FOREIGN DIRECT INVESTMENT TO SUB-SAHARAN AFRICA: THE MAKING AND UNMAKING OF ECONOMIES IN SUB-SAHARAN AFRICA

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ABSTRACT
Foreign direct investments (FDI) play a crucial role in Sub-Saharan African (SSA) countries' development efforts in present integrated world economies. Yet most SSA countries have not been successful in attracting FDI. With the millennium development goals giving the impression of being increasingly difficult to attain, FDI to SSA countries have increased substantially to supplement domestic funds. Exploratory studies conducted by using the existing materials on FDI revealed that the flows to SSA countries is the lowest and unequally distributed both among the countries and within the various sector of the individual countries. The few countries that were able to attract was primarily due to abundant natural resource size of the market. SSA countries will continue to receive FDI from little to large sums and into diverse areas of their economies due varying interest of potential investors. The importance and distortion generated by FDI in the recipient countries are not automatic and varies from one country to another. Yet with proper management and policy planning, the full potential impact of FDI for accelerated development and growth in the recipient could be realised.

INTRODUCTION

Foreign direct investments (FDI) have long been and still continue to play a crucial role in SSA countries' development efforts in the present closer world. It has had pervasive effect on Africa economies during the 1990s. FDI is an investment made to acquire lasting interesting enterprises operating outside of the economy of the investor, with some degree of equity ownership and effective voice in the management of an enterprise (IMF, 1996). That is, it is a corporate governance mechanism. The transfer of control may not for all time benefit the recipient country because of adverse situation under which it occurs. There are the problems of adverse selection and excessive leverage (Loungani and Razin, 2001). Most foreign direct investments have taken the form of acquisition of existing assets rather than investment in new assets (Mwilima, 2003). It is viewed as a major inducement for economic growth and also serves as away of dealing with the financial shortages resources as well as providing for the shortfalls in technology and skills (Marr, 1998 and Mwilima, 2003). It is on record that in the 1980s and 1990s a large proportion of the financial resources needed for development works in SSA were generated from outside due to the various countries inability to organise resources from within their economies.

According to Bennell, 1998 without investment by private and foreign companies there is a real danger that, Africa and for that matter SSA countries will fail to become internationally competitive and will remain at the margin of the world economy. Though there is not much statistics to substantiate this claim, there is every reason to indicate that SSA countries lack the domestic resources for investment and to finance long term development with poverty reduction and other Millennium Development goals looking increasing difficult to achieve by 2015, hence attracting FDI is the important source of external finance (UN, 2005). This is not the only reason as other basis such as corruption, non proactive nature, mismanagement and non resourcefulness of governments and policy makers of SSA countries are major impediments to development efforts. The negative and positive effects of FDI in SSA countries are intertwined. Yet still the crucial role they play in making and unmaking African economies is remarkable, hence the title FDI to SSA countries: the making and unmaking of economies in SSA countries.

TREND AND DISTRIBUTION OF FDI FLOWS TO SSA COUNTRIES

A growing number of countries have received significant capital flow in the form of FDI in the wake of world's liberalisation and globalisation (Bhinda et al, 1999, Kyaw, 2003). This current increase of international investment in Africa has taken place against the backdrop of a worldwide explosion of FDI since the early 1990s (Lai, 2001). In terms of the percentage, Africa receives the least as compared to other regions. The vast proportion of FDI flows go to developed countries which also house the main sources of FDI i.e. the TNCs (about 95% of the total inflows). It is on record that, in 1998, 92% of total FDI outflows came from the developed countries. And 72% of the total inflows returned to these countries (UNCTAD, 1999). Out of the flows that went to low –middle income countries, Asia and Latin America had 42% and 38% respectively, flowed by Central Europe & East Asia with only 6% going to Africa (World Bank, 1999). The volume of annual FDI flow to Africa was doubled during the 1980 to US$2.2 billion compared to the

1970 figure. This has increased to US$13.8 billion in the 2000-20003 financial periods (UN, 2005). These figures mask some important details as in actual fact there has a decline in the percentage received over the years to Africa in general and SSA in particular. There has been a significant increase in the volume of FDI flows world wide. According to UN 2005, Economic development report for Africa, the percentage of FDI flows have actually declined from 6% in the 1980s to 2% in 2001. Yet its important to the development of the region can not be under estimated.

Even though FDI forms a major component of financial and other resources for SSA countries' development efforts, there is growing evidence that benefits are not equally distributed (ODI, 2002). Yet FDI has the potential to make significant positive impacts in the recipient economies, but much depends on sound domestic policies and level of investment management. FDI attraction to SSA is not a new path of development thinking as it has been part of the development framework for most SSA countries since independence to attract FDI for a late industrialisation drive (Mkandawire, 2001). The pace and direction of capital flow to SSA have changed and fluctuated though slowly over the years. It started slowly and showed signs of substantial increase in the 1990s in many developing countries (IMF, 2001). Developing countries received two-thirds of the increase in FDI worldwide between the late 1980s and 1990s, a sharp change from the previous decade, when flows to industrialised countries dominated (World Bank, 2001). Kyaw's work, 2003 the composition of capital flow to developing countries has shifted from bank loans towards FDI and portfolio investment. The work stresses the fact that, in the 1970s and early 1980s, the bank loans were the primary sources and form of private capital flow to developing countries and in particular SSA.

