UNITED NATIONS

A

General Assembly

Distr.
GENERAL

A/43/500/Add.2
15 August 1988

ORIGINAL: ENGLISH

Forty-third session
Item 39 of the provisional agenda*

CRITICAL ECONOMIC SITUATION IN AFRICA: UNITED NATIONS PROGRAMME OF ACTION FOR AFRICAN ECONOMIC RECOVERY AND DEVELOPMENT 1986-1990

Mid-term review of the implementation of the United Nations Programme of Action for African Economic Recovery and Development 1986-1990

Report of the Secretary-General

Addendum

Investment of transnational corporations in Africa

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* A/43/150.

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I. INTRODUCTION

1. It is widely acknowledged that transnational corporations (TNCs) can contribute significantly to the economic development of developing countries. They can provide much needed foreign direct investment (FDI). They can accelerate the transfer of technology, provide employment and enrich human resources development. They can also provide access to external markets and credit. At the same time, various negative effects can be associated with activities of TNCs. Governments of host countries have to take care, therefore, that in formulating policies and in their negotiations with TNCs the negative effects are minimised while positive ones are maximized.

2. The present report probes the opportunities and impediments to greater involvement of TNCs in Africa's development. The major focus is on broad measures to increase FDI and its qualitative impact on development, recognising that each country has itself to decide the extent and forms of co-operation it seeks with TNCs in order to maximize the benefits of such co-operation.

3. The report was prepared by the United Nations Centre on Transnational Corporations at the request of the Economic and Social Council (decision 1988/161 of 27 July 1988). It draws on research and advisory activities undertaken by the Centre in support of the implementation of the United Nations Programme of Action for African Economic Recovery and Development 1986-1990 (General Assembly resolution S-13/2 of 1 June 1986).

II. TRENDS IN FOREIGN DIRECT INVESTMENT

4. Africa receives less than 15 per cent of the total flow of foreign direct investment to developing countries. Unlike Asia and Latin America, FDI in Africa is largely in the primary sector (see figure), particularly petroleum and mining. 1/ FDI inflows are an insignificant source of external financing, as Africa depends predominantly on official resource flows. 2/ Detailed information regarding the role of TNCs in manufactured exports from African developing countries and the transfer of technology to them is not available; indirect evidence strongly suggests that it is not important.

5. As in other developing regions, FDI flows to Africa are heavily concentrated in a few countries, particularly the oil-exporting economies (see table). Eight countries absorbed two thirds of the inflows in 1982, and they increased their share further to four fifths by 1986. Flows to Egypt have accelerated rapidly, to over $1 billion in 1985. However, 80 per cent was in the oil sector rather than in other primary commodities, manufacturing or services.

6. The volume of FDI in the rest of Africa is of an entirely different dimension. Total annual flows have declined 45 per cent since 1980, to about $400 million. Even for middle-income countries (such as Côte d'Ivoire, Morocco, Zambia and Zimbabwe), FDI flows remained quite modest, rarely $50 million per year. For low-income African countries, net FDI flows ranged from a negative balance to a few million dollars per year in most cases.

Figure. Foreign direct capital stock

(percentage distribution, 1982)

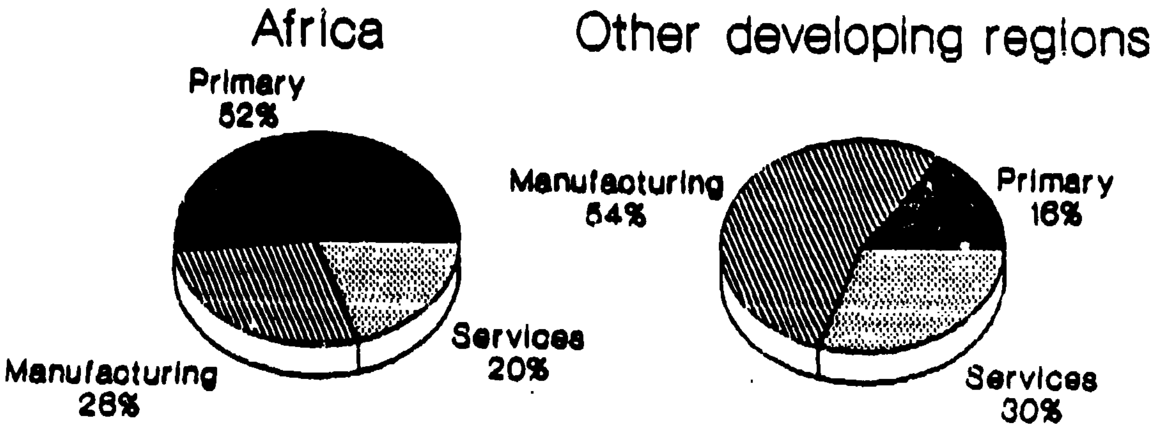

Table. Foreign direct investment inflows, 1975-1986

(Millions of dollars)

