

CHINA, JAPAN, INDIA AND THE EAST AFRICA BLUE ECONOMY

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EXECUTIVE SUMMARY

East Africa's coastal states are attracting increasing attention from global economic powers, not only for the opportunities within these economies themselves, but also for the access they provide through transport corridors to landlocked states in the African hinterland. This engagement is reflected in broader regional economic programmes such as China's One Belt One Road Initiative and Japan and India's Asia Africa Growth Corridor. There are significant opportunities related to the development of trade and infrastructure within the East African Blue Economy, but this will require addressing trade imbalances and strengthening governance to ensure that investments contribute to inclusive and sustainable development.

INTRODUCTION

The period following the global recession in 2008 has seen a marked shift in the dynamics of the international political economy, characterised in part by geopolitical instability, falling commodity prices and slow growth in developed nations. Strong growth off a low base was buoyed by strong commodity prices preceding the recession. The shock of the global downturn, and subsequent fall in commodity prices, have impacted negatively on Africa's resource economies. Nonetheless, a number of developing countries have proved resilient to economic shocks. In general, the post-recession period has seen larger economies lagging (except in Asia) and renewed dynamism in many comparatively smaller economies. Post-2008, China, Japan and India have

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emerged as key investors in certain African regions. East Africa, in particular, has become an important (destination for foreign investment) growth pole.

This paper examines the role of China, Japan and India in East African development, focusing specifically on Kenya and Tanzania. Of particular concern is the regional Blue Economy, which encompasses economic, social and environmental concerns related to maritime industries and, according to the approach adopted by the African Union, also inland water bodies. The Blue Economy, however, is embedded within the broader political and economic context, so that the discussion on maritime trade and port infrastructure leads to broader consideration of infrastructure investments in relation to trade corridors that extend far inland. The paper also considers the wider Indian Ocean region, which is a key economic and geostrategic domain of interest for regional countries as well as major powers outside the region. The paper is divided into three sections. The first analyses the recent economic performance of Ethiopia, Kenya, Tanzania, Rwanda and Uganda. The second discusses existing Chinese, Japanese and Indian engagement (both economic and political) with the East African region. This includes a discussion on the ambitions of these nations, with a particular focus on China's [One Belt One Road \(OBOR\)](#) initiative and the Indian-Japanese [Asia Africa Growth Corridor \(AAGC\)](#). The third section examines the activities of China, Japan and India in Tanzania and Kenya with a specific focus on their investments in infrastructure and energy. It is argued that increased Japanese and Indian investment is driven not only by immediate economic interests, but also concerns around the perceived Chinese dominance in Africa.

RECENT ECONOMIC PERFORMANCE OF EAST AFRICAN NATIONS

Within the East Africa growth story, Kenya and Tanzania play a crucial role. These economies are not only among the larger fast-growing players in the region, but also serve as gateways to Indian Ocean trade for land-locked countries. In Kenya, the port city of Mombasa is a crucial node in the Northern Corridor, linking the eastern Democratic Republic of Congo (DRC), Rwanda, Burundi and Uganda to the coast. In Tanzania, the port city of Dar es Salaam anchors the Central Corridor, which also connects with eastern DRC, Rwanda and Burundi. Other landlocked countries like South Sudan and Ethiopia rely on Kenya for access to maritime trade. Similarly, Zambia relies on Tanzania for port access. Kenya and Tanzania are therefore crucial to the long-term development prospects of the region. However, the infrastructure quality in both countries remains poor.

