence of China's development model in Africa.

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This is an acknowledged vast topic rife with tendencies to drift off course, therefore boundaries are followed and detailed topics are often unfortunately ignored. In general, this is a broad assessment of development models using macro measures of the highest level. Finally, the

[16] Landes, 1998, 155
[17] Pakenham, 1991, xxii

wide-ranging nature of the research topic will prevent definitive answers but instead provide an illustration of a shift in thinking and policies.

Chapter 1 argues the current development paradigm is ultimately doomed due to constraints imposed by the mercantilist global structure. States will always trump the common global good in favour of domestic concems. Chapter 2 reviews China's development model and explores contrast with ideas applied through 'Washington Consensus' policies. Chapter 3 is a case study of South Africa.

Empirical data obtained from leading researchers and institutions will be utilised throughout this review. Primary research through analysis of political speeches and documents produced by governments, international financial institutions (IFIs) and non-governmental organisations (NGOs) will also be heavily drawn upon.

Chapter 1 Development in Africa – A 'Washington Consensus'?

"We have learned once and for all that there are no magical elixirs to bring a happy ending to our quest for growth. Prosperity happens when all the players in the development game have the right incentives"
William Easterly, *Economists' Adventures and Misadventures in the Tropics*[18]

Globalisation and Africa

Not surprisingly, African scholars are quick to dismiss the current globalisation thinking and dispel many of the common myths associated with Africa's role in the modern day. The notion that Africa has never been an integral participant in the globalised community is especially frustrating to African leaders, partly because it is detrimental to attracting investment, but mainly because of its blatant falsity. As noted, international trade on the African continent dates back centuries with well-known established routes to both Mediterranean and Far East regions. Portuguese trading was formalized along the western coasts of sub-Sahara Africa during the 15th century and during the Chinese Ming dynasty, trade prospered in eastern Africa as early as the late 14th Century.[19]

While the debate about globalisation will carry on, international integration is unquestionably happening at a resolute pace. The shifts in power and influence are placing undue stress on the global arena and constantly introducing new players and dynamics to the world's political economy. Understanding these entities and discerning the rules which best explains how these actors try to enrich themselves is a central concern, especially when considering development issues. This chapter will present a literature review of the predominant economic development model, the 'Washington Consensus', since 1989. It will argue these policies fall short due to numerous issues, but a mercantilist global system and the inability of policy makers to adjust for the political economy of nations are the primary causes. A survey of the growing global inequality problem will provide evidence of these shortcomings. As this review is being written in South Africa, attention will be placed on Sub-Saharan Africa and its specific development concerns.

The Global System

Applying a theoretical model which best explains how the multitude of non-state and state participants interact is imperative for further analysis. Specifically, is power being diffused through the state system, the wealthy pro-market classes, or the many organisations acting above the state?

Robert Gilpin's three models provide a framework for answering this question. His ideas track closely to the predominant paradigms within the political economy approach; Mercantilism, Liberalism, and Marxism. The Gilpin-named models: Mercantilism, Sovereignty at Bay, and

[18] Easterly, 2002, 15
[19] Fage and William, 1995, 48

Dependencia, all offer compelling explanations for the current global system but, as expected, they possess weaknesses. Gilpin elaborates further, "Perhaps no one individual would subscribe in full to the arguments made by any one position. Yet, the tendencies and assumptions associated with each perception of the future are real enough."[20]

Beginning with the latter model, Dependencia. It is the most criticised and probably least convincing explanation for the contemporary system. However, this does not mean it lacks significance. All three models address the growing wealth gap between both domestic and international economies, but Dependencia helps to explain the inequality of the international order. Informal coalitions of elite states, as well as domestic upper classes, are devising systems, which further enrich themselves while providing limited spoils to the lower ranks. Dependencia perceives these inequalities through a more malevolent lens than the two other models and specifically cites the multi-national corporation (MNC) as the spear of such movements.[21] Dependencia's prevalent fault is not explaining the global improvement in overall living standards and the non-zero-sum games of international trade gained through liberal policies.

When comparing the Mercantilism and the Sovereignty at Bay models, the argument is not as clear. Sovereignty at Bay is embraced by most because of its unparalleled ability to generate wealth. The emergence of powerful non-state actors and the abundance of free-roaming international capital all fall within the liberal framework. Further, the MNC's loyalty to the State is diminishing as they expand internationally and diversify their profits throughout many regions. "Through trade, monetary relations, and foreign investment, the destinies of societies have become inextricably interwoven,"[22] Gilpin explains.

Of the three models, Mercantilism is the sole addresser of an important element, the nation-state. Proponents note that the prosperity of cross-national organisations could potentially be halted if economic growth was not an assurance. The global digression into protectionist policies between the Great Wars is the commonly mentioned example. However, the cross-state squabbling which Mercantilism suggests as the framework for the global system is difficult to accept. Further, the observation of a MNC's global production structure illustrates the complexity of modern organisations. Despite these important arguments, Mercantilism remains prevalent for one reason: states still maintain the power to stop the process. Most modern nations have embraced

[20] Gilpin, 1975, 216
[21] Ibid, 228
[22] Ibid, 235

liberal reforms because they view it as the best means for which to enrich their populations; however, security or domestic political concerns can quickly cause barriers to be built.

Mercantilism's effect on the global structure is particularly detrimental when considering the role of developing countries. As this chapter will discuss, enormous resources and human energies have been devoted to supporting the poor of Africa and the rest of the developing world. However, powerful states and their associated institutions will ultimately choose to protect domestic interests rather than support those in need beyond its borders. Pareto offers a definition for this group, "the governing class is not a homogenous body…Ruling classes, like other social groups, perform both logical and non-logical actions…we must not think of them as actors in a melodrama who administer and rule the world…They hold no meetings where they congregate to plot common designs, nor have they any devices for reaching a common accord."[23] The elites, or powerful States in this case, are merely a heterogeneous group of governing members seeking to preserve the system which provides wealth for themselves and their communities. This does not imply a lack of altruism nor are profits always first priority, the goal is to simply maintain status quo. The 'boogie-man' approach so often used to define these states overextends political economy theory, for no central body makes decisions with the sole mandate to protect everyone's interests…the international system is far too complex. Thus, despite extensive effort, capital, and rhetoric, development policies set by powerful nations will always serve the self-interests of those in power. This premise does not suggest 'good' is not achieved through international aid or trade, simply that when interests are not aligned between powerful states and developing countries, the former has no incentive to compromise.[24] Speaking to the recent Asian-African summit, South African Minister Dlamini Zuma exclaims, "We must also be able to mobilise resources among ourselves and not rely on donor country aid. If our destinies are in our hands our resources cannot be in the hands of others, we must find the resources to advance progress and develop ourselves."[25] In essence, Africa has to lead itself out of this difficult situation and China – and the surrounding economies – is providing a considerable role model of how to counter the global mercantilist system.

The Emergence of Development Theory - Origins and Noble Goals

Debates and concerns about the wealth and poverty of nations is a recurring and aged theme in international relations. While most political historians cite the forming of the Bretton Woods Institutions in 1944 as the beginning of the development debate, scholars and political leaders

[23] Zuckerman, 1977, 334
[24] For an interesting review of how African and the larger powers interests might align, see David Hale. *How Marginal is Africa?* Hale suggests that the fear of collapsed states supporting terrorism might help lift Africa higher in the international agenda.
[25] Zuma D., 2005

have been deliberating this for ages. The early questions were more self-interested in scope, for writings were generally not concerned with rich countries helping poor ones but how do societies generate enough economic activity to enrich themselves.

A litany of issues are part of this subject but the role of the state is the predominant variable. The field of political economy is where much of this debate has occurred. Adam Smith's, *The Wealth of Nations*, provides an early perspective.

> Political economy considered as a branch of the science of a statesman or legislator proposes two distinct objects, first, to supply a plentiful revenue or subsistence for the people, or more properly to enable them to provide such a revenue or subsistence for themselves; and secondly, to supply the state or commonwealth with a revenue sufficient for the public service. It proposes to enrich both the people and the sovereign.

Smith's definition has since been applied to the modern study of economics, but he captures the central theme of political economy, the discourse between the market and state. Robert Gilpin provides more updated thinking into the subject, but his ideas have not drifted far from Smith's early writings.

> Therefore, I used the term "political economy" simply to indicate a set of questions to be examined by means of an eclectic mixture of analytic methods and theoretical perspectives. These questions are generated by the interaction of the state and the market as the embodiment of politics and economics in the modern world.[26]

During Adam Smith's time, early mercantilists emphasized the necessity of the state as a means to control the industrial output of a nation. The vast majority of the European economies were growing their industrial production and also increasing cross-border trade. However, the states role was not lacking. Smith originally suggested the term mercantilism as a means to describe the protective importing and exporting policies of 16th and 17th century Europe. Constant trade tariffs were used to protect local industries while new markets were pursued for exports. Due to the growing entrenchment of states; competition, conflict and military intervention became a problem. States were therefore required to maintain large standing armies to defend against rivals and extensive tax levies were necessary to support this security.[27] Consequently, the merchants, or those controlling much of the industry and associated tax revenues, gained greater influence within the state leadership structure. Ironically, a system identified with state intervention was named after the entrepreneurs and business leaders who now loathe many of these ideals. While the *Wealth of Nations* brought the criticism of mercantilism to the forefront by emphasising the positive sum game of trade, a new laissez faire ideology was sweeping across both Europe and the United States. The Enlightenment period and associated political ideas of democracy were movements that turned the tide against the economic involvement of

[26] Gilpin, 1987, 8
[27] LaHaye, 2004

governments directing markets and mercantilist policies in general. As Thomas Paine, the British-born tradesmen turned American revolutionary wrote, "Society in every state is a blessing, but government, even in its best state, is but a necessary evil."[28] Ironically, in the same year as Paine's *Common Cents* publication (1776), Adam Smith's *Wealth of Nations* provided the economic framework to implement these ideas throughout the economy. His emphasis on competition and individualistic ideals struck an accord with these early political architects.

Following World War II and the ending of the colonial era, economists began writing seriously about the failures and possible remedies for developing economies. This is the beginning of modern development thought and the first time serious consideration was placed on Least Developed Countries (LDC). The key assumptions of these new scholars and policy makers was two-fold; one, developing countries were different economically, and two, they needed alternate policy prescriptions to generate macro-economic activity.[29] Models and lessons applied from industrialized economies were not adequate to explain the failings of less-developed economies. As one would expect from economists, high-level metrics such as gross national product (GNP) and per capita values of wealth were frequently utilised. Max Singer, Arthur Lewis and other now famed noble laureates contributed to these early development theories. Surplus labour, inadequate education systems and poor infrastructure were all cited as reasons why developing countries were caught in a paradox: capital shortages without enough market activity to generate the necessary capital. Therefore, it was argued that a strong interventionist State guiding investment with a substantial commitment from the international community would be necessary to generate macro-economic growth. Acceptance of international intervention and recommending policy to foreign populations was not without critics. Returning to Robert Gilpin, "Their optimistic belief that every economy had an interest in the development of all, set development economists apart from dependency theorists, economic nationalists, and Marxists, all of who regarded the interests of undeveloped and those of developed economies as antiethical."[30]

Development thought morphed in the 1960's and early 1970's toward a more holistic approach. Sociologists, political scientists and other more diverse fields joined the fray and broader analysis was provided. The United Nation's (UN) Human Development Index and other non-monetary measures were introduced. The 'human-side' was finally told. "Poverty is not just low GDP; it is dying babies, starving children, and oppression of women and the downtrodden."[31] The original assumption that development economics was unique for poorer countries was also challenged. Neoclassical economists argued that economic principles were universal and states should

[28] Paine, 17
[29] Gilpin, 2001, 307
[30] Ibid, 309
[31] Easterly, 2002, 113

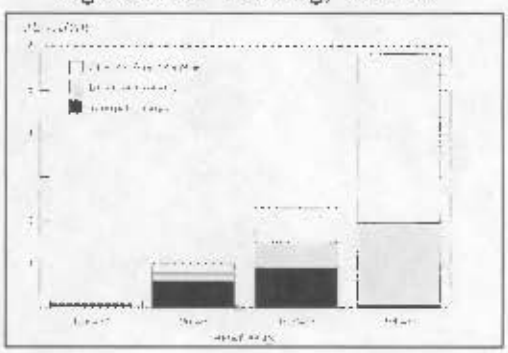
simply remove themselves from the market, or 'get the prices right'. Markets were again en vogue. States were expected to provide macro-economic stability but not hinder business growth with inefficient bureaucratic processes.

