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FOREIGN DIRECT INVESTMENT IN THE MANUFACTURING SECTOR IN BOTSWANA : KEY DETERMINANTS AND DETERRENTS.

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Declaration

I would like to declare that this dissertation is my own original work, produced by my own efforts apart from the assistance received from my supervisor. All sources of information have been fully credited and acknowledged.

I also declare that this thesis has not been, and will not be presented to any other university for any other degree.

Signed by candidate

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Date

This research paper has been submitted for examination with my approval as the supervisor.

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ABSTRACT

There is considerable controversy on the role and impact of foreign direct investment (FDI) on economic growth in developing countries. Empirical studies show inconclusive results. For countries that rely heavily on a single commodity for the bulk of their export revenue, foreign investment is seen as a means by which export diversification can be promoted. Botswana relies heavily on diamond exports and the government has long realised the need for economic diversification. Measures which have been put into place to diversify the economy include a range of policies aimed at promoting sectors such as manufacturing, agriculture, financial services, tourism and construction.

An investigation of whether the government's initiatives to diversify the economy are bearing fruit is thus necessary. This study attempts such an analysis by focusing on developments in the manufacturing sector. It examines the role and impact of FDI in Botswana's economy by investigating the pattern of investment and export behaviour of the country's foreign-owned manufacturing firms. More specifically, the factors that hinder or encourage FDI in the country are also investigated. The study uses survey and secondary data to examine these research problems.

The findings from the survey data reveal that there is hope for the manufacturing sector in Botswana. The sector can become more export-oriented if problems like low labour productivity, the shortage of skilled labour and high interest rates charged by financial institutions can be attended to. In addition, foreign investors interviewed also felt that government incentives, particularly financial ones, primarily benefit citizen or domestic firms. The major policy recommendations that emerge are that the government should continue to encourage foreign direct investment as foreign firms are employment generating. Also, government should continue to promote the manufacturing sector and other non-mining sectors to diversify the country's production base. Moreover, incentives geared towards foreign investors, particularly exporters should be introduced.

Chapter One provides an outline of Botswana's economy with emphasis on the country's dependence on the mineral sector. The rationale of the study, data problems and sources are also outlined in the chapter. *Chapter Two* reviews the literature on the subject of FDI and economic growth; and on exports and economic growth. It is argued that the literature reaches mixed conclusions regarding the impact of FDI on economic growth. *Chapter Three* provides an overview of the Botswana's manufacturing sector and the trends of FDI inflows to the country. Using secondary data from the World Investment Report (2001) and Central Statistics Office (Botswana), it is concluded that economic growth can only be enhanced if more foreign firms geared at exporting their products can establish themselves in the country. *Chapter Four* presents the results of the survey of foreign-owned manufacturing firms and, finally, *Chapter Five* concludes the study and presents policy recommendations.

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Chapter One: Objectives and Scope of the Study

1.1 Introduction

The development of the manufacturing sector is viewed as a source of employment growth and export revenue by many developing countries. For countries, that rely on a single commodity for the bulk of their export revenue, the manufacturing sector also potentially holds the prospect of economic diversification. In their efforts to develop the manufacturing sector, therefore, many developing countries are trying to attract foreign investment.

There is, however, considerable controversy on the role and impact of foreign direct investment (FDI) on economic growth in developing countries. Empirical studies have found that FDI can have both negative and positive effects on economic growth. Some studies argue that FDI can be bad for economic growth, if it is a substitute for domestic saving in the recipient economy. Others argue that governments should be cautious about promoting FDI because it increases competition in the recipient economies leading to the displacement of domestic firms by foreign firms. This argument is supported by de Mello (1997:23) who states that,

> "foreign firms can dominate the market by imposing product differentiation and reaping the benefits of extensive economies of scale to drive their domestic counterparts out of business".

A counter argument is that this competition is good because it removes inefficient firms from the sector and encourages efficient firms to become more efficient by investing in both human and physical capital.

This paper examines foreign investment in the manufacturing sector in Botswana. Particular attention is paid to the problems faced by manufacturing firms and the factors affecting investment in Botswana. In addition, the pattern of export behaviour of foreign-owned manufacturing firms is investigated.

1.2 Rationale of the Study

The mining sector is the largest contributor to Botswana's economy and the country has relied on FDI for the development of its mineral resources. A large proportion of FDI goes to the mining sector, with the trading sector (retail and wholesale) being the second most important recipient (Basu et al., 2002). While the mining sector will continue to play a significant role in the economic growth of Botswana, there are naturally concerns about the depletion of diamonds which are a non-renewable resource. Moreover, the country cannot rely on the mining sector alone because of the instability in the world market for diamonds and other commodities. For instance, fluctuations in diamond prices in the years 1992 to 1994 led to a fall in export earnings and economic growth rates. In addition, the mining sector makes a limited contribution to employment because the sector uses highly capital intensive technology and no new significant deposits have been discovered.

The government of Botswana is, therefore, anxious to promote other sectors to generate further growth. One of the alternatives being pursued by the government is to attract foreign investors into the country so as to diversify the country's production base. Examples include, establishing the country as an International Financial Services Centre; the policy of the privatisation and the objective of making the manufacturing sector more export-oriented. Given the country's increasingly serious unemployment problem and limited agricultural potential[1], the government has realised that the growth of sectors such as manufacturing is essential for employment growth and export revenue. The expansion of the manufacturing sector mostly depends on foreign investment because Botswana does not have the required entrepreneurial skills. In addition, the small size of the domestic market compared to regional and international

[1] The unemployment rate was 19.6% in 2001 while the potential of the agricultural sector is limited in the sense that the structure of the economy has shifted from being agricultural to mineral led. For example, agriculture shrank from 42.7% of GDP in 1966 to 2.6% in 2000/2001 while mining expanded from 17.5% of GDP in 1975/1976 to 36.5% in 2000/2001. Source : Botswana National Development Plan 9.

markets means that the manufacturing sector must be export oriented, if it is to grow rapidly.

As mentioned by Kumar (1995), export-oriented FDI can help host countries expand their manufactured exports. The theme of the country's eighth National Development Plan (NDP 8), which ended in March 2003, was "Sustainable Economic Diversification" while NDP 9, which started in April 2003, is based on the theme "Towards Realisation of Vision 2016: Sustainable and Diversified Development through Competitiveness in Global Markets". In this regard, it is expected that the growth of the manufacturing[2] sector and especially exports of manufactures will play an important role in economic diversification and employment creation, (Jefferis, 1997). A counter argument is that FDI may be restricted to a particular industry like manufacturing, which is export-oriented in nature but without growth-generating productivity spillovers to domestic firms (de Mello, 1997).

The Botswana government is currently offering incentives to foreign investors to stimulate the inflow of FDI into the country. Moreover, Botswana enjoys political stability and it has completely liberalised its exchange controls. According to Amuedo-Dorantes et al. (2001), FDI can be sensitive to foreign exchange uncertainty and political stability. However, according to Borensztein et al. (1995), various distortions, for example, protectionist trade policies, may jeopardize the role of FDI as a means for advanced technology transfer and the effect of these policies may be a flow of FDI that does not respond to higher efficiency, but only to profit opportunities created by distorted markets. Moreover, Mbekeani (1997) has argued that the mechanisms[3] by which FDI promotes economic growth are generally non-existent in developing countries. Conditions necessary for FDI to promote economic growth have, therefore, not been extensively researched. Hence, the need to establish the situation for Botswana.

[2] The government has also been trying to promote other sectors like agriculture, financial services, tourism and construction.
[3] For example, de Mello (1997) argues that knowledge and technology transfers are expected to be the most important mechanisms through which FDI promotes economic growth in the host country.

The objective of the thesis, therefore, is to:

1. Study Botswana's manufacturing sector with a view to investigating the pattern of investment and export behaviour of foreign-owned manufacturing firms.
2. Establish the factors that hinder or encourage FDI in Botswana.
3. Establish whether foreign firms have any growth-generating spillover effects on the economy of Botswana.

1.3 Data Sources and Problems

Initially, the intention was to analyse the relationship between FDI and economic growth, with emphasis on the manufacturing sector using both regression analysis and a survey of foreign-owned manufacturing firms[4]. However, there was inadequate data on aggregate FDI inflows from sources like the Bank of Botswana and the Central Statistics Office (Botswana). Due to this limitation, the study had to rely on survey data to investigate the pattern of investment and export behaviour of the country's foreign-owned manufacturing firms.

One of the main aims of this survey was to establish factors encouraging and constraining FDI. Jefferis (1997)[5] undertook a similar survey in March 1996. The current survey, therefore, allows for comparisons to establish if the manufacturing sector's performance is improving or not. Moreover, this study has a larger sample size compared to Jefferis (1997)'s study and a questionnaire was used to administer the survey.

[4] The idea was to use the Ordinary Least Squares approach to provide the macroeconomic evidence while the firm survey would provide microeconomic evidence. The advantage of using these two methods would have been that firm-level studies of particular countries often find that FDI does not promote economic growth, while macroeconomic studies often suggest a positive relationship between FDI and economic growth. However, the use of the survey method alone can provide useful insights.

[5] The objective was to assess the factors that had led to the success of some of Botswana's larger export manufacturing firms, with the purpose of replicating them to the manufacturing sector as a whole.

Chapter Two: The Relationship between FDI and economic growth

2.1 Introduction

Many cross-sectional and country specific studies have been undertaken to assess the relationship between FDI and economic growth. The relationship between exports and economic growth has also been extensively analysed. Empirical studies show both negative and positive effects of FDI on economic growth whilst some studies show that FDI has no significant impact on economic growth. Similarly, for the analysis of the impact of exports on economic growth, the results are inconclusive. While many studies show positive effects of exports on economic growth others show insignificant results. This chapter introduces an analysis of the relevant literature on the subject matter of FDI.

