FDI in Africa

Policy brief no.4 - October 2010

Over the past two decades, foreign direct investment (FDI)[1] has become a vital source of economic development for the African continent. With an increase from approximately US$ 9 billion in 2000 to US$ 18 billion in 2004 and US$ 88 billion in 2008,[2] FDI has become a major source of finance for Africa's development.

This is particularly striking when considering that ODA flows to Africa reached US$ 44 billion in 2008, only half of FDI inflows. Foreign investors can provide many benefits to African economies: in addition to bringing more capital, tax revenues, exports and export diversification, foreign investors can also inject new technologies and corporate know-how into the local economy through fostering close linkages with local suppliers.

For FDI to contribute fully to economic and social progress in Africa, host-country governments need to create a policy environment that enables them to maximize development returns on investment. Governments should thus develop a set of policies that are not only focused on investment promotion, but also address issues such as human capital, infrastructure and enterprise development, and are likely to increase FDI spillover effects and contribute to economic diversification. This is all the more important because FDI in Africa, with a share of about 5% of global flows, remains small compared to flows to and among industrialised and major emerging countries.[3]

Although the natural resources sector is traditionally a major recipient of FDI flows to Africa, high-value activities in services and manufacturing have recently attracted important investments. In addition, the food crisis has stimulated foreign investors' interest in Africa's arable land. The agricultural sector has faced scant investment leading to low productivity in the past, and a rapid increase in global and domestic demand in recent years. At this crucial juncture, the

This document is part of a series of policy briefs produced by the United Nations Office of the Special Advisor on Africa (OSAA) and the NEPAD-OECD Africa Investment Initiative for African policymakers and their development partners. The policy briefs provide an overview of key economic and development issues affecting Africa today. They are available at www.un.org/africa/osaa, and at www.oecd.org/daf/investment/africa. For more information, please contact: David Mehdi Hamam, Chief (OSAA) at hamamm@un.org or Karim Dahou, Executive Manager (NEPAD-OECD Initiative) at karim.dahou@oecd.org.

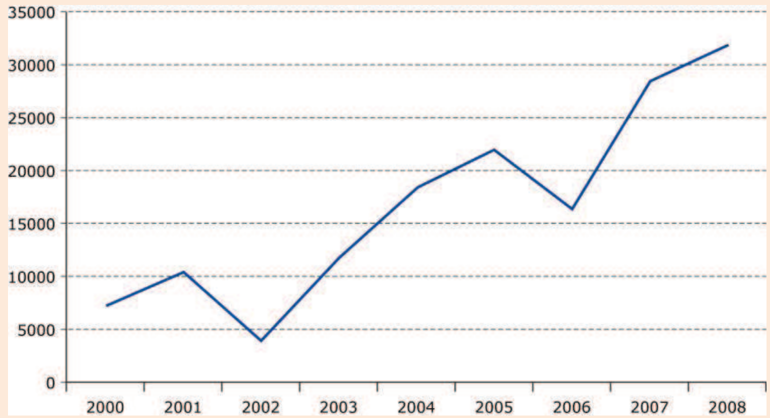
United Nations
Office of the Special Adviser on Africa

NEPAD-OECD AFRICA INVESTMENT INITIATIVE

FDI inflows to Africa fell 36% in 2009, ending 6 consecutive years of increases

After a record high in 2008, the continent saw its FDI inflows falling by 36% in 2009. This marked the end of six consecutive years of increases in FDI flows to Africa.To take only a single example, FDI flows from OECD countries to Africa reached a record level of US$ 32 billion in 2008, compared to about US$ 4 billion in 2002[4] (Figure 1).

Figure 1. FDI Outward flows from OECD countries to Africa, 2000-2008 (US$, millions)



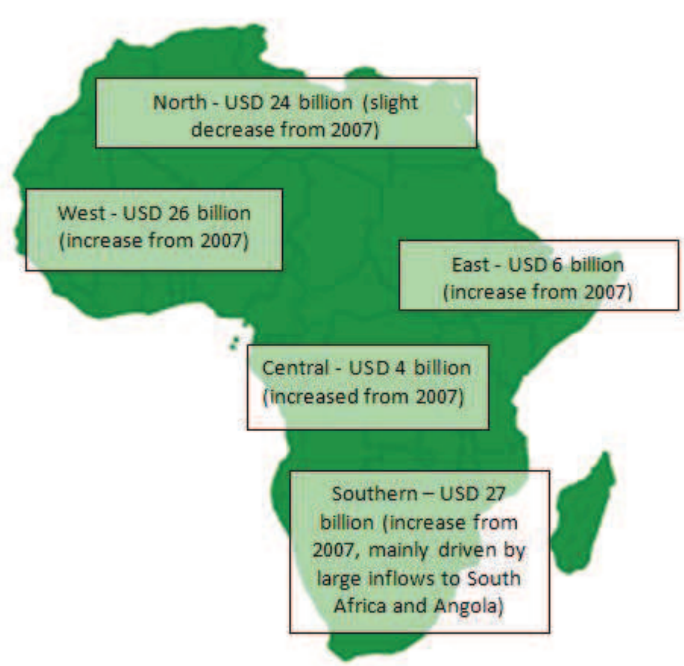
Source: OECD FDI database

Regional distribution shows that natural resources like gas and petroleum attract FDI

As for the regional distribution of FDI in Africa, the North, West and South of the continent attract the bulk of foreign investment. Much of this investment is driven by these regions' large reservoirs of natural resources such as gas and petroleum.[5] Figure 2 provides an overview of the 2008 figures of global inflows, before the effects of the crisis hit the continent in full force.

