

NEPAD and the Challenges of Attracting Foreign Direct Investment in Africa

Zein Kebonang and Sesupo Mosweu

Abstract

The New Partnership for Africa's Development (NEPAD) asserts that to meet its developmental challenges, Africa will have to rely more on foreign direct investment (FDI) than aid. Given the fact that aid flows to Africa have significantly declined over the years and that the continent has now to compete with other countries particularly former communist states in Eastern Europe for the same pool of resources needed for development, reliance on FDI is pragmatic. Nonetheless, the emphasis on FDI appears curious given that the continent has and continues to attract very low volumes of FDI as compared to other regions. Granted that FDI can be an important source of economic growth, it is also instructive that many of the African countries that attract or have attracted significant levels of FDI have made little progress in achieving sustainable economic growth. To understand this paradox, this paper looks at the factors that inform FDI inflows and Africa's relative strength in relation to those factors.

Introduction

The New Partnership for Africa's Development (NEPAD) places greater emphases on the importance of foreign direct investment (FDI) as Africa's new engine of economic growth. Despite this emphasis, the continent remains the least attractive to FDI. Attempts at attracting more FDI through fiscal concession and promulgation of investor friendly laws and regulations have on the whole yielded little success. Although the level of FDI inflows differ from country to country, as a continent Africa attracts less than 3 percent of world wide FDI inflows. Given the centrality of foreign direct investment (FDI) to NEPAD, this paper, seeks to highlight the challenges facing NEPAD in its FDI drive. These challenges are evaluated against the eclectic theory on FDI (or OLI paradigm) that has been put forward by Dunning.

Africa's Attempts at Attracting FDI

In an effort to attract more FDI, a number of African countries have over the years undertaken reforms geared primarily at improving their business environment. These reforms have included changes in the legislative and regulatory framework governing investment; the elimination of price controls on a number of products and inputs; the liberalization of producer markets in some cases; the privatization of state-owned enterprises; financial sector reforms; the liberalization of foreign exchange markets; the establishment of export promotion agencies and the establishment or review of investment codes (Economic Commission for Africa 1997; UNCTAD 1998; 1999b; 2003a; 2004b; Basu and Srinivasan 2002:15).

Trade liberalization reforms which have involved opening up domestic markets to foreign goods and competition, have been at the center of most reforms in many African countries. The main argument in favour of trade liberalization reforms has been that such reforms are crucial to the expansion of the size of markets, in enhancing economies of scale and productive efficiency and in facilitating rapid industrialization (Charlton and Stiglitz 2005:296; Dodzin and Vamvakidis 2004:322; George and Kirkpatrick 2004:441). These liberalization reforms mark a departure from the "tariff jumping" hypothesis which asserted that trade restrictions stimulated investments by encouraging multinational corporations (MNCs) to invest in countries to which it was difficult to export their products (Asiedu 2002:111; Nunnenkamp and Spatz 2002:2; Sachs and Warner 1997:358). It also represents a move away from import-substitution policies which aimed at developing domestic manufacturing capability by restricting both the number of imported goods and imposing tariff and non-tariff barriers to trade (Rodrik 1996:12).

Dornbusch (1992:69-70) argues that there are at least four reasons that have given impetus to trade liberalization reforms. These are: a) the need to limit the role of the state. Under this "anti-state" view, the state is regarded not so much as playing a beneficial role in the market but rather as overly intrusive because of its attempt to regulate every market activity; b) poor economic performances, which have occurred partly as a result of the failure of macroeconomic policies and an adverse external environment, resulting in massive debt crises and hyperinflation; c) advancements in information technology which have made information instantly available and exposed citizens worldwide to opportunities available in other countries; and d) pressures from the World Bank/IMF which have made trade liberalization a central condition of their lending.

Undoubtedly, the opening up of markets has had far-reaching implications for the role of the state in the economy. No longer is the state seen as the dominant player in the market.

According to Picciotto (1998:737), whilst liberalization may have initially been limited to the removal or reduction of national barriers to the flows of commodities and capital, the opening up of markets to increased competition has involved the ending of direct state intervention, whether by ownership, structural controls, or informal support of cartels and entry restrictions.

