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Foreign Direct Investment in Africa- Mali Attracts Foreign Investment

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Abstract: In general African countries have not been very successful in attracting Foreign Direct Investment (FDI). Some by their (abundant) natural resources and the size of their domestic market were able to attract multinational companies. We estimate FDIBC function which indicates that Mali has generated the interest of international investors by improving his business environment, suggesting that one country can become competitive internationally and attracts FDI on a sustainable basis.

Key words: Foreign Direct Investment (FDI), natural resources, multinational companies, FDI business climate (FDIBC), sustainable basis

INTRODUCTION

Recent literature has highlighted the role played by FDI on economic growth. It is argued that FDI has been a major channel for the access to advanced technologies by recipient countries and hence plays a central role in the technological progress of those countries (Borensztein *et al*., 1998). Besides, FDI seems to promote growth through the generation of productivity spillovers. Furthermore foreign, investment may increase the volume of international trade.

Most of the empirical work about the impact of foreign direct investment in host countries has been focused in the Southeast Asian region. Nevertheless, issues related to the contribution of FDI flows in Latin America are less well-known, in spite of the increasing importance of foreign investment in this region. This region is increasingly arousing the interest of transnational corporations and experiencing a dramatic growth in foreign capital inflows, particularly in the form of foreign direct investment. Latin America and the Caribbean is the second developing region in what concerns to the reception of FDI, only surpassed by Southeast Asian countries. According to ECLAC (1999), in 1998 Latin America and the Caribbean countries received approximately 41% of total FDI flows destinated to developing countries. Although most of the countries in this region benefited from increased foreign capital inflows, these flows have been concentrated in only a few countries. Brazil, Mexico and Argentina are the main recipient countries receiving almost two thirds of FDI flows destinated to the region.

There is increasing agreement, both among developed countries and in the developing world, about the types of benefits which are likely to accrue to the host economy from FDI. This is particularly the case for technology and management expertise, as multinational enterprises seem to be one of the principal vehicles for the international transfer of technology. The link between technology and economic growth has been highlighted by an OECD study of both OECD and developing countries, which have found a significant effect on economic growth from the innovation and diffusion of technology (OECD, 1991).

Furthermore, foreign investors can contribute to economic growth because they tend to be more productive than local firms. An analysis of 282 pairs of foreign and domestic firms of similar size drawn from 80 manufacturing industries in Brazil concluded that foreign firms have a significantly higher ratio of value added to output than domestic firms (Wilmore, 1986). Similar results are obtained by De Gregorio (1992) in twelve Latin American countries and by Borensztein *et al.* (1995) for a sample of 69 developing countries.

Another mechanism through which FDI can affect growth is by the generation of productivity spillovers. Blömstrom and Persson (1983) and Blömstrom (1986) find evidence that FDI has led to significant positive spillover effects on the labor productivity of domestic firms and on the rate of growth of domestic productivity in Mexico (Blomström and Wolf, (1994). Kokko (1994, 1996) argues that this effect may arise from a process of competitive interactin between foreign and domestic firms, finding empirical evidence that spillovers are more likely in Mexican manufacturing where foreign and domestic firms are in direct competition and where the technological gap between them is not too greativ.

More direct evidence bearing upon this hypothesis is provided by Kokko *et al*. (1996) who find, for Mexico and Uruguay, that spillovers are difficult to identify inindustries where foreign affiliates have much higher productivity levels than local firmsv.

Nevertheless, the effect of FDI on economic growth is an empirical question as it seems to be dependent upon a set of conditions in the host country economy.

Firstly, the benefits from FDI rely on the technical capability of host country firms. According to Blomström, Globerman and Kokko (2000) there are a greater number of studies estimating direct productivity spillovers for developing countries than for developed countries. The former tend to produce more mixed results than the latter. These authors argue that the reason for these mixed results is that FDI contributes to economic growth only when a sufficient absorptive capability of the advanced technologies is available in the host economy.

Secondly, the beneficial impact of FDI is enhanced in an environment characterized by an open trade and investment regime and macroeconomic stability. In this environment, FDI can play a key role in improving the capacity of the host country to respond to the opportunities offered by global economic integration (OECD, 1998). In the absence of such environment, FDI may thwart rather than promote growth. It may serve to enhance the private rate of return to investment by foreign firms while exerting little impact on social rates of return in the recipient economy (Balasubramanyam, Salisu and Sapsford, 1996).

