

**AN ECONOMETRIC STUDY OF THE DETERMINANTS OF FOREIGN DIRECT
INVESTMENT (FDI) IN SADC COUNTRIES**

By

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ABSTRACT

The growing global competition for foreign direct investments (FDI) has seen many countries and regional economic blocks adopting innovative and bolder investment promotion strategies and policies to attract FDI. Against this background, this paper reviews the experiences of SADC countries in attracting foreign direct investment and explores the major determinants of FDI in the SADC region. A cross-country panel regression analysis using data from 1996-2011 for SADC countries was applied to ascertain the determinants of FDI. The estimation results from a panel of SADC member countries show that agglomeration, credit to private sector, urban population share, trade openness, market size and infrastructural development have a positive significant relationship with FDI inflows in the region. The major recommendation from the study is the need to improve both institutional and governance indicators to create a conducive business environment for FDI. There is also need for SADC member countries to remove restrictions on market seeking and locational advantage FDI. Member states also need to strengthen regional integration and greater diversity on investment matters for the region to benefit from synergetic effects of regional integration through the halo effect.

Key Words: Foreign Direct Investment, Panel Data Analysis, Hausman Test, Fixed Effects, Random Effects

JEL Classification, F21, F23

ETUDE ECONOMETRIQUE DES FACTEURS DECISIFS DES INVESTISSEMENTS DIRECTS ETRANGERS (IED) DANS LES PAYS DE LA SADC

SOMMAIRE

La concurrence croissante dans le domaine des investissements étrangers directs (IED) a abouti à l'adoption par plusieurs pays et blocs économiques régionaux de stratégies et politiques de promotion des investissements novatrices et plus audacieuses en vue d'attirer les IED. A la lumière de cette réalité, ce document examine l'expérience des pays de la SADC dans leurs activités d'attraction des IED et explore les principaux facteurs décisifs des IED dans la région de la SADC. Une analyse transfrontalière de régression sur panel, basée sur des données couvrant la période 1996 – 2011 pour les pays de la SADC, a été faite pour identifier les facteurs décisifs des IED. Les résultats des estimations d'un panel de pays membres de la SADC démontrent que l'agglomération, le crédit au secteur privé, la part de la population urbaine, l'ouverture commerciale, la taille du marché et le développement des infrastructures sont un corolaire important des flux des IED dans la région. La recommandation principale de l'étude est qu'il faut améliorer les indicateurs institutionnels et de gouvernance pour créer un environnement commercial propice aux IED. Il faut également que les pays membres de la SADC lèvent les restrictions sur les IED de recherche des marchés et d'avantages d'implantation. Les états membres doivent également renforcer l'intégration régionale et diversifier les domaines d'investissement dans la région afin de bénéficier de la synergie des efforts d'intégration régionale par l'effet de halo.

1.0 INTRODUCTION

Global competition for FDI has intensified, against the backdrop of continued global economic and financial fragilities and inadequacy of domestic resources to meet investment needs in most economies. Concomitantly, investment promotion strategies employed by countries to attract FDI have also continued to change in a bolder and innovative manner. The increased competition for FDI has seen a number of countries and regional blocs putting in place policies to enhance FDI attraction at both country and regional level. Consistent with this, SADC has passed a number of protocols and policies such as the Finance and Investment Protocol (FIP) and Free Trade Area (FTA) in a bid to enhance the investment climate at regional and country level. Although these policies are yet to be fully implemented, they have already taken root in enhancing the appeal of SADC as an attractive investment destination.

Notwithstanding these developments, SADC member countries still face enormous challenges in building a conducive environment for FDI, as reflected by varied and uneven patterns of FDI flows within the region. Major challenges relate to adverse political developments and political risks, lack of the requisite legislation to protect investment, energy and infrastructural bottlenecks, corruption and weak integration processes at the regional level. Some countries in the region score very low in terms of institutional and governance indicator rankings, such as doing business and government effectiveness. This has deterred potential FDI inflows and negatively affected the regions' growth potential, amid vast untapped resources.

Recommendations from various researchers⁴ point to the need to reduce the cost of doing business and improving infrastructure such as roads, rail and telecommunications, necessary to bring down the comparatively high investment costs for investors. Reports issued by multilateral organizations, such as the World Bank (WB), and their rankings concerning the investment climate of the respective country or region are an international dimension that also affects FDI inflows in SADC. These rankings are seriously considered by investors when making a decision about whether or not to invest in a particular sector in the region.

In addition, barriers to entry still exist in some SADC countries, where certain sectors are reserved for indigenous people. In some cases, investors avoid investing in some SADC member countries due to policy uncertainty and contradictions and high levels of corruption. Although most SADC countries have improved their regulatory frameworks by permitting profit repatriation and

⁴ See for example, FDI in SADC Countries prepared by the Centre for Chinese studies

providing tax and other incentives to attract investment, the challenge remains on the need to attract investment in high value added sectors.

The combination of the various schools of thought on factors affecting FDI in different economies and its impact on economic development highlights the need for empirical research on this subject matter. Against this backdrop, this study seeks to investigate why some SADC countries continue to receive more FDI inflows compared to others, despite comparable resource endowments and common policy stance and direction. The answer to this question calls for a comprehensive analysis of the major factors driving FDI inflows in the region. In view of the different levels of FDI trends in these countries, the following key questions need to be answered:

- a) Why have some countries in the SADC region managed to attract more FDI than others?
- b) Can regional integration increase the likelihood of FDI inflows in SADC countries, In other words, do FTA and FIP have an impact on FDI because of a halo effect⁵, a larger market or easier establishment of cross-border production networks?
- c) What are the implications of the answers to the above questions for national and regional policies?

The rest of the paper is organized as follows, Section 2, presents an overview of recent trends in FDI in the SADC region over the past decade and highlights the major factors that contributed to FDI patterns. Section 3, reviews the existing literature on FDI including the major determinates of FDI, to developing economies. Section 4, highlights the methodology applied in the study and specifies an econometric methodology for assessing the main determinants of FDI in the SADC region. Section 5 presents and analyzes the results from the study and finally, Section 6 summarizes the study as well as provide some policy recommendations, implications and areas for further research.

⁵ It is the phenomenon whereby we assume that because people are good at doing A they will be good at doing B, C and D (or the reverse, because they are bad at doing A they will be bad at doing B, C and D). The phrase was first coined by Edward Thorndike, a psychologist who used it in a study published in 1920 to describe the way that commanding officers rated their soldiers. He found that officers usually judged their men as being either good right across the board or bad.

2.0 SADC REVIEW AND FDI DYNAMICS

2.1 Review of SADC Economies

The last decade has seen a rise in interest from businesses, organisations and governments undertaking systematic political risk analysis when embarking on foreign projects in developing economies. This risk analysis has seen a number of countries entering into various international investment and bilateral investment agreements in order to safeguard their investments. Consistent with this development, regional countries have entered into a number of various investment agreements as shown in the Table 2.1 below.

Table 2.1: List of Bilateral Investment Treaties (BITs) and International Investment Agreements (IIA's) for SADC Countries

COUNTRY	BIT'S	IIA'S	TOTAL
Angola	8	7	15
Botswana	8	6	14
DRC	15	8	23
Lesotho	3	7	10
Malawi	6	8	14
Mauritius	36	9	45
Mozambique	24	6	30
Namibia	13	6	19
Seychelles	7	8	15
Swaziland	5	9	14
Zambia	12	9	21
South Africa	46	9	55
Zimbabwe	30	9	39
Total	213	101	314

Source: UNCTAD 2012

The signing of bilateral investment treaties to protect foreign investments against political risks has complemented the liberalization of FDI regimes. By December 2011, SADC countries had signed 314 such treaties as shown in the table above. Besides political risks, there are other reasons why SADC does not appear to be a very attractive destination for FDI. The amount of FDI inflows to the region also continues to be hampered by poor infrastructure which hinders business growth and efficiency. A further limitation is the perception by prospective foreign investors on the degree and level of corruption, law enforcement on contracts and government ineffectiveness.