The remnants of a strong development state were distinguished in the late 1970's and 1980's in the form of international debt defaults. Foreign governments in Latin America, the Middle East and Africa increased borrowing as early as 1970 and by 1983 Less Developed Countries (LDC) had borrowed over $600 Billion – $350 Billion from foreign private banks.[32] The oil price fluctuations during the 1970's provided wealth to oil-rich countries and foreign banks were eager to lend newly acquired petrodollars to willing developing countries who were suffering through the difficult economic period of the 1970's. Foreign banks did not properly measure the risk nor did developing countries recognize the dangers of being highly leveraged. From the International Monetary Fund's (IMF) historical review of this period,

> Many developing countries that borrowed heavily from commercial lenders in the 1970s came to the Fund after 1982 when commercial financing suddenly dried up in the wake of the international debt crisis. More broadly, the poorer countries that lacked access to private capital markets increasingly turned to the Fund as well as to other multilateral agencies for help in the 1970s and even more so in the 1980s.[33]

A dip in worldwide commodity prices led by oil put greater financial pressure on developing countries and a debt crisis quickly ensued. As Figure 2 demonstrates, the IMF fulfilled the demand of sovereign lending after private banks had grown weary. The move of developing countries borrowing from private lenders to the IMF (and World Bank) had enormous implications. This allowed the IMF to seek longer-term solutions and begin structural reforms in return for bailout funds. Consequently, shortly before this period, industrialised countries no longer needed to borrow money from the IMF and focus shifted toward solely supporting developing countries. The commitment to structural adjustments and macro-economic reforms is what led John Williamson to coin the term 'Washington Consensus' in his now famed (or notorious) 1989 essay.

Figure 3: IMF Lending, 1950–89



Specifically to Africa

Since the emergence of modern development thought and the independence movements (or end of colonialism), Africa has been unable to find solid footing. As the colonial states began their

[32] Frieden, 1983, 8
[33] Broughton, 2001, 47

transitions, most of the world was openly confident due to the United State's post-war economic growth, the continued success of Western Europe's rebuilding plans and the promise of new Chinese and Russian economic systems. Prospering market capitalism, coupled with democratic independent African states, was expected to bring 'first' world living standards to the much neglected African continent.[34]

Unfortunately, this untold optimism quickly unravelled as the African states progressed throughout the 1970's. The Nigerian director of the United Nations Economic Commission for Africa is cited, "How have we come to this sorry state of affairs in the post-independence years which seemed at the beginning to have held so much promise?"[35] Various governance missteps caused economies to collapse throughout the continent. As mentioned, International Finance Institutions began expanding beyond the Northern Atlantic, thus providing new capital for development opportunities. However, African countries quickly assumed $200 billion in unmanageable foreign debt, much of it attributed to military spending. Further stumbles followed. As a means to quell unemployment, countries began to employ large parts of the population within government organizations. By 1980, the non-agriculture public-sector accounted for 50-55% of all jobs, as compared with 36% for Asia and 27% for Latin America.[36] This does not mention the duress caused by conflict or authoritarian regimes.

Until this point, it also is important to note that countries had a choice of political ideologies that carried closely linked development policies. Communist Russia and China were more than willing to provide aid and support to governments wishing not to follow the lead of the United States led development regime. Phillip Short elaborated in his recent book about Pol Pot and Cambodia, "the Cambodians embraced Marxism not for theoretical insights, but to learn how to get rid of the French and to transform a feudal society which colonialism had left largely intact."[37] African nations generally followed the ideology of the previous colonial powers, but this corrupted the development process. Prior to 1989, "African Rulers became accustomed to negotiating their political support of the former colonial power (or indeed other Western or Eastern governments) in exchange for foreign aide."[38] In Cold War times, loans were often not repaid and strong evidence suggests funding was rarely spent toward originally intended projects.[39]

The fall of the Berlin Wall now symbolizes the pinnacle of achievement for the liberal ideology, for no other global economic alternative was seen feasible. This change from a bipolar to single

[34] Young, 1994, 12
[35] Ibid, 4
[36] Ibid, 6
[37] Vosmer, NY Times, 27 February 2005
[38] Chabal P and Daloz JP, 1999, 12
[39] Ibid, 112-116

power world transferred enormous influence to the International Finance Institutions. Military and security concerns were now secondary to economic. Today, nearly all governments follow some recipe of the 'Washington Consensus'; opening the economy to foreign investment, removing exchange controls, deregulating the economy and other structural adjustment programs. Countries which do not choose this 'golden straitjacket' (e.g. Venezuela, Cuba, Zimbabwe) are punished harshly by the international marketplace and are usually marginalised from a development perspective.[40]

However, broad implementation of these policies should not be interpreted as a lack of debate. As John Gray emphasises, "The free market created a new type of economy in which prices for all goods, including labour, changed without regard to their effects on society."[41] The global improvement in overall living standards and the non-zero-sum games of international trade gained through liberal policies are broadly accepted. However, capitalism has a fickle liability towards policy and duration...the rising tide tends to be slow and only under certain conditions. This discourse begs for a more detailed analysis of the 'Washington Consensus' policies and the many criticisms which follow it.

Motherhood and Apple Pie, The 'Washington Consensus'

The term 'Washington Consensus' was innocently created by John Williamson 15 years ago as a broad description of the ten economic policy prescriptions the American government was encouraging in Latin America. Since then, the terminology has transformed into a pseudo-ideology, which is often interpreted as the International Finance Institutions exploitation of the developing world. A Google search returns over 3 million hits and one would have to search hard to find something positive. However, beyond this clamour, the ideas suggested by Williamson are not as radical as the casual observer might suspect. The original ten ideas suggested are the promotion of trade and foreign direct investment, fewer subsidies, fiscal discipline, tax reform, liberalised financial systems, competitive exchange rates, privatization, deregulation and the securing of property rights. None of these solutions are so perverse as to deserve the enormous condemnation over the last decade. Williamson defended these ideas in a 2002 speech to the Institute for International Economics, "For the most part they are motherhood and apple pie, which is why they commanded a consensus."[42]

Despite attempts to slow the usage of the term, the 'Washington Consensus' has grown into something much broader. It now represents the dismay and frustration with the IMF and World Bank at providing economic relief for the developing world. Perhaps it is not quite an ideology but

[40] Friedman T, 1999, 112
[41] Gray, 1999, 1
[42] Williamson, 2002

more a representation of the neo-liberal regime, which has failed to disperse global wealth equally. This argument does not lack merit either, because startling policy inconsistencies between developed and developing countries are apparent. Reviewing in detail all the facets of this debate is beyond the scope of this paper, but the prevalent issues should be addressed. John Williamson provides a parsimonious method to summarize his original observations. His thoughts provide the nexus of the development debate and each of the three areas mentioned are discussed below.

> The three big ideas here are *macroeconomic discipline*, *a market economy*, and *openness to the world* (at least in respect of trade and FDI). These are ideas that had long been regarded as orthodox so far as OECD countries are concerned, but there used to be a sort of global apartheid which claimed that developing countries came from a different universe which enabled them to benefit from (a) inflation (so as to reap the inflation tax and boost investment); (b) a leading role for the state in initiating industrialization; and (c) import substitution. The Washington Consensus said that this era of apartheid was over.[43]

Macroeconomic discipline, a market economy, and openness to the world are the three principles of the development debate and most policies can be placed in one of these three silos. At the highest level, these ideas are relatively accepted, but contention begins with the details. Other discourse is found when policy makers ignore or misjudge a countries political economy and apply changes in a manner that jeopardizes stability. Therefore, good policy is only relative to the situation. This approach simply provides a model of analysis when reviewing a country's development tactics; it is not a policy suggestion.

Macroeconomic Discipline

This realm within the development debate is secure. Creating an argument for large deficits and/or high inflation rates is futile, mainly because it is counter to both business and economic logic. However, when International Finance Institutions (IFIs) are working with potential borrowers, high inflation rates and large deficits are usually status quo. Therefore, this debate is about application, not necessarily the fundamentals of the policy.

Raising taxes or cutting programs are the general means for reducing fiscal deficits. Unfortunately, both require tough decisions and generally hurt the poor. Either of these options also alters the political economy of a country and lenders certainly deserve criticism for ignoring these affects. The counter to these concerns is a country's macro-economic situation must be stabilised before growth returns. While the reduction in services to the poor or increased taxation

[43] Ibid

might affect the domestic situation, everyone benefits from a growing economy. A short-term drop in economic performance and service to citizens is expected, but the long run benefits are unquestionable. Timing and selecting budget changes (while harming the least amount of people) is therefore the crux of the matter. The struggle is some nations are so fragile politically that even a short-term dip in economic performance is enough to create turmoil.

Raising interest rates as a means to control inflation and properly measure the risk of a country is of some concern. In order to attract investors, interest rates should reflect a country's risk and reward those willing to extend capital. However, higher rates affect the ability of many people, especially those in the lower income bracket, from accessing capital. Entrepreneurs and other small businesses suffer due to the increased costs and this helps push some into the informal markets. However, again, a stable macroeconomic environment is more beneficial to small businesses in the end.

A Market Economy

Within the discourse surrounding development policies, privatisation seems to strike 'hearts and minds' more profoundly. In many ways, privatisation, or creating a market driven economy by reducing the states role in providing services, has reached an accord. The fall of communist Russia showed the dangers of a command economy, but the exact mix of governments and markets is the focal point of the issue. Therefore, the need for governments to provide services and safety nets for its citizens is not questioned, but how far should government reach into a nation's economy to find that equilibrium?

The economics behind reducing a State's assets are sound. Usually, the private sector manages capital more efficiently, serves customers better and provides a cheaper product. All citizens benefit from the reduced costs and these savings are spent in other areas of the economy, which further creates growth. The unfortunate truth of this logic is markets are not efficient, certainly not in an equitable sense. Telecommunication companies do not build telephone lines for the rural poor because capital flows where profits can be returned (or perceived to be profitable). The incentives to build water and electricity access to shantytowns are not as strong as for new suburban neighbourhoods. Hence, state managed assets do often provide a re-distribution role.

Selling assets often does not create the desired efficiency either. Competition is essential and bureaucrats mistakenly assume other players will emerge as challengers. "Government monopolies sold to the private sector simply become private monopolies, with no real increase in

efficiency", as described by the economist Nicoli Nattrass.[44] Private monopolies can effectively eliminate competition, even in the private sector.

The loss of economic potential of state-run enterprises can be significant though. William Easterly cites an example, "African state telephone companies have cut new telecommunications investment so much that customers wait an average of more than eight years for new telephone service, yet revenue per line in Africa is exceptionally high by world standards."[45] Thus, states, especially those in the developing world lacking infrastructure, are caught in a contradiction of policies...how do you support the poor while unlocking the wealth and efficiency of a State's asset?

Most governments have accepted the logic of privatising for some parts of the economy, but the timing and implementation of these practices has been highly contentious. If a state chooses or is encouraged by International Finance Institutions to privatise, the process can cause dramatic shocks to an economy lacking institutions, sound governance procedures and adequate social services. The political effects of retraining retrenched workers cannot be ignored and adequate support for the unemployed are rarely in place. The opportunity for corruption is also immeasurable. The problems that ensued after the Soviet Union quickly sold off state assets is still not fully understood and Africa has faced similar struggles. Returning to Easterly, "Nigeria...sold government equity shares in upstream oil ventures for $2.5 Billion – during a period in which $12 Billion in oil revenues disappeared from the official accounts, possibly into the pockets of Nigerian government officials."[46]

The implementation of privatisation can present economic benefits but is ridden with risks for both industrialised and developing countries. Joseph Stiglitz[47], the now famed critic of the 'Washington Consensus', noted the contradictions of privatisation policy while he was working in the Clinton White House, "while we did not believe in market fundamentalism, the view that markets by themselves would solve the economy's (and society's) problems, we pushed market fundamentalism on the rest of the world, both directly and through the IMF."[48] The pendulum of the development debate continues to swing between more and less state involvement but a consistent approach is far from accepted. Fifteen years ago this debate ended in favour of the pro-markets United States based model, but the thinking has since shifted, especially in light of

[44] Nattrass, 2000, 284
[45] Easterly, 2002, 113
[46] Ibid, 115
[47] Joseph Stiglitz was Chairman of Council for Economic Advisors during U.S. President Clinton's first term and subsequently served as Chief Economist for the World Bank for three years.
[48] Stiglitz, 2003, 228

China's success with a stronger state. Governments are growing more willing to accept the loss of some revenue in return for a more equitable society.

Openness to the World

This is an enormously broad realm, but the central question is how a nation manages both foreign trade and capital. The economic losses for countries that chose to shun outside industry are well known therefore nearly all are engaged in the global system. The many institutions and non-state actors that manage international trade and investment are beyond this evaluation, but participation is required if a country wishes to wholly compete in the global economy. Therefore, membership is required to play, but managing foreign trade and capital is rife with risk and is certainly not an egalitarian game.

Few economists would dispute the merit of cross-border trade and the positive sum gain achieved between both trading partners. Understandably, lowering subsidies and opening markets on a global scale has been a central theme of development policy since the ending of World War II. However, despite the idealism of the policy, there is nothing free or fair about trade. Drawing from Africa's experience, the continent faces alarming protectionism from more powerful mercantilist competitors. As an example from recent agro-trade negotiations, it is estimated that cotton subsidies from China, the United States and Europe cost the African economy $1 Billion annually. Cotton produced in the United States exceeds Africa's costs by 50%, yet each acre of American cotton is subsidized with $230.[59] An endless number of similar examples can be cited, but this argument has done little to progress WTO negotiations, despite renewed alliances among some southern hemisphere countries. Other variables (e.g. commodity price fluctuations, floating currencies, protectionist policies) can be cited as important challenges to African trade, but the damaging nature of foreign agriculture subsidies and other protectionist policies is unquestionable.