Direct investment may encourage export promotion, import substitution, or greater trade in intermediate inputs, especially between parent and affiliate producers (Goldberg and Klein, 1998).

Most of multinational firms' investment is an export-oriented investment, so foreign investment can increase the speed with which a host economy can become integrated within a global production network in sectors in which it may formerly have had no industrial experience (OECD, 1998). This is the main conclusion obtained by Rodriguez Clare (1996) and also by Calderón, Mortimore and Peres (1996) who argue that multinational enterprises have been leaders in some of the most important industries on which Mexico has based the expansion of its industrial exports.

African countries attract Foreign Direct Investment (FDI) by their natural resources and the size of their local markets. The apparent lack of Interest of Transnational Corporations (TNCs) in African countries that have attempted to implement policy reforms has also contributed to support this argument. The balkanization of African countries is frequently used as an argument that this continent has been much less favored than Asia and Latin America over the past decade. It has been argued that the reforms in many African countries have been incomplete and thus have not fully convinced foreign investors to develop activities that are not dependent on natural resources and aimed at regional and global markets. True, it takes time for a country to modify its image, especially when the State has a long tradition of policy intervention and when the reforms have been mostly symbolic with the adoption of new texts that have not yet been translated into actions.

Mali has been able to attract FDI by improving his business climate. This country shows that pro-active policies and reform-oriented Governments can generate FDI interest. It simply makes the point that African countries can also be successful in attracting FDI that is not based on natural resources or aimed at the local market, but rather at regional and global markets, by implementing policy reforms. An econometric analysis of the case of Mali illustrates which policy factors have played a significant role in the improvement of his business climate at least in the views of foreign investors.

WHY? DETERMINANTS OF FDI IN AFRICA

Although there has been a considerable number of analytical and empirical studies on FDI inflows, there has been a limited consensus on which factors play an unambiguous role in explaining the location decision of TNCs. It is generally accepted that market size and access to natural resources are crucial determinants in the the location decision of TNDs processes.

Not surprisingly, the African countries that have been able to attract most FDI have been those with the largest tangible assets such as natural and mineral resources as well as large domestic markets.

The role of natural resources in the location decision of TNCs is apparent through the sectoral allocation of FDI inflows within the region. Traditionally, about 60% of FDI in Africa is allocated to oil and natural resources. The Africa region possesses not only large reserves of oil, gold, diamonds and copper but also more than half of the world's cobalt and manganese, one third of bauxite and more than 80% of chromium and platinum. The sub-continent is also among the main exporters of agricultural products such as cocoa, coffee and sugar.

The strong reliance of African countries on their natural resources and market size has been well evidenced by earlier research.

It might be more pertinent to look at which Mali has been successful in attracting FDI over the past few years, not because his natural resources and the size of his domestic market. HOW? To answer we normalize the value of total FDI inflows by GDP and the total value of natural resources For example,for twenty countries of Africa, we label this indicator as the business climate for FDI (FDIBC):

$$FDIBC_i = FDI/(GDP_i * NR_i)\ \alpha \qquad (1)$$

Table 1: FDI inflows and GDP: ranking of 29 African countries, average 1996-1997

Country	FDI inflows	GDP
South Africa	23135	129094
Nigeria	1566.0	36540
cote d' lvoire	305.1	10251
Angola	265.5	7396
Tanzania	154.0	6707
Uganda	148.0	6555
Namibia	109.9	3453
Ghana	101.3	6762
Senegal	92.2	4542
Mozambique	68.3	1944
Zimbabwe	66.5	8512
Zambia	64.0	4051
Mali	61.6	2532
Mauritius	46.7	4151
Cameroon	40.0	9115
Benin	31.5	2137
Guinea	20.6	3998
Chad	16.5	1603
Kenya	16.2	9899
Madagascar	12.1	3552
Congo Rep.	8.5	2298
Central African Republic	5.5	954
Ethiopia	5.0	6330
Rwanda	2.4	1771
Congo Dem. Rep.	1.5	6904
Malawi	1.5	2424
Burundi	1.0	1137
Niger	1.0	1858
Siera Leone	1.0	940

Millions of dollars

where FDI is defined as the FDI inflows in country GDP as the gross domestic product and NR the value of natural resources (all of them expressed in dollars).

Equation 1 assumes that the elasticities of FDI inflows to changes in GDP and natural resources are both equal to unity (a = 1), which seem consistent with the estimated elasticities that will be reported later in the study for the group of African countries surveyed in this research (Table 1).