According to Schneider and Frey (1985), political instability and the frequent occurrences of disorder create an unfavourable business climate which seriously erodes the risk-averse foreign investors' confidence in the local investment climate and thereby repels FDI away. An analysis of political stability and FDI in SADC member countries shows that those countries that have exhibited stable macroeconomic and political stability have also achieved higher FDI growth. For instance, Zambia's attractive investment climate is underpinned by socio economic stability, where the country is now dubbed as a beacon of peace in Africa, coupled with relative good security and low crime levels. This is supported by immense investment opportunities in most sectors with government's pro-private public investment in roads, electricity and other infrastructure.

For instance, the Zambian government has been progressive in ensuring good governance and fighting corruption. These efforts greatly contributed to Zambia being rated "B+" in the sovereign credit rating by Standard & Poors, and Fitch in 2011. Furthermore, over years of committed business reforms, evidence of a favourable and improving investment climate has been observed with the country's World Bank Doing Business ranking improving. The Zambian government has been aggressive in addressing the issue of reducing the cost of doing business by improving infrastructure such as roads, telecommunications, energy and water. Through the central bank, the Zambian government has also created a favorable macroeconomic environment that has led to a downward trend in the cost of borrowing to improve access to long term finance at lower interest rates. Mauritius is another good example. It is one of the most open and financially sound economies in sub-Saharan Africa. The success of the Mauritian economy is largely a result of its political and socio-economic stability, coupled with good governance and its pro-investment policies. Foreign investors judge that Mauritius, which is set against a beautiful tropical environment, is a safe and attractive place to live in as well as a buoyant place to do business. Crime prevalence is very low.

Most SADC countries are also rated lowly particularly with regards to starting business and other institutional assessments. In terms of doing business and the UNCTAD's inward performance⁶ ranking, SADC member countries still lag behind most developing economies.

⁶The FDI performance index captures a country's relative success in attracting global FDI. If a country's share of global inward FDI matches its relative share in global GDP, the country's Inward FDI Performance Index is equal to one. A value greater than one indicates a larger share of FDI relative to GDP; a value less than one indicates a smaller share of FDI relative to GDP. A negative

Table 1.2: Doing Business Rankings for SADC Countries 2012

Economy	Ease of Doing Business Rank	Starting a Business	Getting Electricity	Registering Property	Getting Credit	Protecting Investors	Enforcing Contracts
Mauritius	23	15	44	67	78	13	61
South Africa	35	44	124	76	1	10	81
Botswana	54	90	91	50	48	46	65
Namibia	78	125	105	145	24	79	40
Zambia	84	69	118	96	8	79	85
Seychelles	103	113	149	63	166	65	84
Swaziland	124	161	158	128	48	122	171
Tanzania	134	113	96	137	129	100	36
Mozambique	139	70	172	156	150	46	131
Lesotho	143	144	141	150	150	147	102
Malawi	145	139	177	95	126	79	121
Zimbabwe	171	144	167	85	126	122	112
Angola	172	167	120	129	126	65	181
Congo, Rep.	181	175	152	156	98	155	159

Source: UNCTAD 2012

Countries that are rated highly in terms of doing business and protecting investors tend to receive more FDI inflows than countries which are rated lowly. Mauritius ranks 1st in Africa in the World Bank Ease of Doing Business Report of 2012. Mauritius is opening itself to the world by offering business friendly platforms. The UNCTAD FDI attraction Index for 2011, which ranks countries by the FDI they receive in absolute terms and relative to their economic size, places Mauritius in the category of countries which are in line with investor expectations. South Africa is rated 1st in the world in terms of getting credit. An exceptional case is Angola, with high FDI but rated lowly in terms of doing business indicators. The country's high FDI inflows is, however, due to the abundant resources, coupled with political and macroeconomic stability. In 2011, Zimbabwe's FDI inflows accelerated by 133 percent from 2010 levels of US\$166 million, to US\$387 million in 2011, as its ranking also improved.

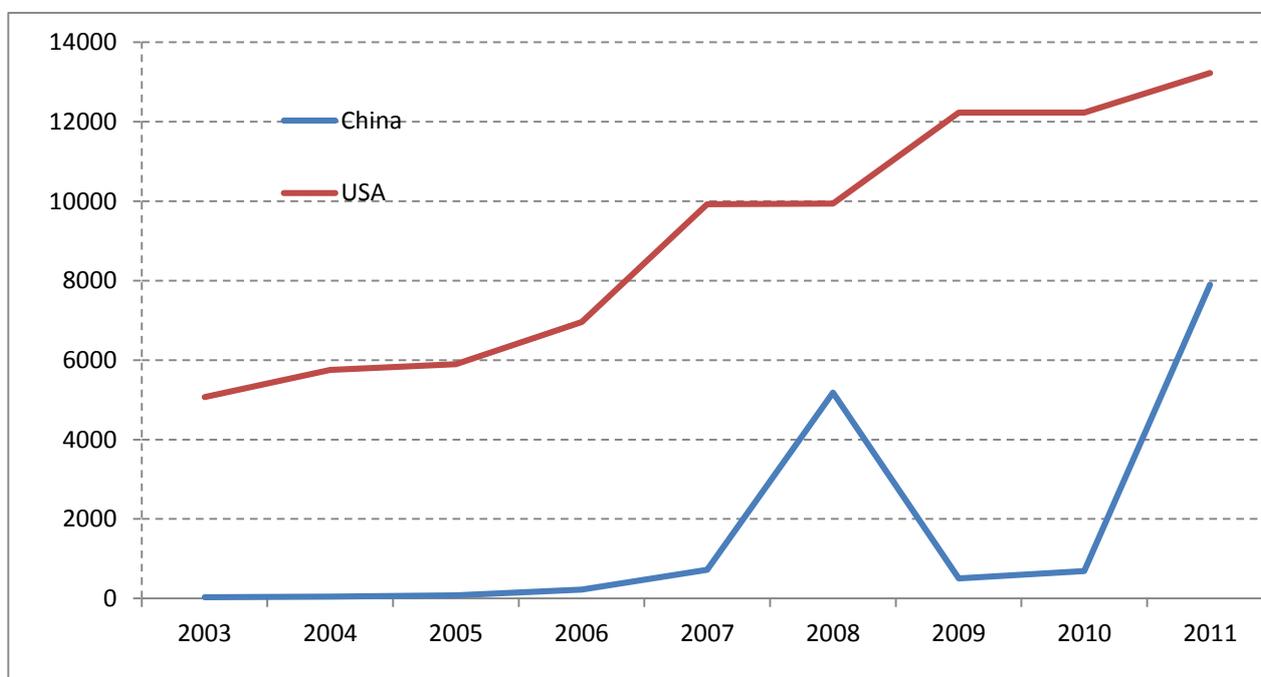
value means foreign investors disinvested in that period. The index is calculated using three-year averages to offset annual fluctuations in the data.

2.2 Review of SADC FDI Dynamics

SADC has witnessed a dramatic change in FDI source countries over the years, with implications on growth and employment creation. Historically, the major FDI source countries in the region were the United States of America (USA), United Kingdom (UK), and France. China has, however, emerged as a major source of FDI in the SADC region in the new millennium⁷. According to the Chinese Ministry of Commerce (MOFCOM), China was the fifth largest FDI source country in the world with US\$56.5 billion of global FDI inflows in 2009. This brought Chinese FDI total stock to US\$245.8 billion, invested mainly in the finance, mining and retail sectors.

In the SADC region, FDI inflows from China are mainly invested in the mining, agriculture, telecommunications and manufacturing sectors. China has been expanding investments into Southern Africa at a time when other traditional sources of FDI are holding back, citing the impact of the global financial crisis. In Zimbabwe, the Chinese are also exploring investments in the electricity, mining and manufacturing sectors. South Africa is also a dominant source of FDI in the region, notably for Zimbabwe, Swaziland, Lesotho, Namibia and Mozambique. Figure 2.1 below shows the trend in FDI from China and the USA.