The most dramatic economic changes over the last decade are due to financial and capital market liberalisation, or generally stated, the management of outside capital.[60] Through the unyielding implementation of technology, financial networks have established themselves on a truly planetary scale. This is certainly the most 'global' aspect of globalisation. "Of the many changes in the world economy in recent decades, few have been nearly so dramatic as the resurrection of global finance...like a phoenix risen from the ashes, global finance took flight and

[59] *The Economist*, 24 July 2004
[60] To John Williamson's defense, he never intended for capital account liberalisation to be included in the 'Washington Consensus' because their was no consensus at the time of publication. However, this topic is unavoidable when discussing the economies of the Indian Ocean and Asia. These economies have unquestionably taken a counter position to the policies of the United States and Europe.

soared to new heights of power and influence in the affairs of nations", as Benjamin Cohen so passionately claimed.[51] However, the adverse impacts of this explosive growth have been paramount, especially when considering the currency collapses and quick fleeing foreign investment from developing countries. Thomas Friedman called these individuals and organisations the 'short-horn' cattle within the throng of global investors. This group includes multitudes of anonymous personas: hedge fund traders, equity managers and the millions of amateur and professional sovereign analysts who try to predict the potential of a nation's economy. The unfortunate nature of this international group is best described by the International Monetary Fund (IMF) as 'herding' or 'momentum trading'. Essentially, investors are caught making judgements based on limited information while simultaneously fearing a fellow competitor has more relative access. Thus, when a respected investor makes a tactical allocation or divesture, it can create an inaccurate stammering. While analysts dryly outline the ill effects of this type of capital movement, it can have devastating impacts on a nation's economy. The shortcomings of this system were harshly exposed during the now infamous East Asian financial crisis.[52] After Malaysia's shocked economy settled, the Prime Minister, Dr. Mahathir Mohamad renounced this group while addressing the World Bank in 1997 as "morons" operating within "a jungle of ferocious beasts."[53]

The East Asian crisis was obviously detrimental to many economies in the short-run but two valuable lessons were learned. First, foreign capital is beneficial but can stampede quickly if not monitored closely and adequate reserves are not maintained. Prior to this, a debate about controlling foreign capital was unsettled and the awareness that a crisis could occur was largely ignored. However, the crisis 'tipped' the indecisive and now most of the effected economies maintain some form of capital controls and reserves have been bolstered. Second, and closely related to the first, below market currency's are preferred to strong ones. While some countries have reversed the trend of fixing their currency to the dollar, most purchase large amounts of US treasuries in order to deflate their exchange rate.[54] From Stephen Roach, Chief Economist of Morgan Stanley, "Asia has led the way in that regard — with hard currency pegs in China, Hong Kong, and Malaysia and soft currency pegs in Japan, Korea, India, Taiwan, Thailand, and Indonesia. Asia's official foreign exchange reserves surged to $2.2 trillion by mid-2004 — more than double the holdings of early 2000. *Asia now maintains 80% of US accounts.*"[55] These

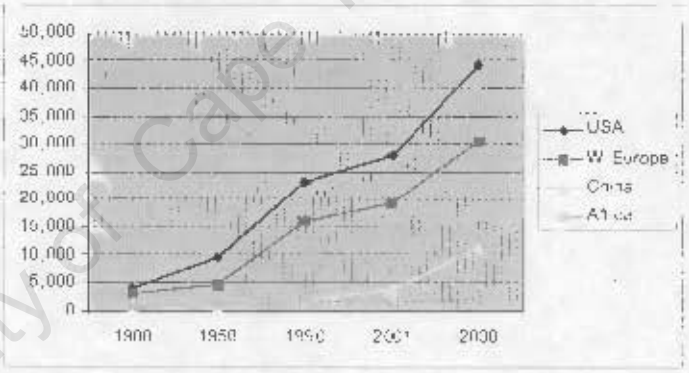
[51] Quoted by Rodrik, 1997, 24
[52] 'Herding' and over-zealous markets were not the complete cause of the Asian Financial crisis. Bad policy and broader structural problems were the drivers. See Nouriel Roubini, 'What Caused the Asian Currency and Financial Crisis Part 1: A Macroeconomic Overview', http://www.stern.nyu.edu/globalmacro/ for a conclusive summary
[53] Friedman, 1999, 112
[54] Power, 2005
[55] Roach, 29 November 2004

events were especially important to China, for it reinforced their commitment to existing policies due to avoiding much of the downward cycle.

Beyond altruism – the successes and failures

Despite global anxiety and pessimism, the improvements of living standards worldwide have been dramatic for the last century (using broad macro measurements). The countries in Western Europe and North America have seen the greatest acceleration, but improvements in living standards are consistent across all geographies. From *The Economist*, "The truth about market liberalisation and economic growth is not that it increases inequality, nor that it hurts the poor: just the opposite. Rather, the truth is that some large parts of the poor world are pulling themselves out of poverty while others are not."[56] However, as Figure 4 demonstrates, the gap between the regions of the world is striking. Where Africa's GDP per capita over the last century has grown almost three-fold, the United States has grown eleven times. *The Economist's* point is the increased growth in China and India has outpaced the United States and Europe, and because these huge populations (nearly two-fifth of humanity!) are experiencing growth, the economic gap is actually shrinking. This might be so, but the wealth disparity in other areas of the world is alarmingly wide. Angus Maddison, a famed scholar known for long-term economic performance assessments, asserts:

Figure 4: GDP Growth per Capita 1900 - 2030



> There are much wider income gaps today than at any other time in the past. Two thousand years ago the average level for Groups A and B was similar.[57] In the year 1000 the average for Group A was lower as a result of the economic collapse after the fall of the Roman Empire. By 1820, Group A had forged ahead to a level about twice that in the rest of the world. In 1998 the gap was almost 7:1. Between the Western Offshoots and Africa (the richest and poorest regions) it is 19 to one.[58]

Even the most optimistic evaluator would have difficulty not accepting systemic problems are apparent. Explanations for the causes for this phenomenon vary anywhere from weather to

[56] *The Economist*, 11 May 2004
[57] Maddison defines Group A as Western Europe, the Western offshoots (United States, Canada, Australia and New Zealand) and Japan
[58] Maddison, 2001, 27

racism.[59] However, a country's policy selections do matter and can greatly enrich or harm a society.

Applying a one hundred year view also does not provide a precise analysis of the 'Washington Consensus' policies either. The United Nation's (UN) Human Development Report published in 2002 reviewed international living conditions and measured 'human progress' for the last ten years. The findings were disappointing. Despite an international renewed commitment to democracy and liberal economic policies, many metrics have actually declined. Only twenty-four countries created the 3.7% annum GDP thought necessary to halve poverty by 2015 while 127 countries, with 34% of the world's population, were below this level.[60] As expected, Sub-Sahara Africa is the worse with 23 of 44 countries failing in most of the measured categories. Poverty is also increasing, "20 countries in Sub-Saharan Africa, with more than half of the region's people, are poorer now than in 1990– and 23 are poorer than in 1975."[61]

The industry surrounding these frustrating statistics is enormous and showing no signs of waning. Governments, development agencies, non-governmental organisations (NGO), other civil society groups, and even multinational corporations are attempting to contribute. Development assistance comes in many forms; official sovereign foreign aid, debt forgiveness, donations from civil society, and providing human resources, just to highlight a few. According to the Organisation for Economic Cooperation and Development (OECD), official development assistance (ODA) was $69 Billion in 2003 alone, an increase of 7% from the previous year. In 2000, there were more than 37,000 International NGO's registered, a 20% increase from 1990.[62] Additionally there are tens of thousands of foreign experts providing assistance in developing countries. Altruism does not guarantee efficiency though. One study found that it takes $3521 in foreign aid to raise one person's income by $3.65 a year.[63]

No Magical Elixirs

What is certain among this dialogue is very little is new, for history demonstrates the longevity of this discourse. Political leaders, academics, and policy advisors have not lost their courage though billions have been lost from experiments gone wrong. The only certainty is some nations have found ways to improve the lives of its citizens, but the right recipe is unique to every situation. Even in Africa, despite an unfavourable global system, success has been found for

[59] This is an exhausted topic crossing all academic disciplines. For interesting long-term views, see David Landes, *The Wealth and Poverty of Nations* (London: Little, Brown and Company, 1998) or Jared Diamond *Guns, Germs and Steel: The Fates of Human Societies*, (New York: W.W. Gordon and Company, 1999)
[60] UN Human Development Report Overview, 2002, 6
[61] Ibid, 8
[62] Final ODA Data, 2003
[63] Easterly, 2002

short periods. Policy, political structures, and the overall political economy of a country unquestionably affects the wealth of its citizens and China is showing that alternate methods can work.

These new campground facilities were built near the Tsodilo Hills, Botswana. However, the local community was not convinced of tourism benefits, for they saw these solutions as a means to water their cattle and donkeys. Good intentions do not justify bad policy.

Chapter 2 China's Development Answer

(The Ruler) is not concerned lest his people should be poor,
But only lest what they have should be ill-apportioned
He is not concerned lest they should be few,
But only lest they should be discontented.
And indeed, if all is well-apportioned, there will be no poverty; if they are not divided against one another, there will be no lack of men, and if there is contentment there will be no upheavals.
Confucius[64]

Grand Experiments

"The changes that have propelled China to a leading role in the global economy have no direct Antecedents."[65] China's importance in the international community is undisputed, but as David Hale illustrates, analysts fall short when seeking other parallels in history. In search for meaning, an array of writings has sought to understand China's phenomenal run, but the discourse is unrelenting. This chapter will seek to clarify the development progression since 1978, which led to China's current standing and demonstrate how it differs from the 'Washington Consensus'. It will argue that China has emerged through a unique blend of market dynamics morphed within a mercantilist structure. Development success was accomplished by harnessing China's political economy and these comparative advantages will be broadly discussed. Finally, China's increased interests in Africa and consequential growth in influence must be understood in order to address the overall research question of this paper.

The Chinese are proud of their history and it is an illustrious 5000-year account of powerful empires and noble achievements. Much of the world has borrowed extensively from China's long list of technology, political and academic achievements for centuries. If some of China's innovations had assimilated faster, the world's landscape would be vastly different. Yet, China's success always seems to teeter on unpredictable and grand experiments. Some of these experiments have brought great riches while others unbelievable misfortune. The current experiment is producing unforeseen affluence, but the certainty of its course is far from decided.

China's history of Indian Ocean trade provides a considerable example. China began extensive naval explorations dating to the early 1400's and completed seven journeys before 1431. These flotillas were a daunting display of technological advancement. The largest extended over 400 feet - nearly four times the length of Columbus' Santa Maria – and boasted nine masts. The first of these fleets launched in 1405 consisted of 317 vessels and carried 28,000 people![66] They explored much of the waters around Indonesia and travelled along the east coast of Africa. As David Landes elaborates, "over a period of three years, the Chinese built or refitted some 1,681

[64] Quoted by, Rapley, 2004, 1
[65] Hale and Hale, 47
[66] Landes, 1998, 93-96

ships. Medieval Europe could not have conceived of such an armada."[67] However, China struggled with the enormous costs and the political will shifted against trade and discovery. As early as 1435, production was reduced and by the middle of the 16th century to travel by sea on a multi-masted ship was established as a criminal act.[68] The magnitude of interrupting this experiment is hard to grasp, but imagine if China had rounded Africa's Cape of Good Hope and entered European ports first. Yet, this was not a short break from maritime pursuits, the first Chinese vessel did not reach Europe until 1851.[69]

Narrowing to the last 50 years reveals a startling tale of grand political and policy experiments that have caused enormous distress with limited prosperity for some. The nature of these experiments has been well intentioned but the effects often crippling to the poor, especially to those living in rural areas. In 1958, during the 'Great Leap Forward', communist model communes were built to increase the production of rural peasants procuring agriculture. All private property was abolished and 123 million agriculture workers were placed into 26,000 communes. The State also eliminated small-scale markets where farmers previously sold produce.[70] Families were expected to eat in shared facilities while "work assignments were distributed as if peasants were soldiers."[71] The consequences of these actions were dramatic. Production levels faltered causing a widespread famine. The associated deaths and decreased birth rate lowered the population by 6 million over three years.[72] Secondary to the dire lack of humanity, some economic analysts estimated the 'Great Leap Forward' lost ten years of growth.[73]

History of China Development Model Since 1978

Despite these well-known failures, the People's Republic of China (formed in 1949) has produced positive economic results. Western Chinese historians generally divide the history of the People's Republic into two eras; the Mao period from 1949 – 1975 and the entrance of Deng Xiaoping in 1978. The Marxist inspired, socialist command economy of Mao Zedong generated a modest performance, but compared to previous regimes of the last two hundred years, the results were tremendous. From 1952 until 1978, GDP tripled, and GDP per capita increased by more than 80 percent.[74] The economy began to shift away from agriculture and the industrial sector more than doubled by 1975. However, this success was outstripped by the growth of both Europe and the United States. Many writings credit the last 50 years for China's return to the world stage, but the change in policy after 1978 defines modern China.

