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**THE INFLUENCE OF HOST-COUNTRY INSTITUTIONS
ON MULTINATIONAL ENTERPRISES (MNEs)
INVESTMENT IN THE LEAST DEVELOPED
COUNTRIES: THE CASE OF ZAMBIA**

By

Roy Kapembwa

September, 2010

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Dedications

This piece of work is dedicated to my lovely wife, Mika Chitalu Kavuzya- Kapembwa and my children, Chilombo Kapembwa, Zoya Kapembwa and Mwanga Kapembwa, for being there for me during the entire period of my study and their unceasing support, and for allowing me to split time between the demands of my work, school work and family. I also wish to dedicate this piece of work to Mr. Derrick Elemu for his relentless support and all my friends for their support throughout my study period. Without their support and understanding, I do not think I could have come this far in my studies. Thank you very much to all of you.

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List of acronyms

CEEC	Citizens Economic Empowerment Commission
DCs	Developed Countries
EBZ	Export Board of Zambia
ERB	Energy Regulation Board
FDI	Foreign direct investment
FSP	Fertilizer Support Programme
GDP	Gross Domestic Product
GMAAs	Game Management Areas
GNI	Gross National Income
GRZ	Government of the Republic of Zambia
HIPC	Highly Indebted Poor Country
ICT	Information Communication Technology
IDA	Ireland Development Agency
IFC	International Finance Corporation
IPA	Investment Promotion Agency
LDCs	Less Developed Countries
LuSE	Lusaka Stock Exchange
MCTIZ	Ministry of Commerce, Trade and Industry Zambia
MDGs	Millennium Development Goals
MFEZs	Multi-Facility Economic Zones
MNEs	Multinational Enterprises
NGO	Non-Governmental Organization
NTEs	Non-Traditional Exports
PACRO	Patents and Companies Registration Organization
PTF	Privatization Trust Fund
REC	Research Ethics Committee
SADC	Southern African Development Community
SEC	Securities and Exchange Commission
SEDB	Small Enterprises Development Board

SFADCo	Shannon Free Area Development Company
SOEs	State-owned Enterprises
TEVETA Authority	Technical Education, Vocational and Entrepreneurship Training
TOE	Tons of Oil Equivalent
UNCTAD	United Nations Conference on Trade and Development
ZCC	Zambia Competition Commission
ZCCM	Zambia Consolidated Copper Mines
ZEPZA	Zambia Export Processing Zones Authorities
ZDA	Zambia Development Agency
ZIC	Zambia Investment Center
ZPA	Zambia Privatization Agency

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Abstract

This paper presents an analysis of Zambia's FDI policy and institutional framework and the role of host-country institutions in attracting and/or hindering the flow of FDI into the country. Following the single embedded case study approach (and using both in-depth interviews with key informants and secondary literature), the paper investigates Zambia's FDI legislation/policy challenges and the role of host-country institutions in attracting FDI.

Specifically, the paper reviews Zambia's FDI legislation/policy challenges and existing institutional frameworks for attracting foreign MNEs into the country; analyzes the role host-country institutions (particularly the ZDA) play in influencing MNE decisions to invest or not to invest into the country via FDI strategies; and finally provides recommendations on the best policy and institutional configuration that is necessary for Zambia to attract FDI via MNEs.

The paper starts with a detailed review of literature on Zambia's economic trends, MNEs and FDI strategies and decisions in Less Developed Countries (LDCs), and finally zeros in on the empirical consideration of FDI flows to Africa, and Zambia in Particular.

With regard to policy framework, the paper highlights that while Zambia has no "Policy" per se governing MNEs and FDI, the ZDA Act stands out as the main investment promotion legislation. This, however, has brought challenges leading to overlapping and even contradicting mandates in the current institutional framework and further impacting on the behavior of MNEs.

The paper then focuses on the ZDA as the leading investment promotion agency in Zambia, highlighting a number of challenges that the organization must overcome if it is to become the one-stop-shop for investment promotion that it is intended. The paper briefly discusses the many stakeholders involved in investment promotion activities in

Zambia and highlights the resultant confusion and mix up in roles and mandates between these players.

Thereafter, the paper discusses critical issues necessary for Zambia to become the preferred investment destination, and thereafter analyses the general policy and institutional framework for attracting FDI, highlighting the positive and negative aspects.

The paper concludes that the Zambian government may have demonstrated reasonable commitment towards FDI, but serious challenges still remain unresolved.

The paper, therefore, recommends that policy and institutional reforms would be critical in the short (policy harmonization) as well as long term (investment policy formulation). Further, the paper recommends that ZDA itself would need extensive surgery and restructuring so that it becomes more effective and efficient in its functions.

This is some of the many aspects that Zambia must resolve if the country is to shift upwards in international ranking for FDI destinations.

CHAPTER ONE

Introduction

Recent developments in globalization have opened up the least developed countries (LDCs) to Multinational enterprises (MNEs) in a variety of ways. As a result, many MNEs seeking to spread their reach have taken advantage of the opportunities that come with such openness in LDCs to increase their market share and profits through foreign direct investment (FDI) (Buckley and Casson, 1998). In this case paper, FDI is defined as investment in lasting interests in enterprises operating outside the economy of the investor (Buckley and Casson, 1998) and excludes portfolio flows and minority shareholdings. FDI of all types has been playing an increasingly important role in the development plans of both developed and developing countries.

Naturally, the demand for FDI exceeds the supply. Thus, competition for FDI continues to grow, both in terms of intensity and complexity. Potential investors are always faced with limitless numbers of attractive options for any new investment (MCTIZ, 2009). As a result, many governments the world over are actively seeking to win an increased share of global investments through a variety of strategies and policy frameworks. However, entry into these markets is not without its own challenges. Host-country institutions in most of these LDCs may not be as receptive and liberalized as most foreign MNEs would expect. Thus, there are challenges that do arise as the new entrants negotiate their way and settle into these new territories.

In the context of Zambia, it should be noted from the outset that over the last two decades, its economic recovery programme has been characterized by structural reforms that sought to transform the economy from one dominated by Government parastatals to a private sector-led economy (GRZ, 2006). At independence in 1964, the Zambian economy was broadly stable but characterized by slow growth. Using the World Bank Atlas method of ranking world economies, Zambia's Gross National Income

(GNI) per capita stood then at US\$200. Zambia's per capita GNI remained higher than those of Botswana, Egypt and Thailand, until the late 1970s and early 1980s (GRZ, 2006, p. 10). In the early 1970s, the macroeconomic environment was destabilized by rising transport and petroleum costs and declining copper prices. This resulted in Zambia's budget and balance of payments surpluses shifting to massive deficits on both accounts. Expecting the terms-of-trade shock to be temporary, the Government chose to finance the imbalances through domestic and foreign borrowing, at variable interest rates. Contrary to expectations, the oil price shocks and declining copper prices persisted; world interest rates were rising sharply; and coupled with regional conflicts among Zambia's neighbours, the macroeconomic environment was destabilized even further (GRZ, 2006).

It was not until 1991 that Zambia embarked on an ambitious effort to liberalize and streamline its economy. This was done by ensuring that a conducive private investment climate was created. In all this, FDI promotion has been one of the most important pillars of the Zambian Government's economic and social policies. The policies being implemented are intended to help discover Zambia's comparative advantage and, in the process, develop strategies for attracting high volumes of FDI in various economically productive sectors in order to create wealth and reduce unemployment. The highlights of the reforms included the privatisation of 260 SOEs. MNEs have bought out previously state-owned enterprises (SOEs) via the Zambia Privatization Agency (ZPA) spearheaded privatization policies.

To facilitate this programme, the Securities and Exchange Commission (SEC) was established through the Securities Act (1993). The Act was meant to regulate the new stock market and protect investors. The Lusaka Stock Exchange (LuSE) began operations and the Privatization Trust Fund (PTF) was established as a temporary warehouse for shares which were to be sold to the public through floatations. By the end of 2004, 259 SOEs out of the original portfolio of 282 had been privatized, including the state Zambia Consolidated Copper Mines (ZCCM) and various other manufacturing plants (Zambia Privatization Agency [ZPA], 2001). In 2000, concerns were raised that

the various institutions and Acts regulating investment in Zambia were extremely fragmented. To overcome this fragmentation in efforts towards attracting investment, these institutions were merged in 2006 under the Zambia Development Agency (ZDA) Act for an efficient, effective and coordinated private sector led economic strategy (ZDA Act, 2006). The Agency was meant to spearhead all investment promotion and facilitation activities in the country. The board would ensure that the investment policy framework, macroeconomic policies, infrastructure and the costs of doing business are streamlined to levels that make the country's producers more competitive regionally and internationally (MCTIZ, 2009).

The ZDA Act also established the concept of Multi-Facility Economic Zones (MFEZs) intended both for domestic and export-oriented activities, in production and trade. The Act allows for the declaration of specific areas, premises or buildings to be multi-facility zones, and indicate the facilities to be provided and maintained within a MFEZ. Further, to benefit from this initiative, an investor must be in one of the priority sectors, namely, tourism, manufacturing and agriculture. Investors who act as "Zone developers will be granted a ten-year tax exemption on profits and dividends, relief from import duty on equipment, and tax free allowances for infrastructure development". Further, investors within an MFEZ were to receive tapered relief from profits tax; dividends tax and import duties on raw materials; and intermediate and capital goods. In addition, double deductions on corporate income tax will cover expenditure on export promotion; human resource development; research and development; and major corporate social responsibility programmes (GRZ, 2009).

It is therefore evident from this background, especially in the post-1991 period that the Zambian Government has endeavoured to improve the competitiveness of the economy in attracting FDI during the liberalisation of the economy in the country. A key challenge confronting Government has been the creation of an institutional and policy framework that would attract rather than hinder the flow of new FDI and lead to accelerated economic growth. These policies bearing fruits, it was envisioned that by 2030, Zambia will grow to become a middle income nation (MCTIZ, 2009). However, despite some

considerable inflow of FDI and some positives in overall economic performance, the policy and institutional framework for attracting FDI currently in place in Zambia has been highly criticized. Furthermore, absolute FDI inflows to Zambia have been deemed to be quite small.

This study therefore sought to analyze Zambia's FDI policy and institutional framework and the role of host-country institutions in attracting and/or hindering the flow of FDI into the country. The study also reviewed the main policy and institutional considerations that stand out in MNEs strategies and decisions vis-à-vis FDI in LDCs. Specifically, the study tried to respond to the question of the role that host-country institutions play in influencing MNEs' decisions to invest in LDCs via FDI strategies.

Statement of the Research Problem

A number of empirical studies have attempted to investigate host-country policy factors that influence MNE entry strategies, particularly with regard to FDI. It is however also evidenced in the literature that most empirical studies on this topic have been undertaken in the context of DCs. For instance, among the more recent works on FDI theory, among others Grosse and Trevion, 2005; Buckley et al., 2007; & Sethi et al., 2002; have all been carried in the context of American MNEs and their FDI in other DCs. Moreover, the majority of these studies have tended to be quantitative in nature and focus on the overall political and macroeconomic policy framework, with limited consideration of the micro-institutional policy level. While comparability between countries is important, leaving out sector specific aspects and "fine-grained" institutional analyses on how MNEs interact with host-country institutions and policies within countries could be detrimental to understanding MNEs' FDI investment strategic choices in LDCs.

In the changing scenario where the global economy has become so intricately integrated, the need to generate new insights in the context of LDCs cannot be overemphasized. Literature has shown that host-country institution-MNE relations are

bound to be contextual, and that they would tend to evolve over-time according to changes in host-country policies and MNE objectives and entry strategies. In fact, these relations would entail consultative and negotiated processes between host-country institutions and MNEs. Over the years, and especially in the post-1991 period, the Zambian Government has endeavoured to improve the competitiveness of the economy in attracting FDI through a variety of initiatives.

In spite of these efforts, Zambia still lags far behind most of its competitors even within the region. A number of critical issues have been highlighted as major contributors to this state of affairs. Among the regularly cited is the lack (and/or) fragmentation in FDI policy/legislation and institutional frameworks for attracting foreign MNEs into the country and the role host-country institutions, particularly the ZDA, could play in influencing MNE decisions to invest or not to invest into the country via FDI strategies.

