Investment Policy in Zambia

– An Agenda for Action

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LIST OF ABBREVIATIONS

AAC	-	Anglo American Corporation
ACC	-	Anti-Corruption Commission
BOZ	-	Bank of Zambia
CA	-	Communications Authority
COMESA	-	Common Market for Eastern and Southern Africa
CSO	-	Central Statistics Office
CUTS	-	Consumer Unity & Trust Society
CUTS-ARC	-	CUTS Africa Resource Centre
DFID	-	Department for International Development
ERB	-	Energy Regulation Board
FDI	-	Foreign Direct Investment
FTA	-	Free Trade Area
GDP	-	Gross Domestic Product
GFCF	-	Gross Fixed Capital Formation
HIPC	-	Highly Indebted Poor Country
IFD	-	Investment for Development
IGO	-	Inter-Governmental Organisation
IMF	-	International Monetary Fund
ILO	-	International Labour Organisation
KCM	-	Konkola Copper Mines
KDMP	-	Konkola Deep Mining Project
LDC	-	Least Developed Country
MCTI	-	Ministry of Commerce, Trade and Industry
MLA	-	Ministry of Legal Affairs
MOE	-	Ministry of Education
MOFNP	-	Ministry of Finance and National Planning
MOH	-	Ministry of Health
MNC	-	Multi-national Corporation
NRG	-	National Reference Group
NWASCO	-	National Water and Sanitation Council

OECD	-	Organisation for Economic Co-operation and Development
PRSP	-	Poverty Reduction Strategy Paper
PSDP	-	Private Sector Development Programme
R&D	-	Research and Development
RIFF	-	Regional Integration Facilitation Forum
SADC	-	Southern African Development Community
SAP	-	Structural Adjustment Programme
TI	-	Transparency International
TNC	-	Trans-national Corporation
UNCTAD	-	United Nations Conference on Trade and Development
WB	-	World Bank
WFC	-	Women for Change
ZACCI	-	Zambia Chamber of Commerce and Industry
ZAM	-	Zambia Association of Manufacturers
ZAMTEL	-	Zambia Telecommunications Company Limited
ZAMTIE	-	Zambia Trade and Investment Enhancement
ZAWA	-	Zambia Wild Life Authority
ZEPZA	-	Zambia Export Processing Zones Authority
ZCTU	-	Zambia Congress of Trade Unions
ZESCO	-	Zambia Electricity Supply Corporation
ZIC	-	Zambia Investment Centre
ZPA	-	Zambia Privatisation Agency
ZSIC	-	Zambia State Insurance Corporation

PREFACE

The policy framework on Foreign Direct Investment (FDI) and economic liberalisation in Zambia has come under public scrutiny in the recent past. The main reason for this critical appraisal is the perceived poor performance of the policies adopted during the 1990s, in not only attracting substantial amount of FDI and domestic investment in key sectors of the economy but also the failure of the economic reforms and privatisation programme in improving the economic condition of the poor.

Despite the introduction of structural adjustment programmes (SAP) and the privatisation of the ailing public sector firms, as suggested by international financial institutions and aid agencies, the sluggish performance of the economy has raised the question of the effectiveness of the policy-making process itself. Civil society and business groups have been quite vocal in pointing out the ineffectiveness of the existing policies, most of which have been inherited. As a response to this, the government came up with a draft Amendment to the Investment Act in 2003, with the objective of improving the investment climate in the country. The proposed amendment has not been adopted as yet, because it failed to address several key concerns of the stakeholders.

The interaction of the research team for this study with the stakeholders, including civil society, business and government officials during the course of the study, have revealed that there are several loose ends in the policy-making and implementation aspects of FDI. For instance, the country could not catch up with the new developments in the investment facilitation arrangements, especially the "all-under-one-roof" facility for a potential investor.

Further, there is inadequate policy co-ordination among not only the various institutions crucial for investment facilitation but also between the agencies such as the Competition Commission and the sectoral regulators. These aspects do affect investment, as they cause delays and, as a result, escalation in costs from the perspective of the investors. There is also inadequate utilisation of the arrangements such as COMESA Regional Integration Facilitation Forum (RIFF) by Zambia in strengthening investment policy matters.

This is the second report on investment policy framework in Zambia prepared by CUTS-Africa Resource Centre (CUTS-ARC), as part of a two-year research project, “Investment for Development”, implemented by CUTS India. CUTS-ARC was the partner organisation in Zambia. The Report has come up with a set of action points for the benefit of the policy-makers, inter-governmental agencies and the civil society organisations, while dealing with investment policy framework in Zambia.