Despite the trade liberalization efforts of many African countries and the pursuit of market friendly policies, there have been limited FDI inflows. The failure by MNCs to react to these reforms could be explained by a number of factors. First, many reforms have been donor driven. Being externally imposed therefore, they have lacked a domestic constituency to sustain them. Second, some reforms have either been inchoate or *ad hoc* (Asiedu 2002:115; Morisset 2000:2; World Bank 1994; Rodrik 1992). As a result, foreign investors have been less convinced about the credibility and sustainability of the reforms, seeing them as transitory and subject to reversal.

Reversal is considered to be more likely because once an investment is made, there is a shift in the bargaining power in favour of the host state (Janeba 2004: 384). But for investors, once an investment is made, especially one which involves physical infrastructure, such an investment cannot be fully withdrawn. Any loss associated with the withdrawal of the investment is borne by the investor. Hence, the lack of credibility, the change in bargaining power and the failure to protect and enforce property rights have tended to dissuade investors from making long-term commitments in Africa. In addition, as many of the reforms have been introduced as part of the aid conditionality, there is a perception that such reforms would be abandoned once aid ends. This uncertainty surrounding the sustainability and credibility of reforms has led investors to either withhold making long-term investments or shift their investments to other regions (Rodrik 1991:230; Aizenman 1992:163).

FDI and the OLI Paradigm

Perhaps to understand fully why Africa has and continues to receive low FDI inflows, one must begin by considering the factors that drive FDI inflows. Although several theories have been advanced to explain the determinants of FDI, none has been more influential than Dunning's eclectic theory on FDI (Dunning 1981; 1988; 1995; 1998; 2000; Asiedu 2004:43; Gastanaga, Nugent, Pashamova 1998:1300; Sethi, Guisinger, Ford and Phelan 2002:688; Markusen 1995:173).

The general thrust of the eclectic theory is that there are at least three sets of advantages that influence the decision of multinationals to expand abroad: ownership, locational and internalization advantages (the OLI paradigm). This OLI paradigm essentially attempts to

answer three basic questions about FDI: (1) Based on present and potential ownership advantages, should a particular firm be involved in foreign markets? (2) Based on location advantages, where should the firm invest abroad? and (3) How should the firm serve foreign markets? Should it be through internalization (FDI or sales subsidiaries) or through arms length arrangements (such as licensing or export through intermediates)? (Oxelheim, Randoy and Stonehill 2001:384; MacMillan 2003:283).

In this OLI paradigm, the “O” stands for ownership-specific (that is, firm specific) advantages. Broadly, these firm-specific advantages relate either to intangible (sometimes referred to as knowledge-based assets) or physical capital assets. Knowledge-based assets of a firm are embodied, for instance, in the human capital of the employees, patents, copyrights, trademarks or the reputation of the firm (Markusen 1995:174). The physical assets relate to equipment and machinery. Thus, in deciding whether to undertake FDI a firm must have developed strong and specific characteristics that enable it to be competitive in the home market. These characteristics must be transferable abroad and strong enough to compensate for the extra costs and barriers that confront those who try to do business abroad (Dunning 1988:2). Firm-specific characteristics typically possessed by successful multinational enterprises are the proprietary knowledge or know-how incorporated in: (1) economies of scale and scope, (2) managerial and marketing expertise, (3) advanced technology stemming from a heavy emphasis on research and (4) differentiated products (Oxelheim, Randoy and Stonehill 2001:384; Dunning 1988:2).

The “L” in the OLI paradigm is concerned with the “where” of production (Dunning 1988:4) and stands for location-specific advantages that skew FDI to a particular market (MacMillan 2003:284; Oxelheim, Randoy and Stonehill 2001:385). The location advantage depends on a number of factors and can be influenced by the host country’s comparative advantage or its transactional cost advantage, including the absence of a tariff on products produced in it (Gastanaga, Nugent, Pashamova 1998:1300).