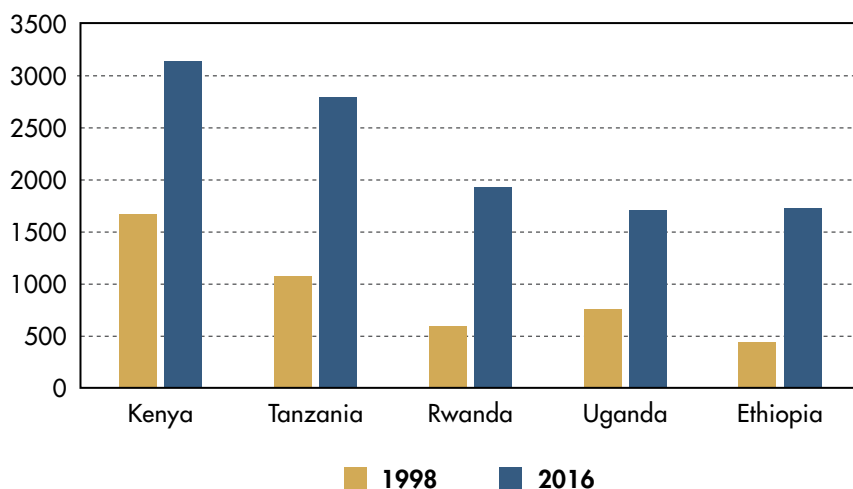
The September 2016 McKinsey Global Institute Report, '[Lions on the Move II](#)',¹ has divided African countries into three categories based on economic performance and political stability. 'Stable growers' represent countries that have achieved both relatively high levels of economic growth (a 5.8% yearly increase in gross domestic product [GDP] between 2010-2015) and remain reasonably stable. Countries included in this category are: Kenya, Tanzania, Uganda, Rwanda, Botswana, Senegal and Morocco. The other categories are 'vulnerable' and 'slow' growers.

The McKinsey report cites impressive economic growth rates as one cause of optimism. It further argues that Africa's greatest potential assets are its rapidly expanding youth population and high rates of urbanisation. As the working populations of China and India age, the demographics will work in Africa's favour.

Therefore, according to McKinsey, it is reasonable to expect countries in the ‘stable growers’ category to continue delivering economic growth and increasing per capita income.² Caution is warranted, however, in that this ‘youth bulge’ carries downside instability risks if employment opportunities fail to materialise. This is especially true in the context of ‘premature deindustrialisation’, in which developing countries find increasingly fewer industrialisation opportunities at far lower levels of income per capita compared to the experience of early industrialisers.³

The figures below illustrate development progress in Ethiopia, Rwanda, Kenya, Uganda and Tanzania over the last two decades.

FIGURE 1 GDP PER CAPITA GROWTH, PPP (CONSTANT 2011 INTERNATIONAL \$), 1998 VS 2016



Source: World Bank, ‘World Development Indicators’, <http://databank.worldbank.org/data/source/world-development-indicators>, accessed 11 June 2018

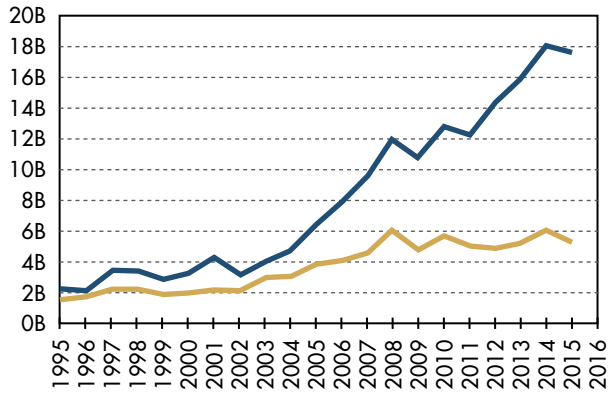
As Figure 1 one shows, since 1998 GDP per capita (expressed in terms of constant 2011 purchasing power parity) has risen sharply in all five countries tabulated. Kenya leads by a significant margin, with the latest (2016) GDP per capita figure at \$3,156. Ethiopia lags at \$1,734, though it has seen the quickest improvement off a low base.

Real per capita GDP growth has driven increasing import purchasing power. Figure 2 illustrates the growth in imports and exports for each country from 1995 to 2016.