In the context of the institutional approach, this study sought to investigate Zambia's case in attracting MNE and the role host-country institutions play in enhancing or hindering FDI flows to LDCs. The case study approach was necessary in order to delve more in depth in Zambia's FDI legislation/policy challenges and the role host-country institutions, particularly the ZDA, could play in influencing MNE decisions to invest or not to invest into the country via FDI strategies. This is critical because to the larger extent, FDI strategies are shaped by host-country institutions and MNE interactions that result from the configuration of the institutional infrastructure in that economy.

Study Objectives

General Objective

To investigate Zambia's FDI legislation/policy challenges and the role of host-country institutions in attracting or hindering the in-ward flow of FDI by MNEs.

Specific Objectives

- To review Zambia's FDI legislation/policy challenges and existing institutional frameworks for attracting foreign MNEs into the country;
- To analyze the role host-country institutions (particularly the ZDA) play in influencing MNE decisions to invest or not to invest into the country via FDI strategies;
- To provide recommendations on the best policy and institutional configuration that is necessary for Zambia to attract FDI via MNEs;

Study Rationale

The literature on MNEs' FDI strategies and decision consideration for investing in foreign countries is plentiful. Many have endeavoured to investigate the historical developments of FDI theory such as those by Hymer, 1960; Dunning 1981, 1998 & 2001. The critical role of host-country institutions and government policies is another area that has received a lot of attention (Grosse, 2005). Yet other writers have focused on the shifting interactions between LDC host-institutions and MNEs from the DCs.

A general glance on the literature indicates that the configuration of institutional infrastructure affects the investment decisions of MNEs and therefore shapes their FDI in LDCs. This is premised on the concept of institutions as formal conventions (rules), as well as informal conventions (standards) of society (Grosse, 2005). In this context, FDI is informed by the institutional infrastructure – the overarching environment in which institutions and organizations operate – that facilitates economic activity.

A number of studies have been done on the institutional determinants of FDI. However, there appears to be limited empirical works on the role host-country institutions are bound to play in foreign MNEs' decisions on which of the LDCs are more viable for FDI. The study will facilitate the production of knowledge which is critical to understanding, and/or explaining the role of host-country institutions and their relative significance in MNEs' investment decisions in the LDCs. These insights will therefore inform both policy review and future research in order to further understand MNE decision when considering FDI in LDCs like Zambia.

Additionally, this study is important as it will be conducted in partial fulfillment of the requirements for the award of the MSc degree.

Structure of the Dissertation

The dissertation is divided into five chapters. To appreciate the context and the magnitude of the challenges Zambia as a country is confronted with *vis-a-vis* its efforts to attract FDI, immediately following this introductory chapter, chapter 2 begins by providing a detailed review of the literature on FDI. In this chapter, the first section provides a theoretical analysis on the many arguments and theories that inform decision-making both by host-country institutions wishing to attract FDI and MNEs wishing to invest in foreign countries.

Thereafter, the methodological issues applied in the study are presented in chapter three. This chapter begins by highlighting the methods, procedures and criteria followed to identify target groups and collecting data. It closes with a description of how the data were analysed and presented in this dissertation.

The main research findings are then presented in chapter four. The first section presents Zambia's FDI policy and regulatory institutional framework for attracting FDI in Zambia, highlighting the major weaknesses and gaps. The section concludes that this is

a continuing process as the policy framework is far from being competitively solid. The second part of chapter four then analyzes the role of host-country institutions in influencing MNE decision to invest or not to invest into the country via FDI strategies.

The fifth and final chapter then highlights the main conclusions and provides recommendations both for policy and future research on the best policy and institutional configuration that is necessary to attract FDI via MNEs in Zambia.

CHAPTER TWO

LITERATURE REVIEW

Zambia's Economic Development Trends

Zambia covers an area of 752,614 square kilometers, with a terrain which is mostly plateau savanna and a climate which is dry and temperate. The population, which is predominantly Christian, is currently estimated to be about 11.7 million with an annual growth rate of about 2.9 percent. The country is endowed with abundant natural resources, which include copper, cobalt, zinc, lead, coal, emeralds, gold, silver, uranium, water and fertile land. The main industries are mining, transport, construction, manufacturing and agriculture.

At independence in 1964, the Zambian economy was broadly stable but characterized by slow growth. Using the World Bank Atlas¹ method of ranking world economies, Zambia's Gross National Income (GNI) per capita stood then at US\$200 (current US\$). Zambia's per capita GNI remained higher than those of Botswana, Egypt and Thailand, until the late 1970s or early 1980s. Zambia's GDP was also larger than that of Botswana, Gabon and Panama during this period.

The overall budget balance and balance of payments were both in surplus at independence and remained so for the next two years. Foreign reserves were also high, amounting to close to twelve months of import cover while public external debt was virtually non-existent. However, while being in balance, the structure of the economy was designed to service the copper mining sector and the white settler community. As a result, the non-mining economy was underdeveloped and human development for the majority African population remained dismally low.

To develop and diversify the economy, the new Government took over fifty-one percent ownership of the mines and nationalized a substantial part of the manufacturing sector, all public utilities and key elements of the transport and communications sector. The Government also constructed socio-economic infrastructure, including an oil pipeline, rail line, roads, bridges, schools, hospitals and housing units. Consequently, investment into socio-economic infrastructure was high, averaging 30 percent of annual Gross Domestic Product (GDP) between 1965 and 1982.

In the early 1970s, the macroeconomic environment was destabilized by rising transport and petroleum costs and declining copper prices. This resulted in Zambia's budget and balance of payments surpluses shifting to massive deficits on both accounts. Expecting the terms-of-trade shock to be temporary, the Government chose to finance the imbalances through domestic and foreign borrowing, at variable interest rates. Contrary to expectations, during the 1970s and 1980s, Zambia's macroeconomic environment was increasingly destabilized by declining copper prices, rising world interest rates and regional conflicts among its neighbours.

During the period 1965 and 2001, the economy grew at an average annual rate of 1.7 percent, compared to 10.3 percent for Botswana, 6.9 percent for Malaysia, and 5.4 percent and 4.8 percent for Egypt and Gabon respectively. The main growth sector in Zambia, while at much slower rates than in Botswana, Egypt, Malaysia, Panama and South Africa, was industry, which accounted for 0.8 percentage points of the 1.7 percent real GDP growth. The rest of Zambia's economic growth was accounted for by the services sector, (0.6 percentage points) and agriculture (0.3 percentage points).

Segmenting the period into pre-market reform (1965-1992) and post-market reform (1993 to 2001) eras, there are indications that during the pre-market reform era, Zambia's economy grew at a period average annual rate of 1.7 percent, far slower than Botswana (11.9 percent), Malaysia (7 percent) or Egypt (5.5 percent). The Zambian economy grew at a period average annual rate of 1.6 percent during the post-market reform era, again far slower than the pace in Botswana (5.5 percent), Malaysia (6

percent), or Egypt (4.5 percent) during the same period. The main sources of growth, during the pre-market reform period were industry, which accounted for 0.87 percentage points of the 1.7 percent growth, followed by services, which accounted for 0.58 percentage points of the 1.7 percent and finally agriculture, accounting for 0.27 percentage points of the 1.7 percent. The main sources of growth, during the post-market reform period were services, which accounted for 0.74 percentage points of the 1.6 percent, followed by industry, at 0.52 percentage points of the 1.6 percent and lastly, agriculture accounting for 0.27 percentage points of the 1.6 percent average annual growth rate.

In terms of Zambia's sector growth performance, during the period 1965 to 2001, the fastest growing sector was agriculture, at 3.1 percent period average annual growth rate, with most of the growth occurring during the post-market reform period (9.7 percent between 1992 to 2001 compared to 0.9 percent between 1965 and 1992). The worst performing sector was industry, which grew at a marginal period average annual rate of 0.5 percent, with its weakest performance being recorded during the post-market reform period (average annual decline of 3.2 percent during the period 1993 to 2001 compared to an average annual growth of 1.8 percent during the period 1965 to 1992). The poor sector performance was mainly due to weak or negative growth in the mining and quarrying and manufacturing sub-sectors.

The poor performance of the mining and quarrying sub-sector was due to declining copper production, which contracted at an average annual rate of 3.2 percent a year between 1965 and 2001. The decline was particularly severe in the 1990s, when the sector contracted at average annual rate of 5.1 percent a year. The decline was driven by falling international copper prices, which declined by an average rate of 3.4 percent a year between 1973 and 2002 as well as due to lack of new capital investment.

Manufacturing value added as a share of GDP increased from 7 percent in 1965 to a peak of 37 percent in 1992. During the period, manufacturing value added grew at an average annual rate of 3.7 percent, compared to 11 percent in Malaysia and 10.3

percent in Thailand. The weak relative performance of Zambia's manufacturing was due largely to the dominance of a stagnant state-owned enterprises sub-sector and the prevalence of state controls. Hence, in 1993, Government commenced the privatization of state-owned enterprises and liberalized external trade. The immediate impact of the reforms was a further deterioration in manufacturing sector performance, due both to restructuring and weak investment: Zambia's gross fixed capital formation declined from a period annual average of 19 percent of GDP between 1971 and 1992 to 14 percent between 1993 and 2001. Average annual value added growth fell to 1.8 percent during the period compared to 7.8 percent for Malaysia and 4.7 percent for Thailand. Average annual manufacturing value added share fell to 11 percent of GDP during the period.

Since 1996, Zambia's manufacturing sector has resumed positive growth, although the recovery has been uneven. The industries that have grown fastest are those that have a growing domestic demand (food, beverages and tobacco) due to population growth and those that have had new entrants with a focus on exports (mainly textiles and leather products). Other industries, including basic metals, non-metallic minerals and fabricated mineral, have remained stagnant or declined.

The share of manufactured goods as a percentage of merchandise exports increased from 1 percent in 1975 to 13 percent in 2001. However, Zambia's share of manufactured goods in merchandise exports is much lower than in Malaysia, South Africa and Thailand where they constitute the majority of merchandise exports. In each of these economies, the rise in the share of manufactured goods in merchandise exports during 1975-2001 was a multiple of the corresponding increase in Zambia

Copper, Zambia's major export, accounted for an average of 67 percent of annual total export receipts between 2002 and 2005. This increase was buoyed by an upward trend in copper prices which rose from US\$0.61 per pound in 2002 to US\$1.61 per pound by the end of 2005. Exports of secondary products including sugar, copper wire and electric cables have also been enhanced by the rise in their constituent prices. However, other world commodity prices have been extremely unstable with Zambian

export prices other than copper generally exhibiting a downward trend, adversely affecting non-traditional exports (NTEs). NTEs largely comprise primary products such as cotton lint, cotton yarn, flowers, vegetables, gemstones and tobacco. Their price declines have resulted in the share of NTEs in Zambia's total export earnings falling from 39.0 percent in 2002 to 25.7 percent in 2005. As NTEs are becoming an important source of Zambia's foreign exchange as well as employment and incomes for many rural households who grow export crops, the decline in their prices is a worrisome portent of future incomes in this sector. Moreover, value added in the export sector as a whole remains weak to non-existent.

In 1964 the size of the Zambian economy, measured by its real GDP, was 12 times larger than that of Botswana and twice that of Gabon. From 1964 to 2001, the size of the Zambian economy increased by only a factor of 1.8, compared to 36.3 for Botswana, 10.9 for Thailand and Malaysia, 6.5 for Egypt and 4.6 for Gabon. In per capita terms, in 1964, Zambia's GNI was 2.2 times larger than that of Botswana in 1964, 1.5 times larger than that of Thailand and 1.3 times larger than that of Egypt. By 2001, the GNI per capita for Botswana, Egypt and Thailand were, respectively, 9.7 times, 4.8 times and 6.1 times larger than Zambia's GNI per capita.