Lastly, the “I” in the eclectic paradigm is concerned with the mode of entry of the foreign investment. Multinational corporations may enter the host country through licensing, export or direct foreign investment. The “I” factor explains why a firm would, for instance, choose to serve a foreign market through FDI rather than pursue alternative modes (licensing or exporting) without ownership control of foreign activity (Oxelheim, Randoy and Stonehill 2001:386; see, also, MacMillan 2003:283; Eicher and Kang 2005:208). For many foreign investors, FDI is usually a superior mode of entry than technology licensing or exporting as it allows them to expand and exploit opportunities more efficiently abroad without concerns that

their trade secrets would be exploited (Yeaple 2003:293-294; MacMillan 2003:283; Barrios, Gorg and Strobl 2000). As Markusen (1995:182) points out, because internalization focuses on characteristics of knowledge capital as opposed to physical capital, by investing directly rather than through licensing, the firm is able to eliminate or minimize certain risks. These risks include (a) the need to reveal its process or product technology to a potential licensee, (b) the danger that the licensee may use information acquired during the licensing period to set up a rival domestic corporation that competes directly with it and (c) the possibility that the quality of its products may be compromised (this is likely to occur when the licensee produces inferior substitute products for want of supervision).

The OLI Paradigm and Africa's Competitiveness in Attracting FDI

What may be discerned from the OLI Paradigm, is that a broad range of factors such as market size, macro-economic stability, effective institutions, political stability, good governance, infrastructure, availability of skilled labour and raw materials will be crucial in influencing both the location and the extent of the investment made by foreign investors. Given these factors, this section assesses Africa's relative strengths or weaknesses in an attempt to explain why the continent has not fared well in terms of FDI inflows.

As noted earlier, an ideal location is one of the factors that influences investment decisions. Although investors may be attracted to different locations because of their strategic importance, ultimately, socio-economic and political factors will affect the choice of the investment location. On a comparative basis, Africa has limited locational advantage compared to its competitors such as Asia and Latin America. African economies are small and fragmented and their capacity to attract FDI has been determined largely by their natural resources and the size of their local market, resulting in the uneven distribution of FDI across the continent. Countries that have been able to attract the most FDI have been those with the largest tangible assets such as natural and mineral resources as well as large domestic markets. Traditionally and even currently, these countries have mainly been South Africa, Nigeria, Ivory Coast and Angola (Morisset 2000:18; Basu and Srinivasan 2002:4; UNCTAD 2004b:40). These are all large countries, both in terms of area and population. They also have access to the sea, especially the Atlantic Ocean making connection to Europe and America easy.

Equally, unlike any other continent, Africa has had prolonged periods of political instability and strife. Nearly 20 countries (or about 40 percent of Sub-Saharan Africa) have over the past 40 years experienced at least one period of civil war (Elbadawi and Sambanis 2000:244; Herbst 2000:270; Guillaumont, Jeanneney and Brun 1999:91). Political instability, whether in

the form of actual or aborted *coups*, has increased the uncertainty in the socio-economic and political environment. It has adversely affected and retarded Africa's economic growth rate as large resources are diverted from providing basic social services to finance wars and huge military campaigns (Murshed 2002:387; Fosu 2004:1187). Although political risk or instability has been used here to refer to civil wars, it should be noted that the term extends to cover such things as disruption of production activities, confiscation or damage to property and threats to personnel (Lucas 1993:394). The instability created is usually not conducive to thriving domestic and foreign investment. In fact, a study by Brempong and Traynor (1999:80) has found that political instability in Sub-Saharan Africa has negatively impacted on economic growth by reducing the levels of investments being undertaken.

Ironically, political instability may not, in and of itself, affect a country's locational advantage. This is particularly true in cases where the returns on investments are so high as to outweigh the dangers posed by such instability. For instance, Angola, which has just emerged from a 30-year-old civil war, and Nigeria which has until recently been subjected to military dictatorships, have been able to attract high proportions of FDI than the relatively more stable countries like Botswana, Namibia and Mauritius. Most of the FDI to Angola and Nigeria has been in the petroleum industry where the significant returns on investment have outweighed the risks involved (Asiedu 2002:113).

