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INDIAN COMPANIES IN AFRICA LEVERAGING COMMERCE SYSTEMS

— REFERENCE CASES OF "MAKE IN AFRICA"—

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SUMMARY

- Indian companies are investing in various industries in Africa. A closer look at the manufacturing industry investments show that companies typically enter a market aiming for exports to third markets by leveraging the preferential tariffs EU and US commerce systems or other trading blocs and schemes provide.

- Reflecting the labor costs and education level in African countries, Indian companies' investments within the manufacturing industry are concentrated in light industries. In addition, although the African manufacturing industry does not have strong brand recognition, business opportunities can be expected through contract manufacturing for European and US companies, and in other areas.

- At present, Japanese companies do not have a strong interest in the African manufacturing industry, but an increasing number of companies are looking to the region with interest via India. Meanwhile, a new African continental commerce bloc is scheduled to begin operating. When Japanese companies start to consider horizontal specialization via Africa, it may be helpful for them to look at how Indian companies are leveraging the commerce systems in their strategies to expand into Africa.

1. INTRODUCTION

In general, Africa is familiar to Indian people because of the region's geographical proximity to their own country and the long history of interaction between the two regions. According to literature written around the 1st century about Indian Ocean trade, merchants in western India had already crossed the sea to trade with eastern Africa by that time. During the colonial era, under the UK's drive to develop the eastern Africa region, many Indians were mobilized for such as building railways, or working as seasonal laborers. In some cases, those Indians settled in the region and their dependent family members relocated to join them. At present, there are approximately 2.63 million African citizens of Indian descent, who are economically and locally influential and have built a network with India. It is because of this affinity with Africa that Indian companies have been able to pursue diverse business interests in African countries.

An executive of the Indian conglomerate Hinduja noted that because the political and economic situations differ from one African country to another, the company adapts its investment to be consistent with the degree of development in each host country. This is embodied by Indian companies making inroads to African markets with a uniquely intuitive approach, which Japanese companies have not demonstrated. The African continent consists of 54 countries and has a population of approximately 1.3 billion, and it is perhaps quite revealing that the countries of the region are not perceived collectively "Africa" in a bunch.

In the past, Japanese companies viewed Africa as a place of business from the perspectives of "Africa and ODA," and "Africa and Resources," which in both cases involved infrastructure development, and "Africa and

Markets," which centered on imports and sales. More recently, "Africa and the Digital Economy" has been grabbing the attention of Japanese companies as a business platform for providing solutions to social issues. However, Japanese companies do not have a strong interest in Africa in the context of "Africa and Factories" seemingly because the setting up of factories in Africa tends to be associated with a high risk, as well as the successive withdrawal of companies from the region owing to political instability and other reasons. Some Indian companies, on the other hand, have made forays into the "Africa and Factories" business and are worth noting for having established a presence to a certain degree in the local markets. In general, African countries are said to be unsuitable for the manufacturing industry because of high labor costs and low education levels, but investment in the manufacturing industry may be feasible depending on the strategy, as illustrated by the examples of Indian companies described later in this report.

2. OVERVIEW OF INDIA'S FDI IN AFRICA

Indian companies are investing in various industries in Africa. The Reserve Bank of India publishes India's bilateral foreign direct investment (FDI) statistics, tabulated by country and industry, as shown in Figure 1. The statistics indicate that Indian companies have been investing in all categories of industries in African countries in these years: a cumulative total of USD 13.8 billion in 36 out of 54 African countries. However, investments in Mauritius, at USD 12.9 billion, account for more than 90% of the total. As the country is a tax haven, it is thought that most of the investments are being diverted to other countries, with a portion going to other African countries. In addition, there should be other investments from India that reach Africa via third countries, but it is difficult to get a clear picture of the flow because of data limitations.