2.2 FDI and Economic Growth

According to economic theory, FDI can impact on growth in a number of ways. The impact can be through capital accumulation in the recipient economy encouraging the incorporation of new inputs and foreign technologies. This will increase the productivity of domestic firms. Secondly, through labour training and skill acquisition, and through the introduction of alternative management practices and organisational arrangements, FDI can augment the existing stock of knowledge in the recipient economy. In this way, productivity in the recipient economy can be stimulated and, as a result, FDI can be viewed as a catalyst for domestic investment and technological progress. Other potential benefits from FDI include market access which gives a country the freedom to sell its products to a given region or market and foreign exchange gains. In summary, it can be argued that FDI affects growth directly by increasing the stock of physical capital in the recipient economy and, indirectly, by promoting human capital development and technological upgrading (de Mello, 1999).

Developing countries lag behind the technology frontier when compared to developed countries. Hence, these "countries need to rely on inflows of foreign technology, as well as indigenous research and development (R&D)" (Saggi, 2002: 351). Absorption of foreign technology can be enhanced by increasing the stock of human capital of the recipient economy and by abolishing the various constraints faced by entrepreneurs. For example, countries such as Korea and Japan invested heavily in improving their stock of human capital and as a result they successfully absorbed foreign technologies.

Spillover benefits from technology introduced by foreign firms can occur in a number of ways. Local firms may adopt technologies introduced by multinational firms through imitation. Moreover, labour turnover may result in the diffusion of technology because workers trained by multinational firms may transfer information to local firms by switching employers, or may contribute to technology diffusion by starting their own firms. However, local firms may also be expected to suffer from increased competition when multinational firms enter the sector.

Most studies argue that FDI promotes economic growth by interacting with the human capital of the host country. For instance, Borensztein et al. (1995) argue that the recent growth literature highlights the dependence of growth rates on the state of domestic technology. They argue further that, in the case of developing countries, the higher efficiency of foreign investment results from the combination of advanced management skills and technology with domestic labour and inputs, and that FDI may be the main channel through which advanced technology is transferred to developing countries. Economies with greater endowments of human capital tend to provide the economic environment favoured by multinational corporations, such that firms in advanced economies specialise in the production of goods and services that cannot be produced elsewhere. Chen et al. (1995) obtained similar results when examining the role of FDI in China's economic development since 1978. They found that FDI in China has forced domestic manufacturing firms to compete globally. Countries that have increasing enrolments at higher levels of secondary and tertiary education provide an efficient and trainable workforce that is attractive to foreign investors. Similarly, in his study examining the contribution of FDI on the growth process in Fiji, using time series data for the period 1976 to 1995, Gani (1999) established that FDI contributed substantially to economic growth in that country.

In his study of the impact of FDI on capital accumulation, output and total factor productivity, de Mello (1999) concluded that the extent to which FDI is growth-enhancing depends on the degree of complementarity and substitution between FDI and domestic investment. His conclusion is that the impact of growth-enhancing FDI through knowledge transfers and capital accumulation is lower in technological leaders than technological followers. This, he says, is attributable to the fact that "the growth-FDI nexus is sensitive to country-specific factors that are unobservable in time series analysis" (de Mello, 1999:148).

On the other hand, Kgabi (1999) found that FDI does not have a significant effect on economic growth in Botswana. Though her results showed a zero relationship, she concluded by indicating that "it would not be sensible to recommend a change of policy without further research" (Kgabi, 1999:67). Kgabi's (1999) study analysed the impact of different types of foreign capital inflows on economic growth while this study is specifically focusing on the impact of foreign-owned manufacturing firms on Botswana's economy. Wells (1993) found that the differences between developing country and industrialised country based enterprises in Indonesia tended to narrow over time as the former moved increasingly into export-oriented manufacturing.

According to Kumar (1995), as much as the continued stake of the foreign technology supplier in the enterprise may force him to keep it updated with technology and encourage sharing other resources of the organisation such as market access, FDI may hamper or weaken the absorption and diffusion of technology within the host economy and result in continued technological dependence. That is, although there are advantages of FDI to the host economy such as access to foreign markets, FDI may also lead to the stagnation of technology absorption within the host economy.

In their study assessing the relationship between economic growth and FDI, Carkovic et al. (2002) found results that do not suggest a strong positive relationship between FDI and economic growth. The researchers used data from 72 countries covering the period 1960 to 1995. They controlled for factors that could bias their results, which included country-specific factors, the endogeneity problem[6] and other growth determinants. Similarly, when using panel data for more than four thousand Venezuelan firms between the years 1976 and 1989, Aitken et al. (1999) found, on one hand, that increases in foreign equity participation are positively related to increases in productivity for small[7] firms in the recipient economy. On the other hand, they found that increases in foreign ownership negatively affect the productivity of wholly domestically owned firms in the same industry.

Doraisami et al. (1995) examined the causality between FDI and economic growth in Malaysia, using data for the years 1965 to 1993. The objective of this study was to establish the significance of export oriented manufacturing and foreign direct investments in the country. The empirical results reveal a bilateral causality between FDI and economic growth. That is, as much as FDI contributes to economic growth in Malaysia, foreign investors are also attracted to the country because of its high economic growth rates. Using a simulation model for Mauritius and the six East Asian countries over the period 1983 to 1992, Fry (1995) found that FDI seems to augment capital formation in Mauritius and the six East Asian countries, but the model shows an opposite effect for eleven other developing countries[8]. The conclusion derived by the author is that the effects of FDI flows vary significantly between different nations of the developing world.

[6] In this case, the endogeneity problem means the joint determination of growth and FDI.
[7] In this case, "small" refers to plants with less than fifty employees.
[8] The six East Asian countries are Singapore, Malaysia, Thailand, Phillippines, Korea and Indonesia while the eleven developing countries outside East Asia are Argentina, Brazil, Chile, Egypt, India, Mexico, Nigeria, Pakistan, Sri Lanka, Turkey and Venezuela.

2.3 Exports and Economic Growth

The overall growth of countries can be accelerated by expanding their exports in addition to increasing the amounts of capital and labour within the economy. The association between exports and growth is often attributed to the possible positive externalities for the domestic economy arising from participation in world markets; for example, from the reallocation of existing resources, economies of scale and various labour training effects.

Medina-Smith (2001) analysed the case of Costa Rica, using annual data for the period 1950 –1997, and found that exports had a positive effect on the overall rate of economic growth. Begum et al. (1998) analysed the effects of exports on economic growth in Bangladesh using data from 1961 to 1992. The results of the analysis reveal that for a small, open economy like Bangladesh that once pursued an import-substitution trade regime, the shift to export orientation has been advantageous. Begum, et al. (1998: 9) argue that the "the sum of the productivity differential and externality effects of the export sector is positive". The finding was not sensitive to the estimation technique employed and the specification of the model.

Awokuse (2003) studied the causal pattern between exports and output growth in Canada using quarterly time series data from 1961 to 2000. The data set consisted of Canadian observations on GDP, exports, terms of trade, manufacturing employment, gross capital formation and the industrial production index for all industrialised countries. The results of the study showed that exports promote GDP.

Boltho (1996) studied the Japanese economy for the periods 1913 to 1937, 1952 to 1973 and 1973 to 1990, to establish whether the country's impressive economic record was caused by strong exports or domestic forces. The results of the study showed that domestic forces rather than exports drove impressive growth rates. However, the author also commented that exports played a significant role in the Japanese economy, even though their total impact was less than that of domestic forces.

In their study to establish whether other exporters can reduce the cost of foreign market access for a firm willing to penetrate foreign markets and to examine whether locating near other exporters increases the probability of exporting, Aitken, et al. (1997) used data from 2104 Mexican manufacturing plants over the period 1986 to 1990. They found that the probability that a domestic firm exports is positively correlated with its proximity to multinational firms. This suggests that

> "foreign investors directly or indirectly provide information and distribution services that enhance the export prospects of local firms" (Aitken, B. et al (1997: 104)).

Singh (2003) analysed the effects of exports on the level of output per capita and productivity in the manufacturing sector in India. He analysed ten industries in the manufacturing sector in India, for the period 1973/1974 to 1993/1994. The finding was that the exports variable did not induce convergence and instead it seemed to accentuate the process of divergence among industries. Moreover, the coefficient of exports was weak indicating economically weak effects of exports on the level of output per worker. On the contrary, Marin (1992) explored the co-movement between exports and productivity using quarterly data from 1960 to 1987 and found that exports promote productivity improvement. The four countries studied were Germany, the United Kingdom, the United States and Japan.

2.4 Conclusion

It could be concluded from this brief review of literature that there are mixed results regarding the impact of FDI on economic growth. The purpose of this study is to contribute towards these debates, using Botswana as a case study. On the other hand, the review of the literature regarding the impact of exports on economic growth on average reveals that export expansion promotes economic growth.

Chapter Three: Review of FDI Inflows and Botswana's Manufacturing Sector

3.1 Introduction: Foreign Direct Investment Inflows in Botswana

The manufacturing sector generally is viewed as the sector through which the twin goals of economic diversification and employment creation can be realised in Botswana. This is because the mining sector which the economy is still reliant on, uses mostly capital intensive methods of production whereas the manufacturing sector uses potentially more labour intensive methods of production. Hence, through the promotion of the manufacturing sector, employment creation and economic diversification can be enhanced. Foreign investment in turn is seen as a vehicle through which foreign technology necessary for the development of the manufacturing sector can be obtained. The limited inflow of FDI into Botswana is, therefore, considered to be of concern. The government of Botswana has taken steps to broaden the country's production base by encouraging FDI into non-mining sectors. In an effort to attract FDI, the government has removed structural deterrents to FDI, for example, by abolishing exchange controls. This chapter reviews the growth of FDI and recent manufacturing development in Botswana.

