Cross-Border Investment (CBI) refers to all capital flows, both private and public, between countries i.e. investment across the geographical borders of countries. Intra-regional CBI is therefore related to capital flows listed within a Regional Economic Community (REC).

CBI is an important indicator used to gauge the level, nature, content and depth of the economic and social integration of a Regional Economic Community (REC). In addition, as a source of Foreign Direct Investment (FDI), it is expected to have positive impacts on the national economies, which include job creation, appropriate technology transfers, introduction of suitable business processes, regional managerial skills, know-how and contribution and integration in international production networks.

However, in contrast to the Asian region where FDI from the investors in the same region account for 30% of total inwards FDI, in Africa FDI provision comes essentially from abroad and remains highly concentrated in the oil and mining sectors. Among the constraints, there exist business and institutional barriers as well as underdeveloped financial markets and prevalence of a quantitative paradigm opposed to a qualitative approach in attracting foreign investment.

This brief argues that in spite of these constraints, recent years have seen an increasing interest for intra-regional CBI across the continent as a key driver for both fostering economic growth, and deepening economic integration. The Southern Africa Development Community (SADC) in particular presents several advantages and enablers — including the various programs that have been launched in line with the SADC Finance and Investment Protocol — that can act in favour of CBI within the region. In addition, by promoting intra-regional CBI, SADC member states expect not only to form closer ties with each other and to link trade with investment projects, but also to diversify the sources of foreign investment.

This brief is divided into six sections. Following the introduction, section two provides information on FDI and intra-regional investment flows in Africa and the SADC region. Section three describes the barriers and the enablers to CBI within the SADC region. The lessons from Asian countries in boosting intra-regional investment that could serve as example for African countries are provided in section four. Section five summarizes the main recommendations to boost intra-regional investment within the SADC, while section six outlines a conclusion.

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II. Overall performance of Africa and SADC in foreign direct investment (FDI) and cross-border investment (CBI)

1. Overview of Africa’s FDI Performance

While FDI flows to developed countries and transition economies continued to contract in 2010, inflows to developing economies recovered strongly and even absorbed, for the first time, more than half of global FDI inflows. Meanwhile, FDI inflows to Africa fell for the second consecutive year after peaking in 2008. Apart from Central Africa and East Africa Regional Economic Communities (RECs), all other African RECs witnessed a contraction, albeit to different extents.

FDI to Africa remains concentrated on minerals, oil and raw materials. However, despite being resource-rich countries, inward inflows to several traditional recipients of FDI in the continent seemed to have accelerated or slowed down. Indeed, new FDI recipients such as Congo, the Democratic Republic of Congo, Ghana and Zambia have emerged. Another change in cross-border investment landscape in Africa is the increasing progression of Foreign Portfolio Investment (FPI). Traditionally, the volume of FDI in Africa has constantly exceeded inward FPI. However, it should be noted that after the financial crises in 2008, FPI tended upwards as international investors became more risk-averse and biased towards short-term investments.

Looking ahead, FDI inflows would certainly recover, given the growing appetite of Chinese and Indian Transnational Corporations to secure supply sources of raw materials, but how long it will take is uncertain. Another key issue that deserves attention is the capacity of African countries to strengthen intra-regional cross-border investment—which can in turn benefit intra-regional trade and more broadly regional economic cooperation.

As shown in Table 1, intra-regional cross-border investment in Africa remains limited. Out of total project value for the African Continent of USD 84 billion over the cumulative period 2003-2010, intra-regional projects accounted for 5% of value at USD 4.6 billion. Within the USD 4.6 billion, FDI project value intra-SubSaharan Africa (SSA) amounted to USD 35 billion, highlighting the dominant regional role of South Africa as a major source of FDI. The figure is similar in terms of the number of intra-regional FDI projects: out of 4,702 total FDI projects in Africa (for the cumulative period 2003-2010), only 570 (12%) are intra-regional FDI projects. 10% of those 570 intra-regional FDI projects are from Sub Saharan Africa to Sub-Saharan Africa, 1% from North Africa to SSA and 1% from North Africa to North Africa. These figures contrast with performances in other regions. For instance, by 2008, intra-regional FDI in the Association of Southeast Asian Nations (ASEAN) countries was estimated at 30% of the total FDI inflows.

The vitality of FDI and FPI flows into SubSaharan Africa (SSA) is a reflection of the region’s improved overall economic performance and growing attractiveness during the past decade. After a long period of stagnation, Sub-Saharan Africa now posts solid growth rates: it is expected to have grown at 4.9% in 2011, just short of the pre-crisis average of 5% over the 2003-2008 period. SSA was largely unscathed from the global crises and paradoxically stands as one of the fastest growing regions in the world.

2. Intra-regional CBI in the SADC

Intra-SADC investment represents a small share of the overall SADC FDI inflows. However, this is likely to change as opportunities for cross-border investment expand and regional integration deepens and remaining barriers to trade are removed. The expansion in cross-border investment will also require a deepening of policy and strategies and incentives for attracting cross-border investment that are transformative, develops regional value chains, and create jobs, such as manufacturing.

