

# “The dynamics of foreign direct investment in SADC countries: experiences from five middle-income economies”

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## The dynamics of foreign direct investment in SADC countries: experiences from five middle-income economies

### Abstract

This paper examines the dynamics of foreign direct investment (FDI) inflows and economic growth in five middle-income SADC countries, namely Botswana, Lesotho, South Africa, Swaziland and Zambia. It also analyzes the individual countries' policies and strategies that are aimed at boosting FDI and economic growth. The analysis of this study shows that in the 1980s and the early 1990s, most SADC countries were still coming out of colonialism and as a result, their policies were focused on import substitution, socialism and a command economy. There was a heavy emphasis on protectionism and the protection of infant industries from foreign competition. As a result, the FDI inflows were fairly low during this period. However in the late 1990s and early 2000s, the majority of these countries embarked on privatization, liberalization, economic structural-adjustment programmes and FDI regulatory reviews. These policies led to significant increases in FDI inflows, especially from developed countries. However, like many other African countries, the FDI inflows into these countries are still fairly low. Some of the constraints identified in this paper include political instability, policy uncertainty, poor infrastructure and difficulty in doing business.

**Keywords:** foreign direct investment, economic growth, middle-income country, GDP, SADC.

**JEL Classification:** F21, G18, G28, O11, O40.

### Introduction

Both the theoretical and the empirical literature reveal that foreign direct investment (FDI), which is defined as international investment by an entity resident in one economy – in the business of an enterprise resident in another economy – that is made with the objective of obtaining a lasting interest (IMF, 1993), can contribute to economic growth. In theory, FDI can boost the host country's economy via capital accumulation by the introduction of new goods and foreign technology and by enhancing a stock of knowledge in the host country via the transfer of skills (Elboiashi, 2011).

Herzer et al. (2008) highlight the fact that FDI plays an important function in host countries' economic growth by increasing investible capital and technological spillovers. OECD (2002, p. 5) further argues that FDI represents a potential source for sustainable growth and development, given its assumed ability to: (1) Generate technology spillovers; (2) assist in human capital formation and development; (3) help host countries to integrate into the global economy trade; (4) assist in creating a more competitive business environment; and (5) enhance the development of enterprise.

According to Dupasquier and Osakwe (2005), FDI complements domestic savings by bestowing foreign savings. Ndoricimpa (2009, p. 34) further argues that FDI fills the funding gap between local savings and investment requirements and can also augment the host country's balance-of-payment receipts. The United Nations Conference on Trade and Development (UNCTAD) also argues that FDI

is a more stable source of funding since it is based on a longer-term view of the recipient country's growth potential, raw material accessibility, and access to markets (UNCTAD, 1999).

Because of these perceived benefits, individual countries and regional blocs across the world have been actively pursuing policies to attract FDI. SADC has taken the lead by crafting a Protocol on Trade (SADC, 1996) and recently, the Protocol on Finance and Investment, which is aimed at deepening intra-regional trade liberalization, industrialization and the promotion of foreign investment (SADC, 2006).

Global FDI inflows grew from US\$50 billion in the early 1980s to US\$1.5 trillion by 2011, although they fell by 18 per cent to \$1.35 trillion in 2012 (UNCTAD, 2013a). Africa and the Southern African Development Community (SADC)<sup>2</sup> have also witnessed substantial increases in FDI inflows. For SADC, FDI inflows have grown by almost fifty times the original investment in the last three decades from a mere US\$372 million in 1980 to US\$17 billion in 2008. Although FDI inflows to SADC decreased to US\$7 billion in 2010, there are signs of recovery as 2011 recorded a 38% increase to US\$10 billion. Total FDI inflows into SADC middle-income countries have also grown by more than 24 times from US\$242 million in 1980 to US\$6 billion in 2011.

Despite the important role of FDI in economic development and the increase in FDI inflows into

<sup>1</sup> SADC 15 member countries: Angola, Botswana, Democratic Republic of the Congo, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Swaziland, Tanzania, Zambia, Zimbabwe, South Africa, Seychelles, and Madagascar.

SADC countries in particular, there is significant dearth of literature on the policies and strategies to attract FDI and boost economic growth. Most studies focus on the impact of FDI on economic growth or on the FDI-growth nexus (Juma, 2012), but they do not chronicle the initiatives and challenges faced by individual countries or regional blocs in attracting multinational companies (MNCs).

The purpose of this paper therefore, is to analyze the policies and strategies that have been used by the SADC regional bloc in general and middle-income SADC member countries in particular, to attract FDI and to boost economic growth. The study also discusses the trends and dynamics of FDI inflows and economic growth from 1980 to 2012 and it further investigates the challenges faced by these countries in attracting FDI and growing their economies.

This paper is organized as follows: section 1 outlines, in a case study format, the policies and initiatives that have been implemented by the five middle-income SADC countries to attract FDI, and to boost economic growth in their economies. The section also presents FDI and gross domestic product (GDP) trends from 1980 to 2012 and the final section concludes the study.