The above bilateral FDI statistics show that among Indian companies' investments in African countries (excluding Mauritius), investments in Mozambique's agriculture and mining industries (USD 92.36 million on a cumulative basis) and Ethiopia's manufacturing industry (USD 84.31 million) are some of the largest. Of the investments in Mozambique's agriculture and mining industries, investments are concentrated in the mining sector especially for large-scale projects, such as for coal development (USD 10.5 million) and natural gas development (USD 7 million).

Considering that Japanese companies have also been giving attention to the "Africa and Resources" business from before, as mentioned above, what should be noted is Indian companies are concentrating their investment on the manufacturing industry. In these years, Indian companies' direct investments in manufacturing in African countries (excluding Mauritius) totaled USD 472.57 million (cumulative). The number of projects was 716, and the statistics show that a considerable number of Indian companies have been investing in the region from the perspective of "Africa and Factories." Representative examples of business development by Indian companies can be seen in countries such as Ethiopia, South Africa, and Nigeria, and are described in the following.

Figure 1: India's bilateral foreign direct investment in African countries

	Agriculture, Mining	Manufacturing	Construction	Wholesale, Retail, Hotel & Restaurant	Financial, Insurance, Business Services	Transportation, Warehousing, Communication Services	Community, Social, Personal Services	Electricity, Gas, Water	Others	Total
Ghana	3,288,900	675,000	–	2,916,200	–	–	102,000	2,773,100	–	15,875,200
Nigeria	10,390,900	14,599,800	223,800	259,600	1,936,500	108,600	613,900	110,200	8,277,400	36,520,700
Mauritius	41,745,000	3,034,699,200	668,032,500	962,357,400	4,601,935,700	2,220,643,300	921,340,100	29,943,000	4,499,000	12,860,907,200
South Africa	6,401,900	29,708,600	5,298,600	13,465,400	88,579,100	–	6,081,200		–	149,534,800
Kenya	320,000	55,709,000	20,900	4,179,200	3,648,700	2,930,100	571,900	50,000	–	67,429,800
Zambia	15,757,800	23,279,000	660,000	608,700	23,601,100	–	10,600	48,790,400	–	112,707,600
Ethiopia	2,277,600	84,313,000	270,000	265,000	–	–	3,687,500	–	–	90,813,100
Madagascar	100,000	158,000	–	–	–	–	–	–	–	258,000
Rwanda	3,140,200	905,100	923,100	–	–	–	715,300	–	–	5,683,700
Tanzania	11,379,900	21,730,200	90,000	886,600	16,500,000	–	350,500	–	–	50,937,200
Chad	–	–	–	–	12,000	–	–	–	–	12,000
Uganda	4,311,700	1,938,900	1,855,800	4,350,300	83,000	200,000	4,487,000	–	–	17,226,700
Egypt	55,100	32,355,500	–	–	2,800	–	–	19,026,900	–	51,440,300
Guinea	27,000	20,000	–	138,500	–	68,000	3,356,000	–	–	3,579,500
Morocco	119,000	55,528,200	–	–	–	–	–	–	–	55,647,200
Mozambique	92,357,800	902,000	321,500	–	828,200	–	–	–	–	94,409,500
Algeria	–	18,600,100	–	40,200	–	–	–	–	–	18,640,300
Mali	–	663,200	–	–	27,800	–	1,400	–	–	692,400
Benin	–	870,900	–	11,000	–	–	162,000	–	–	1,043,900
Malawi	254,300	1,653,900	–	–	39,400	–	–	–	–	1,947,600
Tunisia	–	82,450,000	–	68,000	–	–	–	–	–	82,518,000
Gabon	51,300	14,232,300	–	–	–	–	–	–	–	14,283,600
Zimbabwe	119,100	10,102,100	–	500,000	100,000	–	–	–	–	10,821,200
Gambia	–	179,000	–	–	125,000	–	–	–	–	304,000
Botswana	–	465,000	–	2,962,000	9,780,000	–	–	–	–	13,207,000
Liberia	1,000	–	–	–	–	–	–	–	–	1,000
Côte d'Ivoire	–	9,235,300	–	–	–	20,000	–	–	–	9,255,300
Burkina Faso	–	958,600	–	–	–	–	–	–	–	958,600
Togo	–	3,140,600	–	–	33,000	–	–	–	–	3,173,600
Libya	–	1,122,700	–	–	–	–	–	–	–	1,122,700
Mauritania	–	425,000	115,000	–	–	–	–	–	–	540,000
Seychelles	–	–	–	–	914,300	–	–	–	–	914,300
Namibia	–	525,000	–	–	–	–	–	–	–	525,000
Senegal	–	–	–	–	–	124,100	–	–	–	124,100
Congo	1,660,000	–	–	–	–	–	–	–	–	1,660,000
Sierra Leone	–	–	–	80,000	–	–	–	–	–	80,000
Total	569,470,500	3,507,265,200	677,811,200	993,088,100	4,748,146,600	2,224,094,100	941,449,400	100,693,600	12,776,400	13,774,795,100