Region/country	1980	1981	1982	1983	1984	1985	1986	Annual average 1975-1980	Annual average 1981-1986
All countries	52 240.2	56 504.0	44 072.0	43 888.7	48 652.9	47 958.8	64 449.4	32 208.2	50 921.0
Developing countries	10 978.7	14 126.2	14 210.0	10 575.5	11 220.3	12 803.5	13 046.3	7 343.1	12 663.6
South Europe	68.5	147.1	76.4	88.7	128.0	132.8	175.1	81.7	124.7
Latin America	7 159.3	7 158.4	7 412.0	3 945.7	4 126.3	5 386.5	4 531.2	4 462.7	5 426.7
Other Asia and Oceania	3 197.1	5 249.9	4 815.6	4 720.4	4 845.6	4 639.8	5 622.8	2 009.0	4 982.3
West Asia	257.3	-11.0	395.0	309.1	627.2	583.7	572.6	565.8	412.8
Africa	296.6	1 581.7	1 511.1	1 511.5	1 493.2	2 060.8	2 144.6	823.9	1 717.2
Oil exporters	-499.0	1 102.1	976.2	1 130.1	1 107.6	1 662.8	1 712.6	267.8	1 281.9
Algeria	348.8	13.0	-54.1	..	1.0	..	..	165.8	-6.7
Angola	..	..	..	..	..	..	..	..	..
Cameroon	129.8	135.4	111.4	213.8	17.6	316.0	..	47.4	132.4
Egypt	547.9	752.3	293.7	489.6	728.8	1 177.8	1 217.7	376.1	776.6
Gabon	31.5	54.6	131.8	111.8	8.1	15.1	120.8	63.9	73.7
Nigeria	-739.3	546.0	429.5	353.8	188.6	341.2	195.9	163.3	342.5
Libyan Arab Jamahiriya	-1 089.4	-744.0	-391.9	-327.1	-17.4	-315.8	..	-659.2	-299.4
Tunisia	234.3	296.0	340.0	183.9	113.8	107.6	63.4	103.8	184.1
Non-oil exporters	795.5	479.6	535.0	381.4	385.6	398.0	432.1	556.1	435.3
Benin	4.3	2.1	..	..	..	..	..	2.7	0.4
Botswana	111.5	88.4	21.1	23.8	62.1	53.6	90.5	44.3	56.6
Burkina Faso	-	2.5	2.0	2.0	1.6	..	..	1.7	1.4
Burundi	..	..	..	..	..	..	..	..	..
Central African Republic	5.3	5.8	9.2	4.5	5.1	2.9	..	6.8	4.6
Chad	-	-	-	-	9.2	53.6	28.2	17.1	15.2
Congo	40.1	30.9	35.3	56.1	35.0	12.7	22.4	13.2	32.1
Cote d'Ivoire	94.6	32.8	47.5	37.5	3.0	29.1	..	63.5	25.0
Ethiopia	..	..	..	..	..	..	..	4.9	..
Gambia	-	2.1	..	..	..	..	..	2.5	0.4
Ghana	15.6	16.3	16.3	2.4	2.1	5.6	4.3	15.7	7.8
Guinea	33.7	..	..	..	..	..	..	10.2	..
Kenya	79.0	14.1	13.0	23.7	10.8	18.1	32.7	52.9	18.7
Lesotho	4.6	4.8	3.1	4.8	2.4	4.8	2.1	0.8	3.7
Liberia	-	-	34.8	49.1	36.2	-16.2	-5.7	27.4	16.3
Madagascar	..	..	..	..	..	..	..	-1.1	..

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Table (continued)

Region/country	1980	1981	1982	1983	1984	1985	1986	Annual average 1975-1980	Annual average 1981-1986
Malawi	9.5	1.1	-	2.6	-	0.5	..	6.9	0.7
Mali	2.3	3.7	1.5	3.1	4.1	4.5	4.3	1.6	3.5
Mauritania	27.1	12.5	15.0	1.4	8.5	7.0	4.5	-4.0	8.1
Mauritius	1.2	0.7	1.8	1.6	4.9	8.0	7.4	2.8	4.1
Morocco	89.8	59.0	79.5	46.0	47.2	20.3	..	45.2	42.0
Mozambique	..	..	..	..	..	..	..	..	..
Niger	49.1	-6.1	28.3	1.2	..	..	..	30.7	3.9
Rwanda	16.4	18.0	20.8	11.1	15.1	14.6	17.6	7.9	16.2
Senegal	14.4	34.3	28.0	-34.7	29.1	..	..	17.5	9.5
Seychelles	9.5	10.1	10.0	9.2	9.9	11.7	14.2	6.1	10.9
Sierra Leone	-18.6	7.5	4.6	1.7	5.8	-3.8	-6.5	7.6	1.6
Somalia	-	-	-0.8	-8.2	-15.0	-0.7	-0.1	2.8	-4.1
Sudan	-	-	-	-	8.8	-2.[illegible]	..	-	1.0
Swaziland	26.4	38.8	-9.2	1.2	3.8	10.9	16.0	24.2	10.2
Togo	42.3	10.1	16.1	1.5	-9.9	..	..	35.1	3.0
Uganda	..	..	..	..	..	..	..	1.1	..
United Republic of Tanzania	..	..	..	..	..	..	..	..	..
Zaire	..	..	..	..	..	..	..	54.9	..
Zambia	61.2	-38.9	38.6	25.7	17.4	..	..	36.9	7.1
Zimbabwe	1.6	3.8	-0.7	-2.0	-2.5	2.8	5.2	0.1	1.1

Source: United Nations Centre on Transnational Corporations, based on International Monetary Fund, balance-of-payments computer tape and national and international source.

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7. However, in some countries and in some sectors, TNCs have a significant and even dominant role. For example, in Kenya, Malawi, Somalia, Uganda, the United Republic of Tanzania, Zaire and Zambia, TNCs own controlling interest in plantations in a number of agricultural crops (such as banana, cotton, coffee, palm oils, rubber, sugar, tea, vegetables and flowers). TNCs also enjoy a dominant position in non-fuel minerals in some low-income countries, for instance, in copper in Botswana and Zaire, and bauxite in Ghana and Guinea.

8. Where the African private or state enterprise sector is small or growing slowly, even modest inflows of FDI can disrupt the desired balance between indigenous and foreign ownership, as defined by national objectives. Foreign ownership in manufacturing appears to have declined in some African countries since the 1960s, partly due to divestment policies. Nationalisation is no longer a common phenomenon; Africanization, indigenisation or greater state ownership are now achieved by negotiation. Nevertheless, the size and rate of growth of domestic enterprise, the degree of foreign ownership that is considered appropriate and the extent to which the fears of foreign investors can be allayed are important institutional determinants of FDI in Africa.

9. The global determinants of FDI flows, according to various economic projections, suggest that foreign investments in Africa are likely to remain much more resource-related than in other developing regions. While the relative prospects for extractive sectors are good, the implication of further primary sector investment is that Africa's export revenues will continue to come from a narrow range of commodities with unpredictable world market conditions and volatile prices.