On the contrary, in the 1990s, the capital flows to developing countries have been dominated by bonds and non-debt creating flows in the form of FDI and portfolio investment. The Table 1 below gives a clearer picture of the shift from loans to FDI and portfolio. From the table the percentage of Loans as the main source of finance to developing countries since the 1975-1979 periods has been on the decline. The proportion of loans was 63% in mid 1970s but reduced to 15% in 1995-1999. Within that same period, FDI has been on the ascendancy starting with 18% in the period 1975 – 1979 to 55% in 1995-1999. Portfolios have gain grounds over the years' 1975-1979 with 5% to 29% in the 1995-1999 as shown in the Table 1 below. This is partly the reason why some developing countries especially those of SSA incurred so much debt in the 1970s and 1980 and consequently spent so much in servicing debts. Between 1970 and 2002 Africa received US$540 billion in loan, and paid back US$550 billion. But it still owed US$295 billion because of penalties, interest and arrears. In particular, Nigeria only borrowed US$13.5 billion from the Paris Club creditors between 1965 and 2003; it has paid back about US$42 billion because of penalties and interest accrued. Amazingly, by 2003, Nigeria still had US$25 billion left to pay (Christian Aid, 2005). It is recently that some countries have received debt cancellations. Even with that there is a high possibility that these countries might have finished servicing the loans through the high interest rates charged over the repayment period. Most of the countries with which the debt cancellation could have made significant impact did not meet the criteria for it. Hence FDI is the best way to help

SSA countries to progress to an appreciable level of development. Notably if it involves establishment of permanent structures and skill transfer, it cannot easily removed or taken back from the recipient countries.

TABLE 1: **Composition of Private long term capital flows, 1975-1999**

Percentage of Private long –term flows

	75-79	80-84	85-89	90-94	95-99
FDI	18	19	49	48	55
Loans	63	62	17	7	15
Portfolio	5	4	11	38	29
Other	14	15	23	7	1

Sources: World Bank Global Development finance, 2001

Moreover the public sector was the most important recipient of the flows in the previous period in the 1990s whereas the private agents have taken a greater proportion of the external borrowing currently. In spite of the significant growth in the FDI flows to SSA countries in particular and developing countries in generally, it remains highly concentrated in a few countries. Seventy percent of FDI to developing countries world wide go to the top ten recipients. This includes China, Brazil, Mexico, Argentina, Poland, Chile, Malaysia, Korea, Thailand, and Venezuela (Kyaw, 2003). This never fell below the sixty-four percentage mark through out the 1990s. The bulk of this capital flows have been directed towards Asia and Latin America. Only a few countries in SSA have been successful in attracting FDI (Bennell, 1998). Within the few countries that made the mark in SSA, Nigeria and Angola have received the lion share of the FDI flows to SSA though their political and economic environments are unstable (Morisset 2000). It was in the 1990s that new major destinations like Ghana came into the picture (ODI 1998). This obvious reason for these countries to receive a sizeable FDI was the presence of oil and gold in these countries.

International capital flow largely go around SSA, but these facts mask significant details and differences among countries. The share of long term capital flow in the form of FDI to SSA is lower as a percentage of GNP than that of all other developing regions except South Asia (Kyaw, 2003). SSA countries saw the sharpest decline in private capital flows in the aftermath of the debt crisis in the early 1980s. This made the proponents of structural adjustment saw that increased FDI will be a key factor in sustained economic recovery (UN, 2005). Private capital flows began to recover in the SSA in the second half of the 1980s. It still fluctuated and picked up modestly during 1993/95. Within the SSA, the CFA countries experienced larger and more sustained declines in FDI flows than did non-CFA countries.

The major recipient of FDI flow Africa in general can be placed in three broad groups

- Long term recipient countries comprise Botswana, Mauritius, Seychelles, Swaziland and Zambia.

- Countries that documented a large increase in the FDI flow in the 1990s included Angola, Cameroon, Gabon, Ghana, Guinea, Lesotho, Madagascar, Mozambique, Namibia, Nigeria and Zimbabwe.
- Countries that suffered low and declining in much of the 1980s and 1990s. It only began to turn around few years ago (World Bank, 2001 and Kyaw, 2003).

Large proportions of FDI were directed to the oil and mining sectors. This probably explains to some extent why Nigeria and Ghana were major recipients. In spite of the very modest amount received in SSA, the rates of return on FDI have generally been much higher than other developing regions. During 1990/94 the rate of return on FDI in the SSA region averaged 24-30% compared 16-18% for all developing regions. This points out that the risk perceived to be higher in SSA than in other regions (Bhattacharia et al, 1997).

POTENTIAL CONTRIBUTION AND DISTORTION OF FDI FLOWS TO SSA

The important of FDI in Africa's development cannot be over-emphasised. It is often assumed that greater FDI flows is accompanied by many benefits in the recipient countries, but FDI is only a source of capital and its impact is dependent of the form it takes as well as the state of economy destined country. Some of the perceived advantages and disadvantages are as discussed below.

