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FOREIGN INVESTMENT

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FOREGIN DIRECT INVESTMENT

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List of Acronyms

CEE= Central and East Europe

FDI= Foreign Direct Investment

FIAS= Foreign Investment Advisory Service

GDI= Gross Domestic Investment

GDP= Gross Domestic Product

IMF= International Monetary Fund

LDCs= Least Developing Countries

MNCs= Multi National Corporations

OECD= Organization for Economic Cooperation Development

SSA= Sub-Saharan Africa

UNCTAD= United Nations Conference on Trade and Development

WB= World Bank

FOREIGN INVESTMENT

1. Introduction

1.1. Definition

The term Investment, according to the Dictionary of Random House Compact Unabridged, denotes “*the expenditure of money or capital in order to gain profitable returns, as interest, income, or appreciation in value*”. Similarly, according to the Federal Negaritte Gazette proclamation No. 280/2002 part 1, sub article 2, *Investment* means expenditure of capital by an investor to establish a new enterprise or to expand or upgrade one that already exists. *Investment*, be it a domestic one, or FDI, is meant to transform the social wellbeing of a country, to help the country in self-reliance, to induce and to promote the economic activity of the state and the like. The role that *Investment* plays is so decisive that it has a big role in bringing the desired economic development to countries.

Apparently, there are three kinds of investment: Private investment, public investment, and Foreign Direct Investment (FDI). However, the split between public and private investment is more problematic (Hadjimichale, 1995). Private Investment is indogenous and it is the critical component of Investment, since it determines the nation’s competitive position (Khan & Kumar, 1997). A well-managed private Investment enhances the competitiveness of companies and contributes to a rapid rate of economic growth (Regional Development Policy & data, 1999). The second type of Investment, public Investment, the sum of investment by general government and by state enterprises, is normally the response of Governments (Development Research Group, 2001). Governments spend in areas that are not/ may not be addressed by the private sector because of their less return on Investment. These areas like rural electrification, basic telecommunication services and so on. Some authors are of the opinion that public

investment has a higher coefficient in a cross-country growth regression of many African countries (Hadjimichale, 1995).

Foreign Direct Investment FDI, on the other hand, is a response to fill the gap that has been created due to failure of domestic savings/capital and it also helps fuel growth of a domestic economy by providing new way of doing things, new technology, and machinery (FIAS, 2000). FDI provides more than a finance flow. It can provide an operational link between an enterprise and a foreign partner. A foreign partner that has investment expertise, technology, or market access not available in the host economy can raise the productivity of the enterprise. It has a larger impact than domestic investment (International Finance Corporation, 1997). However, there are prerequisites that countries should do in order to attract FDI and be able *to be seen on the radar screen of FDI*. These are appropriate policy changes, trade liberalization, and other “political “ activities to be done.

Over the last two decades, more and more developing countries have changed their attitude on FDI. Instead of fearing, limiting or even banning FDI, these countries have not only permitted it but indeed are competing to attract it. Beginning with the collapse of the Berlin Wall, many countries have feared that the opening of central and Eastern European countries, including the former Soviet Union, might make these areas irresistibly attractive to direct investment, and thus divert FDI that might otherwise have gone to the less developed countries. The developing countries around the Mediterranean rim, and particularly those of North Africa, have felt most threatened by any such potential shift that MNCs might make their investment strategies. Countries in SSA have similarly been fearful- even if most of them were not attracting very much FDI even before the collapse of the socialist camp. The relative closeness of the Mediterranean rim countries to Central and Eastern Europe is not the only reason for this fear- Western European firms have been by far the main source of their inward direct investment, and these are the very firms that would be the first to succumb to the large markets and skilled labor of members of the now defunct socialist camp.

1.2. Distribution and Trends in FDI

Cumulative FDI- inward stocks-in LDCs was nine times greater than in 1997 (\$ 1,044 billion) than in 1980 (\$108 billion). Annual FDI inflows-in current value- have been an upward trend in LDCs as a whole during the second half of the 1990s, rising from \$ 1.4 billion in 1995 to \$2.9 billion in 1998. Behind this apparently favorable general picture, however, a close examination of the evidence indicates considerable disparities between regions and between individual LDCs.