Zambia's inflation rate increased from an annual average of 3.1 percent in 1964 to a peak of 197 percent in 1992, and then progressively declined to an annual rate of 17.5 percent in 2004. This improvement has continued with inflation declining to 15.9 percent for the year 2005, and falling to less than 6 percent in the second half of that year. The inflation rate in 2006 continued this encouraging performance, falling to a rate of around 6 percent. The exchange rate between the Kwacha and the US dollar depreciated from K0.71 per US\$1 in 1964 to K4, 445 per US\$1 in 2004. However, since 2004, the Kwacha has appreciated by more than one quarter against the dollar, ending 2005 at K3, 383 per US\$1. The Kwacha exchange rate is a measure of the market's confidence in Zambia's financial market outlook, and reflects the anticipated inflation over the short and intermediate term. The recent performance of both is quite encouraging.

At the end of 2004 Zambia's total external debt stood at approximately US\$7.3 billion dollars compared to US \$813.5 million at the end of 1970, a nearly nine-fold increase. In comparison with the other countries in the table above, the increase in external debt is not large. For example, the increase in Gabon's external debt stock was about the same as Zambia's, while Egypt's debt increased by a factor of 18, and that of Malaysia rose by a factor of 33. However, the per capita income in each of these countries also rose (Egypt's by 5 times, Gabon's by 2, and Malaysia by 4 times while Zambia's per capita income fell by nearly half). Thus, the burden of per capita debt rose in Zambia by a factor of more than 16, much more than in these countries.

The ratio of Zambia's debt to GNP increased from 39 percent in 1973 to 224 percent in 1998, and averaged 191 percent between 1988 and 1997. This contrasts sharply with Malaysia and Thailand, whose debt-GNP ratios were 25 percent and 14 percent, respectively. More to the point, the debt service as a share of Zambia's tax revenues were multiples of those of Malaysia and Thailand – particularly given that the ratios shown in Table 4.1.5 for Zambia represent “debt service paid” which was substantially smaller than what was owed. Zambia's accession to the Highly Indebted Poor Countries (HIPC) initiative completion point and the multilateral debt Relief initiative by the G8 in 2005 has virtually wiped out its external debt. Consequently, this debt relief will provide a substantial strengthening of Zambia's financial solvency and increase the application to domestic objectives revenues that were formerly required to service its burdensome external debt.

MNEs and FDI Strategies and Decisions in Less Developed Countries

The literature on MNEs' FDI strategies and decision consideration in the LDCs abounds. Among others, a number of themes are observable, from the early developments in FDI theory (Hymer, 1960; Dunning 1981, 1998 & 2001); the critical role of host-country institutions and government policies (Whitley, 1998); and the shifting interactions between LDC institutional players and MNEs from the developed countries

(DCs). Among the commonly expressed theories, one finds the portfolio theory, neoclassical trade theory, organisational theory and others that relate to industrial organisation. Yet, others have focused on the empirical works done on the institutional determinants of MNEs FDI in the context of LDCs (Buckley et al., 2007).

As far as the origins of FDI theory is concerned, it has mainly been expressed in the context of the neoclassical theory of portfolio flows. This was mainly the case immediately after World War II. This arose from challenges that followed the new developments in international trade and production that necessitated choosing between exporting and FDI. Among others, one usually noted as the founding authorities in this area is Stephen Hymer. His 1960 seminal work that focused on the study of FDI has been cited as the cornerstone of FDI theory as it is articulated today. By way of definition, FDI has been described as “a means of transferring knowledge and other intangible firm assets to organise production abroad; and unlike portfolio investments, such transfers do not relinquish ownership and control” (Sethi et al, 2002).

With time, other scholars felt the need to refine FDI theory (Caves, 1971; Dunning, 1958 & 1980; Teece, 1981; Sethi et al, 2002). For these, FDI was ‘a means of exploiting ownership advantages’ and ‘firms as purely market seeking actors’. This was later extended by the internationalization theories (Casson, 1976; Hosseini, 2005), which highlighted “the need to distinguish between endogenous structural imperfections” ... “associated with ownership advantages and the exogenous transaction cost imperfections” ... “associated with incomplete contracts and bounded rationality” (Grosse, 2005). In this context therefore, deciding to use FDI entails two interdependent decisions on where to locate production and the mode of control. Naturally, FDI entails locating production in a foreign land while controlling administratively. On the other hand, exporting entails producing domestically while controlling administratively. Yet, foreign licensing would entail locating production in a foreign land while controlling contractually.

Other options extend this debate to investment via mergers and acquisitions as opposed to Greenfield ventures and joint ventures versus wholly owned subsidiaries (Buckley and Casson, 1998; Grosse, 2005). The stages model of entry and Upsala school focuses on sequential pattern of entry into successive foreign markets with deepening of commitment to each market, especially in culturally proximate countries with the lowest “psychic distance” (Grosse, 2005). Yet, some perspectives saw FDI as a risky form of diversification of organisational assets and knowledge transfer (Kogut, 1983; Sethi et al., 2002) while others described the bandwagon effect in which MNEs rush investments abroad in response to oligopolistic rivalry (Kogut, 1983; Sethi et al., 2002).

After a critical analysis, Dunning (1980, 1995, & 2000) merged the above theories and came up with what he termed “the eclectic paradigm of FDI”. In this paradigm, Dunning (2000, p. 95), “asserts that international production undertaken by MNEs will be determined by the configuration of three sets of forces: (a) The ownership advantages which come either from a firm’s privileged ownership of, or access to a set of income generating assets, or from their ability to coordinate these assets with other assets across national boundaries in a way that benefits them relative to their competitors; (b) The extent to which firms perceive it to be in their best interest to internalize the markets for the generation and/or the use of these assets; and by so doing, add value to them; and (c) The extent to which firms choose to locate these value adding activities outside their national boundaries, which depends on the locational advantages (market, political, social, economic) of host countries.

Context in this regard is very critical. How such parameters are configured as well as how a specific firm responds to them will be determined by that context. These, among others, reflect the economic and political features of each country, industry and the “raison d’être” for FDI (Meyer et al., 2004). It has been argued that MNEs that choose to engage in FDI are almost always looking for specific and identifiable advantages in the countries they opt to invest in (Dunning, 1994; Jones et al, 2000). Such advantages could include, among others, access to natural resources, both physical and human

(what is termed resource-seeking FDI); market access, both local and adjacent (what is termed market-seeking FDI); and the necessity to achieve product or process rationalization/specialization, both across and/or along the value chain (what is termed efficiency-seeking FDI). To this one could add the acquisition of/or linkage to foreign assets, including technology, organizational efficiency, and many other attributes (what is termed strategic asset-seeking FDI) (Dunning, 1994).

Generally speaking, FDI flows in the 1980s and 1990s, to the large extent, have taken the efficiency or asset-seeking characteristic. As far as FDI flows from DCs to the LDCs are particularly concerned, they have largely been motivated by the search for natural resources and/or market access (Dunning, 1994).

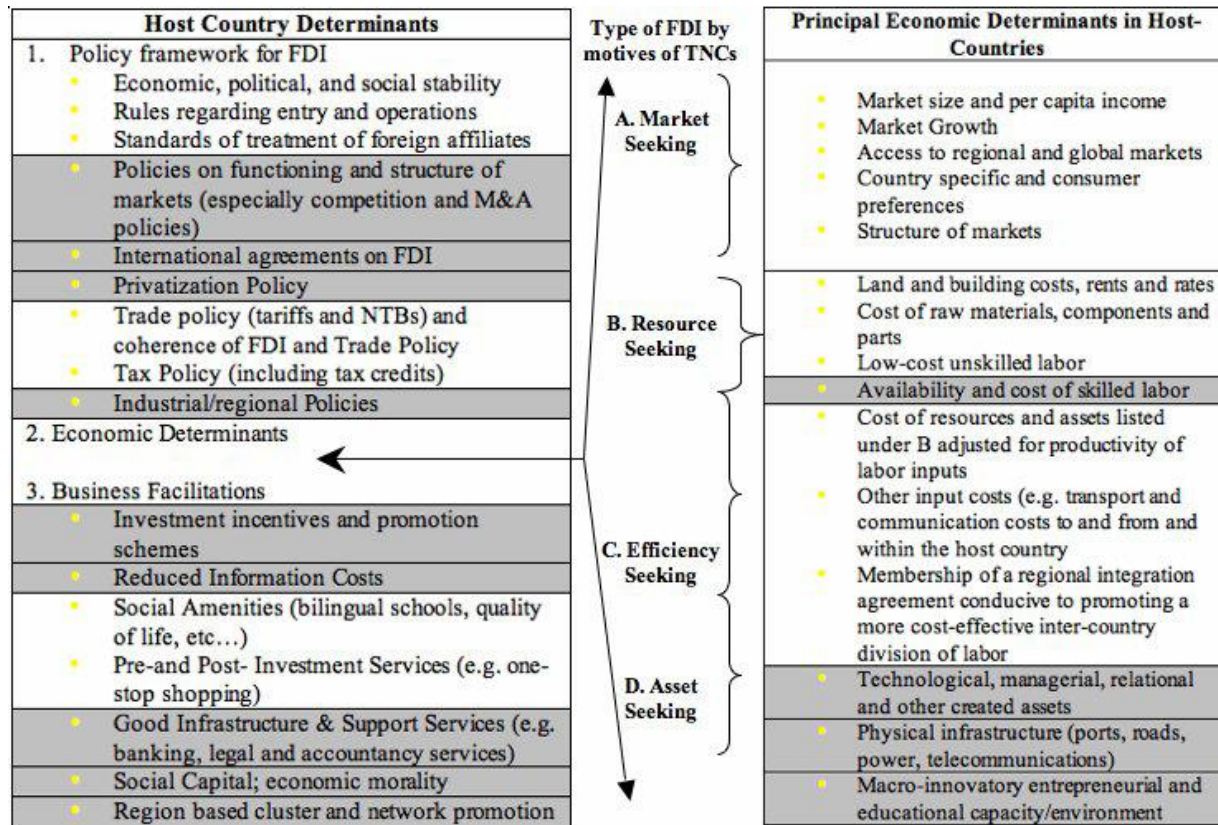
Therefore, the eclectic paradigm could best provide a framework for analyzing the determinants of international production among foreign MNEs (Dunning, 2001). It is also evident that within this paradigm, locational advantages appear to be critical factors entry decisions. They therefore become equally important in informing how governments and other responsible institutions in LDCs, and the options they might have in their efforts to attract MNE FDI.

On the other hand, as opposed to the historical development FDI theory, the institutional perspective to FDI is a recent development. It only came to the fore in the early 1990s. By its core tenets, FDI theory is premised on the notion of institutions as “formal conventions or rules as well as informal conventions or standards of society; and that of individuals and organizations as the entities which devise and implement these institutions” (Grosse, 2005). In this context, institutions are responsible for defining the ‘rules of the game’ that inform all activities and by which they are monitored and enforced. The most common rules include exchange rates, regulations on profit and dividend repatriation, corporate tax, currency devaluation, and tax holidays. Overall therefore, a national state would comprise many different institutions and as far as MNEs are concerned, their object desire is to use these institutions in such a way that they win the game.

Thus, the prevailing host-country institutional structure (the overall environment within which institutions and organizations operate, including regime type, judicial system, economic regime in place, socio-cultural norms, customs, mores and religions, etc) of a particular political economy would provide MNEs with different impetuses for engaging in certain activities in the host-country (Grosse, 2005). An efficient and 'hassle-free' institutional framework would reduce costs of foreignness and other entry liabilities associated with starting from the scratch. It is in this vein that a number of writers have observed that host-country institutions are critical in MNE's decision to enter a foreign country or not, and when they decide to enter, the entry strategy they apply (Hall and Soskice, 2001).

Informed by these realities, Dunning (2005) has developed an analytical framework for host-country institutional infrastructure that would affect the locational decision regarding FDI shown in Figure 1.0. The shaded determinants are those that have become relatively more important in the last decade, due inter alia to technological development, globalization, and the advent of alliance capitalism; and how these in turn, have widened the options open to MNEs in their choice of locations.

