Africa Development, Vol. XXXII, No. 2, 2007, pp. 1–23
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(ISSN 0850-3907)

Attracting Foreign Direct Investment for Growth and Development in sub-Saharan Africa: Policy Options and Strategic Alternatives

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Abstract

Foreign Direct Investment (FDI) plays an important role in fostering economic growth and development in developing countries. While FDI is known to bring to the latter much needed capital for their growth and development efforts, it also brings with it skills and new technology. For most countries in sub-Saharan Africa, whose economies have recently recovered from a long period of stagnation, FDI inflows are needed to accelerate growth, and development. Several countries in the region registered impressive growth rates in the 1990s, with some attaining and sustaining double-digit growth rates in most recent times. However, if sub-Saharan Africa is to accelerate its growth rates to enable it move the majority of its peoples out of poverty, it must attract more FDI. Efforts so far have been encouraging. However, when compared to countries in South East Asia such as Singapore, Malaysia, Thailand and China, FDI inflows into sub-Saharan Africa pale. What are the causes for such low FDI inflows to this region? How can sub-Saharan Africa attract more FDI for its growth and development efforts? What policy options are available to these countries? What strategic alternatives can sub-Saharan countries adopt to increase FDI inflows? What role can multilateral and bilateral organisations play in this effort? This paper will address these questions by examining current FDI flows into sub-Saharan Africa and examine ways through which the sub-region can further attract much needed FDI to enable it to attain sustainable growth and development.

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Résumé

L'Investissement direct étranger (IDE) joue un rôle important dans la stimulation de la croissance et du développement dans les pays en développement. L'IDE est plus connu pour son apport en capitaux indispensables aux efforts de croissance et de développement des pays bénéficiaires. Il leur apporte également des compétences et de nouvelles technologies. Dans la quasi-totalité des pays de l'Afrique subsaharienne, dont les économies sont récemment sorties d'une longue période de stagnation, les flux d'IDE sont nécessaires en vue d'une accélération de la croissance et du développement.

Au cours des années 90, plusieurs pays de la région ont enregistré des taux de croissance impressionnants, et plus récemment certains d'entre eux ont atteint et soutenu des taux de croissance à deux chiffres. Pour autant, si l'Afrique subsaharienne voulait accélérer ses taux de croissance en vue de sortir la majorité de ses populations de la pauvreté, il lui faudrait attirer plus d'IDE. Les efforts déployés dans ce sens ont été jusqu'ici encourageants. Cependant, comparées aux pays de l'Asie du Sud-Est, tels que Singapour, la Malaisie, la Thaïlande et la Chine, les entrées de l'IDE à destination de l'Afrique subsaharienne sont encore insignifiantes. Quelle explication donner à un niveau de flux de l'IDE aussi faible dans la sous-région? Comment l'Afrique subsaharienne peut-elle attirer plus d'IDE pour soutenir ses efforts de croissance et de développement ?

Quelles sont les options politiques à la disposition de ces pays ? Quelles stratégies alternatives l'Afrique subsaharienne peut-elle adopter pour accroître les entrées de l'IDE ? Quel rôle les organisations bilatérales et multilatérales peuvent-elles jouer dans ces efforts ? L'article aborde ces questions en examinant les entrées actuelles de l'IDE en Afrique subsaharienne et les moyens par lesquels elle pourra attirer d'avantage ces flux dont elle a tant besoin pour assurer une croissance et un développement durables.

Introduction

The important role inflows of foreign direct investment (FDI) play in fostering economic growth and development of developing countries cannot be emphasised enough. FDI inflows are known to contribute to a rise in domestic investment. In addition, through FDI, developing countries gain from skills and technology transfers and capacity building, amongst other things. For most countries in sub-Saharan Africa (SSA) whose economies are recovering from a long stagnation after the implementation of macroeconomic reform programmes, FDI inflows is much needed to accelerate growth rates to around eight or nine percent to be able to move the majority of their people out of poverty.

Since the 1990s, most SSA countries have registered impressive growth rates. Several countries in the region attained and sustained double digit growth during this period. For example, real Gross Domestic Product (GDP) growth

in the whole of Africa in the second half of the 1990s averaged four percent per year. This exceeded the continent's previous growth rate of 2.8 percent per year. Export growth doubled to 80 percent a year and real GDP grew by 2.3 percent in 1999, up from 3.1 percent in 1998. No country in the region experienced a negative GDP growth in 1999 and only one posted a growth rate of less than one percent. In 1999, 19 countries had growth rates between zero and 2.9 percent, another 17 clustered between 3 and 4.9 percent, and 12 had growth rates of between 5 percent and 6.9 percent (UNECA 2001) (see Table 1). Mozambique and Equatorial Guinea recorded the highest growth rates of 10 percent. Eastern and Southern Africa, which together account for 45 percent of the region's population and 37 percent of GDP enjoyed a faster growth in 1999.

Table 1: Distribution of African countries by real GDP growth 1995–1999

Growth rate (Percent)	1995	1996	1997	1998	1999
Negative	6	2	4	20	0
0–2.9	11	12	12	13	19
3–4.9	23	28	25	28	17
5–6.9	6	9	10	8	12
7 and above	7	2	2	2	5

Sources: United Nations Economic Commission for Africa, *Transforming Africa's Economies: Overview* (2001); *Economic Report on Africa* (2003).