[67] Ibid
[68] Landes, 1998, 94
[69] Ibid
[70] Maddison, Chapter 3, 1998, 10-12
[71] Ibid
[72] Ibid
[73] Dernberger, 1999, 606
[74] Maddison, Chapter 3,1998, 1

The arrival of Deng Xiaoping in 1978 began a dramatic policy move and much of China's economic rise can be attributed to these new dynamics. Callum Henderson captures the national mood for implementing changes in *China on the Brink*, "China also wants to be a nation that can no longer be bullied, a nation with a strong sense of self-worth, a nation that takes it rightful place on a global scale...Power no longer comes out of the barrel of a gun; it comes out of the economy."[75] The Deng-led government, until his death in 1997, grew the economy by an average of 9.8% (GDP), or nearly 1.5 times more than under Mao.[76] Total GDP growth does not provide a pure measure of benefits to individuals, but household measurements offer some clarity. Under Mao, the per capita household consumption expenditure increased 2.2% per annum, but more than tripled to 7.3% during Deng's rule.[77] Above all, China's economic ascent over the last 20 years is nothing short of remarkable. Very few countries have successfully transferred from a command economy to a market-driven one, and China is now the hallmark for such changes.[78]

These reforms were not set through a grand strategic plan though, and unintentional outcomes often resulted. The famed metaphor (perhaps overused) by Deng Xiaoping provides the orthodoxy behind the application of these ideas, "crossing the river by feeling the stones under the feet" (*Mo zhe shi tou guo he*). The history of failed experiments taught policy makers to follow a tentative pace. Economic zones and other tactics were, and continue to be, used as pilots to mediate the impacts on society and provide time for the necessary institutions to develop. The socialist characteristics of the reforms were also closely guarded, which contributed to the reliance on state assets, despite underperformance.

Ironically, the policies of China since 1978 are arguably aligned with the 'Washington Consensus', but with certain important exceptions. Returning to the model discussed in Chapter 1, China has followed Macroeconomic discipline relatively well by maintaining low national debt while keeping inflation somewhat stable. A market economy has not been fully embraced, but the state's role has been diminished. Moreover, openness to the world is the distinguishing mark of China's new wealth; international trade has flourished, foreign direct investment (FDI) encouraged,

[75] Henderson, 1999: 615
[76] Dornberger, 1999: 613
[77] Household consumption expenditure measures spend on good and services but excludes fixed assets (e.g. housing) and valuables (e.g. durable goods).
[78] Angus Maddison compares China and the Soviet Union, "As China prospered the Soviet economy and state system collapsed. In 1978 Chinese per capita income was 15 per cent of that of the Soviet Union. In 1995 it was 60 per cent of that in Russia." See Angus Maddison, "Dynamics of Development in the New China," in *Chinese Economic Performance in the Long Run* (Paris: OECD Development Centre, 1998), Chapter 3

and China has become a member of all significant world institutions. However, capital flows and exchange rates are managed counter to the consensus.

The following section will review China's policy changes since 1978 in a linear path with a focus on contrasts from the 'Washington Consensus' principles.

Macroeconomic Discipline

China's focus on self-reliance and isolation prevented the country from taking great debt loads during the sovereignty lending run in the 1970's, and this proved to be a critical attribute. In 1978, China was free of both foreign and domestic debt with inflation averaging a low 2 percent.[79] Lacking debt provided China important leeway when implementing reforms. Many assert that China evaded the negative effects of the 'shock therapy' applied to Russia and other transforming economies. Structural adjustments were applied on China's terms and the before mentioned pitfalls of outside economists misjudging a country's political economy were largely avoided.[80]

During the early stages, decentralization of the economy created inflationary problems that were initially uncontrollable. Mainly due to antiquated prices, inflation spikes were common during most of the 1980's and remained a problem well into the next decade. Because China had maintained fixed prices during the Mao period, increases had to be implemented aggressively. Policy makers applied them slowly, but they often adversely influenced the marketplace. 1988 was a particularly bad year with prices from the preceding year jumping nearly 30%.[81]

Concurrently during the decentralisation of the economy, it became clear the financial system was not adequate to manage an open economy or establish fiscal responsibility with so many new non-state actors. Therefore, the People's Bank of China was established as a central reserve institution and commercial banks were dedicated to serve customers as typical in western economies. Tax codes were adjusted to be more focused on individual incomes though problems with revenue collection remain today.[82]

Reforms in the early 1990's included assertive steps to settle the inflation problem. This was generally done by reversing the experiment with decentralisation. State-level bureaucrats more aggressively monitored policy changes and central planners held local officials accountable. However, these moves should not be interpreted as returning to the Mao, command ideology; the

[79] Maddison, Chapter 3, 1998, 11
[80] Why the IFI's loaned significant money to China despite gross human rights violations is beyond this review, however the debate is noteworthy.
[81] IMF, 2004, 232
[82] Dernberger, 1999, 613

country's political economy had already fundamentally changed. A number of other experiments were attempted but most of the improvements can be attributed to more reasonable price controls and shrinking the money supply. Slowing state investments and tightening bank lending practices constrained available capital while the postponement of price increases prevented further rises to consumers.[83] Inflation jumped to an 18% average from 1993-1995 but fell to 3% by 1997.[84]

At present, China maintains conservative macroeconomic discipline, which does not differ drastically from the 'Washington Consensus'. Current inflation rates are always contentious among analysts because of China's statistical practices, but it is generally accepted to be at or below 5%. Explicit government debt is only 26% of GDP and the budget deficit sits at a modest 3% of GDP.[85] China has not been afraid to borrow either, some $104 billion was obtained from both multilateral and private sources by the end of 1996.[86] However, huge savings and capital reserves suggests China is in no danger of immediate fiscal instability. The country also maintains strong sovereign debt ratings and regularly raises capital through private markets. Some might argue China's earlier high inflation rates were counter to consensus, but hyperinflation was mostly avoided. The WorldBank also agrees, "China has been managing macroeconomic conditions well. It has relied on stimulatory macroeconomic policies and a stable exchange rate to sustain domestic demand activity and support structural reforms."[87] Therefore, for this principle, China has, and continues to follow, the rules suggested by the 'Washington Consensus'.

A Market Economy

As noted, the Deng administration's first step was to decentralise much of the economic planning by pushing price mechanisms and resource allocation authority to local officials. This was not a complete embrace of markets, but officials accepted some control had to be relaxed. Direct sale of State Owned Enterprises (SOEs) was not considered, but broad tactical control was passed to local administrators and importantly, profits began to stay within some SOEs. The relaxing of price controls also inadvertently placed market forces on the outputs of the production cycle, therefore unprofitable SOEs were often unexpectedly exposed. The extent of eliminating price controls should not be underestimated either; nearly all of China's prices were set by the state in 1980, but within a decade, two-thirds of agriculture products, 80% of manufactured consumer

[83] IMF, 2004, 232
[84] Roubini et al, 1998, 20
[85] Hale D. and Hale L., 2003, 49
[86] Maddison, 1998, 10
[87] The World Bank, 2004, 27

goods, almost all of the service sector and one-third of producer goods were susceptible to the market.[88]

From an economic sector perspective, liberalising agriculture was an early priority. The communal projects were reversed and peasant farmers returned to their land. The state exerted some control over specific crops, but most of the rural markets were allowed to once again flourish. Quasi-direct land ownership was established through long-term leases and most peasants began pursuing private home ownership. This produced measurable results. From *The Economist*, "The introduction of cash crops, and the growth of informal markets, led to an increase of 14% a year in rural incomes during the same six years (1978-1984). According to the official count, the number of those in poverty fell by a quarter—a reduction of 60m, equivalent to the population of France."[89] These gains were short-lived though. Returning to the household tradition followed for generations helped improve productivity, but the shortage of technology and refusal to privatise property prevented greater gains. In the early 1980's, agriculture was still one third of China's economy but industrial production was beginning to eclipse the once dominant sector.[90] Emphasis on reforms in agriculture slowed and growth ceased until the 1990's when outside technology was finally introduced by outside traders.

Non-state owned enterprises were re-emphasised in the mid-1980's with the intent of creating wealth where agriculture was sputtering in the rural areas. Individual ownership is implied, but this class of ventures, named township and village enterprises (TVEs), was managed by a consortium of interests; local officials, entrepreneurs and banks. This experiment proved fruitful though. In 1985 TVEs employed 14% of the labour force and contributed to over 30% of Gross National Product (GNP). This sector also had longevity; output growth over the next 10 years exceeded 30% annually.[91]

Targeted rural reforms produced results, but more trouble spots were found in the urban, and more populated, industrialised regions. The crux of this matter was with SOE's and China's commitment to an egalitarian society. Deng's gradual introduction of market reforms with a reluctance to privatise were driven by a fear of inequality. However, this approach caused two significant consequences that remain unresolved today. First, a dual labour economy emerged – those employed by the state enjoyed thorough safety nets and life-long employment whereas those in the private sector are susceptible to the benefits as well as the nasty side effects of an unregulated labour market. Further, the private sector is funded through foreign capital, therefore

[88] The Chinese Economy Under Den Xiaoping, 1996, 50
[89] *The Economist*, 11 September 1997
[90] IMF, 2004, 3
[91] Ibid, 6

threats of state supervision generates investor apprehension. Second, SOE's remain unprofitable and are struggling to support the extensive social contracts guaranteed with employment. Loads of pent up capital, surplus capacity and worthless inventory are also part of the SOE conundrum.

Planners recognised this problem as early as 1983, but little has changed. Robert Michael Field writing in 1996 about reforms targeting SOEs, "Implementing this decision would have required a whole range of specific reforms...but events overtook it almost immediately: a downtum in the economy, the struggle between moderates and conservatives, and Tiananmen and its aftermath. The problems faced today are still the same as in 1978 and 1984." Most current analysts would assert little has changed from 1996. For years, banks have been propping up the underperformance with subsidised capital, but this has only hidden the problem. As the 'Washington Consensus' proponents will cite, markets produce more efficient results and China has still not found a panacea for its huge swath of poorly performing state assets. Thus, China is faced with a grave paradox: socialist ideology places SOEs at the core of ensuring an equal society, but a continued commitment might lead to insolvency.

Broadly, China has been reducing the role of the State since 1978. In 1995, government revenue was 11% of GDP whereas in 1978 it was 31.7%.[92] SOEs were 75% of the economy in 1975 and but just 28% in 2000. However, this data is somewhat misleading. The reduction in government revenue reflects the difficulty of collections at the local levels and other fiscal problems, not necessarily an aggressive shift to shrink the state. And while SOE's are a smaller proportion of the economy, they still employed 44% of urban residents in 2000 and accounted for 70% of state revenues.[93]

Despite the success of pushing markets into the economy, China remains lukewarm towards privatisation and its political economy remains state-centric. SOE reforms will continue, but privatisation remains a rejected concept. Stephen Roach warns market advocates, "It is critical to remember that China remains very much a mixed economy — the state still owns approximately 60% of the nation's total assets and still accounts for about 90% of total fixed investment."[94] The historical commitment to socialism and the concern with inequality prevents changes with no foreseeable major shifts. China, as a reformed command economy, began with nominal markets but 'Washington Consensus' countries have advocated market solutions for centuries. Therefore,

[92] Maddison, 1998, 10
[93] *The Economist*, 28 September 2000
[94] Roach, 8 November 2004

China's step toward 'marketization' is a reluctant embrace at best and should be viewed simply as a pragmatic decision necessary to compete globally.

Openness to the World

"At the heart of the issue is the revival of the old 19th-century problem that troubled Confucian reformers who sought to modernize along Western lines while retaining Chinese traditional Confucian values...as epitomized in the slogan...'Chinese learning for the essentials and Western learning for the practicalities' (Zhong xue wei ti, Xi xue wei yong).[95] Michael Yahuda's assessment of China's broad development debate is especially telling when considering how China has managed global trade and capital. At the simplistic view, China created a mercantilist model with strong liberal undertones. Trade, capital, technology and the scores of other benefits bestowed to a nation active in the global economy were highly desired when the Deng leadership began their reign, but socialist roots had to be protected. Through closely targeted liberal reforms, these desires were fulfilled in striking fashion. However, applied mercantilist policies frequently countered the expansion of the new economy. China's experiment with openness has been riddled with reluctance but proved highly successful in economic terms.

To China's credit, these contrasting policies quickly established an impressive and growing footprint in the global economy, but they did not all arrive at once. Moving out of isolation was the first phase. In the classic Chinese way, embracing world-governing institutions was a long process beginning with the United Nations (UN) in 1971, followed by the World Bank/IMF in 1980 and culminating in 2001 with the World Trade Organisation (WTO). Relations with the broader powers began early with Japan restoring diplomatic recognition in 1972 and the United States granting favoured nation status in 1979. During the last twenty-five years, China has steadily embedded itself further into global dialogue. Alastair Iain Johnston concluded from his empirical study, "From the mid-1960s to the mid-1990s, China moved from virtual isolation from international organizations to membership numbers approaching about 80 percent of the comparison states."[96]

As with the other reforms, changes began with decentralising authority by allowing provincial and local leaders to pursue foreign trade independently. Reducing prices and attempting to align them with foreign standards also had to be coupled with this effort. Competing globally also meant the renminbi was not competitive, therefore fixed exchange rates were discontinued through a fivefold currency devaluation from 1980 to 1996.