Figure 1.0: Host country determinants of FDI

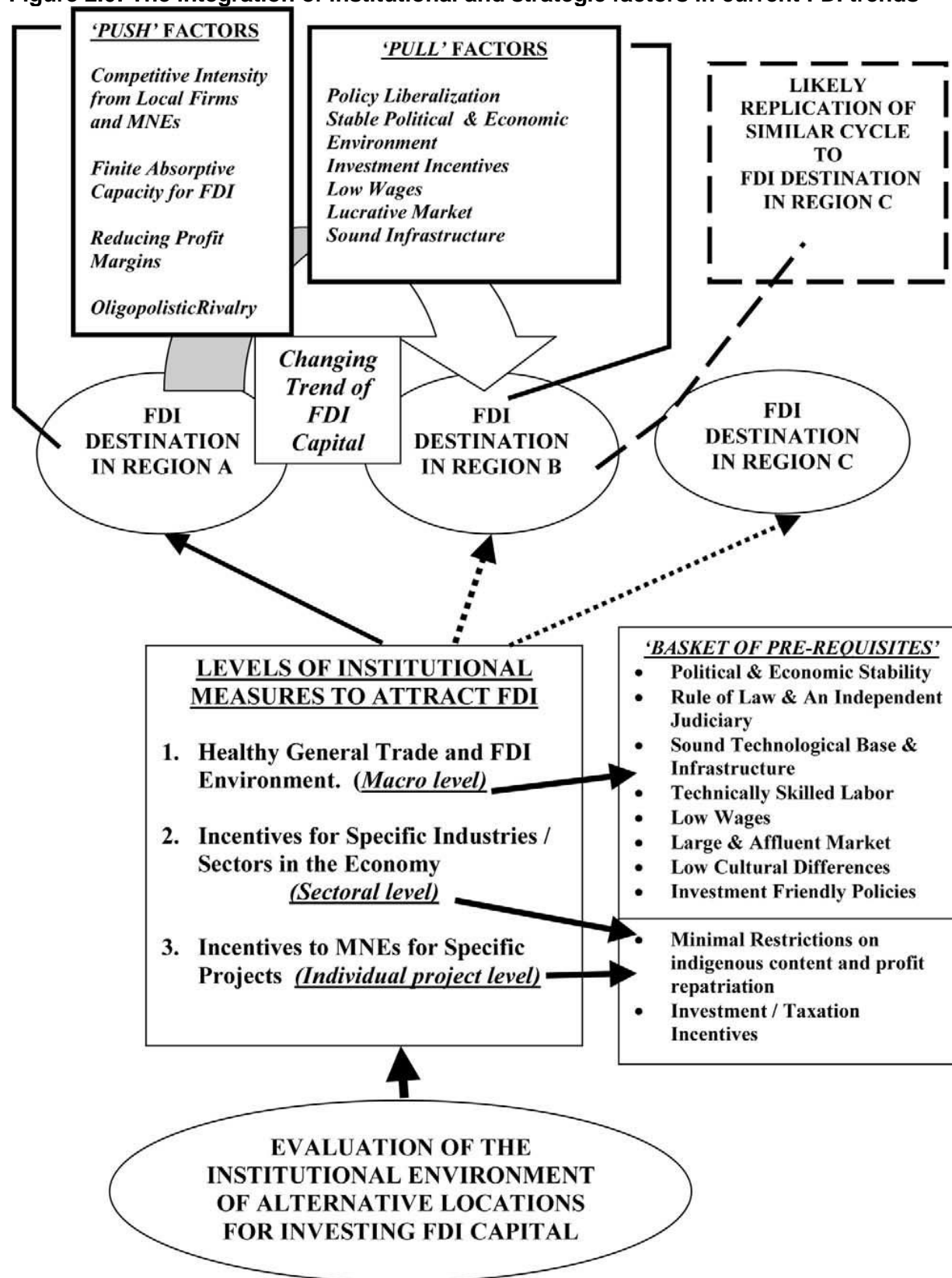


Source: (Grosse 2005)

Another framework that has been developed integrates institutional and strategic factors in explaining current FDI trends (Sethi et al., 2002). These have attributed changes in MNE FDI to what they term push factors within the DCs. Such push factors include “the buildup of competitive intensity, market seeking incentives and oligopolistic rivalry”. In addition, they highlight what they term pull-factors that work from within the LDCs. Among others, these include such occurrences as liberalization tendencies, tradeoff advantages (such as between poor infrastructure and low wages), regional clustering and agglomeration advantages and institutional factors”.

Further, institutional infrastructure could be re-categorized under three broad levels of (1) macro (referring to the overall political and economic environment for trade and investment); (2) sectoral (referring to incentives specifically targeted to attract FDI into specific industries or sectors); and (3) project specific (referring to incentives directly negotiated with individual MNEs). This is illustrated in Figure 2.2 below:

Figure 2.0: The integration of institutional and strategic factors in current FDI trends



Source: Sethi et al (2002)

Among the prerequisites usually highlighted, foremost consideration is given to stable political and economic environments and the overall respect for the rule of law in the host country. Other corresponding requisites may include a benign outlook towards profit repatriation, investment limits, local content, and many such attributes. Overall therefore, a strong and benign institutional infrastructure would enhance the capacity of the host-country to attract FDI. On the other hand, an inefficient and adverse institutional infrastructure might inhibit the flow of FDI into host-country (Grosse, 2005).

In all these aspects, the role of the state in regulating financial and other economic systems; structuring socio-political interest groups; developing the necessary infrastructure; and ensuring the development of relevant skills, imply that each and every country will have a different institutional outlook. When you add the various historical legacies different countries have gone through, the extent of state involvement in economic development; the dominant culture and belief systems; and many other factors are likely to affect the ways in which economic activities are organized (Whitley, 1998).

It is with this background that in the recent past, many LDCs have seen it to be advantageous to implement structural adjustment and liberalization programmes (at both macro and micro levels) in order to transform not only the efficiency with which institutions function but also their overall configuration. This is critical in creating an environment that could attract FDI. In all these efforts, LDCs must avoid what are termed institutional voids. Institutional voids have been described as the absence of specialized intermediation economic entities such as legal rules; trade organizations that are relevant in overcoming market failures due to information problems; and existence of inefficient banking and judicial systems; and many other shortcomings that are rife in most of the emerging markets (Grosse, 2005). Thus, the existence of efficient well-developed host-country institutions and/or institutional voids will engender heterogeneity among markets. Understanding these is therefore helpful in explaining the business climate in host-country economies and also, implicitly the factors that MNEs take into account in forming FDI locational decisions (Khanna and Palepu, 2005).

In sum, government actions do matter for FDI and it is thus imperative to review the work on MNE relations with host governments. Policy decisions such as privatization and liberalization are likely to have lasting effects on institutions and their overall configuration. In the international system, these would be pivotal consideration for foreign MNEs as they make decisions on whether to invest in a country or not.

However, there is also a lot of literature that focuses on alternative strategies which MNEs adopt while avoiding having to get into direct conflict with host-country institutions and policies in LDCs (Khanna et al., 2005). At the same time, it is not always realistic to expect that the overall objectives of MNEs would be consistent with those of the host-country institutions and/or governments. However, as Boddewyn (1998) (in Grosse, 2005) asserts, as political actors, MNEs actively try to influence the political environment within which they operate. It is this that explains why some MNEs have proven successful even in circumstances where mere economic analyses do not sufficiently provide explanations for their success.

Empirical Considerations: FDI Inflows to (Zambia) Africa

According to the United Nations Conference on Trade and Development (UNCTAD)'s 2009 report on world trends in FDI flows, the recent world recession has had significant adverse impacts on FDI flows to Africa generally. Notwithstanding the fact that it is too early to make conclusive analyses on the actual impacts of the global financial crunch, the picture is clear that Africa has been suffering as a result of the global economic recession. Already, trends show that after enjoying uninterrupted growth since 2002, FDI flows to Africa peaked in 2008 when they reached a record high of \$88 billion. As the effects of the financial and economic crisis continue to bite, initial data on a year to year basis show a deep of about 67% in overall inflows of FDI to Africa (UNCTAD, 2009).

It should be noted here that the prospects for FDI in Africa are intimately tied to the overall performance of global markets. Thus, the revival of the global economy is very critical to Africa's own revival vis-à-vis FDI inflows. However, the prospects for recovery remain very high. According to the UNCTAD World Investment Prospects Survey of 2009-2011, transnational corporations the world over are planning an increase in both the number and value of investments in Africa by 2011. Also China has increasingly become an important investor on the continent. The United States and European Union countries also remain crucial sources of capital (MCTIZ, 2009).

It should be noted that on the world stage, the Sub Sahara region has been less successful in attracting productive FDI than other regions. Another aspect that needs to be noted here is that FDI flows to Africa have continued to be highly concentrated in only a few countries. Dominant were a strong growth in flows to West Africa, particularly to such countries as Ghana and Guinea, which saw their annual inflows more than double to well above \$1 billion each. In Southern Africa, the increase in inward FDI was also only concentrated in a very restricted number of countries. For example, increases in FDI flows to the region were almost entirely due to the strong performance of Angola and South Africa. In Central Africa and East Africa, inflows in FDI also exhibited upward trends, though at a much slower pace (MCTIZ, 2009).

While only 29% of privatised companies were acquired by FDI, in value terms, foreign investment dominated the privatisation programme (UNCTAD, 2006). Further, although comprehensive systematic statistical data on FDI inflows by sector, industry or country of origin are scanty, Zambia received an inflow of FDI of up to US\$ 334 million by 2004, US\$ 1.3 billion by 2007 before dipping to US\$ 939 million in 2008 mainly as a result of the global financial crisis (MCTIZ, 2009). In the context of the ZDA, up to 680 enterprises were issued with investment licenses valued at US\$ 12.6 billion, with pledged employment of 66,104 jobs over the period 2004 to 2008. The level of foreign investments increased by over 90 percent from 2004 to 2008 in both value and employment creation terms. The investments have mainly been in mining,

manufacturing, Greenfield, agricultural, construction, tourism, service and financial institutions (MCTIZ, 2009).

In terms of competitiveness ranking¹, Zambia has made a positive move from 122 in 2007 to 112 in 2008, before moving to 99 in 2009 and finally 90 in 2010². Although the overall ranking is still quite bad and offers very little consolation, this is a commendable improvement as it puts the country well on its way to achieving the targeted ranking of 50 by 2014. The result is that FDI flows to Zambia have been much slower than the rest of the region. This is because, even within Southern Africa, there are a number of countries which have a much higher competitive advantage and therefore are able to attract new investment more than Zambia. For instance, by 2008 statistics, South Africa ranked at 45 and Botswana ranked at 66. This is a time when Zambia was on 122 (MCTIZ, 2009). The International Finance Corporation (IFC), a component of the World Bank group, also produces annual international rankings entitled “Doing Business Review”. The 2010 report ranks Zambia as follows (out of 183 countries) (IFC, 2010).

It is therefore not surprising that comparatively speaking, Zambia has been fairing much more poorly as whatever FDI flows come to the region tend to gravitate towards those highly rated countries (MCTIZ, 2009). Given the above scenario, it is clear that the challenge that Zambia is faced with to attract FDI remains formidable, considering that even during the “good times” when FDI into Africa was growing strongly, Zambia did not figure as a major investment location.

¹ Competitiveness ranking is a measure that is examined in detail by potential investors. It is a critical measure of how the country compares vis-à-vis its competitors.

² These rankings are out of a total 134 countries.

CHAPTER THREE

Study Methodology

This section presents the general approach and methodological descriptions that were followed to answer the main research objectives and reach the general conclusions and recommendations for future research and policy implementation. It provides the step-by-step descriptions of the procedures and processes that were followed in this study. Impressionistic as it may be, contextual knowledge has added to the existing body of wisdom and through intelligent presumptions, a number of insights were gleaned from the findings in order to inform future policy and research.

Case study method

The research design that was employed for this case study is the single embedded case study of institutional determinants of FDI. This entails a qualitative in depth case analysis of the host-country institutional influences on FDI in Zambia. The study took multiple perspectives into account and attempted to understand the influence of multilevel host institutions on MNEs and their decisions vis-à-vis their FDI strategies in Zambia.