## 1. A review of foreign direct investment and economic growth dynamics in middle-income SADC countries: case studies

This section presents the country-based literature review. It describes the policy-development trajectory of each middle-income country and it explains the FDI and economic growth dynamics. The section also highlights major incidents which might have impacted on a country's economic growth or investments. Each country is discussed separately using a case-study approach.

**1.1. Botswana.** At independence in 1966, Botswana was rated among the poorest states in the world, with a per capita GDP of only US\$283. By 2008, the country's GDP per capita stood at US\$13,639 and it was estimated to be US\$14,746 by 2011 (World Bank, 2013a). Between 1966 and 1999, Botswana had the highest rate of economic growth in the world. According to the World Bank July 2012 rankings, Botswana is classified as an upper-middle income country. The 2012-13 Global Competitive Index (WEF, 2012) categorized Botswana as one of the 17 economies which are currently in transition from a factor-driven economy to an efficiency-driven economy<sup>1</sup>.

<sup>1</sup> Other African countries in the same category are Algeria, Egypt, Gabon, and Libya. Mauritius, Namibia, South Africa and Swaziland have been categorized as efficiency driven economies.

*1.1.1. Policies to attract FDI and boost economic growth in Botswana.* Botswana is generally applauded for its pursuit of sound macro-economic policies, which have enabled it to use its diamonds wisely. The World Bank (2013a) and The African Development Bank (2009) credit Botswana's impressive economic performance (being the fastest-growing economy in Africa over the past 40 years) to sound macro-economic policies and good governance.

The country's development process has been guided by the six-year National Development Plans (NDPs), which set the government's development strategy. These NDPs are approved by parliament, and enshrined in law and it is illegal to implement any public sector project that does not feature in the current plan – without going back to parliament (Zizhou, 2009, p. 6). The country is currently on NDP 10 (Government of Botswana, 2007), which has been driven by the country's Vision 2016, which sets a broad policy agenda for poverty-reduction and macro-economic stability. The NDPs and Vision 2016 are aimed at improving the private-sector working environment, "so that there is a shift from government spending to that of enhancing the private sector as the main stimulus of economic growth" (Government of Botswana, 2007, p. 6).

The country has been pushing policies aimed at diversifying its economy. For example, the recently enacted new strategy, the National Strategy on Economic Diversification Drive (EDD) spanning 2011-16 is aimed at promoting the private sector to spur economic diversification. Secondly, to promote beneficiation, the country has signed an agreement with De Beers to relocate its Diamond Trading Centre (DTC) from London to Gaborone by 2013 (ADB, 2012). Under this agreement, all diamonds produced in Botswana will be processed and marketed from Botswana. According to ADB (2012), this move will "transform Botswana into a World Diamond Trading Center, as diamonds from South Africa, Namibia and Canada will be aggregated and sold from there".

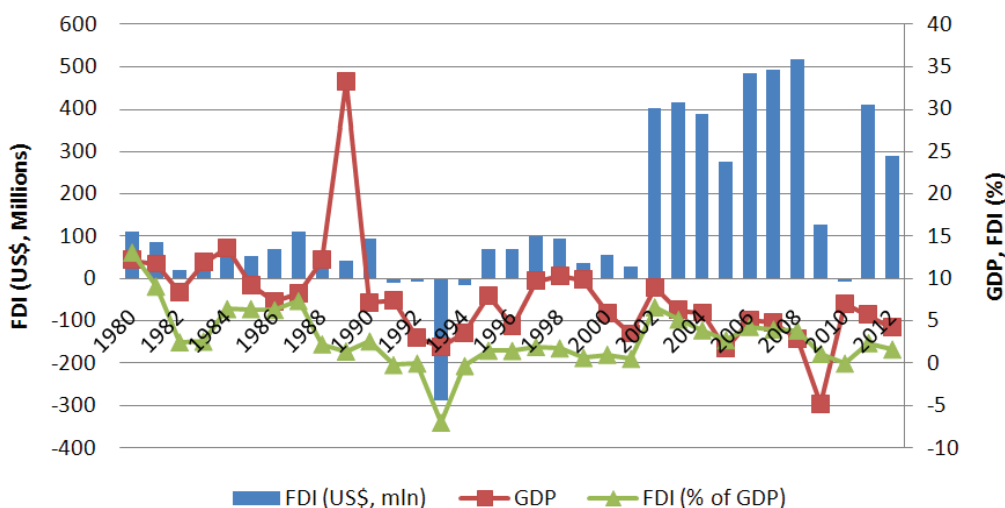
The UNCTD (2003a) notes that Botswana has been open to FDI since independence. Even though other African countries adopted State control and central planning in the 1960s and 1970s, Botswana opted for a market-based system. Before 2002, the country did not have a foreign investment law and therefore relied on sectoral laws to implement policy on the entry of FDI into the country.

An autonomous private-sector led Botswana Export Development and Investment Agency (BEDIA), (which is described as a 'one-stop-shop') assists investors in pre-investment support services including the purchasing or leasing of property, the obtaining of work and residence permits, obtaining the necessary

licenses, and other regulatory authorization, and providing initial start-up grants (BEDIA, 2013).