Table 1 below, shows FDI inflows to selected countries in Africa from 1989 to 2001. FDI inflows into Botswana for the period 1989 to 1994 were not impressive. Inflows started to increase in 1995 to 1997, and then declined slightly in 1998 and dramatically in 1999. However, even though the inflows improved between 2000 and 2001, FDI still did not match the levels achieved in other small countries like Lesotho. Therefore, the question of whether or not Botswana has done enough to create the necessary environment to attract and retain foreign investment and whether the assumption of a mere creation of an enabling environment would automatically enable a country to attract the required level of FDI, should be looked into (UNDP, 2002). The government needs to carefully identify the factors that explain the limited FDI inflows currently experienced by the country.

Table 1: FDI inflows to selected countries in Africa, 1989 - 2001 (Millions of U.S. Dollars)

Country	1989-1994 (annual average)	1995	1996	1997	1998	1999	2000	2001	1995 – 2000 (annual average)
Botswana	-29	70	70	100	96	37	57	57	72
Lesotho	169	275	286	269	262	163	119	118	229
Mauritius	24	19	37	55	12	49	277	n/a	75
Mozambique	21	45	73	64	213	382	139	n/a	153
Namibia	70	153	129	84	77	111	124	n/a	132
Swaziland	67	44	22	15	165	100	-19	69	55
South Africa	n/a	n/a	n/a	3817	561	1502	888	6653	1128
Uganda	23	121	121	175	210	222	254	5	184
Zimbabwe	34	n/a	n/a	n/a	n/a	59	23	n/a	14

Source: World Investment Report, 2001.

In seeking to explain Botswana's unsatisfactory performance in attracting FDI over the specified periods, the UNDP (2002:64) argues that:

> "Other countries in the region have also opened up to FDI and began to receive increasing FDI through privatization programmes and projects in natural resources or in their processing and, secondly, with the end of apartheid in 1994, South Africa became a competitor in attracting flows of FDI into the region and a number of South African companies with investment in Botswana returned to their home country".

This explanation is questionable, considering that Botswana's inflows had been improving from 1995 to 1997, even though they declined slightly in 1998 and 1999

(Table 1). However, the country is still attracting less FDI compared to some other southern African countries.

3.2 Growth of the Manufacturing Sector in the 1980s

In the first two decades after Botswana's independence, the manufacturing sector received minimal protection or subsidy (Harvey et al., 1990). The industry was mostly small scale and privately owned, with the exception of meat processing at the Botswana Meat Commission (BMC) and a small number of firms in which the Botswana Development Corporation (BDC) participated (Harvey et al., 1990). Ninety-five percent of manufacturing output was meat and meat products (SADC, 2002).

Initially, exports were very dependent on regional markets, overwhelmingly Zimbabwe which absorbed 66 percent of Botswana's exports and South Africa (25 percent) (Harvey, C. et al, 1990). Exports were dependent on changes in trading agreements between Botswana and Zimbabwe and between Botswana and South Africa as well as in demand in those particular countries. South Africa thus remains the main exporting destination for the country regionally following the current instabilities in Zimbabwe.

3.3 Recent Developments in the Manufacturing Sector (1990s)

In its effort to diversify the country away from diamonds, the government is trying to promote the country's manufacturing sector[9]. For the decade 1990/1991 to 2000/2001, the average contribution of the manufacturing sector to GDP was only 4.2%[10]. Botswana has entered into trading agreements with other countries as a way of stimulating the growth of its manufacturing sector. For example, because Botswana is an eligible beneficiary of the United States Africa Growth and Opportunity Act, it is

[9] Note that the emphasis in this paper is on the manufacturing sector, even though the government's overall emphasis is to promote all non-mining sectors, including, for example, the service sector.
[10] Bank of Botswana Annual Report (2002).

now enjoying the benefits of its products entering the US market free of quotas and duties.

The manufacturing sector expanded at an annual rate of 17% in the 1970s and 8% in the 1980s. Growth was driven mainly by a rise in domestic demand (which accounted for approximately half of the growth), while import substitution contributed about 37% to the sector's output (www.sadcreview.com, accessed on 13/05/2003). The 1990s saw the manufacturing sector's growth rates declining, though they still remained satisfactory (Table 2). Output recovered during the second half of the 1990s due to increased productivity. Manufactured exports grew rapidly in the mid 1990s influenced mainly by the doubling of exports in the motor vehicle industry. The rapid growth of the motor vehicle industry was, however, short-lived due to the closure of the Motor Company of Botswana, which assembled Hyundai cars, (www.sadcreview.com, accessed on 13/05/2003). The Motor Company of Botswana was closed due to financial problems encountered by the holding company.

The country's investment climate has helped to attract industrialists from various parts of the world. The main sources of foreign investment have been Mauritius, France, Belgium, the United States, the United Kingdom and South Korea. The country is now producing a wide variety of goods which are manufactured for both the local and export markets. Products produced by the manufacturing sector include, inter alia:

- Assembly of trucks and buses
- Parts and components for the automobile industry
- Electronic and electrical items
- Textiles, garments and other related products
- Canned products and
- Leather products.

Table 2 below shows that manufacturing output has been increasing since 1994. However, non-traditional exports decreased between 1998 and 2001.

Table 2: Manufacturing Sector: Output, Employment and Exports

			1994	1995	1996	1997	1998	1999	2000	2001
Manuf. output	Current prices	Pm	1939	2657	2959	3719	4418	4739	5014	5277
	Constant prices	Pm	1939	2283	2323	2493	2717	2758	2730	2635
Employment	Manufacturing		21700	23300	23200	24000	24000	23700	29300	27951
	Total pt. sect.[11]		136200	132600	147100	136200	125900	127000	142200	147661
	Mfg/private	%	16%	18%	16%	18%	19%	19%	21%	19%
Exports (Current prices)	Textiles	Pm	177	146	194	248	303	248	244	193
	Vehicles	Pm	301	957	1144	1183	966	667	270	299
	Other goods	Pm	261	286	323	434	519	692	700	569
	Total non-trad (NTX)	Pm	807	1450	1760	2009	1922	1740	1357	863
	Total traditional[12]	Pm	4158	4491	6373	8382	6775	10488	12477	13444
	Total (TOTX)	Pm	4965	5941	8133	10391	8697	12228	13835	14306
	NTX/TOTX	%	16%	24%	22%	19%	22%	14%	10%	6%

Source : Central Statistics Office and own calculations.

Note: 1) Financial years for Central Statistics Office publications run from July to June the following year. For example, the year 1993/1994 in this paper is interpreted as 1994.

2) Manuf. stands for manufacturing.

Export intensity (the ratio of exports to gross manufacturing output) illustrates the extent to which the manufacturing sector depends on external demand for its activities. The export intensity, whilst only 25% in 1993/1994, rose sharply to 45% in 1996/1997.

Figure 1 below analyses non-traditional exports in more detail. The figure shows that vehicle exports depicted a sustained upward trend from 1994 to 1997. From 1998 onwards, the motor vehicle assembly operations encountered problems and eventually stopped production. The Hyundai plant finally closed in March 2001[13]. However, vehicle exports have continued to rise, albeit at lower levels, due to the establishment of an assembly plant for buses and trucks in Botswana by Volvo to cater primarily for the

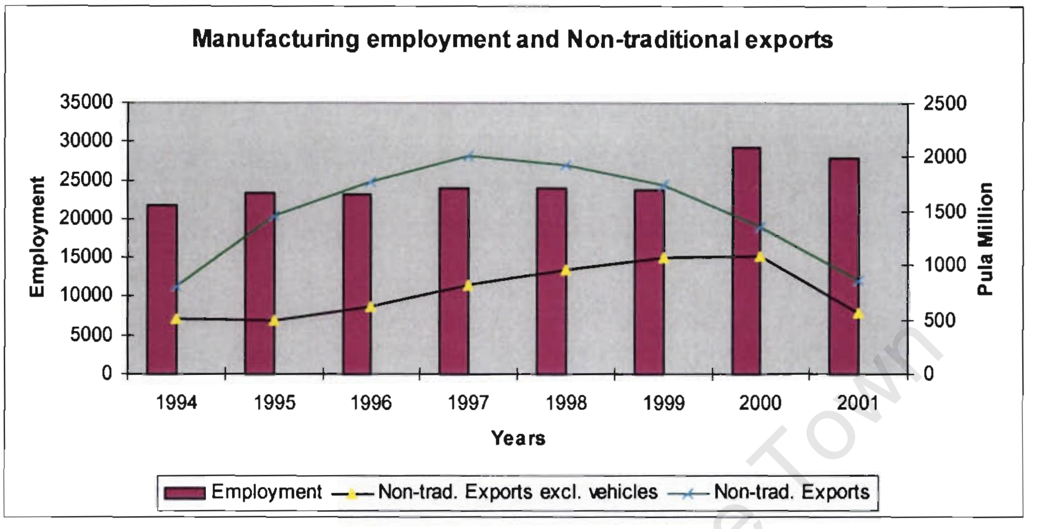
[11] Total pt. Sector=Total private sector.

[12] Traditional exports are beef, diamonds and copper-nickel; NTX=non-traditional exports; and TOTX=total exports.

[13] Bank of Botswana Annual Report (2002).

South African market and also to tap emerging markets of neighbouring Namibia and the Democratic Republic of Congo (BIDPA, 2002).

Figure 1: Manufacturing employment and non-traditional exports



Source : Central Statistics Office.

Figure 1 also shows non-traditional exports excluding vehicles. While non-traditional exports and non-traditional exports excluding vehicle exports depict similar patterns, excluding vehicles exports gives a truer reflection of the performance of non-traditional exports.

With regard to employment levels, Figure 1 shows that from 1994 to 1999, the levels were almost stagnant but increased in 2000. On the other hand, from 1994 to 1997, non-traditional exports were increasing rapidly but decreased from 1998 to 2001. The fact that employment levels are increasing while non-traditional exports are decreasing is puzzling. Clearly, employment levels in the manufacturing sector may be influenced by many factors, such as increased local demand. However, this trend of declining non-traditional exports is worrisome because;

> "there is a need to accelerate the growth of the existing non-mining industries and develop a range of new private sector activities through which a high overall economic growth rate could be achieved" (UNDP, 2002:54).