Between 1980 and 1997, a significant geographical redistribution of FDI took place among LDCs at both the interregional and intra regional levels. In 1997, African LDCs still received the highest proportion of total FDI stocks of all least developed countries, but this proportion was significantly lower than in 1980 (65 percent vs. 85 percent). Yet, the share of African LDCs in total in Africa increased by five percentage points to 17 percent over the same period. Meanwhile, the share of Asian LDCs in overall FDI stocks in LDCs grew from 8 percent to 31 percent, although on average, the share of Asian LDCs in total FDI stocks in Asia remained under 1 percent. The share of the five Pacific island LDCs in total FDI stocks for all LDCs hovered at around 3 percent throughout this period. In 1997, the Pacific island LDCs boasted the highest FDI per capita-\$57- compared for African LDCs and \$22 for Asian LDCs.

LDCs as a group have recorded higher levels of domestic investment during the 1990s than during the 1980s. During the second half of the 1990s, some improvement in investment has been achieved compared with the first half of the decade. The average annual gross domestic investment (GDI) as a percentage of GDP rose from 22.6 percent for the period 1990-94 to 24.4 percent in 1996. It fell slightly the following year, to 23.3 percent. The most plausible explanation for that drop is the Asian financial crisis. However, at less than 25 percent, which is the average for developing countries as a

whole, the average GDI to GDP ratio for LDCs is rather modest. It means that, as a whole, these countries continue to experience very low levels of capitalization, which can only perpetuate their least developed status. With such low levels of investment, LDCs are not investing enough even to meet replacement needs of the capital stock, let alone to create a new productive capacity.

1.2.1.African LDCs

Although African countries have been relatively disadvantaged as far as FDI to developing countries is concerned, a positive trend has become evident during the 1990s. Among African nations, the share of LDCs in total FDI stocks rose by 5 percentage points between 1980 and 1997. In terms of yearly FDI inflows, African LDCs accounted for a greater proportion of total FDI in Africa in 1997 than in 1980 (22 percent vs. 11 percent). Much of the increase in FDI took place during the 1990s, and is attributed mostly to Angola, Equatorial Guinea, Mozambique, United Republic of Tanzania, Uganda, and Zambia. In 1997, the six accounted for about 12 percent of total FDI stocks in Africa (a huge increase, from less than 1 percent in 1980) and 55 percent of total FDI stocks in the 33 African LDCs. Equatorial Guinea, Mozambique and Uganda are among the seven African countries that have been classified as front –runners in attracting FDI in the 1990s (UNCTAD, 1998).

The substantial FDI inflows to the above-mentioned and a few other African LDCs, notably Malawi and Madagascar, have been attributed to market- oriented reforms (trade liberalization, privatization, enhancement of the legal framework) and to efforts by the countries in question to promote new investment opportunities, mostly in the primary sector. Uganda, which is among the countries that signed international agreements governing investment protection, received an award in the United Kingdom for the best African investment promotion agency in 1997. Mozambique was ranked as the second most important recipient of FDI among African LDCs in 1998. The areas that have

proved most attractive to FDI in Mozambique are mining, tourism and energy. The oil sector is the major attraction to FDI in both Angola and Equatorial Guinea.

Several African LDCs have experienced dis-investment at one time or another since the early 1980s. The worst affected include Central African Republic, Democratic Republic of Congo, Niger, Sierra Leone, and Somalia. The recent trend seems encouraging because the number of African LDCs so affected has fallen from 16 in 1983-87 to 12 in 1988-92 and six in 1993-97. Dis-investment in African LDCs amounted to \$292 million during 1993-97, compared with \$ 582 million in 1983-87. The drop in both divested amounts and number of affected countries signifies, at least in part, an improvement in the investors' perception of business conditions and prospects in African LDCs.

Among the developing and transition economies, the volume of FDI flows more than doubled, increasing from US\$ 89 billion in 1994 to US\$ 183 billion in 1999 (with annual inflows averaging US\$ 154 billion during the period 1995-1999). However, these flows have been concentrated in East Asia and Latin America (approximately 77 percent in 1998).