Figure 2.1: Total FDI from China and USA (2003-2011)



Source: UNCTAD 2012

⁷ Refer to study done by the Center Of Chinese Studies on FDI in SADC counties, 2011

Since 1999, the Chinese government has been encouraging Chinese enterprises to invest abroad, following its so-called Go Out or Going Global strategy. The Chinese 11th Five-Year Plan period (2006-2010) saw the implementation of the going out strategy in its entirety. China deliberately mixes assistance and trade preferences with investment policies in its South-South cooperation. Critics point to the fact that most of Chinese FDI is invested in resource-rich countries, a term which is mostly used to refer to countries with large oil and mineral reserves such as gold, diamonds and copper

2.2.2 Foreign Investment Restrictions

Foreign investment restrictions mainly in the form of foreign equity limitations, screening or approval mechanisms, restrictions on the employment of foreigners as key personnel, and operational restrictions prevalent in some member states have also been cited by researchers as deterring potential FDI. In some countries, certain sectors are reserved for locals and this may have some adverse implications on FDI. Mozambique restricts foreign ownership in the fixed-line telecommunication subsector but allows 100 percent foreign ownership in mobile subsector. Only Zambia permits 100 percent foreign ownership in the media sector. Mauritius and Zambia permit 100 percent foreign ownership in telecommunications, while Tanzania has a restriction of 66 percent in insurance. Zimbabwe's Indigenization and Empowerment Act restricts foreign ownership to 49 percent in all sectors. The indigenization and empowerment regulations in Zimbabwe have been cited by many analysts as a major deterrent to FDI attraction.

The Black Economic Empowerment (BEE) in South Africa and Namibia provides for preferential procurement to indigenous people. Lesotho restricts ownership of small-scale retail and services businesses to local entrepreneurs. No foreign ownership, or even board directorship, by a non-citizen is permitted at any level in these restricted businesses in Lesotho. There are, however, no restrictions on foreign ownership in Angola and Malawi in all sectors of the economy. Perennial policy uncertainties in some SADC member countries also affect investor decisions and influence the level of investment and confidence of investors. The high degree of uncertainty explains the huge capital outflows in the form of profit repatriation in some member countries. The significant capital outflows in some member countries obscure them from realizing the full potential benefits from FDI as significant financial resources are not deployed in the local economy to boost other productive sectors.

2.2.3 Infrastructure Deficit

Infrastructural deficits have been cited by many researchers as causing a significant drawback to attraction of FDI in the region. With the exception of South Africa, other countries still lag behind on various dimensions of infrastructure development. Although SADC's infrastructure ranks consistently above the other Sub-Saharan African regions on all aggregate infrastructure indicators, investors still advocate for more improvements. Infrastructure development in SADC has been constrained by declining levels of public investment on infrastructural projects, soaring debt burdens in some of the countries, sluggish economic growth, and increased pressure on governments to reduce expenditure. Many governments find it easier, and politically expedient to reduce on capital expenditure, including infrastructure, where they will suffer less of a political backlash than if they were to reduce spending on the public service wage bill.

Major improvements are required in areas such as access to improved sources of water and sanitation, as well as electricity, where the differences between SADC and the Economic Community of West African States (ECOWAS), the next-best performer in terms of aggregate performance, are not significant. In terms of paved road density, fixed line telephone and internet density, SADC performs significantly better than all the other regions. Table 2.3 below shows the region's infrastructural indicators against other regional blocs in Africa.

Table 2.3: Infrastructural indicators in Africa

	Western	Eastern	Southern	Central
Paved road density	38	29	92	4
Fixed line telephone	28	6	80	13
Internet density	2	2	4	1
Electricity Coverage	18	6	24	21
Improved Water	63	71	68	53
Improved Sanitation	35	42	46	28

Source: UNCTAD 2012

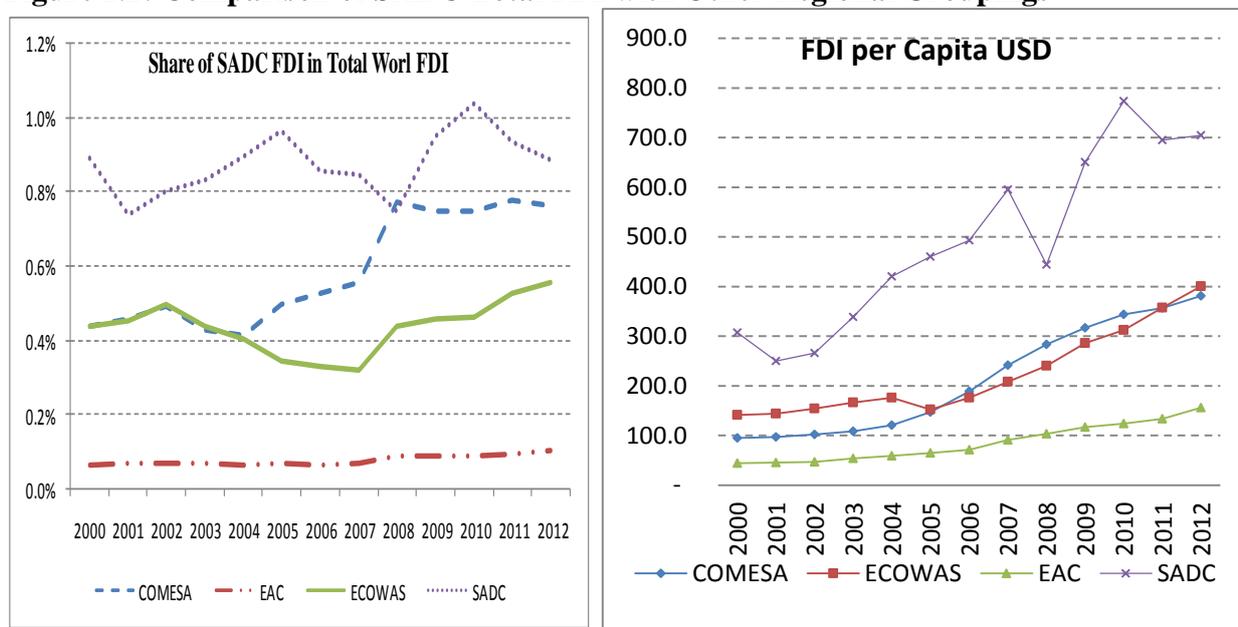
The backlog in infrastructure development influences the overall cost of doing business in SADC countries and as such, reduces profitability. Higher communication costs, high percentages of unsurfaced roads deter potential FDI inflows. Mauritius presents a good example for FDI attraction linked to infrastructure. The entire island is connected with electricity and water supply for agricultural, industrial and household consumption. Industries can thus be located anywhere on the island. In addition, Mauritius has a well-developed digital network infrastructure and offers excellent telecommunication facilities and telecommunication system that compares favorably

with that of many countries in the developed world. Similarly, Seychelles has a well-developed electricity infrastructure, water supplies, and road network.

2.3 DYNAMICS OF SADC-FDI

The stock of FDI in SADC countries increased considerably over the past three decades, from around US\$24.7 billion in 1980 to US\$204 billion by 2011. This notwithstanding, FDI per capita and the share of SADC FDI stock to total world FDI has remained relatively small, although relatively high when compared to other regional blocs in Africa. Figure 2.2 below shows the trend in the share of SADC FDI stock to total world FDI, compared to other regional economic blocs in Africa.

Figure 1.2: Comparison of SADC Total FDI with Other Regional Groupings



Source: UNCTAD 2012

The trend indicates that SADC has increasingly become an attractive investment destination in recent years. The trend slightly reversed in 2009, reflecting the effects of the global financial crisis. SADC has, however, great potential of attracting increased FDI flows from emerging economies, such as China, India and Brazil.