An important new development in FDI flows to Africa over the past decade is the increase of investment from non-OECD countries, especially from Asia and Africa itself, such as South Africa, Egypt and Morocco.

Figure 2. Regional distribution of FDI in Africa



Source: adapted from UNCTAD WIR 2009

Although Asian investment in Africa predominantly targets the energy sector, there are important investments in the telecommunications and real estate sectors[6] (Table 1). New investors are also active in areas that are particularly important to Africa's development agenda, such as infrastructure and agriculture. A great share of foreign investment in agriculture is undertaken through sovereign wealth funds (SWFs), yet the implications of this development are still to be fully grasped. Moreover, even though the media have recently highlighted land-grabbing by foreign investors in Africa, thorough analysis of the matter is needed to assess the potential benefits and drawbacks that foreign investment could bring to Africa's agriculture.

Table 1. Selected 10 Asian greenfield FDI projects in Africa, 2002-2006 (US$, millions)

Value	Company	Source Country	Industry	Year	Destination Country
6000	ONGC	India	Energy	2006	Nigeria
4300	PetroVietnam	Viet Nam	Energy	2006	Algeria
3600	Pertamina	Indonesia	Energy	2005	Libyan Arab Jamahiriya
1500	Huawei Technologies	China	Telecom	2006	Ethiopia
1300	Marvis	Singapore	Energy	2006	Gabon
1000	Petronas	Malaysia	Energy	2005	Sudan
1000	CNPC	China	Energy	2003	Sudan
413	RanHill	Malaysia	Real Estate	2006	Libyan Arab Jamahiriya
400	Global Formwork	Malaysia	Real Estate	2005	Nigeria
392	BHEL	India	Energy	2006	Sudan

Source: Adapted from UNCTAD, Asian foreign direct investment in Africa, 2007

Impact of the Crisis

The global economic crisis has led to a decrease in demand, and a subsequent drop in export revenues which has adversely affected Africa's commodity-based economies. In addition, remittances have shown a marked decrease, investors are more risk averse and investment prospects are less bright.

At the beginning of the crisis, FDI inflows to Africa were hardly affected, but the figures for 2009 show a drop of about 39% from the previous year. This decline is partly due to the decrease of cross-border M&As, which are a major driver of FDI on the continent. Least Developed Countries (LDCs) absorbed the bulk of the impact, as the drop in demand for commodities had a negative effect on FDI flows to natural resource-based economies.*

Altough this says little about FDI distribution among sectors, this decline has reduced government revenues, exports, employment and African companies' access to capital, new technology and corporate know-how. Nevertheless, investment policy reforms have helped mitigate the crisis' consequences and should allow the continent to take full advantage of the recovery.

* http://www.unctad.org/en/docs/webdiaeia20101_en.pdf.

Policy challenges and opportunities

Another encouraging sign is that African countries have resisted adopting protectionist policies and the policy environment has remained conducive for FDI. The drop in FDI inflows necessitates an effective response on the part of African governments. This might include using export surpluses in oil-rich countries to diversify and steer the economies towards higher value-added activities. Host government policies should also continue to promote domestic linkages, particularly in sectors like agri-business and services. In addition, implementing a sound policy framework for Public Private Partnerships (PPP) can help attract FDI in public utilities and infrastructure.

Outlook and prospects

Although it is difficult to predict the FDI outlook for Africa with certainty, we can expect foreign investment in agriculture to continue increasing. First, Africa's inward FDI stock in agriculture accounts for just 7% of the total stock in developing countries – compared to 78% for Asia and Oceania, and 15% for Latin America and the Caribbean.[7] This clearly illustrates the potential for increasing the investment rate in a sector in which global FDI tripled from US$ 1 to US$ 3 billion a year, as a result of rapidly rising demand and prices, land and water shortages in some emerging economies and increasing demand for biofuel.

To make the most of agricultural investment for Africa's development, strong policy action is needed from both home countries and host states. It entails implementing international standards for responsible business conduct, while also enhancing host-country policy frameworks. Such an effort would complement other policy priorities like improving the overall business climate, diversifying FDI sources and attracting foreign investment to high value-added activities. Africa should thus quickly overcome the crisis and sustain its course for social and economic progress.

Notes

1 FDI as treated here refers to "a category of cross-border investment made by a resident in one economy (the *direct investor*) with the objective of establishing a lasting interest in an enterprise (the *direct investment enterprise*) that is resident in an economy other than that of the direct investor. The motivation of the direct investor is a strategic long-term relationship with the direct investment enterprise to ensure a significant degree of influence by the (former) in the management of the (latter)." Definition from the OECD Benchmark Definition of Foreign Direct Investment, 4th ed. 2008.

2 UNCTAD World Investment Report 2009.

3 However, given the small size of African economies, FDI flows to Africa as a percentage of GDP reach South-East Asia's levels.

4 OECD FDI database – data does not include figures from New Zealand (2003, 2005, 2006, 2008), Canada and Mexico. For Norway, only data from 2005, 2006 and 2007 are included.

5 Manufacturing, especially in Northern Africa, is also a major FDI driver. However, the recent increase in FDI flows to the manufacturing sector was due to a few individual acquisitions (UNCTAD World Investment Report 2009, p.46).

6 Adapted from UNCTAD, Asian foreign direct investment in Africa, 2007.

7 UNCTAD World Investment Report 2009, p.116.