Flows to Sub-Saharan Africa (including South Africa and excluding Egypt) more than quadrupled to approximately US\$ 5 billion in 1998 (from US\$ 1 billion in 1990), with average annual inflows increasing from US\$ 1.7 billion (1990-1993) to US\$ 5.0 billion (1994-1998). However, since the growth rate of FDI flows to the region was lower than that of global FDI flows, the percent share of FDI flows to the region actually declined from a high of 4.2 percent in 1995 to 2.6 percent in 1998.

FDI as a percentage of GNP in SSA increased threefold (1990-1998) to a level higher than that of Middle East and North Africa and Southern Asia. Pigato and other researchers have attributed the improved performance of SSA in attracting FDI flows to overall policy improvements, macroeconomic reform, the efforts of to create more business- friendly environments, as well as the successful privatization in the

telecommunications and mining sectors (e.g. South Africa, Ghana, Nigeria, Zambia, and Cote d'Ivoire). However, with exception of South Africa and a few other countries in the region (Angola, Mozambique, and Botswana), a significant portion of FDI flows went to countries rich in natural resources but with some of the worst policy and financial risk ratings in the region (e.g. the Congo Republic, Equatorial Guinea, and Nigeria). According to Pigato, the significant exception is South Africa where approximately 40 percent of FDI inflows (1994-1997) have gone to the manufacturing sector.

In 1998, the major sources of FDI flows to SSA were the United States (US\$ 7.6 billion in 1994-1998), France and the United Kingdom. Among the other OECD countries, FDI flows to Africa have increased for Canada, Italy, the Netherlands, Norway, Portugal and Spain. According to OECD statistics, FDI flows from these countries to SSA increased –percent (1994-1998 compared to 1990-94). Also, consistent with a trend started during the 1980s, FDI flows from Asia (e.g. Malaysia and South Korea) increased, despite the slowdown during the Asian economic crisis. Intra-African FDI is also increasing as South African, Egyptian, Moroccan and Zambian firms have sought investment opportunities in other countries.

Clearly SSA continues to face significant challenges in its efforts to increase the volume and quality of FDI and thereby upgrade the productive and export structures of their economies. Even the countries that have initiated significant reform programs continue to attract the greater portion of FDI inflows to the primary sector and infrastructure

Ethiopia had low FDI per head while Singapore has \$2,424 in 1998 and \$ 3,147 in 1996. Indonesia and Korea are also major recipients of FDI.

Ethiopia's share was \$ 12 million in 1980 and \$5 million in 1996. The main problems associated with FDI were: potential for widespread foreign ownership of industry, with implications of foreign dominance, potential involvement of large foreign companies in politics. These problems are difficult to quantify, being subjective and

emotional issues, but they are still important. It is confined to certain sectors. No foreign investment is permitted in the financial sector in Ethiopia.

1.2.2.Asian LDCs

The share of Asian LDCs in FDI stocks fro all LDCs increased progressively from 8 percent in 1980 to 31 percent in 1997. This dramatic rise is a function of the surge in intraregional investments, the main sources of which have been China, Republic of Korea, Malaysia, Singapore, and Thailand.

In Bangladesh, FDI from Asian developing countries accounted for 83 percent of FDI stocks between 1990 and 1994. The corresponding figure for Myanmar was 39 percent during the same period. A total of 204 foreign investment projects were approved in Myanmar between October 1988 and September 1996, with Singapore as the main source of FDI, followed by the United Kingdom, France and Malaysia. Between august 1994 and March 1996, more than half of all FDI in Cambodia came from Malaysia and Singapore. Thus, the “flying geese” model of development, observable in the newly industrializing economies of the region, has benefited many neighboring Asian LDCs by stimulating DDI in low –cost, labor –intensive activities in which these countries have a comparative advantage.

The financial crisis that hit several East and South- East Asian economies in July 1997 exposed the vulnerability of Asian LDCs’ dependence on intraregional investments. FDI flows to Asian LDCs in 1996-97 grew by barely 10 percent, compared with 42 percent in 1995-96 and 53 percent in 1994-95. In Cambodia, which relies mainly on investments from China, Malaysia, Singapore and Thailand, FDI was scaled back by 63 percent during the first half of 1998 (ESCAP at el. 1999). In Lao People’s Democratic Republic, `where foreign investments come principally from Thailand, Republic of Korea, and the United States, FDI fell from \$ 128 million in 1996 to \$ 86 million in 1997

and \$ 45 million in 1998. The Asian crisis also led to a precipitous decline in Bangladesh's foreign portfolio investment in 1997.