In an effort to further boost FDI, the government of Botswana developed investment incentives (Government of Botswana, 2003, 2007 and 2009). These incentives or FDI attractions include a stable political environment and good governance, a stable exchange

rate and macro-economic policies, good labor relations, low rates of tax and of corruption, low crime levels, and trade agreements with several countries to provide free access to goods produced in Botswana (Government of Botswana, 1997). Figure 1 below shows the trends of GDP and FDI inflows into Botswana during the period of 1980-2012.



Source: Compilation from UNCTAD and WDI's databases.

Fig. 1. Botswana GDP and FDI trends (1980-2012)

*1.1.2. Challenges facing Botswana in attracting FDI and boosting economic growth.* Despite the successes discussed above, the Botswana economy faces several challenges. Firstly, Throup (2011, p. 2) argues that the country's prosperity is fragile, as the economy is heavily dependent on diamond mine revenues, which account for 55% of government income. Diamond revenues are in turn susceptible to global fluctuations in prices and demand for gemstones.

Secondly, Botswana has one of the world's highest-known rates of HIV/AIDS infection. The 2012-13 Global Competitive Index (WEF, 2012) notes that "Botswana's greatest comparative weakness is the health of the workforce"<sup>1</sup>, which in turn affects FDI inflows and economic growth.

Thirdly, the WEF (2011) categorized the country as having a long processing system for granting construction permits (24 procedures that take about 125 days) which does not compare favorably with that of some Sub-Saharan African countries, where it takes an average of 17 procedures and 51 days.

**1.2. Lesotho.** The IMF (2012a) estimates that 20% of the Lesotho GDP in 2010 was made up of remittances from South Africa<sup>2</sup>. According to the

World Bank (2013b), the economy of Lesotho is based on agriculture, livestock, manufacturing and mining. The country is a regular wheat or maize importer and is susceptible to food crises (IMF, 2012a). Lesotho is a lower-middle income country (World Bank, 2012a).

*1.2.1. Policies to attract FDI and boost economic growth in Lesotho.* According to the Government of Lesotho's Ministry of Industry Co-operatives and Marketing (Government of Lesotho, 2003, p. 5), the country's macroeconomic policy is circumscribed because of its membership in the Common Monetary Area (CMA).<sup>3</sup> Under the CMA, currencies are pegged at parity with the South African Rand. This eliminates monetary-policy autonomy and it implies that Lesotho's external competitiveness would be reflected in movements in the real effective-exchange rate (REER) of the Rand. Because of this relationship, Lesotho imports its monetary and exchange-rate policy from South Africa (IMF, 2012). This brings with it the benefits of a credible monetary policy and stable interest rates, on the one hand, but also the disadvantage of significant currency volatility *vis-à-vis* the rest of the world (IMF, 2012, p. 33).

In its review of the services policy of Lesotho, the UNCTAD (2013b) notes that the country's national development goals and overall economic growth

<sup>1</sup> The CIA, however, noted that despite the high HIV/AIDS infection rates, Botswana also has one of Africa's most progressive and comprehensive programmes for dealing with the disease.

<sup>2</sup> According to the IMF (2012, p. 32), the "World Bank estimates that the number of migrants working in South Africa in 2010 from Lesotho amounted to about 30 per cent of its labor force".

<sup>3</sup> The other members are Namibia, South Africa and Swaziland.



strategies have gone through a number of changes and structural shifts in the last two decades. UNCTAD (2003) advised the Government of Lesotho to provide sustained support to the country’s developmental initiatives, the country’s ability to stimulate local investment and its ability to attract FDI and deepen improved access to export markets.

The key government economic-development policies are Vision 2020, the National Development Plan, the Poverty-Reduction Strategy (which was prepared in partnership with the World Bank) and the Interim Poverty Reduction and Growth Facility (prepared in partnership with the IMF). Some of the key development and economic goals outlined in these documents include:

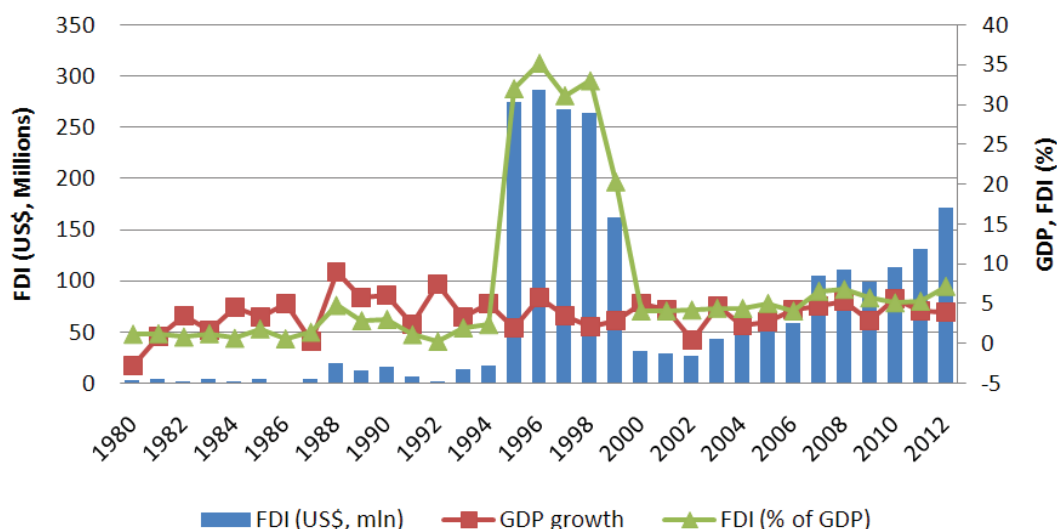
- ◆ The development of an aggressive programme of entrepreneurship at all levels of the economy.
- ◆ Economic diversification, which is seen as the way to reduce the potential vulnerability of negative developments in the two main markets, namely: South Africa and the United States of America.
- ◆ Improving the business environment in order to encourage the development of the private sector while emphasising investment in high-return public infrastructure, such as roads and water supply.
- ◆ Improvement of the investment climate.