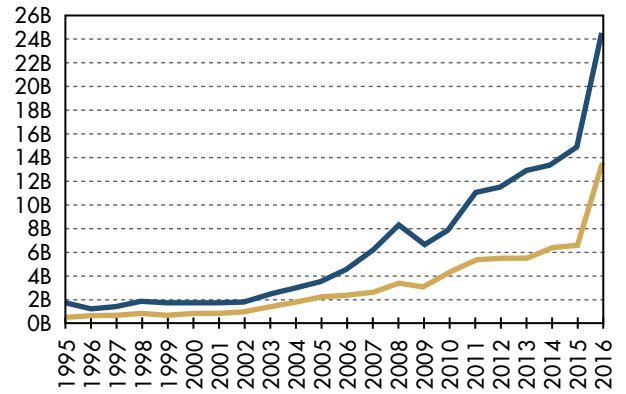
While GDP per capita growth has driven import purchasing power growth, the increasing trade imbalance in all these countries entails downside risks. Exports are still heavily dependent on natural resources in all cases. Exporting relatively low-value products and relying extensively on imported refined petroleum (except in Kenya) is likely to limit competitiveness. The lack of diversity in the export basket is a major component of economic complexity measures, which is proving to be a robust predictor of future development and inequality (or lack thereof).⁴

FIGURE 2 TRADE BALANCE PER COUNTRY, 1995 TO 2016 (TRADE IN \$/YEARS)