Table 2 shows a remarkable increase in the growth performance of most countries in Africa. For example, between 2000 and 2004, around five to seven countries saw their GDP growth rise above 7 percent. Between 20 and 27 countries witnessed growth rates from 4–7 percent in the same years and 16 to 27 countries also witnessed between 0–3.9 percent growth rates within the same period. Africa as a whole recorded a 4.6 percent growth rate in 2004, an increase over the 4.3 percent it witnessed in 2003 (UNECA 2004).

Table 2: Growth performance distribution in Africa, 2000–2004

Growth Performance	2000	2002	2003	2004
Negative growth	2	5	7	2
Zero and positive growth	49	48	45	50
Low (0–3.9 percent)	22	27	16	17
Medium (4–7 percent)	20	16	24	27
High (more than 7 percent)	7	5	5	6
Total number of countries	51	53	52	52

Source: UNECA, *Africa Economic Outlook*, 2004.

From the above Tables 1 and 2, one can see a gradual growth in African economies from six countries, which had a negative growth in 1995 to zero with a negative growth in 1999. It is equally striking that in 1995, only six countries in the region had a growth rate of 5–6.9 percent. In contrast, 12 had such growth rates in 1999. These growth rates have improved over the years as depicted by Table 2. Overall, what is becoming clear is that countries in the region have growth rates converging above 3 percent. Such an outlook has positive implications for the development prospects of the region. These promising economic data of SSA point to the fact that in general, the majority of the economies in the region are on the mend, even though there might have been a few that stumbled in the year 2001.[1] Also, the September 11 attack on the Twin Towers in New York and the global economic slowdown that ensued had an impact on numerous economies around the world. Fortunately, the impact on Africa was limited. It was the only developing region to witness faster growth in 2001. Table 3 supports this view as it shows a remarkable improvement in GDP growth for the different regions of the continent over the years.

Overall, GDP in Africa rose from 3.5 percent in 2000 to 4.3 percent in 2001. Countries like Ethiopia registered growth rates of 8.7 percent, Mozambique 9.2 percent, Uganda 5.4 percent. In its 2004 report on the Economic Outlook of Africa, the UNECA notes that Africa recorded 4.6 percent growth in 2004, an improvement from the 4.3 percent registered in 2003 (UNECA, 2002, 2004).Despite such promising growth figures, this growth falls short of the 7 percent required by SSA countries to achieve the Millennium Development Goals 1, to halve poverty in Africa by 2015.

Table 3: GDP Growth in Africa by Region, 1998–2004 (percent)

Region	1998	1999	2000	2001	2002	2003	2004
Africa	3.1	3.2	3.5	4.3	3.4	4.3	4.6
North Africa	4.4	3.5	4.1	5.8	2.8	4.8	4.8
Sub-Saharan Africa	2.6	2.9	3.1	3.3	3.7	3.9	4.5
West Africa	3.6	3.2	2.7	3.3	3.3	6.7	4.3
Central Africa	4.9	4.4	4.4	4.9	4.4	4	7.3
East Africa	2.5	4.1	3.1	5	5.2	2.5	5.8
Southern Africa	1.7	2.2	3	2.4	3.5	2.5	3.5

Source: United Nations Economic Commission for Africa, 2004.

Thus, if SSA is to attain its MDGs and to sustain its accelerated growth, one of the alternatives is that it must attract more Foreign Direct Investments (FDI).[2] Efforts so far have been encouraging. For example, FDI inflows into Africa increased from US$12 billion in 2002 to US$15 billion in 2003 and rose to US$20 billion in 2004. But, compared to the South East Asian (SEA) countries and China, these amounts arepale. China alone attracts over US$50 billion in FDI every year. China and South East Asian countries have been able to leverage a lot more than African countries in the areas of education and Information and Communications Technology (ICT) infrastructure and development and an enabling environment to make their regions attractive. This has contributed to more FDI flowing into those regions. Malaysia has set up the Multimedia Super Corridor to attract ICT companies from around the world to use their country as a production base. Singapore is moving into biotechnology industries. Most countries in the South East Asian region are investing heavily in the education and the training of knowledge workers to give their respective countries the requisite competitive advantage they need and to enable them to attract FDI for their continuous growth and development efforts (Abdulai 2004).

So, what are the causes for such low FDI inflows to SSA? How can SSA attract more FDI for its growth and development efforts? What lessons can SSA learn from other developing countries? What role can multilateral and bilateral organisations play to help SSA in this effort? These are some of the questions this paper hopes to answer. Its main objective is to examine the ways through which SSA can attract FDI inflows. Thus, answering the aforementioned questions will entail a look at the development of workable policies and strategies that will be applicable to the African situation. This

qualitative paper attempts to make an effort to find answers to some of these questions. It is organised into the following sections. Section I examines SSA's economic recovery process, which serves as an impetus to attract FDI for sustained growth. Section II examines some of the theories of FDI. Section III deals with reasons why SSA should attract FDI. In section IV, the current trends of FDI inflows into the region are examined in comparison to other regions in the developing world, mainly, South East Asia and China. In section V, some of the reasons for low FDI inflows into SSA are examined and explored. Section VI explores policy options and strategies for SSA to attract FDI. The role, which multilateral and bilateral organisations should play in this effort, is offered in section VII. Section VIII concludes the paper by suggesting that it is through the deepening of reforms in SSA, the removal of the negative image of the region, the development of an educated and productive labour force as well as developing good infrastructure and infostructure in the various countries that SSA will be able to effectively compete to attract more FDI for its accelerated growth and development efforts.