10. Africa's internal developmental needs are potential opportunities for foreign investments in new activities. However, growth prospects would need to be more favourable than at present. Intra-regional trade, which is frequently an intermediate step for foreign investors from import substitution into production for industrial country markets, could provide additional stimulus. There is evidence to suggest that the lowering of cross border tariffs will lead to increased trade among members of the Preferential Trade Area for Eastern and Southern African States (PTA). The domestic equity regulations for the applicability of preferential tariffs, however, have had a negative effect on foreign investment.

11. In summary, the prospects for FDI as a source for non-debt-creating resource flows to stimulate Africa's recovery and development are not promising. The present very small flow of foreign investment, relative to other developing regions or as a source of foreign financing, necessarily means that even if FDI flows were expected to increase rapidly, and more rapid than in other developing countries, FDI would continue to be of minor importance, unless international co-operation alters its role.

III. OPPORTUNITIES FOR INCREASED INVESTMENT

A. Economic reforms

12. The 1980s have witnessed a more welcoming attitude to foreign private investment by many African countries. In addition to those countries that have signed international agreements, such as that of the Multilateral Investment Guarantee Agency (MIGA), or bilateral agreements with home countries of TNCs, between 1982 and 1987 more than one third of African countries either introduced or made adjustments to their investment codes or guidelines in order to attract foreign investors. Other measures have included (a) incentives traditional to foreign investment promotion like tax holidays (for up to 10 years), for example in Mauritius, (b) removal of controls on remitting dividends, or relaxation of rules on retaining export income (for example in Nigeria, Mauritius and Zambia) and (c) simplified approval procedures (as in Angola). Countries previously considered not congenial by private foreign investors, such as Mozambique and Guinea, have introduced new legislation offering a wide range of guarantees and opportunities for foreign investors.

13. In March 1988 Nigeria announced radical changes in laws affecting foreign investment. Foreign investors can now hold 80 per cent of the equity of agricultural enterprises and of those listed in "schedule three" of the Nigerian Enterprise Promotion Decree; "schedule one" companies will now accommodate up to 20 per cent foreign ownership; and "schedule two" companies will now be recognized as fully Nigerian enterprises for the purposes of entering joint ventures with foreign partners. Other domestic measures include the establishment of export processing zones.

14. Promotion of foreign investment in Africa, and also in Asia and Latin America, is principally intended to attract investment either by new foreign investors or perhaps investments into new activities by existing ones. In practice, it has meant increased investment opportunities for subsidiaries of the large number of TNCs already present on the continent. These opportunities, especially when accompanied by favourable economic conditions across the economy, have been particularly important in countries where a backlog of retained but unremitted earnings exist. Inasmuch as these investments reduce the outflow of earnings they provide a significant boost to the balance of payments, particularly for Africa.

15. There is growing evidence of substantial investment being undertaken or planned by TNCs with a long history of involvement in Africa. In Nigeria, for example, UACN, John Holt, Lever Brothers, Johannes Rau, Metal Box and Dunlop are all either expanding their operations or moving into new areas of activity but with very little new external equity. In Kenya, the Del Monte subsidiary, Kenya Canners Ltd., is involved in a $25 million investment and expansion programme. In Zimbabwe, various TNC subsidiaries have reinvested from $10 million to over $150 million between 1980 and 1986.

16. Countries where changes in policies have led to significant inflows of foreign private investment include Gabon and Mauritius; in the latter the number of firms operating in the Export Processing Zone has risen from 10 in 1971 to over 450

today. In other instances, more favourable policies in relation to particular subsectors have led to significant inflows of foreign investment into these subsectors; this would be true for Ghana following the introduction (in 1986) of its new minerals investment code.

17. However, FDI incentives are unlikely to be successful in the absence of macroeconomic policies important to TNCs. There are instances where inflows of FDI were impeded not because of foreign investment legislation but because of unfavourable perception of macroeconomic policies, particularly those aspects related to foreign exchange allocation and price controls.

18. Adjustment programmes can also discourage FDI, particularly when the programme is intended to have a deflationary effect. If it includes tariff reform, reduction in protection may be actively opposed by foreign investors. Any change in policy must also face the twin problems that that change needs to be seen as credible and permanent, while not itself provoking the foreign investor's complaint that policies are too often changed.

19. Thus, there are often trade-offs between the three sets of considerations important to investors: the particular economic opportunity that they hope to seize; general economic conditions; and current government policies. Both the evidence on the ground and surveys of foreign investors' views show clearly that all three matter and probably in the order just listed.

20. It should be stressed that, although it is usually necessary to improve both the general climate for foreign investment and the range of particular incentives in order to increase the inflow of foreign investment, such improvement is not a sufficient condition. For instance, few countries in Africa have a more liberal set of incentives for foreign investors than does Gambia, yet there has been hardly any increase in foreign investment in that country following the introduction of more favourable policies. Similarly, the long-term welcoming attitude to foreign investment of Botswana has led to little substantial investment in the manufacturing sector.

21. In summary, while policy change certainly improves the climate for FDI in Africa, one cannot be too sanguine about the overall impact, especially when viewed in the global perspective. Many Latin American and Asian countries relaxed their controls on FDI in the mid-1970s. The fact that African countries are now easing restrictions already removed or relaxed in other regions may not be viewed as a special opportunity by TNCs.

B. Equity sales, swaps and other forms

22. The selling of state or parastatal enterprises has become a widespread phenomenon throughout Africa in recent years. Purchases have been taken up by foreign private investors or are under their active consideration in a number of countries involving a wide range of activities. 3/ Ghana, for instance, has recently named 32 more domestic companies for which it is seeking foreign purchasers.

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23. One of the main purposes of the move to privatisation has been to raise the efficiency of state or state-related operations. In these cases, the capital-supplying role of foreign investment is less crucial than in the policies considered in paragraphs 12 to 21 above. In some cases other forms of participation have occurred. Zaire is an example of a country that after failing to attract equity participation, arranged management contracts for its airline and its copper and gold mines.

24. It has also been far from uncommon for new TNCs to invest in some parts of Africa in order to replace TNCs that wish to withdraw. While initially this does not lead to a net increase in foreign equity, foreign exchange gains have frequently occurred both as a result of expanded investment and greater export earnings. Additionally there have been opportunities for foreign firms to take over all or partial interests in local private companies, as happened for instance in early 1988 when DAF Trucks of the Netherlands took up shares in Kabwe Transport in Zambia.