[95] Yahuda, 1998, 551
[96] Comparison states are United States, Japan, and a world average. See Johnston, Alastair Iain, Is China a Status Quo Power? *International Security*, Vol. 27, No. 4 (Spring 2003), p.13

Special enterprise zones (SEZs), with preferential policies to accommodate foreign direct investment (FDI) and exports, were instituted in the early 1980's. SOEs, joint ventures, privately held companies and foreign owned businesses all operated in these economic units. Provincial leaders were given further authority to attract investment by offering tax breaks and other incentives. As these regions grew, others were introduced thereby creating competition among the different areas. SEZ locations were also placed where SOEs were not prevalent and this partly explains the emergence of the southern coastal region as the most heavily developed. Shenzhen, one the first four zones created in 1980, provides insight into the magnitude of change...it grew from a mere 23,000 residents to over 3 million by 1996."[97]

These early reforms created a flurry of increased trade and FDI. Returning to the Shenzhen zone for an example, from 1987 to 1991, FDI grew nearly four-fold from $274 million to over $1 Billion.[98] New trade and capital continued to be aggressively pursued but trade practices also had to be modernised. By 1991, China began to lower tariffs and standardise reporting methods for an attempt to resume membership in the General Agreement on Tariffs and Trade (GATT). This eventually led to acceptance into the WTO after nearly twenty years of pursuit.

After the retrenchment of the early 1990's, the economy's growth path began to take-off. Deng was finally able to convince the ruling party that a market economy was not incompatible with socialism. This formal political acceptance is cited as the final stride towards a complete restructure of the economy. The acceleration of FDI flows after 1991 signifies the importance of the political change. From 1979 to 1991, FDI totalled $23 Billion. While from 1992 to 1996, total inflow was $152 Billion.[99]

The East Asian Financial crises proved to be the next decisive moment. The debate surrounding the causes of the economic collapse will remain unresolved but China's resilience during the struggle made a profound impact on China's policymakers. Most of the surrounding economies dealt with massive short-term capital flight and dramatically depreciated currencies, while China remained stable.[100] The effects of the regional crisis were certainly felt, but China emerged from the struggle in a much stronger economic position. China's policies of keeping tight capital controls and pegging the renminbi to the dollar remained contentious, but leadership's reluctance with markets was reaffirmed. "Other Asian economies are suffering the distress of currency

[97] Maddison, 1998, 12
[98] Bell et al, 1993, 107
[99] Maddison, 1998, 11
[100] Roubini et al, 1998, 20

devaluations forced upon them by the markets; China devalued at its own initiative in early 1994, and is currently reaping the benefit in booming exports" as highlighted by *The Economist*.[101]

Narrowing to the last few years reveals the acceleration of established tactics; currency market intervention through large purchases of US government securities and a continuance of currency controls. As noted in Chapter 1, the practice of purchasing US government debt as a means to stabilize currency is utilised by most Asian countries. However, a recent ground swell of activity has occurred. While Japan still leads, China has been quickly catching up. In 2002, China purchased over $100 Billion of US treasuries and it has since been on a buying spree. From December 2001 to August 2003, China's reserves (mostly in dollars) increased by 65% while Japan's moved up 36%. In 2004, China added $207 billion and completed the year with the grand sum of $610 billion in foreign reserves. China has also refused to relax currency controls. The renmimbi was 8.30 to the dollar a decade ago, it was recently 8.28.[102] These mercantilist instruments have remained intact despite significant international pressures to further liberalise the capital account and the overall financial system. The next significant evolution for China probably involves revisiting these policies, but current guidelines remain steadfast.

At present, China continues the remarkable record of attracting trade and FDI flows. According to the OECD, China surpassed the United States, the world's largest economy, with FDI of $53 Billion in 2003. Trade levels follow a similar trend. China's overall share in world trade was less than 1% in 1979 but accounted for 6% in 2003.[103] Rehashing further macro measures is redundant, for financial publications are awash with data points about China's economic movements and most are not-surprisingly exuberant. Where these new riches will lead China is unknown and their continuance is not foregone. China will retain its unique mercantilist model despite calls for liberal reforms and a path based on socialist values remains firmly drawn.

China's Political Economy Advantages

David Landes, when reviewing the economic history of China in *The Wealth and Poverty of Nations*, captured the notion of over-zealous speculators, "...the potential size of the market—so many people!—made China the legendary El Dorado of the nineteenth and twentieth centuries."[104] In many ways, this perception continues with the private sector still pursuing China's huge markets despite a controversial political economy. China's oligarchic governance style of suppressing democratic ideals and shunning human rights is the antonym to western democratic systems. Subramanian Swamy, president of India's Janata Party and former minister

[101] *The Economist*, 11 September 1997
[102] As of July 2005, China adjusted the renminbi by 2%, but the possibility of future depreciations are not agreed upon
[103] IMF, 2004, 3
[104] Landes, 1998, 93

of law, commerce and justice worries, "If China continues to grow and grow, people will inevitably begin to think this is proof of the validity of their system, and that would be very bad for all of Asia."[105] But, as this paper demonstrates, China has so far defied critics who claimed market reforms were not achievable without a democratic process. Foreign multinationals and IFIs seem to agree with China, or at least they have not wavered with financial support. China is the World Bank's largest customer. Western countries acceptance of China's unique political economy is complex and outside this analysis, but outlining how China's political economy enabled such growth despite historical precedence is essential to addressing the broader research question of this paper. Therefore, how has China's political economy, or its relationship between market and state, created so much affluence?

Evaluating China's demographics provides some foundation. China has a huge population of 1.3 Billion people that are surprisingly homogenous, nearly 90% are Han. The depth of the socio-economic spectrum is also startling. Very large wealthy classes have emerged but millions still live in poverty. The IMF has estimated per capita income at only $1060, despite twenty plus years of phenomenal economic gains.[106] According to the World Bank, there were 205 million people living in poverty in 2000 (official numbers have it at under 30 million).[107] Regardless of definitions, China is comprised of a disturbing number of people living under the subsistence level. On the inverse, there is a large and growing upper and middle class. Products ranging from luxury goods to automobiles have seen explosive sales and both domestic and foreign companies are fighting for market share.

The combined features of a wealthy domestic market with ample low-cost labour have created a powerful draw for investment not seen before in the developing world. The OECD noted the reasons for attracting FDI have shifted, "the size of domestic markets in big developing emerging economies, particularly, China is attracting foreign firms. This contrasts somewhat with earlier decades when OECD companies were primarily investing in developing countries to benefit from lower wages and production costs."[108] China therefore has the best of both; accessible labour and wealthy domestic consumers.

As China's legacy proves, the pure vastness of the market is not enough. A capable state apparatus is a critical component. China also has a long established history with bureaucracies. Angus Maddison explains, "China was a pioneer in bureaucratic models of governance. In the tenth century, it was already recruiting professionally trained public servants on a meritocratic

[105] Sengupta and French, The New York Times, 10 April 2005
[106] IMF, 2004, 3
[107] The World Bank, 2005, 18
[108] Maddison, Summary and Conclusions, 1998, 1

basis. The bureaucracy was the main instrument for imposing social and political order in a unitary state over a huge area."[109] As a result, the state has strong, well-practiced bureaucracies (in some areas) capable of managing intricate policies or projects.

Due to the autocratic political processes within China, governing authority and resource allocation is opaque at best, especially when contrasted against western-style democracy. This provides debatable benefits though. "In fact, because China's economic reforms disrupt the lives of millions of people, they are often unpopular", David Hale details in *Foreign Affairs*, "Were China a democracy, it would probably have to weather a populist movement opposing the reforms. But it is run by an authoritarian regime – a feature that allows it to implement radical change quickly."[110]

Reviewing recent infrastructure investments explains this further. As expected, Chinese administrators do not need to wade through the often slow and arduous processes found in democracies. Local constituents are often non-factors and decisions can be driven through despite untold costs to the local population. The notorious Three Bridges Dam in China demonstrates how controversial projects can be imposed. This new dam was first approved by China's Parliament in 1992 and has been in partial operation since last year. The costs were between $21 to $30 Billion (depending on who is counting) and the dam was completely funded by China due to the World Bank's and IMF's reluctance. The project displaced 1.3 million people, put nearly 600 kilometres under water and the environmental impacts are still not understood. This was all done without a clear case of how the dam would benefit the region.[111]

Looking to India and its prolonged quest for infrastructure improvements helps to extend support for this aspect. The *NY Times* reported, "There is constant talk these days of turning Mumbai, the southern commercial metropolis formerly known as Bombay, into a new Shanghai, China's most glittering modern city. More to the point may be Bangalore, India's booming capital of telephone call centers and high-tech software. Growth there has been menaced by political delays that have stalled construction of a new airport for seven years. Shanghai, on the other hand, built one of the world's most spectacular airports in three years."[112] China's state structures suffer the same ills of other nations (e.g. inefficiencies, corruption), but they allow less scrutiny and are thus arguably quicker. The events of Tiananmen Square[113] in 1989 illustrate the political risks, but the implementation of party decisions with few outlets for dissent can produce results.

[109] Ibid
[110] Hale and Hale, 2003, 51
[111] *The Economist*, 5 June 2003
[112] Sengupta and French, The New York Times, 10 April 2005
[113] Tiananmen ironically translates to 'the Gate of Heavenly Peace'

The state management of labour has also been a central characteristic of China's political economy. China's export-led growth plan has been accomplished by providing extraordinarily cheap labour. According to the Institute for International Economics, China's manufacturing wages averaged 88 cents per hour in 2002, which is just 6% of the US average.[114] As expected, foreign and domestic firms have setup extensive production facilities to exploit this comparative advantage. China is now the world's leader in manufacturing.

Low wages have been partly maintained because millions of migrant workers formerly performing agricultural duties entered urban areas over the course of the boom. Wage increases have not risen dramatically due to the sheer number of workers still waiting to enter the industrialised sector of the economy. Rural labour, or about 50% of the workforce, is still estimated be some 370 million people.[115] Beyond low wages, the labour market is also troublesome due to insufficient regulations and lax enforcement practices. This has obviously contributed to keeping wages very low, but humanitarian concerns are rife. Protests in rural areas and periodic spikes in unemployment have generated political concerns but China has thus far avoided dramatic social unrest. Recent labour shortages in some of the southern industrialised regions suggests working conditions and wages might be improved due to market demands, but the breadth of people living in poverty and unemployed suggests factories will move where there is less wage competition. Therefore, this critical, unresolved predicament is embedded within accomplishing further economic ascendance.

The transformation of China's political economy has created a 'perfect storm' for attracting investment and generating trade, but its political framework is troubling. Its large, economically diverse population, inexpensive labour and centralised planning has created the potential for the largest economy ever built. However, the limitations of the political system as well as the lingering remnants of the command economy reinforce that fact that China is still in transition. Some academic studies show that economic progress generally leads towards democratization, but non-democratic systems can sustain growth for long periods of time because broad political changes are undermined.[116] The Middle Kingdom has been defiant so far. Callum Henderson, a noted critic, wrote "China is not a democracy, whatever its merits, and the authorities that govern it will not go quietly – if go they do...For the West to think otherwise is merely wishful thinking..."[117] Political risks are apparent and long-term stability is a distant goal.

[114] Hufbauer et al, 2004, 10
[115] Hufbauer et al, 2004, 10
[116] Nattrass and Seekings, 1998, 31
[117] Henderson, 1999, 245

Sino-African Trade and Development

As a developing country from the southern hemisphere and lacking a colonial interventionist past, China's has enjoyed mostly robust relations with African countries. Historically, trade reaches back centuries and China has provided aid to African countries for decades. Cold War, ideologically inspired projects were pursued during the 1960's and 70's but interest faded in the 1980's when China's focus shifted away from communism and toward GDP growth. Extensive trade networks have periodically thrived and significant development projects, particularly the Tanzania-Zambia railway, have occurred. When compared to western countries, China has never shown an enduring interest in Africa, though this has significantly changed in the last five years.

The nucleus of this issue is China's avid pursuit of resources. Economic expansion requires raw materials and China has pursued them relentlessly. Commodity imports for the Middle Kingdom totalled $140 billion in 2004. China is now a larger consumer than the United States for copper and is expected to lead aluminium in 2005. Steel production is the most telling of all – China produces more than the US and Japan combined.[118] Recent global oil price hikes are also partially related to China's increased consumption. How is China, a developing country, consuming so much? David Hale offers a partial explanation, "As China's nominal GDP is only $1.3 trillion compared to over $10 trillion for the US, its consumption of raw materials should be less than America's, but the reality is that China's real GDP is probably half of America's."[119] The misleading size of China's economy is only one side of the issue though; the other is a lack of efficiency. "We are using too many raw materials to sustain this growth...To produce goods worth $10,000, for example, we need seven times more resources than Japan, nearly six times more than the United States and, perhaps most embarrassing, nearly three times more than India. Things can't, nor should they, be allowed to go on like that" as affirmed by Pan Yue, China's environment minister.[120] Africa, and its vast natural resources, has now become an important strategic region for China and good relations are imperative to achieving goals at home.