Economic recovery in SSA

The macroeconomic and reform policies undertaken by most countries in SSA from the 1980s and in the early part of the 1990s have reversed years of stagnation. Between 1993–1994, average real GDP grew to around an average of one percent. From 1995–1998 this rose to an average of about five percent (excluding Nigeria and South Africa due to the relatively large sizes of the two economies). According to the International Monetary Fund (IMF), forty out of forty-seven countries in SSA have shown increases in their annual per capita incomes since 1994. Inflation has been brought down to manageable levels in most of the countries and internal as well as external imbalances have also been brought down. The average inflation as measured by the consumer price index has declined from a peak of 121.6 percent in 1994 to 9.9 percent in 2002. Furthermore, the external current account deficit in the region has remained at an average of US$9.5 billion. But for the Asian Financial crisis of 1997-1999, the deficit could have been narrowed (See Table 4). The overall fiscal deficits for the region were cut from 8 percent in 1993 to 3 percent in 2002. Recent reports from the African Development Bank (AfDB) and the Organisation for Economic Co-operation and Development (OECD) show that in the year 2003, SSA has shown relatively good economic progress, chalking up a growth rate of 3.6 percent despite weak global economic growth and continued structural and political constraints in some parts of the continent. The report predicts that the growth of the region is holding up in 2004 and should rise to 4 percent by 2005 (*African Economic Outlook* 2003/04, 2004). This growth figure was achieved.

The sound fiscal and monetary policies which most of these countries pursued led to a reduction in the macroeconomic imbalances in the region. Important structural reforms have also been undertaken. These include a substantial removal of domestic price controls, establishment of market-determined interest rates, liberalisation of exchange rates, and the restructuring of public sector enterprises to mention just a few.

Table 4: Selected Economic and Financial Indicators for Sub-Saharan Africa, 1993–2002

	1993	1994	1995	1996	1997	1998	1999	2000	2001*	2002*
	(growth rates, percentage)									
Real GDP	0.4	1.6	4.2	5.4	4.6	3.8	3.1	2.8	3.9	5
Consumer price index	73.7	121.6	57.4	58.7	24.7	16.9	21.7	27	20	9.9
	(percentage of GDP)									
Central government fiscal balances	-8.1	-6.6	-5	-3.8	-4	-3.7	-4	-4	-3.1	-2.8
External public debt outstanding	72.5	80.8	74.7	71.1	67.5	70.6	70	69.2	69.3	65.3
	(billions of U.S. dollars)									
Payments balances on current account	-9.7	-7.1	-8.9	-7.8	-11	-13.7	-11	-7.1	-9.2	-9.5

* = Estimates.
Source: IMF, *World Economic Outlook 2001* (Washington).
Note: Excluding Nigeria and South Africa owing to the relative large size of their economies.

The implementation of these reforms also coincided with the movement of countries in the region towards democratic reforms and participatory forms of governments. The region has also seen an improvement in its political situation, albeit a few hot spots still pertain. Despite such remarkable achievements compared to the precarious situation of the region in the 1970s and 1980s, SSA is still lagging behind countries in developing Asia in attracting FDI. Its ability to be able to meet most of the internationally agreed Millennium Development Goals (MDGs) by 2015 remains a challenge.

Thus to be able to create employment opportunities for its rapidly growing populations and to meet its MDGs, especially the reduction of poverty in the region, SSA needs to raise its average real GDP to about seven to nine percent annually on a sustained basis for at least a decade (Ouattara 1999; UNCTAD 2005). Such a goal would only be possible when governments in the region invest about 25 percent of their annual incomes in technology and in sectors that increase GDP growth (Calamitsis 1999). This will require the acquisition of up-to-date techniques, methods and skills to increase production. There will also be the need to restore peace in the region. Before the end of the Cold War, governments in the region could count on generous aid disbursements from developed countries to assist in this effort. This was because most of these developed countries wanted to keep various countries in the region in their ideological camps and aid was one of the carrots used. Today, aid to SSA countries and Africa as a whole, has been on the decline since the early 1990s. For example, aid to Africa from all donors fell from approximately US$33 billion in 1991 to less than US$20 billion in 1999 (DAC 2001). In addition, the US has a target to cut 30 percent of its US$800 million aid budget to Africa (Lippman 1996). Even those countries that were once generous with their aid to the region have developed what most development practitioners call 'donor fatigue'. It must be mentioned that with the recent support of the international community for the New Partnership for Africa's Development (NEPAD) initiative, the region has seen some increase in aid inflows. But such in flows are still below levels of 1990 and the proposed targets pledged at the United Nations Financing for Development Conference in Monterrey in 2002. But if SSA is to accelerate its growth and development, aid can help but it is not a sustainable option. This author believes that the best avenue for countries in SSA to find the requisite resources to accelerate and sustain growth and development in the region is through FDI. An overview of some of the theories of FDI in this paper will thus be appropriate.

Overview of some of the theories of FDI

The first of these theories is the neo classical microeconomic theory. It was the dominant theory used to explain reasons for FDI in flows until the 1960s (Dunning 1993). According to this neo-classical microeconomic theory, capital movements are caused by the differences in interest rates that exist between countries. From the view of this neo-classical theory, capital is a commodity, thus its price determines its supply as well as its demand and allocation. In this case capital, according to the neo-classical analysis, is determined by the interest rate (Aggarwal 1984). Capital will thus flow freely from countries with low rates of return to those with relatively high rates of return

under conditions of perfect competition (Iverson 1953). The limitation of this theory according to its critics is its inability to explain the role of Trans-National Corporations (TNCs) in capital mobility because it limits itself to explaining how and where firms decide to obtain the capital needed to finance their global plans. Critics also hold the view that because the theory does not say anything about the purpose of its investment, i.e. either for managerial control or production capabilities, its role in modern times is thus suited only to the explanation of portfolio investments rather than FDI (Hymer 1976).