25. Perhaps of wider applicability has been the increasing participation of foreign investors in investment packages that include non-African international institutions such as the International Finance Corporation (IFC), the Commonwealth Development Corporation (CDC), the Deutsche Finanzierungsgesellschaft fuer Beteiligungen in Entwicklungslandern (DEG), the European Investment Bank (EIB) and OPIC. A whole range of packages has been designed involving one or more of the following: local private investors, government participation, local or regional bank participation and the involvement of more than one foreign investor, with investment or management advice from the international agency. Some recent examples of these sorts of foreign investment would include the Utexafrica textile project in Zaire, the Lonrho/International Finance Corporation (IFC) farm projects in Mozambique and a number of ventures of Bookers with IFC and CDC. But it is notable that in comparison with other regions, Africa receives only a small proportion of these agencies' attention, whether measured by number of projects or share of financing.

26. In noting these examples where the role of actual new capital is limited, it is important to keep in mind the original purpose of encouraging foreign investment. This would be equally true of any large-scale spread to Africa of the new forms of foreign investment that increased in other developing countries in the 1970s or of the use of debt-equity swaps.

27. New forms of foreign investment include joint ventures between foreign and local capital or between foreign capital and some other local contribution, such as knowledge of local markets or political support or between local capital and some other foreign contribution such as initial design, management, training or technology contracts, or commitment to buy some proportion of the output. Countries that pursue this route have the advantage of obtaining a specific element of foreign investment without sacrificing other elements of local control or content. New forms of investment generally involve less capital contribution by TNCs, but capital is precisely what most African countries promoting investment want, and there often is little local capital to complement it. Such new forms of foreign investment are therefore likely to be suitable on a selective basis in current African conditions.

28. Debt-equity swaps also have limited applicability, given the much smaller weight of commercial debt in African liabilities. In Egypt and Nigeria, there is considerable interest in the potential for debt/equity conversion schemes, which TNCs maintain will enhance their willingness to invest in the economy, and at least one company is considering it in Zambian agriculture. Normal current practice is for banks to sell debt paper to the foreign investor for foreign currency at a deep discount, and for the foreign investor then to buy equity (usually at some, but a smaller, discount) receiving the equivalent of the local currency value of the debt. However, if the investment would have been made in any case, the country loses the full amount of new foreign capital, while gaining, in the short run, only the foreign exchange saving on servicing the debt. Foreign exchange controls, which (as discussed in paras. 61 and 62 below) are usually seen as a hindrance to foreign investment, must be in effect to restrict the immediate repatriation of the value of the equity.

29. Foreign investors in Africa are not unaccustomed to using blocked capital for foreign investment, and may gain advantages from their national guarantee agencies if this is treated as new investment rather than reinvestment. This is a benefit if there is idle capacity for investment, and presents some reason why investment is possible for a foreign company but not for a local one (for example, restrictions on the activities or the local borrowing capacity of the national government). If not, and the unemployed resources are not there, the locally financed foreign investment will simply crowd out other investment.

30. Finally, there are instances of foreign investors bringing in capital to Africa as a result of participation in projects supported by aid monies. One instance of this occurred in Angola when in late 1987 DAF Trucks of the Netherlands won a $17 million contract to assemble a range of vehicles partly as a result of a mixed credit scheme from the Government of the Netherlands.

C. Sectoral opportunities

31. Agriculture and minerals are the two important sectors for many countries in Africa. Agricultural development is a priority of the United Nations Programme of Action, and has also benefited from a substantial recent expansion in the export of tropical and sub-tropical horticultural and processed products to major world markets such as the European Economic Community (EEC). While part of this expansion has been caused by a drop in imports from South Africa, there are also independent indications of additional demand for such products within EEC and Scandinavian countries. This expansion could be reinforced by technological innovations both in improving the productivity of crops and in transport, which make trade in perishable crops more profitable and more feasible. Further in the future, the prospect for real progress in reducing controls on agricultural trade in the industrial countries by the end of the present round of the General Agreement on Tariffs and Trade (GATT) could provide extra opportunities.

32. The comparatively high profits earned by TNCs in African agriculture have led others to increase or to wish to increase their investments on the continent. There is evidence of some quite substantial private foreign-investment in the

agricultural sectors of a number of African countries (Cameroon, the Congo, Côte d'Ivoire, Gabon, Ghana, Mozambique, Tanzania, Zaire, Zambia and Zimbabwe). It should be added that new investments in agriculture have not been confined to large-scale estate investments. For instance, in Kenya a foreign-controlled sugar project entailed the supply of cane by over 25,000 small farmers with holdings of less than two hectares each. Investments by TNCs in agriculture have sometimes tilted the balance between cash crops and food production, and there is a need to undertake such investment in the context of national food strategies.

33. The relatively favourable entry into Europe provided by the Lomé Convention presents opportunities well beyond investment in agriculture. For instance, the 1987 purchase of two Togolese textile factories by a Republic of Korea/North American consortium was due in large measure to the duty free access to EEC markets. Regional export markets also played a part in this and other similar investment decisions.

34. A second area of foreign investment interest is in metals and ores. Several countries have benefited from investment in gold (Angola, Ghana, Guinea and Zimbabwe) and in diamonds (Angola, Botswana, Ghana, Namibia and Zaire). To the extent that supplies from South Africa are disrupted in the years ahead or even if prices of gold and diamonds rise as a result of fears of broader international sanctions against South Africa, independent Africa's reserves of these two minerals in particular will become more attractive.

35. Energy is an active field for foreign investors, and opportunities are likely to continue. Oil and gas exploration has been maintained in the mid-1980s in spite of the decline in international oil prices. Firms from France, the United States, Spain, the Federal Republic of Germany, Belgium, Italy, the United Kingdom and Ireland have been particularly active. In relation to specific countries, mention can be made of the Congo (on-shore oil exploration), the Sudan (on-shore drilling), Nigeria (liquified natural gas), and Ghana (recent drilling), and Irish investment in gas in Senegal and Gabon (on-shore oil).