There are few statistics on intra-regional cross-border investment in Africa as well as in the SADC. For this reason, a study on “Intra-SADC Cross-Border Investment” was conducted, targeting the following five countries: Botswana, Mozambique, Mauritius, South Africa and Zambia. Based on available and comparable data, the Tables 2 to 4 give a snapshot of inward and outward investments by some of the major players of the region. While Botswana, Mozambique and Zambia appear as “net recipients”, South Africa is more likely the net provider of

| Source: UNCTAD, WIR, 2011 |

Table 1: Value and number of intra-regional FDI projects in Africa (cumulative 2003-2010)

<table>
<thead>
<tr>
<th>Total and intra-regional FDI</th>
<th>USD billion</th>
<th>%</th>
<th>Number</th>
<th>Projects</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total FDI projects in Africa</td>
<td>USD 846</td>
<td>100</td>
<td>100</td>
<td>4,702</td>
</tr>
<tr>
<td>All intra-regional FDI projects</td>
<td>USD 46</td>
<td>5</td>
<td>970</td>
<td>12</td>
</tr>
<tr>
<td>North Africa to North Africa</td>
<td>USD 8</td>
<td>1</td>
<td>66</td>
<td>1</td>
</tr>
<tr>
<td>SSA to SSA</td>
<td>USD 35</td>
<td>4</td>
<td>461</td>
<td>10</td>
</tr>
<tr>
<td>North Africa to SSA</td>
<td>USD 2</td>
<td>0.2</td>
<td>43</td>
<td>1</td>
</tr>
<tr>
<td>SSA to North Africa</td>
<td>USD 0.2</td>
<td>0</td>
<td>1</td>
<td>0</td>
</tr>
</tbody>
</table>
FDI and FPI in the region and even for the continent. South Africa has the lion’s share of investment in the SADC region, both for FDI and FPI. Since 1994, the pivotal year in which South Africa held its first democratic elections, its companies have engaged in a sustained outward FDI thrust with substantial impact on the SADC countries and in the whole African region. At the end of the year 2010, FDI and FPI to Botswana, Mauritius, Mozambique and Zambia stood at US$ 980 million and USD 467 respectively. At the same time, the country is also the main FDI destination in the region accounting for 85% during the 2007-2009 period. Unlike in most of the other African countries, a significant volume of foreign investment in South Africa goes to the manufacturing sector. The country has successfully applied investment incentives to develop an export-manufactured industry, especially in the automotive sector.

The importance of South Africa’s investments into Mauritius—namely through equity participation—is a clear indication of the dynamism of intra-regional investment from that country. Such investments can be attributed to the presence of South African companies in various sectors of the Mauritian economy, namely financial services, food and retail, among others. However, if South Africa is a main provider of FDI/FPI, the country and the concerned companies also benefit from it. Indeed, the benefits perceived by South African companies are multifold as the main source of intra-regional investments. South African firms earn net economic rents from the use of their exclusive assets, i.e. superior technology, administrative and entrepreneurial skills. For South African firms, the host countries could mean better markets with prospects for growth and profitability for the investing country. It has been argued that regional investing in banking by South Africa offers “a return on equity of above 30% compared to 20% – 23%in South Africa”. In telecommunications, better markets than South Africa exist which are of benefit to the investors. The South African investors also benefit in that they would have new markets once their own home country markets get saturated or if they lose market shares at home.

But Mauritius is also recognized by its role as a new source of Intra-African FDI and FPI. Indeed, the country is emerging as an important investor in Madagascar, Seychelles, South Africa, Ivory Coast, Tanzania, Kenya, Uganda, Mozambique and Reunion. According to OCED figures, outward FDI from Mauritius to four African countries (Madagascar, Mozambique, Seychelles and South Africa) stood at USD 46.1 million in 2011. Similarly, Mauritian FPIs for those four countries reached USD 1.5 billion in 2010, with South Africa being the main host of these investments. Mauritian investment in Madagascar reflects the appetite of Mauritius companies for intra-regional investment. Indeed, Mauritian FDI stock in Madagascar amounted to USD 94 million in 2009, and the figure experienced an increase of 108%. The prominent sectors being targeted by Mauritian investments in Madagascar, based on FDI stock, relate mainly to distribution of petroleum products (41%), financial services (24%) and telecommunications (21%).

The rational for Mauritian investment in Africa can be understood in the context of frantic pace of globalization, marked by rampant competition among developing countries, especially from the Asian continent. Thus, Mauritian companies are usually directly tied to the presence of natural resources or their processing, and to an attempt to reduce cost of production.