This approach was informed by a number of theoretical insights from the literature for conducting research on the country-specific institutional determinants of FDI. The shortcomings highlighted in the literature also necessitated the adoption of the institutional approach and the configuration of institutions as the most ideal theoretical lenses for adequately responding to the research objectives in this study. Zambia is a developing country and as indicated in the literature, it exhibits various institutional inadequacies that are bound to affect FDI flows. Thus, an institutional approach becomes a critical lens for analyzing FDI flows into the country. Many FDI strategies and priorities are bound to be guided by the configuration of the institutional infrastructure in the economy. In most cases than not, the configuration of institutional

infrastructure affects both the cost and ease of doing business for MNEs, and this will therefore affect their FDI decisions in developing countries.

The epistemological foundations of this approach therefore lie between survey research and ethnographic imperatives of critical enquiry. Thus, the case involved in-depth study of both primary and secondary data. This facilitated the development of compelling evidence on the configurations of institutions in Zambia and how these institutions contribute towards defining both the nature and quantity of FDI in the country.

Limitations of the Case Study Method

A frequent criticism of case study methodology is that its dependence on a single case renders it incapable of providing a generalizing conclusion. One would therefore consider the case study methodology as "microscopic" because it "lacked a sufficient number" of cases. Moreover, it is in the nature of case studies that a particular research does not need to have a minimum number of respondents, or to randomly "select" those interviewed. As a result, the researcher was called upon to work with the situation that presented itself in this particular case.

The further weakness relates to the lack of control by the researcher. As an ex post facto approach, it was not possible to manipulate the environment within which the study was undertaken. Furthermore, the behavior observable among host-country institutions can only be described, not explained. The small number of participants involved could also make it difficult, or even unreasonable to make generalizations about entire population of LDCs.

Despite these drawbacks however, this study design allowed the gathering of insights in the natural environment. This allowed for a more comprehensive understanding of Zambia's FDI legislation/policy challenges and the role of host-country institutions in attracting or hindering the in-ward flow of FDI by MNEs.

Data collection and Target Groups

Target groups

Target group (a); (That of Key Informants in Government officials): This included officials from all institutions working towards creating an attractive local environment for FDI in Zambia. Among others, these included the Zambia Development Agency (ZDA), Ministry of Commerce and Industry, the Chinese Investment Center, and many others working in this field.

These were selected by purposive sampling method in that those selected had to be representatives of such partners and stakeholders as have been described above. The sample size was determined by the number of partners and/or stakeholders that were identified.

Target group (b); (That of Foreign MNEs in Zambia): This included representatives from foreign MNEs working in Zambia. Being the main stakeholders, their knowledge, experiences, views, and aspirations were critical in establishing evidence on their perceptions of the institutional determinants of FDI in Zambia.

They were also included by purposive sampling method in that they were included by virtue of their positions in those institutions deemed as foreign MNEs working in Zambia.

Data Collection Tools

This was an in-depth study that used both primary and secondary data. Thus, it utilized two main data collection tools, document review and the in-depth one-to-one structured interview.

Document Review: Since a lot of information was already available on MNEs and FDI in Zambia, this information was collected via document review before and during the study. Thus, review of relevant policy and other institutional documents was the first and main step in data collection.

In-depth one-to-one structured interview: Interviewing those people and stakeholders working in and/or with the institutions and MNEs working in this area in Zambia was very critical to the success of this study. Thus, in-depth interviews with key respondent segments were held in order to validate and ascertain the data from document reviews.

The in-depth one-to-one interviews were therefore used to collect information from all Government and related stakeholders, including representatives of the MNEs working in Zambia. One-to-one interviews were ideal for these categories of respondents as they offered room for more intimate in-depth interaction with the major players and thereby allowing for the collection of richer and well thought out information.

Content Analysis

As far as data obtained through in-depth interviews are concerned, transcription commenced immediately after the interviews had been completed. The recorded interviews were listened to several times, and then transcribed verbatim. Notes taken during interviews were used alongside the tapes during transcription.

Being a qualitative study in large part, content analysis was the main approach to analyzing the information. The first step of the analysis involved familiarization with the data. This entailed immersion in the data in order to gain an overview of the depth and diversity of the material and identification of recurring themes and issues. The transcript content was thoroughly studied in order to identify common trends, themes and patterns.

Having identified a number of key themes at the familiarization stage, these were examined in detail with a view to setting up a thematic framework. This involved checking the responses to each question from the respondents in the study and noting down typical responses, and then taking note ensuing themes which should be as mutually exclusive as possible. Responses which appear less frequently were lumped into a category labeled 'other'. This required thorough and careful reading of transcripts in full to ensure that any theme is grounded in the original accounts and observations. While some index categories were identical to the original topic research objectives, it was important to be on the lookout for emergent themes. This went hand-in-hand with reflections on the general meaning, tone and impression of what the participants were saying. Greater weight was given to commonly held perspectives and those individual perspectives that showed greater intensity.

At this point, graphs were created to present and summarize the quantitative aspects of the data while and narrative summaries were created to summarize the qualitative aspects of the study. For this study, frequency counts (or what are called descriptive statistics) are all that were needed in this report.

Ethical Considerations

Ethical approval was obtained from the local Research Ethics Committee (REC) at the University of Zambia in Lusaka, Zambia.

CHAPTER FOUR

Research Findings and Discussion

Zambia's FDI Policy Framework (The continuing process)

This section presents findings on Zambia's FDI legislation/policy challenges and existing institutional frameworks for attracting foreign MNEs into the country. Information presented in this section was obtained mainly from desktop literature review and in-depth interviews with the key stakeholders, including government, professional organizations and investors.

When asked to comment on the overall policy framework for attracting FDI through Multinational Enterprises (MNEs) in Zambia, all research participants noted that there was no policy in place at the time of the interviews (June 2010). It was however acknowledged that through an Act of Parliament, the ZDA Act, the ZDA is provided with the mandate to stage investment promotion activities both in Zambia and abroad. Thus, with regard to specific legislations, the majority positively isolated the ZDA Act as quite explicit on ZDA functions and mandate. However, the Act was overwhelmingly criticized in that it does not give the ZDA the authority and exclusivity in staging investment promotion activities.

Further, while there is no "Policy" per se governing investment and the ZDA Act stands out as the main investment promotion legislation in Zambia, respondents noted that the country has experienced a significant increase in government regulatory legislation on business since the 1990s. It was revealed that there are approximately over 86 Acts of Parliament regulating an aspect of business operation in Zambia in one way or other. The report on business licensing and regulatory reforms in Zambia also lists a total of up to 15 pieces of legislation that are bound to impact on investors and impose demands on them for compliance. This is in addition to the numerous pieces of regulations, rules and by-laws that are used to regulate and control business activities in the country. "This creates an almost impossible situation for potential investors. When

investors come to consult about investing in Zambia, they are faced with such high numbers of pieces of legislation that they would have to “take into account” when deciding to invest in the country. In fact, critically speaking, the number of such pieces of legislation would go beyond the 15 given in the report on business licensing and regulatory reforms in Zambia” (GRZ, 2009). The business sector in Zambia has made representations to government on several occasions regarding the massive number of regulations that they need to comply with that adversely affects their doing business in the country. This is in spite of the fact that the many in the private sector have pointed out that some of these regulations are in fact obsolete.

Further, many stakeholders, especially foreign investors and potential investors have observed that procedures for keeping track of all the regulations and licenses have not kept pace with modern processes, procedures and technological advancements (GRZ, 2009, p. 61). In addition, the private sector has complained over the intractable problems that result from the large volume of inter-related and overlapping legislation, and the compartmentalization of regulatory authorities in the country.

The respondents also highlighted a number of legislations which they thought were negative to investment promotion in the country. Among others, the immigration and deportation Act was repeatedly isolated. “The Act requires potential investors coming to Zambia to show proof of transfer of US \$250,000 into a local bank account before they can be considered for self employment permit. This is a very retrogressive requirement and limits the number of investors willing to come into the country” (MNE Representative, interview, 2010). Another Act that was isolated as negative was the Lands Act. Many respondents noted that “the process of acquiring land in Zambia was very bureaucratic and too open to corruption” (ZDA Representative, interview, 2010).

In addition to the above observations, the business licensing and regulatory framework is not well streamlined and does not clearly identify when an activity or business enterprise needs a license, permit, registration or mere notification. Moreover, there is no clear and distinct criterion or requirements pertaining to each of these categories. In

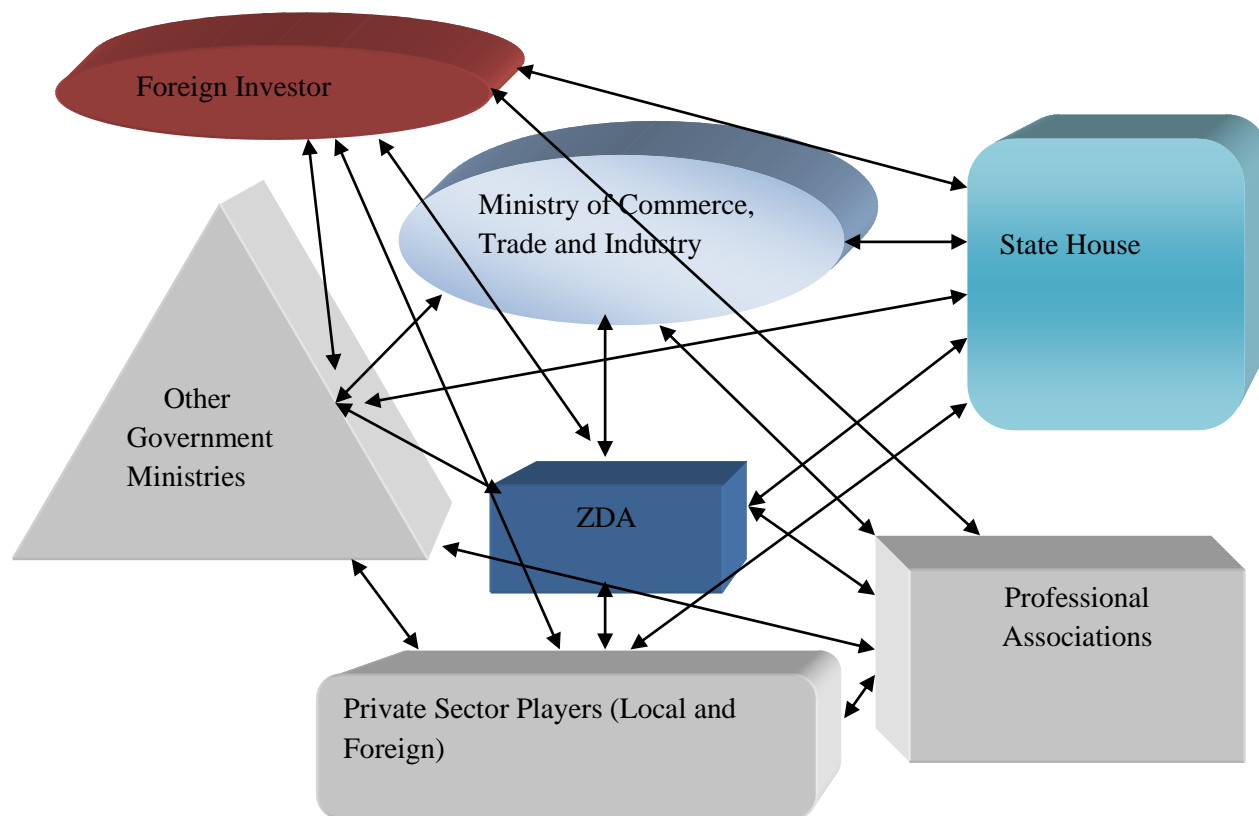
fact, the criteria and requirements for all three categories are almost the same, resulting in the same information being requested by different regulatory authorities within the same public sector. According to the World Bank, the Doing Business in Zambia Report of 2008 reveals that doing business in Zambia is tedious, takes too long to get started, takes ages to receive feedback in the form of decisions regarding issuance of licenses, certificates, permits or other authorizations and clearances and there are numerous bottlenecks to overcome both at the start of operations and during operations (GRZ, 2009). As at 2008, Zambia was ranked 116 out of 178 countries reviewed in the Report.