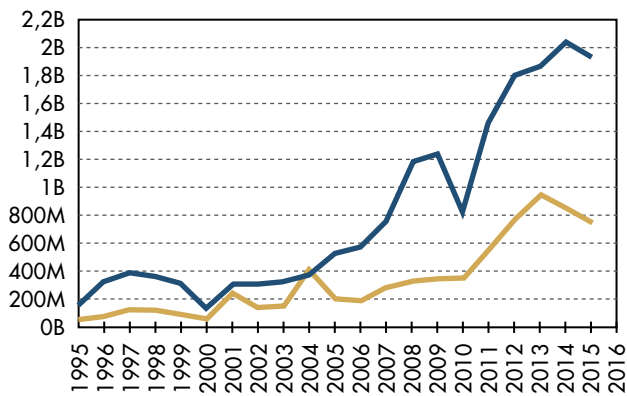
KENYA



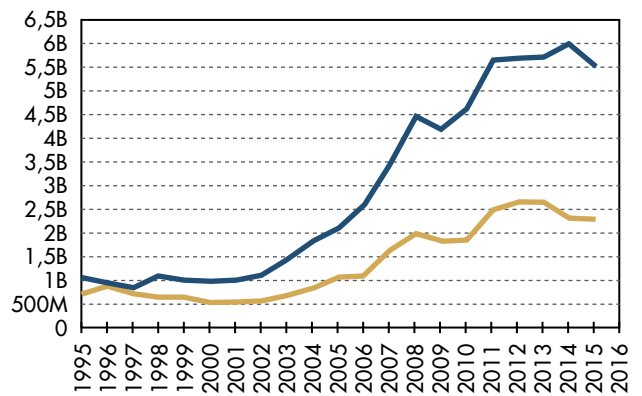
TANZANIA



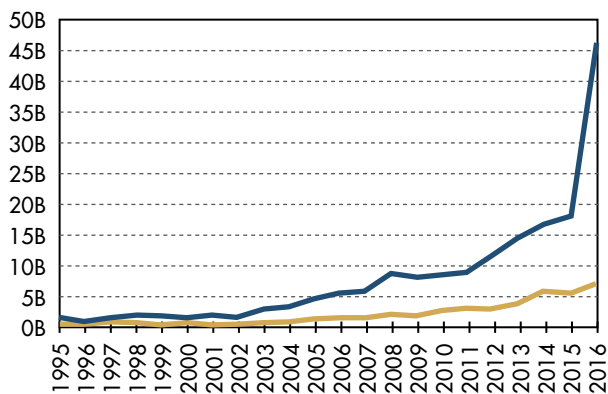
RWANDA



UGANDA



ETHIOPIA

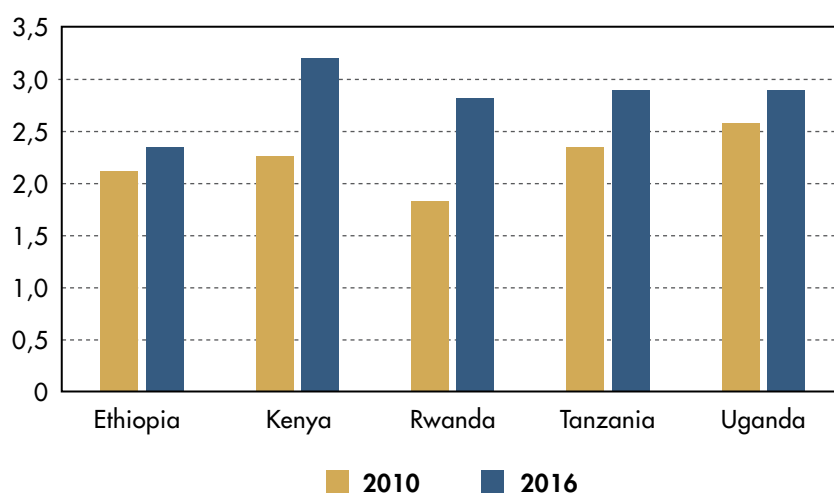


— Exports — Imports

Source: Simoes A, 'The Observatory of Economic Complexity', (Attribution-ShareAlike 3.0 Unported (CC BY-SA 3.0), <https://atlas.media.mit.edu/en/>, accessed 11 June 2018).

Further constraining the growth potential of many African countries is a weak infrastructure system, as illustrated in Figure 3. Poor infrastructure linkages, combined with a lack of complementary tradeable products, curtail opportunities for regional integration. Unless the required investment is allocated and high-quality infrastructure built, not only will regional integration be delayed, but the long-run growth prospects for these economies will be undermined. The latest [Infrastructure Consortium for Africa](#) report notes that African countries may require anywhere between \$174 billion (on current trends) and \$240 billion (to match the performance of best-performing peers) annually to 2040 to meet its infrastructure needs.⁵

FIGURE 3 LOGISTICS PERFORMANCE INDEX: QUALITY OF TRADE AND TRANSPORT-RELATED INFRASTRUCTURE (1=LOW TO 5=HIGH), 2010 VS 2016



Source: World Bank, 'World Development Indicators', <http://databank.worldbank.org/data/source/world-development-indicators>, accessed 11 June 2018

While the listed countries have recorded notable improvements in living standards, they remain some of the poorest countries in the world. To build the infrastructure projects needed to support the increase in transported goods, they will require extensive external funding and support. Some of the most enthusiastic investors in East African infrastructure have been China and Japan. India, while not as heavily invested, has also expressed an interest in expanding its engagement in the region.

CURRENT CHINESE, JAPANESE AND INDIAN ENGAGEMENT WITH AFRICA

The 1990s saw a significant expansion of China's economic engagement in Africa. Chinese demand for minerals drove investment in resource sectors throughout the 1990s and early 2000s, but Chinese investment and trade also include manufacturing and agricultural goods, as well as significant infrastructure investments. Resources continue to dominate Chinese trade relations with the continent. In 2000, the Forum on China-Africa Cooperation (FOCAC) was established as an important

platform to promote strengthened economic and diplomatic relations between China and Africa. This coincided with a broader ‘going out’ strategy, announced in 2000, that saw China emphasise international investment and trade.⁶

By 2015 trade between China and Africa totalled \$179 billion, with pledges to increase this to \$400 billion by 2020.⁷ FOCAC has since grown beyond economic diplomacy to include multilateral support on a number of fronts.

As with China, ‘resource diplomacy’ has been an important element of Japan’s engagement with Africa. The Tokyo International Conference on Africa’s Development (TICAD), established in 1993, has since served as a key forum to promote cooperation. Aid and technology transfer have also been important elements of this relationship. TICAD’s initial purpose was to bring Western aid donors and African aid recipients together, as well as bringing together relevant partners to reduce African debt and reverse the ‘lost decade’ of the 1980s. The second purpose of TICAD sought to boost African development by using Asian models of development in an African context. Despite Japan taking a relatively early interest in Africa, the country’s trade and investment statistics lag far behind China’s. In 2015, total Japanese foreign direct investment totalled just \$1.24 billion, while Japan’s total bilateral trade with Africa is valued at \$24 billion.⁸ In 2016 TICAD was for the first time hosted in Africa (past conferences have been hosted in Japan), possibly indicating a renewed commitment from Japan to deepen political and economic ties with the continent. At this conference, Japan pledged an additional \$30 billion in investment to Africa over the next three years. At least \$10 billion of the pledge would be committed to infrastructure development. This \$30 billion is in addition to the \$32 billion in investments that Japan pledged over a nine-year period at the 2013 TICAD.⁹