The study also acknowledges the importance of advocacy in the policy-making process. This document basically aims at advocacy, awareness generation and discussion on the investment policy-making matters, by targeting the key stakeholders. In this regard, the document has incorporated the views that emerged from the three national consultations and a civil society survey carried out as part of the study.

My acknowledgements are due to the authors, Mr. Eric Kalimukwa who expired before the finalisation of this report and Mr. James Chansa, for their contribution.

We are thankful to the members of the National Reference Group (NRG), constituted under the project, and respondents of the civil society organisations for their valued inputs.

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25 November, 2003 | Sajeev K.S. Nair
Lusaka | Programme Officer

CHAPTER-1

Introduction

Foreign Direct Investment (FDI) has been long considered as a major source of capital in many developing countries in the world. Since many developing countries do not have adequate domestic capital, they adopt measures to attract capital from external sources. Although investment is considered as one of the crucial factors for higher economic growth and development, there is no unanimity among stakeholders about the role of FDI in achieving these objectives. This is especially true in the context of the sub-Saharan African countries, where FDI has not made considerable impact on the economic situation.

The capacity of African countries to attract and channelise FDI to productive sectors is principally determined by their natural resource base and the size of their local markets. United Nations Conference on Trade and Development (UNCTAD) World Investment Report (WIR) 2003 has identified the natural resources sector as an important determining factor for FDI flows into Africa.

Although there have been several analytical and empirical studies on FDI inflows, there is little consensus on which factors play an unambiguous role in explaining the location decision of foreign investors. It is generally accepted that market size and access to natural resources are crucial determinants in their decision-making processes on investment. The various incentive schemes of host countries normally play a secondary role in attracting investment. The 1990s, however, saw the growth of efficiency and strategic asset-seeking FDI.

Globally, trans-national corporations (TNCs) are the major source of FDI. Globalisation, a worldwide trend towards integration of markets, has led to a change in the FDI strategies of TNCs. Faced with increased international competition, TNCs' global strategies seek to maximise their competitiveness, by locating facilities in multiple locations around the world. Thus, attracting FDI is increasingly dependent on the ability of countries to provide a favourable FDI regime and competitive factors of production.

Investment in natural resources-based production systems brings with it a number of drawbacks. First, the prices of mineral, energy and similar primary products are, historically, prone to wide fluctuations and, thereby, expose the countries to great vulnerability. Second, many natural resources are non-renewable and require strict management. Third, investment in natural resources-based sectors can attract massive inflows of foreign currency, and that can lead to a continuous appreciation of the local currency for some time, but can lead to depreciation as soon as the boom period is over. Finally, many of these sectors (e.g., mineral, oil, gas, etc.) are capital-intensive, with standardised processes that require very little adaptation to local labour and technologies, thus generating only modest, spontaneous positive spillovers and backward linkages to the local economy.

A stable, efficient and professional environment that welcomes investors into most economic activities, without discrimination, is a necessary prerequisite for FDI inflows. Modern, legal and intellectual property rights, effective competition policies, a strong judiciary and minimum bureaucratic procedures are all important to attract foreign investors. However, the ultimate determinants of FDI are the competitive factors of production which no longer mean just cheap raw materials, labour and basic infrastructure but also require adaptable labour skills, sophisticated supplier networks and flexible institutions. While tax incentives can enhance a country's attractiveness, if other factors are unfavourable, these will be insufficient to significantly increase inflows of FDI.

The promotion of FDI in the natural resources sector in Zambia should, therefore, be accompanied by enforceable policies aimed at industrial diversification, the promotion of an R&D-base and backward linkages from natural resource-based industries to local industrial companies. Policies should aim to encourage a shift from the exploitation in this sector to the promotion of more refined goods for export purposes. This is especially important with regards to non-renewable resources, the use of which provides a one-time boost to the industrialisation process.

The Investment for Development Project

In the light of the critical importance of FDI in the framework of developing countries, the 'Investment for Development' project endeavours to study the investment regimes of selected developing/transition economies and build capacity on investment policies, trends and perceptions. The emphasis is on co-operation between countries and regions sharing information and experience and engendering joint initiatives.

This two-year project, launched in September 2001, is being supported by the Department for International Development (DFID), UK, and implemented by Consumer Unity & Trust Society (CUTS), India, in collaboration with UNCTAD.