Another theory of FDI is that of the intangible capital approach. According to this theory, the possession by a firm of specific 'monopolistic advantages' or 'intangible assets' is a sine qua non for its overseas production (Lall 1980). These advantages may include production techniques, managerial skills, industrial organisation, and knowledge of the product as well as the factor markets. The theory outlines three useful purposes, which these advantages must serve. First, these advantages must provide a competitive edge to the firm concerned and they must outweigh those of foreign rivals as well as those in the prospective country in which it plans to invest. Second, the monopolistic advantage that the firm possesses must be transferable abroad and should be employed most economically at the foreign location. Thirdly, the firm itself must profit from the exploitation of these advantages rather than licensing or selling them out to an independent firm (Lall and Siddharthan 1982).

The last FDI theory that this paper will review is that by Kojima. According to Kojima's theory, there are two types of FDI, macroeconomic and microeconomic. Macroeconomic FDI responds to change in comparative advantage, whilst microeconomic FDI does not (Kojima 1982; Kojima and Ozawa 1984). Macroeconomic FDI according to this theory is that which is undertaken by small firms in order to facilitate the transfer of production from high wage countries to low-wage ones. Microeconomic FDI on the other hand is that carried out by large firms aimed at exploiting oligopolistic advantages in factors as well as product markets (Gary 1982). Kojima's theory has been criticised as being grossly inaccurate and theoretically misleading because his theory rejects the basic microeconomic determinants of FDI (Arndt 1974). Arndt argues that firms, large or small, undertake FDI to overcome competition either in their home country or in a foreign one – an issue synonymous with both macroeconomic and microeconomic FDI. Other criticisms of Kojima's theory posit that the microeconomic determinants of FDI are not an alternative to a macroeconomic theory of FDI. Hence to argue that microeconomic theory fails to explain macroeconomic phenomena is invalid (Lee 1984). The overview of some of these theories of FDI offers the opportunity to understand the basic models that determine FDI

inflows. It would, thus, help to ascertain some of the determinants of FDI inflows into SSA and serve as a guide to the type of policies that should be developed by SSA policy makers to attract specific kinds of FDI.

Arguments why SSA should attract FDI

In SSA's efforts to move from the stabilisation of its economies to achieving accelerated growth, FDI inflows will help to transfer the requisite technological skills as well as the provision of the right training and management skills to local workers. FDI embodies advanced technology as well as production know-how and techniques, which firms would bring with them when they invest in SSA. It is also envisioned that FDI will encourage innovation and spin-offs. It will also enhance the productivity of the local workforce and domestic industries (OECD 1995). FDI can also help the development of capital markets in Africa to be able to attract much-needed capital for investment in large-scale projects. As foreign firms invest in SSA, they will also bring with them their existing channels of distribution and knowledge of the global market place. This will help domestic firms in SSA to gain from spillover effects. It is thus imperative for SSA to attract FDI if it is to grow and develop at this particular stage in its development history.

Furthermore, FDI will offer the much-needed capital investments in heavily populated poor countries in SSA. This capital would make it possible to employ more labour from the rural farm sector, where productivity is almost zero, in the advanced productive sector. Such a dual-economy analysis view posits that a reduction in unemployment entails some social benefits. The new workers would receive wages, which would exceed the real wages of the rural sector providing a better standard of living (Lewis 1978). An increase in wages could also lead to increased savings and investment in the domestic economy as local companies may now also have access to capital. Profits from this domestic capital could result in a further increase in wages in other sectors, due to redistribution of profits from the domestic sector as a whole. Thus, attracting FDI will bring enormous benefits to SSA.

Finally, FDI inflows into SSA will lead to an increase in exports, from which profits and an increment in income would be realised. This will help countries in the region generate much-needed foreign exchange. This foreign exchange can be used to acquire the necessary capital equipment that countries in the region need to develop other revenue generating sectors for growth and development. Countries in the region could also use this foreign exchange to pay interest or the principal on their foreign debts. Furthermore, FDI inflows into specific industries in SSA would lead to a realisation of economies of scale that most local firms do not have the requisite capital and technological know-how to achieve. This will help in the effective capacity

utilisation of resources in specific sectors and will also result in low prices for finished consumer goods as a consequence. Thus the overall benefits of attracting FDI by SSA countries according to this analysis are positive because of the contribution FDI can make to the accelerated growth and development efforts of the region.