The widening gap in FDI flows between Asian LDCs on the one hand, and African LDCs on the other, reflects the decisive role of intraregional investment in Asia, especially since the beginning of the 1990s. Despite efforts at regional integration in Africa, intraregional investment in that continent's LDCs plays only a peripheral role. Owing to historic ties, those countries have relied mainly on Western European investors. For the present, there are no signs of an African regional spill-over effect of a magnitude equivalent to what has happened in the Asian economies. However, South Africa, with its high growth potential, is expected to play an increasingly important role in FDI regionally in the foreseeable future, especially in the context of SADC. In deed, South African investors are largely responsible for what interregional investment has taken place in the SADC region's LDCs.

2. NEGOTIATION OF FOREIGN INVESTMENT

It is clearly known that the decision to invest ultimately rests on the result of foreign investor's negotiations with the host country. It is common to negotiate over the terms of entry, conditions of performance, and duration of the investment. Ideally, such negotiations should be based on a through cost- benefit analysis. More investment projects are now the outcome of a cost-benefit analysis in negotiation between the foreign investors and host governments, but as yet, a comprehensive economic analysis is only approximated to various degrees in actual negotiations. Nonetheless, it is still desirable to have an ideal model in mind when negotiating. This type of model attempts to rationalize the mixture of incentives and restrictions that host governments place on foreign investment. It also may suggest arrangements that will give a higher payoff for both investor and host country.

Before attempting to jump in to investing in host countries, foreign firms have to be aware of the development objectives and priorities of the host country and understand how their investments may contribute to the country's development strategy. The foreign investor has to be prepared to demonstrate the contribution of private foreign capital in terms beyond private profit. At the same time, the government must recognize that if risks are too high, or the return on investment is too low. FDI will be inhibited from making any contribution at all. The negotiation process should establish policies that will meet the mutual interests of private investor and host country.

In essence, the foreign investor must convince the host government that the increase in real income resulting from the investment project is greater than the resultant increase in the income of the investor. If the value added to output by FDI is greater than the amount appropriated by the foreign investor, social returns exceed private returns. The negotiating objective of the foreign investor, therefore, is to convince the host

government that the benefit-cost ratio of the FDI is greater than unity and to secure the most favorable conditions for entry and operation. *To this end, the foreign investor may point to a considerable list of benefits from the investment: local value added, inflow of foreign exchange, creation of employment, infusion of skills, contribution of taxes and royalties, and the creation of external economies elsewhere in the economy beyond the investment project itself.

2.1. How do MNCs choose where to invest?

There are many determinants of the decision to invest abroad, and hence investors must consider a number of preference curves. These determinants can be grouped in to two. In most cases, a firm will decide to set up facilities abroad either so that it can serve the local market directly (“market seeking”), or the particular country possesses the right combination of production factors (Labor, Capital, Land/Resource) needed to manufacture a certain product. In the latter case (“sourcing”) production may be primarily destined for export.

If there is a trade-off that affects investment location decisions as between CEE countries and those of the Mediterranean rim, then certain specific conditions must be present. The amount of investment that investors as a whole are willing to commit must be limited. In addition, the elements that contribute to the attractiveness of countries in two different zones must be similar. This latter condition implies that the attractiveness of different countries must be comparable both for investors following a multi domestic or horizontal strategy and those for who have adopted a global or vertical approach.

In 1993, FDI was the largest single source of external finance for developing countries, accounting for about half of all private resource flows. Following the virtual disappearance of commercial bank lending to these countries in the 1980s, many countries liberalized their restrictions on incoming foreign investment.

The pro-investment policies of the 1990s are very different from the wave of nationalizations, which drove out of foreign investment in many regions during the 1960s and 1970s. The new attitude is in part driven by the need for alternative sources of new capital, and in part driven by increasing skepticism about import- substituting trade and investment strategies.