Note: Unit = USD. Figures are based on notifications and are cumulative for the period from January 2015 to June 2019. Main examples of development projects in the yellow shaded areas are shown in Figure 2.
Source: Compiled by MGSSI based on data from the website of the Reserve Bank of India

Figure 2: Main examples of Indian companies' development in African countries

Investment in the Kenyan manufacturing industry	Pharmaceutical company Alkem Laboratories has established Pharmacor to manufacture and sell drugs for chronic diseases. The company aims to expand its operations throughout the 21-member free trade area called the Common Market for Eastern and Southern Africa (COMESA), which includes Kenya, Egypt, and Zimbabwe.
Investment in the Ethiopian manufacturing industry	JK Metal Industries, the largest manufacturer of aluminum cookware in India, has established JK Cookware Manufacturing.
Investment in the Moroccan manufacturing industry	Automotive and aircraft parts maker IM Gears, which receives technology support from Amis of France, has established IM Gears Morocco.
Resource development JV established in Mozambique	The Indian state-owned enterprise ONGC Videsh has invested in an offshore energy JV along with Mitsui & Co., Anadarko Petroleum of the US, and others.
Manufacturing JV established in Tunisia	A phosphate fertilizer manufacturing JV has been established through a partnership between two Indian companies, Coromandel International and Gujarat State Fertilizers & Chemicals, and the Tunisian group formed by Compagnie des Phosphates de Gafsa and Groupe Chimique Tunisien (CPG-GCT). All of the output is exported to India.

Note: The details correspond with the yellow shaded parts of Figure 1.
Source: Compiled by MGSSI based on information from company websites

3. INDIAN COMPANIES EYEING THIRD MARKETS BY LEVERAGING COMMERCE SYSTEMS AND OTHER SCHEMES

3-1. Examples of two Indian companies in the textiles industry

A typical strategy employed by Indian companies investing in the African manufacturing industry is one designed to gain entry to a market for exports to third markets. A good example of this is the strategy of companies investing in the textiles industry in Ethiopia. One such company is Raymond, India’s largest fabric and apparel maker. The company that founded in 1925 established its first overseas production base with its move into Ethiopia in 2017.

Among many countries and regions with thriving textile industries, such as China, Southeast Asia, and South Asia, in addition to the company’s home country of India, Raymond was able to expand into the African region because of a strategy that combines the following three advantages. The first is the Ethiopian government’s preferential treatment of FDI. The government has readied a variety of investment incentives as it is prioritizing foreign capital attraction. For example, companies making new investments in the manufacturing industry are exempted from paying corporate tax for up to seven years, and in the case of additional investments, the exemption applies for two years provided the project exports at least 50% of its output. As for customs duties, tariffs imposed on the importation of materials used in the manufacturing of products for export will be refunded, and tariffs on imported materials are eliminated for companies located within government-designated industrial zones, such as Hawassa Industrial Park on the outskirts of Addis Ababa where Raymond is situated. Raymond’s Ethiopian plant imports fabrics from India, which would normally have tariffs of 5-30% levied on them. Significant benefits can be obtained from these incentives without letting merchandise through the tax haven of Mauritius.