Current trends in FDI inflows to SSA

So far, the efforts by SSA countries to attract FDI for growth and development are far from adequate. Since 1970, FDI inflows into SSA increased modestly. Average inflows to the region according to United Nations Conference on Trade and Development (UNCTAD) is put at US$1.9 billion in 1983–1987, US$3.1 billion in 1988–1992, US$6.0 billion in 1993–1997 and to $8.3 in 1998–2000 (World Investment Report, various Issues). Despite the fact that FDI inflows to developing countries in general have quadrupled from less than US$20 billion in 1981–1985 to an average of US$75 billion in 1991–1995 and US$198 billion in 1996–2000, inflows to SSA have dropped from 11 percent in 1976–1980 to nine percent in 1985, five percent in 1991–1995 and to less than four percent in 1996–2000 (UNCTAD 2001). Data by UNCTAD also show that most of the inflows of FDI into SSA go to countries with oil or minerals. For example, between 1996–2000, US$1.2 billion FDI inflows went to Nigeria, and $1.5 billion went to South Africa. Oil exporting countries in the region attracted US$2.5 billion for that period (UNCTAD 2001). This trend shows that FDI inflows into the region go mostly to resource-rich countries. This is going to continue with the increase in the price of oil, gas, gold and other commodities. Compared to other regions in the developing world, these inflows are small as evidenced by Table 5 below. The table shows a comparative distribution of FDI inflows by regions in the developing world from 1995–2000. It can be seen from the table that SSA received the lowest percentage of inflows, while most countries in Asia received the most FDI inflows. So what are some of the reasons given for such low FDI inflows into SSA compared to other countries in the developing world? These differences in low FDI inflows to SSA as compared to other developing regions in the world are ascribed to reasons that range from the negative image of SSA, portrayed especially in the Western media, the small size of its domestic markets, to the lack of the requisite infostructure and infrastructure, respect of obligations, contracts, governance, policy credibility, and the inadequate protection of intellectual property, to mention just a few (UNCTAD 2005; OECD 2003; Akinkugbe 2003). Let’s look at some of these reasons in detail.

Table 5: Regional distribution of FDI inflows, 1995–2000
(Billions of US dollars)

	1995	1996	1997	1998	1999	2000
Developed countries	203.4	219.7	2714	483.1	829.8	1,000.5
Developing countries of which:	113.3	152.5	187.4	188.4	222.0	240.2
Africa	4.7	5.6	7.2	7.7	9.0	8.2
Latin America and the Caribbean	32.3	51.3	71.1	83.2	110.3	86.2
Asia	75.3	94.4	107.2	95.6	99.7	143.5
Southeast Asia (excluding China)	37.8	49.2	54.3	42.2	55.9	96.5
China	35.8	40.2	44.2	43.8	40.3	40.8

Source: UNCTAD, *World Investment Report 2001*, 2002.

Some reasons for low FDI inflows into SSA

One of the main reasons for such low inflows of FDI into SSA can be attributed to the negative image often depicted of the continent in the media (Dagash 1998). Images of civil unrest, coups d'état, starvation, diseases and economic disorder are most common on television, in newspapers and magazines throughout most Western countries when Africa is reported about. Cases in point were the images of the civil strife in Liberia, Sierra Leone, Rwanda, Sudan, Zimbabwe, the Democratic Republic of Congo and Côte d'Ivoire that graced television screens around the world most recently. These images jaundice the view of many prospective investors who perceive the region to be unstable and hence the risks of investing in them are also perceived to be higher in SSA than in other regions. While these negative images are true of some countries in the region, it is not a true picture of the majority of SSA countries. Often, Africa is viewed as a single country rather than a continent of so many different countries with varied political systems as well as human and economic development. This view and the negative reporting about some countries in SSA have affected FDI inflows into the region.

Another reason given for low FDI inflows into SSA is the perception on the part of most Multinational Corporations (MNCs) and prospective inves-

tors that it is a region that has large unskilled labour force. This would have been an advantage when most of the previous exports of MNCs to developed countries were based on the production of labour-intensive manufactured goods. Today, advances in technology and increased competition have brought about an increase in the capital and skill intensity ratio in many industries and the goods produced. Labour costs alone today do not serve as a pull factor for FDI. A high quality, productive, well-educated, skilled and disciplined labour force is what is required to help maintain the competitive edge of most MNCs in the global market place. Because such a skilled labour force is limited in most SSA countries, it therefore serves as one of the causes of its low FDI inflows.

Poor infrastructure and infostructure of SSA countries is another reason for low FDI inflows into the region. Physical, financial and institutional infrastructures in general are less developed. Roads, telecommunications, ports and airports are poor or undeveloped and thus hamper business growth and efficiency. For example, road transport in the region accounts for 80 to 90 percent of SSA's passenger and freight movements (*The Economist* 1995). But because little has been done to maintain these roads, most of them are in disrepair and this situation hampers transportation of inputs as well as finished goods for export. The same can be said of most of the telecommunications infrastructure in the region, which is underdeveloped and in most countries non-operational. In the current knowledge economy, a good infrastructure and infostructure are a sine qua non to business growth and competitiveness of countries (Abdulai 2001). Those countries without such infrastructure are going to lag behind in their ability to attract FDI. Investors today like to be able to get in touch with their respective head offices and families with ease when they are abroad, check their e-mails and undertake other transactions from their phones or computers. It is difficult to do so from areas with poor telecommunications infrastructure as it is the case in most countries in SSA. The poor nature of SSA's infrastructure and infostructure adds an enormous cost to doing business in the region and thus hinders FDI inflows.

Furthermore, even though most SSA countries have liberalised their economies and investment policies to make it easy for foreign companies to invest in certain sectors, many countries in the region still restrict entry into other sectors of their economies in response to pressure from domestic interest and pressure groups. Such discriminatory investment policies affect FDI inflows. In addition, most of the countries in the region do not have in place the requisite legal structures and reforms to protect foreign investors, especially in the wake of internal upheavals. The few that have undertaken legal reforms do not effectively enforce them. Many prospective foreign inves-

tors thus worry that without such legal sureties, they may have their investments and properties nationalised or expropriated by the state for arbitrary reasons as it has been the case in some African countries in the past.