Apart from political instability, locational advantage may be enhanced by both micro and macro-economic stability. Under microeconomic reforms, there is a decentralization of economic decision-making from the state to the private sector, so that market forces drive the economy (Dunning 1993:69). On the other hand, macro-economic stability, which is concerned with governmental monetary and fiscal policies, is important in stabilizing exchange rates and keeping inflation and government expenditure down (Rogoff and Reinhart 2003:4; Trevino, Daniels and Arbelaez 2002:31; Basu and Srinivasan 2002:7; Mlambo and Oshikoya 2001:40). High inflation rates and huge government budgetary deficits tend to erode returns on investment as governments resort to imposing higher taxes to finance their expenditure. Except for a few countries, government budget deficits and inflation rates are higher in Africa than in other regions. Average inflation rate for the continent has increased over the years: from 34 percent in 1996 to 47 percent by 1997 (UNCTAD 1998:169). As Table 1 below shows, by 2001 a number of countries had inflation rates way in excess of 40 percent.

Table 1. African Countries for Which the Average Inflation Rate During 1970-2001 was above 40 Percent

Country	Average Annual Inflation, 1970-2001
Congo, Dem. Rep. of the	1,112.9
Angola	345.4
Uganda	67.2
Ethiopia	43.0
Zambia	41.1

Source: Rogoff and Reinhart (2003:8). Table slightly modified.

A study by Mlambo and Oshikoya (2001: 12) has found that despite implementing economic reforms aimed at improving the economic environment, investment in Africa is yet to show a robust improvement. According to the study, the sluggish response by investors to these reforms has been primarily due to the uncertainty regarding fiscal, financial and monetary policies. In the face of high inflation rates and government budgetary deficits, an important consideration is usually to achieve macro-economic stability. Bringing down inflation and government deficits sends positive signals to the private sector about the direction of economic policies and the credibility of the authorities' commitment to manage the economy efficiently (Mlambo and Oshikoya 2001:27). Such stability encourages savings and capital accumulation by the private sector because it allows for long-term planning and investment decisions to be made (Mlambo and Oshikoya 2001:27).

Similarly, Africa's competitiveness has been affected by its lack of or limited technological advancement and its poorly developed infrastructure. As NEPAD notes in its base document, if Africa had the same basic infrastructure as developed countries, it would be in a position to focus on production and to be internationally competitive (Paragraph 98 NEPAD Base Document 2001). Although good infrastructure increases the productivity of investments and hence stimulates FDI inflows, Africa's infrastructural development not only lags behind but is also less reliable (Asiedu 2002:111; Collier and Gunning 1999a:71, Mlambo and Oshikoya 2001:23; Limao and Venables 2001; Fabayo 1996:358). This lack of basic infrastructure has handicapped its economic growth and development. In some perverse cases, the incentive has been not to develop the infrastructure but to keep it in a state of disrepair for political ends. The following passage from Hoff and Stiglitz (2001:424) is instructive on this point:

When President Juvenal Habyarimana of Rwanda asked for armed support to help fight an insurgency, Mobutu responded, *'I told you not to build any roads...building roads never did any good...I've been in power in Zaire for thirty years and I never built one road. Now they are driving down them to get you* (emphasis added).

Likewise, the existence of authoritarian dictatorships and unaccountable governments has made its fair contribution to the continent's lack of development. Whilst several studies have found either a negative, positive or no correlation between democracy and economic growth (see, for instance, Milner and Kubota 2005; Ali and Isse 2005; Busse 2003; Addison and Heshmati 2003; Manuel and Ho Sung 1995; Alesina and Rodrik 1994; Helliwell 1994; Przeworski and Limongi 1993), it would appear that, even accepting the argument that democracy cannot on its own lead to economic development in the absence of complementary growth enhancing-factors, the dominant view remains that democratic rather than authoritarian regimes offer a relatively stable environment within which stable policies and economic growth may be achieved or maintained (Quinn and Woolley 2001:637; Ali and Isse 2004:251; Milner and Kubota 2005:137). In short, prosperity is likely to be achieved in a democratic setting rather than in an authoritarian one.