3.4 Conclusion

Policy makers should try and establish the reasons for limited FDI inflows experienced by the country with the intention of addressing constraints. The manufacturing sector has the potential to grow but since the domestic market is small, higher growth rates can only be achieved if more foreign firms geared at exporting their products can establish themselves in the country. Small businesses that are mostly owned by local citizens should be promoted so that they can also contribute to the development of the manufacturing sector.

Chapter 4: Results of the Survey

4.1 Introduction

This chapter gives both a descriptive and analytical overview of the results of the surveys[14] that were conducted in Botswana. The surveys investigated the pattern of investment and export behaviour of Botswana's foreign-owned manufacturing firms, with a view to contributing to research on the role of FDI in Botswana's economy. Factors that encourage or hinder the firms' performance were also analysed. Equally important, were the questions of the origins of the main inputs used by firms and the firms' opinion of the sources of manufacturing sector growth in Botswana. These two questions are important in the sense that the former question checks if the domestic sector is developed by the existence of foreign investors in the country[15]. The latter question, on the other hand, establishes if foreign-owned firms feel that the growth of the manufacturing sector in Botswana could be enhanced if firms become more export-oriented in nature or if factors other than growth of exports contribute to the growth of the manufacturing sector.

4.2 Overview of firms interviewed

Fourteen foreign-owned[16] firms were interviewed and this sample represents about 4%[17] of the population of total foreign-owned firms in all sectors of the economy. Nine out of the 14 (64%) firms surveyed were 100% foreign-owned and the remaining 5 (36%) firms were joint-ventures. These surveyed firms employ 5408 people, which is 25% of the total employees in all foreign-owned and joint-venture manufacturing

[14] The questionnaires that were used for the surveys are contained in appendices A and B.
[15] This is one of the benefits of FDI in the host country. Note that the channels by which foreign investment impacts on the domestic economy include a range of micro and macro elements.
[16] Foreign-owned firms encompass wholly foreign-owned firms and joint partnerships between citizens and foreigners.
[17] According to the Department of Industrial Affairs (Botswana), there are 1974 citizen-owned firms, 116 joint-ventures and 253 non-citizen firms.

firms[18] in 2002. A total of 30 287 people were employed by the formal manufacturing sector as at 2002[19]. Hence, the firms surveyed comprise 18% of the entire manufacturing sector work force. Given the small sample size of the firms interviewed, this figure represents a significant proportion of the formal work force.

Twenty-four firms were approached and only fourteen responded to the questionnaires. The firms that were approached were all foreign-owned and joint-venture exporting firms based in Gaborone, Lobatse, Ramotswa, Selibe-Phikwe and Francistown. A list of foreign-owned firms was obtained from the Botswana Export Development and Investment Authority (BEDIA) to select the sample. Two different types of questionnaires were used for the survey: the short questionnaire that catered for firms far from Gaborone like Francistown and Selibe-Phikwe. For these firms, the questionnaire was faxed to them and queries were dealt with by telephone. Three firms responded to the short questionnaire. One company which is based at Selibe-Phikwe was interviewed face to face because it has a branch in Gaborone. The other questionnaire was longer and respondents were interviewed face to face. This questionnaire was administered in Gaborone and surrounding areas like Ramotswa and Lobatse. It is worth mentioning that most large businesses are established in urban areas, where they have access to services and the required infrastructure. Firms that are established in villages like Ramotswa for example, are very near to the urban areas of Gaborone and Lobatse.

Eleven firms were interviewed using the long questionnaire. The firms fell into three sectors, namely motor vehicles/parts, foodstuffs and textiles/clothing. Seventy-one percent of the firms interviewed were in the textile and clothing sub-sectors. This is roughly in line with the finding by the Department of Industrial Affairs (Botswana) in its 2001 survey on manufacturing firms that textiles and clothing sub-sectors account for 60% of total employment in manufacturing and are also the largest sub-sectors in

[18] According to the Manufacturing Sector Database of the Department of Industrial Affairs (Botswana), 7556 people were employed by joint-venture firms and 14 187 were employed by the foreign-owned firms as at April 2002.

[19] Source: Central Statistics Office (Botswana).

output terms. It also seems that market seeking investment has been quite common in the manufacturing sector, and that preferential market access has attracted firms producing clothing to locate in Botswana.

The survey took place in April 2003 and the following firms were interviewed:

Table 3: Firms interviewed, their locations, business profiles and current employment levels

Firm	Location	Product(s)	Current employment level
Western Textiles	Gaborone	Towels, face & dish cloths and baby napkins	100
Western Knitting Mills	Gaborone	Knitted fabrics	22
Western Apparels	Gaborone	T & golf shirts, shorts and ladies tops	60
Rising Sun	Selibe-Phikwe	Denim wear	500
Auto Ancillaries	Gaborone	Leaf springs, u-bolts and welding electrodes	91
B & M Garments	Shashe Village	T-shirts	816
Garnet Promotions	Selibe-Phikwe	Knitted garments	130
Harness Manufacturing Botswana	Gaborone	Electrical harnesses	601
Caratex	Gaborone	Jerseys (sweaters)	1300
Sugar Industries	Lobatse	Packed sugar	140
Algo Industries	Gaborone	Denim wear	256
Premier Clothing	Gaborone	Work wear e.g overalls, dustcoats, uniforms	300
Dinesh Textiles	Selibe-Phikwe	Men and ladies clothes made of denim, twill and corduroy.	310
Bolux Milling	Ramotswa	Maize meal and wheat flour	782

Source : Own Survey, 2003.

4.3 Markets and Marketing

Table 4 below presents the proportion of total sales generated from exports. It can be seen that in years 2000, 2001 and 2002, 8 out of 11 firms, 11 out of 14 firms and 11 out of 14 firms' respectively had exports exceeding 30% of total sales. Over time, the table indicates that there has been no significant change in the share of sales generated from exports by the surveyed firms.

Table 4: The percentage of total sales generated from exports

Year	Percentage of exports	Number of firms	Total firms in a year
2000	70-100	8	
	30-69	0	
	Below 30	3	11
2001	70-100	10	
	30-69	1	
	Below 30	3	14
2002	70-100	10	
	30-69	1	
	Below 30	3	14

Source: Own survey, 2003.

Notes: 1) Category of below 30% also includes one firm that does not export at all.

2) For the category of total firms in year 2000, the number is less than 14 firms because three firms exported after year 2000.

4.3.1 Trend of exports in real terms

As mentioned previously, the Botswana government is trying to attract investment into the non-mining sectors of its economy. This is to reduce the dependence of the economy on the mining sector which is prone to volatile world prices. In this regard, expansion of exports into the non-mining sectors is viewed as a strategy that will increase the production base of the country.

Table 5 below shows the expected trend of real exports next year and in the next five years. It shows that in the coming year, half of the firms expect their exports to increase by 1-10% annually while one firm expects a decline of over 5% in exports annually. For the next five years, 9 firms expect their exports to increase by 1-10% annually while one firm expects its exports to decline by over 5% annually. The expectation, therefore, is for moderate growth in exports by surveyed firms.

Table 5: Trend of exports in real terms

Expectation	Next Year	Next five years
Decline by over 5% annually	1	1
Decline by 1-5% annually	0	0
No significant change	6	4
Increase by 1-5% annually	5	5
Increase by 6-10% annually	2	4
TOTAL FIRMS	14	14

Source: Own survey, 2003.

Notes: 1) A firm that does not export was also included in the category of no significant change.

2) Note that average inflation in 2002 was 8.1% and the expected rate for 2003 is 6.0%[20].

From the interviews, 6 firms felt that because they are newly established, they expect their real exports not to change in the coming year. One firm expects its real exports to decline by over 5% in the coming year. This was attributed to the appreciation of the Pula against the Rand in 2001 and 2002. The mentioned firm exports 100% of its products to South Africa and lower margins in the South African market led to a sharp cutback in production. The firm respondent commented that, "*We thought we could compensate our losses by supplying the domestic market, and we're still making losses since local people do not buy products made in Botswana. Besides, most local people don't even know our firm exists in Botswana*".

[20] Source: Ministry of Finance and Development Planning Annual Economic Report (2003).

4.3.2 Destination of exports

Botswana currently exports to a limited number of countries. This is in spite of the fact that the country has an open economy. The country depends largely on Europe for export markets (Table 6).

Table 6: Botswana's export markets 1991 - 2001 (Percentage share of total)

Year	SACU	Zimbabwe	Other Africa	Europe	USA	Other
1991	5.0	6.8	1.5	86.4	0.3	0.0
1992	6.9	4.5	1.5	86.7	0.3	0.1
1993	8.9	3.2	1.3	86.2	0.3	0.1
1994	13.9	2.7	1.0	81.5	0.7	0.2
1995	21.5	3.1	0.8	73.6	0.9	0.2
1996	18.3	3.1	0.6	76.8	1.0	0.3
1997	14.3	3.7	1.1	79.7	1.0	0.2
1998	17.2	2.9	1.3	77.1	1.0	0.6
1999	10.4	2.4	1.1	84.7	0.7	0.7
2000	6.7	3.9	0.9	87.2	0.6	0.7
2001	6.5	2.6	0.8	89.0	0.2	0.9

Source: Central Statistics Office (Botswana).

As Table 6 indicates, over the period 1991 to 2001, the major destination of Botswana's exports (mainly rough diamonds and beef) was Europe. The Southern African Customs Union's (SACU) share of exports increased from 1992 to 1998 and declined sharply after that. The rise and subsequent decline in exports to SACU is attributable partly to the initial rapid increase in exports of vehicles following the establishment of the Hyundai vehicle assembly operation and its subsequent closure. Zimbabwe was an important export market in the early 1990s, but its share has substantially declined since then because of the economic and political problems in that country.

South Africa is, not surprisingly, a much more significant market for Botswana's manufacturing exports than for exports as a whole (Table 7).

