Africans, don't rely on international investors

The coronavirus will change permanently the world economy. European and American companies will reshore a lot of activities from low-cost countries. This will affect African business.

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For more than 70 years, after the period of global protectionism during the Great Depression, the highly-industrialized countries were trying to tear all kind of barriers to international free trade. The coronavirus will change that probably too. In Europe, the big debate is currently which kind of products should not be produced anymore in low-cost countries: Mouth masks, latex gloves and other medical day-to-day equipment. This can go further as the German government was quite before corona helping to build a battery manufacturing plant. This trend is not unique to Europe. US President Donald Trump won the election in 2016 on claiming "America First".

Europeans and Americans were, for quite a while, hard believers in free trade. David Ricardo (1772-1823), the British economic thinker, developed at the beginning of the 19th century his theory on the comparative advantage of foreign trade, based on the ideas of Adam Smith: Even if Portugal has in his example advantages over Great Britain in producing textiles and wine, it will be beneficial for Portugal to specialize in wine and to leave the textile production to the British.

Don't forget market power

This might be so in the theoretical world of pure and perfect competition. In the real world, there is one disadvantage: In terms of market power, it is not neutral if you produce textiles or wine, if you specialize in cocoa beans or in chocolate, in copper extraction or in cars. The chocolate producer tends to exercise a bigger market power over the farmer whose income depends from just one crop he is planting.

For a long time, Europeans and Americans were relocating labour-intensive activities to low cost countries according to the product life-cycle theory, developed by the American economist Raymond Vernon (1913-1999). He stated that developed countries should concentrate on innovation and know-how intensive activities and offshore labour-intensive mass production to developing countries.

This conviction made the fortune of Hong Kong, Japan and later China. Welcoming labour-intensive, low-technology mass production was a major kick-off for their economic success stories. But Asian emerging countries were not stick to this kind of international division of labour and used the funds they got from export activities to develop themselves into manufacturers of highly sophisticated goods.

The security of supply chains matters, too

Today, it is different. It is not only the security of supply of products Europeans and Americans consider as strategical ones. Digitalization too makes it easier for companies from the North to reshore manufacturing. Apple, Electrolux, NCR, Lenovo and many other companies are moving back production facilities from China and Asia to the Europe and the US. Today, it is not as important as in the past to produce mass production in huge series. Today, it is much more important to be able to produce small series or even individualized goods. Adidas, the German sports fashion company, also relocated production from China or India back to Europe and the US. The first reason are costs: 1000 jobs in an Asian plant were downsized thanks to robots and digitalization to 160 in Europe. The second reason is that modern IT-based manufacturing is able to produce small series which contributes to flexibility and shorter time to market.

In Africa, the hope was for a long time to benefit from relocating European or American or even Chinese manufacturing to low wage – and often weakly regulated – countries in Africa. African policy makers should not rely on this strategy anymore. It is highly probable that this dislocation will not happen in the future to an extent that could really boost African economies.

Labour productivity is key

There is one lesson African policy makers should take from Adam Smith (1723-1790), the father of modern economics: He stressed on the importance of labour productivity. And we agree that productivity is much more decisive for the economic future of a country than economic growth measured by the increase of GDP.

Low productivity is the big vulnerable point of the African growth story. “Labour productivity differences between Sub-Saharan Africa and more advanced economies have remained large”, the

World Bank economists say in a report on productivity in Sub-saharan Africa published in 2018. “More recently, the story of misallocation (inefficiencies in the use of technologies) has become relatively more important than undercapitalization (low capital stock) in driving these productivity differences.”

If, and only if, Africa succeeds in increasing labour productivity, the continent has a real chance to join the club of the prosperous economies of the world. Therefore, African governments should intensify efforts to give every child a basic education in writing, reading and calculating and to stress on technical, digital and mechanical training and the establishment of technical colleges.

Developing productivity will be key to the future of Africa as the German-American economist Friedrich List (1789-1846), born in the Swabian town of Reutlingen in Southwest Germany, was saying: “The power to create wealth is infinitely more important than wealth itself.”