According to UNCTAD (2003), FDI is generally welcome and is free to enter in most sectors of the Lesotho economy, especially in export manufacturing which is currently being actively promoted and supported. However, the country does not have foreign investment laws or foreign ownership restrictions in

sectoral licensing laws, except some licensing restrictions in small-scale mining and ubiquitous trade.

The Lesotho government established the Lesotho National Development Corporation in the late 1960s with the aim of initiating, promoting and facilitating investment and development in the country (Malefane, 2007, p. 101). The impact of the new institution was modest in the early years (1960-1988), as the country recorded an average of US\$4 million FDI inflows per year (Malefane, 2007, p. 101). The FDI grew to US\$21 million per year in 1988 in response to the IMF stabilisation programme of 1988 and the privatisation of State-owned enterprises led to further growth in FDI peaking at US\$43 million (5.6% of GDP) in 1994 (Malefane, 2007, p. 101).

As a way of improving its investment climate to attract FDI, the government set up an Inter-Ministerial Task Team (IMTT) for attracting and maintaining FDI in the country (Government of Lesotho, 2013). The team comprises both public and private sector involvement in investment-related matters. The IMTT then launched the ‘One Stop Shop’ in 2007 with a mandate to offer “streamlined services, comprising business licenses, import permits, export visas, and the issuance of residency permits and work permits, in addition to further improvements to business registration” (Government of Lesotho, 2013). Figure 2 below shows that the GDP growth rate of Lesotho has been fairly stable throughout the study period. The country’s economy grew steadily from a negative growth rate of 2.7% in 1980 to a peak of 9% in 1988. Since then, the growth rate has been fluctuating from year to year averaging at 3.9%. The surge in FDI during the period 1995-1999 can be attributed to privatisation sales and investment in garment manufacturing (UNCTAD, 2003).



Source: Compilation from UNCTAD and WDI’s databases.

Fig. 2. Lesotho GDP and FDI (1980-2011)

*1.2.2. Challenges facing Lesotho in attracting FDI and boosting economic growth.* Lesotho is one of the members of Southern African Customs Union (SACU)<sup>1</sup> and a major recipient of the SACU customs revenue. However, the IMF (2012) points out that the revenues from these sources have been volatile and decreasing, which has an impact on the country's fiscus and economic growth. Secondly, Lesotho has a long-standing one-to-one currency peg to the South African Rand. As a result of this relationship, Lesotho imports monetary and exchange rate policy from South Africa<sup>2</sup>. This brings the benefits of a credible monetary policy and stable interest rates on the one hand and on the other hand, the disadvantage of significant currency volatility *vis-à-vis* the rest of the world (IMF, 2012, p. 33). Malefane (2007) argues that the country's FDI initiatives face stiff competition from South Africa, which is more developed and has better business prospects.

The UNCTAD (2003) reviewed Lesotho's investment policies and concluded that though the country was largely open to FDI and treats foreign investors well, its legal framework for investment was poorly developed and required rationalization to enhance transparency and consistency. It noted weaknesses in taxation and business regulation, land regulation, work and residence permits, industrial and trade licensing, competition policy and foreign-exchange control.

**1.3. South Africa.** South Africa's total GDP was estimated at US\$408 billion by the World Bank (2013c). The World Bank (2013c) commends the democratic government<sup>3</sup> for its persistent record of macro-economic shrewdness, sound budgetary policies and an ability to tap into a helpful global environment, which has enabled the country's GDP to grow at a steady pace for almost two decades up to the global financial crisis of 2008-2009 (World Bank, 2013c). The country is currently ranked as an upper-middle income economy with GDP *per capita* of US\$8,070, up from US\$3,547 in 1994 when the new democratic government was sworn in.

*1.3.1. Policies to attract FDI and boost economic growth in South Africa.* Soon after the democratic elections in 1994, the new government came up with the Reconstruction and Development Programme (RDP), a socio-economic development programme advocating for greater equity as the basis for long-term development and growth (Government of South Africa, 2011). The RDP encompassed interventions

aimed at stimulating the economy such as checks on fiscal spending, the reduction of government borrowing, tax reduction and trade liberalization, but with a special focus on social service extension to historically disadvantaged individuals and the roll-out of infrastructural programmes (UN, 2011, p. 6).