Table 7: Destination of exports by surveyed firms (manufacturing firms)

Destination	Percentage of exports	Number of firms
South Africa	70-100	6
	30-69	0
	1-30	5
SADC (excluding South Africa)	70-100	0
	30-69	0
	1-30	3
Global (Outside SADC)	70-100	5
	30-69	0
	1-30	1

Source: Own survey, 2003.

Note: Not all the firms interviewed export to all destinations, hence, for each destination the number of firms does not correspond to 14 firms.

Although South Africa is the country's largest market for manufactured goods, local firms are beginning to penetrate other global markets such as the United States, Germany, Portugal, Spain and the United Kingdom. This supports the NDP 9's objective of promoting the country's competitiveness in global markets. The country's small domestic market compels it to follow an export-led growth strategy.

4.3.3 Sources of inputs into the manufacturing sector

The manufacturing sector currently depends heavily on imported inputs. Figure 2 shows the origins of the main inputs used by surveyed firms. Five firms purchased 100% of their main inputs from foreign suppliers other than South Africa. These countries include China, India, Mauritius, Zambia, the European Union, United States, Hong Kong and Zimbabwe. Three firms purchased the bulk of their main inputs from

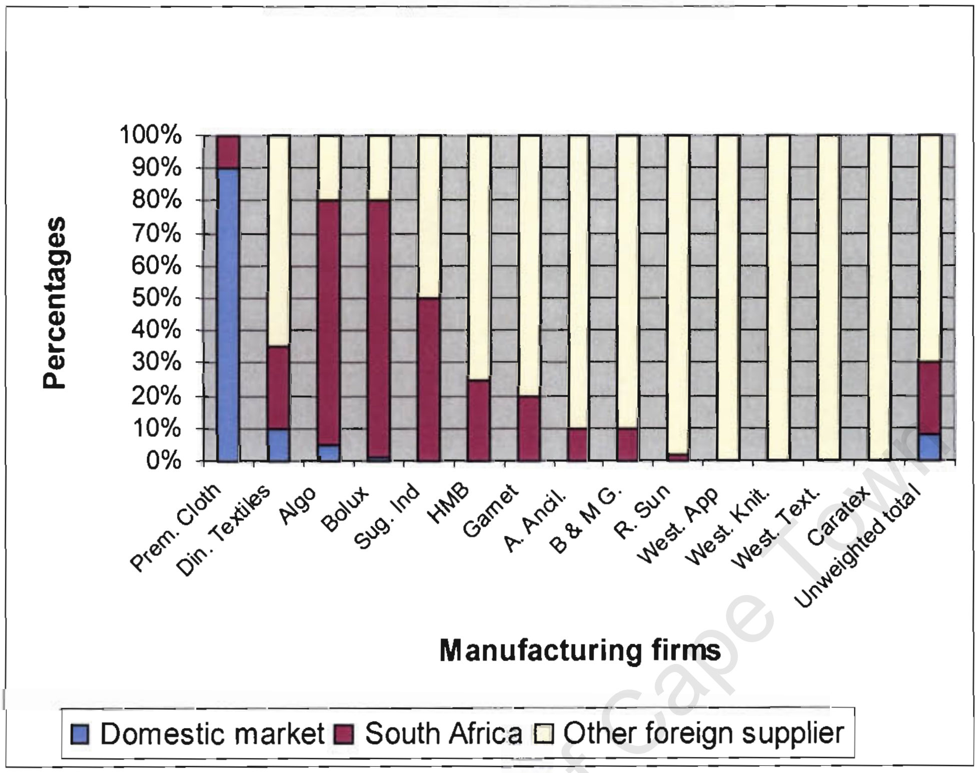
South Africa. Only five firms purchased any of their main inputs domestically and in only one case did local suppliers account for the bulk (90%) of inputs used. This general picture is worrying because of the fact that firms do not get most of their main inputs locally, and this means that local suppliers are not developed. Generalising from the survey, therefore, one may conclude that the impact of foreign firms, in this regard, is quite limited.

Backward linkages[21] of manufacturing exporters are clearly undeveloped and hold little promise for local suppliers. It could be argued however, that Botswana, like many small economies, may not be able to produce all inputs efficiently. Therefore, the country should specialise and reap the gains from trade. Limited backward linkages are characteristic of export processing in small and undeveloped manufacturing sectors and it could be argued that as long as foreign investors create jobs in the host country, then one should not worry about the origins of the raw materials that they use. This view was expressed by the Botswana Minister of Trade and Industry in his speech to mark the beginning of a concerted investment-promotion drive in South Africa. He explained that,

> "*The recent inclusion of Botswana as a least developed country under AGOA 2 presents an opportunity for investors who locate in Botswana to source cheaper and better quality raw materials from non-African third countries and still qualify for AGOA preferences*", (Source: "Botswana: A Business Report Review, October 2002, www.businessreport.co.za).

[21] Backward linkages occur when an incoming firm purchases inputs from domestic firms.

Figure 2: Sources of main inputs into the manufacturing sector



Source : Own survey, 2003.

Note: A guide to abbreviations can be found in Appendix C.

One respondent commented that "*If the materials we need were there in Botswana, we would gladly use them to manufacture our products, they are not there! So what do we have to do? Import from foreign suppliers*".

Limited backward linkages are a function of the low level of industrialisation in Botswana and the related lack of critical mass in major sectors (e.g garments) sufficient to attract suppliers. This does place a question mark over the ability of the sector to provide a major source of diversification.

4.3.4 Sources of manufacturing sector growth

Lewis, R.S. et al (1988) in Jefferis (1997)) analysed the sources of manufacturing sector growth for the period 1975 to 1985 in Botswana. They found that 51% of the growth came from rising domestic demand, 26% from import substitution and the remaining 24% from exports.

Table 8 below presents the average responses to the survey question asking firms what they perceive to be the sources of manufacturing sector growth in Botswana. The table compares Lewis's study (cited in Jefferis) with the results of this study. The obvious message from the table is that firms perceive manufacturing growth in Botswana to be stimulated by exports, followed in importance by rising domestic demand and then import substitution. This finding is a biased one because firms only that export were interviewed. On average, firms believe that the sector can grow further through export expansion than by targeting the domestic market. In this regard, the government's initiative of creating an environment that is conducive for exporting to international markets, is therefore, supported. For example, the current AGOA 1 and the proposed AGOA 2 are necessary for the expansion of the manufacturing sector in Botswana.

Table 8: Sources of growth in the manufacturing sector (%)

	Lewis's 1988 study cited in Jefferis (1997)	Own survey, 2003
Rising domestic demand	51	20
Import substitution	26	8
Exports	24	72

Notes: 1) Refer to questionnaire (Part 2, question 14).

2) The question referred to firms' views about the economy as a whole, not just the perspective of the firm being interviewed.

Sources: Own survey, 2003 and Lewis's 1988 study cited in Jefferis (1997).

One respondent supported the above finding by saying, "*Unless local people change their attitudes toward goods produced in Botswana, there is no way the manufacturing sector can grow when supplying only the domestic market. Firms need to explore external markets*".

The above table reveals that firms feel exports now play an increasing role in the manufacturing sector growth as compared to the earlier analysis of the sources of manufacturing sector growth for the period 1975 to 1985.

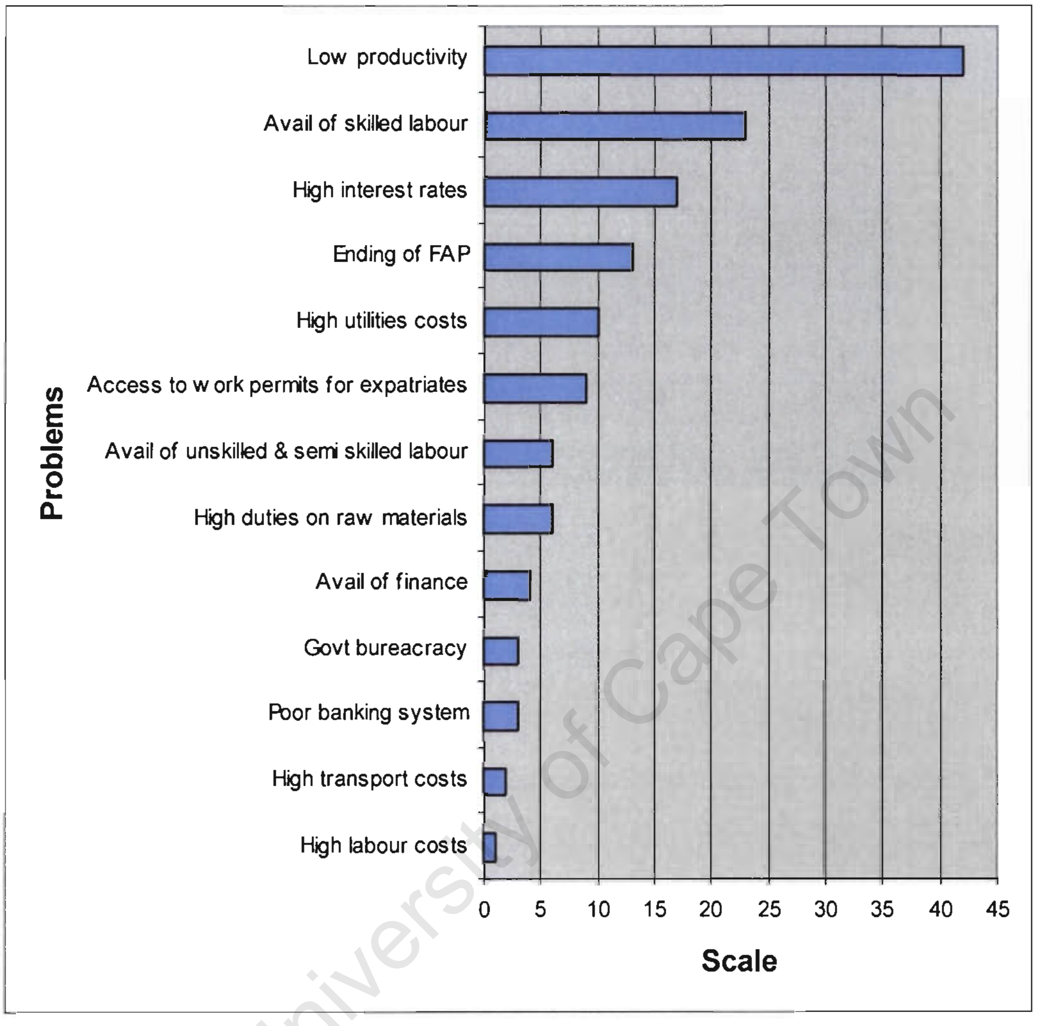
4.4 Location and other factors affecting investment

A conducive environment is necessary for both domestic and foreign investment. If a country's environment is not investor-friendly, then fewer investors will be attracted to that country. FDI is influenced by various factors, which include amongst other things, the attractiveness of incentives provided by the host country to enhance investors, the country's economic status, the availability of labour and the desire of investors to access new markets. This section highlights the problems faced by firms and factors affecting investment in Botswana.