Trade between Africa and China grew 50% from 2002 – 2003, totalling $18.5 billion, China's largest jump for any region. It was only $6.5 billion in 1999.[121] By 2006, trade levels are expected to nearly double to $30 Billion.[122] In comparison, according to the US Commerce department, US-Africa trade was $44.5 billion last year. The export composition of these figures are not surprisingly commodity centric, with the majority of exports being oil – Sudan, Chad,

[118] Hale, Will China Need a Blue Water Navy to Protect Commodity Imports, 2005, 2
[119] Ibid, 13
[120] Sengupta and French, The New York Times, 10 April 2005
[121] Domingos, 2004, 5
[122] Mooney, 2005

Nigeria, Angola and Gabon all have oil agreements with China. This is misleading though. While business linkages might have begun with oil, other sectors are seeing activity. Forty trade deals have been signed with African countries, many of them not mineral or oil rich. From the *Yale Global*, "Almost every African country today bears examples of China's emerging presence, from oil fields in the east, to farms in the south, and mines in the center of the continent."[123] China's FDI flows to Africa reflect this diversification trend. Manufacturing leads with resource development and services following closely behind. Chinese investments in telecommunications, construction and agriculture have all seen increased expansion throughout the continent. Regionally, the investments are also widespread. South Africa and Zambia (mainly copper mines) account for 34% of the capital but the rest is spread across 18 other countries.[124]

Diplomatic rhetoric and multilateral commitments have escalated. China has sought to leverage its hybrid position as a developing country with developed country credentials (mainly through the UN Security Council seat). Speaking to the China-Africa Cooperation Forum in Addis Abbaba, China's premier Wen Jiabo said "China is ready to coordinate its positions with African countries in the process of international economic rules formulation and multilateral trade negotiations, with a view to safeguarding the legitimate rights and interests of developing countries."[125] The China-African Business Council (CABC) was formed last year with cooperation from the UN to further private investment into Africa. African visits from high-level party officials are now a common occurrence. The Chinese also have troops under the UN in Liberia and Congo. These efforts have been successful, "For historical reasons, we used to pay attention only to Western countries" notes Kheri Iddi Milao, acting chief of the Zanzibar Bureau of Foreign Affairs, "Now this has changed. We are shifting our eyes to Asia."[126]

China also understands the African sensitivity to being solely exploited for resources and has sought political cover through aid. And as one author reminds us, "Foreign Aid – the transfer of concessional resources from one government to another – is a tool of statecraft". The Yale Global provides further analysis, "Chinese are busy developing much-needed African infrastructure: roads and rail lines in Ethiopia, Sudan, and Rwanda; a new hospital in Sudan; a farm and a bridge across the Nile; reclaiming thousands of hectares of farmland in Tanzania."[127] Total China development aid to Africa is estimated at $1.8 billion in 2002, but these figures are suspect due to China's reluctance with providing figures. Debt exemptions are provided and they have hastened in the last two years with $1.2 billion written-off for 31 African countries. Not all

[123] Ibid
[124] WorldBank, Patterns of Africa-Asia Trade and Investment Potential for Ownership and Partnership, 2004
[125] Beijing Times, 15 December 2003
[126] Harsch, 2004, 1
[127] Mooney, 2005

aid (and trade) comes without conditions though. China quietly requires support for its Taiwan and 'One China' policy. Only 7 African nations have formal relations with Taiwan and business links are shunned. Where most Asian countries divest investment across the continent, the vast majority of Taiwan's FDI flows only go to one African state, Liberia.[128]

"We don't believe that human rights should stand above sovereignty" as spoken by He Wenping, director of the African Studies Section at the Chinese Academy of Social Sciences in Beijing.[129] The unabashed realist principles of China's aid and business policies are providing considerable debate for African countries. Aid without conditions has been highly desired as an obvious counterweight to the structural reform requirements demanded by the IFI's. After Hu Jintao's visit to Gabon in February 2004, Gabonese President Omar Bongo commented, "it seems to me that the aid provided by certain countries is tied aid...cooperation with China comes without conditions, with mutual respect and regard for diversity"[130]. Aid is also closely tied with business. Angola was granted a $2 billion soft loan in return for 10,000 barrels of oil a day.

These tactics are questioned when China works with controversial governments though. The recent genocide in Sudan has captured the most attention. China's refusal to support resolutions presented in the UN Security Council reaffirms China's reluctance to interfere with domestic issues. However, comprehensive oil investments and thousands of Chinese troops guarding pipelines in Sudan make these policies seem suspect. Increased interaction with Zimbabwe has created a new stir. A trade delegation passed through Zimbabwe promising over $100 million in additional investment despite sanctions imposed by most western government. During an interview with Sky News last year, President Mugabe was defending his new $9 million home, "You say it's lavish because it is attractive. It has Chinese roofing material, which makes it very beautiful, but it was donated to us. The Chinese are our good friends, you see."[131]

Without debate, Africa is no longer an undertone to Chinese foreign policy. Increased business interests and development aid are flowing into Africa – mostly within the last few years. While these activities do not yet rival the United States or the European Union, the divide is closing. Considerable aid and business from the West have always weighed on decisions made by African leaders, but having an alternative partner, with different principles, is beginning to affect Africa's political economy. Could this new influence lead to changes in Africa's development models?

[128] WorldBank, Patterns of Africa-Asia Trade and Investment Potential for Ownership and Partnership, 2004
[129] Mooney, 2005
[130] Harsch, 2004, 1
[131] McLaughlin, 2005

New Hegemon or Another El Dorado?

Studying those foretelling the future of China reveals an endless variety of perspectives. The optimists predict a new hegemon while the sceptics acclaim another El Dorado.[132] As with most analysis, the truth probably falls in the middle but is nearly impossible to predict. China is managing through its grandest experiment and the importance to global humanity has never been more important. Unquestionably, China's current situation has brought untold benefits but troubling problems. Vivienne Shue, writing in *The China Quarterly* in 1996, reviewed several books published 15 years after the reforms began and captures the uncertainty of the situation that remains today.

> For these new works – some explicitly and some more inadvertently – seem to want to teach us yet again lessons we have already learned from previous episodes of dramatic "transition" in China's modern history: that stunning changes do not necessarily signify social progress: and that sweet progress, when it does appear, only needs its pockets turned out to reveal what seeds of bitter backlash it has to sow.[133]

For now, China appears to have again found the ambiguous 'elixir' of policy and political ideals to successfully lift many out of poverty. This has been accomplished through a previously unseen development model that leverages the three 'Washington Consensus' pillars while challenging some aspects through shameless mercantilism. Macroeconomic Discipline has been tirelessly followed, but A Market Economy has only been tentatively implemented. Openness to the World is the most celebrated aspect of China's economy, but underlying currency and capital controls have remained steady.

The traits of the Middle Kingdom's political economy have allowed many of these policies to flourish. The demographics of China and the socio-economic spectrum of the population have provided the unusual trait of wealthy markets coupled with an abundance of labour. Investment and trade have since inundated the marketplace. In addition, the competent bureaucracy with autocratic political processes has accelerated industrial expansion and squelched populist concerns.

China's unique political economy and policy recipe has led to a phenomenal expansion that is now upon the African shores. China's need for natural resources ignited trade flows, but stronger, more diversified ties are now being forged. This has created a flurry of new Chinese trade and aid activities never seen before and the political consequences are far from being completely understood. Africa is now an integral strategic interest for China. African leaders are

[132] For a short, less optimistic review of China's future, see Gilboy, George J. "The Myth Behind China's Miracle" *Foreign Affairs* July/August 2004
[133] Shue, 1995, 1779

beginning to take notice of the geo-economic movements to their East and now believe developing countries can challenge the 'Washington Consensus'.

Chapter 3 Case Study - South Africa

"China and developing Asian economies are continuing to industrialise and deepen their services sector rapidly, on the strength of high savings rates, broad skills pools and competitive export sectors. Growth has also recovered strongly in the United States, but its sustainability is threatened by huge imbalances in both the fiscal accounts and the balance of payments
Trevor Manuel, South African Finance Minister, 2005 Budget Speech to Parliament

Looking East

Parallels between African and Indian Ocean/Asian development paths have been drawn since the end of colonial rule. Most studies comparing economic gains between the two regions show similar starting points in the 1960's with an income gap quickly emerging. The causes for this unfortunate period are endlessly complex but most Asian citizens have emerged in a more prosperous position. Disturbingly, this trend continues today.

Following the end of the Cold War, African countries were applying the reforms recommended by the International Finance Institutions (IFI) while their Asian counterparts utilised a more state-centric, mercantilist model. The correctness of these rivalling ideas will never ultimately be resolved but China's success and East Asia's recovery from the 1997 financial crisis have only reaffirmed the potential of Asian policies. Legitimate and proven alternative approaches to the 'Washington Consensus' are now accepted. It should therefore not be a surprise that African leaders continue to look East for ideas about how to enrich their populations.

A number of prominent African officials have reaffirmed their interest in Asia. At the 2004 Tokyo International Conference on Development (TICAD), Mwai Kibaki, President of Kenya, explained, "Today we share similar aspirations for socio-economic development. In this respect, Asia has led the way and TICAD provides Africa an opportunity to learn form the economic successes of Asian countries."[134] Ethiopian Prime Minister Meles Zenawi noted at the same conference in 2003 how recent trade and aid interactions "introduced an alternative development paradigm based on the successful development experience of many East Asian countries and thus helped expand the tool kits at the disposal of African development practitioners."[135] An interview with Minister Dompok of Malaysia highlights how Asian countries are sharing knowledge at a pragmatic level. "Technical training courses for African practitioners draw on Malaysia's long experience with development planning, in particular how government can work closely with the private sector, while at the same time maintaining a focus on the social needs of the people."[136] Due to China being at the centre of Asia's emergence and the world's largest developing country, the emphasis is on their model. The South African *Mail & Guardian* demonstrates,

[134] Kibaki, 2005
[135] As quoted, Harsch, 2004
[136] Ibid

"South Africa is increasingly tempering liberal economic policies based on the Washington Consensus with a state-led growth model that draws its inspiration from a very different capital...Beijing."[137]

Beyond the discussions of political leaders and media reports, a critical look at implemented tactics and policies is necessary to answer the research questions of this paper. A thorough review of development models for every country in Sub-Saharan Africa is a far-reaching task, therefore a case study of South Africa will be utilised. This case will provide a brief history of South Africa's development model since the end of Apartheid in 1994 and exhibit how policies and ideologies have morphed over the last ten years. The 'Washington Consensus' model introduced in Chapter 1 will provide the framework for the analysis and distinctions from China's approach will be stressed. Finally, South Africa's political economy ultimately decides the extent and success of policy changes; therefore, its defining attributes will be investigated.

Overall, this case will explain that recent policy changes have moved South Africa's model closer to China's, but the domestic political economy prevents a complete adoption.

Why South Africa as a Case Study

South Africa is the economic hegemon of Southern Africa. The isolation of Apartheid prevented interactions with the rest of Sub-Saharan Africa and even after South Africa shed the old regime, economic integration did not accelerate for some time. However, the empirical evidence now suggests a strong, widespread South African presence that is only expanding.

Exactly how much of the South African economy accounts for the overall GDP of Southern Africa is not readily agreed upon. The *Economist* in 2004 stated the South African economy was 45% of Sub-Saharan Africa's GDP. Whereas a recent publication from the South Africa Foundation lists a smaller estimate, 33%.[138] Either measurement is striking considering the size of the region. Investment across the continent has increased dramatically and South Africa is now one of the top 10 investors in nearly every African country.[139] The United Nations Conference on Trade and Development (UNCTAD) estimates total South African investments to be $1.4 billion in the last 10 years. As expected, trade levels are on a similar course, but more export heavy. Exports to the rest of Africa increased 10 times from 1991 to 2002 and are roughly R40 Billion a year.[140] Imports from the region into South Africa are stronger but only one-fourth of total

[137] *Mail and Guardian*, 11 February 2005
[138] The South Africa Foundation is a research group sponsored by predominate South African-based multinationals and understandably attempts to downplay South Africa's expansion.
[139] South Africa's Business Presence in Africa, South Africa Foundation, 2004
[140] Ibid

exports. A recent World Bank study also acknowledges the correlation between South African domestic growth and the broader benefits to Africa. Based on data ending in 1999, for every 1 percent increase in South African economic growth, other African countries grew .5 to .75 percent.[141] Further, from 1980-2003 South Africa accounted for 30% of Africa's GDP growth.[142] Conclusively, South Africa and Africa's economic relationship is approaching a marriage.

Correctly, regional economic assimilation does not establish direct causality with how a country chooses a development path. While Mozambique, Botswana, and Namibia can be seen to embrace similar models as South Africa, Zimbabwe is an important exception. It would be short-sighted, however, to suggest South African methods do not highly influence the region. This economic dominance means Southern Africa's future is very much tied to how well South Africa expands both politically and economically. This cannot be done without the further expansion of trade and investment. From South Africa's Former Deputy President Jacob Zuma, "our growth and development is intimately linked to that of the rest of the African continent...We view African problems as our problems, as we cannot be an island of peace and development in the midst of poverty and conflict."[143] A local collapse would ensure a damaging ripple effect across the rest of the region and South Africa understands the gravity of the integration.