Prospective investors also fear that they may not get proper justice in the settlement of disputes because of the poor judicial systems in the region. The perception is that the weak judicial systems in most countries in SSA would make it hard to enforce contracts once they are broken. Some countries do not have effective courts or institutions for arbitration of business conflicts. Thus the issue of sanctity of laws is of extreme importance and needs to be seriously addressed if SSA countries are to attract FDI. For example, many investors who won government contracts from Nigeria during the last days of military rule in that country saw their contracts cancelled when the civilian regime of Olusegun Obasanjo took over. The Obasanjo civilian government sensing how such an act could affect FDI inflows into Nigeria argued that the former military governments of Nigeria for the past 29 years were corrupt. Hence, most of the contracts these regimes awarded were not on the basis of competitive bidding to allow the country to benefit from the skills of the best companies and their products for the money. The government also set up an anti-corruption agency and a special tribunal to search and seize 'ill-gotten wealth' and to stamp out bribery and theft in the country (*Wall Street Journal Europe* 1999). It was thus acting in a way to counter the negative image of corruption in Nigeria, which affected FDI inflows. Yet, despite the good intentions, the perception the action created can have adverse effects on FDI inflows into the country and possibly into Africa, as most potential investors can always point to Nigeria's example as a high risk and a reason not to invest in SSA.

The aforementioned observations raise the importance of corruption as a hindrance to attracting FDI in SSA. Corruption in the public sector and judiciary systems in most SSA countries has always been cited as one of the reasons that deter investors from the region (Bhattacharya, Montiel, Sharma 1997). Corruption increases transaction costs, creates bottlenecks, inconveniences and it is often risky. Formerly, most European firms who wanted to invest in SSA and other parts of the developing world could regard bribes and other corrupt practices as a cost of doing business. These costs were allowed by some European governments as tax-deductible at the end of the fiscal year. This is no longer acceptable since the Organisation of Economic Co-operation and Development's (OECD) anti-bribery convention came into force. European firms who bribe foreign countries for contracts could face prosecution and bad publicity at home. This holds true for US firms as well with the passing into law of the Foreign Corrupt Practices Act (FCPA) in 1977, amended in 1988. This act makes it a criminal offence for US busi-

nesses to pay any money or monies as bribe to government officials abroad in exchange for business. The ability of such laws passed in the West to stop corruption is laudable. It is hoped that corrupt officials in SSA will see the light and desist from their nefarious ways as they have a severe impact on the flow of FDI into the region.

Furthermore, many SSA countries still have overvalued currencies and others still impose restrictions on foreign exchange transactions. The advent of adjustment policies in the region has forced many countries to liberalise their foreign exchange systems. However, many of these foreign exchange liberalisations have been accomplished by decree without a follow-up on the part of many governments in the region with the requisite legislative instruments to support their enforcement. This creates an uncertain atmosphere for prospective investors as they grapple with the possibility of being able to repatriate their profits and this can affect FDI inflows into the region.

Finally, the small size of domestic markets in the region has been held out as another reason for the low FDI inflows. Because of competition amongst MNCs, they produce for both domestic and foreign markets. Thus, market size is an important FDI determinant. Unfortunately, most domestic markets in SSA are fragmented and small and cannot effectively demand goods produced by the MNCs. In addition, if domestic markets in SSA were large, MNCs could experience economies of scale because they could increase production with the cost per unit of output being low. Thus, because most domestic markets are small in SSA, it affects FDI inflows. Most countries in South East Asia as well as China faced the same problems of attracting FDI a while back. But these countries have been able to overcome these problems through regional integration and are now attracting more FDI than most regions in the world. This author has the confidence that SSA can do the same. Section VI of this paper looks at some of the policy options available to SSA countries and the requisite strategies they can adopt to bring about an increase in FDI inflows into the region.

Policy options for SSA countries to attract FDI

In view of the reasons given so far that hinder the flow of FDI into the SSA region, it is therefore imperative that leaders in the region formulate appropriate policies to help them attract more FDI. However, developing appropriate policies and strategies alone is not enough. Governments and policy makers in the region must make sure that the policies and strategies they develop and implement are effective and investor-friendly based on specific and achievable goals. They must also initiate Investment Policy Reviews (IPRs) in collaboration with United Nations Conference on Trade and Development (UNCTAD) as well as their bilateral partners. IPRs would help SSA coun-

tries improve their investment climates and enable the international private sector to become familiar with the investment climates in their respective countries.

The following are some of the suggested policy options and strategic alternatives that SSA policy makers should consider: First policy makers in SSA must create and foster an enabling environment. This environment should include policies that aid the development of the private sector as well as collaboration between the public and private sectors to help in the proper functioning of markets. SSA leaders must also continue to deepen macroeconomic reforms. Emphasis should be placed on the reduction of fiscal deficits, inflation, interest rates and the strengthening of their various financial systems. The setting up of efficient securities trading and settlement systems and the presence of international custodians are important elements of such a financial infrastructure (Battacharya, Montiel and Sharma 1997). SSA countries should also provide conducive and well-structured institutions to support investor friendly policies. These should include well functioning legal institutions that support market transactions, protect property rights as well as laws that protect investors in times of upheavals or any sudden changes in the legal and economic environment.

The signing of Bilateral Investment Treaties (BITs) by most countries in SSA aimed at protecting and promoting FDI, clarifying the terms under which this FDI can take place between them and partner countries, is a step in the right direction. But such efforts need to be deepened. For example, as of January 1999 according to UNCTAD, SSA countries signed 335 BITs. These treaties contribute to a more secure environment for foreign investors in the region. The conclusion of Double Taxation Treaties (DTTs) by most countries in SSA is another encouraging step in an effort to attract FDI into the region. DTTs help prospective investors avoid paying taxes twice on the same transactions. Many countries in the region can learn from the example of Uganda, which concluded three of such DTTs in 1997 with Kenya, South Africa and Tanzania (Uganda Investment Authority 1998). Hopefully, many SSA countries will follow these examples.