36. Tourism is an area in the services sector in which opportunities are likely to continue. Sustained expansion in high-class hotels has occurred more because of the rise in non-African tourism than in the rise in conference business or a dramatic upturn in overall economic activity in the continent. The race for dominance between international hotel groups in Africa will increase TNC involvement, particularly on the management side (which does not lead to major new inflows).

37. Beside these general trends, a wide range of particular opportunities has risen in specific countries leading to significant foreign investment. Two country examples are, Nigeria: chemical and petrochemical products; agriculture, particularly with the improvements planned in rural roads and manufacturing for exports, seen as a policy target because of the need to move from dependence on oil, and Mauritius: small consumer goods, and assembly of high technology goods advanced products based on sugar, including perfume and chemical derivatives and fruit products; further integration of the textile industry and expanding tourism exploit existing advantages.

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38. Within manufacturing the major potential is for further import substitution initiatives, which are likely to be of a larger scale than similar projects conceived in the 1960s and 1970s because most now make provision for at least regional exports. African countries are at an advantage relative to the possible recipients of foreign investment in Latin America or Asia, where such opportunities have already been taken and where investors now require the possibility of either larger local markets or exports. Although many African countries offer smaller markets than foreign investors would normally consider, in a few cases (particularly the island economies) the extra transport costs caused by isolation may increase the expected profitability.

39. Finally, mention needs to be made of the changing policies of particular countries that provide unique opportunities for investment. For instance, the objective of the Zimbabwean Government of reducing the influence of South African private capital interests in the country has led to many opportunities for the purchase of South African interests, often in the form of joint ventures with the Government. Further buy-outs of South African interests have still to take place.

D. Assessment

40. Evidence from successful foreign investors suggests that most initially entered a country because of a particular opportunity relevant to their firm. One approach to encouraging capital inflow has been investment fairs or other general introductions of a range of potential investors to a choice of opportunities. In Africa such fairs have been organized, for example, by the United Nations Industrial Development Organization (UNIDO) or even the International Chamber of Commerce. Important are also the efforts to increase mutual understanding and in particular, to promote mutual appreciation of the expectations and concerns both of host governments and of TNCs; in this respect the experience of the investment round table sponsored by the Centre on Transnational Corporations for China was encouraging. The high proportion of total investment accounted for by a small number of investors, the need to offer a significantly superior opportunity and to attract attention to it, and the importance of existing trade and other contacts in attracting investors (when they are asked to list potential areas, they tend to list extensions of existing products or types of production, in the same or nearby countries) - all these factors suggest that the areas mentioned here should be regarded only as examples: what is important is to concentrate on promoting one or a very few.

41. Africa has had a relatively high share of its foreign investment from France and the United Kingdom, and a relatively low share from the United States and Japan (the major investors in other developing countries). 4/ This reflects the poor opportunities perceived by investors: most investment has come from existing investors. Promoting new opportunities is the only way to change this pattern, but the reluctance of investors to look in new areas when there are profitable opportunities in countries with which they are familiar places African countries at a disadvantage.

42. The continuing interest of Japanese investors in natural resources could make the opportunities identified in this area particularly important. In

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manufacturing, they are more likely to see themselves as primarily offering technology or marketing skills, and to want local partners, so that they may be less suitable for this sector in Africa. Sizeable foreign investment by some Asian countries and areas, notably Hong Kong and India, could provide opportunities in import-substituting light industries, but the presence of similar opportunities in Asia, most notably in China, where markets are substantially larger than in any African country could limit their interest in Africa.

43. The small size of potential new foreign investment in Africa measured from either the investors' or the countries' point of view suggests that attention must be focused on particular cases both to make attracting such investment a feasible target and to avoid taking general measures that are not only ineffective but may conflict with other requirements of government policy.

IV. IMPEDIMENTS AND POLICY MEASURES

44. The fundamental conditions for increased foreign investment into Africa are higher economic growth rates, lower levels of debt service, more adequate supplies of foreign exchange and balance-of-payments support, together with greater political stability. Beyond these general considerations there are a range of structural impediments and policy obstacles to expanded foreign investment, of varying importance in different countries.

A. Structural impediments

45. A number of readily identifiable structural features inhibit FDI in Africa. Not only are incomes low and growing slowly, many countries have small populations. With a population of about 7 million, Burkina Faso, Malawi and Mali have a gross national product (GNP) in the $1 billion range, or one tenth of the GNP of Guatemala, for example, a middle-income country with a comparable population. Many countries have still lower levels of pc ulation and GNP. Investment in natural resources is not affected by market size, but the possibilities for domestic processing and other investment opportunities in economies that are so small and fragmented are clearly very limited. Even if the rate of profit is reasonably high, TNCs attach little importance to such operations because of their small contribution to overall corporate earnings.

1. Regional trading opportunities

46. The possibilities of producing for export usually compare unfavourably with those in other developing countries: physical infrastructure is less adequate, and trained and skilled labour is also frequently in short supply. The creation of the Southern African Development Co-ordination Conference (SADCC), the Economic Community of West African States (ECOWAS) and the PTA have stimulated foreign investment, usually on a joint venture basis, to exploit regional opportunities. Countries like Kenya or Zimbabwe, which already have a range of locally produced simple consumer goods, may do relatively well. Problems remain, however,

particularly the shortage of trade finance and export credits without which regional trade is likely to remain at its current low level. There are restrictions on majority foreign-owned firms taking advantage of regional agreements, particularly in the PTA, which are seen by TNCs as a particular obstacle. There is a lack of road and rail links between many African countries, and actions such as the cessation of trade among the countries of the former east African community clearly disrupt confidence in regional markets.

