Foreign Direct Investment (FDI)

* Offers one source of foreign exchange inflows
* In any resource constrained country, FDI can contribute towards:
  + Promoting technology and institutional innovation
  + Building human capital
  + Creating jobs and increasing household incomes
  + Promoting overall development
* Many emerging countries have benefited from increased flow of FDI (India, China, Brazil, South Africa)
  + Latin American countries had particularly benefited from FDI in promoting agricultural commercialization
* Developing countries are receiving an increasing share of FDI

FDI is generally a positive thing:

* FDI Helps the country by increasing the country’s capital stocks, helping with the balance of payments.
* FDI can create employment.
* FDI can introduce new technology which is then adopted by locals.

Trends in FDI to sub-Saharan Africa

FDI hasn’t changed much over time in SSA. In Absolute terms, the volumes of FDI are up, but the share of FDI going to SSA is quite small.

|  |  |  |
| --- | --- | --- |
| Decades | FDI to SSA | SSA Share in Word FDI |
| 1970s | US$907 Million | 5 Percent |
| 1980s | US$ 1.3 Billion | 2 Percent |
| 1990s | US$ 4.3 Billion | 3 Percent |
| Early 2000 | US$10 Billion | 4 percent |

* FDI to Africa has increased in absolute terms, but has declined relative to growth in overall flow of FDI to developing countries.
* Understanding this puzzling trend is subject of large body of research

What will attract FDI to Africa?

* The simplest answer to the question is “ possibility of profitability”
* What determines the FDI profitability? Consider the following:
  + Economic openness
  + Size of the economy
  + Political stability
  + Infrastructural development
  + Institutional capacity
  + Regulatory environment

One way to analyze why FDI vary by country is to compare a common indictor. World Bank produces such an indicator, called “the ease of doing business”. It ranks countries based on the following indicators

* + Starting a Business
  + Dealing with Construction Permits
  + Registering a property
  + Getting credit
  + Protecting Investors
  + Paying taxes
  + Trading across borders
  + Enforcing contracts
  + Closing business
* It seems that something isn’t being captured in the World Bank’s ease of doing business scale. AAMP countries are performing just as well as BRIC countries according to this scale, yet the economies of the BRIC countries are far outstripping those of SSA.

Sub-Saharan Africa has lagged behind other developing countries in terms of FDI. In the Zambia v. Brazil example, it’s remarkable to note that from 1970 to the early 1990’s the two countries received very little FDI. Then, after 1994, Brazil began to attract huge sums compared to Zambia.

What is Brazil doing that Zambia is not doing? How can SSA attract more FDI?

Supply -

Where does the supply of foreign currency come from? Most foreign currency comes from exports. When coffee is sold from the highlands of Tanzania, US Dollars come into the country. Export of services is another prominent source of foreign currency. When tourists visit Mt. Kilimanjaro or take a Safari, they leave Euros, Yen, and US Dollars behind. Another avenue is through FDI. As we explored earlier, SSA has a relatively small share of the world’s FDI, Finally, remittances are a source of foreign exchange. Workers from abroad send money back to their families in the form of Forex.

Demand –

Who demands foreign currency? Imports are purchased in foreign currency, and many households hold forex as a form of savings. Because US Dollars and other forex are relatively stable, they lose less value over time in the form of deflation.

The basic assumption is that enhancing confidence,

good governance

the management of public goods

political alternation,

regional integration in Sub-Saharan Africa would becomes an instrument conducive to increased private

investment. This assumption is premised on the theory

that regional integration creates a larger-economic space

with enlarged markets, promotes the harmonization of

economic and social policies, legalization and institutionnalization cooperative frameworks, and frees the mobility

of goods, capital and labor, among others