### Table 2: Inward-Outward Equity Investment (2010, US$ Millions)

<table>
<thead>
<tr>
<th>To / From</th>
<th>SA</th>
<th>MAU</th>
<th>MOZ</th>
<th>ZA</th>
<th>BOT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Botswana (BOT)</td>
<td>-</td>
<td>176</td>
<td>12</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Mozambique (Moz)</td>
<td>-</td>
<td>155</td>
<td>179</td>
<td>-</td>
<td>28</td>
</tr>
<tr>
<td>South Africa (SA)</td>
<td>-</td>
<td>-</td>
<td>143</td>
<td>-</td>
<td>15</td>
</tr>
<tr>
<td>SADC to North Africa</td>
<td>0.2</td>
<td>0</td>
<td>1</td>
<td>-</td>
<td>0</td>
</tr>
</tbody>
</table>

### Table 3: Inward-Outward Debt Investment (2010, US$ Millions)

<table>
<thead>
<tr>
<th>To / From</th>
<th>Botswana</th>
<th>Mozambique</th>
<th>South Africa</th>
</tr>
</thead>
<tbody>
<tr>
<td>Botswana</td>
<td>149</td>
<td>10</td>
<td>-</td>
</tr>
<tr>
<td>Mozambique</td>
<td>-</td>
<td>39</td>
<td>0</td>
</tr>
<tr>
<td>South Africa</td>
<td>-</td>
<td>198</td>
<td>61</td>
</tr>
</tbody>
</table>

### Table 4: South Africa Outward Investment within SADC Region (2010, US$ Million)

<table>
<thead>
<tr>
<th>Country</th>
<th>BOI</th>
<th>MAU</th>
<th>MOZ</th>
<th>ZA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity</td>
<td>339</td>
<td>7,036</td>
<td>1,036</td>
<td>178</td>
</tr>
<tr>
<td>Debt</td>
<td>94</td>
<td>1,015</td>
<td>122</td>
<td>33</td>
</tr>
<tr>
<td>Total</td>
<td>433</td>
<td>8,051</td>
<td>1,158</td>
<td>211</td>
</tr>
</tbody>
</table>

It is certainly true that FDI in the SADC region has had a positive effect on several countries in terms of economic growth, infrastructure investment, and emergence of a middle class. However, FDI impact in diversifying and transforming the economy, creating conditions conducive for long-term growth and job creation has been limited compared to other regions in the world, namely Asia. In particular, the industrial sector despite significant flows of FDI within the SADC region remained undeveloped, with the exception of South Africa. Indeed, a cursory look at economic data in most SADC countries excluding South Africa shows that FDI has led to a rapid expansion in the distributive and construction sectors, while there has been marginal impact on key sectors, such as manufacturing, likely to sustain growth over time. The policy of trading resources for infrastructure investment has also led to mega-infrastructure projects, which may be ill-timed. Many road projects, including transport corridors have poor impact on economic transformation and job creation as the linkages between the infrastructure project and economic activities alongside those corridors is not ensured. Over time, such mega-projects could be a drag on the economy as resources have to be deviated to their maintenance.

Two countries’ experiences are highlighted for advocating a more qualitative approach to FDI policy, i.e. Botswana and Mauritius. These two countries have often been showcased as role models by international organizations. They rank high in the ease of doing business of the World Bank, they
have political and macroeconomic stability and liberal FDI policies. Yet in the case of Botswana, despite several years of rapid growth, visible signs of economic development and significant achievement in the Millennium Development Goals, "the share of non-diamond sectors in total GDP has been roughly constant (about 38 per cent)." The policy challenge that has emerged is how to sustain the growth path as "diamond production slows and reserves are depleted." In Mauritius, after a remarkable performance induced by FDI inflows in the manufacturing sector in the 1980s, FDI performance for the period between 2006 and 2011 has been less successful. With respect to this, Governor FundhlaRikhen said that the Government policy to open up the property sector to non-residents in 2007 was "an unbalanced investment programme heavily skewed towards a sector with a very limited capacity to sustain growth." In these circumstances, FDI in the property and real estate sector can be a rather interesting and viable alternative. However, policy-makers and regulators have to perform a fine balancing act between, on the one hand, the imperatives of economic and financial sector growth and, on the other, concerns about a potentially disruptive speculative property bubble which could defeat the very purpose the policy was meant to fulfill.

It is abundantly clear that the quality of FDI does matter. FDI should be strongly linked to local enterprise development and not confined to small ancillaries as the benefits of FDI do not accrue automatically and are not uniform across sectors and countries. Experience shows that the authorities need to go beyond traditional liberal FDI policies. In particular, they need to pay more attention to the broad set of regulatory and institutional frameworks conducive to an enabling environment both for foreign investment and for domestic entrepreneurship.

These concerns provide the justification for a more qualitative approach to FDI in Africa. The main issue, however, is how to do it - what kind of FDI policy should resource-rich countries adopt to ensure sustainable economic development over several decades that would make a difference to the poverty in Africa? Intra-regional investment is one of the solutions that can contribute to promoting economic cooperation within a region as well as enhancing sector specialization and complementarity.