The recent wave of democratization in Africa has had mixed outcomes: some countries have been more successful in the progress of democratization but others less so. Once in office, some political leaders have sought to lengthen the number of terms they serve in office despite clear constitutional term limits. Attempts by President Frederick Chiluba of Zambia to run for a third term in office (which was constitutionally prohibited) failed to materialize. This was not for lack of trying on his part but because of sustained external pressure and internal opposition to constitutional amendments to allow for a third term (Ihonvbere 2003:79). In Namibia, President Sam Nujoma succeeded in getting constitutional amendments passed to allow him a third term in office. Ultimately, the success or failure by African leaders to adhere to basic democratic principles may have a bearing on whether investors feel confident or uneasy about the continent as an ideal investment location.

Good governance is another important factor that has a bearing on locational advantage. NEPAD and indeed a vast literature on governance proclaim that good governance is a key element in attracting FDI (see, for example, UNCTAD 2004c: 3; Kaufmann and Kraay 2003; Hellman, Jones and Kaufmann 2002; Gathii 2000: 971; Wei 2000:1; Campos, Lien and Pradhan 1999:1065). However, it would appear that the extent to which good governance has

a bearing on FDI depends largely on the sector in which the investment is being made. The primary sectors (such as mining) seems less affected by poor governance than the secondary sectors (manufacturing) of the economy. For instance, Nigeria, which has consistently been classified by Transparency International (2002; 2003; 2004; 2005) as the second most corrupt country in the world, has been able to attract more investments than the relatively less corrupt and well-managed countries like Botswana and Namibia. It would appear as if corruption is an advantage in certain contexts. Nigeria's vast oil reserves and the profits derived from it have seen a continuous influx of foreign investors.

Africa's bad reputation and its rating by international credit agencies has also helped to undermine the continent's locational advantage. The global media by focusing mainly on matters such as famines, desertification, refugees, human rights violations, *coup d'etats*, internecine violence and health problems, has managed to project a negative image of the continent (World Bank 1989:23). In alluding to this negative image, NEPAD indeed reiterates that unless investors' perception of Africa as a "high-risk" continent is addressed as a matter of priority, there will be little private capital flows to the continent (paragraph 151 NEPAD Base Document 2001). Ratings that are comprised of weighted indexes reflecting a country's macro-economic and financial performance and prospects, and an assessment of institutional factors such as the degree of bureaucratic delays, governance, corruption, the respect for property rights and contract enforceability have generally been negative for Africa (Aron 2003:472). Although the continent is made up of 53 independent states—that differ in their political, social and economic development—the tendency has been to regard the continent as though it were a monolithic state. This failure to distinguish between states has meant that no proper distinction or assessment is made between exemplary, mismanaged and rogue states. Consequently, FDI inflows to the continent are often affected by the failure to distinguish between states. Not surprisingly, a country in Africa, whatever its potential, receives less FDI by virtue of its geographical location (Asiedu 2002:116; Gelb 2002).

Africa's poorly developed and inefficient institutions have likewise made the continent less attractive to FDI. In countries such as Somalia, Liberia and Sierra Leone, the formal institutions necessary to promote and secure the rule of law, as well as to enforce property and contractual rights do not exist. In these countries, the regulation of social, political and economic life has become dependent on informal structures and on warlords who have divided some of the countries into mini-territories (Aron 2003:473). The lack of formal and effective institutions has not only meant that citizens but also foreigners remain vulnerable to extortion and violence.

In other countries such as Zimbabwe and Swaziland, although formal institutions exist, they have failed to limit government's arbitrariness. In Zimbabwe, for instance, a court judgment calling upon the state to allow a privately owned newspaper, (which had previously been shutdown by government) to resume publication was ignored by government—the judgment being described by Jonathan Moyo, Zimbabwe's Information Minister at the time as “outrageously politically, unacceptable” (BBC News 19th December 2003 World Edition). Disturbingly, it is not only court decisions that have been ignored in Zimbabwe: judges too, have been coerced into leaving office by threats and intimidation. As the BBC reported, the Chief Justice of Zimbabwe, Anthony Gubbay, was compelled to resign from Office “after a self-styled war veteran [who had been let by the police into the chief justice's office] had forced him to step down or face the consequence” (BBC News 2nd March 2001 World Edition).

