

Contemporary Insights into the Dynamics of Foreign Direct Investment in Zambia

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by

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ABSTRACT

Foreign direct investment (“FDI”) has been acclaimed by authors and policy makers alike to be one of the pivotal interventions that African countries need in order to support the capital investment required to sustain economic growth, alleviate poverty, and achieve the Millennium Development Goals in the region.

This research report aims to explain the evolution of the modern Zambian FDI environment and describe the dynamics at play in this thriving, yet poverty-stricken economy.

Over the last 25 years, Zambia has made remarkable progress in transforming its investment climate in order to successfully attract increased inflows of FDI over time. The primary interventions that brought about these changes in the country’s investment climate involved privatization and liberalization policies of the 1990s, institutional reforms of the early 2000s, and the more recent establishment of the Zambian Development Agency for the facilitation of all local and foreign investment. As a result, the international community responded with growing interest in the Zambian economy.

Despite having surpassed other African countries in attracting increasing levels of FDI, Zambia does not fully portray the perceived benefits of an economy experiencing an upswing in investment inflows i.e. – reduced unemployment, increased income, infrastructure upgrades, skills and knowledge transfer etc. The economy is still heavily dependent on one sector – copper mining, yet there remains a wealth of untapped natural resources which hold potential to improve Zambia’s social and economic status – fresh water, arable land and gemstones.

Key challenges in the country range across the spectrum from inadequate infrastructure to labour market challenges as well as the consequence of rising foreign firm entry – crowding out of local investment.

The report suggests key policy interventions to be considered should be aimed at infrastructural service delivery improvement through privatization, leveling of the playing field for local and international firms to improve domestic market competitiveness and a focus on skills and knowledge transfer obligations of foreign firms.

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GLOSSARY OF TERMS

BOZ	Bank of Zambia
COMESA	Common Market for Eastern and Southern African States
EAC	East African Community
FDI	Foreign Direct Investment
FTA	Free Trade Area
GDP	Gross Domestic Product
GRZ	Government of the Republic of Zambia
IMF	International Monetary Fund
JV	Joint Venture
LDC	Least developed countries
MFEZ	Multi-facility Economic Zones
MNC	Multinational Corporation
OECD	Organisation for Economic Cooperation and Development
PPP	Public-Private Partnership
PSDRP	Private Sector Development Reform Programme
RISDP	Regional Indicative Strategic Development Plan
SADC	Southern African Development Community
SEZ	Special Economic Zones
SOE	State-owned Enterprise

ACKNOWLEDGEMENTS

“Commit your work to the Lord, and your plans will be established.” (Proverbs 16:3) Truly, I give this work to Him who guides my steps, who planted this desire in my heart, and brought it all to fruition.

Professor Soko, my supervisor, for his professionalism, advice and patience – thank you.

To my late mother, Nokuthula, this is a tribute to your lifelong love and sacrifice. Your memory will live on forever. To my father and my sisters, thank you for going along with my crazy plans even when you didn't understand.

To all my family, friends and colleagues, thank you for giving me the space and time to attain my dreams as you waited quietly in the wings.

And my beloved, Charles, words cannot express how much your love and support have meant to me. Thank you does not even begin to describe my gratitude, here's to our future!

INTRODUCTION

Background to the Study

The world is constantly getting smaller. With the proliferation of technology and increasing trend of international trade, businesses are no longer confined to their domestic markets when searching for ways to meet capital, labour, operational, and customer needs.

For Africa, this has translated into an opportunity to become a supplier of choice to the global market, as the continent is endowed with a vast amount of natural resources, a young population to occupy the labour force and an untapped potential for market development that has long been saturated in the Western world.

In the movement towards lifting Africa from insufficiency and underdevelopment, foreign direct investment has been acclaimed to be one of the pivotal interventions that African countries need in order to support the capital investment required to sustain economic growth, alleviate poverty, and achieve the Millennium Development Goals in the region.

“Immediately following independence, policy makers across the region hoped that attracting FDI, often with the bait of high tariff protection and generous incentive packages, would provide the catalyst for a “late industrialization” (Evel, 2005).

Zambia’s history of foreign investment follows much the same pattern. The last decade has seen immense trade liberalization and increased foreign investment flows into the country. However, Zambia has also had a record of extreme sovereign indebtedness resulting in mass poverty and substandard living conditions for a large majority of its population. It is on this basis that an investigation into the foreign direct investment environment is relevant, as it has played an essential role in the country’s growth path.

Problem Definition

Over the last decade, the Zambian economy has transformed from a poverty stricken and single-commodity dependent to one that is more diversified, growth driven and investor friendly. Foreign direct investment and investment policy has been a pivotal factor in the development and evolution of the economy. This study probes into the intricacies that explain the current state of Zambia’s economy in relation to foreign direct investment.

Research objective

The objective of the study is to understand the dynamics of foreign direct investment in the Zambian economy, with specific reference to the origins, sectorial patterns, and impact on the local economy.

Research questions and scope

Primary research question

The overarching question to be answered in this report is:

What are the principal themes of foreign direct investment in Zambia today?

Secondary research questions

1. What is the history of foreign investment in Zambia?
2. Which industries attract the majority of FDI inflows in Zambia?
3. How has the Zambian foreign investment climate evolved over time?
4. What FDI trends are prevalent in the key sectors of the economy?
5. What have been the impacts of increased levels of FDI in the local economy?

Research Relevance

The study adds to the literature in that it provides a consolidated review of the current literature that describes the investment environment of Zambia. This report provides a basis for further research and policy promulgation both in Zambia and in other countries within the region.

Chapter Outline

The report is structured as follows:

Chapter 1: The introductory chapter provided an overview of the motivation for the study, presents the objectives of the report and outlines the research questions.

Chapter 2: The literature review is presented and discusses the history and issues pertaining to FDI in Africa, Southern Africa and Zambia to provide a background and context for the study.

Chapter 3: The chapter is an overview of the Zambian investment climate included to provide the context necessary to understand and interpret the findings of the case study appropriately.

Chapter 4: This chapter unpacks the findings of the research through an analysis of all data collected.

Chapter 5: The final section summarises the findings of the report, provides recommendation on addressing current challenges in the Zambian investment environment and highlights key areas for future research.

Conclusion

In this chapter, an orientation of the entire report has been presented. The chapter begins by defining the research problem, identifies the objectives, and clarifies the questions to be answered by the report. The chapter concluded with an outline of the chapters included in the report.

REVIEW OF THE LITERATURE

Introduction

This section provides the relevant background knowledge necessary to answer the research questions. The literature review presents the theoretical framework within which this report is conducted. The section begins with a definition and description of the types of foreign direct investment. Secondly, the theory behind firm decisions on internationalization strategies is discussed. The chapter then looks at the history, reforms, challenges and outlook for Foreign Direct Investment in Africa, and Southern Africa respectively. Finally, the above mentioned aspects are studied at a micro level for the country under review; Zambia.

Definition and types of Foreign Direct Investment

According to the OECD Benchmark definition, FDI is a term that describes cross-border investment by an entity in one country with the objective of obtaining a lasting interest in an enterprise resident in another country (OECD, 2008).

Unlike portfolio investments, which can be short-term and speculative, FDI involves the acquisition of a long-term controlling interest in the operations of the host country company. The long-term interest infers the existence of a long-term relationship between the direct investor and the enterprise, as well as significant degree of influence by the investor on the operational activities and management of the enterprise (OECD, 2013). In order for an external entity's investment to be considered FDI (and to exert influence on operation and management of an enterprise), the direct investor is required to own at least 10% of voting class equity (OECD, 2005).

FDI can take one of four forms, such as mergers and acquisitions, greenfield investments, brownfield investments, and financial restructuring. Mergers involve the amalgamation of two separate entities, whereas acquisitions take place when the investor company purchases the host country entity. Greenfield investments are those in which the investor company establishes new operations, in contrast to brownfield investments that are an expansion of existing operations in the FDI recipient country. Financial restructuring transactions are those that require new equity financing in order to meet recipient company debt repayments or minimizing operational losses(Oecd, 2008).

FDI Strategies for Foreign Market Entry

Rugman and Collinson (2006) define internationalisation as “the process by which a firm enters foreign markets”. Foreign direct investment is key part of the firm internationalisation process as it determines the flow of funds and structuring of the market entry transaction.

The extent of the impact and influence a firm has in the investee country depends on the level of control the foreign firm has in the investee company. Similarly, the level of influence is determined by the mode of entry that the foreign firm selects when deciding to expand internationally. Firms have various motivations for moving into new markets, as well as the how they enter these markets (Boojihawon & Acholonu, 2013).

Considerations influencing FDI mode of entry

In their analysis of the determinants of choices made by MNCs in selecting an entry FDI mode into developing economies, Bhaumik and Gelb (2005) found that the following factors are central to determining the preferred mode of market entry – level of technological competitive advantage, information on local market (information asymmetry), transaction costs of establishing local business, level of reliance on local resources, and the growth rate of the local market.

In instances where the MNC has high competitive advantage due to its skills and/or technology, but little knowledge of the local market, the authors find that MNCs are more likely to choose a joint venture or acquisition market entry strategy. This is also the case in scenarios where the MNC relies heavily on local resources in the host country (Müller, 2007).

When transaction costs are low and the effect of information asymmetry is negligible, MNCs are more likely to enter the local market through greenfield (and brownfields) investment. This is also the case when the MNC has prior experience operating in similar markets, or the dependence on the local market for resources is low.

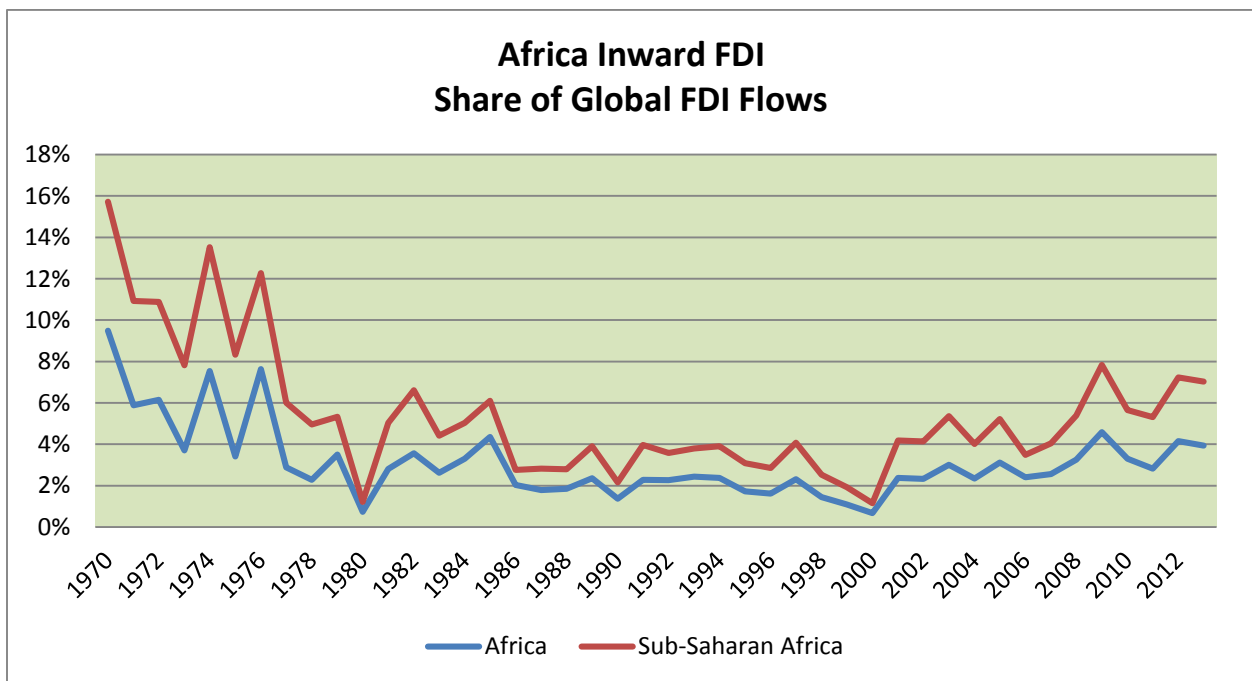
A primary motivator for MNCs wanting to enter foreign markets is to access growing and developing markets, and expand outside local markets as they become more saturated. Geographic diversification provides new sources of revenue and limit concentration risk (Bhaumik & Gelb, 2005).