The RDP was replaced by a macro-economic policy framework called the Growth, Employment and Redistribution (GEAR) in the year 1996. GEAR was aimed at achieving sustained annual real GDP growth of 6% or more by the year 2000, while creating 400,000 new jobs each year (UN, 2011, p. 6). This was supposed to be achieved through macro-economic stabilization and trade and financial liberalization as a panacea to fostering economic growth, increasing employment and reducing poverty (Ncube et al., 2012, p. 9).

However, the United Nations (UN, 2011, p. 7) argues that GEAR brought mixed outcomes. On the one hand, it could be acclaimed for bringing in sound financial discipline and macro-economic stability; while on the other hand, it could be blamed for failing to increase formal employment and more evenly distributed wealth (Gelb, 2005), not meeting the GDP growth targets and the failure to attract FDI as was expected. As a result of these short-comings, the government came up with a new macro-economic policy in 2006: the Accelerated and Shared Growth Initiative for South Africa (AsgiSA).

As the name suggests, the AsgiSA was meant to help the country in accelerating its growth, and to ensure rising living standards for the majority (Government of South Africa, 2006). AsgiSA was replaced by the current New Growth Path (NGP) and National Development Plan (NDP). The NGP identifies various structural impediments to faster growth and makes recommendations for promoting economic growth with employment creation. The NGP aims to grow the economy at a rate of between 4% and 7% a year (Government of South Africa, 2010). The NDP on the other hand, includes NGP as it is a longer-term strategy up to 2030<sup>4</sup>. The two policy documents tend to be complementary as they both advocate faster economic growth and increased employment creation largely through government interventions in the following areas: infrastructural investment, micro-economic reforms that lower the costs of business, competitive and equitable wage structures, and the effective removal of constraints to investment in certain sectors of the economy (Government of South Africa, 2011).

It is worth noting that since 1996, South Africa has been restructuring its economy to allow for more private sector participation. Furthermore, recent

<sup>1</sup> This includes South Africa, Botswana, Lesotho, Swaziland and Namibia.

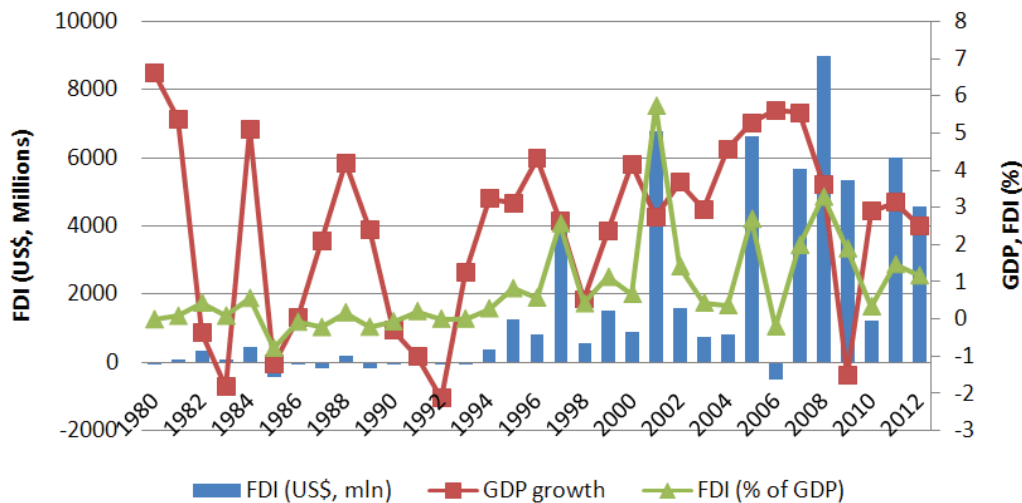
<sup>2</sup> The IMF (2012) quoted Asonuma and others (forthcoming), who find that the use of shocks to South African inflation improve the forecasting of inflation for the BLNS countries, especially in regard to food prices.

<sup>3</sup> This democratic government came into power through the first multiracial elections in 1994.

<sup>4</sup> Its full name is National Development Plan: Vision 2030.

policies like GEAR have emphasized economic growth, as a tool to stimulate FDI inflows while the NGP sights FDI as one of the most important sources for funding the country's developmental

initiatives, especially the green economy (Government of South Africa, 2010). Figure 3 below shows the trends of FDI and GDP during the period of 1980-2012.



Source: Compilation from UNCTAD and WDI's databases.

Fig. 3. South Africa GDP and FDI trends (1980-2010)

**1.3.2. Challenges facing South Africa in attracting FDI and boosting economic growth.** As part of the preparatory work for the *National Development Plan: Vision for 2030*, the South African Government produced a *Diagnostic Report* which identified nine challenges to the economic development of the country. The economic challenges identified include: skills shortages and the lower quality of education; poorly located, underdeveloped and insufficient infrastructure to foster higher growth; the lack of diversification, where the economy is too resource-dependent and widespread corruption (Government of South Africa, 2011). Nevertheless, the country was ranked 52<sup>nd</sup> in the world in *The Global Competitiveness Report (2012-13)* making it the highest-ranked country in SADC and 3<sup>rd</sup> among BRIC's economies. However, the same report recommends that South Africa needs to work on the following to improve its competitiveness: labor market inefficiency, skills shortages, poor security (which leads to a high crime rate), high business costs and the health of the workforce.