The SADC region's performance with regard to attracting FDI⁸ was relatively poor throughout the 1990s and early 2000s. During that time, most SADC countries had double-digit inflation rates,

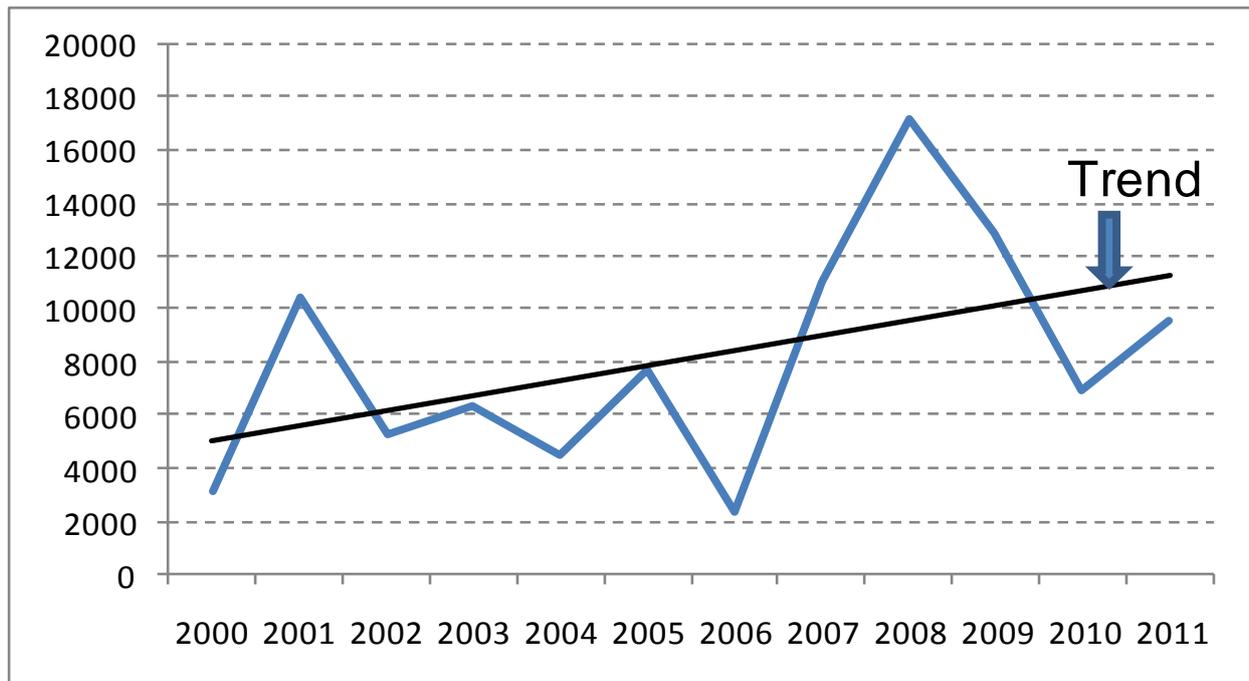
⁸SADC 2010, Finance and Investment Protocol Information brochure Report: 3.

which were not favourable to investors⁹. The low levels of FDI were also attributed to the small size of domestic markets and other socio-economic issues, such as high levels of crime and corruption. SADC, however, maintained an upward trend in FDI inflows from 2001 up to 2008, before slowing down in 2009, mainly due to the effects of the global financial crisis. FDI in most member states, notably, South Africa, Botswana, Angola, Tanzania, Zambia, Namibia, Mozambique and Zimbabwe has mainly been resource seeking as opposed to locational advantages and market seeking. An exception is Mauritius, which is not endowed with natural resources. The strength of Mauritius, however, lies in the quality of its human resources. Mauritius has the highest adult literacy rate in Africa and is now reaping the benefits of a strong commitment to free education for all initiated in the late 1970's. Angola and South Africa topped the list of FDI destinations in SADC. South Africa's FDI is dominated by mining and agricultural activities, whereas FDI in Angola is concentrated in the petroleum extraction industry and mining.

Angola has a wide range of mineral resources, which include diamond, iron, gold, phosphate, manganese, copper, lead, zinc, uranium, titanium, beryllium, quartz, gypsum, marble and granite. South Africa is one of the most sophisticated, diverse and promising emerging markets globally. Strategically located at the tip of the African continent, South Africa is a key investment location, both for the market opportunities that lie within its borders and for the opportunity that exists to use the country as a gateway to the rest of the continent. The unique combination of a highly developed first-world economic infrastructure and a huge emerging market economy has given rise to a strong entrepreneurial and dynamic investment environment. South Africa is the economic powerhouse of Africa and is a member of BRICS which also include Brazil, Russia, India, and China. Figure 2.3 below shows the trend in FDI inflows to SADC countries.

⁹Muradzikwa, 2002 "Foreign direct investment in SADC", Development Research Unit Working Paper 2

Figure 2.3: FDI Inflows in SADC Countries



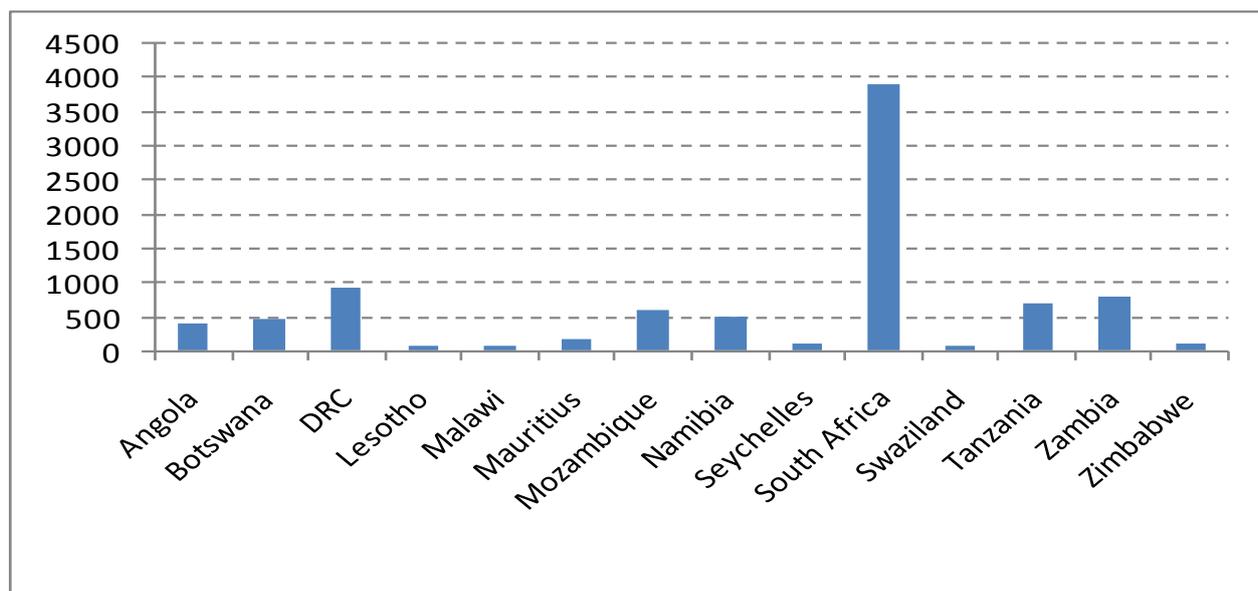
Source: UNCTAD 2012

The trend depicts a general upward trend from the year 2000 onwards. The significant decline in FDI flows to SADC in 2009 could also be attributed to a decision by Shell and BP to disinvest from their downstream business activities, retailing, in particular and the effect of the global financial crisis. The world investment report for 2011 notes that Shell announced plans to withdraw from down-stream activities in 21 African countries, while on the other end BP disinvested in five SADC countries.

A notable feature from the trend in FDI¹⁰ is that countries that made significant strides towards privatisation of state-owned enterprises, such as Mozambique and Zambia, have been able to attract substantial amounts of greenfield FDI that has provided the stimulus for growth in these economies. In this respect, privatisation of state-owned enterprises could be seen as a catalyst for FDI, which other SADC countries can carefully consider so as to improve the levels of FDI. In Mozambique, FDI reached historical levels in 2011 amounting to more than US\$2 billion and investment was mainly in natural resource exploitation. The Mozambique government has been implementing reforms on fiscal and financial sectors aimed at improving the business climate in the country. Figure 2.4 below shows the average net FDI inflows for the SADC region from 2001 to 2012.