Remarkably, the Zimbabwean case is not an isolated one. In many African countries the institutional environment within which the business sector and foreign investment can thrive is lacking; the judiciary is not insulated against interference from the executive branch of government and a fair legal framework that is enforced impartially hardly exists. Studies by Collier and Gunning (1999b:86) show that only “a quarter of African lawyers consider the judiciary fully independent of the executive. The legal process often involves delays, and most judicial officers appear to be only moderately knowledgeable about the law”. Since 2003 for instance, Swaziland has been operating without a court of last resort after the entire Court of Appeal bench resigned in protest against what the judges perceived to be the government's flagrant disregard of the court's decisions (Mosoti 2004:172).

Incidents of corruption in the judiciary are also common. In Kenya, it has been reported that to secure a favourable court judgment, it takes as little as US\$50 to bribe a magistrate, between US\$636–20,356 to bribe a high court judge and as much as US\$190,800 to bribe a court of appeal judge (BBC News 3rd October 2003 World Edition).

In recognition of what the above limitations have placed on Africa's socio-economic growth, NEPAD commits the continent to improve and adhere to principles of good governance (political and corporate), democracy, peace, respect for the rule of law, and human rights, infrastructure development, capacity building and sound economic management (paragraph 71; 151 NEPAD Base Document 2001). Whilst its commitment to these principles is laudable, the greatest test will be in translating intent into action.

FDI and the “Resource Curse”

As noted earlier, in terms of the OLI paradigm, there are three sets of advantages that must exist for MNCs to engage in FDI. These are: (a) ownership (O) advantage which makes it profitable for the MNC to invest or relocate abroad (b) location (L) advantage which is typically linked to the host country's specific characteristics and (c) internalization (I) advantage which allows the MNC to manage the advantage internally rather than to license it or trade through the market. Although Africa fares poorly in terms of attracting FDI particularly in its manufacturing sector, the continent has been successful in attracting more FDI to its natural resource sector (UNCTAD 2004b:39). In terms of the OLI paradigm, it is its location advantage that explains investment in its primary sector. This is an area in which the continent enjoys considerable advantage over other regions and it is an area that is particularly important to many economies in the continent. In 2001, for instance, oil production generated 20 percent of the combined gross domestic product (GDP) of sub-Saharan and accounted for between 64 and 82 percent of government revenues in Angola, Democratic Republic of Congo (DRC), Equatorial Guinea, Gabon and Nigeria (Herringshaw 2004a:175). Similarly, in 2002, mining constituted about eight percent of the GDP of the Southern African Development Community and 43 percent of the region's exports, with countries such as Botswana, the DRC, Namibia and Zambia all deriving over 50 percent of their export earnings from the mining sector (Herringshaw 2004:175).

Several factors explain why the continent has attracted more investments in its mineral sectors than in its manufacturing and agricultural sectors. Apart from the obviously huge profits in the mining sector, this sector is not affected by the lack of infrastructure or the poor economic state of the host economy. It is also capital intensive and therefore requires less labour. On the other hand, the manufacturing sector is adversely affected by lack of domestic markets, lack of skilled labor, high transport costs, macro-economic instability and poor infrastructure. Likewise, drought, poor soils, acidic rains, tropical climates and low investment profits have made investment in the agricultural sector unattractive (Sachs and Warner 1997:340). Although Africa could have a comparative advantage in the agricultural sector, agricultural subsidies by the United States and the European Union to their farmers have made African agricultural products uncompetitive in the international market. As important as investment in the mining sector is, one of the major setbacks with its dominance over the economy is that it tends to lead to the neglect of both the agricultural and manufacturing sectors of the economy (Shaxson 2005:314-15; Karl 1999:43; Sachs and Warner 1999:16). This has been particularly true in many countries that are either oil or diamond driven. The discovery of oil in Nigeria and Equatorial Guinea saw a decline in the importance of both manufacturing and agriculture in the national economy (Shaxson 2005:314-15; Kraxberger

2004:414; Frynas 2004: 542; Awe 1999:11), as did the discovery of diamonds in Botswana. The neglect, shrinkage or weakening of the competitiveness of non-mining sectors (agriculture and manufacturing) may on the whole be harmful if such sectors had major positive spillovers or externalities in the economy (Sachs and Warner 1999:16; Auty 1999:59).