The second advantage is the low cost of labor. The average monthly wage of general workers is USD 283 in Bengaluru, where one of Raymond's Indian plants is located, but it is significantly lower at USD 50-70 in Addis Ababa, Ethiopia. The company says it senses a crisis looming in the future, as India is exposed to competition from Bangladesh and other nations with even lower labor costs. For example, workers in Dhaka, Bangladesh, earn USD 109 a month on average, while workers in Phnom Penh, Cambodia, take home USD 201 and those in Ho Chi Minh City, Vietnam, make USD 242.[1] In other words, the company's Bengaluru factory has a competitive disadvantage internationally in this respect, but in turn, Ethiopian factory enjoys the low cost of labor as its competitive advantage.

Food prices are high in African countries because many rely on foodstuff imports and that has led to high labor costs. As a consequence, it is said that it is difficult to expand manufacturing operations in the region. In fact,

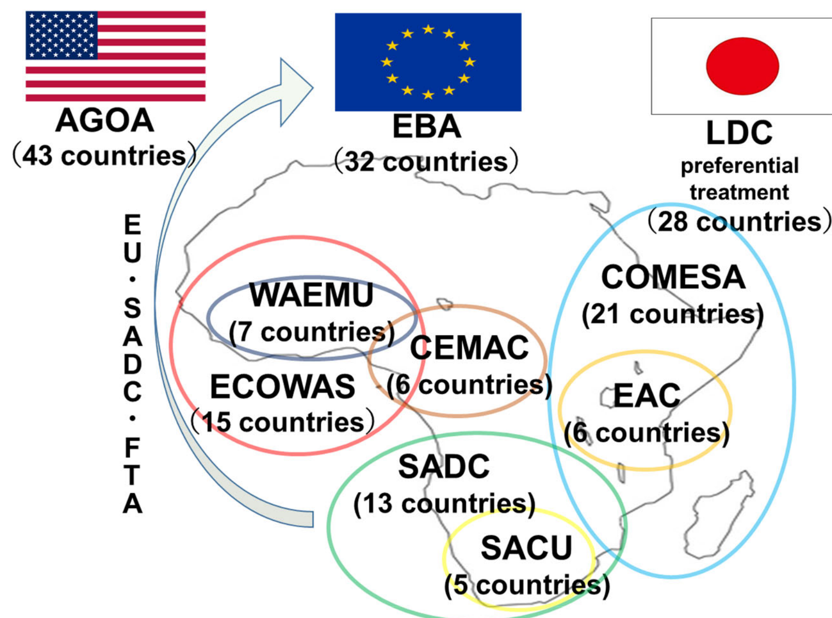
[1] Investment cost comparison website of the Japan External Trade Organization (JETRO)

monthly wage levels for general workers are as high as USD 1,602 in Johannesburg, South Africa, and USD 742 in Casablanca, Morocco. However, wages are low in some countries, such as Mozambique (Maputo), where it averages USD 141, and Nigeria (Lagos), where it is USD 137-192, so the range is wide. Labor costs are by far the lowest in Ethiopia.

However, the quality of the labor force is a problem. While the global average literacy rate is 86%, the rate in Sub-Saharan Africa is 66% and in Ethiopia it is 52%. Raymond also points to the necessity of training Ethiopians to establish a work ethic, including an understanding of the importance of punctuality, for instance, and a work style for performing repetitive work while remaining in a sitting position for an extended period of time. As the company was aware of these circumstances when it invested, it could be said that the move into Ethiopia was a rational option for avoiding the risk of rising labor costs in India. Determining whether or not the low labor costs are commensurate with the low quality of workers, as in this example, could be regarded as one of the key points for deciding whether to invest in the African manufacturing industry.

The third advantage is the use of commerce systems, including preferential tariffs (Figure 3). Raymond does not ship any of the output from its Ethiopian plant to the domestic market nor to its home market of India, but exports all of them to the European and US markets. The company explains it is making use of the EU and US commerce systems to achieve this, emphasizing its significant benefits of zero tariffs.