III. Barriers and enablers to cross-border investment (CBI) in SADC

1. Barriers

- Not all Impediments are Business Climate Driven
Some of the barriers hindering and constraining additional SADC regional investment seem to be unrelated to the macro impediments usually referred to in the "lack of doing business" and business climate improvement methodology and are more related to micro issues such as corporate governance, lack of transparency in investment projects, lack of skills in investment project studies and finally lack of managerial skills to handle investment projects from concept to financing. So in trying to establish the serious impediments to regional cross-border investments, one should clearly distinguish the factors requiring the upgrading of skills and support of the private sector from the one requiring business climate improvements. The former impediments require a different type of approach in terms of capacity building and skills development.

- "Business Climate" Barriers to Intra-SADC Investment
(Broadly, barriers which can be referred to as impediments to SADC regional investments within the category of "business climate barriers" are as follows:

  - Unclear and arbitrary administrative requirements: The issues mentioned pertain to company registration, and to the approval of foreign workers. The recruitment of skilled and qualified local workers appears to be a significant obstacle to intra-SADC investment. There are lots of difficulties and some quite arbitrary decisions in obtaining work permits for expatriate employees. The unwillingness to grant foreign investors work permits is based on the grounds that making authorizations of expatriate staff a cumbersome and long process might help to generate job opportunities for the locals.
  - High on the list of obstacles is also the uncertainty arising from different interpretations of the provisions of new legislation and the frequency of changes in the laws. A recurrent situation is the "big ticket" investment projects that did not face the same constraints as the relatively smaller SADC regional investors.
  - High dependence on commodities: Several African countries rely on the export of a few primary commodities for foreign exchange earnings. Because the prices of these commodities are highly volatile, they are highly vulnerable to terms of trade shocks, which result in high country risk, thereby discouraging foreign investment.
  - Increased competition: Globalization has led to an increase in competition for FDI among developing countries, thereby making it even more difficult for African countries to attract new investment flows, including cross-border investment flows. Relative to other regions of the world, Africa is regarded as a high-risk area. Consequently foreign investors are reluctant to make new investments in, or move existing investments to the region.
  - Other constraints such as: corruption, delays of clearing imports through customs, high interest rates, lack of sound and reliable infrastructure and uncertainty related to macroeconomic stability.

- Underdeveloped Financial Market
Although some progress has been made in deepening financial instruments in Africa in recent years, financial market activities remain limited, with low capitalization and inadequate liquidity in capital markets. Meanwhile, most financial instruments continue to be concentrated at the short end of the term structure. Consequently, the lending rates remain very high. Another issue is the underdevelopment of financial markets. Indeed, only a limited number of financial instruments are issued through the financial markets, making it extremely difficult to hedge against financial market risk in Africa. The absence of a proper and affordable insurance cover against political risks is frequently mentioned as well as the fact that the capital market is still highly fragmented.

In view of promoting financial market development within the SADC region, it is accepted that there is the need to: (i) integrate and consolidate the SADC financial markets; (ii) facilitate the access to information and its free flows; (iii) harmonize the regulatory and legislative frameworks for stock market and listing of securities operations; and (iv) speed up the implementation and monitoring of the Financial and Investment Protocol. In this context, the "一个重要" Barriers and the Quantity Paradigm
The promotion of FDI is a multi-dimensional undertaking which requires a broad set of strategies with multi-faceted goals and objectives. While one of the main goals is improving the business sector is the quantum of FDI received, the underlying national investment strategy for the attraction of FDI needs to encompass a comprehensive set of components, objectives, national characteristics, competitive advantages and preferred activities leading towards the fulfillment of the ultimate vision.

Like other Investment Promotion Agencies (IPAs) in Africa, the IPAs in the SADC region still focusing on the quantum of FDI only while there is no specific and tailor-made investment strategy to tap the regional investment potential.

The preference for this one-dimensional paradigm introduces potential risks of long-term failure and selection of unsustainable foreign investments. Whilst one of the outputs expected from IPAs is to attract as much as possible of FDI, the quality of such FDI in the relevant sectors of the economy and in terms of job creation also matters. There is, therefore, a necessity for all the SADC countries to devise and adopt a national investment strategy that will guide and help the IPA they need to attract the source of foreign direct investment, to " prioritize" sectors where the country has its competitive advantage, the most promising job creation effect is expected and economic cooperation with neighboring countries can result.

2. Enablers

- Geographical Proximity and Market Size
It is widely accepted that a country's success in attracting high levels of FDI cannot be attributed to its one particular characteristic, such as its investment climate, competitiveness and country location. Indeed, geographical proximity matters and could be a driver for regional CBI. In the case of the SADC, the motivation of neighbor investors to invest into another SADC country is very often different from those of the investors outside Africa. The regional investors "business investment" prerequisites seem to be much lower than those of investors from outside Africa and the region who have a different perception of business and political risks, a much longer time horizon and a hurdle rate for its "patient capital" which is much easier to achieve. From this perspective, intra-SADC investment with relatively longer term, committed capital, and with 'patient' investors can be an important building block to shift the region's comparative advantages in a sustainable manner into more diversified production and sources of capital. Henceforth, regional CBI is likely to be deterred by temporary political instability and uncertain investment conditions in the region unlike with non-regional foreign investors.