¹⁰ See Annex

Figure 2.4: Average Net FDI Inflows USD Millions (2001-2012)



Source: UNCTAD 2012

FDI in the SADC region has over the years been directed mainly to greenfield investments as opposed to mergers and acquisitions. Between 2005 and 2011, a total of 1 626 greenfield investments were approved in the 14 member countries excluding, Madagascar, with a total value of US\$181.5 billion. This can be compared to investments through mergers and acquisitions, where a total of 394 projects with a value of US\$30.6 billion were approved during the comparable period. This indicates that the region has a lot of untapped business ventures, where FDI can be directed. Table 2.4 below shows the cumulative number of projects for both greenfields and mergers and acquisitions approved in SADC countries from 2005 to 2011.

Table 2.4: Cumulative Greenfields and Mergers and Acquisition (2005-2011)

Country	Greenfield Investments		Mergers and Acquisition	
	Number	Value(US\$ Million)	Number	Value(US\$ Million)
Angola	247	29,599	5	530
Botswana	68	5,157	12	128
DRC	64	12,735	5	180
Lesotho	8	856	0	0
Malawi	15	1,500	4	0
Mauritius	44	2,858	35	605
Mozambique	86	29,625	17	98
Namibia	63	6,114	20	408
Seychelles	11	1,767	4	157
South Africa	711	54,433	243	28 110
Swaziland	15	860	3	0
Tanzania	115	10,309	13	62
Zambia	110	14,951	20	296
Zimbabwe	69	10,702	13	47
Total	1626	181,466	394	30 621

Source: UNCTAD 2012

3.0 LITERATURE REVIEW

3.1 Theoretical literature

According to the OECD¹¹, foreign direct investment reflects the objective of obtaining a lasting interest by a resident entity in one economy in an entity resident in an economy, other than that of the investor. The lasting interest implies the existence of a long-term relationship between the direct investor and the enterprise and a significant degree of influence on the management of the enterprise. Accordingly, direct investment involves both the initial transaction between the two entities and all subsequent capital transactions between them and among affiliated enterprises, both incorporated and unincorporated.

A variety of theories have tried to explain the motives for FDI. However, there is no single theory that explains the different motives of FDI in all countries. The early theories of related to capital

¹¹ Refer to OCED Benchmark Definition For Foreign Direct Investment Guideline, 1996

market and portfolio investments were used to describe the origination of FDI (Kindleberger, 1969). This approach stated that in the absence of uncertainties or risks, capital tended to flow to areas where it realizes the highest return. This view motivates direct investors to invest their capital from low return countries to high return countries. However, this context failed to incorporate the fundamental difference between portfolio and direct investment. As stated in the OECD FDI definition, direct investment entails some degree of control. Accordingly, the important theoretical shortcoming of the capital market and portfolio investments theory is that it does not explain control. If interest rates are higher abroad, an investor will consider lending money abroad, but there is no logical necessity for that investor to control the enterprise to which he or she lends the money (Hymer, 1976).

Dunning (1977 and 1979)'s eclectic framework provided a comprehensive theory on the motives for FDI. The eclectic framework postulates that firms invest abroad in pursuit of Ownership (O), Location (L) and Internalisation (I) advantages. This is usually referred to as the OLI framework. The owner-specific advantage of property rights/patents, expertise and other tangible assets allow a firm to compete with others in the market it serves regardless of the disadvantage of being foreign because it is able to have access to exploit and export natural resources and resource based products that are available to it. The location advantages are those that make the chosen foreign country a more attractive site such as the country's natural endowments, government regulation, labour, transport costs, macroeconomic stability, trade barriers, gains in trade costs, and cultural factors, among other things.

The internalisation advantage arises from exploiting imperfections in external markets, including reduction in uncertainty and transaction costs in order to generate knowledge more efficiently as well as reduction of state generated imperfections such as tariffs, foreign exchange controls and subsidies. When the O, L, and I advantages outweigh the costs and risks of producing abroad, FDI arises. The eclectic, or OLI paradigm, suggests that the greater the O and I advantages possessed by firms and the more the L advantages of creating, acquiring (or augmenting) and exploiting these advantages from a location outside its home country, the more FDI will be undertaken. Where firms possess substantial O and I advantages but the L advantages favour the home country, then domestic investment will be preferred to FDI and foreign markets will be supplied by exports. From the eclectic theory, the main motives for FDI according to Dunning (1993) are thus, resource seeking (to access raw materials, labour force, and physical infrastructure resources, market seeking (horizontal strategy to access the country's markets); efficiency seeking (vertical strategy

to take advantage of lower labour costs, especially in developing countries); and strategic-asset seeking (to access research and development, innovation, and advanced technology).

Although the OLI paradigm does explain the existence of foreign investors, its main problem is that it has difficulty explaining the recent trends in FDI such as the surge and concentration of FDI among similar countries. Furthermore, no sound empirical models have been generated in order to compare real data with the theory. However, eclectic paradigm is mainly criticised for having too many variables that it loses any operational practicality. Dunning himself accepted this fact and stated that it was an inevitable consequence of trying to incorporate the different motivations behind FDI into one general theory. This criticism resulted in the Investment Development Cycle or Path theory that proposes a link between a country's level of economic development and its international investment positions, the net outward FDI stock per capita. The basic hypothesis is that when a country develops, the conditions encountered by foreign and local firms will change. Consequently, this affects the flows of inward and outward FDI which in turn will have an impact on the economic structure of the country. As a result, there is a dynamic interaction between the two. This theory accepts the fact that a Government can influence the country's condition through its policies, thereby affecting FDI flows and domestic firms' ownership advantages. In this way, the Investment Development Cycle theory introduced a new notion of a dynamic approach to Dunning's eclectic theory.

Although these theories have examined in detail the economic factors affecting FDI, they did not adequately explore political factors (Buthe and Milner, 2008). There is however, a common view that the motives for FDI are to reap the benefits in the form of location, firm- specific or internationalization of markets. The FDI theories also acknowledges the fact that government policies play a vital role in attracting foreign investments in the economy.

3.2 Empirical Literature

FDI has received more and more interest from economists and policymakers, owing to its growing economic importance for both developed and developing countries. According to the 2010 World Investment Report, FDI inward flows accounted for 9.1 percent of Gross Fixed Capital Formation in 2009¹², revealing the importance that these flows can have for economic growth. A recent study

¹² See UNCTAD Investment Report 2010

by the Centre for Chinese Studies¹³ has noted that SADC member countries can learn from one another for the benefit of making the region more attractive to FDI. The SADC Secretariat can draw lessons from the increasing FDI inflows in some member states and use this knowledge to suggest adaptations to other member countries in order to make them more attractive to FDI. The study recommended that Mauritius be used as a good example of maximizing FDI potential.

Lederman et al (2010) used international data and a micro-data set of firms in thirteen (SADC countries) to investigate the benefits and determinants of FDI in the region and found that income level, human capital, demographic structure, institutions, and economic track record affect FDI inflows per capita. They also found some differences between SADC and the rest of the world in FDI behavior, namely, that in SADC, the income level and openness are less important in explaining FDI behaviour. However, relative to other regions of the world, they found that SADC's low FDI inflows are explained by economic fundamentals such as previous growth rates, average income, phone density, and the adult share of population.

Mauro (2000) used the gravity-model approach to analyze the impact of regional integration on FDI. The variables considered include tariffs, non-tariff barriers and exchange rate variability. In his gravity model the sample of home countries examined include France, Germany, Italy, UK, Japan, South Korea, US and Canada, while a set of host countries for FDI is constituted by both OECD and non-OECD members. The paper considered three years: 1988, 1993 and 1996. The results show that FDI does not respond to changes in tariffs, which in turn suggests that the tariff-jumping argument is not supported empirically. In other words, an increase in the tariff level has no significant impact on FDI.