Figure 3: Major commerce systems benefiting Africa



Source: Compiled by MGSSI based on customs data and information from the WTO website

The EU has introduced a preferential tariff system called the Everything But Arms (EBA) scheme for the poorest countries.[2] Under the initiative, tariffs are exempted for all imports to the EU from the countries covered by the scheme. At present 32 countries in Africa are included in the scheme and Ethiopia is one of them. For textile products as well, even if they are made from imported fabrics, the products are eligible for tariff-free treatment under the EBA.[3] Therefore, Raymond is able to export textile products manufactured at its Ethiopian plant to the EU markets without having to pay tariffs. India, in contrast, is not a country covered by the EBA, so exports of Raymond's products from its Indian factories to the EU markets would be subject to tariffs of 8-12%. In

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[2] REGULATION (EU) No 978/2012 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 25 October 2012 (https://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1500986680646&uri=CELEX:32012R0978)

[3] COMMISSION REGULATION (EU) No 1063/2010 of 18 November 2010 (https://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1570492116061&uri=CELEX:32010R1063), and the "Generalized System of Preferences Handbook on the Scheme of the European Union" 2015 UNCTAD

addition, many other major exporters of textile products are not eligible for EBA. For example, exports from China and Vietnam to the EU are imposed tariffs in the same way as those from India.

The US, meanwhile, has legislated the African Growth and Opportunity Act (AGOA)[4] and applies it to 43 Sub-Saharan African countries. The act is an extension of the US Generalized System of Preferences (GSP), and exempts tariffs on exports from eligible countries to the US. Specifically, on top of the approximately 4,500 items covered by the GSP, the AGOA adds around 1,500 items for tariff-free treatment, bringing the total to approximately 6,000 items. The AGOA went into effect in 2000 and was initially valid until 2008, but the act has been extended a number of times ahead of its expiry date, and is currently valid until 2025.

The AGOA eliminates tariffs on textile products that are not included in the GSP, but for the rule to apply, the fabric used in the item must be sourced from within the exporting country or the US. However, in eligible countries where GNP per capita was less than USD 1,500 in 1998,[5] the tariff-free benefit applies even if the products are made from fabrics sourced from a third market. This provision applies to 24 of the AGOA countries, including Ethiopia.[6]

Raymond imports fabrics from India to manufacture textile products at its Ethiopian plant. As such, by taking advantage of Ethiopia's eligibility under the above AGOA, the company is able to export the products from the plant to the US market without having to pay tariffs. In contrast, if Raymond were to export products from its plants in its home country of India to the US market, an 18% tariff would be levied. The same goes for exports to the US from other major textile product exporters, such as China and Vietnam. By setting up a factory in Ethiopia, Raymond has secured the most favorable tariff terms for exports to the European and US markets.

Another example of an Indian company that has entered Ethiopia with a strategy aimed at exporting to third markets is Arvind. Established in 1931, the company is headquartered in Gujarat and engages in apparel manufacturing and other operations. Arvind entered the Ethiopian market in 2015, and employs over 2,000 workers at its factories, including the Hawassa Industrial Park. The company's annual production volume in Ethiopia is approximately 8.3 million items of clothing, including suits, shirts, jeans, and it exports all of the output to Europe and the US. As expressed by an Arvind executive's comment to the effect that Ethiopia has strategic advantages, the company, like Raymond, has been able to expand in Africa because of a strategy that combines the benefits of favorable treatment, such as the abovementioned EU and US commerce systems.

In addition, Arvind is collaborating with other companies. Together with its partner Phillips-Van Heusen (PVH), a major US apparel company that owns such brands as Calvin Klein and Tommy Hilfiger, the company established PVH Arvind Manufacturing in 2016. The joint venture has a factory in the Hawassa Industrial Park, and produces 8 million shirts annually for the Calvin Klein and Tommy Hilfiger brands for export to the US market. According to the Ethiopian government, a total of 31 Indian companies had invested in its textiles industry as of 2018.