**1.4. Swaziland.** The Kingdom of Swaziland (herein referred to as Swaziland) is a geographically small landlocked country with a small open economy heavily reliant on export-based agricultural commodities and industries, especially sugar exports and tourism, with more than 80% of its imports originating from South Africa (Basdevant et al., 2011). The country's economic growth and development are affected by climatic conditions, global economic developments and commodity prices as well as investments and aid flows. The

country is classed as a medium-development country by the United Nations (UN) and as a lower middle-income country by the World Bank (2012).

**1.4.1. Policies to attract FDI and boost economic growth in Swaziland.** From its independence in 1968, the country's socio-economic development policies, strategies and goals were set in successive five-year national development plans (NDPs) and currently in successive three-year rolling development plans. However, in 1988, the Government decided to embark on an improved and more comprehensive planning system and formulated the *National Development Strategy (NDS)*. The NDS is a national macro-economic development policy which sets out a 25-year development framework from 1997 to 2022. The current NDS states its vision as "By the Year 2022, the Kingdom of Swaziland will be in the top 10% of the medium human development group of countries founded on sustainable economic development, social justice and political stability" (Government of Swaziland, 1999, p. 4).

The NDPs, on the other hand, are annual 3-year rolling plans, which depict policies, programmes and projects per prioritized economic sector in terms of current and expected contributions to the economy. Special priority is given to the "Millennium Projects", which are aimed at accelerating investment in infrastructure and tourism in order to create employment and reduce poverty (Government of Swaziland and European Commission, 2002). The country also has the *Economic and Social Reform Agenda (ESRA)* which is a monitoring tool that

imposes pressure on ministries to perform efficiently and to accelerate the implementation of programmes.

The ESRAs are designed in phases just like NDPs, and are aimed at increasing the speed of economic growth, improving social services and enhancing administrative governance. Strategies to accelerate economic growth include the promotion of large-scale investment, the development of small, medium and micro-enterprise sectors and the development of a vibrant tourism sector (Government of Swaziland and European Commission, 2002).

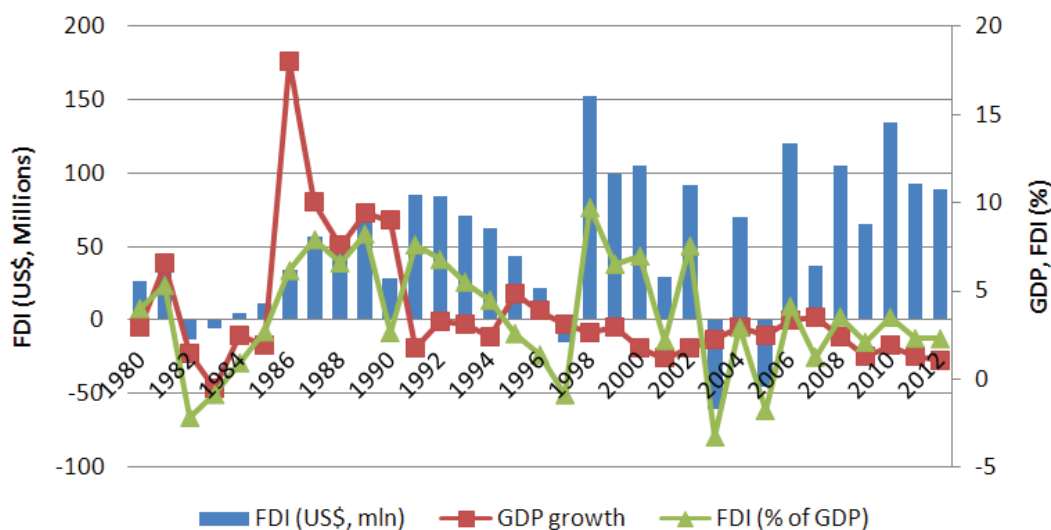
Other policies include the Millennium Action Programme (MAP), the Smart Programme for Economic Development (SPEED), the Government's Programme of Action 2008-2013, the Small and Medium Enterprises Policy of 2005, the Privatization Policy of 2004 and the Decentralization Policy of 2006.

The agency that is responsible for initiating, coordinating and facilitating the implementation of government policies and strategies on investment is the Swaziland Investment Promotion Authority (SIPA). SIPA was created through an Act of Parli-

ament in 1998 (SIPA, 2012) and the same Act sets out general principles in regard to investor treatment and deals with the protection of investment and the settlement of investment disputes.

In the Swaziland Investment Policy of 2009, the government "notes the importance of political stability to inflows of foreign direct and portfolio investment, as well as locally generated investment" (USAID, 2009, p. 15). The goals of the investment policy among others are to: (1) Increase the levels of investment, which would increase economic growth; (2) increase employment opportunities; (3) encourage higher levels of productivity in the economy; (4) export development; (5) increase levels of management skills; (6) the promotion of new technology; and (7) encouraging the growth of small enterprises.