Nonetheless, despite huge FDI inflows into the mining sector, Africa has not been transformed socially, politically or economically. Whilst one would expect to find economic growth and prosperity, Africa's natural resource wealth has paradoxically promoted poor leadership, led to economic stagnation, conflict, engendered corruption, poverty, poor governance and exacerbated underdevelopment (Herringshaw 2004: 174; Sachs and Warner 1999:19). In other instances, it has led to the criminalization of the state where government officials acting in concert with criminal associates plunder national resources (Wood 2004: 553). Except in notable cases such as South Africa, Botswana and Namibia, many countries that have abundant natural resource wealth appear to suffer from a phenomenon known as the "resource curse" or the "paradox of plenty" (Herringshaw 2004:174; Ross 1999:297; Karl 1999:32). Rather than lead to economic prosperity, the natural resource "blessing" has instead corrupted governance, destabilized economies, increased rent seeking and poverty (Sachs and Warner 1999:19).

Even though the problem of underdevelopment is not limited to just resource-rich countries but also extends to resource-poor countries, the latter countries have often been able to undertake developmental reforms much more quickly than the former. In resource-rich countries, particularly oil-rich states, the pace of reform is often sluggish and the problem of underdevelopment is more pronounced (Karl 1999:36). Whilst one would expect mineral economies, given their additional import capacity and extra investment resources which mineral exports provide, to outperform other developing countries, ironically some have been outperformed in economic growth by resource poor economies (Sachs and Warner 1999:13; Auty 1999:55). Oil booms and the ability to secure more funding by using oil as collateral has allowed leaders of "petro-states" to avoid or to prolong the implementation of badly needed reforms compared to other developing countries (Karl 1999:36). The availability of petrol money not only pre-empts efforts to mobilize domestic resources through taxation, but also reduces tolerance for austerity and produces a dangerous reliance upon the state for the resolution of all problems (Shaxson 2005:315; Karl 1999:36). As Sachs and Warner (1999:14) put it, "resource abundance blocks countries from the kind of beneficial structural change that often accompanies the development process". The failure to undertake the necessary reforms

in “petro-states” is usually directly linked to the perverse incentive structure shaping the behaviour of both politicians and business leaders. According to Karl (1999:36):

What distinguished oil states from other states, above all else, is their addiction to oil rents. Where this oil addiction takes hold, a skewed set of both political and market incentives so penetrate all aspects of life that almost anything is eventually up for sale. Actors in oil states do not behave the same as they do elsewhere; they simply don't have to. Oil companies, for example, do not assess political risk in the way that other firms do. They will continue to operate in the midst of civil war...even where widespread regional unrest threatens stability.

The problem of underdevelopment and perverse corruption in the “mist of plenty” has been manifestly demonstrated in Angola, Equatorial Guinea and Nigeria. In Angola, for instance, more than one billion dollars of government income from oil (20 percent of the total) has been disappearing every year since 1996 (Herringshaw 2004:174). Similarly, in Equatorial Guinea, although recent oil discoveries have transformed the country's once stagnant economy into one of the fastest growing economies, it has also fostered economic underdevelopment and political mismanagement (Frynas 2004:541; Wood 2004:547). Living standards for the majority have fallen despite the huge rise in GDP per capita. The country's wealth has become concentrated in the hands of a tiny elite whilst most of the population barely survives through subsistence agriculture (Wood 2004:553; Frynas 2004:542). Describing how the country's leadership, from the office of the President to government ministries have become part of a criminal syndicate, Wood (2004:553) states:

[Whilst] there are many recorded instances where the African state has degenerated into a kleptocracy, characterized by the intense personalization of authority and the voraciousness of a small government elite and its constituents, the Equatoguinean state however is relatively distinct on account of both the extreme personalization of authority and the government's relationship with a range of legal, quasi-legal and criminal supporting enterprises. *Indeed, it is one of the*

few African countries that can be correctly classified as a criminal state (emphasis added).

