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Africa's untapped investment potential

Continent offers many opportunities for foreign investors, says UNCTAD

By Ernest Harsch

The potential for highly profitable foreign investment in Africa is enormous, but many investors remain unaware of the past record and current opportunities, argues the UN Conference on Trade and Development (UNCTAD). Although external investment in Africa has been increasing in recent years, it still lags far behind the flows to other developing regions, in part because of the generally negative image of the continent portrayed in the international media, explains the UNCTAD report *Foreign Direct Investment in Africa: Performance and Potential*, released in early July.

"Africa's profitability is one of the best kept secrets in today's world economy," UN Secretary-General Kofi Annan declared a week later, on 12 July in Algeria, at the annual summit meeting of the Organization of African Unity. Specifically citing the UNCTAD report, he noted that Africa also has experienced impressive economic growth rates in recent years, despite the effects of ongoing conflicts, the Asian crisis and depressed commodity prices. Nevertheless, he said, "most chief executives of multinational companies never look in detail at the prospect of any African country. They know Africa only from a few headlines or the odd minute of television news, which show a continent disfigured by conflict."

While a "gross distortion" for Africa as a whole, Mr. Annan said, that negative image has a basis in reality in the wars and economic difficulties that continue to afflict some countries. African leaders therefore "have an obligation to help change that reality," he affirmed, while at the same time highlighting the investment opportunities that currently exist.

Profits and policies

The profitability of foreign companies in Africa has been consistently higher than in most other regions of the world, reports the UNCTAD study. Since 1990, the rate of return on foreign direct investment (FDI) in Africa has averaged 29 per cent, and since 1991 it has been higher than in all other regions, in many years by a factor of two.

Between 1983 and 1997, the rate of return for US companies in Africa has been above 10 per cent, except in 1986 (see graph). Net income from British direct investment in sub-Saharan Africa (excluding Nigeria) increased by 60 per cent between 1989 and 1995. And in 1995 Japanese affiliates in Africa were more profitable (after taxes) than in the early 1990s, and were more profitable than in Asia, where most Japanese investments are concentrated.

In recent years, UNCTAD notes, many African countries have significantly improved their policy environment, bringing both greater economic stability and growth and much more liberal conditions for foreign investors. Of 32 least developed countries in Africa covered in a 1997 survey, 26 had a liberal or relatively liberal regime for the repatriation of dividends and capital. In many African countries, the report emphasizes, policies toward foreign investment are now similar to those in most other developing countries. In addition, numerous investment promotion agencies have been set up across the continent to publicize Africa's economic opportunities and facilitate investment.

Partly in response to these changes, flows of FDI to Africa have been increasing significantly during this decade. Annual average FDI inflows rose from \$1.9 bn in 1983-87 to \$3.1 bn in 1988-92, then nearly doubled to \$6 bn in 1993-97. However, these increases pale by comparison with the explosion of foreign investment to developing countries as a whole, which rose from an annual average of \$20 bn in 1981-85 to \$75 bn in 1991-95. As a result, Africa's share of total inflows to developing countries dropped from 11 per cent in 1976-80 to just 4 per cent in 1996-97.

Dynamic 'frontrunners'

However, such overall trends and continent-wide averages obscure the great variation among African countries, observes the UNCTAD report. Two countries, Egypt and Nigeria, have traditionally accounted for a high share of FDI inflows to Africa, in part because they have relatively large economies. Their share of total FDI inflows has been declining, however, from 67 per cent in 1983-87 to 38 per cent in 1993-97. Many other African countries received very small inflows, reflecting the small size of many economies, although the report notes that in such countries FDI "may have a much higher developmental impact" than elsewhere.

More recently, UNCTAD reports, a number of African countries have been attracting rapidly increasing FDI inflows. These "frontrunners" -- Botswana, Equatorial Guinea, Ghana, Mozambique, Namibia, Tunisia and Uganda -- took one-quarter of all FDI inflows in 1996, although they collectively accounted for just 9 per cent of Africa's population and 8 per cent of the continent's gross domestic product (GDP).

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-- Kofi Annan, UN Secretary-General

Most of these dynamic "frontrunners" share a number of features: they have stable and predictable policy and macroeconomic environments, active privatization programmes, higher GDP growth rates over the past decade, favourable trade policies, relatively well-developed infrastructure, intense investment promotion activities and efforts to improve the education levels and skills of their people. Their performance shows that "being located in Africa does not per se rule out success in attracting foreign firms."

While the primary sector (oil and minerals) was once the main target of foreign investment in Africa, the report observes, this is changing. Services and manufacturing now are taking growing shares of FDI inflows, even in oil-exporting countries like Nigeria. With more than 25 sub-Saharan governments in the process of privatizing all or part of their telecommunications sectors, these areas of activity hold great potential for attracting more foreign investment, UNCTAD affirms.

African TNCs

Meanwhile, not all African countries have only inward flows of FDI. Some African firms are growing into transnational corporations (TNCs) and investing in other countries, UNCTAD reports, citing two mining houses based in South Africa, a food-processing firm in Morocco and Zambia's large copper mining enterprise, among others. In 1997, the total FDI stocks of African TNCs held outside their own countries stood at \$43 bn, 13 per cent of the external stocks of all developing countries that year. Although still relatively small and few in number, these African TNCs nevertheless "have become important regional and subregional players, demonstrating that there are firms in Africa that can compete internationally," the report observes.

To help realize Africa's untapped investment potential, the report concludes that it is essential to change "the negative and stereotypical picture of Africa, which still prevails among large parts of the business community and the wider public outside the continent."

African countries themselves can do much to attract more foreign investments, UNCTAD says. It urges African governments to make every effort to ensure political and economic stability, promote private-sector development and engage in greater dialogue with private enterprises. There is much room for further policy improvements, and the report suggests that countries consider initiating "investment policy reviews" in collaboration with UNCTAD (six African countries already are doing so).

Those countries currently receiving little FDI should improve their promotional efforts, perhaps by highlighting the opportunities in particular industries or projects. Citing the example of successful investment promotion agencies in Europe and Asia, the report argues that "it is crucial to concentrate promotional efforts on a limited number of home countries and industries." Collaboration among groups of African countries also can help, both in mounting collective promotional initiatives and in establishing subregional markets that are more attractive to potential investors. The report cites efforts in this direction in Southern Africa, East Africa and North Africa.

The home countries of transnational corporations also can do more to encourage increased investment in Africa. UNCTAD notes a variety of initiatives already under way: various schemes by the European Union to support investment in Africa, the Africa-Asia Investment Information Centre headquartered in Malaysia, and an investment and trade agreement between the US and South Africa (similar US framework agreements are currently under negotiation with Ghana and the Economic Community of West African States).

Donor agencies should provide greater technical assistance to improve labour and management skills in Africa, as well as the physical infrastructure, says UNCTAD. Developed countries also should open up their own markets more to products manufactured in Africa, thus enabling external investors to take better advantage of Africa's plentiful and cheap labour force.

Donor countries also should take more energetic action to help reduce Africa's debt burden, the report argues, noting that high debt-servicing costs deprive African countries of badly needed savings for domestic investment to improve the physical and human infrastructure. "Debt reduction," says UNCTAD, "should thus be a cornerstone of the international community's efforts to improve Africa's growth prospects in general and its attractiveness for FDI in particular."

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