2. Capital markets

47. The low level of domestic savings in Africa, 5/ coupled with a paucity of entrepreneurs, reduces the scope for joint ventures and most non-equity forms of relationship between TNCs and local enterprises. Stock exchanges exist in some countries and have been promoted as a means of diffusing equity ownership, as in Côte d'Ivoire, Nigeria, Mauritius and Kenya. But these have been largely used to raise funds for the Government, with little contribution to private companies. Foreign investors, however, depend on local sources usually only for working capital, and thus inadequacies in the local banking systems are important. In many countries, the low level of development of the financial sector and, with the exception of only a handful of countries, the lack of functioning capital markets inhibit both the generation of domestic saving and the channelling of liquid resources into productive investment. For instance, lack of working capital has been a particularly serious problem in Zambia.

3. Human resources

48. The shortage in many countries of managerial, accounting and a wide range of technical skills leads to inefficiencies and low levels of productivity, which deter foreign investors. Interviews suggest that foreign investors see a large gap between what the Asian and Latin American countries can offer and the average African country, not merely for specific skills, but more generally in relation to basic education and familiarity with equipment.

49. Especially in the more developed economies of Africa, where in absolute terms the inflow of foreign investment is likely to be more significant, it is frequently difficult to redress skill shortages through importation because of restrictions and delays in obtaining work permits for foreign workers. This problem has arisen, for example, in Kenya, Nigeria and Zimbabwe in recent years. However, expatriates cannot usually be relied on in the necessary quantities to meet the shortage of middle-level skills, which even in more advanced countries are frequently seen as a serious constraint.

50. Skill shortages can be overcome by learning-by-doing and on-the-job training programmes. There is little doubt, for instance, that the emphasis placed on technical training and planned maintenance schemes have been a major factor in the advance, diversification and competitiveness of the manufacturing sector in Zimbabwe.

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51. The small size of the labour force in most African countries is an obstacle to attracting investors interested in processing based on mass production (electronics factories employing 1,000 to 2,000 people in a unit). The advantage of low-wage cost either for export or for import substitution is often counteracted by inadequacy of skills or small market size, so the main sector where low-wage cost is likely to be relevant is tourism.

4. Physical infrastructure

52. A reliable power supply, good telecommunications, adequate transportation facilities and efficient water supply and waste disposal are vitally important to modern industrial enterprise, but tend to be in very short supply in African countries. When little or disproportionately low levels of funding is allocated to public-sector investment, particularly infrastructural development, foreign investment is unlikely to be significant. Where structural adjustment conditionality has led to a significant contraction of public-sector investment this has also adversely affected private-sector investment, as occurred in Gabon, especially after the 1985 budget. As some areas of infrastructural investment are customarily barred to private and particularly to foreign investment, there is no obvious way around such an obstacle except through external official assistance. Transport has of course been a traditional project choice for such agencies. Some countries, however, have developed joint ventures, for example a consortium in Zimbabwe to manage the Beira investment includes business interests, parastatal and private.

53. Transport is seen as a major obstacle to FDI even in many countries that are already advanced in obtaining it. In addition to simple lacks of capacity of roads, ports, and international shipping, the costs of dependence on foreign shipping lines, frequently owned by companies with their own production interests, are frequently mentioned.

54. One possibility that should be closely examined in each case is to persuade foreign investors to contribute to infrastructural development directly. This has been encouraged in export-processing zones, for example, in Malaysia as part of policies to make these zones self-financing, and many foreign investors do it on a limited scale, ranging from messenger services to satellite communications links. The greenhouse type of environment of the export processing zone coupled with a concentration of limited infrastructural resources in a well defined area, low labour costs and the administrative facilities that go with the zone's legal status have proven to be a major attraction to foreign investors.

55. Land-locked countries are at a particular disadvantage because they depend on their neighbours' infrastructure as well as their own for imported machinery and inputs, even if they are not seeking export-oriented investment. Another disadvantage is that the costs of lengthy road transport are higher than sea transport, while they are likely still to face the fixed costs of port trans-shipment at some stage. Thirteen of Africa's independent countries are land-locked. In some of these countries, air services may need attention: as they are publicly regulated in all countries, the scope for government

intervention and pressure may be relatively large. In several African countries (notably Zimbabwe, Malawi and other southern African countries) political and military problems raise the costs, directly and through forcing countries to develop new routes quickly. This is a serious obstacle because it adds significantly to the costs of even natural-resource-for-export investment.

56. Although the disadvantages of poor transport and communications structures affect all investors, they are likely to be particularly damaging to foreign investors. By their nature, foreign investors are more dependent on transport and communications infrastructure than an "average" company: they may enter a country as an exporter of a natural resource; they probably import more of their equipment or inputs; they may wish to move from import substitution into exporting; as large companies, they are likely to want to market in all parts of a country.

B. Policy obstacles

57. Apart from questions of location, market size, skills and infrastructure, the overall business environment in host countries appears to weigh heavily in TNCs' decisions to invest, more so in small countries. Among the main elements are political and macro-economic stability, official attitudes towards foreign investment and generally towards private investment, equal treatment *vis-à-vis* local firms, the ease with which profits can be remitted, stability and clarity in the rules concerning foreign investment and fairness and efficiency in administering these rules. It is difficult to judge their relative importance but such considerations almost always outweigh the significance of fiscal incentives. There are frequent conflicts between removing policy obstacles and other national objectives, and a country should always carefully consider the disadvantages as well as the advantages of attracting foreign investment and adapt its policies accordingly. There are quantitative and qualitative dimensions to FDI.

58. Although over the past five years major advances have been made in up-dating, altering or publishing investment codes or guidelines to make foreign investment more attractive, there are still a number of specific policies that potential foreign investors find a major drawback to investing.

1. Lack of formal legislative provision for foreign investment

59. Lack of formal legislative provision for foreign investment applies today only in a minority of African countries. In these cases foreign companies are reluctant to invest in no small measure because of the greater likelihood that the host Government will change the rules for foreign investors. This concern for fixed and certain legislation is one of the most frequent complaints of foreign investors. If legislation is changed, notice could be given and retroactive legislation strictly avoided. Lack of legislation to protect patents or copyrights may be a deterrent to some types of investment, notably in pharmaceuticals and informatics, and to certain types of technology transfer in many other industries. The Central African Republic, Egypt, Kenya and Nigeria are among countries with investment laws that safeguard patents and trademarks.