Mauro (2000) also finds that non-tariff barriers negatively affect FDI which could be explained via the argument of market-accessibility and the existence of sunk costs. When foreign firms invest in a host country, they incur sunk costs in setting up the affiliates and if they then cannot access a larger market, not because of tariffs, but because of non-tariff barriers, their losses can even be greater than for the exporters. The major problem with this study is that it concentrates on trade openness (tariff and non-tariff barriers) only leaving out other important FDI determinants such as

¹³ Refer to the Study By Centre For Chinese Studies On Assessing China's Role In Foreign Direct Investment In Southern Africa 2011

market size, size of the labour force and political stability found to be significant by other studies like Asiedu (2006), Obwona (2001), Walsh and Yu (2010).

Campos and Kinoshida (2003) examined the importance of agglomeration economies and institutions vis-à-vis initial conditions and factor endowments in explaining the locational choice of foreign investors. The study used panel data for 25 transition economies¹⁴ between 1990 and 1998. In order to test for agglomeration effects, the study relates current FDI stock to past FDI stock and other explanatory variables and employed the generalized method of moments (GMM). The study also examined the impact of macroeconomic variables: market size using GDP as a proxy, trade openness and inflation. The study finds that the main determinants of FDI are institutions, agglomeration, and trade openness.

Chiguvu (2009) analyzed the determinants of inward FDI in the SADC region for the period 1995 to 2007 using a panel data approach. The determinants of FDI in the SADC region considered in his study are trade openness, inflation, government size, external debt, market size and growth, labour availability, infrastructure quality, financial depth and corruption. Chiguvu (2009) like Obwona (2000) used nominal total population as a proxy for labour availability in a country. His main findings suggest that more open economies attract FDI. He also finds that major pull factors of FDI are bigger markets, low inflation, lower external debt, and quality infrastructure. These results confirm findings of other studies, Asiedu (2006), Campos and Kinoshida (2003), among others.

Walsh and Yu (2010) find that primary sector FDI has no strong linkages to either macroeconomic stability, level of development, or institutional quality, while clustering effects appear important, with larger FDI stocks attracting greater additional inflows. This is intuitive, as FDI decisions in, for example, mining or petroleum are primarily determined by the location of those resources, with both equipment and labor easily transferable across borders. Secondary and tertiary FDI benefits from agglomeration or clustering effects while FDI in services appears to be more strongly impacted by macroeconomic conditions than FDI in manufacturing.

¹² The economies covered in the data are Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovak Republic, Slovenia, Ukraine, Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyz Republic, Moldova, the Russian Federation, Tajikistan, Turkmenistan, Ukraine, and Uzbekistan

Furthermore, Walsh and Yu (2010) contend that a weaker real effective exchange rate draws more manufacturing FDI into an economy, while it reduces the amount of tertiary FDI. Tertiary FDI flows are also higher in more rapidly growing economies, than those which are more open. More flexible labor markets and deeper financial markets attract more secondary FDI, while better infrastructure and a more independent judiciary attract more tertiary FDI. Educational attainment was found to have little relationship to either type of FDI.

Asiedu (2006) used a panel data for 22 countries¹⁵ in Sub-Saharan Africa over the period 1984-2000 to examine the impact of political risk, institutional framework and government policy on FDI flows. Measures of institutional quality considered in his study are corruption and the extent to which the rule of law is enforced. Political risk factors considered in the study are coups, assassinations, revolutions and riots. Coups are the number of forced changes in the top government, while assassinations include any politically motivated murder or attempted murder of a senior government official. Revolutions include any illegal or forced change in the ruling government, and riots are the number of violent demonstrations or clashes of more than 100 citizens involving the use of force.

Asiedu's study reveals that an efficient legal system, a good investment regulatory framework, an educated labor force, natural resource endowments, good infrastructure, and large markets promote FDI, whereas, high inflation, corruption and political instability deter FDI. An important implication of his results was that FDI to Africa is not solely driven by natural resource endowment, and that governments can play an important role in promoting investments to the region.

¹⁵ Countries in the sample are Cameroon, Congo Rep., Cote d'Ivoire, Ethiopia, Gabon, Gambia, Ghana, Kenya, Madagascar, Malawi, Mali, Mozambique, Niger, Nigeria, Senegal, South Africa, Sudan, Tanzania, Togo, Uganda, Zambia and Zimbabwe

4.0 EMPIRICAL METHODOLOGY

Based on the theoretical framework of FDI and the structure of SADC economies, we used a cross-country panel regression for the period 1996-2011 to establish the hypothesized relationship between FDI inflows and the relevant independent variables. The period was chosen to coincide with data on institutional variables which are only available after the 1996 period.

4.1 Model Specification

The model specification derives from the common factors that influence FDI in the region. The panel specification is as follows:

$$FDI_{t,i} = \alpha + \beta_4 \ln(PGDP_{i,t-1}) + \beta_{11} \ln(URB_{i,t-1}) + \beta_1 \ln(CPS_{i,t-1}) + \beta_2 \ln(CPI_{i,t-1}) \\ + \beta_6 \ln(OPEN_{i,t-1}) + \beta_7 \ln(INFRA_{i,t-1}) + \beta_9 \ln(PS_{i,t-1}) + \beta_{10} \ln(ROL_{i,t-1}) \\ + \beta_3 \ln(GOEF_{i,t-1}) + \beta_5 \ln(FDI_{i,t-1}) + \varepsilon_{t,i}$$

$$(t = 1996, 1997 \dots 2011; i = 1, 2 \dots 14)$$

where subscript i represents each of the 14 SADC¹⁶ member countries to be used in the study t refers to years from 1996 to 2011, α is the intercept and $\varepsilon_{t,i}$ is the error term.

The regression equation is expressed as a log-linear in order to capture the elasticity of FDI inflows with respect to each of the explanatory variables. Further, the variables were lagged to facilitate the interpretation of model results as the reaction of FDI to changes in either of the independent variables. We used the FDI inflow as a percentage of GDP as the dependent variable (FDI), a widely used measure¹⁷. The FDI inflow variable is desirable to the FDI stock variable as it specifically capture the changes in economic fundamentals and policy pronouncements. The independent variables include measures of market size, financial depth, macroeconomic environment, governance and institutional factors. Market size is a measure of the host country's domestic market and is proxied by the log of per-capita income to GDP (PGDP) and urban population share (URB).

¹⁶ SADC member states in the sample are: Angola, Botswana, Democratic Republic of Congo, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe

¹⁷ See studies by Adeisu, 2002 and Quarzi, 2005.

A large market size implies greater demand for goods and services and offers economies of scale for the investor. Financial depth is measured as the size of a country's monetary system and is proxied by the ratio of credit to private sector to GDP (CPS). Macroeconomic factors are proxied by the country's inflation rate (CPI). Inflation is used as an indicator of macroeconomic instability (Buckley et al., 2007). A stable macroeconomic environment promotes FDI by showing less investment risk. The institutional and governance factors considered in the model include trade openness (OPEN), infrastructure (INFRA), political instability (PS), rule of law (ROL) and government effectiveness (GOEF).

The model also included the lagged FDI variable to test for agglomeration effects. Agglomeration may exist under the assumption that foreign investors may be attracted to countries with existing foreign investment. In this case, foreign investors may view the investment decisions by others as a good signal of favorable conditions and invest there too, so as to reduce uncertainty. The commonly used institutional factors that influence FDI in an economy are trade openness and infrastructural development. Trade openness portrays the ease with which investors can freely move capital in and out of an economy and is measured as a percentage of the sum of exports and imports to GDP. The impact of openness on FDI can have a positive sign if FDI is export-oriented and a negative one if FDI is tariff jumping. With regards to infrastructural development, there are varying theoretical and empirical views on its impact on FDI. Ang (2008), Asiedu (2006), and Onyeiwu and Shrestha (2004) find that the relationship between the level of infrastructure development and FDI flows is significantly positive. However, Marr (1997) argues that the prevalence of poor infrastructure in the areas of road, rail system, electricity and telecommunication, can create an incentive for the flow of foreign investments.