History of South African Development Since 1994

As with any analysis of South Africa, the effects of Apartheid and colonial practices present unique circumstances to economic administrators and business leaders. A half-century of malevolent minority rule established a two-tier economy where the white minority enjoyed superior education levels, job security and infrastructure while the majority was largely constrained to impoverished areas with few opportunities. The political transition in 1994 brought optimism but the economy has rebounded slowly and the socioeconomic divide has only widened. The World Bank's Gini Coefficient (2002), where South Africa is only slightly higher than Brazil, the world's worst, reaffirms this reality. GDP growth since 1999 has averaged 3.1% annually, but the per capita measure has been a meagre 1.3%. Frustrations for not obtaining higher growth rates are frequently voiced but when considering the enormity of the political achievements, patience is understandably requested. Projections for the next few years are obviously divergent but the economy is expected to remain on the current course with potential for modest gains.

The policies since 1994 are usually categorised into two periods. The first is the state centred Reconstruction and Development Program (RDP) with roots dating before the political transition

[141] Vivek and Vamvakidis, 2005, 4
[142] Ibid, 10
[143] Zuma, J, 2004

and influenced by the communist and labour political bases of the ANC. The second, viewed more 'Washington Consensus' and private industry focused, was coined Growth, Employment and Redistribution (GEAR). The short-lived RDP lacked time to leave a lasting impression, but was politically popular with the poor and rural bases. A great deal has been written about the change in economic strategies, but the ANC has never seen the switch as abandoning a particular ideology. RDP provided the high-level objectives while GEAR provided the financial roadmap.

Placing semantics aside, the entrance of GEAR into the socioeconomic arena brought a more refined, detailed plan but liberal ideas. The shift expectantly attracted contentious rhetoric across the political spectrum, but the new direction never jeopardized the ANC tri-alliance as so many predicted. Fredrick van Zyl Slabbert summarises the rivalling opinions about GEAR, "From one perspective it could be argued that GEAR is simply conventional IMF and World Bank economic policy, (i.e. foreign domination), from another perspective the Government could argue, it is necessary to generate the wealth, precisely to meet the demands and needs of those who resist its implementation (i.e. domestic pressure)."[144]

Unlike China, a change in leadership did not spark the transition; both Nelson Mandela and the ANC were firmly in power during the entire process. The ANC economic thinking had deep nationalistic and anti-privatisation roots dating to before publication of The Freedom Charter in 1956; however, the drift right toward a neo-liberal agenda was not gradual.[145] Nelson Mandela's comments during the early 1990's offer poignant observations about the ANC's leaderships changing beliefs. After his 1990 release, the state-centred economic direction of the ANC was confirmed, "The nationalisation of mines, bank and monopoly industry is the policy of the ANC and a change or modification of our view in this regard is inconceivable."[146] However, his well-documented turn toward a pro-market model after the 1992 World Economic Forum revealed early insecurity with the ideology woven into RDP. Upon Mandela's return, he remarked to the ANC leadership, "We either keep nationalization and get no investment, or we modify our attitude and get investment."[147] Of course, Nelson Mandela was not the sole spokesperson for the diverse ANC political base, but his comments hinted at a looming amend toward the pro-business factions that remain today.

Beyond the RDP vs. GEAR debate, South Africa remains a tormented state where globalisation demands 'Washington Consensus' policies but domestic socio-economic realities encourage a

[144] van Zyl Slabbert, 11
[145] Nattrass, 1994, 344
[146] Nattrass, 1994, 345
[147] Sparks, 176

strong state and aggressive redistribution. As Padraig Carmody argued in 2002, "the South African government is attempting a compromise between globalisation and social democracy."[148] After 1996, the development model encouraged open trade and privatisation with the end goal of attracting foreign investment and capital. Missing FDI, lacklustre GDP growth and a failure to generate jobs (for the poor) since the espousal have created rising frustrations though. South Africa is now beginning to question the logic of this development path and is changing course to one that appears more similar to the state-centric China.

The following section will outline South Africa's development choices since 1994 and argue South Africa is challenging some of the previously accepted 'Washington Consensus' principles. The analysis method introduced in Chapter 1 and applied in Chapter 2 will be utilised. Contrasts from China's policies as well as those from the 'Washington Consensus' will be emphasised.

Macroeconomic Discipline

Nicoli Nattrass and Jeremy Seekings explain the macroeconomic situation during the political transition, "Whatever the failings of the pre-1994 government, democratic South Africa did not inherit hyperinflation, severe indebtedness, or a massive external imbalance."[149] Like China's reformers, South Africa avoided the shackles of high national debt or runaway inflation and was in a strong position when drafting a new economic plan. The primary challenge of the day was more political, for the pressure to spend was rightly demanded. The imbalances between the black and white populations were arresting. Black income was one-tenth of the white population and nearly half of the labour force had no formal job. Housing, water, and education were equally disparate. Based on this disturbing evidence, left leaning economists suggested the economy could sustain aggressive redistribution and a strong interventionist government in order to repair the socio-economic gaps in the society. The ANC economic team dismissed these 'demand side' policies and followed a more conservative doctrine. Debt loads were still high and re-entering the global economy presented risks no one could accurately predict. Thus, pragmatic budgets were enforced.

Even as South Africa successfully transitioned throughout the 1990's and the economy generated more wealth and stability, policy makers remained unwilling to alter the before mentioned economic doctrines. Debt servicing always took precedence over social spending. *The Economist* agreed with the approach.

[148] Carmody, 261
[149] Nattrass and Seekings, 1998, 52

> Fiscal discipline has been exemplary: the government's budget deficit has been reduced from 9.1% of GDP in 1993 to an estimated 2.4% in 2003. Economic growth, which averaged a miserable 0.6% a year between 1981 and 1993, ran at a more respectable 2.8% a year between 1994 and 2002, outstripping population growth of 1.8%.[150]

Like China, exchange reserves have also been a key focus. South Africa's official foreign exchange reserves have been increased to over $15 Billion, more than four times the current short-term debt.[151]

Critics of GEAR's macro approach have justifiably remained though – anyone can cite the growing wealth disparity as evidence the model has failed. Disapproval has not solely been voiced from labour unions and the communist party either, even a United Nations (UN) report published in 2003 offered a strong stance. The *Financial Mail* summarised the divisive report, "The 290-page document says in essence that government's growth, employment & redistribution (Gear) policy is ill-directed and unable to end the cycle of poverty and racial inequality weighing down the country."[152]

Parallels with China's macroeconomic decisions are noticeable and both nations have chosen to follow the guidelines of the 'Washington Consensus'. Despite socioeconomic imbalances, fiscal restraint and aggressive inflation targeting have been unapologetically applied. As evidence the international community agrees with this approach, Investor Service Companies (e.g. Standard & Poor's) have consistently upgraded debt ratings for both China and South Africa. The obvious difference in the macroeconomic management of their development models is China has been successful in attracting foreign capital where South Africa is still searching for large investments. Yet, this divergence has causality beyond macro economic choices.

A Market Economy

The planners of the new South Africa inherited two distinct features that left a troubling legacy on the countries market economy. The ineptness of bureaucracies created during the apartheid regime was the first. South Africa never approached a centrally controlled economy as found in China, yet the abuse of the State and subsequent parastatals for political reasons was common. By way of example, bureaucracies were often utilised to ensure full employment for the minority, which allowed highly inefficient service delivery mechanisms to fester. Delivery problems and the inability of government agencies to spend their budgets were alarmingly common. RDP originally allocated large swaths of money to government organisations with the mission to extend and improve services, but much of the budget was never spent. Intense criticism followed and this

[150] *The Economist*, 15 January 2004
[151] Trevor A Manuel, South African Minister of Finance, 2005 Budget Speech to Parliament
[152] Honey, 2004

contributed to the ANC's switch to the more pro-market GEAR, just two years after the country's first free elections.

For the second, Apartheid isolated the economy and a highly monopolised marketplace consequently manifested. Domestic conglomerates won the market because international embargos forced companies to create essential goods previously imported. They also had available capital to buy MNC's assets, who were hastily exiting. Writing about South Africa's history, John Iliffe notes, "Although monopoly and oligopoly are commonplace in late-industrialising market economies, they have been so extreme in South Africa as to compel special attention."[153] He further supported his observation by calculating that four conglomerates accounted for 83% of the Johannesburg Stock Exchange in 1987. The key sectors of the economy – financial services, manufacturing, and mining - were essentially managed by these four organisations.[154] Hence, while South Africa was not China in the sense that state bureaucracies controlled most of the industrialised output, but hugely powerful (and protected) corporations dictated the nations supply.

Progress toward remedying these negative trends has found mixed success, but markets have been the drivers. Lester, Nel and Binns elaborate, "GEAR is an economic strategy which, like those of the late-twentieth-century global metropoles, rests on the assumption that markets are reliable, well-functioning institutions."[155] GEAR sought to reduce the state by encouraging privatisation, with the most noteworthy example being the partial sell of Telekom to international buyers. In addition, in line with the macroeconomic discipline, state bureaucracies and parastatals were never heavily capitalised, thus limiting the mismanagement and poor use of funds.

Ending the economic grip of the local conglomerates has been especially difficult. A modest, free market approach through the encouragement of small business development and lowering barriers for foreign companies to re-enter the market has produced some results. Small business growth has been notable and government-sponsored financial support continues. "Only 44% of people in the private sector were employed by SMMEs in 1995, but this number had risen to 52% in 2000 and 68% in 2002", according to the *Financial Mail*.[156] However, foreign firms have largely stayed away from South Africa and the economy remains heavily reliant on domestic activities. The United Nations Development Programme's (UNDP), "SA Human Development Report 2003"

[153] Iliffe, 1999, 97
[154] Ibid
[155] Lester et al, 320
[156] Crankshaw, 2004

analysis showed the domestic private sector accounts for 75% of total investment, 86% of employment and 80% of national income.[157]

At present, the ANC economic team, and notably Thabo Mbeki, have grown increasingly frustrated with their market led approach. Alternate plans have not been formally announced, but the State is again expanding. State expenditures have been increasing, or "surging" according to a leading South Africa financial publication.[158] Spending in 2005 is expected to be 28% of GDP, a 2% increase over four years.

Privatisation has also ceased. In 2001, privatisation was expected to generate R18.5Billion in proceeds for the state, but only R2.3 Billion was collected.[159] From *Business Today*, "The confirmation, from treasury director-general Lesetja Kganyago yesterday, underlines the radical shift that has taken place in official thinking on privatisation, as the former comerstone of SA's economic policy has fallen off government's agenda."[160] R3 Billion from privatisation was forecasted in 2004, however only R13 Million was raised. For now, privatisation has ended in all but name.

Now that state assets are no longer for sale, South African officials are hoping to mirror the success of China's SOE's-led infrastructure development. Powerful parastatals such as Transnet, Eskom, the Industrial Development Corporation (IDC) and Development Bank of Southern Africa (DBSA) have long found success in South Africa and across Africa. They are now receiving even more focus and funding. Mammoth sized planned projects include a R27 Billion investment in electricity delivery, port upgrades for Durban and Cape Town, and R5 Billion to improve Transnets locomotive and wagon fleets.[161] The communicated reason for these projects is to raise South Africa's global competitiveness, but expenditures are viewed pro-poor as well. Trevor Manuel explains in his 2005 Budget Speech to Parliament, "We need to press more urgently on the labour-absorbing potential of infrastructure and building programmes."

Clearly, a tide change against markets in favour of parastatals and bureaucracies to deliver for the poor has occurred over the last few years. Following the example set by China, South Africa is rejecting many of the ideas found in this tenet of the 'Washington Consensus' and is revitalizing the State.

[157] Honey, 2004
[158] Cobbet, 2005
[159] OECD, 2003, 283
[160] Rose, 2005
[161] Trevor Manuel's Budget Speech to Parliament, 2005, 18

Openness to the World

China and South Africa shared similar starting points when new economic models were assimilating. Both were stepping out of largely closed economies that had produced antiquated technology with inadequately skilled resources. Their populations were grossly divided along socio-economic lines and poverty was (and remains) the primary political concern. Globalisation and access to international markets were understood to be necessary, but strong political factions were highly sceptical of opening the economy.

For remedies, similar paths have been chosen with the distinction of South Africa being more aggressive. While China slowly utilised international institutions, South Africa quickly joined all significant bodies and led regionalisation projects such as the African Union (AU).[162] Both opened their economies and sought international players, but China limited activity to certain zones.

The management of Capital has been different though. Where China has maintained strict controls on domestic capital, South Africa has periodically allowed flows to exit the country. Compared to developed countries, South African capital has been monitored and guarded, but more relaxed when compared to China or other Asian models. South Africa has also freely floated the Rand and rarely intervened despite wild valuations. From Nicoli Nattrass and Jeremy Seekings writings, "Perhaps the most important point to be made is that the ANC, although not representing capital (except perhaps nascent African capital), is very responsive to the interests of capital."[163] In general, the South African government has been very pro- business with only slight restrictions on capital movements.

The glaring difference between China and South Africa's entrance into world markets has been outcomes. South Africa has not achieved strong economic returns through FDI, despite open policies. Therefore, the correctness of exposing the economy to global competition remains a strongly contested idea.