2. Tax policy

60. Tax policy, in general, appears most important at the time of entry, the point at which comparisons with other countries are made, and before operating conditions become relevant. A more important element may be the taxation policies in other countries, which raises the threshold of what companies expect. As only a few industrial countries offer credit for tax not paid because of concessions under dual taxation agreements (the Federal Republic of Germany and Belgium among the principal foreign investors), such a concession, which may be beneficial to local investors, is less valuable to foreign investors, but still costly to Governments. In some countries foreign investors are exempt from real estate and sales taxes and on salaries paid to expatriate employees in joint venture enterprises. Investment projects that make a substantial contribution to job creation are exempt from taxes on workers' wages in Zaire. However, African countries resort less to credits and investment allowances than Asian and Latin American countries. Differentiated concessions for foreign investors are not generally regarded as favourable because of the potential for ill-feeling, generally or by domestic investors. Countries must consider the possible losses if this means companies pay less in tax than the share of their activities within a country would justify.

3. Foreign exchange controls

61. Such controls, particularly on profit remittances, are a major impediment to FDI. Several countries levy a withholding tax on dividends and profit remittances. Nearly all have exchange controls of some variety, so that it is the nature of such controls (or unexpected changes in them) that can constitute serious deterrents. Such is the case, for example, if controls are set with reference to the local currency value of the initial investment in a country with severe devaluations (as was the case in Kenya) or if they are part of an unusually tight package of restrictions on all outflows.

62. Foreign exchange restrictions on capital may also hinder foreign investors by restricting the source of imports, for example to franc zone countries in the case of Mauritius. Especially in those countries that have quantitative foreign exchange allocation systems, a major impediment to FDI is the frequent lack of guarantee that the foreign investor will obtain access to foreign exchange in order to purchase the intermediate imports required for production.

4. Restriction on certain activities or sectors

63. Restrictions, such as on local borrowing or buying into local companies or owning land, are serious impediments for foreign companies, which are also prevented from remitting abroad all their profit and dividend payments. Countries where the extent and nature of restrictions are uncertain or changeable, as has been suggested for Zambia, may be particularly discouraging for investors.

5. Investment protection agreements

64. It is argued that potential investors are deterred from investing because of the failure of some African countries to sign investor guarantee agreements (Angola, Algeria, Ethiopia, Libyan Arab Jamahiriya and Zimbabwe). For a new recipient, this could be taken as a negative indicator, but the history of extensive foreign investment in Latin American countries that have not signed such agreements and the indifference to them shown in surveys of foreign investors suggest that in the past this was of minor importance.

6. Tariffs

65. Tariffs have been one of the main instruments that developing countries have used to encourage foreign investors to make import-substituting investments, and available evidence suggests that these have been effective. However, caution is needed in using tariffs to attract FDI, because investment in activ ies in which a country does not enjoy a comparative advantage is not socially beneficial.

C. Public administration

66. A common impediment to foreign investors has been and continues to be a range of factors associated with the administration and decision-making arm of the host government. These factors frequently begin in long delays in obtaining the initial permission to invest in the country even when the foreign investment conforms in every way with the respective investment code of guidelines. Thereafter, managers of foreign investment projects (frequently in common with their domestic counterparts) face numerous administrative hurdles that need to be overcome successfully and repeatedly in order to operate their companies.

67. Much delay occurs because of inexperience or inappropriate procedures, where reform will benefit both foreign and domestic investors. It is, however, particularly damaging to foreign investment: foreign investors are more aware of it, because they are familiar with procedures in other countries; and they have the choice of where to invest. One method of alleviation, sometimes used in Asian countries, and commonly advocated by foreign investors, is the establishment of "one-stop" investment offices, where officials familiar with the requirements of all the other ministries dealing with investment could advise and assist foreign investors.

D. Negotiation capacity

68. Paradoxically, lack of confidence on the part of the host country can be an obstacle in dealing with foreign investors. The relations between TNCs and host governments are governed by negotiation, not convention. The initial experiences are often tho most difficult; countries are over-cautious in reducing controls and making decisions, which reinforces the policy and bureaucracy obstacles discussed above. Advisory activities of the Centre, however, show that negotiation capacity

can be quickly built up. Existing arrangements can often serve as a standard for new ones. A wealth of information exists on foreign investment sources and on the variety of ways and means to tap those sources. The use of new forms of investment in the 1970s has helped to establish a range of market charges for different elements of foreign investment. Improvements in accounting standards through the 1970s for firms in industrial countries (notably in the United States) offer additional information. Such information and related advisory assistance are readily available to new FDI recipients through the Centre and other international organizations.

V. INTERNATIONAL ACTION

69. Africa's prospects for FDI are not bright, relative to other developing regions and Africa's own past experience (most notably in the 1960s). Much depends on the external environment, which was adverse in the 1980s but has begun to turn around with international support. National attitudes towards foreign investment in many countries are more forthcoming than at any time since independence. However, the climate for FDI depends also on many factors beyond the control of national policy such as developments in commodity prices, interest rates, growth of world trade and the performance of the world economy. Furthermore, overcoming the structural impediments will require supportive actions at the regional and international levels.

70. In the eyes of TNCs Africa is a region dominated by drought, famine and debt. The reality of African development is less stark; as indicated in previous sections, current opportunities for further profitable private investment are greater than perceptions of potential investors would suggest. Unless perceptions of TNCs change, in consonance with the removal of impediments to FDI, reflecting a more favourable view of FDI by host countries in Africa, there will be no stimulus to significant investments. Considerable promotional effort - an information campaign - is needed to counter the negative view of Africa that is so prevalent. The organization of round-table meetings between government officials and executives of TNCs could be a useful tool in this respect.

71. A more active, international approach towards foreign investment in Africa must start with clearer priorities on the part of Governments based on careful analysis of the merits and demerits of foreign investment. Clearer assessments of national needs - for investment capital, transfer of technology, training, human resources and infrastructural development - would yield more meaningful performance requirements for TNCs and a better gauge against which to decide the inevitable conflicts between removing policy obstacles and other national development objectives. The Centre provides advisory services to Governments seeking assistance in formulating FDI policies and legislation and in streamlining procedures.