Numerous studies have been conducted in an effort to understand the multinational firm’s motivation for opting for a specific FDI market entry mode. This report aims to explain some of these motivations for firms operating in Zambia.

Foreign Direct Investment in Africa

Historically, foreign direct investment in Africa has exhibited three main features; these are; 1) lagging behind in share of global FDI, 2) FDI concentration in selected countries, and 3) flows concentrated in limited sectors (Moss, Ramachandran, & Shah, 2004).

Despite world FDI flow growing 14% per annum over the last four decades, Africa’s share of global FDI averaged 5% p.a. during the 1970s, decreasing to 2% p.a. in the 1980s, and remained at this level during the 1990s, increasing marginally to 3% p.a. in the 2000s. The meagre performance in attracting FDI can be attributed to other developing regions growing share - particularly Asia whose share of global FDI flows increased from 6% to above 22% of global FDI over the period - resulting in a net decrease in Africa’s share. Also, the adverse approach towards foreign funds in post-colonial Africa led to newly independent governments creating policies that stifled the business environment for potential foreign investment. Nationalization and expropriation of economically productive assets was a phenomenon that saw a marked decrease in the continent’s attractiveness to receive FDI(Moss et al., 2004).



Source: Adapted from UNCTAD FDI database 2015

The latter characteristics of FDI in Africa can be considered to be interrelated. The high concentration of FDI in extractive sectors strongly influenced the geographical flow of funds on the continent. Africa’s wealth and abundance of natural resources has resulted in the skewed nature of FDI flows in the region. Investment in the oil, gas and precious metal mining industries has resulted in countries such as Angola, Nigeria and South Africa being the top attractors of foreign investment, and maintaining this position over the last three decades (UNCTAD, 1995). The majority of investment received in Angola, Nigeria, Equatorial Guinea, Sudan and Chad has been in oil-related activities. For countries such as South Africa, Tanzania, Botswana, Ghana, Zambia and Namibia(Ezeoha & Ugwu, 2015), the attractiveness for FDI was driven by the rich mineral reserves such as gold, platinum, copper and diamonds, making mining the largest FDI receiving industry in these countries (UNCTAD, 1995). The table below illustrates the above fact by showing how the top FDI recipient countries in Africa are those naturally endowed with precious natural resources.

Rank	Country	FDI Inflow 1970 -1990	Abundant Resource(s)
1	Egypt	US\$ 11.0 billion	Petroleum, Natural Gas
2	Nigeria	US\$ 8.1 billion	Petroleum
3	Liberia	US\$ 2 .4 billion	Diamonds, Gold, Iron Ore
4	Tunisia	US\$ 1.9 billion	Petroleum, Iron Ore
5	Papua New Guinea	US\$ 1.8 billion	Oil, Copper, Gold
6	Algeria	US\$ 1.5 billion	Crude Oil, Natural Gas
7	Angola	US\$ 1.0 billion	Oil, Gas, Diamonds
8	Zambia	US\$ 1.0 billion	Copper
9	South Africa	US\$ 983 million	Gold, Diamonds, Coal
10	Cameroon	US\$ 955 million	Oil, Natural Gas

Source: Adapted from World Bank World Development Indicators, July 2015

Over time, the composition of Africa’s top FDI recipients may have changed, resulting in new FDI hotspots emerging. However, the key driver of that shift in foreign investment is largely driven by discoveries of further or new deposits of natural resources, as evidenced in the below table.

Rank	Country	FDI Inflow 1991 -2013	Abundant Resource(s)
1	Nigeria	US\$ 79.5 billion	Petroleum
2	South Africa	US\$ 71.7 billion	Gold, Diamonds, Coal
3	Egypt	US\$ 66.7 billion	Petroleum, Natural Gas
4	Morocco	US\$ 26.9 billion	Phosphate, Copper
5	Algeria	US\$ 23.6 billion	Crude Oil, Natural Gas
6	Sudan	US\$ 22.0 billion	Petroleum
7	Mozambique	US\$ 21.6 billion	Natural Gas, Coal
8	Democratic Republic of Congo	US\$ 21.5 billion	Diamonds, Gold, Oil
9	Ghana	US\$ 21.3 billion	Gold, Diamonds, Aluminium
10	Tunisia	US\$ 20.6 billion	Petroleum, Iron Ore

Source: Adapted from World Bank World Development Indicators, July 2015

The large volume of naturally occurring valuable resources available may have been the foremost influencing factor attracting investment into Africa, but this is not the sole condition upon which multinational corporations choose where to invest. Other motivations for FDI relate to the economic environment in which a venture is to take place i.e. depth of the market – number of willing buyers and sellers, market prices for the said commodity, as well as cost of establishing and operating the business (UNCTAD, 1995). As markets develop and diversify, new opportunities are created for value seeking external investors.

Due to the extensive amount of research that advocates FDI as a tool for economic development, and the emphasis on a sound business environment that facilitates a country’s attractiveness for recipient FDI, African countries have slowly liberalized macroeconomic policies to increase their share of FDI flows (Moss et al., 2004).

As a result, numerous African countries have made significant macroeconomic policy changes to attract foreign investment and liberalize the business environment. Sectors that were previously restricted from foreigners have been opened up, further drawing investment from outside the continent. Other initiatives by states include tax holidays, relieved import and customs controls, infrastructure investment, and improvement of labour laws (Moss et al., 2004). The resultant effect of these policy reforms has in many instances not been the desired increase of FDI, but rather ensued in a competition for foreign funds, as investors look for the lowest cost destination for

funds. This can result in recipient countries accepting unreasonable FDI terms, not realizing the skills, technology transfers, or economic growth that FDI is envisaged to bring about.

Challenges to attracting FDI

In its 2014 Executing Growth report, Ernst & Young highlights the following key challenges that multinational corporations expanding into Africa are familiar with, including entities that have been successful at it.

First and foremost is the inherent political risk that is ever-ominous in the region. Leaders are known to use policies as a tool to entrench power and control of economic assets. Widespread violence, civil wars and overall social instability plague many countries at any given time. Furthermore, there is still a need for enhanced skills to public sector officials for informing, facilitating, and regulating the business environment. This fuels the perception that Africa is unstable and dangerous, making investors who are unfamiliar with the environment averse to doing business on the continent.

Backlog in infrastructure development on the continent makes business activities difficult and impractical. Power outages, insufficient rail and road transport links, and narrow telecommunications networks make the cost of establishing and operating a business expensive, and limit access to key markets for expansion. There is often insufficient capacity and capability in the public sector to develop projects to bankable stage (Ernst and Young, 2014).

Lack of skilled human capital affects investor prospects in a similar way to infrastructure backlog. The need to educate, develop and transfer skills before seeing productive results longer timelines for returns and more effort from foreign investors.

In spite of the challenges, Africa still offers vast opportunity for global investors, these include;

- 1) Large investment in infrastructure to connect economic hubs in order to increase trade routes;
- 2) New investment hubs are coming to the fore, providing more markets for international investors to utilize in greenfield and/or brownfield investments. Countries such as Kenya, Ghana, Mozambique, Uganda, Tanzania and Zambia are becoming attractive investment destinations apart

from the traditional favoured investment destination like South Africa, Nigeria and Angola and (Ernst and Young, 2014);

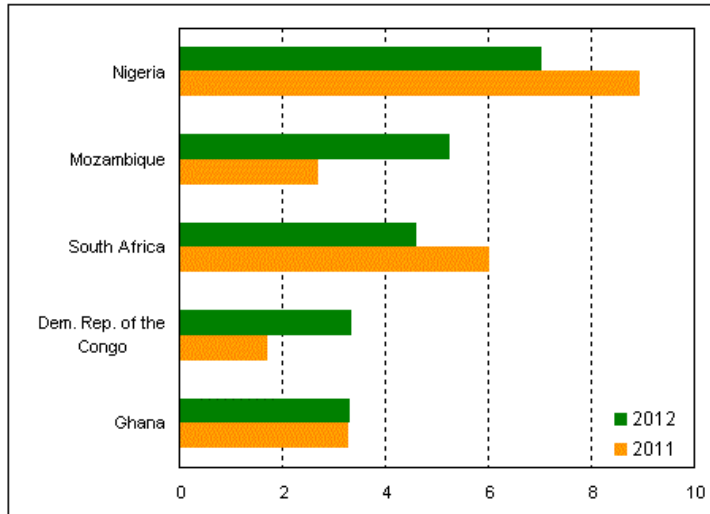
3) Rapid growth of urbanization and increasing middle class resulting in a growing consumer class (Ernst and Young, 2014).

Outlook and trends

With the privatization of large state utilities and entities, African countries are relying progressively less and less on foreign investment in extractive industries. According to Liberatori and Pigato, privatization of formerly state-owned and run entities was the impetus for a structural shift in investment diversification of African assets. Early stage privatization focused on loss making small and medium enterprises in industrial service sectors, however as policy and capital market reforms progressed in the 20th century, larger entities in the utilities sectors, such as power, rail transportation, water and telecommunications came to the fore (Liberatori, Pigato, 2000). In the period 2000 to 2014, the extractive sector's portion of total greenfield projects announced decreased from an estimated 26% of all greenfield projects to 8% of all total project value. On the rise are investments in the manufacturing and services sector, which account for approximately 90% of the value of greenfield projects in Africa and least-developed countries (UNCTAD, 2014).

Historically, Nigeria and South Africa have been the top recipients of FDI on the continent. South Africa maintained its powerhouse status, accounting for 20% of the continent's foreign investment in 2014 of US\$ 10.3bn (www.worldbank.org, 2015). On the contrary, Nigerian FDI flows decreased by 20% to US\$5.5bn, as a result of divestment of assets in the petroleum sectors by large transnational corporations such as Shell and Chevron. However, these countries are being overtaken by new FDI attractions such as Mozambique due to growth in the oil and gas sectors, claiming an estimated US\$ 7.3bn in investments during 2014. Other growing markets attracting FDI include Ghana, Uganda and Zambia (Mendelsohn & Kwafo-akoto, 2014).

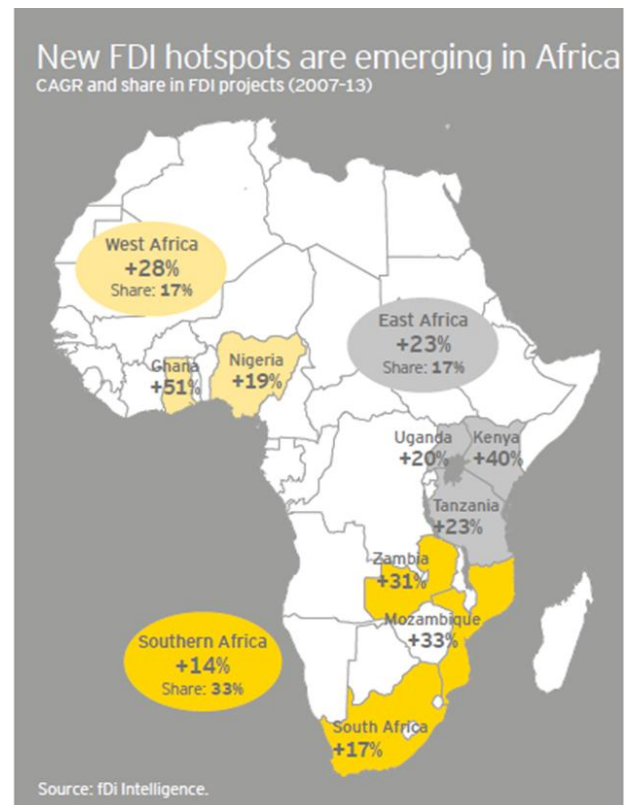
Top 5 FDI recipients of FDI in Africa 2011-2012 (US\$ billions)



Source: World Investment Report 2013, UNCTAD

Although South Africa continues to be the favoured destination for FDI projects, countries including Ghana, Nigeria, Kenya, Mozambique, Tanzania and Uganda, are becoming increasingly more attractive for foreign investment. Ernst and Young’s 2014 Attractiveness survey showed “Kenya and Ghana featured in the top four rankings in 2013 for the first time, having previously ranked in the bottom half of the top 10 FDI destinations”.