In addition, the SADC region can capitalize on its market size.

- Special Economic Zones (SEZ)
The renewed interest for SADC countries to establish SEZ could improve the business climate, mainly in countries facing serious infrastructure problems or countries in need of foreign investment and partnerships to develop agriculture potential. The Nasca SEZ could be cited as an example of effort by the Government of Mozambique to attract foreign investment by putting in place special business environment and fiscal regimes.

- Regional Stock Markets
The flotation of new companies, coupled with the stellar performances of African stock markets during the last few years, has seen the market capitalization of the ten largest markets in Africa grow from USD 222 billion to over USD 700 billion between 2002 and 2008, i.e. at a compound annual growth rate of 18%. Within the SADC region, stock markets such as the Johannesburg Stock Exchange and Mauritius Stock Exchange could definitely play a key role in this regard. The SADC region constitutes an interesting space, one which could be used as a pilot case to understand the changes that need to be brought to the operational, regulatory and technological framework for stock exchanges in the region to foster the growth of intra-regional trading, intra-regional portfolio investments and intra-regional funding of listed companies through Initial Public Offerings (IPOs).

IV. Lessons from Asian experience

Intra-Asian FDI accounts for one third of total regional FDI inflows and among the other sub-regions, ASEAN countries have shown a comparatively increasing tendency of intra-ASEAN FDI flows. Hattori and Rajan (2008) find that among Asian countries, while intra-regional investment between East Asia and South Asia remains stable, intra South-East Asia investment increased from 3.6% to 7.4% between the two periods of 1997-2000 and 2001-2004 respectively. The growth of intra-regional FDI in Asia (Figure 2) shows the level of intra-regional FDI among ASEAN countries has increased from 1995 to 2009.

"SADC's Protocol on Finance and Investment (PFI)"
The SADC PFI encourages countries to take advantage of the existing opportunities for regional CBI by adopting policies and measures that promote open cross-border investment regimes. This includes business climate improvement across countries and the adoption and implementation of the SADC PFI.

"Diversified Sectors and Opportunities"
Beyond mining, there are other sectors representing significant opportunities for investors. Given the significant amount of investments required to cover infrastructure needs, the infrastructure sector clearly has opportunities that are ripe for exploitation, mainly by the private sector. Other promising sectors include tourism, agriculture (where important areas for cultivation remain unutilized), finance and telecommunications.
have political and macroeconomic stability and liberal FDI policies. Yet in the case of Botswana, despite several years of rapid growth, visible signs of economic development and significant achievement in the Millennium Development Goals, "the share of non-diamond sectors in total GDP has been roughly constant (about 38 per cent). The policy challenge that has emerged is how to sustain the growth path as "diamond production" slows and reserves are depleted." In Mauritius, after a remarkable performance induced by FDI inflows in the manufacturing sector in the 1960s, FDI performance for the period between 2006 and 2011 has been less successful. With respect to this, Governor Kundu seeing Bhargava said that the Government policy to open up the property sector for non-residents in 2007 was "an unbalanced investment programme heavily skewed towards a sector with a very limited capacity to sustain growth". In these circumstances, FDI in the property and real estate sector can be a rather interesting and viable alternative. However, policy-makers and regulators have to perform a fine balancing act between, on the one hand, the imperatives of economic and financial sector growth and, on the other, concerns about a potentially disruptive speculative property bubble which could defeat the very purpose the policy was meant to fulfil.

It is abundantly clear that the quality of FDI does matter. FDI should be strongly linked to local enterprise development and not confined to small enclave as the benefits of FDI do not accrue automatically and are not uniform across sectors and countries. Experience shows that the authorities need to go beyond traditional liberal FDI policies. In particular, they need to pay more attention to the broad set of regulatory and institutional frameworks conducive to an enabling environment both for foreign investment and for domestic entrepreneurship.

These concerns provide the justification for a more qualitative approach to FDI in Africa. Indeed, it is to do just what kind of FDI policy should resource-rich countries adopt to ensure sustainable economic development over several decades that would make a difference to the poverty in Africa? Intra-regional investment is one of the solutions that can contribute to promoting economic cooperation within a region as well as enhancing sector specialization and complementarity.

III. Barriers and enablers to cross-border investment (CBI) in SADC

1. Barriers

- **Not all Impediments are Business Climate Driven**
The former impediments require a different type of approach in terms of capacity building and skills development.