Second, the issue of peace and stability in the region must be addressed with increased urgency as the impact on FDI inflows cannot be emphasised enough. The extra costs of security for firms who wish to invest in SSA and those who are already in the region especially in areas of instability are high. Firms have to spend extra money on security guards and equipment just to stay in business. The headaches and extra cost from the view of many prospective investors makes such investment efforts not worth it. Hence they stay away. Conflict prevention, peace and stability in SSA would help create a favourable economic environment, which would allow the imple-

mentation of sound investment friendly policies to attract FDI. Also with the end of the Cold War, SSA leaders can no longer play the erstwhile superpowers against each other and point to them as the source of their instability. They must begin to accept responsibility for the role they have also played to fan these conflicts. Thus, leaders in the region must find ways to prevent conflicts before they arise and intervene to put down conflicts, as has been the case in Liberia and Sierra Leone by the ECOWAS Cease-fire Monitoring Group (ECOMOG) in West Africa (French 1996). Stability on the continent will serve as an impetus and an encouragement to investors to see SSA as a safe investment environment and destination. The recent establishment of a Rapid Response Team to intervene in conflicts before they become unmanageable by the African Union is a step in the right direction. Mention should also be made about the efforts of the African Union troops monitoring the peace in the Darfur region of Sudan as laudable efforts aimed at bringing peace and security to Africa, an indispensable feature in the effort to attract FDI to the region.

Attaining peace and stability in the region would also help governments in the region not only to divert resources from armaments to the training of the labour force to develop the requisite skilled and competitive work force for their own development purposes but also to attract FDI. Equally important is the training of skilled and motivated administrative and managerial personnel in both the public and private sectors in the region. Such an educated and knowledgeable work force will serve as a strong support of policies and help in their effective implementation as well as working in symbiosis with the private sector to achieve the requisite development goals of the various countries. SSA in actual fact had a 56 percent illiteracy rate and a 19 percent secondary school enrolment rate as compared to the 36 percent and 45 percent in Asia (IMF 1999). Such low literacy rates will inevitably have an impact on human resource development and can contribute to the less attractiveness of the region for FDI inflows. SSA governments must therefore reduce their share of GNP spent on defence and increase the share of Gross National Product (GNP) spent on the education of its people and on the development of its human capital.

Governments in SSA must also invest in the building of their communications, roads and technology infrastructures or form partnerships with the private sector in their various countries and in the region to develop these infrastructures. Good infrastructure contributes to the lowering of transaction cost and serves as an impetus to FDI inflows. But having good infrastructure alone is not enough. Competition for FDI around the world is more intense than it has ever been. Hence SSA countries must do more to promote their various countries in key countries around the world. To cut cost on

these promotional activities, SSA countries should consider joint efforts and activities to promote the entire region as an investment destination to encourage FDI inflows. The example of the Southern African Development Community (SADC) countries is a case in point. In June 1998 in Centurion, South Africa, these countries formed the SADC Committee of Investment Promotion Agencies. Later in July of the same year, they set up a committee on investments, which was charged with the task of providing input to SADC's Finance and Investment Protocol. This will help bring the region in line with current global investment agreements and facilitate cross-border investments. Furthermore, most of the investment promotion agencies in the region are joining the World Association of Investment Promotion Agencies (WAIPA) to enable them benefit from such an association and from the exchange of information on best practices in investment promotion (Tillett 1996).

Since market size has been one of the factors hindering the flow of FDI into the region, SSA governments must develop effective methods to create large markets to make the region attractive for more FDI inflows. A good way to begin is through the expansion of markets in the different regions in SSA. The August 1996 trade protocol between the fourteen SADC countries to create a free trade area by 2004 is a good example in this direction. This will facilitate trade and investment in the framework of the Common Market for Eastern and Southern Africa (COMESA). Mention should also be made that efforts are being undertaken between East and West African countries in advancing integration in their sub-region as per the recommendations of the Lagos Plan of Action. Such efforts when realised would lead to the creation of a significant market size which will serve as a pull for FDI into the region.

Finally, SSA governments and leaders should endeavour to create trust between themselves and their people as well as with their domestic entrepreneurs. They should also encourage their citizens residing abroad to invest in their various countries. SSA leaders and policy makers should keep in mind that the action of domestic businesses as well as its citizens is an important indicator of conditions in a country. Hence it can affect FDI inflows. A study by UNCTAD secretariat states that only three percent of FDI stock in Africa originated from the continent itself, compared to close to 30 percent in South, East and South East Asia (UNCTAD 2005). The confidence of local businessmen and women in the economies of their various countries serve as a barometer for foreign investors who are willing to invest in these countries. After all, why should foreign investors want to invest in a country or region in SSA in which its own citizens do not want to invest? SSA governments and leaders should also take the lead to eradicate the negative image and

perception of Africa that prospective investors may have, through a well-planned continuous education effort, and better-targeted promotion methods. Despite the aforementioned proposals that SSA governments must undertake to help them attract FDI, the role of multilateral and bilateral efforts in this schema cannot be emphasised enough.