Our indicator captures the attraction Mali for FDI based on everything except on his natural resources and market size. Therefore, it reflects not only policy and political variables but also a series of structural factors such as infrastructure, transport costs and human capital.

The ranking of 29 African countries according to the indicator in 1995-1997 (Table 2), the most attractive country was Namibia, followed by Mali, On the other hand, Mali and Mozambique have not been ranked very high by the ICRG and II indexes but are among the most attractive countries according to our indicator.

The FDI cannot be explained by the size of the local market and the availability of natural resources. It reflects not only the policy and political environment in a host country but also a series of factors such as the

Table 2: Business Climate for FDI: ranking of 29 African countries, average 1995-1997

country	FDI/business climate[a]	ICRG political risk	Institutional investor[c]
Namibia	1	1	Na
Mali	2	12	13
Mozambique Zambia	3	11	18
Chad	4	4	14
Senegal	5	NA	NA
Angola	6	13	6
Benin	7	18	20
Mauritius	8	NA	12
Cote d'Ivoire	9	NA	1
Tanzania	10	8	8
Uganda	11	5	10
Central Afr Rep	12	15	11
Ghana	13	NA	NA
Madagascar	14	7	4
Burundi	15	9	NA
Rwanda	16	NA	NA
Zimbabwe	17	NA	NA
Congo Rep	18	4	3
Nigeria	19	14	19
Niger	20	17	15
Guinea	21	20	NA
Malwi	22	19	17
Cameroon	23	6	7
Kenya	24	16	9
South Africa	25	5	5
Ethiopia	26	2	2
Siera Leone	27	10	15
Congo Dem.Rep.	28	21	22
	29	22	21

Sources: Author's own calculations; Pigato (1999).

[a] The business climate index is defined as net FDI inflows normalized by GDP and the total value of natural resources in each host country.

[B] Political risk rating based of option of banks,TNCs and other institutional investors indicating corruption, political and juridical institutions.

[c] Institutional investors rating measures a country's creditworthiness, which is mostly determined by economic and financial variables.

geographical location, infrastructure and the stock of human capital. The ICRG and II indexes capture only the political and financial risks in each country. Another major difference is that these indexes are built with investors' surveys, mainly international banks and thus are more subjective and forward-looking.

Mali has shown significant changes in his business climate over the past decade. Foreign investors have recognized a real progress, FDI inflows jumped about 600, 100 and 90%, respectively, between 1993-1994 and 1995-1997 (Table 3).

What makes a business climate attractive in Mali?

As non oil exporting and landlocked country, Mali would have made the strongest effort to improve his business climate to attract foreign investors. There are two-complementary approaches that can be followed to attempt to define what Mali has been doing right.

First, an econometric analysis can help to identify the main factors. Second a description of the policy reforms implemented in the country may be practical starting point.

Table 3: Comparison over time of the business climate for FDI in Africa

Rank	Average 1986-1990	Average 1991-1994	Average 1995-1997
1	Zambia	Benin	Namibia
2	Mauritius	Namibia	Mali
3	Chad	Chad	Mozambique
4	Benin	Zambia	Zambia
5	Rwanda	Mozambique	Chad
6	Niger	Angola	Senegal
7	Congo,Rep	Mauritius	Angola
8	Central African Rep	Senegal	Benin
9	Repub. Guinea	Ghana	Mauritius
10	Namibia	Uganda	Cote d'Ivoire
11	Madagascar	Madagascar	Tanzania
12	Angola	Nigeria	Uganda
13	Mozambique	Guinea	Central African Rep
14	Senegal	Rwanda	Ghana
15	Nigeria	Tanzania	Madagascar
16	Cote d'Ivoire	Congo,Rep	Burundi
17	Kenya	Mali	Rwanda
18	Burundi	Zimbabwe	Zimbabwe
19	Ghana	Malawi	Congo,Rep
20	Ethipia	Burundi	Nigeria
21	Malawi	Kenya	Niger
22	Uganda	Cote d'Ivoire	Guinea
23	South Africa	Ethipia	Malawi
24	Mali	South Africa	Cameroon
25	Congo Dem.Rep	Congo Dem.Rep	Kenya
26	Cameroon	Cameroon	South Africa
27	Zimbabwe	Niger	Ethipia
28	Siera Leone	Central African Rep	Siera Leone
29	Tanzania(N/A)	Siera Leone	Congo Dem.Rep