Likewise, despite it being the largest oil producer in Africa and the fifth largest in the Organization of Petroleum Exporting Countries (OPEC), Nigerian oil revenue, which accounts for 90 percent of the foreign exchange and 80 percent of the federal revenue, has benefited only a few individuals to the exclusion of a vast majority of the citizens who have remained indigent (Manby 1999:284; Awe 1999:11; Picciotto 2003: 141). Instead of the oil wealth transforming the country into one of the most successful states in Africa, it has led to worsening levels of poverty and underdevelopment. Over the years, the percentage of people living in poverty in Nigeria has been increasing. Whilst this percentage stood at 28.1 percent in 1980, by 1996 it had reached 65.6 percent (Kraxberger 2004:415; see, also, Shaxson 2005:311). Despite its huge oil reserves, the country remains one of the poorest in the world, with a per capita gross national product of US\$ 260 a year (Manby 1999:284). The bulk of the oil revenue, which is distributed to the central government, is dissipated through corruption involving political leaders and government officials (Kraxberger 2004:414; Picciotto 2003:141). As noted earlier, Nigeria has come to enjoy an invidious reputation as being one of the most corrupt countries in the world (Transparency International: 2002; 2003; 2004; 2005). Manby (1999:285) articulates the problem of corruption and economic exclusion in Nigeria as follows:

Minority ethnic groups in Nigeria's multi-ethnic Federation have successfully demanded that new states and local government units be established over the years in the hope that they will receive some benefits from the oil money and be compensated for the damage done by oil production. Paradoxically, however, the Nigerian federation has become ever more centralized in practice, and power and money have been concentrated in the hands of fewer and fewer people. *Politics has become an exercise in organized corruption, most spectacularly demonstrated around the oil industry itself, where large commissions and percentage cuts of contracts have enabled individual soldiers and politicians to amass huge fortunes. Meanwhile the majority of Nigerians have sunk deeper in poverty (emphasis added).*

Just like in Equatorial Guinea, at the heart of Nigeria's underdevelopment and corruption has been the country's political leadership. Successive Nigerian governments, whether military or civilian, have all succeeded in mismanaging the national economy to the point of collapse by "salting the [oil wealth] away in [their] foreign bank accounts rather than investing it in education, health and other social programs" (Manby 1999:298; see, also, Kraxberger 2004:415). Ironically, the hypothesis that poor leadership, bad governance and corruption keeps away investors is clearly qualified by the Nigerian, Angolan and Equatorial Guinean cases. These three countries continue to receive large FDI inflows especially in their oil industry. Nigeria has in fact been one of the largest recipients of FDI in Africa (UNCTAD 2000a; 2003a; 2004b). Angola, Nigeria and Equatorial Guinea, are not the only African countries afflicted by the "resource curse". This also extends to the "blood diamond" syndrome affecting the Great Lake nations such as Liberia, Sierra Leone and the Democratic Republic of Congo (DRC).

Conclusion

Attracting significant inflows of foreign direct investment will require Africa to seriously address the myriad socio-economic and political problems besetting the continent. The OLI paradigm discussed in the paper is instructive in its explanation of what drives FDI. Factors such as political and macro-economic instability, poor infrastructure, absence of skilled labour, lack of effective and efficient institutions, absence of the rule of law and unfavourable climatic conditions point to the fact that there is nothing distinctive about Africa. In fact, in term of the OLI paradigm, these are some of the many disadvantages of investing in Africa. However, investment in the primary sector, particularly in the oil industry, explains perfectly well why the OLI paradigm works. Unlike in the manufacturing sector, in the primary sector, oil companies do not have to share their trade secrets or worry about whether there are effective institutions in the host country. Because they have the expertise and the technical knowledge of how to extract oil, they have an internal (I) advantage which allows them to come in as foreign investors. Secondly, returns on oil or other minerals mean that locational disadvantages matter less. They can import their own capital, infrastructure and rely less on local institutions to do business. In seeking FDI and diversifying African economies must not only address institutional and structural factors but must also in the process promote investor confidence. Without investor confidence, investment reforms and liberalization efforts will remain only that. A more realistic approach for NEPAD lies not only in attracting increased FDI inflows but also identifying the comparative advantages of each African country so that countries do not compete for the same investor. In other words, different countries must be able to attract different types of FDI.

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