The promotion of enhanced regional integration by African leaders has seen the rise of Intra-African investment. At the forefront of this development are transnational corporations from South Africa, Nigeria and Kenya. This type of investment is especially significant in non-resource exporting and landlocked countries, as this forms the majority of foreign capital inflows. Intra-regional FDI in Africa grew at a compound annual growth rate (“CAGR”) of 31.5% in the period 2007-2013 (Ernst and Young, 2014). In the East African Community, intraregional flows make up circa 50% of inter-African investments, and in the Southern African Development Community over 90%. These are due to investments from



Kenya and South Africa into neighboring countries. For other Regional Economic Communities, the portion of intraregional investments is significantly smaller, with average share of cross-border investments from within Africa at 18% for the continent (UNCTAD, 2014). Intra-Africa investments are the second largest source of foreign investment and job creation in Sub-Saharan Africa, after Western Europe.

Foreign Direct Investment in Southern Africa

There are two definitions of Southern Africa. The United Nations recognizes the following five countries as part of Southern Africa – Botswana, Lesotho, Namibia, South Africa and Swaziland. The second and more widely accepted group of countries constituting Southern Africa is the regional economic community known as the Southern African Development Community (Sobhee, Sanjeev K , Bhowon, 2007). For the purposes of this report, SADC is taken as the definition of Southern Africa, as it includes all the countries subject to investigation herein.

SADC is an inter-governmental organisation headquartered in Gaborone, Botswana comprising of 15 member states, namely Angola, Botswana, the Democratic Republic of Congo, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe. SADC strives to uphold peace, security, and economic integration in the region in order to reduce poverty and obtain macroeconomic stability in the region. It is the largest of eight regional economic communities formally recognized by the African Union as a stepping stone toward achieving an African Economic Community (www.sadc.int, 2015).

Boasting the highest per capita income rates, SADC is the richest regional economic community in Sub-Saharan Africa and accounted for more than half of its GDP in 2009. Despite SADC's relatively developed economic position, the region's income varies widely among member countries, as it is mostly anchored on the economic performance of South Africa. South Africa contributes more than half of the region's GDP, but lags behind Botswana and Mauritius with respect to per capita income (Burgess, 2009).

As at 1 July 2015, the World Bank classified the various SADC member states by income as follows:

- High-income countries: (GNI per capita US\$ 12,736 or more): Seychelles;
- Upper-middle income countries (GNI per capita US\$ 4,125 – US\$ 12, 735): Angola, Botswana, Mauritius, Namibia, and South Africa;
- Lower-middle income/ developing economies (GNI per capita US\$ 1,045 –US\$ 4,125): Democratic Republic of Congo, Lesotho, Swaziland, and Zambia;
- Low-income countries (GNI per capita US\$ 1,045 or less): Madagascar, Malawi, Mozambique, Tanzania, and Zimbabwe.

The SADC persistently pursues policies and strategies to attract FDI (Mahembe, 2014). These include the Protocol on Trade of 1996, the Regional Indicative Strategic Development Plan of 2001, and the SADC Protocol on Trade and Investment of 2006.

The SADC Protocol on Trade aims to create “*a Free Trade Area (“FTA ”) in the SADC Region by 2008 and its objectives are to further liberalise intra-regional trade in goods and services; ensure efficient production; contribute towards the improvement of the climate for domestic, cross-border and foreign investment; and enhance economic development, diversification and industrialisation of the region*”(Mahembe, 2014). The overall goal of the Protocol on Trade is to allow for free migration of capital, labour, goods and services thereby creating a deeper market for international investors.

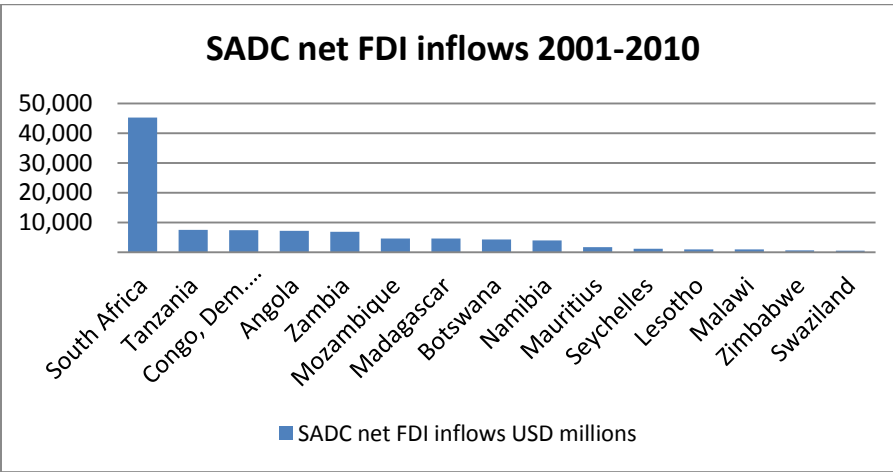
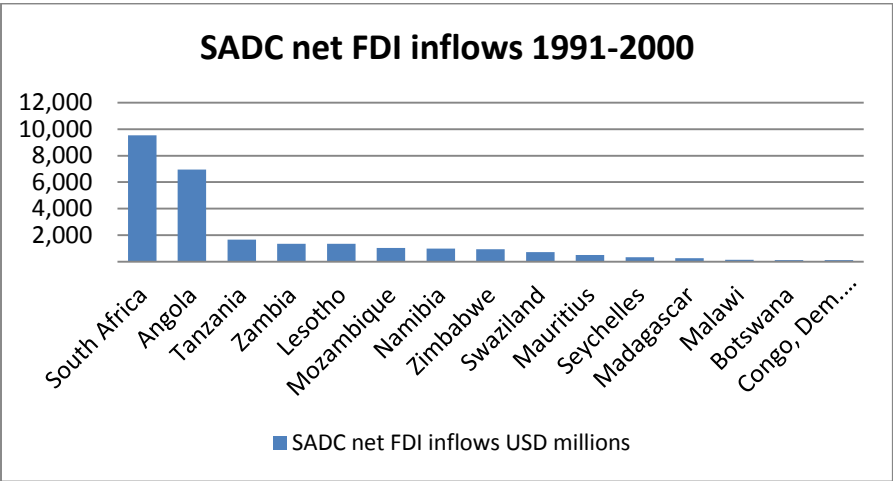
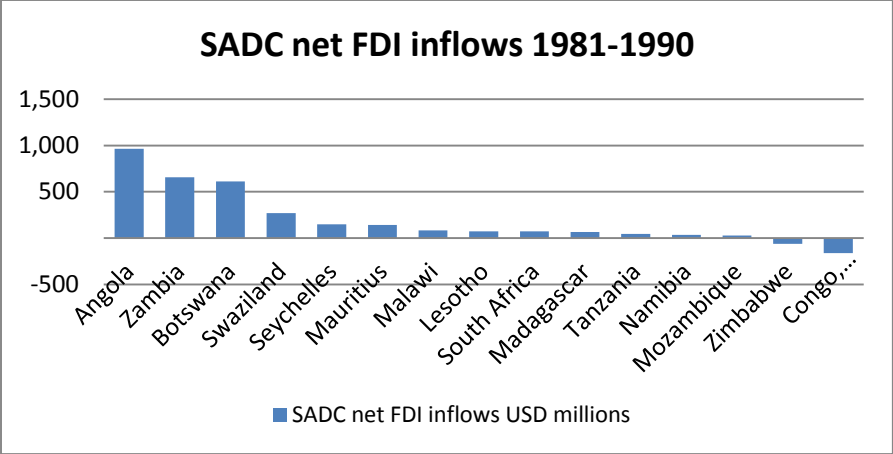
The Regional Indicative Strategic Development Plan (“RISDP”) “*is a comprehensive development and implementation framework guiding the Regional Integration agenda of the Southern African Development Community (SADC) over a period of fifteen years (2005-2020). It is designed to provide clear strategic direction with respect to SADC programmes, projects and activities in line with the SADC Common Agenda and strategic priorities, as enshrined in the SADC Treaty of 1992*” (SADC, 1999). The RISDP serves as the overarching implementation plan to achieve regional integration and identifies priority intervention areas, resource mobilization techniques and specifies monitoring and evaluation mechanisms.

The SADC Protocol on Finance and Investment was written with the purpose to align investment policies across the region in order to create an environment conducive for foreign investment through increased intraregional trade and coordination of the financial sectors. The Protocol also provides a guideline to member states for creating their own Bilateral Investment Treaties (BITs), even though it allows for deviations in certain circumstances (SADC, 2006).

Despite this, FDI policy in the SADC region is not harmonious across the board. Each Member State functions according to its own regulatory framework and individual level of economic liberalisation. Although fully open to foreign investment in numerous sectors, the majority of Member States place limits on level of foreign ownership of extractive industries, particularly mining, oil and gas, transport, telecommunications, banking and insurance, and media. These sectors fall under special policies and programmes aimed at economically empowering local citizens of the region and protecting independence (SADC, 2006).

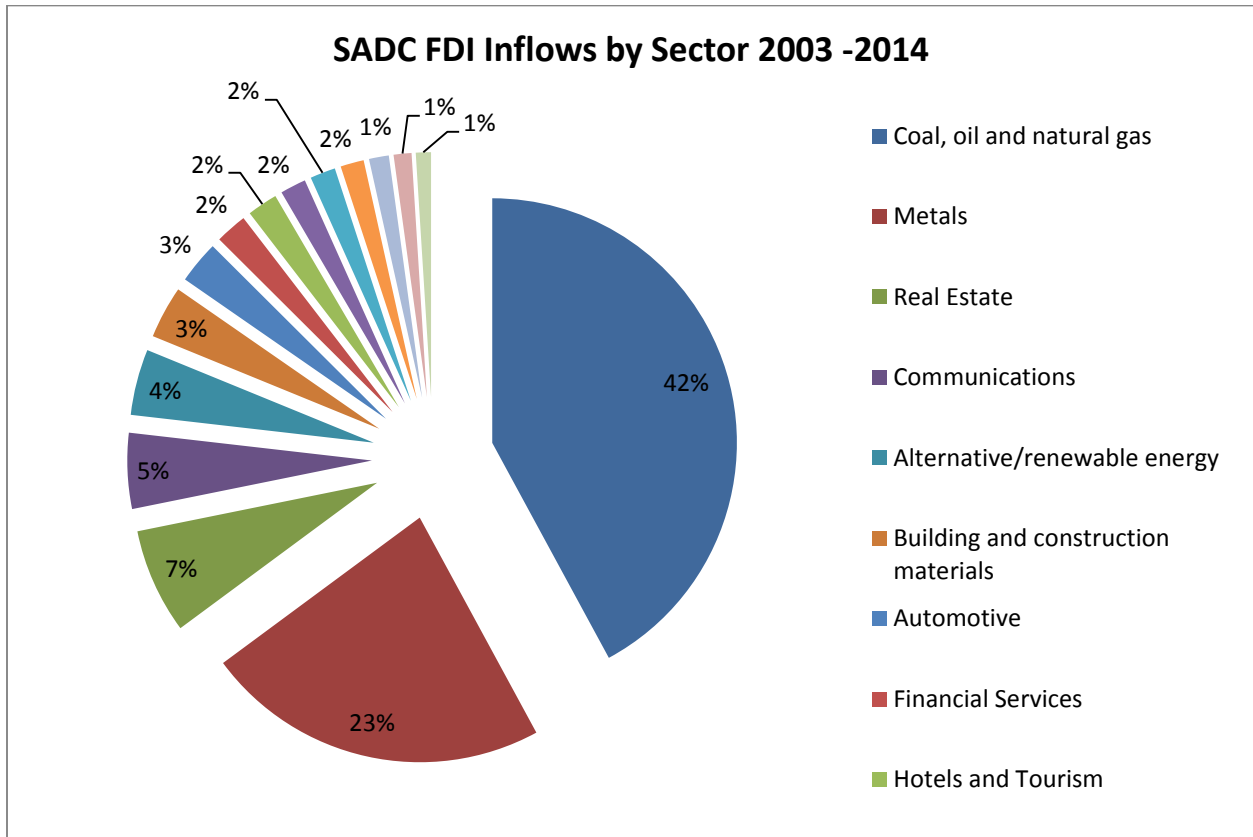
History of FDI flows to Southern Africa and main industries

The illustrations below are adapted from the World Bank's World Development indicators showing the spread of FDI flows amongst the SADC member states over the last three decades; namely 1981-1990, 1991-2000, 2001-2010.