72. Within the frameworks of intersectoral priorities determined by national governments, the technical assistance capability of the Centre in several areas could be particularly useful to African countries in securing agreements that are mutually beneficial both to host countries and to TNCs. These concern structuring

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of wholly-owned FDI, joint ventures or non-equity arrangements in mining and petroleum, agriculture and fisheries, and services, particularly tourism.

73. With commitment and clear purpose, Governments should seek out foreign investors in sectors or activities where foreign investment is considered beneficial in a manner parallel to advertising for tenders for construction projects. That such an active approach to foreign investment in Africa produces positive effects is indicated by the privatization experience in a number of African countries. For instance, the textile plant privatization in Togo was concluded in February 1987 only after the Government had considered 11 competitive bids from foreign investors as far afield as India, Western Europe and the United States.

74. Regional co-operation is an effective means for small countries to leverage their collective market shares behind the particular investment opportunities of each country. The role of the Centre in assisting in the formulation of the charter for multinational enterprises in the PTA is the type of assistance that could strengthen similar processes in Africa. Furthermore, the Centre could assist in the establishment of such enterprises involving two or more African countries and in negotiations between those enterprises and foreign investors.

75. There is advantage to dealing with large TNCs that have a long-term planning horizon and are more likely to make reinvestments once established. Such companies usually make decisions on the basis of their own investigations, so that, provided the opportunity offered is real and conditions are in fact sufficiently favourable, media perceptions are relatively less of an obstacle.

76. However, small and medium-sized TNCs may also be suitable partners for many African countries, mainly because such TNCs are often more innovative and flexible and because products and technologies developed by them may be particularly appropriate to African countries. However, searching out potential technologies is a painstaking task requiring access to engineering records, and international organizations (such as UNIDO and the new IFC technology transfer service) could be useful intermediaries between countries and TNCs.

77. Since the 1970s many developed countries have played active roles in supporting their industries' activities in developing countries. Home countries should give consideration to special incentives to their TNCs for investment in Africa. Scandinavian countries, such as Sweden, encourage their small and medium-size firms to internationalize by providing information about possible projects in different host countries, help in mediating contracts and financial support such as loans and guarantees. The resulting FDI have largely flowed to Europe, however. Such programmes of encouragement targeted to Africa could bring non-traditional foreign investors and a new kind of technology transfer. Further thinking about what home countries can do to encourage FDI in Africa is required.

78. By providing African countries greater access to world markets, developed countries can increase the prospects for FDI in manufacturing. The relatively successful experience of the Lomé Convention in inducing FDI in agriculture should be generalized to other sectors and markets and should be complemented by

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facilities for export credits, reduction of commercial risks and soundly managed export processing zones. Consideration might be given to the establishment of an African investment promotion centre, underpinned by developed countries' agreements to provide open access of African exports to their internal markets. International assistance should also be given to strengthen the development of financial institutions that could support production and trade.

79. There is need for innovative mechanisms of support to potential local private entrepreneurs. The Centre has initiated programmes to tap directly the resources of TNCs in developing entrepreneurship and technology-based enterprises in Africa. The programmes aim at creating the overall enabling environment for increased interaction between TNCs and the indigenous private sector, with TNCs entering as equity shareholders, providers of finance, collateral, technology or management skills; the Centre provides only technical assistance to the Government.

80. It was noted earlier that several African Governments have taken initiatives to privatize some of their state enterprises. Here again, the Centre could assist in negotiations with TNCs within the framework of such privatization programmes in so far as Governments consider participation of TNCs worthwhile.

81. Official development flows, by improving fundamental economic conditions in African countries, indirectly promote the prospects for FDI in Africa. For example, the use of public capital inflows, or counterpart funds, to build up physical infrastructure and develop human resources would help alleviate key long-term structural obstacles to FDI. Multilateral assistance for surveys in exploring mineral resources, fisheries and tourism potential is important, as is international co-operation in energy exploration and development.

82. In many countries, restrictions on profit remittances are necessitated by wide fluctuations in foreign exchange earnings. Therefore, balance-of-payments support by multilateral financial institutions can help underwrite government guarantees on profit remittances and thereby relieve a major policy constraint to larger FDI inflows. International actions to resolve Africa's debt problem would have a very substantial beneficial effect. In this context, it may be mentioned that the Centre could provide advisory services to African Governments in exploring the possibilities of debt-equity swaps and in the analysis of costs and benefits of such swaps.

83. The Centre intends to explore these and other possibilities at greater depth with a view to encouraging mutually beneficial foreign investment in Africa and other least developed countries. In the mean time, the Centre stands ready to respond to any request concerning elaboration or implementation of some of the ideas mentioned above, if so desired by African Governments.

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Notes

1/ Africa is dependent on commodity exports, and investment in the primary sector has helped build up this export capacity; however, the earnings of foreign export-oriented enterprises should be assessed in relation to financial outflows (explicit and invisible payments to foreign factors of production) and in some instances such outflows have been relatively large.

2/ FDI comprises only 2 per cent of net resource flows to sub-Saharan Africa. See Financing Africa's Recovery, Report and Recommendations of the Advisory Group on Financial Flows for Africa, United Nations, February 1988.

3/ Over the past few years these enterprises have included the following: Cameroon - banana plantation; Congo - cement; Côte d'Ivoire - agro-industry, trade, public works, tourism; Ghana - palm oil; Guinea - soft drinks; Liberia - petroleum refining; Nigeria - chemicals; Rwanda - matches; Sudan - agriculture, manufacturing (announced June 1988); and Togo - steel, textiles, oil, agricultural implements, plastics, marble.

4/ In 1985 and 1986, Japanese official statistics record no new investments in Africa.

5/ The savings ratio in all developing economies in 1986 was 24 per cent, but out of 35 African countries whose data were individually recorded, only 11 had ratios greater than 15 per cent; for 10 countries the ratio was lower than 5 per cent (see World Bank, World Development Report 1988, Washington, D.C., 1988).