ECONOMETRIC ANALYSES

We tested a number of explanatory variables. The selection of these variables was done on the basis of the existing literature and the following equation was chosen:

$$FDIBC_t = a_0 + a_1 g + a_2 IR + a_3 T + a_4 Tm + a_5 Up \quad (2)$$

with: FDIBCt = business climate for FDI at time t
g = GDP growth
IR = Illiteracy rate (percent of people aged 15 and above)
T = Trade/GDP
TM = Telephone mainlines (per 1,000 people)
UP = Ratio of urban to total population

A brief explanation might be necessary for our selection of explanatory variables, which has been partly driven by the availability of data in the World Bank's database. The economic growth rate should influence positively the business climate for FDI as it reflects an improvement in economic performance. Most recent studies have also evidenced that the degree of openness, as measured by the trade share in GDP, should influence positively foreign investors through trade liberalization and higher competitiveness. The illiteracy rate should be inversely related to the availability of relatively skilled labor-a major factor in the location decision of TNCs. The number of telephone lines per 1,000 people is viewed as an indicator of infrastructure and communication development. Finally, the recent literature has argued that investors can be lured by concentration of other companies or customers, since it reduces their transport costs and there are evident economies of scale in the development of backward and forward linkages. This argument might be partially captured by the share of urban population (as a percentage of total population). Note we will also test the relationship between our indicator of business climate and the political and financial risks indicators reported in the preceding section.

We estimated Eq. 2 for the panel data of 29 countries over the period 1990-1997. Alternatively, we proceeded with cross-country regressions using the average values of the selected variable during the same period. The panel data regression includes fixed-term effects because the results from testing the homogeneity of such effects indicate that the changes in the FDI business climate include critical time correlated elements common to all countries.

The estimated results of our panel regression indicate that GDP growth rate and trade openness have been positively and significantly correlated with the investment climate in Africa (Table 4). The positive impact of trade openness seems to confirm the arguments that trade liberalization leads to a more general reduction

Table 4: Econometric results: sensitivity of business climate to policy variables (T-statistics in parenthesis)

	Panal data (FDI business)		Cross country (FDI business)	
Dependente variable	FDI business climate	FDI inflows	FDI business climate	FDI inflows
Economic growth	0.123		0.101	0.587
	(1.90)		(1.71)	(1.96)
Trade openness	0.163	2.812	0.172	1.812
	(2.43)	(3.23)	(1.94)	(1.50)
	-0.209	1.097	0.139	0.489
Illiteracy rate	(-0.39)	(1.09)	(1.33)	(0.80)
Telephone lines	-0.0404	-0.407	0.0129	-0.144
	(-0.51)	(-0.42)	(0.15)	(-0.46)
Urban population	-0.978	-0.228	-0.0937	-0.525
	(-1.21)	(-1.26)	(-0.49)	(-0.63)
GDP		0.91		1.415
		(3.97)		(4.28)
Natural resources		0.92		1.214
		(7.09)		(3.89)
Adj R^2	0.08	0.433	0.040	0.56
Number of observations	236	236	29	29

in administrative barriers and improve the business environment in the host economy-countries with low trade barriers also tend to have low barriers to FDI -as well as conveys the right signal to the international business community (Lall, 2000). In a more specific context, free trade zones have been much successful in attracting FDI with stable, growing economic environment and trade liberalization (Madani, 1999). In contrast, the illiteracy rate, the number of telephone lines and the share of urban population do not appear to have been major determinants in the business climate for FDI in the region. Those results corroborate those obtained in the cross-country regression. Note that we also tested the impact of political and financial risks (as measured by ICRG and II), but these did not appear significant in the business climate in our (cross-country) regressions. These findings are not surprising in view of the significant differences in the rankings presented in Table 2, but contradict somewhat the results obtained in other studies. For example, Zdenek Drabek and Warren Payne (1999) found a highly positive correlation between the ICRG index and FDI for a sample of countries, including both industrial and developing countries. The inclusion of only four African countries in their sample may explain the difference between their and our estimated results.

The above results are indicative but should be interpreted with caution because of several statistical and econometric problems. There are numerous data shortcomings in most African countries. For example, it would be interesting to separate how much of the FDI inflows were the result of privatization receipts; but the data were not consistent and available for the surveyed countries over a sufficient period of time. Also, the variables used in the regressions may capture imperfectly the relationship with the business climate; for example the number of telephone lines does not always reflect the quality and costs of the telecommunication infrastructure in each country. The same problems can be associated with the illiteracy rate and the urban population. The estimated effects of the GDP growth and trade openness might be biased because of causality problems since changes in the business climate may determine and be determined by the GDP growth rate. Foreign companies may simultaneously follow or push the trade liberalization effort in a country.