A more recent look at FDI inflows in SADC from 2003 – 2014 shows South Africa, Angola and Mozambique to be the first tier recipients. Second tier FDI destinations include the Democratic Republic of Congo, Tanzania, Zambia and Zimbabwe. When FDI flows are separated by sector,

the trend is similar to what was observed at a continental level. Resource-based industries are the major FDI attractors in the region (Bezuidenhout, 2015).



Source: Adapted from Financial Times FDI Intelligence Data, *Financial Times*, fdimarkets.com, 2015

Intraregional investment in SADC makes up a small percentage of total FDI inflows in the region. Among the member states, South Africa and Mauritius are the largest net intraregional investors. In 2010, South Africa’s level of FDI into Botswana, Mauritius, Mozambique and Zambia stood at US\$ 980 million. Of this investment, approximately 82% of funds went to Mauritius, 12% to Mozambique, 4% to Botswana, and 2% to Zambia (Mougani, Rivera, Zhang, Mezui, & Kim, 2013).

The majority of Mauritian investments are directed to countries such as Madagascar, Seychelles, South Africa, Tanzania and Mozambique. Investments in these countries amounted to US\$ 46 million in 2011(Mougani et al., 2013).

Key challenges for attracting FDI

The foremost issue impeding SADC's attractiveness for increasing FDI is the weak regulatory framework and systems. The African Development Bank noted micro issues such as the lack of corporate governance guidelines, transparency of reporting, and managerial skills shortage as the foremost inhibitor of FDI for SADC countries.

“Business climate barriers” or weak corporate governance structures such as those described in the World Bank's Doing Business report constitute the second most pressing issues preventing investors. Ambiguous administrative requirements, weak enforcement of property rights, and inferior administrative skills hamper rate of increase of foreign investment in the SADC region (Mougani et al., 2013).

The underdevelopment of financial markets is another reason cited for lack of foreign investor appetite within SADC. The limited variety of financial instruments, low capitalization rates and illiquid nature of financial markets makes hedging and diversification across asset classes difficult for potential investors.

Muradzikwa (2002) also highlights the perceived (and actual) higher rates of crime and corruption in Southern Africa when compared to developed country counterparts as a factor deterring foreign investment in the region. Corruption not only increases the cost of doing business, but erodes the value that could be added to local citizens' lives and livelihoods, therefore limiting the positive spillovers expected to be gained from foreign investment.

Although SADC has 15 member states, the size of the market in terms of population and spending power is much smaller than that of developed world regional economic regions. For international investors, the consideration of market size is key in deciding where to position operations (Muradzikwa, 2002).

Zambia

The landlocked country of Zambia, formerly known as Northern Rhodesia, is home to 15 million citizens. The nation was previously classified as Heavily Indebted Poor Country (“HIPC”), but through the World Bank’s Multilateral Debt Relief Initiative (“MDRI”), Zambia’s external debt was written off in 2006, allowing the nation to rebuild its stock of foreign reserves and reduce dependence on foreign aid (OECD, 2011). The Zambian economy reached its highest level with a GDP of US\$ 27 billion in 2014. The country has showed impressive growth in the last 10 years, growing at an average of 6.7% p.a. The economic growth was stimulated by the thriving copper mining sector, as international copper prices rose along with investment in the sector (“Zambia GDP,” 2015). The key sectors contributing to Zambian GDP are copper mining, agriculture, construction and trade (World Bank, 2015).

The Zambian Economy at a Glance

The Zambian economy has exhibited robust positive GDP growth of above 6% p.a. (Rasmussen, Munkoni, & Lwanda, 2014) in the last decade. The impetus for the robust economic growth has been government’s focus on diversifying the economy away from traditional export revenue earning products such as copper and cobalt, and promoting investment into the construction, transportation, communications, trading and public sectors. This economic diversification was achieved through tight monetary policy, expansionary fiscal policy and the facilitation of incentives for foreign investment.

The table below presents a breakdown of GDP contribution by sector for the 2013 fiscal year as collated by the African Development Bank.

Sector	% GDP contribution 2008	% GDP contribution 2013
Agriculture (incl. hunting, forestry & fishing)	21.2	17.7
Mining	3.9	2.2
Manufacturing	10.1	8.2
Electricity, gas, and water	3.0	3.0
Construction	17.2	29.1
Wholesale & retail trade (incl. tourism)	19.8	15.1
Transport, storage and communication	4.4	3.9
Finance (incl. real estate)	9.8	9.2
Public administration (incl. education, health & social services)	2.8	2.9
Other	7.9	8.8
Total	100	100

From the above, one observes that Zambia's economy is gradually becoming less (although marginally) dependent on the copper mining sector when compared to the 2008 fiscal year.

From a socio-economic perspective, agriculture is the most vital sector as it provides "*employment opportunities for 60.0% of the country's informally employed population of 4.9 million and 8.0% of the only 625 000 formally employed*" (Rasmussen et al., 2014). The sector is susceptible to erratic rain patterns, which is a key determinant in the potential output every year.

The manufacturing industry's persistent positive growth comes as a result of increases in output from agri-business, such as food processing, tobacco and beverages, as well increased demand for materials inputs in the construction industry. The decline in manufacturing output in 2013 was primarily caused by sluggish growth in agri-business.

Positive growth in the construction industry is supported by government's increased allocation to infrastructure expenditure mainly in the road network. Projects such as Link 8000 and Pave Zambia will see US\$ 5.9 billion being utilized to upgrade 8000 kilometers of the country's road network by 2018 (German Chamber of Commerce, 2014) and 2000 kilometers of residential roads across the country paved whilst employing up to 18 000 citizens (Road Development Agency, 2012).

According to the World Bank 2013 Zambia Economic Review, Zambia has a young and rapidly growing population. It is anticipated that the population will almost double by 2030. The overall unemployment rate is estimated at 13.3% of the working age population. A closer look at this figure reveals that many Zambians living in rural areas are employed from a young because they do not have the option to further their education and to escape poverty. The majority of Zambians are employed on farms, in nonfarm home businesses, and in wage jobs. Despite the low unemployment rate, the reality, however, is that 60% of the population live below the poverty line because their earnings from work are low (World Bank, 2015). Unemployment is particularly problematic for youth in urban areas, where unemployment rates were in the region of 19.6% in 2010, due to a lack of skilled jobs available to university graduates (World Bank, 2015).

Key sectors of the Zambian Economy

The Zambian economy is established around its abundant natural resources – copper, cobalt, zinc, lead, coal, emeralds, gold, silver, uranium, fresh water, and 33 500km² of arable land. As a result, copper mining and processing, construction, hydropower, chemicals, textiles, fertilizer, and horticulture are among the leading industries (Ernst & Young, 2012; KPMG International, 2014).

“Zambia at independence was among the richest countries in sub-Saharan Africa. With copper, the country's major export, enjoying high rates on the market, the country had the necessary resources for development. But lack of investment in the sector, eventually led to low levels of copper output. The country started experiencing high levels of unemployment and underemployment, which could not be offset by revenue from other sectors of the economy.” (www.zambia-advisor.com, 2015).

In the last two decades, Zambia's impressive real GDP growth was mainly attained through diversification across sectors such as manufacturing, mining, construction, transport, communications and the public sector. Although tourism and agriculture have shown the largest growth, the copper mining industry is still the country's lifeblood, contributing about 70% to export earnings. However, over the last few years, the variety of exports has grown substantially (African Development Bank, OECD, & UNDP, 2014).

Copper Mining in Zambia

The discovery of world-class copper reserves during the 1930s laid the foundations of industrial mining in Zambia, but was disrupted by World War I and lack of sufficient capital to exploit the abundant resources. Despite initial setbacks, copper mining and beneficiation development grew rapidly, resulting in the creation of large mining towns like Ndola, Kitwe, and Chingola in the Copperbelt (Limpitlaw, 2011).

The industry grew bigger after the country received independence, with the state acquiring majority ownership in prominent mines like Roan Selection Trust (which became Roan Consolidated Mines) and Rhodesian Anglo American Corporation (thereafter known as Nchanga Consolidated Copper Mines) – with a focus on mass employment (Limpitlaw, 2011). *“During the socialist rule the copper mines fell under the control of the mostly state owned Zambia*

Consolidated Copper Mines (“ZCCM”). Profitable mines subsidized those that ran at a loss. The idea was to keep everyone working – the perfect socialist nirvana built on natural resource extraction. And it worked... for a while, until copper prices fell (Mills, 2010).”

The foremost objective for state ownership of the Copperbelt mines was the provision of secure employment. The state-owned miner, ZCCM, was not able to achieve this. In 1991, nearly two decades since independence, 70% of the population was estimated to live below the poverty line, increasing to 73% by 1998 and worsened due to privatization and retrenchments. Membership of the Mine Workers Union of Zambia (“MUZ”) decreased from 60 000 members in 1978, to an estimated 37 000 members in 1998. By the end of 1999, privatization resulted in a total of 8 329 employees being retrenched, diminishing the livelihoods of nearly 42 000 miners’ dependents (Limpitlaw, 2011:738).

The privatization revolution resulted in 257 of Zambia’s total 284 SOEs being privatized between 1990 and 2002. Of these companies, 65% were acquired by Zambian entities, 29% by foreign entities, and 6% dissolved. Despite the majority in volume of assets sold to local entities, in value terms, foreign investment surpassed domestic investment. The majority of assets sold to international investors were mining assets previously held by Zambian Consolidated Copper Mines (“ZCCM”) (UNCTAD, 2007).

Following the privatization efforts to turnaround Zambia’s mining sector from 1996, the country is rebuilding its powerhouse status and in 2011 was the world’ 6th largest copper producer accounting for 4.4% of global output (KPMG International, 2014).

Copper mining in Zambia is the second largest provider of employment after agriculture. It is the single biggest driver of foreign exchange earnings, making the economy extremely sensitive to any movement in the global copper market (Mills, 2010). With an economy almost entirely dependent on a single commodity, the nation has a mammoth task of ensuring that all investment into the sector results in widespread growth and long-term socioeconomic benefits for its population. This case study investigates how effective these efforts have been.

Agriculture in Zambia

With 42 million hectares of arable land and a water supply of 40% of the central and southern Africa's water supply Zambia's agricultural sector has immense potential to be the backbone of the country's economy.

Zambia's surface and underground water resources are of the highest grade that can be found in Africa due to many rivers, lakes and dams running across the country. The majority of these resources are still unexploited, as only about 50,000 hectares of a prospective (conservatively) estimated 423,000 hectares of arable land available is irrigated (Zambia Development Agency, 2014).

The Government of Zambia has earmarked agriculture as one of the primary engines of the economy's growth for the future. *“Agriculture generates between 18-20 % of the Gross Domestic Product (GDP) and provides livelihood for more than that 50 % of the population. The sector absorbs about 67 % of the labour force and remains the main source of income and employment for rural women who constitute 65 % of the total rural population. Increase in rural incomes will therefore result in overall poverty reduction and increased food security.”*

Agriculture in Zambia is dominated by subsistence farmers (small-medium scale farms), and a very small number of large commercial farmers. According to the Ministry of Agriculture and Cooperatives/Central Statistical office in 2009-2010, *“Zambia had about 1.4 million small- scale farmers in Zambia and around 1, 500 large-scale famers”*(Sikombe, 2012).