A progressive liberalization of policy toward foreign capital has occurred during recent years. Many countries now recognize that an inflow of private capital may offer some special advantages over public capital, and a number of investment incentive measures have been recently adopted or are under consideration. These incentive devices include assistance in securing information on investment opportunities, the provision of supplementary finance, the establishment of economic overhead facilities such as in industrial estates, protective tariffs on commodities that compete with those produced by foreign investors, exemptions from import duties on necessary equipment and materials, the granting of exchange guarantees or privileges, tax concession schemes for the encouragement of desired new investments, and special legislation for protection of foreign investments.

2.2. Benefits and Costs of FDI

FDI is a key ingredient for successful economic growth in developing countries. This is because the very essence of economic development is the rapid and efficient transfer and adoption of (best practice) across borders. FDI is particularly well suited to effect this and translate it into broad-based growth, not least upgrading human capital as growth is the single-most important factor affecting poverty reduction, FDI is or the particular country possesses the right combination of production factors (labor, capital,

land / resources) needed to manufacture a certain product, in the latter case, (“sourcing”) production may be primarily destined for export.

FDI is a key ingredient for successful economic growth in developing countries. This is because the very essence of economic development is the rapid and efficient transfer and adoption of “best practice” across borders. FDI is particularly well suited to effect this and translate it into broad-based growth, not least by upgrading human capital. As growth is the single-most important factor affecting poverty reduction, FDI is central to achieving that goal.

Beyond promoting growth, FDI has the following potentially desirable features that affect the quality of growth and assist with poverty reduction:

- It helps reduce adverse shocks to the poor resulting from financial instability as during the recent Asian crisis.
- Relative to other forms of promoting private sector investment, FDI helps improve corporate governance. In particular, it is not easily subject to asset stripping that may render property rights distribution more unequal.
- Contrary to popular criticism, FDI can help improve environmental and labor standards, because foreign investors tend to be concerned about reputation in markets, where high standards are seen as desirable. It could also provide a great help in the form of worker training which can not be replicated in domestic firms or purchased from abroad, such as managerial skills.
- FDI generates taxes that support the development of a safety net for the poor. Many foreign investors also invest substantially in community development in areas where they operate and thus in the safety net for the particular area. Also, FDI can help improve the management of the social safety net, particularly the service delivery to the poor, for example, water supply.
- Domestic labor in the form of higher real wages.

- Technology spill over since new technology may not be commercially available and innovating firms may refuse to sell their technology via licensing agreements (Meier and Rauch, 2000)
- Domestic labor in the form of higher real wages, *x repeated*
- Consumers by way of lower prices, and
- The government through higher tax revenue. Beyond this, and most importantly in many cases, there are likely to be
- Indirect gains through the realization of external economies

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In any country, development planning requires the government to influence the performance of private foreign investment, but in doing this, the government should appreciate fully the potential contribution of this investment and should devise policies that will meet the mutual interests of private investor and host country.

A progressive liberalization of policy toward private foreign capital has occurred during recent years. Many countries now recognize that an inflow of private capital may offer some special advantages over public capital, and a number of investment incentive measures have been recently adopted or are under consideration. These incentive devices include assistance in securing information on investment opportunities, the provision of supplementary finance, the establishment of economic overhead facilities such as in industrial estates, protective tariffs on commodities that compete with those produced by foreign investors, exemptions from import duties on necessary equipment and materials,

the granting of exchange guarantees or privileges, tax concession schemes for the encouragement of desired new investments, and special legislation for the protection of foreign investments.

The essence of the case for encouraging an inflow of capital is that the increase in real income resulting from the act of investment is greater than the resultant increase in the income of the investor. In the value added to output by the foreign capital is greater than the amount appropriated by the investor, social returns exceed private returns. As long as foreign investment raises productivity, and this increase is not wholly appropriated by the investor, the greater product must be shared with others, and there must be some direct benefits to other income groups.

For a developing country, the inflow of foreign capital may be significant in not only raising the productivity of a given number labor, but also allowing a large labor force to be employed.

Domestic consumers may also benefit from direct foreign investment. When the investment is cost reducing in a particular industry, consumers of the product may gain through lower product prices. If the investment is product improving or product innovating, consumers benefit from better quality products or new products.

2.3. Costs of FDI

Apart from the good sides of Foreign Investment, there are side effects that foreign investment may hinder development activities of LDCs. Some of these problems are:

- Even if MNCs hire employees from host countries, they prefer to hire highly skilled and professional workers. That means, they tend to use capital-intensive firms in countries where there is more than enough labor.