4.4.1 Problems faced by firms

Figure 3 below presents responses to the survey question asking firms the problems they are facing in Botswana. Firms ranked up to four important problems. For each firm, each problem chosen was ranked according to importance, with 4 points allocated to the most important problem, 3 points to the second most important problem and so on.

Figure 3: Problems faced by the interviewed firms



Source : Own survey, 2003.

Note: Refer to questionnaire (Part 3, question 19).

The results in Figure 3 show that low productivity was the most pressing problem, followed by the availability/cost of skilled labour, high interest rates and finally the phasing out of the Financial Assistance Policy (FAP). To show the seriousness of the problem of low productivity in Botswana, one respondent commented that "……. *Because employees are not serious about their work, GDP growth cannot be stimulated. In a case like this, the government should favour firms that promote less labour intensive production methods rather than those that promote more labour* *intensive methods*". Another respondent emphasized this point by stating that, "*Botswana is not ready to start the manufacturing sector because employee awareness is very limited. Employees are only interested in money. Accordingly, no government incentive scheme will work if citizens do not change their attitudes*".

Evaluating these statements, the only remedy for the high unemployment rate in Botswana is for citizens to be more serious with their work rather than for firms to use capital intensive production methods. This view was emphasized by one respondent: "*In Botswana, production should entirely be labour intensive, looking at the fact that Botswana has a problem of unemployment*".

However, not all respondents felt that productivity was a major problem. One respondent stated that "*Due to productivity increases in our firm, employment levels are decreasing every year*". This statement reflects that some firms feel labour productivity is improving or has improved. There is generally the perception that Botswana's labour is unproductive. This may not be true because the Botswana manufacturing sector is dominated by the textile sub-sector which is both export intensive and labour intensive in production. The fact that production of this sub-sector is labour intensive means that output per employee is low and this could be the contributory factor to the perception that Botswana's labour productivity is low. In addition, the fact that labour productivity may be improving, does not rule out the fact that labour may be unproductive. Moreover, productivity levels may still not be good enough to allow for expansion of production and sales to other more competitive markets.

Commenting on the phasing out of FAP, one respondent added that, "*After the ending of FAP, what incentives have the government put in place to attract foreign investors? None and these are some of the problems that make foreign investors go back to their countries*".

Although investors generally complain about the high utilities costs charged by service corporations, the results of the survey do not show this to be the main problem. On a general perspective, one respondent commented that, "*At the moment the country's environment is not conducive for foreign investors. For example, CEDA only caters for citizen-owned businesses. Furthermore, the government only concentrates on the macro aspect of foreign investment but not the micro aspect. For example, it doesn't say anything about the high utilities costs charged to us*".

4.4.2 Factors important in selecting Botswana as the best location

Botswana advertises itself to potential investors as a country that is the most stable and most transparent on the African continent. It claims to have a supportive investment climate (Figure 4). For example, foreign investors are free to repatriate dividends and capital and the country has completely liberalised its foreign exchange controls. The country also has favourable market access to the EU, the US and South Africa.

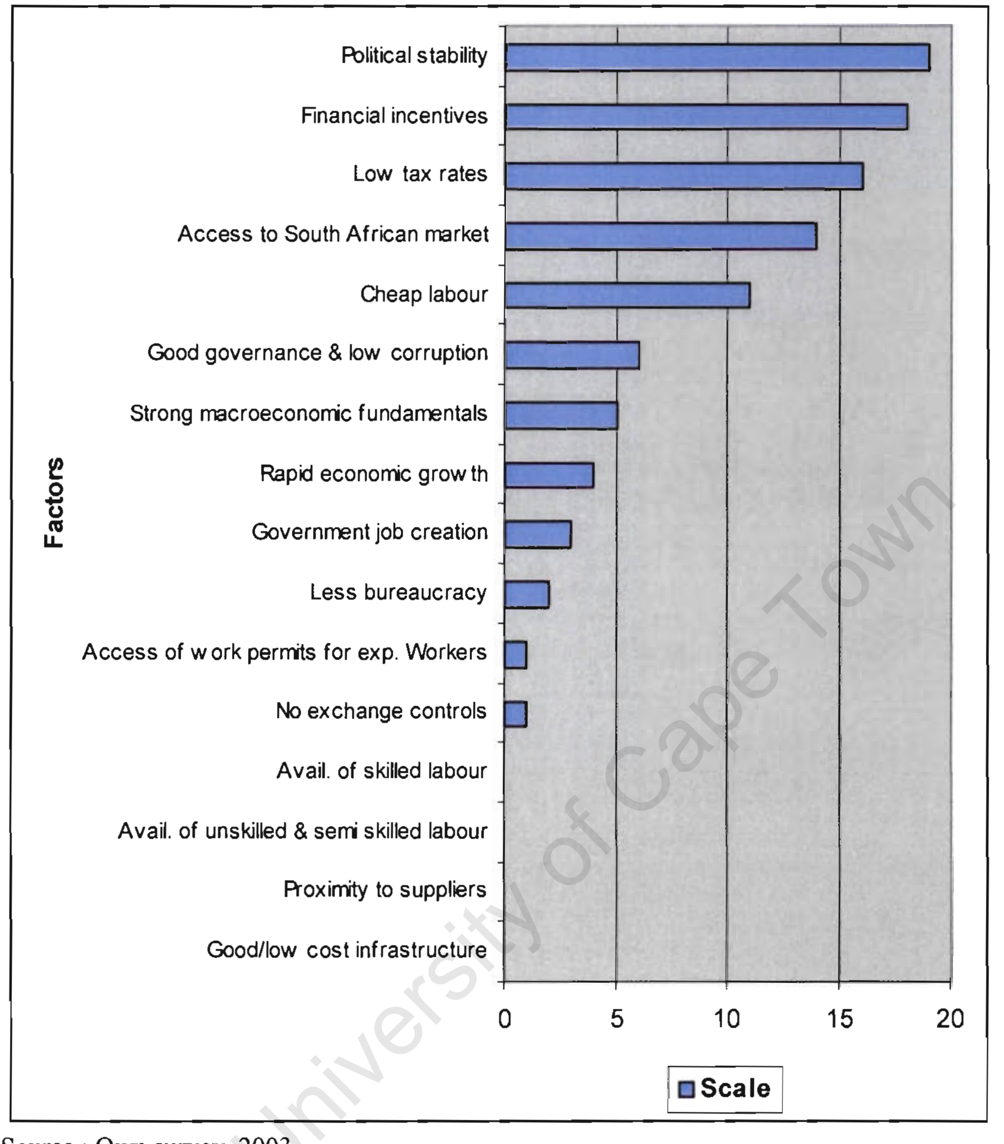
The findings of the survey which are presented in Figure 5 provide some support for these claims. Figure 5 shows that surveyed firms considered the most significant locational advantage of Botswana to be of political stability followed by financial incentives and low tax rates. Access to the South African market and cheap labour were also considered important factors. Surprisingly, rapid economic growth was not considered one of the most important factors. The surveyed firms also felt the availability of skilled, unskilled and semi-skilled labour, proximity to suppliers and good or low cost infrastructure were unimportant in attracting them to locate in Botswana.

Figure 4: Botswana's Unique Investment Climate

Botswana fact sheet : Unique investment climate
• Politically the most stable country on the African continent • Profits, dividends and capital can be readily repatriated • Has recorded the highest growth rate in the world, for the period 1970 –1990 • No foreign exchange controls • No labour disputes, no strikes • Corporate tax is only 15% for manufacturing companies, and the international financial services centre • The most transparent country on the African continent according to Transparency International • Duty free and quota free access to the EU market • Duty free access to South Africa, Namibia, Lesotho and Swaziland • The least risky country in Africa according to OECD • The Africa Growth & Opportunity Act of USA allows new opportunities for duty free and quota free access to US markets • The highest foreign exchange reserves amongst the developing world representing 36 months of import cover • Preferential access to markets of 14 Southern African countries

Source: "A Business Report Review, October 2002.

Figure 5: Factors considered important by firms locating in Botswana



Source : Own survey, 2003.

Note : Totals were ranked as follows: Initially, firms ranked up to four important problems. For each firm, each problem chosen was ranked according to importance, with 4 points allocated to the most important problem, 3 to the second most important problem and so on.

4.5 Government Policies and Incentives: Perceptions of BEDIA's performance by firms

This section presents responses to the survey question asking firms how they rank the performance of the Botswana Export Development and Investment Authority (BEDIA)[22]. Only ten firms responded to this question as the question was not asked to firms responding to the short questionnaire. Forty percent of the firms felt BEDIA's performance is good, 20% considered its performance acceptable and the remaining 40% rated its performance as poor. A frequent complaint about investment agencies worldwide is that they focus on new investors instead of providing "aftercare" assistance to firms already established in the country.

One respondent stated that "*Before BEDIA goes out to bring the investors into the country, it has to make the country attractive by having some export or performance related incentives. It should contact the existing manufacturing firms to find out the problems they are facing*".