Historically, the Zambian government's focus in the agricultural sector was mainly on maize production for food security (Felgenhauer, 2008). However, since 1992, the state has made concerted efforts to increase access to the agricultural sector. Significant policy reforms include liberalisation of agricultural marketing for all inputs and products including exports, the privatisation of all former agro parastatals and increased private sector participation in commodity marketing and input supply and restructuring of the Ministry of Agriculture and Cooperatives (Zambia Development Agency, 2014).

Privatisation efforts and trade reforms starting in the early 2000s have resulted in an increase in the variety of export crops other than maize. Through the creation of export processing zones and the implementation of tax and duty reduction incentives, goods such as cotton, tobacco, spices, horticultural products, and honey have seen a marked increase in export volume (Felgenhauer, 2009).

Despite the positive strides towards increased contribution and productivity of Zambia's agricultural sector, numerous challenges remain. These include poor access to services for small farmer, poor infrastructure and access to markets, poor accessibility and administration of land, as well as lack of access to finance to upscale production (Felgenhauer, 2008).

Emerging Industries

The main sectors contributing to Zambian GDP are services (approx. 46%) – including wholesale and retail trade, financial services, transport, tourism and communication, industry (approx. 34%) – which includes mining, construction and manufacturing trades, and agriculture (approx. 20%)(Agency, 2015).

“The liberalisation of the Zambian services sector has over the years been influenced by a number of developments in the domestic, regional and multilateral trading system. Under unilateral liberalisation, following the adoption of Structural Adjustment Programme (SAP), the Government of Zambia was forced to autonomously liberalise a number of service sectors that included communication, financial, energy, trade and distribution services and transport.” (Habbu, 2008).

Much like the rest of the Zambian economy, trade liberalization through privatisation has had a positive impact on the services industry, allowing much needed foreign investment into the country, increasing output and employment. As such, tourism's contribution to GDP averaged 2.4% of GDP during the period 2001-2006 from 1% in 1998, whilst simultaneously creating 22 000 direct jobs. Similarly, transport and communication grew by 6.5 percent in 2004, while construction grew at an average growth rate of 17.5% per annum for in the period 1996-2006 (Habbu, 2008:3). Since 2000, service sub-sectors such as wholesale and retail trade, construction,

financial services including insurance, and tourism have together contributed more than 70% to the country's annual GDP (Habbu, 2008).

Despite the positive impact trade liberalisation has had in various sectors, foreign direct investment inflows have not reached the levels required to realize the economy's full potential and exploit the country's resources efficiently. In some sectors, FDI has not had the desired effects of technology and skills transfer. Habbu suggests that more domestic reforms such as lowered costs of establishing business are necessary to maximize the potential value that FDI can bring.

FDI theory – Merits and Drawbacks

In research papers examining FDI in Africa published in 2004 and 2006 respectively, author Asiedu found that countries in sub-Saharan Africa have the potential to realize numerous employment benefits of FDI such as decent infrastructure, higher income, and openness to trade as well as increase education levels. The author noted that African countries that are resource rich or that have large markets attract more FDI even after controlling for the effects of other significant determinants of FDI like adequate infrastructure, an educated labor force, macro stability, openness to FDI, an efficient legal system, less corruption, and political stability. To realize these benefits, Asiedu recommends that countries attract investments in non-natural resource industries in order to reduce the dependence on natural resources. The benefits of FDI observed by Asiedu echoed a similar notion found in the research conducted a decade prior. Borensztein & De Gregorio (1998) tested the effects of FDI on economic growth in 69 developing countries over 20 years and concluded that FDI was a key factor in the successful transfer of technology and subsequent increase in total factor productivity. The positive effects of FDI on economic growth observed by Borensztein et al seemed only attainable in economies where the absorptive capacity of the economy was adequate i.e. the country possesses some minimum threshold stock of human capital.

Amongst the myriad of reasons cited for the importance of attracting foreign investment into an economy, Maliwa and Nyambe (2015) add that the alleviation of high unemployment rates, creation of competitive markets, and skills transfer to the local workforce are of particular importance in Zambia. The authors also highlight increased FDI does not necessarily lead to

economic growth, stating this is only possible in a policy environment that is conducive to foreign investment.

The above propositions relating to the effects of foreign investment on economic growth have their roots in the neoclassical macroeconomic models which assert that long term economic growth is based on the level of capital accumulation and technological advancement (Seyoum, Wu, & Lin, 2014). The neoclassical growth theory motivation behind the perceived benefits of increased FDI flows is due to two reasons; firstly through increased capital investment and secondly through technology and skills transfer into the host economy that would have otherwise not have been available endogenously (Seyoum et al., 2014).

As much as FDI has been lauded as the answer to many of the inefficiencies of developing economies, it has also been subject to much resistance in some circles for various reasons. Dependency theory suggests that foreign direct investment can also be counterproductive to an economy's growth. In their assessment of the relationship between FDI and economic growth in developing African Nations, Seyoum et al present the reasons cited by dependency theorists that lead to destruction of growth through increasing levels of FDI. These include the fact that 1) the benefits of foreign investment can often be skewed toward the investor country and/or entity rather than the investee economy, 2) large multinational corporations can distort the competitiveness of host economies since they can crowd out local business and monopolize entire industries through their economies of scale, 3) international firms can introduce technology that negates the need for local human capital, thereby increasing unemployment, 3) multinational corporations can worsen the inequitable distribution of income, 4) the introduction of MNCs can lead to a dilution of local culture through the introduction of global practices, and 5) international firms can destabilize just political practices by manipulating governments in need of investment.

Much attention has been dedicated to finding the determinants of FDI, and how to inform policies that attract such investment into African countries. The majority of the theoretical and empirical literature presupposes that foreign investment is beneficial to addressing the region's developmental needs, and goes further to suggest how countries should go about increasing their share of FDI.

Although few and far between, studies covering FDI in Zambia do not find conclusive evidence that these investments have resulted in improved economic conditions in the recipient country.

In 2008, Lungu noted that although privatization increased the level of FDI inflows to Zambia, there was a loss in the social welfare of mining communities as international private companies did not have paternalistic welfare objectives.

Maliwa and Nyambe's study on the existence of a causal relationship between FDI and economic growth in Zambia showed that there is no such relationship, and leaves open the question as to what conditions would need to exist in this economy to make this relationship occur.

This paper adds to the literature in that it brings to light the current themes emerging in the Zambian FDI environment, their origins, patterns, strategies and perceived impacts. The study focuses on the state of the Zambian investment environment some four decades post-independence, taking into account the regional, economic, and industry nuances at play.

Research Methodology

This section describes the process that was followed in order to answer the research questions and achieve the objective of the study. The purpose is to give insight on how the research was conducted and tasks executed. It describes the method of collecting, organizing and reviewing the data.

Research Approach and Strategy

Research Approach: Case Study

The qualitative research method is useful for researchers wanting to study complex phenomena within their real-life context. A qualitative case study approach allows for the use of multiple data sources to ensure that the topic is explored thoroughly and the crux of the phenomenon can be uncovered (Baxter & Jack, 2008).

Yin (1994) advocates that a case study research method should be considered when “(1) the focus of the study is to answer “how or why” questions relating to the subject, (2) the researcher has little no control over events, (3) the focus is to understand the issue in its real-life context, and, (4) the line between phenomenon and context is unclear.

This research report will take the form of an explanatory case study in order to answer the question of “what is the current state of the foreign direct investment environment in Zambia?” Yin considers this type of case study most suitable for instances in which the researcher is seeking to answer a question related to presumed causal links in real-life interventions too complex to answer through survey or experimental research techniques (Baxter & Jack, 2008).

Limitations of the Case Study Approach:

Case studies can be susceptible to lack of rigor due to biased views being weighed too heavily by the researcher, resulting in a single opinion forming the basis of swayed results and conclusions. This risk is controlled for in this study by basing the report on official secondary data from various reputable sources to give as objective a view as possible within the scope of the research.

A second shortcoming of case study research is the inability to make generalisations about the population or universe in question from the chosen sample based on single case. The objective of a case study however, is not to generalize case findings to theoretical propositions. Likewise, the purpose of this report is not to concur or disagree with the hypothesis that increasing levels of foreign direct investment have a positive impact on socioeconomic conditions of host economies, but rather describe what the current dynamics are.

Research Method

Ghauri and Gronhaugh (2005) describe three categories of scientific research. These are exploratory, descriptive, and explanatory research. Exploratory research is conducted to provide a basic understanding of new phenomenon or issue about which there is little or no prior knowledge. The research design is not easily defined and may evolve as the researcher undertakes his/her study. Descriptive research aims to define the characteristics of situations and/or events through a qualitative or quantitative approach. Descriptive research aims to describe the nature of a relationship between two concepts. Explanatory research seeks to explain the existence of a certain relationship between phenomena, by trying to answer question of “why” and “how” certain phenomena are observed (Bhattacharjee, 2012).

This research report is designed to explain the current state of foreign direct investment in Zambia. Therefore, it takes the form of an explanatory research paper based on a qualitative approach in order to give insights into and understanding of the factors that affect the FDI origins, patterns, strategies and its impacts.

Data sources and collection method

Secondary Data

The main objective of this research report is to present a consolidated review of the current literature that details the current state of the Zambian foreign direct investment environment. To this end, secondary data is used to give reliable official accounts of the status of various aspects of the Zambian investment environment. By amalgamating a critical review of all the various sources, the researcher endeavours to give a multifaceted description of the subject matter.

Data Analysis Methods

This research report will be conducted using qualitative secondary analysis methods.

The general definition of secondary analysis given by Irwin and Winterton (2011) is “*the re-use of data produced on a previous occasion to glean new social scientific and/or methodological understandings*”. The authors also state that qualitative secondary analysis is a recognized research technique in quantitative research circles, and is gaining more traction in the qualitative research sector as well.

Some benefits of the use of qualitative secondary analysis noted by Irwin and Winterton include the ability to:

1. Evaluate the credibility of new research findings using existing established and proven data;
2. Complement existing primary data;
3. Provide context and historical background as a basis for further research;
4. Unearth new insights through analysis of prevailing data under a new or different research framework and;
5. Increase knowledge regarding remote populations or sensitive topics without having to disturb their natural state.

Validity and Reliability

The greatest care has been taken by the researcher in selecting reputable, official publications of the source data in an effort to avoid misrepresentation of the true state of affairs of the subject matter.

Limitations of the Research Paper

This research paper has been subject to a number of limitations. These include, amongst others, the time and cost implications of travelling to the state under review and collecting primary data. The researcher is also limited by the number and type of sources available to external members of the public.

Research Findings

Zambia as an Investment Destination

The World Bank (2014) Doing Business Report is published annually and benchmarks the relative ease of doing business amongst 189 countries worldwide based on the regulatory landscape of each country. According to the 2016 Doing Business report, Zambia ranks 97th out of 189 countries on overall ease of doing business. Although not exhaustive, the rating is based on ten categories of the business environment that policy makers can use to enhance the investment and business climate.

At a regional level, Zambia is the third highest ranked economy in Southern Africa behind Botswana (72) and South Africa (73), and fourth highest in Sub-Saharan Africa with Rwanda ranking first. Although the Zambian Government has made positive strides towards improving the regulatory environment to enhance the business environment, the Report cites that significant areas for improvement still exist. The country displays its lowest rankings in the areas of registration of property, cross-border trading (exports), and contract enforcement.

Zambia's investment climate is currently highly conducive to increased business activity due to a number of positive factors such as its strategic location, extensive natural resources, a young and growing labour force, and stable socio-political environment (OECD, 2011).

Zambia's unique location allows for easy access to large, growing untapped regional markets. The country shares borders with eight Southern African countries – Angola, Botswana, the Democratic Republic of Congo, Malawi, Mozambique, Namibia and Zimbabwe.

The country's membership to regional economic communities such as the 15-member Southern African Development Community and 19-member Common Market for Eastern and Southern African States gives it locational and trade preference advantages for export-oriented business.

As the region continues to solidify efforts to create a Free-Trade Area across all SADC, COMESA and East African Community nations, Zambia's locational advantage is set to only increase its competitiveness as an investment destination.

