Features

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Kiwi minister tests the water in Africa

New Zealand eyes Africa's potential and agricultural resources for mutual benefit

A worker checks equipment on a farm managed by New Zealand dairy export giant Fonterra Co-operative Group in Yutian County, Hebei Province around 150km south-east of Beijing in this file photo taken in March 2012. The dairy farm is part of a new international investment strategy by Fonterra that involves the building and operating of its own large-scale dairy farms. PHOTO: REUTERS

Peter Fabricius

NEW ZEALAND produces just 3 percent of the world's dairy goods, but it markets over a third of them. In that wide discrepancy lies much of the country's large potential for Africa, both as a partner but also as a model.

And it is now looking to realise that potential, for mutual benefit.

To do that, New Zealand foreign affairs minister Murray McCully has just completed a six-nation tour of southern Africa, visiting South Africa, Botswana, Namibia, Lesotho, Mauritius and Mozambique.

The tour is part of a drive by New Zealand to get to know Africa better, to do more business with it, and to drum up support for New Zealand's bid for a seat on the UN Security Council in 2015 and 2016.

McCully acknowledged that diplomatic relations with Africa had been "pretty thin" with embassies only in Pretoria and Cairo, as New Zealand had limited means and had been over-represented in Europe, because of its heritage.

Recently it added a third embassy to Ethiopia and the AU in Addis Ababa. "We're looking to step up our relations with Africa. We're a small country and we need to focus on the things we have a natural advantage in; and the biggest is agriculture. And a large proportion of the world's undeveloped agricultural resources are on this continent."

McCully said New Zealand had been used to thinking of itself as a country that produced goods, especially agricultural goods, at home and then exported them. But it had now run out of farmland and so its future lay in expanding agricultural partnerships with other countries, especially in Africa.

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"Our dairy sector is our big player. We market and trade over a third of the world's dairy products, but we only produce 3 percent of it" because of foreign partnerships.

The scope for such partnerships is huge; global demand for dairy produce is forecast to grow by 3 percent a year – equal to New Zealand's production – every year.

New Zealand is already developing huge dairy partnerships with China and Southeast Asia.

New Zealand was the only developed country with a free trade agreement with China, McCully said. And, despite initial fears of being swamped by cheap Chinese imports, the free trade had helped New Zealand narrow the trade gap to almost parity over five years.

It was the Chinese, in fact, who looked for a *quid pro quo* for allowing New Zealand dairy products duty-free into their markets. That came in the form of an agreement by New Zealand to invest in boosting their dairy sector.

McCully said New Zealand understood that South Africa and other African countries would expect the same. "And we accept that that's the deal."

Just as in Asia, growing African economies were expanding the middle class and, therefore, the demand for protein.

The other commercial potential New Zealand sees in Africa is exporting its renewable energy technology, which it has developed as a country that generates 77 percent of its electricity from renewable means.

As a small country, New Zealand did not have a huge aid budget, McCully said, spending about NZ$13 million (R99m) a year, mainly on scholarships for developing countries, including Africa on top of NZ$100m a year for UN humanitarian aid plus some further direct funding for aid to victims of famine in the Sahel and Horn of Africa.

But he and his officials pointed out that with its very liberal agricultural trade policy, New Zealand offered a better route to development through trade.

Politically, he said, New Zealand offered Africa an independent foreign policy and a fair deal. "We think our brand is about being fair-minded and good listeners."

He noted, for example, that New Zealand had parted company with its big neighbour Australia and most other Western governments by supporting Palestine's controversial bid for observer status at the UN last year.

"We ask countries to sit down and say, if you've got trouble in your neighbourhood, who do you want to have on the Security Council looking at that issue?

"And generally they want someone who will listen to them and deal with them in a fair-minded fashion."

McCully has visited South Africa twice before, for rugby. In 1995, he captained the Kiwi parliamentary rugby team which was victorious here, just before the All Blacks lost to the Springboks in the World Cup final. His experiences brought home to him the "the special bond" between the two countries forged by rugby.

"We haven't done enough with that and need to leverage more off it," he said, noting that that was one of the important key performance indicators he had given to the new High Commissioner to South Africa, Richard Mann.

China's potential won't happen on a spreadsheet

George Magnus

Paul Krugman, professor of international trade and economics at Princeton University and Nobel Prize-winning economist, during an interview in New York. PHOTO: BLOOMBERG

CHINA'S economy has grown rapidly under the investment and direction of the state, which put workers and resources to productive use compared with pre-industrial China. But sooner or later, the state is going to hit a wall and growth will slow to a more typical pace – or the state will have to make major reforms and get out of the way.

In a three-part series, George Magnus, an independent economist and an adviser to UBS and other investment banks, analyses how China can manage this shift. Part I goes as follows:

Once upon a time, 1994 to be precise, Paul Krugman wrote a seminal article for foreign affairs entitled "The Myth of Asia's Miracle".

China has reached the end of extrapolation. Its considerable economic potential won't happen on a spreadsheet.

The purpose of his essay was to explain that there was nothing about what the World Bank had previously labelled the "Asian miracle" that couldn't be explained in a straightforward manner.

The "miracle" – albeit well executed – amounted to little more than organisational and institutional efforts to deploy physical labour and capital to great economic effect.