- **Business Climate** Barriers to Intra-SADC Investment

Broadly, barriers which can be referred to as impediments to SADC regional investments within the category of "business climate barriers" are as follows:

  - Unclear and arbitrary administrative requirements: The issues mentioned pertain to company registration, and to the approval of foreign workers. The recruitment of skilled and qualified local workers appears to be a significant obstacle to intra-SADC investment. There are lots of difficulties and some quite arbitrary decisions in obtaining work permits for expatriate employees. The unwillingness to grant foreign investors work permits is based on the grounds that making authorizations of expatriate staff a cumbersome and long process might help to generate job opportunities for the locals.

  - High on the list of obstacles is also the uncertainty arising from different interpretations of the provisions of new legislation and the frequency of changes in the laws. A recurrent situation is the "big ticket" investment projects that did not face the same constraints as the relatively smaller SADC regional investors.

  - High dependence on commodities: Several African countries rely on the export of a few primary commodities for foreign exchange earnings. Because the prices of these commodities are highly volatile, they are highly vulnerable to terms of trade shocks, which result in high country risk, thereby discouraging foreign investment.

  - Increased competition: Globalization has led to an increase in competition for FDI among developing countries, thereby making it even more difficult for African countries to attract new investment flows, including cross-border investment flows. Relative to other regions of the world, Africa is regarded as a high-risk area. Consequently foreign investors are reluctant to make new investments in, or move existing investments to the region.

  - Other constraints such as: corruption, delays in clearing imports through customs, high interest rates, lack of sound and reliable infrastructure and uncertainty related to macroeconomic stability.

- **Underdeveloped Financial Market**

Although some progress has been made in deepening financial instruments in Africa in recent years, financial market activities remain limited, with low capitalization and inadequate liquidity in capital markets. Meanwhile, most financial instruments continue to be concentrated at the short end-of-term structure. Consequently, the lending rates remains very high. Another issue is the underdevelopment of financial markets. Indeed, only a limited number of financial instruments are issued through the financial markets, making it extremely difficult to hedge against financial market risk in Africa. The absence of a proper and affordable insurance cover against political risks is frequently mentioned as well as the fact that the capital market is still highly fragmented.

In view of promoting financial market development within the SADC region, it is accepted that there is the need to: (i) integrate and consolidate the SADC financial markets; (ii) facilitate the access to information and its free flows; (iii) harmonize the regulatory and legislative frameworks for stock market and listing of securities operations; and (iv) speed up the implementation and monitoring of the Financial and Investment Protocol.

- **Institutional Barriers and the Quantity Paradigm**

The promotion of FDI is a multi-dimensional undertaking which requires a broad set of strategies with multi-faceted goals and objectives. While one of the final measurements assessing FDI performance in the business sector is the quantum of FDI attracted, the underlying national investment strategy for the attraction of FDI needs to encompass a comprehensive set of components, objectives, national characteristics, competitive advantages and preferred activities leading towards the fulfillment of the ultimate vision.

Like other Investment Promotion Agencies (IPAs) in Africa, the IPAs in the SADC region still focusing on the quantum of FDI only while there is no specific and tailor-made national investment strategy to tap the regional investment potential. The preference for this one-dimensional performance goal introduces potential risks of long-term failures and selection of unsustainable foreign investments. Whilst one of the outputs expected from IPAs is to attract as much as possible of FDI, the quality of such FDI in the relevant sectors of the economy and in terms of job creation also matters. There is, therefore, a necessity for all the SADC countries to devise and adopt a national investment strategy that will guide and help the IPA to neutralize the so-called "source of foreign direct investment", to "prioritize" sectors where the country has its competitive advantages, the most promising job creation effort is expected and economic cooperation with neighboring countries can result.

2. Enablers

- **Geographical Proximity and Market Size**

It is widely accepted that a country’s success in attracting high levels of FDI cannot be attributed to its one particular characteristic, such as its investment climate, competitiveness and country location. Indeed, geographical proximity matters and could be a driver for regional CBI. In the case of the SACU, the mobilization of neighbor investors into invest into another SADC country is very often different than those of the investors outside Africa. The regional investors “business investment” prerequisites seem to be much lower than those of investors from outside Africa and the region who have a different perception of business and political risks, a much longer time horizon and a hurdle rate for its “patient capital” which is much easier to achieve. From this perspective, intra-SADC investment with relatively longer term, committed capital, and with “patient” investors can be an important building block to shift the region’s comparative advantages in a sustainable manner into more diversified production and sources of capital. Henceforth, regional CBI is likely to be deterred by temporary political instability and uncertain investment conditions in the region unlike with non-regional foreign investors.

In addition, the SADC region can capitalize on its market size. Indeed, the SADC counts a population size of 257.7 million inhabitants. Meanwhile, it is expected the rapid expansion of the middle classes who will be the potential consumers of goods and services, is expected. In this regard, there is a huge and ever-growing opportunity for manufacturers and retailers in the region. The SADC regional investors’ decision-making process seems to be grounded in a longer time horizon.