Zambia is naturally endowed with a wealth of resources comprising metals (copper and cobalt), precious stones (emeralds, amethyst, aquamarine, gold and diamonds), industrial minerals (iron and phosphate) agricultural land, building and energy minerals (marble, granite, clay, limestone, coal, and water). Of these resources, the most widely exploited is copper which forms the backbone of the Zambian economy. Zambia's copper mining and production industry makes the nation the world's seventh largest producer, and second largest in Africa. Foreign direct investment in the mining sector has been growing steadily since 2007, due to increases in international copper prices and output has risen steadily since (OECD, 2011; Zambia Development Agency, 2015).

Despite a vast abundance of economically viable resources, there still remains large scope for development of these resources. This provides considerable opportunities for potential investors with resource-seeking investment motives (Zambia Development Agency, 2015).

Although Zambia has a growing, young labour force, unemployment is rife and there is high demand for skilled and technical workers. Given this, investors can stand to gain from relatively lower labour costs in return for the transfer much-needed skills in the Zambian economy.

The political and regulatory environment has also evolved from a single-party to a multi-party democracy since 1991. The transition has been a peaceful one, as the country has not experienced any military coups, civil war, or prolonged protest action as a result. The Government of the Republic of Zambia has also taken policy steps to improve the economic environment through an extensive privatization program and various national development plans, in which diversification and investment promotion are key focus areas. These are discussed in further detail later in chapter.

Background to FDI in Zambia

Following its independence in 1964, the Zambian economy was centrally planned and all economic assets were held by the government. For the first decade post-independence, international prices of copper were on the rise, attracting sufficient flows of foreign reserves into Zambia to sustain spending in the paternalistic state. Thereafter, state-owned enterprises were subject to grave mismanagement and over indebtedness during the period 1974 - 1994 when international copper prices plummeted.

Due to the pressure faced by the government from international donors, significant policy changes began to be implemented in the 1990s, following the first democratic elections in 1991. In 1992,

the Zambian government undertook a privatization programme that encouraged an open trade regime (OECD, 2011). The policy reforms focused on privatization of state owned enterprises, removal of exchange rate and price controls, and trade liberalization (Bank of Zambia, 2014).

As a means to attract foreign direct investment, the newly formed democratic government embarked on an aggressive privatization programme from 1994 -2001 that saw sectors previously under the management of government sold to private investors. As a result of this, the majority of Zambia's parastatals were sold to foreign entities, thus the first substantial flows of FDI into the country took place (Bank of Zambia, 2014). When privatization programmes were first initiated, more than 80% of domestic firms were under state control. The first phase of divestment of nationalized firms involved the sale of smaller businesses to local private investors; hence the impact on FDI flows was negligible. As government divested larger firms to international investors, inflows of FDI into Zambia rose from US\$ 40 million in 1994 peaking to US\$ 207 million in 1997, remaining between US\$ 100 – 200 million p.a. from 1998 to 2000 (Zambian Development Agency, 2015:12). Most of the investment inflows into Zambia were directed to copper and cobalt mining, the agricultural and tourism sectors (UNCTAD, 2007).

Foreign direct investment inflows to Zambia have been dominated by the copper mining sector, especially during periods of rising international copper prices. The current focus of the Government of the Republic of Zambia is to encourage diversification away from mining into other priority sectors of the economy and increased local beneficiation of mineral resources. The policies and incentives implemented to bring this change about are discussed in the sections that follow.

Investment Policy Framework

Following the multi-party elections in 1991, the Zambian Government embarked on an extensive private sector development plan and economic liberalization programme. The sentiment driving this approach was to create an enabling economic environment for private sector participation – both foreign and domestic. This resulted in numerous significant reforms including the removal of price controls on domestic goods, removal of exchange rate controls, interest rate liberalization, privatization of state owned entities, consent for repatriation of profits by foreign companies, trade liberalization and removal of restrictions on import products (Bank of Zambia, 2014).

Alongside the rapid reforms came the creation of various institutions to promote and administer economic liberalization and encourage investment. These institutions were the Export Board of Zambia (“EBZ”), Zambia Privatisation Agency (“ZPA”), Zambia Investment Centre (“ZIC”), and the Small Enterprises Development Board (“SEDB”) and later on the Zambia Export Processing Zones Authority (“ZEPZA”) (Bank of Zambia, 2014).

Investment Promotion and Facilitation Policy Strategies

With the promulgation of the Private Sector Development Reform Programme (“PSDRP”) in 2004 – a policy initiative with the purpose of improving the investment climate, policy and regulatory framework in Zambia – a new investment agency, the Zambian Development Agency was formed. The ZDA was formed by integrating the institutions previously tasked with performing the separate investment-related goals of the Government i.e. the EBZ, ZPA, ZIC, SEDB and ZEPZA. The Act outlines the function of the ZDA to be *“to further the economic development of Zambia by promoting efficiency, investment and competitiveness in business and promoting exports from Zambia.”*(ZDA, 2015b)

The aim of the agency is to create a one-stop-shop for business registration that reduces the cost of doing business for local and foreign investors. Further, the ZDA Act gives powers to the agency to act in the advancement of trade development, investment promotion, enterprise restructuring, development of green fields’ projects, small enterprise development, trade and industry fund management, and skills training development (ZDA, 2015b).

The implementation phase of the PSDRP from 2006 to 2009 also brought about other positive policy changes such as the Citizens Economic Empowerment Commission; the approval of policies in Information Communication Technology (ICT) Policy, Energy Policy, Public Private Partnership Policy and Micro Small and Medium Enterprise Development Policy; the creation of the Public Private Partnership (PPP) Unit; and the establishment of a Credit Guarantee Scheme for Micro and Small Enterprises (NEPAD -OECD, 2011).

The PSDRP was extended to PSDRP II, which introduced more policies set to enhance the Zambian investment environment. The focus areas for PSDRP II concern the improvement of business licensing and regulatory framework; labour reform and labour productivity; and Private-Public-Partnership (“PPP”) development (NEPAD -OECD, 2011). Furthermore, more emphasis has been

put on the tourism, agriculture and manufacturing sectors. The implementation phase of PSDRP II is expected to run from 2009 -2014 (OECD, 2011).

This chapter discusses the various aspects of the investment environment and the applicable policies.

Market entry and Establishment of Operations

Local and international investors are required by the ZDA Act to submit to screening tests in order to acquire approval to invest. The application review process allows the ZDA to involve the Zambian Government in the evaluation of proposed investments to ascertain whether broad criteria such as promotion of economic development goals, employment, exports and transfer of technology can be attained through the proposed investments (UNCTAD, 2007).

The ZDA's application review process reverts to applicants within 14 days of the submission of investment license application. Rejected applicants have the option to appeal a decision of the Agency not to grant a license. Prospective investors who obtain approval are issued an investment license which is valid for ten years post-issuance. Successful applicants are those that can demonstrate that all legal and regulatory requirements for the investment have been met and that the said projects will yield positive developmental impacts as well as avoid harm to the environment (UNCTAD, 2007).

Access to Land

All administration and land policy enforcement lies with the Ministry of Lands. A Customer Service Centre has been established to provide foreign investors with information regarding land transactions, such as title deeds, qualification criteria, legal requirements etc.

The ZDA works alongside the Ministry of Lands as well as the Ministry of Agriculture and Cooperatives in the demarcation and reservation of land banks specifically earmarked for use by investors in the priority sectors. By December 2010, various farm blocks across 9 had been reserved for use by investors (NEPAD -OECD, 2011).

Industrial land has also been reserved for the creation of multi- facility economic zones ("MFEZs") and industrial parks for investment purposes (Engstrand, 2013). Special Economic Zones ("SEZs")

are defined by the World Bank as “*geographically delimited areas administered by a single body, offering certain incentives to businesses which physically locate within the Zone*”. In Zambia, these industrial zones are known as multi-facility economic zones described as “*special industrial zones for both export-oriented and domestic-oriented industries, blending the best features of the free trade zones (“FTZs”), export processing zones (“EPZs”) and the industrial parks/zones concept and create the administrative infrastructure, rules, regulations etc. that benchmark among the best dynamic economies*” (ZDA, 2015a).

To date, the ZDA has announced the development of six industrial areas earmarked as MFEZs, located in Chambishi, Lusaka East, Lusaka South, Lumwana, Ndola and Roma. Of these industrial zones, the Chambishi based Zambia–China Economic and Trade Cooperation Zone (“ZCCZ”) is the most advanced. The trade zone is anchored around a copper smelter and was commissioned in 2009 (UNCTAD, 2011).

This model forms one of the key strategic policy elements that the Government of Zambia is using to attract foreign investment into the country, and has thus far attracted significant interest and pledges from Asian trade partners like China and Japan (UNCTAD, 2011). This scenario is particularly beneficial for foreign investors, as it lessens the burden of locating suitable land for potential investment initiatives.

Competition Policy

The Zambian Competition Commission (“ZCC”) is an independent body brought into existence through the Competition and Fair Trading Act. The commission’s key responsibilities include the prevention of 1) the abuse of a firm’s dominant market position, 2) predatory behavior, 3) discriminatory pricing, 4) restrictive distribution and 5) collusion (UNCTAD, 2007).

The ZCC undertakes to find a balance between ensuring that no merger or acquisition results in a compromise of the country’s trade conditions and not allowing excessive administrative obstacles to inhibit the flow of FDI into Zambia. The Commission’s assessment is based on the 50% merger threshold in line with international standards. If a newly incorporated entity would have more than 50 percent of the market or if the new entity, together with two other existing firms in Zambia, would together have more than 50 percent of the Zambian market, the ZCC deems oligopolistic (UNCTAD, 2007).

The Commission plays a crucial role in the FDI sector of Zambia, as it is tasked with authorizing all mergers and acquisitions prior to their completion. Despite the fact that foreign investors prioritize obtaining an investment license from the ZDA for entry into the Zambian market, those international investors whose strategy is a merger or an acquisition of existing Zambian firms, ZCC approval is paramount.

Dispute settlement

As a signatory to the 1958 New York Convention and member of the International Centre for the Settlement of Investment Disputes (“ICSID”), in cases of international arbitration all resulting arbitral awards are binding and enforceable in Zambia. Apart from being a member of the ICSID, Zambia is also a member of the World Bank’s Multilateral Investment Guarantee Agreement and the African Trade Insurance Agency, as well as and the United Nations Commission of International Trade Law (UNCITRAL). Within Zambia, the 2000 Arbitration Act covers domestic arbitration cases (UNCTAD, 2011).

Investment Potential and Opportunities

Zambia's abundant natural resources, stable political environment and strategic location give the country a natural advantage against neighbouring countries within the region. This section details the various sectorial, economic and other factors that make Zambia a favourable foreign investment destination.

Mining, Metals and Minerals

Resource-based activities have been the foundation of Zambia's economy for decades. Despite this, there still remains a vast array of untapped resources available to draw further FDI into the country.

Copper: Zambia's biggest export commodity and foreign exchange earner has a long been in operation; nevertheless there still remains an abundance of copper deposits being discovered. New copper deposits have been identified, like in the Lumwana and Kanshanshi regions of the north-western province. Existing mines also have potential for further output, given that sufficient capital can be raised to exploit the reserves. With international copper prices rising during 2002-2005 foreign investment in the sector increased, expanding copper production alongside growing international demand. Thus, the copper mining sector has the potential to continue bringing flows of FDI into Zambia (UNCTAD, 2011).

Gemstones: Zambia holds a wealth of precious and semi-precious stones. It has the world's second largest reserves of emeralds, and Africa's largest store of tourmalines, aquamarine and amethyst. Other gems include garnet and malachite. Due to the amount of attention and investment directed to the copper sector, gemstones have been left largely untouched. Increased foreign investment in mining has the potential to increase Zambia's profile as a renowned international supplier of gemstones, given that policy, institutional, and infrastructural framework is conducive (UNCTAD, 2011).

Manufacturing

Zambia has numerous opportunities in both upstream and downstream activities across a number of industries, mainly stemming from the fact that it has many natural resources that are key inputs

into various manufacturing processes. Commodities such as cotton, copper, and various agricultural products can be a comparative advantage for Zambia versus neighbouring countries in attracting FDI.