In this paper, we used the number of telephone and mobile phone subscribers per 1000 people as a proxy for infrastructure (INF) provision. This measure is consistent with proxy used by UNCTAD, among other factors, to compile the inward FDI potential index. Information, Communication and Technology (ICT) infrastructure and skills are now critical in integrating local producers into international technological and communications networks, and in attracting vertical FDI in services as well as manufacturing¹⁸. We also examined the impact of governance indicators on FDI in SADC countries. The governance indicators were proxied by the control of corruption, regulatory quality and rule of law (Lederman et al., 2010; Globerman and Shapiro, 2002). The World Bank has come up with six worldwide governance indicators namely, regulatory quality, rule of law, control of

¹⁸See studies by Addison and Heshmati (2003)

corruption, voice and accountability, government effectiveness and political stability. The governance indicators included in this paper are government effectiveness, political stability and rule of law. Politically stable economies guarantee the safety of investors' interest and reduce uncertainty over future possible policy reversals.

According to the World Bank, political stability measures the likelihood that the government in power will be destabilized through unconstitutional or violent means. The rule of law index covers the effectiveness and the predictability of the judiciary and the enforceability of contracts and aims at measuring the confidence that agents have in the legal system. Government effectiveness captures perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies. Surveys¹⁹ of investors have indicated that political stability is one of the key concerns of potential investors, although empirical results are somewhat mixed. Wheeler and Mody (1992) find that political risk is insignificant in determining the production location decisions of US firms. On the other hand, Asiedu (2005) examined the impact of political risk, institutional framework and government policy on FDI flows into sub-Saharan Africa over the period 1984-2000 and found that political stability deters FDI.

4.2 Panel Estimation Models

The estimations were conducted using panel data analysis under the OLS assumption. However, panel estimation of FDI regressions raises some econometric issues stemming from the dependence of FDI on past values of some explanatory variables such as infrastructure. Potential endogeneity arises in the sense that public FDI does not only react to the infrastructural deficit in the country, but can also influence this variable. Accordingly, the OLS results were cross checked with results from the General Methods of Moments (GMM) for robustness check. The Hausman Specification test (Table 5.2) was used to select between the fixed effects and random effects model. The test chose the random effects as a perfect fit (Table 5.2). As a result we used the results of a random effects model which can jointly capture cross-country and within country determinants of FDI. Non stationary variables were differenced to avoid the problem of unit roots given that most economic data are integrated of order one I(1).

¹⁹ See Jenkins and Thomas (2002) and WIR Survey conducted by the United Nations Conference on trade and development

4.3 Panel Cointegration

We also analyzed the long-run cointegrating relationships between FDI and explanatory variables. The estimation for panel cointegration was conducted using the Kao (1999) residual cointegration tests. The panel cointegration will facilitate the pooling of information regarding long-run relationships from across panel, while allowing the associated short run dynamics and fixed effects to be heterogeneous across the panel.

4.4 Data Needed and Sources

The data for the trends and regression analysis was obtained mainly from SADC member countries as well as the International Monetary Fund (IMF), UNCTAD, World Bank, and African Development Indicators data sources. It was, however, noted that some SADC member countries do not have adequate records on FDI by partner countries and also by sectors. All the independent variables were lagged by one period, on the assumption that FDI decisions may be made based on historical data and hence all the independent variables that are supposed to have effect on FDI inflow would materialize their effect the next period (Lederman 2010).

5.0 RESULTS PRESENTATION AND ANALYSIS

5.1 Empirical Results Presentation

As a preliminary analysis, we tested for the stationarity of the data and estimated the pairwise correlation coefficients between the model variables to identify potential sources of multicollinearity in the estimated model. We also tested for the existence of a long run relationship between the variables using the panel co-integration approach. Table 5.1 below shows results of the panel unit root tests conducted using the Levin, Lin Chu (2002) t-tests.

Table 5.1: Results of Panel Unit Root Tests

	Level	First difference
CPS	2.01457 (0.2568)	4.67978*** (0.0000)
FDI	2.2198* (0.0832)	5.53805*** (0.0000)
GOFF	0.78393 (0.2165)	8.66397*** (0.0000)
CPI	0.87380 (0.8089)	0.87380*** (0.8089)
INFRA	3.93034 (0.9898)	14.4403*** (0.0000)
OPEN	0.51853 (0.3020)	6.860148*** (0.0000)
PGDP	3.61219* (0.0632)	4.6638*** (0.0000)
PS	1.66828* (0.0476)	11.6939*** (0.0000)
ROL	0.45055 (0.3261)	4.76607*** (0.0000)
URB	1.6548 (0.3215)	5.50087*** (0.0000)

Note: *** stationary at 1%, ** stationary at 5%, * stationary at 10%

The results from the panel unit root test in Table 5.1.2 shows that all variables are stationary after first differencing. Table 5.2 below shows the correlation coefficient results.

Table 5.2: Correlation Matrix for the FDI and Its Determinants

	CPS	FDI	GOFF	CPI	INFRA	OPEN	PGDP	PS	ROL	URB	VIF
CPS	1.00										1.70
FDI	0.17	1.00									1.36
GOFF	0.46	0.06	1.00								8.98
CPI	-0.08	0.02	-0.21	1.00							1.13
INFRA	0.38	0.19	0.42	-0.10	1.00						2.66
OPEN	-0.01	0.33	0.11	0.10	0.34	1.00					1.90
PGDP	0.40	0.24	0.67	-0.10	0.72	0.50	1.00				5.02
PS	0.15	-0.03	0.70	-0.28	0.37	0.11	0.36	1.00			4.09
ROL	0.32	-0.02	0.88	-0.24	0.37	0.12	0.52	0.81	1.00		6.95
URB	0.35	0.07	0.31	0.03	0.39	0.35	0.58	-0.05	0.13	1.00	1.92

The results in Table 5.1.2 show that, per-capita income, rule of law and government effectiveness overlap with one another, government effectiveness and rule of law variables exceeding the

Variance Inflation Factor (VIF) conventional benchmark of 5²⁰. As a result, these variables were dropped and catered for through the political stability variable. The VIF quantifies the severity of multicollinearity in an OLS regression analysis. It provides an index that measures how much the variance (the square of the estimate's standard deviation of an estimated regression coefficient is increased because of collinearity).

Table 5.3 below summarizes the regression results for panel cointegration using the Kao residual Cointegration tests.

Table 5.3: Results of Panel Cointegration

Series	Panel statistic	P-Value
FDI,CPS,URB,OPEN,PGDP,PS,INFRA,CPI,GOFF,ROL	2.364537	0.0462
Residual Variance	0.001051	
HAC Variance	0.006420	

The results of the panel cointegration in Table 5.3, rejects the null hypothesis of no cointegration, implying that a long run relationship exists between FDI and the explanatory variables.

Table 5.4 below shows results of regression analysis conducted using the random effects OLS model and the GMM approach.

²⁰ See Kutner, Nachtsheim, Neter, Applied Linear Regression Models, 4th edition, McGraw-Hill Irwin, 2004.