Though India has strong historic ties with Africa, in particular the East African region, Africa has only recently been prioritised in Indian foreign policy. The India-Africa Business Forum was established as recently as 2010. Despite this late engagement, bilateral India-Africa trade has jumped from \$5.3 billion in 2001, to \$75 billion in 2014.¹⁰ However, just six countries – Nigeria, South Africa, Angola, Egypt, Algeria and Morocco – constitute 89% of African exports to India.¹¹ Moreover, the trade profile is similar to other major economies, with a strong focus on mineral and energy resources.

CHINA, INDIA AND JAPAN: EXPANDING TRADE AND INVESTMENT IN KENYA AND TANZANIA

The rise of emerging powers in the Indo-Pacific region over the course of the 20th and 21st centuries represents a fundamental shift in the global balance of power. More specifically, the recent rise of India and China has shaped, and will continue to shape, geopolitics in the region.

India is set on strengthening its power in the Indian Ocean, yet it must contend with the proximity and economic power of China. The Indian economy is significantly smaller than those of China and Japan. Despite the gaps in economic and military size, India and Japan retain ambitious economic, political, military and diplomatic goals – both within and beyond their immediate zones of influence. This geostrategic positioning shapes the engagement of these three powers with

the East African region. In the realm of security, Djibouti already plays host to both a Chinese and a Japanese military base. Moreover, China, India and Japan have unveiled ambitious economic schemes that include the East African region and, via transport corridors, extend further into central Africa. Of particular importance is the OBOR initiative, and Japan and India's recently launched AAGC. Both initiatives will see the importance of East Africa heightened. Kenya will serve as a key component of the new maritime silk road for the OBOR initiative, while Tanzania stands to benefit from Chinese infrastructure investments.

The AAGC foresees a significant strengthening of Japan and India's engagement in East Africa. There are four main components of the programme: development and cooperation projects; quality infrastructure and institutional connectivity; capacity and skill enhancement; and building people-to-people relationships. Since the AAGC was only launched in 2017, progress in achieving these four core components has been limited. Nevertheless, the statement of intent from India and Japan is clear: both countries want to increase their roles and influence in the Indo-Pacific region.

Despite the OBOR and AAGC initiatives being relatively recent, there is already tangible evidence of increased Chinese, Japanese and Indian activity in Tanzania and Kenya. The biggest investments that China and Japan have been making in Africa are infrastructure-orientated. Japanese investment in the Kenyan port of Mombasa is representative of the projects that are strategically important to Asian partners.

Mombasa, in particular, has been a focal point of promised Japanese investment, having received up to \$500 million. The upgrades to Mombasa's port have hitherto proceeded in two phases (with an envisioned total of three) – in both phase I and phase II, the Japanese government has provided vital investment. Phase I of the renovations was completed in February 2016. During this phase, the Kipevu Container Terminal was constructed, which added 550 000 twenty-foot-equivalent-units (TEUs) to Mombasa's container capacity; before the improvements the port had a capacity of 1.1 million TEUs. Phase II of the operation is expected to add a further 450, 000 TEUs. The second phase of the project was enabled by a \$340 million loan from Japan. Once all three phases are completed, the capacity of Mombasa's port will have increased by over one million TEUs.¹² In the first half of 2017, the Kenyan Port Authority reported that Mombasa port recorded a 12% increase in cargo traffic, thereby demonstrating the outcome of a higher TEU capacity.¹³

The Chinese have also taken an interest in the city. The Chinese government invested \$4 billion in a 600 km railway line connecting Mombasa and Nairobi, of which some 90% has been financed by China Exim Bank.¹⁴ It is expected that up to 22 million tonnes of cargo will be transported along this railway each year. The project was completed in May 2017, 18 months ahead of schedule.