Textiles: In 2007, Zambia was the world's 24th largest cotton exporter. Cotton exports are predominantly in raw form, and have been increasing in value from the year 2000. The biggest export markets for Zambian raw cotton are South Africa, Mauritius and East Asia (ZDA, 2014).

The high availability of cotton gives Zambia a comparative advantage in the manufacture of textile products. This advantage has not been used due to the lack of investment in the sector.

Copper products and mining services:

Despite having a thriving mining industry, copper processing and beneficiation is still relatively small-scale and downstream operations are limited to the production of unwrought metals, copper wires and cables. World demand for copper products is robust and forecasts show that this trend will remain positive for the foreseeable future; hence investment in the sector can reap significant returns (UNCTAD, 2011).

Agro-processing:

“The potential for agro-processing industrial development in Zambia is largely associated to the relative abundance of agricultural raw materials and low-cost labour. The most suitable industries therefore are those that make intensive use of these abundant raw materials and unskilled labour” (ZDA, 2014).

Currently, agro-processing is mostly limited to sugar refining, cotton ginning and spinning of yarn cotton, and drying of paprika for exports. There is considerable scope for increasing sugar production and expanding the range and improving the quality of sugar products. Presently, South African sugar company Illovo, along with some minority foreign partners is the main sugar producer, with approximately 65% being sold domestically and the balance exported through the region (UNCTAD, 2007).

Agriculture

Zambia has an estimated 74 million hectares of arable land, yet only approximately 14% of suitable land is currently in use for agricultural purposes. Moreover, Zambia has ample fresh water supply that can be used in irrigation systems. Zambia's attractiveness for agricultural FDI has increased since the early 2000s' resulting in the growth of horticultural and floricultural products. The Government of Zambia has already developed plans to reserve 1 million hectares of land separated into nine blocks across the country for cultivation and investment, and development (UNCTAD, 2007). These developments within the agricultural make this sector attractive for foreign investors at this time when food security in Southern Africa and internationally become increasingly serious problems.

Services

Tourism: Zambia is home to many tourist attractions that lie in rural areas. Investment in this sector has the ability to unlock much needed jobs and industrial activity to lower-income areas of the country. The potential of this sector is limited by lack of supporting services such as access roads, electricity, telecommunication facilities and airline connections to main tourism markets which is where FDI can play a crucial role (UNCTAD, 2011).

Infrastructure services:

A large number of the contributing factors why FDI inflows into Zambia have not reached their highest potential are due to a dearth in the economic infrastructure. Telecommunications, water, electricity and transport services are strategically important for any country's diversification and growth strategy. These elements of the economy have the power to significantly increase the supply capacity of all industries and act as a catalyst to unlocking the economic potential of natural resources already abundant in supply.

Apart from the Zambia Railways which is run under a concession and the liberalization of the cellular phone industry, all infrastructure services are provided by state owned enterprises, the majority of which are reported to be subject to poor management, weak financial practices, and uncompetitive offerings. Privatization of infrastructure services such as the provision of road

infrastructure, hydropower, and water services can unlock a considerable amount of FDI into Zambia (UNCTAD, 2007).

Investment Incentives

In an effort to stimulate economic diversification away from traditional mining exports, the ZDA Act offers distinctive incentives to investors. Investors qualify for fiscal and non-fiscal investment incentives based on a minimum investment amount and the particular sector or product to be invested in. The priority sectors include agriculture and agro-processing, information and communication technology, health, education and training, manufacturing and tourism (see Annex 1 for full list). Below is a description of the main fiscal and non-fiscal incentives that are applicable to the major sectors of the Zambian economy available to investors who invest a minimum of US\$500,000 in a Multi Facility Economic Zone (“MFEZ”), an Industrial Park, a Priority Sector and invest in a Rural Enterprise under the ZDA Act have access to the following financial and non-financial incentives.

Financial Incentives: Tax

Tax incentives differ for mining and non-mining industries. The table below describes the tax allowances applicable to corporates operating in Zambia.

Corporate Taxes	General	Mining	Agriculture & Non-traditional Exports	ZDA Incentive for Foreign Investors
Income Tax	35%	30%	10-15%	0% - for 5years 50% of Tax rate year 6-8 75% of tax – year 9-10 Full tax – year 11 onwards
Variable Profit Tax	15% on profits exceeding 8% of turnover	15% on profits exceeding 8% of turnover	15% on profits exceeding 8% of turnover	15% on profits exceeding 8% of turnover
Mineral Royalty Tax	3%	3%	3%	3%
Withholding Tax on Dividends	15%	0%	15%	
Value-added Tax	16%	16%	Option to defer on capital equipment and machinery	
<u>Import Duties:</u>				
Capital goods and raw materials	0-5%	0-5%	0% on capital goods, machinery and equipment for 5 years	
Intermediate goods	15%	15%		
Finished goods	25%	25%		
Export Duties	Export duty is exempt on all products produced for export with the exception of Copper concentrates (taxed at 15%), Cotton seed (20%) and Scrap metal (taxed at 25%).			

Table adopted from OECD Investment Policy Review of Zambia 2011

Non- Financial incentives:

Investors whose investment equal or exceed US\$250,000 in any sector or product not provided for as a priority sector or product are entitled to the following rights under the ZDA Act:

Repatriation rights: The ZDA Act provides guarantees for rights of repatriation with respect to profits, debt service, fees, royalties and divestment proceeds(UNCTAD, 2007).

Administrative assistance: International investors in priority sectors have access to services such as application of immigration permits, secondary licenses, land acquisition and utilities free of charge.

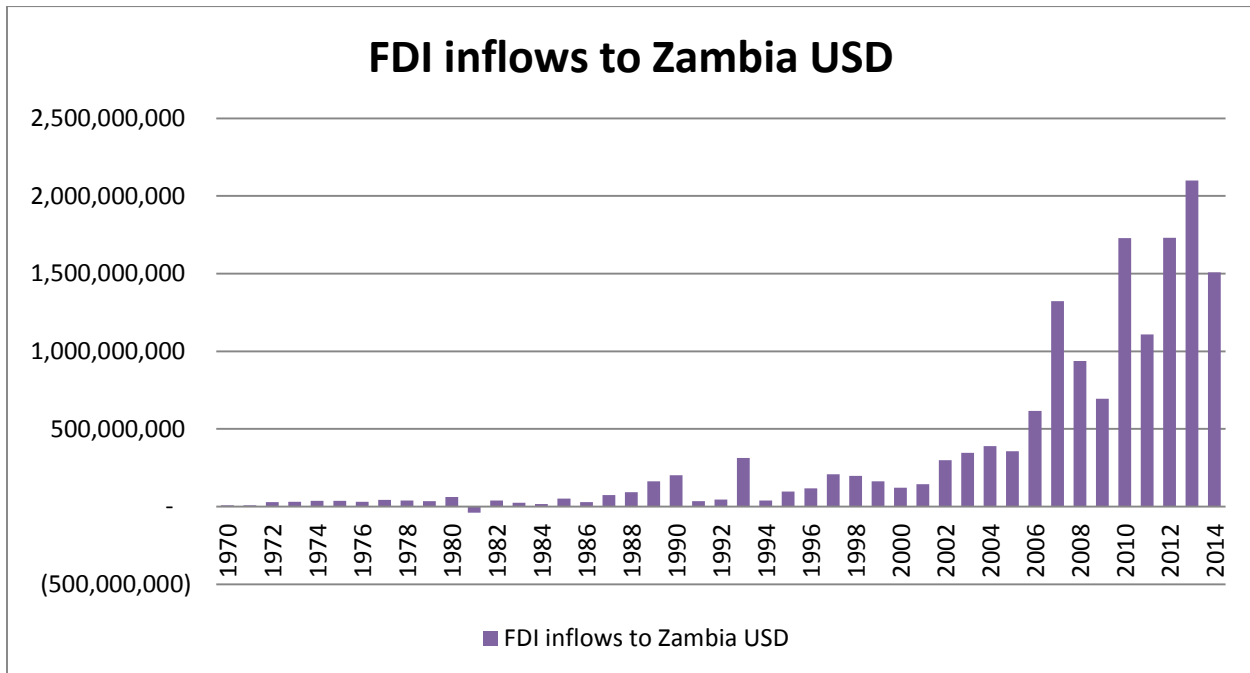
Investment Guarantees and Protection of Property Rights:

The ZDA Act contains specific clauses for the protection of property rights of investors. These provisions state that investments can only be expropriated by an Act of Parliament relating to the specific property expropriated. In this instance, full compensation must be made at fair market value, convertible at the prevailing exchange rate. Land, which foreign investors are permitted to hold under 99-year leases, may in turn revert to the government if it is ruled to be undeveloped (NEPAD -OECD, 2011).

The Ministry of Commerce, Trade and Industry and the Patents and Company Registration Agency (“PACRA”) are the foremost institutions in the design and implementation of intellectual property laws. Extensive work has been undertaken to update and align Zambia’s intellectual property legislation to international standards. Consequently, the Intellectual Property Rights Policy and its implementation plan, aimed at merging Intellectual Property and Copyrights Laws, were launched in 2010. These measures are expected to improve the environment required by the private sector in order to foster creativity and innovation (NEPAD -OECD, 2011).

FDI Trends and Impacts

Trends



Adapted from World Bank World Development Indicators Data, 2015

One noticeable element concerning the overall trend of FDI inflows to Zambia is that foreign investment is on the rise. Various reasons can be attributed to each of the leaps in investment. From the 1970s through to 2000, foreign investment was driven by international copper prices – a rise in copper prices meant foreign investors were willing to increase their funding of copper mining activities within Zambia, and vice versa. This trend is still very dominant within the Zambian economy today.

The first significant change in the FDI landscape came about in the 1990s when economic liberalisation, privatization and removal of exchange controls began the wave of denationalization of state-owned assets. A decade later in 2003, the copper price boom brought in a large wave of FDI directed into the copper mining industry. From 2005, domestic and international factors worked simultaneously to support the upward trend in FDI flows. Firstly, the promulgation of Zambia's Private Sector Development Reform Programme in 2005 provided a more supportive legislative climate and secondly, the increase in demand for copper and copper products from Asian countries sustained the trend into recent times. This increasing trend has been disturbed by

the global financial crisis of 2008 and some projects have been delayed, and others abandoned as a result(Bank of Zambia, 2014).

Although the overall trend if FDI inflows in Zambia is upward, the country lags behind regional neighbours in terms growth in FDI flows compared to population and GDP growth. This signals an untapped potential to increase FDI flows to be in line with the rest of the economy.

Sectorial

Until recently, more than 50% of all foreign investment into Zambia was in the copper mining sector or supporting industries. Therefore, the pattern of FDI flows in the country is heavily indexed on activity within the copper mining sector, more specifically the international price of copper (UNCTAD, 2007). Unfortunately, there is very little historical data on the sectorial split of foreign investment inflows available. For this section a snapshot of FDI by sector is presented for different points in time in order to illustrate the shift in sectorial split of FDI inflows into Zambia.

Top 5 FDI attracting sectors in the Zambian economy

Rank	Sector	% of total FDI Invested 2007	Sector	% of total FDI Invested 2011	Sector	% of total FDI Invested 2013
1	Mining and Metals	59%	Mining and Metals	86.2%	Mining and Metals	65.5%
2	Financial Sector	8.4%	Wholesale/retail trade	6.9%	Manufacturing	21.2%
3	Manufacturing	8.2%	Financial sector	6.4%	Financial Sector	10.6%
4	Wholesale/retail trade	6.1%	Real Estate	3.9%	Agriculture	4.1%
5	Transport and Communication	5.1%	Information and Communication Technology	3.8%	Wholesale/retail trade	1.4%

Statistics provided by the Bank of Zambia

The above table illustrates that FDI has become slightly more diversified. Although not clearly deducible from the above, sectors such as power, manufacturing, coal oil, and natural gas are

attracting an increasing amount of investment into the country. It is also important to note that a snapshot view of the distribution of FDI by sector is heavily influenced by economic conditions at a certain point in time. For Zambia, these influences include the international copper price as well as rainfall pattern for the period. These factors are direct influences on the country’s largest industries – mining and agriculture.