Where's the Growth - South Africa's Political Economy

A number of South Africa's political economy attributes have been discussed throughout this chapter, but the broader question of why South Africa's economy has not generated more wealth remains the prevalent dilemma. According to the principles of Western development thought, governments that open their economies, respect property rights and tightly manage their budgets

[162] As mentioned in Harry Stephan's essay, "The Scramble for Africa in the 21st Century", South Africa acceded to 70 multilateral treaties and joined more than 40 inter-governmental institutions after 1994.
[163] Nattrass and Seekings, 1998, 49

will be rewarded with flocks of global investors. "South Africa's post-Apartheid immersion within globalizing, late-capitalist political economy, has been accomplished through an insistence on government respect for the market and for property," as argued in *South Africa Past, Present and Future.*[164] However, GEAR's bet on foreign investment has never culminated while China's counter-'Washington Consensus' policies have generated large returns. The causes for these differences are numerous and not agreed upon, but some common assumptions exist.

Simple population size and geography explains much. While South Africa's population of 44 million creates a large market for foreign investors, this is a mere fraction when compared to China's roughly 1.3 Billion people. The endless potential of so many consumers has attracted foreign investors from all major western economies. South Africa also lies in an area considered risky by investors. The conflicts in central Africa and the isolation of Zimbabwe have created a region thought questionable for long-term capital investments. In contrast, the Asian and Indian Ocean economies have been leading global economic expansion for well over two decades.

China has also found great success leveraging foreign capital to create world-class manufacturing facilities staffed through extraordinarily cheap labour. Unregulated wages or workplace standards have allowed China's labour costs to fall below anything seen in the world economy. In South Africa, the ANC led government has not used this easy means to create growth. "Look at that guy hawking oranges," says James Lennox, head of the South African Chamber of Business. "If I was allowed to pay him what he would accept, I could create thousands of jobs."[165] The role of COSATU and other labour movements within the ANC has clearly affected worker policies. Many growing developing countries, most recently China, have ignored labour regulations and allowed low cost manufacturing to jump-start their economy. This has generated significant economic growth, but South Africa is unwilling to allow 'sweat shops' and other questionable business models to develop locally. Further, the collective memory of Apartheid will not allow the South African leadership to gamble with a low-cost labour strategy.

Finally, the ANC has built a 70% majority in the last election, but this does not transfer into an autocratic state such as China. The split alliance of the ANC prevents the consolidated implementation of a sole set of ideals and the democratic constitution insures local participation before decisions are made. China can implement policy even in the face of civil discourse, but South Africa politicians could never acquire such power.

[164] Lester et al, 322
[165] *The Economist*, 15 January 2004

South Africa's development path is consequently constrained by these variables. Ten years of seeking foreign investment has proven global investors are timid. Enticing manufacturing through low-cost labour is not possible due to political realities and, lastly, the democratic system does not support aggressive policy implementations. Hence, South Africa has been mired with modest economic gains although socio-economic progress cannot be made without significant increases.

Regional Efforts

China's ability to implement a mercantilist leaning development model within a liberal global framework is mainly attributed to one trait – scale. The potential of a large, relatively homogeneous market has trumped the many concerns investors and governments have voiced about China. South Africa's mid-tier economy is not as fortunate, but global and regional efforts have been pursued to both increase market size and consequently challenge the external forces applied by globalisation. The ANC, speaking through the *ANC Today* newsletter, recognises "that none of us, including our own country, can achieve sustained development outside the context of regional and African cooperation and integration."[166]

The more pronounced South African projects include the African Union (AU), the South African Development Community (SADC) and the South African Customs Union (SACU).[167] All of these commitments show the potential of creating larger markets and more secure political systems, but the timing of the benefits differ. The AU includes an enormous population, but the immediate economic benefits do not appear promising due to the brevity of interlacing such a large, extremely diverse region. SADC has size potential with 14 members and a 260 million-population base. A ratified free trade agreement is also expected in 2008 and the regions strategic location between the Indian Ocean economies and the America's suggests a central trading hub could be established. However, SADC is still an enormous body of land with political differences and persistent conflict. Envisioning SADC with widespread infrastructure, stability and prospering trade is a grand vision, but might be decades away.

SACU is the remaining project, and more interesting in the short-term. SACU, the oldest customs union in the world, consists of South Africa, Botswana, Lesotho, Namibia and Swaziland[168]. A new agreement was signed in 2002 reaffirming political and economic commitment to the project. While the population of the region (roughly 50 million people) does not elicit huge commercial investments, the importance of SACU is potential. This region is viewed as the significant

[166] Mbeki, 19 August 2005
[167] The Common Market for Eastern and Southern Africa (COMESA) is also important, but South Africa is not currently a member.
[168] Negotiations to add Mozambique are underway and perhaps Angola in the future

building block, or pilot, for the other regional plans mentioned.[169] The successful implementation of SACU could incent SADC and AU countries to invest more into broader regionalisation ventures. Therefore, SADC's importance is about demonstrating the prospect of a large African market working in concert.

Now that the new agreement has been ratified (after eight years of negotiation), the South African Customs Union (SACU) is currently pursuing Free Trade Agreements (FTA) with China, India and the United States. The United States negotiations have been occurring for over two years but an agreement has been stalled over SACU's reluctance with a complete opening of markets. SACU wants a phased, mercantilist approach to protect sensitive industries while the US has pushed for a faster liberalisation. In contrast, negotiations with India are more precise and will likely address specific sectors and not conclude with broad-sweeping liberalisation. Discussions with China are still early with a Free Trade Agreement being a contentious subject considering the competitive advantage China has with certain industries (e.g. textiles). A sector-by-sector agreement might be the ultimate outcome. Generally, SACU is aggressively seeking agreements and recognises large economies like China, India and the US might pursue agreements with other regions (e.g. central Africa) if terms cannot be met.

South Africa is the unquestioned leader of SACU, therefore it is not surprising the customs union is pursuing trade agreements with such persistence. SACU's negotiation stance also seems to fall along the lines of South Africa's development model where liberal methods are applied but mercantilist principles are in place to protect young and/or vulnerable industries. The importance of these negotiations should not be underestimated though, for South Africa has to broaden its market in order to compete with the other large trading blocks or countries. A successful SACU is only a small step toward a broader regional consolidation that will be needed to challenge mammoth economies like China.

Could South Africa Return East?

Modern South Africa and China have a short, but busy history. Official relations were not established until 1998, but high-level Chinese visits have been frequent over the last few years. These official trips included Vice President Hu Jintao (February 1999), Vice Premier Qian Qichen (June 1999), Li Peng, Chairman of the National People's Congress Standing Committee (November 1999), Premier Zhu Rongji (September 2002); and most significant, President Jiang Zemin (April 2002).

[169] McCarthy, 2003, 605

Diplomatic relations have reflected economic ones. Trade volume between China and South Africa has increased from R 9.3 billion in 1990 to R 23.3 billion in 2003. South Africa assumes 20% of the total trade volume between China and Africa, a large share considering South Africa has no oil fields. The quick ascension of Chinese imports to South Africa is especially pertinent. According to South Africa's Department of Trade and Industry, in 2002 China was South Africa's 18th highest export receiver, in 2003, China had risen to 8th. For imports, China was 5th in 2003, behind Japan, the United Kingdom, the United States and Germany.[170] The diplomatic and trade figures suggest an important relationship has already forged and it should only strengthen as China expands.

Beyond the diplomatic and economic ties, could China's development model travel to South Africa? The answer is both yes and no. Reviewing the 'Washington Consensus' framework used throughout this paper provides insight. South Africa and China's development models adhere to the same macroeconomic discipline. Both countries have opened their economies to global competition with the important exceptions of China still maintaining currency pegs and aggressive capital controls[171]. The real distinction comes when reviewing the market economy. China is steadfast with a state-led growth plan while South Africa is still searching for the right balance. South Africa aggressively experimented with a market approach but has recently realigned its development model back to the State. Over the last few years, parastatals have been recapitalized, privatisation has stopped, and infrastructure and social spending has been expanded. These changes should not be viewed as insignificant. Modern South Africa has always operated in a global economy hostile to far-reaching social welfare and large infrastructure programs. In order to stay competitive, developing countries were strongly encouraged to remain lean and flexible to market conditions.[172] South Africa is therefore unravelling fundamental principles not considered challengeable even a few years ago. Thus, from a development model perspective, South Africa is slowly accepting ideas championed by China and counter to the developed countries promoting 'Washington Consensus' tenants.

The important exception to this conclusion is a matter of South Africa's political economy. A complete implementation of China's success is simply impossible. South Africa does not have the market size or a willing political system to attract investment through ultra-cheap labour. The democratic constitution prevents the government from cramming through aggressive development projects and a common economic ideology could never be sold across the South African political spectrum. Hence, a complete adoption is not feasible for the future. South Africa

[170] South Africa's Merchandise Exports and Imports, South African Department of Trade and Industry (DTI), 2003
[171] China's recent revaluation of the Yuan to the US dollar shows potential for a free-floating currency, but this is far from certain.
[172] Lester et al, 321

is therefore quietly stepping away from the 'Washington Consensus' principles expressed through GEAR and is seeking a different development model leveraging the successes of China and the surrounding economies.

Conclusion – Cognitive Dissonance

Outlining the details of a country's development model can be overwhelming, but viewing the policies through broader International Political Economy (IPE) theory provides clarity. As introduced in Chapter 1, Liberalism, Mercantilism and Marxism all adequately explain some aspects of a countries development plan, but most current methods can be reduced to either liberal or mercantilist in nature. For powerful western economies, the answer is clear: liberal policies have generated enormous wealth for the global structure and therefore all countries should adjust tactics accordingly. However, the view from the developing world is starker and more complex. While openness to the global economy is nearly a universal axiom, weaker states are learning they must provide some counterweights to protect their economies. The arrival of China and the mercantilist economies surrounding the Indian Ocean demonstrate the potential of this new thinking. Thus, established development principles are being challenged and new mercantilist alternatives might help Africa rise from its despondent situation.

Much of this discussion is obviously tied to China's current grand experiment. A continued Chinese ascent would provide Africa needed flexibility and an increased global bargaining position. The optimists believe an economy passing the United States is feasible within two decades.[173] The pessimists are unimpressed by GDP growth and point to the coming political tempest; just as few observers foresaw the collapse of the Berlin Wall, China, and its authoritarian regime, will suffer a similar fate. Whatever the long-term outcome, Sino-African interests should increase exponentially in the coming years and this will further inflate China's influence in Africa. Increased trade and a scramble for African markets present a litany of new opportunities for the continent.

As the South African case study demonstrates, a development policy shift is already occurring in Africa, but differences from China are apparent. The unique blend of China's political economy has created unparalleled economic fruit, but Africa's situation does not allow for a complete replication of ideas. A number of academics and analysts have explained that South Africa is caught in a globalised economy not supportive of States seeking to equalize their societies. *South Africa: Past Present and Future* summarises this observation.

[173] Michael Power, an economist for Investec, offers the following plausible scenario to support China surpassing the US in twenty years. Assume the US economy grows at 3% p.a. (per anum) and China at 6.6% p.a. This alone would be nowhere near sufficient to close down the gap between the two countries. But now assume that China's Remnimbi appreciated by 300 percent – from 12 US cents a Remnimbi to 48 cents Remnimbi. (After the collapse of the last Bretton Woods agreement in 1973, the Japanese yen appreciated 338% in 23 years. 1 US Dollar in 1970 = ¥357; 1980 = ¥238; 990 = ¥144; 2000 = ¥102). In 2024, China's GDP at US$20 trillion would be a larger economy than the US at US$19.9 trillion.

> It (South Africa) did not enter some 'neutral' post-modern, post-industrial and post-apartheid arena in which it could transcend inherited inequalities and contract a totally revised political discourse and economic structure. Rather it remains inescapably embedded within a globalized, Western-dominated, capitalist system, which continues to actively produce inequalities.[174]

Perhaps this reality is changing. We appear to be witnessing a historical cognitive dissonance where the beginning signs of a new order are denied by larger powers, but a gradual change is unquestionably occurring. The extensive world system is not returning to its protectionist and mercantilist past, but unbridled liberalism is being challenged. Africa has taken notice and is finding opportunity within the previously rigid global framework. The motions of the international system are presenting the potential for a renewal. Ironically, riches and ideas are not arriving from the West, but from the reviving East, Africa's original trading partner.

[174] Lester, Alan, Nel Etienne, and Binns, Tony South Africa Past, Present and Future p. 322

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Figure 2: Chart from IMF report. James M.Boughton. Silent Revolution: The International Monetary Fund 1979 - 1989. 2001. The International Monetary Fund (IMF). Please see http://www.imf.org/external/pubs/ft/history/2001/ch01.pdf

Figure 3: Diagram created by author. Ideas from John Williamson, 'Did the Washington Consensus Fail', speech given to Institute for International Economics, http://www.iie.com/publications/papers/williamson1102.htm.

Figure 4: Chart created by author with data from World Development and Outlook 1820-2030: A Quantitative Perspective. Revised Note by Angus Maddison for Meeting of OECD Economics & Environment Directorates, June 25, 2004. Please see, http://www.eco.rug.nl/~Maddison/