- MNCs tend to import raw materials for their affiliate companies from where their head quarter is located, thus reducing the amount of income that host countries would have gained
- Very little labor mobility between domestic firms and foreign subsidiaries,
- Limited subcontracting to local firms,
- No research and development by subsidiaries, and
- Few incentives by multinationals to diffuse their knowledge to local competitors.

In addition to this, there is no evidence that the benefits accruing to joint ventures or local subsidiaries of multinationals are diffused to domestic firms. In other words, foreign investors provide direct benefits to those firms receiving investment, but there are no spill-over to other plants. In fact, an increase in MNC presence hurt the productivity of domestic competitors, in part b/c MNCs took market share away from domestic plants. The lack of technology transfer to domestic competitors can be explained by the limited hiring of domestic employees in higher level positions.

3. POLICIES TO ENHANCE PRIVATE LENDING TO DEVELOPING NATIONS

3.1. Favorable Policies to enhance Foreign Investment

With the help of promoting private investment, countries across the SSA have undertaken a seeping change of policy in the past decade to liberate and open their economies. The varying degrees, attention has been focused on areas such as:

- ⌘ Creating a stable macroeconomic environment,
- ⌘ Liberalizing controls on Foreign exchange transactions,
- ⌘ Liberalizing price, licensing, and other controls on both domestic markets and international trade,
- ⌘ Rationalizing tax and tariff structures, including reduction of average rates,
- ⌘ Liberalizing investment laws,
- ⌘ Actively promoting foreign investment and exports.

Despite these and other improvements, however, the formal investment response in most countries has been disappointing. As the same time, micro and informal enterprises are not only failing to “graduate” to the formal sector, but are playing an increasingly important commercial role.

3.2. Obstacles that hinder flow of FDI

The key factors in the investment environment that may inhibit, constrain, or reduce private (domestic and foreign) investment activity include:

- A poor business environment. A favorable business environment encompasses a number of elements including a transparent and nondiscriminatory regulatory framework, effective competition policies, an efficient judicial system, and positive attitudes toward private business on government, politicians, and other opinion leaders.

- Distorted incentive policies. Controls on product and factor prices, special tax incentives, trade protection, state subsidies, preferential access to scarce resources may benefit some groups at the expense of others, reduce the overall efficiency of resource allocation, and offer opportunities for corruption.
- Inadequate framework. Dynamic private sector economic activity and efficient market relationships require a strong framework of laws and an effective, independent judicial system which provides for the fair and timely adjudication of claims. In the absence of such framework, private activity may be limited to the pursuit of quick profits and to rent seeking, rather than to long-term, growth-oriented investment.
- Distorted or institutionally weak financial system. Competitive financial markets and market-oriented institutions are essential to the efficient provision of credit and other financial services to private enterprises.
- Access to land. Difficulties in gaining access to land through outright purchases or leasehold contracts, often impede foreign investment since investors are seeking secure tenure of land where facilities are located.
- Bureaucracy. An inefficient and non-transparent bureaucracy contributes to high transaction and business costs for investors. It is necessary to streamline the bureaucracy and increase the transparency of rules in general and particularly those governing investment, labor and trade, the environment, and taxation. The equitable, consistent and efficient application of the rules increases predictability, minimizes cost and corruption, and helps to increase investor confidence.
- Poor infrastructure. Efficient and low-cost communication networks, domestic and international transportation links, and reliable power supplies are important for attracting FDI in certain sectors.
- Lack of skilled or trainable labor. Low-cost, unskilled labor is becoming less important in the non-extractive and agriculture sectors. The demand for

skilled or highly trainable human capital that can cope with emerging technologies is increasing.

- Absence of supplier networks and clusters. For countries seeking to attract high value-added, efficiency-seeking FDI, the development of local supplier networks is increasingly important. With appropriate conditions, supportive policies and dynamic local enterprises, foreign investors can facilitate and contribute to the development of these networks and clusters.