- **SADC’s Protocol on Finance and Investment (PFI)**

The SADC PFI encourages countries to take advantage of the existing opportunities for regional CBI by adopting policies and measures that promote open cross-border investment regimes. This includes business climate improvement across countries and the adoption and implementation of the SADC PFI.

- **Diversified Sectors and Opportunities**

Beyond mining, there are other sectors representing significant opportunities for investors. Given the significant amount of investments required to cover infrastructure needs, the infrastructure sector clearly has opportunities that are ripe for exploitation, mainly by the private sector. Other promising sectors include tourism, agriculture (where important areas for cultivation remain unutilized), finance and telecommunications.

- **Special Economic Zones (SEZ)**

The renewed interest for SADC countries to establish SEZ could improve the business climate, mainly in countries facing serious infrastructure problems or countries in need of foreign investment and partnerships to develop Agricultural potential. The Nasca SEZ could be cited as an example of an effort by the Government of Mozambique to attract foreign investment by putting in place special business environment and fiscal regimes.

- **Regional Stock Markets**

The flotation of new companies, coupled with the stellar performances of African stock-markets during the last few years, has seen the market capitalization of the ten largest companies in Africa grow from USD 222 billion to over USD 700 billion between 2002 and 2008, i.e. at a compound annual growth rate of 18%. Within the SADC region, stock markets such as "Johannesburg Stock Exchange" and "Mauritius Stock Exchange" could definitely play a key role in this regard. The SADC region constitutes an interesting space, one which could be used as a pilot case to understand the changes that need to be brought to the operational, regulatory and technological framework for stock exchanges in the region to foster the growth of intra-regional trading, intra-regional portfolio investments and intra-regional funding of listed companies through Initial Public Offerings (IPOs).

IV. Lessons from Asian experience

Intra-Asian FDI accounts for one third of total regional FDI inflows and among the other sub-regions, ASEAN countries have shown a comparably increasing tendency of intra-ASEAN FDI flows. Hattari and Rajan (2008) find that among Asian countries, while intra-regional investment between East Asia and South Asia remains stable, intra South-East Asia investment increased from 3.6% to 7.4% between the two periods of 1997-2000 and 2001-2005. Figure 2 shows how the level of intra-regional FDI amongst ASEAN countries has increased from 1995 to 2009.
By joining Regional Trade Agreements (RTAs), countries benefit from overcoming higher transaction costs.

In terms of geographical barriers, enhancing informational asymmetries by investing in telecommunication infrastructures thus, reducing investment-related costs would positively affect CBI in Africa. Secondly, as formation of RTAs tends to increase trade between its members, deepening of regional trade would stimulate intra-regional investment. However, the existence of RTAs is not in itself self-sufficient; it has to be backed up by domestic reforms, an important factor for encouraging inward FDI. The Asian experience underlines the need for African countries to create investment-friendly environments, to attract both intra-regional and extra-regional investors. Also, the ASEAN experience has highlighted that regional economic cooperation requires setting up a common goal and moving forward together. For African countries in the middle of duplicated RTA agreements to entangle “spaghetti bowl”, emphasis should be put on the role of regional cooperation and domestic reforms for harmonizing investment policies in the region.

In view of intra-regional CBI support in the SADC region, the following recommendations are proposed:

- **CBI strategy**: A specific intra-SADC investment strategy will need to be developed at SADC level to attract the regional investor who does not face the same constraints as the investors from outside Africa. More specifically, intra-SADC investors need to be approached with targeted and specific investment opportunities (projects). The availability of specific investment projects is essential to encourage commitment and genuine interest from investors. Such a strategy should also link the promotion of intra-SADC investment to intra-African trade as a way of accelerating progress towards regional integration. It is worth noting that the experience with other regional blocks suggests that regional capital flows are partly driven by trade.

- **FDI Statistic Harmonization and Investment Portal**: An interactive and dynamic web-based investment portal that combines statistics on intra-SADC CBI, intra-SADC investment success stories, investment opportunities and investment events into a single SADC investment portal is suggested. This requires regular, reliable and harmonized FDI and CBI data. The SADC statistics for which the Central Banks will be the key providers. An institution in charge of the management of this portal should be set up to ensure the availability and consistency of data and information on FDI and CBI. In this view, the creation of a FDI/CBI Observatory within the SADC is recommended.

- **Web-based SADC Regional Investor Surveys**: In order to ensure a bigger sample of regional companies to be surveyed and for the timely completion of the survey, it is recommended that a web version of the “SADC Regional Investor Survey” be organized. The technical assistance could be provided by the Zambia Development Agency, the Central Bank of Zambia, and the Zambian Central Statistical Office which have conducted such surveys for the second year.