Multilateral and bilateral initiatives

Multilateral and bilateral organisations are essential vehicles that SSA can use to attract FDI. Multilateral organisations can help fill in the gap created by limited investment or the lack of it in certain sectors of SSA by the international private sector. An econometric study conducted by UNCTAD which investigated the 16 largest economies in Africa showed that multilateral and bilateral lending tends to be a catalyst for private capital inflows. Mention should be made that this relationship does not hold for grants (UNCTAD 2000). Most international private companies are not willing to invest in infrastructure and social welfare projects especially when these projects have no direct or complementary benefits to their businesses. Multilateral and bilateral organisations should provide the necessary financing or guarantees that will enable the international private sector to undertake these projects.

Another way multilateral and bilateral organisations can help is by finding host country partners willing to invest in SSA. This could be done after they have developed projects or when opportunities have been identified in certain sectors in the region. They could also offer subsidies to make up for market imperfections (Berlot and Weigel 1992). It will help provide the necessary FDI to SSA countries; as well as provide profits for companies in developed countries who will otherwise have no clue as to how realise these opportunities.

Furthermore, most potential investors in SSA are often unaware of the investment opportunities in the region. Efforts by international organisations like UNCTAD, Multilateral Investment Guarantee Authority (MIGA), Overseas Private Investment Corporation (OPIC) and similar reputable organisations should help in getting this information to the investing community. An example of such efforts include 'investment guides and capacity-building in least developed countries', launched by UNCTAD and the International Chamber of Commerce (ICC).

In addition, multilateral and bilateral organisations should act decisively to forgive SSA's crippling debt that amounts to more than US$10 billion a year from African countries alone. The debt has been a big impediment to the creation of a good investment climate for investors. One of the ways SSA's debt affects FDI is that it creates balance of payment problems which directly affect the ease in which investors can repatriate profits because of

the numerous regulations that might be put in place to ration foreign exchange. Besides, debt affects savings on the part of the government to undertake improvement of physical and human infrastructure, which is one of the pulls for FDI. Furthermore, in SSA, income levels are rather low to be able to generate adequate domestic resources for the attainment of even modest rates of investments and growth. Debt forgiveness can help alleviate this challenge. It must be mentioned that multilateral and bilateral organisations have started the process of relieving the debt of some SSA countries under the HPIC programme. So far, African countries like Ghana, Uganda, Zambia, Kenya and Burkina Faso amongst others, are some of the countries that are going to benefit from the HIPC programme. But this process should be speeded-up to bring debt relief to some countries in SSA which will free up resources for investment in infrastructure, health, education and training. Mention should be made that at the time of this writing, some countries in SSA have started to benefit from the HIPC initiative.

Multilateral and bilateral organisations should also increase technical assistance as well as convince most of the rich countries whose members comprise the boards of these organisations to do likewise. An increase in technical assistance would help most of the countries in SSA to overcome the lack of sufficient skilled personnel in key sectors as well as sectors that will help draw in FDI. Assistance should also be given in the form of troop enforcement, training and logistics to help restore stability to most of the troubled spots in the region that gives the whole region a negative image and subsequently affecting FDI inflows to the region.

Finally, multilateral organisations like the World Trade Organization (WTO), which is calling on developing countries to open their markets to goods and services from developed countries, should persuade developed countries to do likewise. They should open their markets to non-traditional exports and labour intensive goods from SSA. Access to the markets of developed countries could help entice MNCs to locate their production facilities in the region, thus attracting more FDI into the region. The US African Growth and Opportunity Act (AGOA) that allows textile exports duty free access to the US market is a step in the right direction. But more needs to be done. Equally, the US and European countries should stop the subsidies of their agricultural sectors to enable farmers in SSA to be able to compete. For example, the European Union alone spends about 43 billion euros annually on farm subsidies; and the US subsidises its cotton farmers to the tune of US$40 billion a year. The ability of African farmers to compete on the international market on an equal footing will go a long way to attract foreign investment into the agriculture industries in these countries and help in their growth and development efforts.

Conclusion

The challenge of attracting substantial FDI into SSA is multifaceted; as a result, efforts to tackle these challenges require ingenuity and collaboration among the various stakeholders in the region, with appropriate solutions and directives devised and put in place. The challenge is not only the duty of policy makers and economic blocs such as the SADC and ECOWAS in the region but also that of the individual countries. While policy makers and economic blocs attempt to make the region a better place for the people of Africa as well as for foreign investors to invest in, respective countries must ensure political and economic stability. Hence, these countries must continue to deepen reforms. Such reforms should include the promotion and adherence to good governing practices in the region, transparency and accountability in managing all public resources, and the conduct of government officials in the day-to-day running of the country should be beyond reproach. Bilateral and multilateral organisations can only help to champion SSA as an attractive place to invest but that might not pull in a lot of FDI. Consolidating macroeconomic stability should be a continuous process in the region. Policy makers should continue to implement sound fiscal and monetary policies to reduce inflation and government budgetary deficits. A reduction in government budgetary deficits would spare resources to develop physical as well as financial infrastructures to be able to attract more FDI. Governments in the region must also work hard to eradicate the perception of the region as one that is unstable to invest in. They must also vigorously promote opportunities for investment in their respective countries in strategic markets around the world to stimulate FDI inflows into the region.

Notes

1. In 2001, Côte d'Ivoire, Gabon, Liberia and Zimbabwe registered negative GDP growth. For Zimbabwe, the reason could be the land redistribution problems while in Côte d'Ivoire the situation is due to the political unrest.
2. Foreign Direct Investment (FDI) as used in this paper refers to investment by foreign businesses in SSA, whereby such an investment guarantees them full ownership, partial ownership or a controlling interest in the business or its subsidiaries.

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