China's main project in Kenya is, however, far grander in ambition. In 2014, the Kenyan Port Authority and the China Communications Construction Company (CCCC) reached an agreement for the construction of a new deep-water port at Lamu. The port represents only one part of a far larger infrastructure investment programme, the 'Lamu Port-South Sudan-Ethiopia Transport' (LAPSSET) Corridor.

Landlocked Ethiopia and South Sudan will benefit from access to Lamu Port via the transport corridor. A total of 32 berths, are to be constructed, with the cost totalling \$3.5 billion. The first three berths are being constructed by the CCCC, with \$689 million being provided by the Kenyan government. The port is expected to begin operations in 2020; with the CCCC expecting to complete the first berth of the port in mid-2018.¹⁵ The total cost of the LAPSET investment programme is expected to be \$25.5 billion, exceeding the cost of Mombasa-Nairobi rail project by a large margin.

Chinese investment in railway projects has proliferated across the entire East African and Great Lakes Region. In 2018 the China Railway Group and the China Civil Engineering Construction Corporation completed a \$4 billion railway line connecting Ethiopia to Djibouti. With more than 95% of Ethiopian trade passing through Djibouti, the construction of the railway is vital to fulfilling Ethiopia's growing need for imported goods. By 2025, the railway is anticipated to haul 24.9 million tonnes of freight.¹⁶

While Tanzania is not formally a part of OBOR, this has not prevented China from making extensive investment in Tanzania's infrastructure. As with the construction of Lamu Port in Kenya, China is assisting in building a new port at Bagamoyo. In 2017, after years of delay, the government of Tanzania announced the revival of the project, with the port to be finished by 2021. Linked to Bagamoyo Port will be a special economic zone (SEZ); once both of these projects are completed, the Bagamoyo SEZ is anticipated to attract over 700 industries. The total cost of both the port and the SEZ will be \$10 billion.¹⁷

The main port in Dar es Salaam also stands to benefit from Chinese investment. In 2017 the Tanzanian government signed a \$154 million contract with the state-run China Harbour Engineering Company to expand the port in Dar es Salaam.¹⁸ As Tanzania wants to expand its container throughput to 28 million tonnes per year by 2020, the upgrades at Dar es Salaam and the construction of Bagamoyo Port will help to achieve this.

In 2015 the Tanzanian government announced that Chinese rail companies had been awarded contracts valued at \$9 billion. A consortium of Chinese companies, led by Chinese Railway Materials, were tasked with building a 2,561 km standard gauge railway connecting Dar es Salaam to Tanzania's land-locked neighbours. This project accounted for \$7.6 billion of the contract. Another agreement, comprising the remaining \$1.4 billion, was signed with the China Railway No. 2 Engineering Group for the building of a railway line to the southern port of Mtwara.¹⁹

Japan has also been investing in Tanzanian infrastructure. In 2013, six flyovers were constructed to ease traffic congestion in Dar es Salaam at a cost of \$32.6 million. In the same year, Japan pledged \$12 million to The Project for Rural Water Supply in the Tabora Region, which supplied fresh water to 40,000 people.²⁰ In 2018, the Japan International Cooperation Agency provided Tanzania with \$34.5 million for phase II of the widening of the New Bagamoyo Road – to improve the efficiency of goods distribution. Japan is also financing another lane widening initiative: the 12.9km stretch between Mwenje junction and Tegeta junction will be upgraded to four lanes at a cost of \$44.3 million.²¹

Indian investment in Tanzania and Kenya is substantially lower than Chinese and Japanese investment. From 2008-2016, Africa secured 21% of total Indian foreign direct investment (FDI). However, Mauritius received 95.7% of this 21%. From 1996-2017, the East African Community (EAC) received only 0.5% of India's total FDI outflow to Africa, with Kenya and Tanzania each receiving a share of 0.1% of India's total investment.²²

Although only a small percentage of overall Indian investment, Kenya and Tanzania still receive the lion's share designated for the EAC. From 2007-2016, Kenya received 54.1% of EAC FDI, making it the biggest recipient of Indian FDI designated for East Africa. Tanzania received 21.7%, making it the second largest beneficiary. In terms of numbers, through 2007-2016, Kenya received \$2.1 billion in FDI. Most of these investments were directed towards the energy (coal, oil and natural gas), communication and manufacturing sectors.²³