Regulatory and Institutional Frameworks for FDI in Zambia

When commenting on the overall institutional framework for attracting FDI through multinational enterprises (MNEs) in Zambia, respondents pointed out that there were too many players involved in the investment promotion process. The Central government level is mainly comprised of various ministries which operate either as regulatory authorities and/or strict licensing authorities. These ministries regulate business in line with the allocated portfolio functions as specified in the Government Gazette, which is issued under the Statutory Portfolios and Functions Act (GRZ, 2009).

There are several regulatory authorities that issue to the regulated entities various licenses, permits or registration certificates (GRZ, 2009, p.45). This is very confusing for the investors who do not know where to go for what and who is telling the truth (ZDA, interview, 2010). Furthermore, respondents highlighted that the fact that the ZDA reports to the Ministry of Commerce, Trade and Industry was a very negative institutional arrangement. They noted further that the ZDA deals with other ministries beyond the MCTI and that this creates a lot of confusing reconciling the roles of the various ministries especially that no ministry has the mandate to act over another. The result has been a lot of confusion within the ZDA and among the potential investors.

Figure 3.0: The Mix-up in Roles and Mandates in Investment Promotion Activities



Many key informants felt that the ZDA and any other host-country institutions should play the role of quickening investment facilitation, policy advocacy based on empirical evidence, such as results from the survey on foreign investment and investor perceptions. They added that the manner host-country institutions have been performing in Zambia has been very bad. They noted a number of shortcomings, including low staffing level, low funding, misplaced human resources, no investor targeting and literally no investor tracking. They therefore advised that there was a dare need to improve performance in these and many other area if host-country institutions have to have a positive influence on FDI in-flows to Zambia.

The ZDA as a leading investment promotion institution

The preamble to the Zambia Development Agency Act, the Act that establishes the ZDA, states:

“An Act to foster economic growth and development by promoting trade and investment in Zambia through an efficient, effective and coordinated

private sector-led economic development strategy; to establish the Zambia Development Agency as a one-stop facility which will ensure, among other matters, client focus, dialogue with the private sector and create confidence in public sector support for business; to provide for the functions and powers of the Agency; to attract and facilitate inward and aftercare investments; to provide and facilitate support to micro and small business enterprises; to promote exports and globalisation; to streamline bureaucratic procedures and requirements faced by investors; to facilitate industrial infrastructure development and local services; to promote Greenfield investments through joint ventures and partnerships between local and foreign investors; to promote and encourage education and skills training so as to increase productivity in business enterprises; to encourage measures to increase Zambia's capacity to trade and enable business to participate in a competitive global environment; to ensure that the private sector takes advantage of and benefits from international and regional trade agreements and to provide for matters connected with or incidental to the foregoing”

The Act, in Part II Section 5 (2), goes on to list the functions of the agency. There are 26 functions specified, which elaborate the intentions in the preamble. While one cannot disagree with the majority of these functions, as they are all important in driving Zambia's quest for new investment and overall development forward, they are too diverse and varied. In every respect, this is a formidable set of objectives and functions for any agency, even for those with a large staffing capabilities and adequate financing. Operating within the current constraints, the challenge is an almost impossible mandate for the ZDA to undertake with the current structure (GRZ, 2009).

The ZDA as it is currently structured is the result of an amalgamation of five different agencies that took place in 2005/2006. These agencies were the Export Board of Zambia, Zambia Privatization Agency, Zambia Export Processing Zones Authority, Zambia Investment Centre and the Small Enterprises Development Board. While the

idea of amalgamating these agencies was excellent, the execution was not well handled. The result was that the ZDA was left with a confused and complicated mandate. While the executive staffing level of about 80 members of staff is more than sufficient for the basic tasks of an IPA, it becomes impossible for that kind of staffing to undertake all the varied functions specified in the 2006 ZDA Act. In addition, while the ZDA was established under legislation (the ZDA Act), the legislation is well below best practice and not really any comfort to the agency. It is necessary for an IPA to have a proper and legal basis for its establishment and operation. This is important when it comes to legal matters and the issue of suing and being sued.

Furthermore, to be completely effective, respondents cautioned that the ZDA needed to overcome its major weaknesses. Among others, it was argued that the ZDA should deal with the problem of the lack of a centralized database and information management system. This, it was asserted, was a huge problem for people (both within the ZDA and those outside, including potential investors) looking for investment information on Zambia. Furthermore, the amalgamation of the five formerly independent institutions brought a huge liability burden into the ZDA. Thus, there was need to find a way to deal with these liabilities from the institutions that now comprise the ZDA. Inconsistencies in the ZDA Act were also cited as a serious weakness in the operations of the ZDA as an investment promotion agency.

Additionally, there have been allegations that the ZDA is not free from political influence. This comes out quite clearly from discussions with many private sector stakeholders already operating in Zambia. While there will always be some degree of political interference in the running of an investment promotion agency, it is important that such interference is kept to the minimum. It is important to ensure that decisions regarding incentives and investment decisions are made solely on the basis of merit and entitlement rather than politically motivated. It is unacceptable for an IPA to be influenced by political considerations. Once this happens, the agency loses credibility in the market place and potential investors are reluctant to discuss their plans with the agency for fear of them being disclosed for political gain (GRZ, 2009).

It should also be noted that, while the ZDA does have a Board with a private sector chairman, its composition is not best practice. Over 75% of the members are from the public sector, either from line ministries or other public sector bodies (GRZ, 2009). It is this that raises questions as to the independence of the agency, especially regarding political interference. Most IPAs around the world have boards whose composition includes public sector representatives. However, while it is desirable to have some public sector representatives (from ministries that are important to the agency in fulfilling its mandate) the majority of the board should come from the private sector, particularly the chair person. Having an international consultant from abroad could also bring in an international perspective to the agency.

Another aspect of the ZDA that needs critical consideration is its budget allocation. This is one of the many issues that need to be examined in determining the overall inability of the ZDA to full-fill its mandate. The overall budgetary allocation to the ZDA has been said to be inadequate. The budget that has been allocated to the ZDA puts the organisation at “subsistence level”. In other words, the organization is forced to worry about barely surviving. In the process, it is unable to undertake the main functions expected of an IPA. Its budget is basically a total of the budgets of the agencies that were amalgamated to form the ZDA. Since it was formed, the mandate of the agency has been expanded, but without any budgetary adjustments. Some have even wondered whether it would be questionable to argue that closing the ZDA would be very cost effective unless its budget could be increased to make the organization more effective so as to provide a good return even on the fixed costs.

It is important for an IPA to be free from bias in its dealings with investors. It must be independent of pressures being exerted through funding sources. The Government should be the main source of funding for an IPA. In this way, the IPA becomes responsible to the people through the Government. All countries that have succeeded in attracting large amounts of mobile FDI have world class IPAs with large budgets. For example, during the 1980’s when Ireland was one of the poorest countries in Europe,

the Industrial Development Authority (IDA) Ireland was given an annual budget equal to approximately 15% of the amount of money that the government collected in income tax. This is a reflection of the priority that the government placed on the attraction of FDI (GRZ, 2009).

This may represent a lack of real commitment from political leaders with regard to the importance of the work of the ZDA. This statement barely needs expanding in that the situation speaks for itself. If the politicians were serious about the work of the ZDA, then it would be allocated an adequate budget. It is easy to hide behind the fact that there are only limited resources available and they have to be distributed evenly throughout the ministries. However, there are poorer and much smaller countries than Zambia where governments allocate a far higher budget to their IPAs on the basis that it is money well spent and that the return will justify the expenditure (GRZ, 2009).

Beyond inadequate budgets, there is no clear mandate from the legislation that established it. The Zambia Development Agency Act of 2006 is not up to international best practice. It tries to do too many things and falls short of the mark. It appears to be a “cut and paste” piece of legislation, with passages drawn from other acts. It does not give the ZDA a proper framework within which to operate. In addition, the lack of a National Investment Policy again leaves the ZDA without a structure within which to frame its own strategies.

It becomes even more challenging for the ZDA as it is mandated to provide a wide and diverse range of services to satisfy local business while at the same time work to attract new foreign investment to Zambia. Observers have noted that the mandate and functions of the ZDA are far too wide and diverse. A glance at the list of functions to be performed by the ZDA shows clearly that it is almost impossible to expect a single under-funded organization to fulfil. Among others, the ZDA is mandated to develop entrepreneurship skills; make detailed impact analysis on select sectors of the economy; formulate investment promotion strategies; facilitate investment in Zambia; development of micro and small scale businesses; plan, manage, implement and

control the privatization process; develop multi facility economic zones; and encourage and promote the transfer of appropriate technology. Other functions include encouraging increased private sector investment in education; exploring ways of fostering business linkages; providing marketing support services to business enterprises; and cooperating with other State institutions and private sector in area linked with trade, such as, protection of intellectual property rights (IPRs), standardization and certification, trade and the environment, trade and labour, and consumer policy (GRZ, 2009).

Important as these functions are, this is an impossible mandate for any single organization with the funding and staffing that ZDA has. Ireland provides an excellent comparison. The country has two large agencies, IDA Ireland, with a staffing level of about 300 (focuses on attracting new FDI) and Enterprise Ireland, with a staffing level of about 750 (to promote the development of domestic SME's as well as large companies). In spite of such high staffing levels (and most probably, higher funding), put together these institutions do not handle such a comprehensive list of functions as ZDA (GRZ, 2009).

Further complication arises from the fact that too many other official bodies have been getting involved in the business of the ZDA. There are too many entities involved in the process of attracting new FDI. The problem starts at the top, with State House actively getting involved in running around to different countries to invite new investors in the context of bilateral government to government negotiations. In addition, this is also done through line ministries, which also promote new investment in their respective areas of operation. The situation is chaotic with no clear policy establishing exactly the mandate of all these stakeholders.

These are huge challenges each of which could sink any IPA, let alone having to deal with all five! Zambia should therefore draw lessons from other countries. Examples of some of the most effective countries in the world in the promotion of investment may include, among others, Singapore, Ireland, Mauritius, Malaysia and the Czech Republic

(GRZ, 2009). What these countries have in common is a world class investment promotion agency for the attraction of FDI. Each of these agencies has a clear mandate, operates within clearly defined boundaries and is the only agency mandated to undertake the promotion of FDI. In certain countries, there are two agencies involved with the overall promotion of investment; one for FDI and the other for domestic enterprise development. This is equally good practice depending on the requirements and priorities of the country.

However, what is important in both cases is that they do not have a lot of agencies or ministries involved in investment promotion as is the case in Zambia. Having too many players doing the same thing only confuses potential investors as they find it very difficult and confusing to negotiate their way through such a thicket of agencies and/or ministries. The experience of Ireland makes good best practice that Zambia can follow. In the 1970's, Ireland had two separate agencies promoting the country for new FDI investments - IDA Ireland and Shannon Free Area Development Company (SFADCo), promoting the Shannon Free Trade Zone (GRZ, 2009). Each of these agencies has its own network of overseas offices and undertook their marketing campaigns independently of each other. Two serious consequences were the result; there was massive wastage of resources while at the same time, this led to great confusion in the marketplace, especially in those circumstances when representatives from the two agencies called on the same companies (often within days of each other) selling Ireland a location for new investments.

However, as time went on, Ireland eventually decided that IDA Ireland would be the sole marketing agency for both Ireland in general and Shannon Free Trade Zone. The idea here was that it does not really matter where FDI locates within Ireland as long as it was in Ireland. Thus, there was no need to have a special agency just for the Shannon Free Trade Zone.

This is a good lesson for Zambia where the ZDA, State House, government ministries, all want to play a part in attracting FDI. This has led to institutional confusion, especially

that the roles and responsibilities for each of these in promoting foreign investment are not clearly specified. Interviews with representatives of different agencies and/or ministries revealed that the degree of over-lapping in activities is quite incredible. Commenting on the involvement of government or ministries in attracting FDI in Zambia, one respondent said "... it is mere confusion as each ministry has its own investment promotion strategy which is unknown to the other institutions, particularly the ZDA which has the mandate for the purpose" (MNE Representative, interview, 2010). The respondents noted that the involvement of so many players and the resultant confusion in promotion activities was not necessary. "There should be only one institution (the ZDA) mandated to promote all investment activities in the country. All those resources scattered across the various ministries should be channeled to the ZDA and then, the ZDA should create strategic links with these institutions and create a pool of information from which all stakeholders could tap.