The policy allows for all types of private investment (except that which contravenes the Swazi legislation) and offers incentives to domestic investors with a minimum of US\$50,000 and to foreign investors with US\$100,000 minimum investment. Figure 4 shows the trends of FDI and GDP in Swaziland during the period of 1980-2012.



Source: Compilation from UNCTAD and WDI's databases.

Fig. 4. GDP and FDI trends in Swaziland (1980-2012)

**1.4.2. Challenges facing Swaziland in attracting FDI and boosting economic growth.** As indicated above, Swaziland is a small open economy which is susceptible to weather conditions, global economic developments and to international commodity prices. For example, the country experienced a severe fiscal crisis in 2011, which is assumed to be a lagged impact of the global financial crisis of 2009 (Basdevant et al., 2011). The ADB (2012) also ascribed the current decline in FDI inflows to the country's limited access to land, limited external competitiveness, overvalued exchange rates, high

wages, monopolized telecommunication infrastructure, excessive regulations and also the absence of a well-functioning "one-stop shop" for investors and to the weak marketing of the country as an investment destination.

**1.5. Zambia.** Zambia's total real GDP stood at US\$10.5 billion in 2011; and it is estimated to have grown to US\$11.2 billion in 2012. The country's economy has had over a decade of rapid growth, averaging at 4.75% per annum between 1996 and 2011. Zambia was classified as a lower-middle income country by the World Bank in July 2011 (World Bank



2013d), exactly seven years after reaching its Heavily Indebted Poor Countries (HIPC) completion point in 2005 (IMF, 2005). The country's GDP per capita fell from US\$673 in 1980 to US\$319 in 2000 but it has since rebounded to reach US\$1,425 in 2011.

*1.5.1. Policies to attract FDI and boost economic growth in Zambia.* Thurlow and Wobst (2004) argue

that Zambia's economic development history has been shaped by the expansion and eventual decline of the mining sector (especially copper) and the resultant economic structural adjustment, which began in 1991. These economic development phases are summarized below as chronicled by Saasa (1996), Thurlow and Wobst (2004) and the Government of Zambia (2004).

Table 1. Phases of economic development trajectory in Zambia

Economic policy	Period	Policy actions and result
Pre-policy reforms	1964-1983	<ul style="list-style-type: none"> <li>◆ Centrally planned and protectionism with heavy state control in the ownership and management of economic activities.</li> <li>◆ Economic policies were focused on import substitution, protection of domestic industry from external competition and government directives on investments through industrial licensing.</li> <li>◆ The economy was heavily dependent on copper the proceeds of which were used to subsidize agricultural produce.</li> <li>◆ As a result, the economy deteriorated, mainly as a result of the oil price shock, the falling copper prices in the 1970s and inadequate economic-management responses.</li> </ul>
Economic structural adjustment programme	1983-87	<ul style="list-style-type: none"> <li>◆ Deregulation and privatization of the economy.</li> <li>◆ However, the partial removal of exchange controls led to a substantial depreciation of the local currency (kwacha) and an increase in inflation. This led to food riots in 1986, threatened mining revenues and undermined political support.</li> </ul>
Policy reversal	1987-89	<ul style="list-style-type: none"> <li>◆ Fearing a loss in political power, the government abandoned the recently introduced market-based reforms and reverted back to a command-style economy which included exchange rate controls, fixing of interest rates and price controls on designated products.</li> <li>◆ This led to shortages in the market and the government responded by introducing food coupons to lessen the burden of subsidies and to ration the commodities.</li> </ul>
Liberalization	1990-91	<ul style="list-style-type: none"> <li>◆ Reintroduction of economic liberalization through relaxing exchange and trade controls, privatization and public sector reform.</li> <li>◆ This was, however, accompanied by fiscal and monetary policy contraction.</li> <li>◆ This did not work and then government lost the elections.</li> </ul>
Economic reforms	1991-present	<ul style="list-style-type: none"> <li>◆ Economic restructuring programme under the direction and support of the International Financial Institutions (IFIs) and bilateral donors.</li> <li>◆ The policies included macro-economic stabilization, public sector reform, external liberalization, market-based agricultural reforms and the privatization of state assets.</li> <li>◆ The result was a new growth path, which includes sustained decrease in inflation (to less than 10% currently), growth in the economy averaging at more than 5% in the 2000s and FDI averaging more than 7% of GDP per annum in the same period.</li> </ul>