4. MULTINATIONAL ENTERPRISES IN DEVELOPING WORLD

Multinational corporations (MNCs) do the overwhelming proportion of foreign investment in third world countries. A Multinational is an enterprise that produces in more than one country and considers overseas operations to be central to its profitability. Multinational enterprises come in all sizes and from all regions of the world, including the developing countries, but a relatively small number are dominant. In 1980, roughly 10,000 MNCs were in existence, exercising control over nearly 90,000 affiliates. But only 500 of these firms accounted for 80 percent of the world's stock of direct foreign investment in that year.

Most Multinationals are based in the industrial countries. By the end of the 1980s, over 95 percent of the yearly outward flow of foreign investment- almost \$240 billion in 1990- was from rich country investors. Most multinational investment is also directed toward other wealthy countries: in the late 1980s, at least 70 percent of the outflow of direct foreign investment was from one industrial country to another. Of the \$159 billion of private foreign assets located in developing countries in 1985, half was in Latin America and close to a third in Asia. Direct Investment in developing countries comes from three dominant countries. Over a five-year period during the 1980s, 30 percent of the flow of direct investment in to developing countries came from the United States, 21 percent from Japan, and 19 percent from the United Kingdom.

Contrary to popular belief, multinational investment in developing countries does not consist largely of manufacturing firms searching for "cheap" foreign labor. Indeed, among the major investing countries, only Germany had more than a third of its developing country assets in the manufacturing sector in the 1980s. Mining and modern services are the other main destinations for MNC investment, and both are capital-intensive sectors. Similar multinational from Korea, Taiwan, and Hong Kong, and other middle income countries do, however, invest overseas in export-oriented manufacturing

in such labor intensive industries as textiles, footwear, sporting equipment, and electronics assembly.

Multinationals are a much more diverse group. Only 161 of the world's largest 500 companies were American in 1994, according to Fortune Magazine; 128 of them were Japanese. Multinationals are not even necessarily from the industrial countries. Fifteen developing countries had companies in the top 500, including Korea (12 entries), South Africa (4), India (3), and Turkey (3). Nor are multinationals always private firms; the top 500 includes a number of giant, state-owned companies producing petroleum and steel, especially from the developing countries. Nor are multinationals always large; small companies, especially in East and Southeast Asia, have been investing overseas for many years. The largest of the multinationals, however, are very large. Many multinationals have worldwide sales and assets that exceed the GDPs of some large developing countries. General Motors, the largest MNC, had sales in 1992 equivalent to more than half the GDP of India and larger than the Turkish GDP. The sales of Toshiba, the twenty-fifth largest multinational, exceeded the GDP of Egypt, twenty-fifth largest economy.

5. CONCLUSIONS AND RECOMMENDATIONS

Data on sectoral distribution of FDI and other forms of investment in LDCs are difficult to come by and need to be compiled systematically as a matter of priority. In the pre-reform period, when the public sector was dominant and macroeconomic instability was the order of the day in LDCs, private capital tended to shy away from productive investment. Owing to perceived risk and uncertainty, investors tended to invest in short – term liquid assets with shorter turnover periods (especially trading), rather than such long-term physical investments as manufacturing. Further research is needed in order to establish the extent to which this situation has changed. Indications are that in SSA, only modest progress has been made (Nissanke, 1998). Those LDCs that are bedeviled by internal conflicts have hardly made any headway in attracting productive investment, although the case of conflict –ridden Angola indicates that, where rich natural resources are involved, investors are prepared to take risks. All in all, an increasing number of LDCs appreciate the value of FDI and are shaping an economic and political climate conducive to inspiring investors' confidence.

The available evidence, within its own limitations, indicates that macro-economic and other reforms, in particular privatization and the creation of national investment promotion agencies, have been able to create an environment in which private capital is being increasingly redirected in to productive investment. The most attractive area remains the extractive primary sector, especially mining, timber, oil and gas. There is, however, a need for both foreign investors and LDCs to ensure that issues pertaining to environmental protection of natural resources. Slowly but surely, investors' interest is also rising in respect of low value-added and labor-intensive manufacturing, especially textiles and agro-processing; electricity and energy; telecommunications; and services, especially tourism and financial services. Furthermore, commercialization of LDC utilities has created space for private-sector participation in this sector. A survey

undertaken by UNCTAD in 1999 among African investment promotion agencies indicates that most of these sectors will remain the major focus for FDI in the immediate future.

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