This is even made more complicated in that there is no overarching organ overseeing the allocation of roles and responsibilities. For example, for ministries, their functions and powers are set by the Cabinet while for other state agencies, their functions and powers are set in their enabling legislation. In this scenario, you find that each agency blamed others for trespassing into their domain. Even among government ministries, the confusion is apparent. For example, the Ministry of Commerce, Trade and Industry has its FDI attraction activities; the Ministry of Agriculture has its own; while the Ministry of Mining is also doing the same. Each of these has their own policies and strategies, in most cases implemented without consultation of each other. With confusion among agencies, it is therefore not surprising that most potential investors who come to learn about opportunities of doing business in Zambia end up more confused rather than enlightened.

Discussion

Upon analyzing the data arising from desk-top review of literature and interviews with key stakeholders, two broad categories of determinants are identifiable – the positive and the negative.

Positive institutional environmental attributes of FDI

As far as the positive institutional attributes are concerned, one critical observation made by most MNE representatives interviewed relates to the overall political climate that Zambia is well known for. Many noted that Zambia is mainly considered for FDI because the general investment climate is friendly. They argued that as a country Zambia is very peaceful and that the Zambian government has over the years exhibited strong commitment to the upholding of property rights. Another general attribute that was highly rated as a contribution to the conducive environment for FDI in Zambia is government's commitment to the fight against corruption. As one of the MNE representative acknowledged "the process of granting permits is reasonably smooth and free of major corruption as has been experienced in other countries" (Interview, 2010).

Another positive aspect relates to competition policy and intellectual property protection in the country. Literature and interviews with stakeholders agree to the fact that the Competition Commission, which authorizes all mergers and acquisitions and has a merger threshold of 50% market share, has been working very well to ensure "good balance between competition objectives and concern for policies aimed at promoting FDI" (GRZ, 2009: 38). Stakeholder also noted that the Commission has also been working to ensure that it responds swiftly to any requests for approval and MNEs entering the market do not meet rarely faced artificial entry barriers such as exclusive dealing contracts (Interview, 2010).

Furthermore, some of the key stakeholders applauded the fact that there are no listing obligations and no restrictions on the shareholdings of companies in Zambia. However, the law requires that boards of directors include Zambians to represent local stakeholders. In addition, the government encourages listing on the Lusaka Stock exchange in the context of the Citizens Economic Empowerment (CEE) Act. The CEE Act was designed to promote local participation in economic growth. From the interviews with the key stakeholders, it appears that the majority of MNEs have welcomed this initiative. They argued that this provides them with the opportunity to embed their activities in the local communities. Thus, many of them use philanthropic listings which are in most cases less than 20% of their subsidiaries. It is in this vein that a number of retail, telecommunications and manufacturing MNEs operating in Zambia have off-loaded a proportion of their stakes to demonstrate local ownership and raise funds for expansion purposes (GRZ, 2009, p. 38).

MNEs have also been very satisfied with the removal of restrictions on profit repatriation and foreign exchange. Especially ecstatic are those MNEs that have subsidiaries in Zimbabwe, Malawi, South Africa and other countries which have restrictive laws on foreign exchange and profit repatriation. This is one important aspect that makes Zambia a more attractive destination for FDI in the region. Furthermore, many stakeholders were appreciative of the fact that import regulations and procedures have also been simplified. This is even more critical because of the weak manufacturing base in Zambia, creating the necessity to import most inputs used in most production activities in the country. To this, one could add the fact that the government has given tax free incentives on capital equipment for the first three years of investment for any MNE interested in investing in the country.

The role of intergovernmental relations was also highlighted as a positive one. Many MNEs noted that they have benefited from bilateral arrangements between Zambia and their home countries. For example, Explicit Bilateral Investment Treaties have been signed with Germany and Switzerland with most favoured nation clauses (UNCTAD, 2006). Additionally, the government has been in long standing relationships with Asian

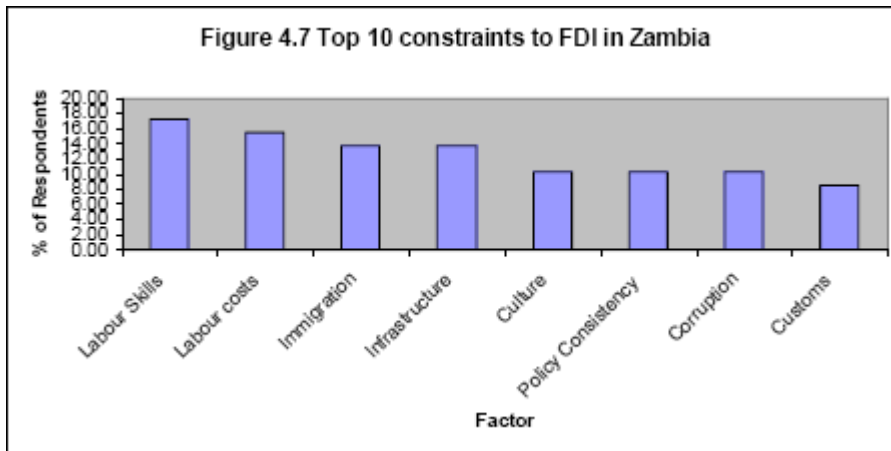
economies such as India and China. MNEs from these countries benefit from higher work permit allocations, and in some cases, the opportunity to bid for contracts involving large scale infrastructural projects.

Further, MNEs have also hailed Zambia's macroeconomic stability since reform as it has enabled more stability in their cash flows and promoted healthy competition. The banking sector has particularly benefited from a balanced budget and sectors heavily reliant on foreign exchange from exports are now able to project with some level of certainty, the profitability of their businesses and thus have found an enabling climate with macroeconomic stability.

The English cultural orientation is another aspect of Zambia that was praiseworthy. A number of MNE representatives were of the opinion that it was easier to choose Zambia as an investment destination because it is English speaking. Despite of the fact that Zambia has over 70 dialects, English runs throughout the country as the official language. This has resulted from the monoculture of being a British colony (GRZ, 2009, p. 40).

Negative institutional environmental attributes of FDI

On the negative side, there are a number of obstacles which MNEs have faced in their pursuit for returns on investments. These obstacles are largely sector specific rather than systemic. The following sections highlight what could be termed the top obstacles to FDI in Zambia.



First among the obstacles noted during key informant interviews were those that arise from the nature of Zambia’s Labor laws (GRZ, 2009, p. 41). It was reported that MNEs in Zambia faced two main problems with labor laws. To start with, there appears to be an abnormally high frequency of industrial action and many of these strikes are not carried out in accordance with the law and collective bargaining agreements. Secondly, severance pay was said to be very high (currently pegged at three months basic pay for each completed year of continuous service). It is this that makes many MNEs to be wary and opt for short-term contracts, which are not conducive for skills transfer.

The second obstacle highlighted concerned immigration laws and procedure for obtaining permits. The conditions for obtaining work permits are very restrictive, and this is very retrogressive for a country like Zambia that does not have qualified personnel in certain critical fields. For instance, sectors that are knowledge-intensive but invest less capital, such as the telecommunications sector, can require extensive foreign expertise to put certain technological and management systems in place. While the immigration department states that it will exercise flexibility in certain cases where the benefits of foreign expertise have been made clear, the procedures do not live up to that claim.

The other obstacle identified during key informant interviews was *Policy consistency* – In March 2008, the Government effected policy changes due to increased copper prices on the world markets. One of the mining multinational had this to say:

In order to encourage increased investments in the mining sector, government of the Republic of Zambia introduced Development Agreements. Such agreements included a provision for negotiation. However, the government u-turned on this and cancelled all the agreements starting 1 April 2008. Mining companies were invited for a meeting by the Republican President who assured the industry that the agreements were legally binding, adding that the copper prices at the time had made it inevitable to re-negotiate the terms. We had no choice but to agree with this. In addition, the Ministry of Finance in the 2008 National Budget put the tax at 47%, which was greater than contained in the Development Agreements. We complained about this as the total taxes, including windfall tax, now amounted to 79-90%. As usual, the government turned a blind eye to our concerns.

Consistency in policy should be cherished to avoid unnecessary revision of initial business plans. In order to win investor confidence, policy must be predictable, which was not the case in the above scenario. For example, in the same period, mineral royalties were increased from 0.6 to 3%. In addition the government reduced capital allowance from 100% to 25%. This led to reduced economic activities as planned expansion projects as well as supply contracts were frustrated. Most businesses directly depending on the mines were severely affected.

Apart from the mining sector, the telecommunications sector has found inconsistent policies between central and local government in terms of council taxes and levies. MTN director expressed exasperation at the charges in terms of local authority taxes and levies are another classical example of policy inconsistency. A telecommunications company (MTN) director narrated:

“When the company wishes to set up transmitters the communications authority asks as to pay 5% of gross revenues and this is besides license fees required for setting up of rural development projects for universal service provision and we are also charged development fees by the council”. “In addition, we are slapped service charges, inspection and transmission fees and pole levies.”

The implication of the above is increased cost of doing business in the country which has potential to further erode the country as a preferred investment destination. Thus, as has been highlighted in the recommendation chapter of this paper, these are some of the challenges that Zambia as a country needs to overcome if it is to be an attractive destination for MNEs willing to invest via FDI.

CHAPTER FIVE

Conclusions and Recommendations

Conclusions

In concluding this paper, a number of issues must be highlighted. To start with, it is clear from past efforts that, although some may label it superficial, the Government has demonstrated reasonable commitment to ensuring that the business climate is favourable to FDI. It was in this context that in 2007, the Government passed the ZDA Act to amalgamate the Zambia Privatization Agency, Zambia Investment Centre, Export Board of Zambia, Zambia Export Processing Zones Authority and the Small Enterprises Development Board was done to form the Zambia Development Agency (ZDA). The objective of amalgamating these bodies was to streamline the processes for investing in Zambia and thus provide for an enabling environment for investment and doing business.

Further, in spite past efforts and regardless of whether they can be termed successful or not, Zambia's efforts, both at policy and host-country institutional levels, remain an on-going endeavour. A number of serious challenges still remain unresolved and if Zambia is to become an attractive destination for FDI, both government and the ZDA must undergo serious structural reforms as prescribed in the recommendations. The Government has to be aware that growth rates of over 10 percent have to be attained if the Vision of becoming a prosperous middle income nation by 2030 is to be realized. This will entail major changes in policy, legislation and the institutional framework governing public service delivery, and facilitation of the operation of the private sector (both local and foreign), and review of the business licensing and regulatory framework which currently inhibits the growth of the formal business sector.

What this paper has also shown is that Zambia does not have an investment policy in place yet. Although the process of developing one is underway, it is erratic and dragging. As a result, the fragmented and sometimes even contradictory legislation and

the institutions they engender have to confuse the investment environment in the country.

Furthermore, and may be as a consequence of the above, host-country institutions, including the ZDA, have not been performing in the manner that would make Zambia the deserving destination for FDI. The current institutional framework does not clearly specify roles and mandates overlap, at times even contradicting. Most host-country institutions lack adequate funding and staffing levels fall short of the required numbers as per their mandates. The issue of lack of consistency in policy formulation and implementation has just made it even more difficult for these institutions to perform effectively, let alone efficiently. Changes in policy are frequent and unpredictable, with, in most cases no apparent logic for the change beyond politics. This is a major impediment to investment as investors are frightened by a volatile policy regime. This is an issue that is well documented as a commonly recurring complaint, and applies to all aspects of doing business in the country. Anecdotal evidence refers to over 500 different types of legislative procedures, licenses, approvals, certificates, etc. that can apply in one form or another to a company seeking to invest in Zambia (GRZ, 2009). Even if such a figure was way out by 100%, it still represents a formidable barrier to enterprise and FDI promotion (GRZ, 2009).