From 2007–2016, Tanzania received a total \$829 million in FDI from India; the tourism industry received the highest percentage. The manufacturing sector has also been a primary recipient, receiving a total of 26.4%. Indian firms, as with many other firms from Japan and China, have invested heavily in the extractive industries. With the discovery of offshore natural gas, Larsen & Toubro Ltd. (an Indian registered company) constructed a \$100 million gas-processing plant and pipeline.²⁴

TRADE RELATIONS

In 2016 at least 66% of Kenya's export basket to China was in raw materials: 42% titanium ore products and a further 24% comprising niobium, tantalum, vanadium and zirconium ore. Its imports from China in the same year were highly diversified, presenting a significant bilateral trade imbalance. Forty two percent of Tanzania's exports to China were precious metal ore (mostly gold) and 24% in oily seeds.²⁵

Kenya's exports to Japan were relatively diversified but still heavily resource-orientated, with titanium ore accounting for 20%, cut flowers 18%, coffee 11% and tea another 11%. It imported cars (42%), delivery trucks (20%) and hot-rolled iron (13%). In the same year, Tanzania exported precious metal ore (32%), copper ore (28%), and coffee (16%), followed by oily seeds (9.4%) and raw tobacco (9%) to Japan. As with Kenya, its imports comprised mostly cars (41%), hot-rolled iron (13%) and delivery trucks (10%).²⁶

Kenya's exports to India are mostly dried legumes (46%) with another 16% in carbonates. Imports from India are mostly (40%) in refined petroleum and packaged medicaments (12%). Tanzania's imports from India are also predominantly refined petroleum products (47%). Its export basket to India is slightly more diversified, with gold accounting for 33%, dried legumes 24%, and coconuts, brazil nuts and cashews a further 24%.²⁷ Again, however, the export basket is heavily weighted towards raw materials.

The overall picture that emerges is one of large trade imbalances between the two East African nations of Kenya and Tanzania, and its Asian trade partners China, India and Japan, as illustrated in Table 1. The value difference is explained by the fact that the African countries are exporting raw materials and importing high-value finished products (or refined petroleum) from their Asian counterparts.

TABLE 1 TRADE FLOWS BETWEEN CHINA, INDIA AND JAPAN; AND KENYA AND TANZANIA, 2016

	Imports			Exports		
	China	India	Japan	China	India	Japan
Kenya	\$5.59bn	\$2.46bn	\$744m	\$89.9m	\$117m	\$54m
Tanzania	\$3.95bn	\$1.89bn	\$373m	\$419m	\$856m	\$235m

Source: Simoes A, 'The Observatory of Economic Complexity', <https://atlas.media.mit.edu/en/>, accessed 11 June 2018.

CONCLUSION

The East African Blue Economy is attracting significant attention from global economic powers. This paper has focused on only three players, China, Japan and India. Each of these countries has significant geostrategic and economic ambition in the broader Indo-Pacific region, including the East African seaboard. Critically, East Africa's coastal countries are important not just in their own right, but also through their role as transport nodes linking Indian Ocean trade routes with the African interior. The review of investment and trade relationships has highlighted the deep and growing engagement of China, Japan and India in Kenya and Tanzania specifically. As this relationship deepens geostrategic competition may become more overt, though any speculation around overt conflict is certainly premature. To date, Kenya and Tanzania have been able to engage all three of these global powers, as well as others, without being pushed to 'pick sides'. There are significant opportunities for the region as it seeks to expand its infrastructure and trade, yet with the increase in investment interest and the launch of various mega-projects there is a concomitant need for improved governance and political decision making to ensure that the benefits of such projects contribute to broader development and that environmental sustainability is not undermined.

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ACKNOWLEDGEMENT

The Governance of Africa's Resources Programme (GARP) is funded by the Norwegian Ministry of Foreign Affairs. SAIIA gratefully acknowledges this support.

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JULY 2018

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