FDI contribute to Gross Domestic Product (GPD), total investment in the recipient countries as well as balance of payment. Studies have shown that there is a positive correlation between GDP and FDI in flows, though not true for all case (OECD 1999). A decade ago, in central Europe, when FDI in flows increased the GDP for that period dropped. It is a major stimulus to economic growth according to the 'gap ' theories but the level of FDI do not necessarily give any indication of domestic gains (UNCTAD, 1999). Recipient countries of FDI most often lose through corporate strategies. According to Gardiner 2002, protective tariffs and transfer pricing can reduce the level of corporate tax received by the host governments. Then again certain aspects of FDI limit the economic gain to the host economy. For instance management fee, royalties, profit repatriation, capital flight among the lots clear take a great proportion that the host should have. There the gains from FDI are not automatic; rather the full impact realisation will depend on the state of the host economy.

The effects of FDI on domestic investment are not always favourable and vary from country to country. Both crowding in and crowding out occurs at different countries and different regions. 'Crowding in' happens where FDI companies can stimulate growth in upwards/ downwards stream domestic business within the national economy. Whilst 'crowding out' is where the mother companies control the local markets, stifling local competition and entrepreneurship (Gardiner 2002). Crowding out is as result government regulation which are kept artificially very low to attract foreign investors, who are pretty much aware of the fact lower standards can reduce short term operational cost for business in the country. Studies conducted Ayosin and Mayer 2000, indicated that FDI has an almost balance effects on domestic investment as it stimulates new investment that would have taken place in their absence. In general positive impacts of FDI are not assured. This under pin policy towards FDI in most developing countries that FDI is always good for a countries development and that liberal policy towards MNEs is sufficient to ensure positive effects failed to be held the data (Ayosin & Mayer 2000).

More often than not parent companies support foreign subsidiaries with human resource and infrastructure especially with 'Greenfield' investment. These can stimulate new infrastructural and technological development which can also result in social and environmental benefits. These are usually spill over effects (Gardiner 2002). The mother companies also help with innovation in production and processing techniques through research and development. The above mention benefits are not always the case. There at times the technology may not be appropriate as well as capital intensive will limit the number of employees within the organisation's locality. It also has negative effects on local competitor especially smaller businesses.

Further more there FDI also help to generate employment, raise wages and revitalise the declining market sector. But a handful of people benefit as the educated and wealthy urban dwellers. These lead to wage differentials and subsequently increase the gap between poor and the rich. There is also problem of local consumers developing culture of consumerism with its associated negative environmental. These occur as a result of diverting FDI from subsistence and food production to more sophisticated products. There is also a danger of pushing out small scale and rural businesses due to the inability to attract FDI and loans from banks to keep up the competition effects (Gardiner 2002).

DETERMINANTS OF FDI FLOW TO SSA

Despite the handicaps that present itself in SSA countries quest to attract FDI, efforts are being made to be a focus for more FDI for development especially short term to boost up the SSA economies. Experience has made known that foreign investors choose countries with stable political and economic environments (Bhattacharya et al. 1997). Open market, minimal regulation, good infrastructure facilities and low production cost are the key factors in attracting and retaining FDI. If not all, some combination of these factors has made extremely difficult for many SSA countries to entice foreign investors. The factors mentioned above have different weights in terms of impact as the existence of some of them are nullified by the presence of another. For instance, in 1990s, Angola was a major recipient of FDI in Africa though the civil war of country was at its peak. These coupled with general poor investment climate, little or no infrastructural base acted to the disadvantage of most SSA countries. Pictures from the countries that have had a significant level of FDI inflows indicate that they were not free from impediments. So do FDI into Africa consider any factor at all? FDI in the immediate past were channelled to countries with mining and oil centres such as Nigeria and Angola. Even within these countries the negative environmental impact is very crucial and far more expensive than those aggregate benefits. Minimum or no particular attention is paid to the consequence of their action. In some cases the source of the FDI is a powerful TNC that the leaders of the host countries can not do much to offset the negative impacts. In the light of the weaknesses, economic gaps and distortions FDI could still play a constructive role in SSA countries' development (UN, 2005).

THE FUTURE OF FDI IN SSA

The future of FDI in Africa still looks great as foreign investor are beginning to diverse their money into other sectors due to the popular privatisation polices that is becoming increasingly vital throughout SSA. But still key factors, to catch the attention of foreign investors, will be economic stability and good governance. These will improve the business climate backed by economic growth and aggressive trade liberation so as to serve as incentive for investors (Morisset J. 2000). Above all the countries of SSA should adopt the open door policy to entice investor into various sectors of the economy and mounting an image building efforts with the participation of high powered delegation including the president (Morisset J. 2000). SSA countries can be successful in attracting FDI that is not as a result of natural resource and wide local markets rather aim at regional and global market. In spite of these, for some countries the future of FDI inflows seems bleak partly due to ill-prepared nature of their governments to implement policy reforms. For years to come, FDI will continue to be a force in African's development efforts hence the need for host countries and investors to bridge the gap between the positive and negative impacts of their actions and inactions.

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