Another respondent asked, "*Why is it that countries like Singapore can export things made from diamonds and gold back to Southern Africa when this region is well endowed with these natural resources? It means something is wrong with the way we are doing things. BEDIA should visit countries like Singapore and Italy to 'hunt' for technical expertise*". This statement is valid because the method of production for the mining sector is mostly capital intensive in Botswana and it is not helpful with regard to employment creation. Therefore, the establishment of manufacturing firms linked to the mining sector, for example, diamond polishing firms should be considered in the country to help enhance export diversification and employment creation.

Another respondent commented that, "*BEDIA is only taking care of foreign investors and is neglecting domestic investors. In this case, how can the domestic sector be*

[22] BEDIA was established in 1997 by an Act of Parliament to promote foreign direct investment into the country with special emphasis on export-oriented manufacture, to identify market outlets for products manufactured in Botswana and to construct factory buildings to be leased out to investors.

developed?" Some firms also complained of the limited interaction between the industry and policy makers in government departments.

On the other hand, some respondents feel BEDIA is doing a good job even though they have some reservations. For example, one respondent commented that, "*BEDIA is generally doing a good job, but the problem is, its ability to deliver is limited because it is under the government. For it to be effective, it should be an independent body in the private sector. By so doing, it will be more effective as it will report directly to His Excellency, the President"*.

In summary, the allegations that BEDIA is inefficient may not be refuted and the organisation should examine itself and establish how it can improve its performance.

4.6 Conclusions from the survey

This section summarises the findings from Chapter Four. The conclusions are as follows:

1. Most major exporting firms were no longer in operation as they could no longer sustain themselves. This conclusion was reached from the findings of the survey[23].

2. Exports were seen to be the major source of manufacturing growth in Botswana. This supports the view that, given the small domestic market of Botswana, firms should be more export-oriented in nature to take advantage of regional and global markets that offer wider market opportunities.

3. Investors do not have a problem with investing in Botswana. What discourages investors are the problems they encounter while in Botswana. They believe that if

[23] Three firms from the sample were of this view.

the government can make an effort to remove these impediments then Botswana will be more investor-friendly, given the advantages it has over other countries in Africa, with regard to rapid economic growth and political stability.

4. A high proportion of the firms in the sample feel Botswana's labour is very inefficient. Interviewers insisted that if the effort put in by workers does not improve, then there is no way locals will benefit from the skills offered by these foreign firms.

5. Government incentives, particularly financial ones, only benefit citizen or domestic firms. Hence, foreign firms have to resort to commercial banks for finance and the commercial banks charge very high market rates. The phasing out of the Financial Assistance Policy (FAP) also posed a problem to the foreign firms as these firms depended on this scheme for finance and training grants.

6. The performance of the Botswana Export Development and Investment Authority (BEDIA) was viewed by 40% of firms as poor. Firms feel there is no interface between government departments tasked with the responsibility of attracting foreign investment and foreign investors. A representative of one firm commented that BEDIA is only concerned with attracting investors into the country and once the investors are established in the country, BEDIA does not care to find out how they are doing. "*The organisation is only interested in new investors*", he said. If this statement is true, then this may be a factor why firms after establishing themselves in Botswana, go back to their home countries or relocate to other countries.

7. From the sample of firms interviewed, it was found that with one exception, they were catering for the export market, rather than the domestic market. The export markets catered for include, amongst others, South Africa, the European Union (EU), the United States and SADC countries. In the past, most firms were exporting only to South Africa and now it can be observed that firms are penetrating new markets like the EU and the United States. This could be attributed to the fact that

Botswana is an eligible beneficiary of the Africa Growth and Opportunity Act (AGOA), whereby members are allowed duty and quota free access for most commodities to the United States of America. This also goes hand in hand with the NDP 9's objective of globalisation.

8. Almost all firms interviewed obtain their main inputs from outside Botswana. Backward linkages are therefore limited. The reason they give is that Botswana does not have the required inputs.

9. Most firms were expecting their volume of exports and fixed investment to increase the following year and in the next five years but only at a moderate pace. Only one or two firms indicated that they expect their exports to decline the following year and in the next five years.

10. In sum, the results of the survey indicate that the manufacturing sector in Botswana has a potential to grow even though the sector has been through difficulties. It can be more export-oriented if the problems, cited above, are attended to.

Chapter Five: Conclusions and Policy Recommendations

5.1 Introduction

The main objective of this study was to determine the impact of foreign investment on Botswana's economy. The analysis was done, based on a survey of fourteen foreign-owned manufacturing firms. This was with a view to investigating the pattern of investment and export behaviour of Botswana's foreign-owned firms. Factors that encourage or hinder the firms' performance were also analysed.

5.2 Conclusions and policy recommendations

The results of the survey show that the country still depends largely on the mineral sector for the bulk of its export revenue. The government's efforts to broaden the country's production base by encouraging FDI into non-mining sectors have been limited in this regard. Data from the Central Statistics Office (Botswana) reveal that traditional exports which include beef, diamonds and copper-nickel have been increasing from 1998 to 2001 while non-traditional exports were decreasing in the mentioned years. It can, therefore, be concluded that to an extent, the government's efforts to diversify exports have been limited.

Secondly, the manufacturing sector was also seen not to help much in the diversification drive adopted by the government. The sector has been going through some difficulties. For example, from 1998 onwards, the motor vehicle assembly operations encountered problems and eventually stopped production in March 2001. As a result, non-traditional exports were negatively affected. The results of the survey also revealed that the sector has been experiencing difficulties as indicated by some of the exporting firms that are no longer in operation. In spite of the difficulties experienced by exporters, they still employ a significant proportion of Botswana's workforce.

Overall, FDI together with export manufacturing can be growth enhancing and employment generating in Botswana. However, in the case of Botswana, which is a mineral rich country, the competitiveness of sectors like manufacturing is limited in relation to the mining sector. This could be attributed to the damaging effects of the "Dutch disease[24]" problem.

The following recommendations are made:

- The government should continue to encourage foreign direct investment because foreign firms can have a major employment generating impact.

- Since FDI inflows are decreasing, it is necessary for the government and the public to work together to increase the volume of domestic private investment in the non-mining sector to fill the gap left by declining FDI.

- The government should continue to promote the manufacturing sector and other non-mining sectors as these sectors have potential to grow in Botswana. This is an essential step for Botswana to reduce its exposure to the mineral industry and mineral prices.

- The government should try to introduce more incentives geared towards foreign investors, particularly some export and performance related ones. This can help retain existing investors and motivate them to invest further.

It can be concluded that the diversification drive is important for Botswana, which is a mineral rich country. However, considering that the performance of the manufacturing sector is limited in relation to that of the mining sector, there is also a need to promote sectors like services in conjunction with manufacturing to achieve this objective.

[24] The Dutch disease theory states that a primary export commodity boom, for example, diamond exports, may result in de-industrialisation and a negative impact on other sectors of the economy through the appreciaciation and overvaluation of the real exchange rate.

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Appendix A : Long questionnaire

QUESTIONNAIRE OF THE IMPACT OF THE MANUFACTURING SECTOR IN BOTSWANA'S ECONOMY

PART ONE : GENERAL INFORMATION

1. When was the firm established? ……………………..

2. To what extent is your firm integrated into the global network of your parent company? Has this in any way resulted in an increase in exports? If so, why?
………………………………………………………………………………
………………………………………………………………………………
………………………………………………………………………………
………………………………………………………………………………
…………

3. Current number of employees ……..What were the figures in the last three years?

Year	Employment level

4. What is your firms's annual turnover?

   1) 0 million to P10 million
   2) P10 million to P50 million
   3) P50 million to P100 million
   4) P100 million to P150 million
   5) Over P150 million

5. What countries are your competitors? **Please tick the relevant answer. You may tick more than one answer.**
   1) South Africa ……….
   2) Other African countries (excluding South Africa) ……….
   3) Global (Specify country) ………………. ……….
   ……………..

6. What is your firm's origin? **Please tick the relevant answer.**

1) New business (Greenfield) ....
2) Relocation ....
3) Acquisition of local firm ....

7. If the answer to Question 6 is relocation, from which country?

....

PART TWO: MARKETS AND MARKETING

8. Items produced (**list leading items**) ....

....
....
....
....
....
....

9. In what year did you commence exporting?

....

10. What percentage of total sales were exports in the last three financial years?

Year	Percentage

11. At what rate do you expect exports to increase/decline in real terms?

	Next year	Next five years
Decline by over 5% annually		
Decline by 1-5% annually		
No significant change		
Increase by 1-5% annually		
Increase by 6-10% annually		
Increase by over 10% annually		

12. Which of the following reflects the destination of your exports or goods? **Give percentages.**

Percentages

1) South Africa
2) SADC (excluding South Africa)
3) Global (outside SADC) (Specify country)..........................

13. From which of the following sources do you purchase your main inputs? **Give percentages**

Percentages

1) Domestic market
2) South Africa
3) Other foreign supplier (specify country)...........................

14. What is your perception of the sources of the manufacturing sector growth in Botswana? **Give percentages.**

1) Rising domestic demand
2) Import substitution(replacement)
3) Exports
4) Others (specify) ....

PART THREE : LOCATION AND OTHER FACTORS AFFECTING INVESTMENT

15. If this firm had relocated to Botswana, could you mention the main circumstances that were responsible for the closure of the plant abroad.

....
....
....
....
....

16. Which factors were deemed important in selecting Botswana as the best location option? **Please rank up to <u>FOUR</u> important responses (1 = most important response; 2 = second most important response, etc)**

1)	Access to South African market	
2)	Cheap labour	
3)	Low tax rates	
4)	Financial incentives	
5)	Availability/cost of skilled labour	
6)	Availability/cost of unskilled / semi-skilled labour	
7)	Good governance and low levels of corruption	
8)	Strong macroeconomic fundamentals	
9)	Political stability	
10)	Less bureaucracy	
11)	Easy access of work permits for expatriate workers	
12)	Rapid economic growth	
13)	Proximity to suppliers	
14)	Good / low cost infrastructure	
15)	Others (specify)	

17. Were there any particular facilities supplied by this town not found in other places which motivated you to settle here? **Please tick the relevant answer.**

1) Yes ....
2) No ....