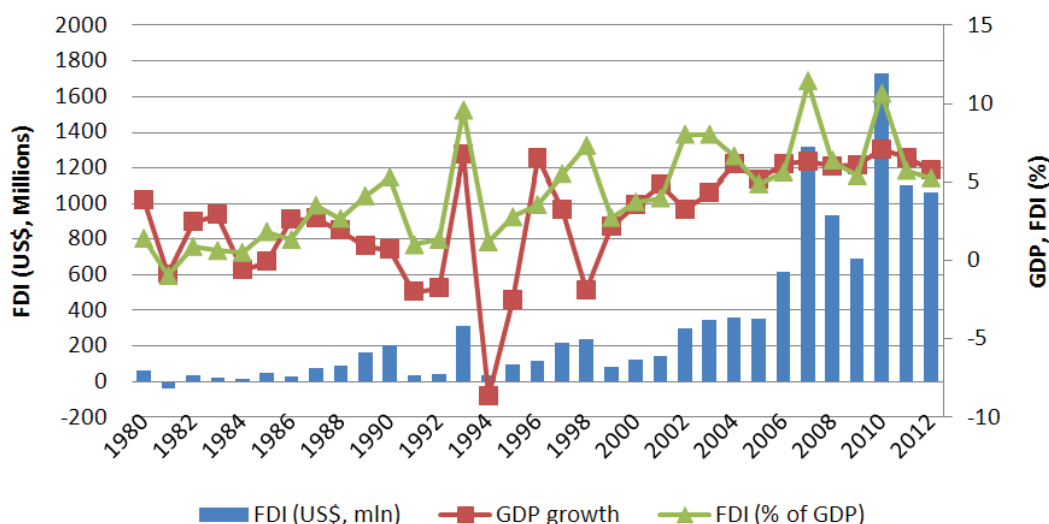
Source: Own illustration from Saasa (1996), Thurlow and Wobst (2004) and Government of Zambia (2004).

From 1991 to date, Zambia has been producing policies and strategies aimed at boosting economic growth and attracting FDI. These include the National Action Plan; the Public Investment Programmes of 2000-2002 and 2001-2003; the Zambia Poverty Reduction Strategy Paper 2002-2004; the Five-year Institutional Strategic Plans; the Sectoral Investment Programmes; and the three-year rolling Medium-Term Expenditure Framework (MTEF) (Mwanawina, 2007).

In a bid to stimulate both domestic and foreign investment, the Government of Zambia adopted an Investment Code in 1994. The code was amended and incorporated into the Zambian Development Agency Act of 2006, which gave birth to the Zambia Development Agency (ZDA). The mandate of ZDA is to address the private sector development needs of the country (UNCTAD, 2011). In 2004, the Government launched the Private Sector Development-Reform

Programme (PSDRP) aimed at improving the investment climate, reducing the cost of doing business and stimulating rapid and sustained private sector-led economic growth (OECD, 2011). The country also set up special economic zones through the support of the Chinese, to incentivise both foreign and domestic investors (Alves, 2012).

Zambia has also been undertaking reforms that are aimed at making it easier for enterprises to do business. These efforts have resulted in Zambia's improved ranking on the World Bank's Doing-Business Index, moving from 90 in 2009 to 76 in 2010 out of 183 economies. Additionally, Zambia has attained a sovereign credit rating of "B+ with stable outlook" by Fitch Ratings in March 2011. Furthermore, Zambia is seen as one of the most open economies to foreign equity ownership (OECD, 2011). Figure 5 shows the trends of FDI and GDP in Zambia during the period of 1980-2012.



Source: Compilation from UNCTAD and WDI's databases.

Fig. 5. GDP and FDI trends in Zambia (1980-2011)

*1.5.1. Challenges facing Zambia in attracting FDI and boosting economic growth.* In its Economic Brief on Zambia, the World Bank (2012b) acknowledges that medium-term prospects for the country's economic growth continue to be strong, but cautioned against significant challenges stemming from global uncertainties as Zambia's economy is heavily dependent on copper exports and fuel imports. The Government of Zambia (2004) highlighted the following as some of the main challenges facing the Zambian economy: the lack of proper co-ordination of fiscal and monetary policy leading to persistent fiscal deficits; underdeveloped and segmented financial markets which limit the country's ability to attract more FDI and low savings and investments.

In its Zambian Investment Policy Review report, the OECD (2011) lauded Zambia for its efforts and successes in improving the business and investment environment over the past years, but noted the lack of "a complete and coherent investment policy". The study also highlighted that ZDA's current mandate was too broad considering its capacity thus limiting its ability to promote and facilitate investment in a focused manner. Other recommendations include the development of a predictable and fair tax system, and the easing of bureaucratic and costly processing in obtaining incentives for investment.

## Conclusion

This paper has explored the dynamics of FDI inflows and economic growth in five middle-income SADC

countries. It has also analyzed the individual countries' policies and strategies aimed at attracting FDI and boosting economic growth. The findings of this study show that in the 1980s and early 1990s most SADC countries were still coming out of colonialism and hence their policies were mainly focused on import substitution, socialism and command economies, with strong emphasis on the protection of infant industries. As a result, FDI inflows were fairly low during the first two decades. FDI into SADC started peaking in the late 1990s as governments embarked on privatization, liberalization and economic structural-adjustment programmes. These reforms saw the warming up of countries to MNCs and the setting up of investment-promotion agencies. Some of the policies that were implemented by these countries include: (1) the deregularization of the economy; (2) the relaxation of exchange controls; (3) the adoption of 'market-friendly' policies, such as privatisation and trade liberalisation; (4) the protection of foreign investments; (5) political stability; and (6) participation in multilateral and bilateral trade and investment agreements. It is also worth noting that countries, such as South Africa, Zambia, etc., that pursued the privatization of state-owned enterprises, recorded a significant increase in FDI inflows and economic growth. Some of the constraints currently faced as FDI inflows into these SADC middle-economies include political instability, policy uncertainty, poor infrastructure and difficulties in doing business.

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