To circumvent these statistical and analytical shortcomings, one could use more sophisticated econometric techniques or alternative indicators. Instead, we propose to examine more closely the experience of economy of Mali - that has shown major improvements in his business climate during the 1990s, as reported in Table 3. If, in terms of FDI growth, the performance of Mali appears less impressive, it has to be taken into account that its geographical position (landlocked) is not as favorable.

WHAT HAS MALI BEEN DOING RIGHT?

This can be hard to summarize because establishing an attractive business climate for FDI is a multidimensional effort. Yet, a few major actions can be identified (see table 5 for details and chronology). First, it appears that has established a stable macroeconomic environment, at least by regional standards, for a prolonged period of time. The political climate also became secure after a period of high instability.

Mali used aggressive trade liberalization and privatization programs to attract foreign investors. The Governments approved important pieces of legislation, including new Mining (1991) and Investment (1995) Codes in Mali

Mali used aggressive trade liberalization and privatization programs to attract foreign investors. The Governments approved important pieces of legislation, including new Mining (1991) and Investment (1995) Codes in Mali

Moreover, the adoption of international treaties related to FDI helped to increase the Governments' visibility in the international business community as well as provided additional insurance to potential foreign investors. Last but not least, the President has played an important role in promoting the country abroad.

The same argument obviously applies to privatization. As an illustration of this multiplier effect, it suffices to look at the investment projects financed by the International Finance Corporation (IFC)-the private arm of the World Bank Group-in Mali over the past few years. Those investments range from projects in banking to printing and tourism, for a total commitment of $65 million and $134 million in Mali, respectively, as of June 1998. Interestingly, while that in Mali ranked in sixth position, greater than that in Nigeria, Cameroon or Ghana. We believe that the IFC's portfolio allocation illustrates well the interest of the international private community in Mali and the progress that they have achieved in their business climate.

MAJOR ACTIONS IN MALI

Macroeconomic stability: The macroeconomic indicators improved dramatically, as real GDP growth reached approximately 7% in 1997, up from 0.6% in 1990.

Average annual inflation, as measured by the consumer price index for Bamako, was reduced from 12.4% in 1995, to 4% in 1998. Both the external account deficit and fiscal deficit were reduced and a prudent credit policy was pursued.

The economic growth rate jumped from 4.0% in 1990 to 13.3% in 1997.
Inflation was reduced from 70% in 1994 to single digits by 1997.

Trade liberalization : The trade openness ratio increased from 49% in 1990 to 60% in 1997, with a reduction in tariffs and the elimination of several non-tariff barriers.

The trade openness ratio increased from 53% in 1990 to 63% in 1997. In 1996, the Government rationalized and lowered the tariff structure, averaging around 14%.

Privatization: After a slow start, privatization receipts reached $22 million in 1997, including the sale of several enterprises in the financial and manufacturing sectors.

Focus on one/few major projects: Investment projects in the mining sector (gold) were realized by Rand Gold and Ashanti, facilitated by the reform of the Mining Code in 1991.

Political stability: In March 1991, a series of clashes between the people and the army culminated in the arrest of the President. In January 1992, the Alliance pour la democratie au Mali (ADEMA), leading a coalition of opposition parties, established electoral dominance, while its candidate was elected President. He was recently reelected in May 1997 for another five-year term.

Implementation of new laws and accession to international agreements related to FDI:

- Mining Code (1991)
- Investment Code (1995)
- Multilateral Investment
- Industrial Free Zone (1994)
- Multilateral Investment
- Guarantee Agency (1994)
- Guarantee Agency (1992)
- Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1994).
- World Intellectual Property Organization (1996)
- Convention on the Settlement of Investment Disputes between States and Nationals and States (1995)

A final word of caution might be necessary. In Mali, there is still much room for improvement in areas such as infrastructure, transport costs and human capital.

CONCLUSIONS

Spectacular improvement in the business climate during the 1990s reveals that the implementation of a few visible actions is essential in the strategy of attracting FDI. Beyond macroeconomic and political stability, Mali focused on a few strategic actions such as:

- Opening the economy through a trade liberalization reform.
- Launching an attractive privatization program.
- Modernizing mining and investment codes.
- Adopting international agreements related to FDI.
- Developing a few priority projects that have a multiplier Effects on other investment projects.
- Mounting an image building effort with the participation of high political figures including the President.

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