These strategies being employed by Raymond and Arvind (Figure 4) are not seen at most of the Japanese companies that have ventured into Africa. According to a JETRO survey on 315 Japanese companies with a presence in Africa,[7] the most often cited reasons for establishing a base in Africa were "future market potential" and "market size" of the local market, and in fact, none of the companies said the reason was to set up a base for manufacturing products for export to foreign markets.

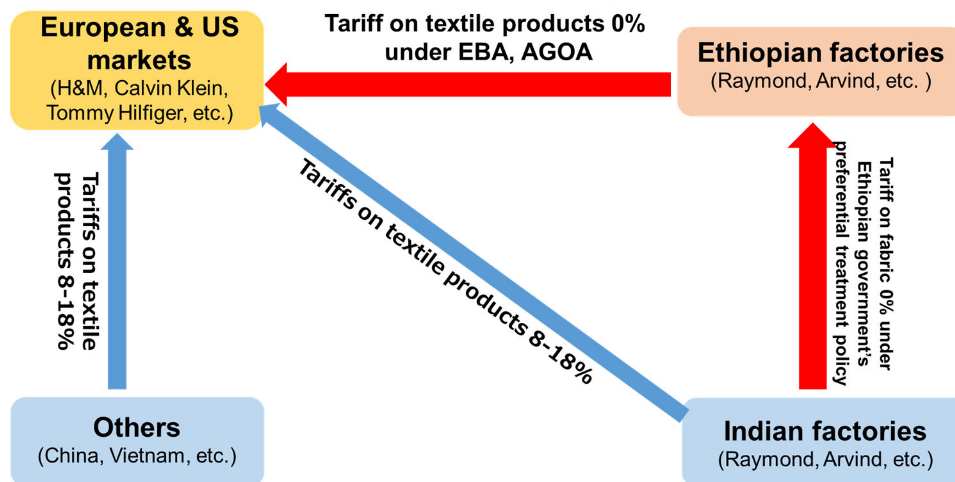
[4] https://agoa.info/images/documents/2/AGOA_legal_text.pdf

[5] Per-capita GNP in Ethiopia was USD 130 in 1998, and USD 790 in 2018.

[6] AGOA.Info (https://agoa.info/about-agoa/country-eligibility.html)

[7] JETRO's 2019 Survey on Business Conditions of Japanese-Affiliated Firms in Africa, January 2020.

Figure 4: Schematic of using commerce systems Via Africa



Source: Compiled by MGSSI based on REGULATION (EU) No 978/2012 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL, COMMISSION REGULATION (EU) No 1063/2010 of 18 November 2010, AGOA.Info (https://agoa.info/about-agoa/country-eligibility.html)

3-2. Examples of two Indian companies in the automotive industry

Automakers are also among the Indian companies that have invested in Africa in search of access to third markets. One of them is Mahindra & Mahindra (M&M), the core company of the Mahindra Group. In 2018, the company began operating a pickup truck assembly plant with annual production capacity of 4,000 units in South Africa. South Africa, as an exception among African countries, has already seen many automakers, including Japanese companies, penetrate its market, suggesting that perhaps not a great deal can be noted for M&M in the context of the vehicle assembly industry. However when taking a closer look at how the company is leveraging the commerce systems, what we can view changes.

According to a M&M's executive, strategy is to make South Africa a base for exports to Sub-Saharan Africa in the future. With that in mind, the company has begun exporting to neighboring countries by taking advantage of the Southern African Customs Union (SACU). The SACU's member countries are South Africa, Botswana, Lesotho, Namibia, and Eswatini (formerly Swaziland), whose tariffs are eliminated among the five countries. However, M&M's truck assembly and manufacturing operation in South Africa relies on parts imported from outside the SACU, which are subject to customs duties. The company says that tariffs as much as up to 30% are imposed on auto parts imported from India. Therefore, it is trying to increase local sourcing to account for around 40% of total parts procurement. Moreover, M&M also manufactures agricultural machinery and began exporting tractors from South Africa in 2019, and has started manufacturing and exporting construction machinery and generators. In this way, the company aims to expand exports of its diverse range of in-house products by using automobiles as a foothold.