Table 5.4: Random effects Regression Results on FDI determinants in SADC

Variable	OLS	GMM
α	2.474414** (2.020824)	0.056429*** (2.091917)
$\ln FDI_{i,t-1}$	0.889922*** (34.27891)	0.925714*** (34.39151)
$\ln CPS_{i,t-1}$	0.007221* (1.997760)	0.005177* (1.812457)
$\ln(URB_{i,t-1})$	0.539019** (2.030380)	0.096986* (1.923457)
$\ln(OPEN_{i,t-1})$	0.100711** (2.050489)	0.070263*** (2.701403)
$\ln(PS_{i,t-1})$	-0.002444* (-1.627475)	-0.009791*** (-3.258763)
$\ln(PGDP_{i,t-1})$	0.006517** (2.198376)	0.036245** (2.398376)
$\ln(INFRA_{i,t-1})$	0.554832** (2.089666)	0.244466** (2.002451)
$\ln(CPI_{i,t-1})$	0.001444 (0.218312)	0.000454 (0.124567)
Diagnostics		
Adjusted R-squared	0.871664	0.899129
DW- Statistic	1.973168	2.251534
Hausman Test	Prob<chi2=0.2560	
J-Statistic		193.000

Note: *** significance at 1%, ** significance at 5%, * significance at 10%

5.2 Empirical Results Analysis

The estimation results using the Swamy-Arora random effects estimations and the GMM yield almost similar results, with slight differences in the level of significance. This result was also confirmed by previous studies (Catrinescu et al 2006), (Aggarwal et al 2006) and Anyanwu 2010). As such, the analysis in this paper is based on the OLS Swamy-Arora random effects results. The results generally show that agglomeration, credit to private sector, urban population share, trade openness, market size and infrastructural development have a positive significant relationship with FDI inflows to SADC member countries. The positive and significant coefficient on agglomeration shows that countries that are already enjoying high FDI flows tend to receive more FDI due to inertia. The existing level of FDI in an economy can attract other forms of FDI such as debt and equity through the financing of expansion programmes. High levels of FDI are also a signal to other potential investors on the investment climate of a country.

Credit to private sector was found to have a positive and significant effect on FDI, contrary to the hypothesis that FDI will be greater where the capacity of the private sector to finance its investment is constrained by an underdeveloped domestic financial sector. Foreign investors prefer to invest in countries with higher levels of credit to private sector because they can access working capital domestically after their initial investment. The positive and significant coefficient on openness is consistent with foreign investment to most developing countries being mainly export-oriented. It is also consistent with the FDI theory that openness is indicative of the host countries' ease of access to the world market for material inputs. It also suggests that economies in which trade is important also have relatively higher FDI. Jun and Singh (1996) found that higher levels of exports lead to higher FDI inflows.

The positive coefficients on market size and urban population share suggest that FDI to the region has been market seeking. A large urban population signifies a bigger market as the urban population has generally higher income levels. According to Scaperlanda and Mauer (1969), FDI responds positively to the market size once it reaches a threshold level that is large enough to allow economies of scale and efficient utilization of resources. Enhanced regional integration will therefore increase market size in SADC and help attract investors currently constrained in part by the small size of some domestic SADC markets. This is all the more important given our finding that large market size attracts FDI to SADC.

Political instability was found to have a negative relation with FDI, implying that perceived political instability and government ineffectiveness in some SADC countries continues to deter potential FDI inflows in those countries. The negative impact of political instability could be due to weak law enforcement, government bureaucracy, and inefficient regulatory structures that characterize most African economies (Egger and Winner, 2005). In the presence of political instability, there is high risk of not getting the full benefits across all components of FDI, namely equity, reinvested earnings and debt. Infrastructural development was found to have a positive impact on FDI, implying that recent increases in mobile telecommunication networks into SADC countries have had a significant impact in explaining increases in FDI inflows over the past decade. This positive effect has been confirmed by a number of previous studies, including Ang (2008), Onyeiwu and Shrestha (2004), and Asiedu (2002).

5.3 Policy Implications

The policy implication from the above assessment is that SADC countries should avoid instituting stricter foreign investment regulations in sectors which they do not have unique comparative advantage, because investors would move to other countries offering better investment conditions. However, in sectors where a country has some unique comparative advantages such as extractive industry, investors may not necessarily be deterred by strict investment regulations. The regional integration initiatives by SADC, such as the Free Trade Area and the Finance and Investment Protocol, among others have enhanced market seeking FDI flows into the region as reflected by the recent upward trend in FDI inflows to the region.

The significant openness variable, underscore the need for SADC to promote greater regional integration by removing remaining trade obstacles, particularly in extractive industries, which need huge capital outlay, beyond the capacity of the domestic financial system. Enhanced trade openness will enable the SADC region to benefit as a whole, by knocking down barriers to trade and opening the doors of mutual gain by strengthening policies aimed at ensuring free flow of goods and services. There is also need to strengthen governance through promoting effective contract enforcement and fighting corruption. Sound governance, infrastructure and institutional quality, especially the rule of law, not only attracts FDI, but also creates the conditions under which domestic TNCs emerge and invest abroad. Deepening regional integration and economic cooperation will help improve the competitiveness of SADC in attracting FDI through the halo effect and a large market size. A regional approach can enhance these factors where an individual country by itself has limited scope in achieving enhanced locational competitiveness associated with the benefits of agglomeration, full capacity utilisation and in overcoming the handicap of small markets.

6.0 CONCLUSION AND RECOMMENDATIONS

This study was aimed at reviewing the experience of SADC countries in attracting FDI and to explore why some member countries continue to receive more FDI than others. The study noted that countries with higher FDI levels (agglomeration), credit to private sector, urban population share, trade openness, market size and adequate infrastructure tend to attract more FDI, compared to others. The study also established that countries which have made significant progress in the privatization of public enterprises and reducing the cost of doing business in general have also managed to attract more FDI flows compared to others.

Countries with unique specific factors such as availability of natural resources also tend to receive more FDI flows, notwithstanding the presence of unfavourable investment regimes, such as political instability, absence of rule of law and corruption. These countries can institute stricter foreign equity requirements and empowerment regulations without running the risk of losing potential investors in those sectors. However, the existence of foreign investment impediments can affect FDI in other sectors of the economy, especially those requiring market seeking and locational advantage FDI, which are sensitive to unfavourable investment climates.

The major implication from this study is the need for SADC to promote greater regional integration by removing remaining trade obstacles, particularly in extractive industries, which need continuous cutting-edge investments. The SADC region will benefit as a whole from becoming more open to itself, by knocking down barriers to trade and opening the doors of mutual gain by strengthening policies aimed at ensuring free flow of goods and services. There is also need to strengthen governance through promoting rule of law in contract enforcement and ensuring political stability and fighting corruption. SADC should also put more efforts on creating a common set of trade and investment rules that will help to provide a better investment environment for those who service the SADC market and potential investors who locate to SADC to service outside markets. Deepening regional integration and economic cooperation will help improve the competitiveness of SADC in attracting FDI through the halo effect and a large market size. A regional approach can enhance these factors where an individual country by itself has limited scope in achieving enhanced locational competitiveness associated with the benefits of agglomeration, full capacity utilisation and in overcoming the handicap of small markets.

The consolidation of the financial sector also plays an important role to attract FDI to the country and the region as a whole. Countries need to deal with the high cost of financial intermediation, interest rate differentials and credit provision procedures. There is, therefore need to harmonize the fiscal legislation, especially the taxation policy, and to invest more on basic infrastructures such as roads, bridges, power plants in order to facilitate trade amongst member countries and lure foreign investors to the region. As such, central banks have a role to play in terms of ensuring a conducive financial environment for the provision of domestic credit to the productive sectors of the economy.

There is also need to explore diversification through developing new investment niches in dynamic sectors, beyond natural resources sector, by tapping into other areas such as engineering, software

development and computing. This can be achieved by removing obstacles such as foreign investment restrictions in market seeking investments. SADC countries with high FDI in extractive industries such as mining should actively promote FDI in other sectors of the economy. In essence, SADC countries need to aggressively promote FDI in sectors that provide backward, forward and horizontal linkages with extractive industries through refining and beneficiation.

Overall, it can be concluded that the reasons why investors choose to invest in a particular country are wide-ranging and complex, reflecting the macroeconomic, institutional, social and natural environment. Understanding the major factors why investors choose to invest in the region is paramount to enhance the region's appeal as a destination of choice. The major policy areas SADC countries should focus on, to attract more FDI, is to institute policies aimed at improving stability of the monetary system, removing foreign investment restrictions, allocating more resources to infrastructural development, opening their markets by entering into the right kind of bilateral and multilateral trade agreements, and improving governance and institutional indicators such as doing business, political stability, rule of law and the fight against corruption. Significant progress in these areas will not only attract FDI, but can also bring credibility on the effectiveness of governments.

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