18. If yes, what are they?

....
....
....
....
....

19. Which of the following best describes the problems your firm is facing in Botswana? **Please rank up to <u>FOUR</u> important responses (1 = most important response; 2 = second most important response, etc)**

1)	Low Productivity	
2)	High labour costs	
3)	Availability/cost of unskilled and semi-skilled labour	
4)	Availability/cost of skilled labour	
5)	High utilities costs	
6)	High duties on raw materials	
7)	Ending of FAP	
8)	Availability of finance	
9)	High interest rates	
10)	Government bureaucracy	
11)	Access of work permits for expatriate workers	
12)	Others (specify) ……………………..	

PART FOUR : GOVERNMENT POLICIES AND INCENTIVES

20. How would you rate the performance of Botswana Export Development and Investment Authority (BEDIA) and other relevant institutions in attracting investors and making sure that foreign investors are welcomed into the country? **Please tick the relevant answer.**

1) Poor ………..
2) Acceptable ………..
3) Good ………..
4) Very good ……….

21. How could the performance of these institutions be improved?
…………………………………………………………………………………………
…………………………………………………………………………………………
…………………………………………………………………………………………
…………………………………………………………………………………………
…………

22. What Government incentives does your firm use?

1) FAP
2) LPS
3) Others (specify) …………………………..

23. How useful are the Government's incentives in your firm? **Please tick the relevant answer.**

1)	Very useful	
2)	Helpful to a limited extent	
3)	Do not have any impact	

24. If the incentives are not useful, what should be done to make them attractive?
....
....
....
....
....
....

PART FIVE : IMPACTS, HUMAN DEVELOPMENT AND TECHNOLOGY TRANSFER

25. Which of the following are true for Botswana's labour? **Please rank up to three valid answers (1 = most valid response; 2 = second most valid response, etc)**

1)	Labour is efficient	
2)	Labour is trainable	
3)	Low production cost	
4)	High cost of management posts	
5)	Skilled labour is available	
6)	Labour is inefficient	
7)	Labour is not trainable	
8)	Skilled labour is unavailable	
9)	Others (specify)	

26. What do you expect to happen to employment levels in your firm when compared to your current employment level?

		Next year	Next five years
1)	Decline by more than 4% annually		
2)	Decline by 1-4% annually		
3)	Remain at around current levels		
4)	Increase by 1-4% annually		
5)	Increase by more than 4% annually		

27. What do you expect to happen to investment in fixed assets when compared to average investment levels over the past three years?

		Next year	Next five years
1)	More than 30% below last three years		
2)	5-29% below last three years		
3)	No significant change		
4)	5-29% above last three years		
5)	More than 30% above last three years		

28. Training and Education in the firm for the past three financial years.

Year	Percentage of total training bill	Average number of hours of training received annually by production workers

Note : Estimate for year

29. What is your firm's primary means of Human Resources Development with reference to technological capability? Please select more than one if necessary.

1) In-house training courses (including On-the-job training)
2) Re-education at University of Botswana and the country's colleges
3) Re-education at foreign technical education institutes (e.g regional training centres)
4) Visiting foreign companies
5) Attending academic conferences
6) Expertise from parent company
7) Others (Please explain) ....

30. What is your opinion of locally-owned firms in your sector ? **Please rank up to two valid answers (1 = most valid response; 2 = second most valid response, etc)**

1)	Efficient	
2)	Inefficient	
3)	Reasonably efficient	
4)	Don't Know	
5)	Others (specify)	

THANK YOU FOR YOUR COOPERATION

Appendix B: Short questionnaire

QUESTIONNAIRE OF THE IMPACT OF THE MANUFACTURING SECTOR IN BOTSWANA'S ECONOMY

Please return the survey on or before 25 April 2003 to:

Ms Pinkie Maduo
P.O. Box 20395
Gaborone
Botswana

Or Fax number: 3904525

PART ONE : GENERAL INFORMATION

1. When was the firm established? ……………………..

2. Current number of employees ………What were the figures in the last three financial years?

Year	Employment level

3. What is your firms's annual turnover? **Please tick the relevant response.**

   1) 0 million to P10 million ……..
   2) P10 million to P50 million ……..
   3) P50 million to P100 million ……..
   4) P100 million to P150 million ……..
   5) Over P150 million ……..

4. What countries are your competitors? **Please tick the relevant answer. You may tick more than one answer.**

   1) South Africa ……….
   2) Other African countries (excluding South Africa) ……….

3) Global (specify country) ………...   ………

5. What is your company's origin? **Please tick the relevant answer.**
   1) New business (Greenfield) ……….
   2) Relocation ……….
   3) Acquisition of local firm ……….
6. If the answer to Question 5 is relocation, from which country?
   ………………

7. Which of the following best describes the problems your firm is facing in Botswana? **Please rank up to <u>FOUR</u> important responses (1 = most important response; 2 = second most important response, etc)**

1) Low Productivity	
2) High labour costs	
3) Availability/cost of unskilled and semi-skilled labour	
4) Availability/cost of skilled labour	
5) High utilities costs	
6) High duties on raw materials	
7) Ending of FAP	
8) Availability of finance	
9) High interest rates	
10) Government bureaucracy	
11) Access of work permits for expatriate workers	
12) Others (specify) ……………………..	

8. How useful are the Government's incentives in your firm? **Please tick the relevant answer.**

1) Very useful	
2) Helpful to a limited extent	
3) Do not have any impact	

PART TWO: MARKETS AND MARKETING

9. Items produced (**list leading items**) ……………………………..

   ……………………………
   ……………………………
   ……………………………
   ……………………………

10. In what year did you commence exporting? …………………

11. What percentage of total sales were exports in the last three financial years?

Year	Percentage

12. At what rate do you expect exports to increase/decline in real terms?

	Next year	Next five years
Decline by over 5% annually		
Decline by 1-5% annually		
No significant change		
Increase by 1-5% annually		
Increase by 6-10% annually		
Increase by over 10% annually		

13. Which of the following reflects the destination of your exports or goods? **Give percentages.**

	Percentages
1) South Africa	
2) SADC (excluding South Africa)	
3) Global (outside SADC) (specify country)...............	

14. From which of the following sources do you purchase your main inputs? **Give percentages**

	Percentages
1) Domestic market	
2) South Africa	
3) Other foreign supplier (specify country)..........................	

15. What is your perception of the sources of the manufacturing sector growth in Botswana? **Give percentages.**

1) Rising domestic demand	
2) Import substitution (replacement)	
3) Exports	
4) Others (specify)	

16. Which factors were deemed important in selecting Botswana as the best location option? **Please rank up to <u>FOUR</u> important responses (1 = most important response; 2 = second most important response, etc)**

1) Access to South African market	
2) Cheap labour	
3) Low tax rates	
4) Financial incentives	
5) Availability/cost of skilled labour	
6) Availability/cost of unskilled/semi-skilled labour	
7) Good governance and low levels of corruption	
8) Strong macroeconomic fundamentals	
9) Political stability	
10) Less bureaucracy	
11) Easy access of work permits for expatriate workers	
12) Rapid economic growth	
13) Proximity to suppliers	
14) Good / low cost infrastructure	
15) Others (specify) ……………………………...	

PART THREE : IMPACTS, HUMAN DEVELOPMENT AND TECHNOLOGY TRANSFER

17. What do you expect to happen to employment levels in your firm when compared to your current employment level?

	Next year	Next five years
Decline by more than 4% annually		
Decline by 1-4% annually		
Remain at around current levels		
Increase by 1-4% annually		
Increase by more than 4% annually		

18. What do you expect to happen to investment in fixed assets when compared to average investment levels over the past two years?

	Next year	Next five years
More than 30% below last two years		
5-29% below last two years		
No significant change		
5-29% above last two years		
More than 30% above last two years		

THANK YOU VERY MUCH FOR YOUR COOPERATION

Appendix C: Firms interviewed

Abbreviation	Full name
Caratex	Caratex
B & M G.	B & M Garments
Garnet	Garnet Promotions
HMB	Harness Manufacturing Botswana
Sug. Ind	Sugar Industries
Algo	Algo Industries
Prem. Cloth	Premier Clothing
Bolux	Bolux Milling
Din. Textiles	Dinesh Textiles
R. Sun	Rising Sun
West. App	Western Apparels
West. Knit.	Western Knitting Mills
West. Text.	Western Textiles
A. Ancil.	Auto Ancillaries

Appendix D : Data bank for Botswana's exports (1994 -2002, Pula '000)

'ear	Meat & Meat Products	Live Animals	Hides & Skins	Diamonds	Copper Nickel Matte	Textiles	Soda Ash	Vehicles	Other Goods	Total Exports	Meat, Diamonds & Copper
1994	181760	2302	28294	3717797	258787	177351	36779	300645	261284	4964998	4158343
1995	179189	2133	36575	3983684	328449	146286	21800	957144	286211	5941470	4491322
1996	206337	1519	28573	5721880	444745	194296	69066	1144374	322568	8133358	6372962
1997	231387	2257	31973	7670042	480613	248392	109767	1182660	433609	10390700	8382041
1998	298537	2966	33602	6040452	435907	302638	98481	965702	518638	8696922	6774895
1999	223384	1949	23992	9706383	557916	248475	106963	666825	691960	12227848	10487683
2000	263514	1211	43731	11383587	830322	243683	98129	270419	700087	13834682	12477422
2001	365858	6908	61339	12085896	597351	192953	128200	298735	569248	14306488	13443917
2002	31834	3	8195	3341730	130993	37208	39618	101463	144755	3835800	3646528

Source: Trade Statistics, Botswana

Note: Figures for year 2002 are up to April 2002