Another Indian automaker that has entered Africa to pursue expansion into third markets is the commercial vehicle manufacturer Ashok Leyland, the core firm of the Hinduja Group. The company has production sites in nine countries around the world, including an assembly plant in Nigeria in Africa. It is a member of the customs union called the Economic Community of West African States (ECOWAS). Given than ECOWAS has 15 participating members, including neighboring countries Benin and Niger, exports from Ashok Leyland's Nigerian plant to these West African countries through ECOWAS are thought to be eyed for

A company executive explains that Africa is strategically important for the global growth of Ashok Leyland, which ranks 10th in the world for truck manufacturing and 5th in the world for bus manufacturing. Therefore, the Indian company is said to be planning to set up new assembly factories in Côte d'Ivoire and Kenya in addition to the one in Nigeria.

4. CONCLUSION

The 2007 version of the JETRO survey mentioned above reveals that just as with the 2019 survey, the most commonly cited reason by Japanese companies for their decision to establish a base in Africa was "future market potential." This can be interpreted to mean that Japanese companies have been waiting for the African markets to expand for more than a decade. At the same time, as noted earlier in this report, some Indian companies have been investing in Africa with strategies that are different from those adopted by those Japanese companies. However, considering the labor costs and education level in African countries, at present, it is not pragmatic to set up operations for any field of manufacturing in any and all regions of Africa. Rather, the reality is some countries can establish operations for textile product manufacturing or automotive assembly, as in the examples described, or centered on the light industries such as automobile parts assembly, marine product processing and wire harnesses. The African manufacturing industry does not have strong brand recognition at this time as is the case with the Ethiopian textile products industry that has been presented in this report as one example of Indian companies' market inroads. That said, business opportunities can be expected in the form of contract manufacturing for companies with strong brands, such as European and US companies, thus providing a reason to explore the transfer of manufacturing industries from Asia, for example, to these African countries. When considering using Africa as the medium for achieving this kind of horizontal specialization, an effective approach would be to take advantage of commerce systems, such as EBA, AGOA, and SACU, to search for markets in foreign countries.

Going forward, new commerce systems are anticipated in Africa. That is to say, for example, the creation of the African Continental Free Trade Area (AfCFTA), in which all African nations have said they will participate and for which an agreement came into effect in 2019, and free trade agreements (FTA) that would join countries outside Africa with the AfCFTA. In the AfCFTA accord, African countries have agreed to eliminate at least 90% of tariffs, and have set the goal of making the agreement operational from July 2020. If the operation of the AfCFTA gets on track, it could open up possibilities for the arrangement of FTAs between African countries, as a whole, and other countries. Potential partners include India, which has yet to conclude an FTA with any African country even though Indian industries have been seeking such treaties, and the US and other countries, where plans to conclude FTAs with African countries are emerging as the scheduled expiration of the AGOA is drawing near.

Under such circumstances, standing out recently are Japanese companies looking to Africa from India, as they have come to recognize the value of the affinity between the two regions. They include Panasonic, which has established a hub in India to oversee African markets; Daikin Industries, which, in addition to its local company in the UAE that is in charge of Africa, has changed its organizational structure to give its Indian unit jurisdiction over East Africa; and Bridgestone, which has positioned India in the same strategic business unit as Africa. If the number of such companies increases in the future, it is likely that more of those companies and related companies that supply them with parts will contemplate the transfer of some production processes to Africa in response to changes they discern in the business environment, such as rising labor costs. In doing so, the strategies of Indian companies in Africa, as detailed in this report, should serve as a useful reference for companies looking to leverage the new commerce systems in their pursuit of business in Africa.

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