FDI source countries

There is a link between which countries invest in Zambia and the sectorial distribution of FDI flows. Most FDI in Zambia is resource seeking in accordance with the demand for a certain resource in any particular country. As a result, the top FDI providers are highly correlated with the highest FDI attracting sectors. Demand for copper in China, Canada and the United Kingdom influence the large amount of FDI in the mining sector. India’s search for coal, oil and gas has led to it being the largest provider of FDI in this sector. FDI directed to the financial sector is dominated by South African institutions as they increase their footprint in the African continent. Chines and Indian firms are also very active in the Zambian alternative energy space (Ernst & Young, 2012).

There has been a visible shift in the composition of Zambia’s foreign investors. Historically, so-called first world nations have been the main providers of foreign investment into Zambia. However, this trend is changing as more emerging market investors are investing into operations in Zambia.

Rank	Top FDI Investors 2007	Top FDI Investors 2010	Top FDI Investors 2013
1	Australia	Australia	United Kingdom
2	Canada	Canada	Switzerland
3	India	United Kingdom	China
4	Switzerland	South Africa	South Africa
5	United Kingdom	British Virgin Islands	Australia

Statistics provided by the Bank of Zambia

Impacts

Despite the fact that notable strides have been made in increasing the flow of FDI into Zambia, there are conflicting views on whether the impact of the increase in FDI has been for the good of the Zambian economy as a whole. This section explores the impact of FDI on a number of aspects of the Zambian investment environment.

Skills/knowledge transfer: Although minimal at an economy level, skills transfer in the agriculture and hospitality industries has made a significant difference in the quality of output and service. The entry of international hotel brands into Zambia has resulted in many hospitality staff being trained to international levels of performance. The Natural Resource Development College/Zambia Export Growers' Association ("NRDC/ZEGA") is an institution founded by foreign investors alongside the Zambian Government that trains local farmers on the safe and effective use of chemicals in their farming processes, with specific emphasis on environmentally friendly practices (UNCTAD, 2007).

Diversification of economy and non-traditional exports: Increased foreign investment in the economy has been partly responsible for the increase in the growth of non-traditional exports such as horticultural products, cotton, tobacco, non-copper mining, telecommunications and tourism (OECD, 2011).

Development of local business: The extensive amount of incentives awarded to foreign investors have resulted in local businesses struggling against the high cost of large capital outlays and hefty tax burdens which foreign investors are not subject to in the first 10 years of operation. The cost of these incentives to Government of Zambia should be recoverable through the increased taxable earnings of Zambians, which has not been directly observable thus far (UNCTAD, 2007).

Creation of employment: Increased FDI inflows to Zambia have had minimal overall impact on levels of unemployment in the economy. Foreign investors cite that human capital in Zambia is expensive to train and strict labour laws increase the cost of labour, hence many international firms employ expatriates in technical and managerial roles (OECD, 2011).

Barriers to FDI accumulation in Zambia

Despite having made significant strides in growing the level of FDI inflows, there remain factors that are significant barriers to Zambia realizing its economic potential through rising FDI.

- i. Low productivity and high cost of labour: Zambia's labour force is highly unionized, poorly skilled and productivity is low relative to other developing markets. The majority of the population lacks the adequate technical and managerial skills required to work in international firms, which also limits the capacity of the labour force to absorb the technological and skills transfer spillovers from foreign investors. Strict labour laws also add to the cost of labour borne by foreign investors (UNCTAD, 2011).
- ii. Limited access to and high cost of finance for local investors: Although Zambia has numerous incentives in place to encourage foreign investors to set up operations in priority sectors, local investors struggle to compete due to a lack of funding. Increased local economic activity increased the potential of a country to attract FDI. Zambian businesses are forced to borrow from international banks, making them susceptible to high interest rates and exchange rate fluctuations (UNCTAD, 2011).
- iii. Infrastructural backlog: Zambia has a lack of adequate access roads between rural and industrial areas, and surrounding export markets. Less than 20% of the population has access to electricity and water resources are largely underutilized. All these factors work together to increase the cost and complexity of doing business in any economy (UNCTAD, 2011).
- iv. Underdeveloped sectors: Zambia has a wealth of underutilized natural resources that can be developed into thriving industries. The gemstone sector has been highly neglected, alongside tourism, hydropower and infrastructural services to name a few high impact industries. As local firms make use of these resources, it demonstrates the untapped potential of the sectors, spurring further investment interest from abroad (UNCTAD, 2011).
- v. Small domestic market: Although Zambia is strategically located next to large and growing markets in East and Southern Africa, the country itself has a small, underdeveloped domestic market in which poverty is rife. In order to spark foreign investor interest in the country, a growing and active market must be created where citizens have sufficient buying power to increase local demand for goods and services being offered by international firms.

Conclusions and Recommendations

The purpose of this report was to give an overall description of the current themes in the Zambian investment climate with specific reference to foreign direct investment activity. The discussion detailed the various elements at play in the economic, political and legislative spheres and how these affect the trend in FDI inflows over time and across sectors.

The main findings of the research are:

- i. FDI inflows have displayed an upward trend overall, however the rate of increase in FDI is not in line with population and economic growth, thus the spillover effects have the potential to be greater than currently observed. Historically, the increase in FDI inflows has been heavily indexed on the copper mining sector and supported by privatization policies. These factors are still strongly influential in the Zambian economy today.
- ii. Despite reporting increasing GDP figures throughout the past decade, growing FDI inflows have had minimal impact on the overall socioeconomic status of Zambian citizens. The majority of the population still lives in poverty, with no access to electricity or water.
- iii. Most of the FDI inflows into Zambia are resource seeking and this fact is also connected to the countries of origin from which FDI flows. It is based on this that over time, one can observe that first world nations such as Canada and the United Kingdom have decreased in share of Zambian FDI inflows and have been surpassed by developing nations such as China.
- iv. FDI in Zambia has historically been concentrated in the copper mining and minerals sector. Over the last decade, the manufacturing, financial and wholesale/retail trade sectors have increased their share of FDI flows through incentives given by the Government for investments in non-traditional export sectors. This has led to the diversification of the economy's income to a certain degree, yet more can be done to reduce the country's dependence of copper mining revenue.
- v. Policy initiatives to attract foreign investment have assisted in diversifying the economy through the growth of non-traditional exports, yet there remains more opportunity to augment this growth through the effective use of natural resources such as gemstones and cotton.

- vi. Despite a positive trend in the growth of FDI in Zambia, major constraints remain that need to be addressed. These include low productivity and high cost of labour – due to lack of technical and managerial skills within domestic workforce, limited access to and high cost of finance for local investors, high infrastructure backlogs, unexploited potential in various sectors for which natural resources are abundant, as well as a limited domestic market for the consumption of locally produced goods and services.

Recommendations

Based on the investigation and critical review of the current literature concerning the Zambian investment environment, the following recommendations are put forward.

- i. Low productivity and high cost of labour: To assist in addressing the skills shortage of the Zambian workforce whilst maintaining operational efficiency of the firm, partnerships between public sector training centres and foreign firms should be established in order to facilitate knowledge and skills transfer to citizens. In this manner, institutions train students to the level of expertise and productivity required by foreign firms and locals are eligible to be employed in multinational corporations.
- ii. Limited access to and high cost of finance for domestic firms: A thriving domestic market not only attracts foreign investment, but also increases employment rates and alleviates poverty. The Zambia Development Agency has played a key role in empowering small-to-medium enterprises to this end. However, uniting efforts with development finance institutions will streamline the finance process for local businesses, enabling them to compete alongside foreign firms as well as provide goods and services to these firms.
- iii. Provision of infrastructure services: The provision of basic services such as electricity, water and sanitation should be privatized or provided through concessionary models in order to increase operational efficiency, reduce costs and increase competition. Public Private Partnerships can also be utilized in the provision of road, energy and telecommunications services.
- iv. Underdeveloped sectors: It is recommended that Zambian authorities give qualifying local small- medium entities incentives to start operations in previously unexploited sectors, as such activity creates markets for goods previously not available, which attracts foreign investors to want to partake in these sectors as well.
- v. Small domestic market: Income earned by individuals and firms drives the demand for goods and services within an economy, which stimulates the need for more productive capacity. As Zambia is a relatively small market, it should make full use of its locational advantages and regional trade agreements to foster an export led market and become a productive hub within the SADC and COMESA regions.

Limitations of the research

The scope of this research report was limited by a number of factors. These include, amongst others, the time and cost implications of travelling to the state under review and collecting primary data. Due to time constraints, the scope of the research paper was limited to a critical review of secondary data. The researcher was also limited by the number and type of sources available to external members of the public.

Areas for Further Research

The issues highlighted in this report give way for further research in other areas of the Zambian (or other) investment environment. The topics for further research emerging from the above analysis include:

- i. There currently exists no cost-benefit analysis of the incentives used by governments to attract foreign investment. This is an opportunity to investigate the real cost of financial and non-financial investment incentives.
- ii. Privatisation is one strategy that can attract large amounts of foreign investment into an economy. It would be noteworthy to understand what the determinants of successful privatization strategies are.
- iii. Many African countries are rich in precious mineral resources; however the net benefit from these resources is seldom realized within the borders of the resource-bearing country. How to leverage abundant natural resources (and other comparative advantages) through foreign direct investment for the maximum benefit of the host country and foreign investor.
- iv. Despite an increase in FDI inflows, Zambia's population is largely poor. This warrants an consideration of the roles and responsibilities of foreign investors: does FDI imply an onus of social responsibility?

Annexure 1 – ZDA Priority Sectors

- (a) Floriculture fresh flowers and dried flowers
- (b) Horticulture fresh and dried vegetables
- (c) Processed foods wheat flour other processed foods
- (d) Beverages and stimulants
 - (i) Tea and tea products
 - (ii) Coffee and coffee products

- (e) Production and the processing of the following products in the textile sector
 - (i) Cotton
 - (ii) Cotton yarn
 - (iii) Fabric
 - (iv) Garments

- (f) Manufacturing of the following engineering products
 - (i) Copper products
 - (ii) Iron ore and steel
 - (iii) Cobalt
 - (iv) Other engineering products

- (g) Beneficiation of phosphates and any other related material into fertilizer
- (h) Beneficiation of rock materials into cement
- (i) Production and processing of raw timber into wood products
- (j) Production and processing of the following products in the leather sector:
 - (i) Cattle hides
 - (ii) Crust leather
 - (iii) Leather products

- (k) Building of mini-hydro power stations
 - (i) Education and skills training

MFEZ Priority Sectors are:

(a) Information and Communication Technology (ICT)

- (i) Development of computer software
- (ii) Assembly/manufacture of ICT equipment

(b) Health

- (i) Manufacture of pharmaceutical products;
- (ii) Repair and maintenance of medical equipment;
- (iii) Provision of laundry services to medical institutions;
- (iv) Ambulance services;
- (v) Medical laboratory services;
- (vi) Diagnostic services; and
- (vii) Other medical services.

(c) Education and skills training

(d) Manufacture of:

- (i) Machinery & machinery components
- (ii) Iron & steel products
- (iii) Electrical and electronic products & components & parts thereof;
- (iv) Chemicals & petrochemicals
- (v) Pharmaceutical & related products
- (vi) Wood & wood products
- (vii) Palm oil & their derivatives
- (viii) Pulp, paper & paper board
- (ix) Textile & textile products
- (x) Transport equipment, component & accessories
- (xi) Clay-based, sand-based & other non-metallic mineral products;
- (xii) Plastic products
- (xiii) Professional medical, scientific, & measuring devices/parts
- (xiv) Rubber products

- (xv) Leather & leather products
- (xvi) Packaging & printing materials
- (xvii) Fertilizer
- (xviii) Cement

(e) Tourism

(f) Processing of:

- (i) Agricultural products
- (ii) Forest products
- (iii) Non-ferrous metals & their products
- (iv) Gemstones

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