- **Support program or projects of IPAs**: IPAs are major actors of promoting investments. This brief recommends the creation of a regional program/project targeting institutional capacity building of key structures/institutions such as the IPAs, the Central Bank and the Statistical Office to: (i) design and implement specific SADC reforms and measures aiming at improving the regional business environment for intra-regional investment; (ii) raise the visibility and potential of SADC region as an investment location by devising country-specific investment strategies to promote SADC CBI; and (iii) improve the availability of statistics and capacity to monitor the intra-SADC investment flows.

- **Private equity funds**: Private equity funds are important vehicles in channeling funds into SADC. They should be promoted by concrete regulatory and fiscal measures. Moreover, a SADC private equity fund dedicated to finance SADC cross-border investment projects exclusively could be set up in consonance with other finance and developed institutional investors.

- **Facilitation of movement of professionals and business operators**: The creation of a FDI/CBI Observatory within the SADC is required.

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Asian Crisis. It stemmed from the countries’ expectation that the process of FTAs as well as ASEAN countries’ own efforts made after the 1997 positive effect of FTAs on attracting FDIs is attributable to the credibility of bilateral FDI flows by roughly 68%. For Schiff and Winters (2003), the economic gains such as enlarged market, economies of scale and RTAs and FTAs capabilities, between countries. It provides justification for the importance of RTAs and FTAs to entangle “spaghetti bowl”, emphasis should be put on the role of regional cooperation and domestic reforms for harmonizing investment policies in the region. In view of intra-regional CBI support in the SADC region, the following recommendations are proposed:

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Institutional Reforms

Institutional reforms are one of the most important determinants of FDIs and a number of studies have shown the positive relationships between the good quality of institutions and FDI flows. The reasoning provided is that an effective institutional and regulatory system reduces transaction costs incurred by investment-related process, and thus stimulates FDI inflows (Daniela and Marco, 2006). Asian countries have introduced a series of reforms in order to raise inward FDI. These measures taken by ASEAN countries include liberalization (Malaysia), deregulation (Malaysia and Laos) and cutting red tapes (Indonesia) and reducing transaction costs (The Philippines and Indonesia).

- **RTAs and FTAs**: By joining Regional Trade Agreements (RTAs), countries benefit from economic gains such as enlarged market, economies of scale and inward FDI increase as well. According to Hattori and Rajan (2008), the operational Free Trade Agreements (FTA) between two countries increase bilateral FDI flows by roughly 68%. For Schiff and Winters (2003), the positive effect of FTAs on attracting FDIs is attributable to the credibility guaranteed by sound international regimes. The regional increase in FDI inflows in ASEAN is explained in combination with the positive effect of RTAs as well as ASEAN countries’ own efforts made after the 1997 Asian Crisis. It stormed from the countries’ expectation that the process of financial recovery would be accelerated by inducing FDI. Also, ASEAN members realized the importance of regional economic cooperation and integration in the aftermath of the Crisis, and this led to the proliferation of Bilateral Investment Treaties (BITs) and FTAs in the region (Figure 4). The establishment of the ASEAN Comprehensive Investment Agreement (ACIA) in 2009 which consolidates the ASEAN Investment Area (AIA) and ASEAN Agreement for the Promotion and Protection of Investment (OA) into a single agreement should be noted. It covers the liberalization, protection, facilitation and promotion of investments. ACIA played a critical role in the establishment of ASEAN Economic Community, designed to establish ASEAN single market and to ensure free flow of investment. In addition to efforts from the regional level, individual ASEAN countries have made progress in facilitating inward investments.

- **Regional FDI rise in Asian countries**: Among others, the following could be replicated.

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VI. Conclusion

Regional CBI will have to be supported through a targeted program for it to become a significant component of FDI within the SADC region. The Finance and Investment Protocol is an important step towards this objective but concrete and effective complementary measures need to be implemented as argued in the precedent sub-section.

South Africa and to some extent Mauritius have emerged as significant sources of investment into other SADC countries. Some other countries can also become significant regional investors while other may become major recipients of SADC investment. More specifically, cross-border investment from the more developed countries in the region especially those that have had export oriented policies and diversification measures can facilitate the transfer of adapted technologies, management and entrepreneurial skills to the rest of the region. Such a trend needs to be encouraged in order to develop the industrial base of the SADC countries.

Finally, more in-depth research is needed on the role of intra-regional investment in the context of regional economic integration of SADC. Further research could investigate the impacts of these regional capital flows on the “quality” of economic growth and development. The areas which could be covered include the extent to which regional direct investment is more labor-intensive and whether there are more skills and technology transfers which accompany regional direct investment as compared to investment from outside Africa. The findings of such an in-depth research would inform a wide range of economic policies for the SADC secretariat.

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Books and articles


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About Us

NEPAD, Regional Integration and Trade Department (ONRI) was established in March 2006 to enable the African Development Bank to play a focused and leading role in supporting the implementation of NEPAD and promoting Africa’s regional integration and trade. By supporting and advancing the soft and hard aspects of regional economic and financial integration, trade, investment and regional infrastructures, ONRI contributes to promoting competitiveness, economic growth and poverty reduction in Africa.

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