But once the limits of these efforts had been exploited, growth would slow down. In fact, Krugman argued, it would become quite pedestrian in the absence of new innovation- and efficiency-led productivity growth.

His analysis is as true today as it was then. In addition, today we also benefit from a voluminous literature exploring the significance of robust, enabling and inclusive institutions to sustainable growth.

We know a lot more about the tendency for most middle-income countries to fall into a so-called "middle-income trap". This typically happens when per capita income reaches about $15 000 (R135 079) in today's terms.

At the time of Krugman's writing in 1994, China was still a low-income country. It was not yet a decade into the organisational transformation that was courageously unleashed by Deng Xiaoping's reforms in the late 1980s, in the face of entrenched opposition and resistance.

The rest, as they say, is history. China's per capita income has more than tripled to almost $6 000. It is on course to triple again by the middle of the 2020s. By then, China's gross domestic product (GDP) will have overtaken that of the US.

It so happens that these numbers are the key exhibits of an industry of hyperbole that does not just go on to predict the dominance of China in the global system. (There is an industry of hyperbole that predicts the dominance of China in the global system.)

It also heralds the ascendancy of Chinese consumer markets, the explosion of Chinese global companies and brands, the replacement of the US dollar by the yuan as the world's major reserve currency and much else.

But, in my view, this hype-sterism is taking extrapolation too far.

It is undeniable that trend growth in China is slowing down. That statement is true even though measures taken in 2012 to boost construction, infrastructure and already feisty credit creation have succeeded in lifting the tempo of China's economic growth from 6 percent in early 2012 back to 8 percent.

Slowing economic growth in China should come as no surprise to anyone. Many transformational achievements have either been fully exploited or now show only limited potential.

These newfound "limits of growth" include:

- The harvesting of the demographic dividend (that is the expansion of the working age population and falling child dependency)
- Rural-urban labour transfer
- High secondary school enrollment rates and standards
- High levels of savings and investment, and
- The wider technological frontier created by openness to foreign direct investment.

The biggest growth driver in China in the last decade has not been its fabled export sector; rather it was a surge in capital investment to an unprecedented 50 percent of GDP.

More recently, the driver has been a growing dependence on credit creation to finance investment and economic growth.

China's growth model has created interrelated imbalances that will soon slow growth or undermine it.

It isn't as though Chinese consumers have been shy in contributing to growth.

For many years, real personal consumption has been growing by about 8 percent per year.

The consumption and wage shares of national income have fallen over the last decade to around 35 percent and 40 percent, respectively, because of the extreme push to expand capital investment.

China's growth model has created a number of interrelated imbalances that will soon retard growth or undermine it. These include:

- The investment- and credit-centric nature of growth,
- The still strong role played by state-owned enterprises,
- A weak services sector
- Financial repression (read: artificially low interest rates) that punishes households
- High-income inequality, and
- Suppressed factor prices (that is, of land, capital, money and energy)

Without radical reforms, China could only sustain an 8 percent growth rate at the risk of exacerbating these imbalances, resulting in probably severe economic and social disruption.

There was nothing about what the World Bank labelled the "Asian miracle" that was a miracle.

Rebalancing the investment and consumption shares of GDP is going to happen regardless. The major question is how it happens.

Will it occur in the context of a reform-led, steady slowdown to about 5 percent per annum?

Or will it be the result of a more disruptive slowdown as a result of an investment and credit bust?

To avoid both a hard landing in the next few years and a middle-income trap over the medium term, many analysts and commentators, including in China, call for changes. These concern:

- The role of government in the economy
- Encouragement of private enterprise and innovation
- Adoption of the rule of law and an independent judicial system, financial liberalisation
- Stronger service industries and tertiary education, and
- More market determined prices for land, resources and capital

Further, China's leaders will have to pursue vigorous programmes to lower income and social inequality. And they need to widen access to primary health care and insurance, and pension income.

The urbanisation of the country will have to be matched by the urbanisation of people. This especially implies reform of the *hukou* system of alien registration.

Under the current system, China's 250 million urban migrants are deprived of basic social and economic rights and better living conditions.

The solutions are not mysterious or beyond reach. The problem is that implementing them requires strong political engagement and leadership.

The test lies immediately ahead for China's new leaders, soon after they assume their positions formally – and much sooner than they would wish for.

The highly regarded Caixin magazine has recently urged for a shift away from the dominance of the state in the economy.

It argued that the heavy state involvement stifles competition, distorts markets and encourages rent seeking, corruption, the abuse of power and extremes of income inequality.

But is this a political bridge too far, even for the renowned pragmatism of the Chinese Communist Party? Some in Beijing debate openly the fate of the USSR, which opened up to radical reforms in 1985, and collapsed four years later.

But without reforms, China's economic development path cannot be sustained, since its imbalances will simply worsen.

To stay on track, China will have to meet the demanding standards of smarter growth, social consent, a cleaner environment, a rapidly ageing population and economic stability over the coming decade.

To achieve that, China will have to reboot its economic model. This includes the implementation of widespread reforms that will be costly and may be incompatible with the primacy of the party.

China's economic potential is considerable, but it won't happen on a spreadsheet. China has reached the end of extrapolation.

Editor's Note: This is the first of a three-part series. Read Part II next week. This article is provided as a courtesy by The Globalist (www.theglobalist.com), the daily online magazine on the global economy, politics and culture.