There is currently a process underway to amend the Zambia Development Agency Act, 2006. While this appears to be a logical development looking at the shortcomings apparent in the Act, it also appears to be an unnecessary waste of resources and time since Zambia is at the same time in the process of developing the investment policy. Thus, rather than have parallel activities with the same ultimate objective, it is important to suspend the work done on the ZDA Act and incorporate them into the submissions as part of the process to develop the investment policy. It does not make sense to pass amendments to the Act, when the investment policy may advocate something different, which may require entirely new legislation.

Moreover, the ZDA Act has been criticized by many investors that it does not offer sufficient protection for their investment. Some have expressed concern that Zambia could follow the pattern set by Zimbabwe, which would have disastrous consequences for the country. In addition, some pronouncements from the CEEC have raised more concern as some investors fear that the push for “citizen’s empowerment” could lead to some form of nationalization (GRZ, 2009). While these perceptions may not represent the absolute truth, they are perceptions that could affect Zambia’s attractiveness and therefore need to be addressed with the seriousness they deserve. This is even more critical as the indicators of the IFC Doing Business Review of 2010 shows that under the heading “protecting investors”, Zambia recorded a drop in rating.

Recommendations

Zambia’s investment vision reads – “Making Zambia a middle income country by 2030”. While this is a very laudable vision, and one that can be achieved, it is a huge challenge and requires bold and fundamental decisions at the highest level. It is clear that every other country in the world is working to improve its economic outlook in order to attract more FDI. Unfortunately for Zambia, many of these countries are experiencing economic growth at rates that are far superior to those obtaining in Zambia. Thus, for Zambia to achieve its vision of becoming a middle income country by 2030, it will need to do better than a number of countries which currently have a higher GDP in order to overtake them by 2030.

There are a number of critical steps that Zambia as a country needs to take in order to ensure that the investment environment in the country is greatly improved. They are all inter-related and it is no use just picking one or two of them, they all have to be implemented as a package. To start with, there is need to harmonise the various laws that border on investment and make sure that the process of developing the National Investment Policy is hastened and completed soon rather than later. In this regard, nothing short of a complete re-vamp of the legislation and regulatory procedures surrounding the investment process will lead to an improvement. This is clearly the best

course of action. However, when one examines the number of laws involved, it is clear that it will be a difficult call to achieve. This will therefore require strong political will on the part of government (GRZ, 2009).

The problem can be solved through the following:

In the short-term, the One-Stop-Shop function of the ZDA should be fully established so that it can undertake all the necessary bureaucratic functions on behalf of investors. In addition, the Ministry of Commerce, Trade and Industry and other ministries should leave the promotion of investment to the ZDA and concentrate on their core activity of policy development. They should not get involved in the functions of an executive agency. This, however, does not mean that they could hold occasional promotional activities whenever it is necessary, especially with regard to the creation of an overarching framework within which the ZDA should operate effectively. For example, in situations where it is necessary to establish government-to-government arrangements as facilitation for new flows of investment, the Ministry of Commerce, Trade and Industry and other ministries could play a strategic role.

In the longer term therefore, Zambia needs a National Investment Policy. This is the only sure and effective way to harmonise the various laws that border on investment. This will also assist in reducing the cost of doing business and make the Zambia competitive and attractive as a desirable investment destination.

Developing a national investment policy is not a simple task that can be done on the basis of crude research and discussion among the few stakeholders in Lusaka only. There are many issues that will have to be addressed in the policy document. Therefore, serious consultations are critical with all stakeholders both local and foreign, and public and private in order to identify all the critical issues and key areas to concentrate on. Therefore, those to be tasked with this mammoth venture, particularly the Ministry of Commerce, Trade and Industry, need to understand the depth of the task and the financial implications this could come with. It would also be important to agree

on the composition of a Steering Committee and all other sub-committees that will oversee the preparation of the policy document. The Steering Committee and all other sub-committees should be predominately composed of private sector representatives. The time-line for this process will also be critical to consider upfront.

In developing this policy, there are a number of overarching principles that must be adopted. To start with, the formulation of the policy should be driven from within the Ministry of Commerce, Trade and Industry. This should be done using mostly local expertise so that the staff of the Ministry can learn from the process and are able to use the experience in the future development of other policy documents. In the long run, this will help reduce on the cost of consulting 'experts' from abroad. Furthermore, the approach to the new policy should be even-handed so that support to the development of domestic enterprise is not overlooked in favour of attracting new foreign investments (FDI) into the country. This is very important as both will play important roles in the future development of the country.

Incidental to the above process is the need to develop new appropriate legislation to give effect to the investment policy. The new National Investment Policy will be of little effect without accompanying new legislation to facilitate its operationalization. This may entail combining the processes of harmonizing laws that affect investment in Zambia with a complete re-writing of the Zambia Development Agency Act No. 11 of 2006 so that the new policy is more user-friendly and effective. The new legislation must be drafted in line with international best practice and this should simultaneously be accompanied by extensive amendments to the various pieces of legislation which impact on investment.

In addition to the above, the ZDA itself would need extensive surgery and restructuring so that it becomes more effective and efficient in its functions. It may also be prudent to split up the ZDA into two organizations, one dealing with domestic enterprise development and the other focusing on attracting new foreign investments. The ZDA must re-position itself as a professional organization of world-class standard with the

emphasis on investment promotion, investor facilitation and customer service. The central features of the new ZDA should be the separation of the elements that are essential for successful investment promotion from those that are not essential.

The mission of the ZDA, in relation to the development of domestic industry needs to be examined and then measurable goals leading to the achievement of this mission need to be developed. These goals need to be agreed upon with the private sector, as it is the private sector that will ultimately deliver on these goals. This can be achieved within the process of developing the Investment Policy discussed earlier. The government needs to be reminded, on a continuous basis, that it is people and companies that create wealth and jobs, not governments (GRZ, 2009). The job of government should be to facilitate entrepreneurs and companies. Changes must be put in place in Zambia that encourage and assist the creation of new companies, both by local and foreign entrepreneurs. With regard to the selection of priority sectors for promotion, the government should exercise caution as it may lead to punitive exclusion of some sectors which could themselves be potential driver sectors.

The current structure has an over reliance on “back office” staff that represents about 45% of the executive staffing level. This leaves about 55% as “front of house” staff. This needs to be revisited so that about 70% of the executive staff can interact with promoters and investors. This can be facilitated as part of a re-structuring following the development of the new legislation. Furthermore, there is need for an intensive program of development for all staff. This should include international “best-practice” seminars as well as instructive, interactive training programs such as effective boardroom presentations, maximizing use of international contacts and trade fairs and providing world class customer service. Extensive team building training should also be included.

Ultimately, the new ZDA must be adequately empowered both in terms of budgetary allocation and autonomy in order to perform its functions effectively and efficiently. It is not possible to determine from the outset what the ultimate structure for the new ZDA or agencies empowered to promote investment will be. However, one thing is critical and

that is the necessity for an adequate budget and autonomy to get on with the job and not have the stage crowded by a host of other players confusing the investment environment. Allocating adequate resources is the only sure way to enable the ZDA to perform its functions to international best practice standards. This is an area where Zambia falls behind the competition and thus requires urgent attention.

Another area that needs urgent attention is that of allocating clearly defined and demarcated roles and responsibilities to the various players involved in investment promotion in Zambia. For sure, State House – through the President, has the desire to attract as much FDI as possible. Likewise, the various ministries would want to attract as much FDI in their own sectors. However, they cannot be allowed to continue operating as things are currently. There is need to ensure that each ministry and State agency has a clear view of its own functions and responsibilities. These should be clearly defined in the new investment policy and accompanying amendments to existing legislation recommended in this paper. In addition, all such activities must be undertaken in collaboration with and within the framework of the new ZDA. Even where it becomes necessary for ministries to come in, may be because there is need for government-to-government negotiations, these activities must be embedded in the context of the ZDA. In areas of strategic national importance such as the mining sector, the line ministry with responsibility for the sector should conduct the negotiations with the promoters within the ZDA on setting up new companies in the country. Thus, the best ministries could do is to ensure that they develop an excellent overarching policy framework within which the ZDA can operate effectively. On the other hand, the ZDA should create strategic links with other stakeholders involved in attracting FDI such as State House, Government Ministries and departments, Zambia Revenue Authority, and other professional bodies and only co-opt such stakeholders in investment promotion activities as and when it is appropriate.

Finally, beyond tidying up the bureaucratic mess caused by conflicting legislation and public sector procedures, the new National Investment Policy must make sure that the provision of strategic infrastructure is streamlined. The new investment policy should

pull together the strategic plans of all the infrastructure providers in the country to ensure that they are all aiming for the same strategic goals. This will lead to greater efficiencies within and across sectors. This is one of the many aspects that Zambia must resolve if the country is to shift upwards in international ranking for FDI destinations.

What has been suggested as recommendation in this paper are not completely new. Most of these processes have been under discussion as early as 2008. The initial starting point for the process of developing a National Investment Policy was initially pegged for January 2009, with an anticipated completion date tentatively scheduled for the end of 2009. Further, this process was discussed and approved by the Ministry of Commerce, Trade and Industry, and some donors, including the World Bank and the EU have offered to assist should there be need (GRZ, 2009). Unfortunately, Zambia is still dragging its feet and not much has been achieved towards finalizing the new National Investment Policy document.

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Apendix 1: List of Meetings

(Names listed in the order of meeting)

Ministry of Finance and National Planning

Zambia Revenue Authority

Ministry of Commerce, Trade and Industry

Ministry of Energy and Water Development

Ministry of Local Government and Housing

Ministry of Agriculture and Cooperatives

Ministry of Mines and Minerals

The Citizens Economic Empowerment Commission

Ministry of Tourism and Natural Resources

The Tourism Council

Policy Analysis Coordination Group

The Irish Embassy, Lusaka

Ministry of Labour and Social Security

Zambia Development Agency

Ministry of Lands

Zambia Association of Chambers of Commerce and Industry

Zambia Association of Manufacturers

EU Capacity Building for PSD Project

GTZ (German Technical Assistance In Zambia)

The World Bank

Appendix 2: Interview Guide for Key Informants

STUDY TITLE: THE INFLUENCE OF HOST-COUNTRY INSTITUTIONS ON MULTINATIONAL ENTERPRISE (MNE) INVESTMENT IN THE LEAST DEVELOPED COUNTRIES: THE CASE OF ZAMBIA

Salutations and Introduction

My name is Roy Kapembwa. I am a student of the Master of Science Degree at Edinburgh Napier University. In partial fulfillment of the requirements for the award of this degree, we are required to produce a dissertation based on both secondary and primary data. I am undertaking a study on the influence of host-country institutions on MNE investment in Developing countries. You have therefore been purposively included for the interview by virtue of your position in your institution, which is a key stakeholder in FDI investment in Zambia. The information being collected is strictly for academic purposes and everything you share will be treated with utmost confidentiality.

I thank you in anticipation of your cooperation.

1. Would you comment on the overall policy framework for attracting FDI through Multinational Enterprises (MNEs) in Zambia?
2. Would you comment on the overall institutional framework for attracting FDI through Multinational Enterprises (MNEs) in Zambia?
3. What specific policies/legislations would you isolate as positive?
4. What specific policies/legislations would you isolate as negative?
5. What specific institutional arrangements would you isolate as positive?
6. What specific institutional arrangements would you isolate as negative?
7. What would you say should be the role of host-country institutions in influencing MNEs' decision to invest in Zambia via FDI?
8. What is your opinion on the manner host-country institutions have been performing in Zambia?
9. Focusing on the ZDA, what would you say have been its strengths?
10. What would you say have been the ZDA's greatest weaknesses?
11. How would you interpret the involvement of government/ministries in attracting FDI in Zambia?
12. How should these stakeholders interact?
13. How would the overall policy framework for attracting FDI be improved in Zambia?
14. How would the overall institutional framework for attracting FDI be improved in Zambia?
15. In your considered opinion, what should be the role of host-country institutions, particularly the ZDA in attracting FDI to Zambia?
16. How should the ZDA interact with other stakeholders involved in attracting FDI such as State House, Government Ministries, other professional bodies, etc.?
17. Overall, what would you want to add that you feel is important in Zambia's efforts to improve its attractiveness to FDI?

APPRECIATION AND CLOSE OF INTERVIEW