The project involves fact-finding and advocacy work on investment regimes in seven developing and transition economies, namely, Bangladesh, Brazil, Hungary, India, South Africa, Tanzania and Zambia. CUTS Africa Resource Centre, Lusaka, is the partner organisation for the project in Zambia.

National Reference Group (NRG)

One of the key components of the IFD Project was to form a National Reference Group (NRG) in each of the project countries. The role of the NRG was to:

- monitor the quality and content of the research outputs generated;
- create a sounding board which could be used for advocacy on foreign investment regimes in the project countries;
- facilitate discussions on international investment issues and deliberate on strategies which could be used by developing countries at international fora; and
- attract attention to the project at the national level, through NRG meetings scheduled throughout the timeframe of the project.

The NRG in Zambia comprised of the following:

- academia;
- media;
- civil society organisations that have a bearing on economic issues;
- non-governmental organisations (NGOs);
- government ministries, departments and statutory bodies that deal with investment issues, in one way or the other; and
- Chambers of Commerce.

Highlights of the Report

This report is one of the seven such reports prepared by each partner organisation, as part of the project. This report contains:

- the highlights of the discussions in the NRG meetings;
- the background and analysis of key areas of the debate on FDI; and
- prioritised policy recommendations emerging from the project research and the meetings.

It also contains action points on FDI for civil society, governments and inter-governmental organisations. The report will be distributed widely in the country among policy makers, civil society organisations and business groups.

Organisation of the Report

This report comprises seven sections, *Introduction* being the first one. Section two deals with investment policy, performance and perceptions in Zambia; section three discusses briefly stakeholders' views on FDI in Zambia, while sections four, five and six discuss the advocacy points for the government, inter-governmental organisations and civil societies, respectively. Finally, section seven contains a brief conclusion.

CHAPTER-2

Investment Policy, Performance and Perceptions in Zambia

An Overview

Since 1991, the Government of Zambia has been pursuing liberal economic policies. The important aspects of this policy framework have been the implementation of a rapid and far-reaching Structural Adjustment Programme (SAP). This strategy, supported by the International Monetary Fund (IMF) and the World Bank (WB), was a major shift from the previous economic policies, which were guided by strict government control on economic management.

At the heart of the new order of economic management has been, *inter alia*, trade liberalisation, removal of exchange controls, public service reform, introduction of cost-sharing (arrangement where both government and citizens share the responsibilities of meeting the costs) with respect to the service sectors – education, health, water, electricity, etc. The private sector-driven approach also had emphasis on attracting foreign investors to Zambia.

In order to attract foreign investors to Zambia, the government offered generous fiscal incentives in the Investment Act of 1993. This statute repealed and replaced the Investment Act of 1991. The 1993 Investment Act, as amended in 1996 and 1998, promotes investment, including FDI, mainly in productive activities. The government has continued to revise and offer other additional incentives through the annual national budget and the recently enacted Zambia Export Processing Zones Authority Act (ZEPZA) of 2002.

Articles 16(1) of the Constitution and 35(1) and (2) of the Investment Act provide for protection of investment projects. In accordance with the above, no property or interest in right over property can be compulsorily acquired, except for public purposes, under an Act of Parliament and against prompt payment of compensation. The Investment Act also guarantees investors the right to transfer funds abroad. These are positive steps towards establishing investor confidence and attracting investors to Zambia.

Have these incentives made a difference in attracting FDI to Zambia? To be objective, it has been difficult to discern the exact levels of FDI inflows have been to Zambia. More often than not, the Zambia Investment Centre (ZIC) has information on only investment pledges/commitments. May be this is an area that needs further research.

Trends in FDI Flows

Zambia's gross fixed capital formation (GFCF) declined from about 43 percent of the GDP in 1996 to around 18 percent in 2000. This was largely due to the poor performance of the mining sector. FDI flows increased from US$97mn in 1996 to US$198mn in 1998, but declined to US$72mn in 2001.

Investment commitments from Zambian and foreign investors increased from US$185mn in 1996 to US$1,013.2mn in 1998 and declined to US$82.2mn in 2000 and US$110.3mn in 2001. On the basis of the commitments, South Africa ranks first among the source countries of investments, followed by the United Kingdom. Zambian investors accounted for little more than one quarter of the investment commitments made over the period 1995-2001 and nearly 15 percent were made jointly by domestic and foreign investors.

The implementation of the privatisation programme, including the sale of state-owned mining companies, has largely influenced the trends in FDI flows since the early 1990s in Zambia. Despite a decade of liberalisation and reforms, FDI flows constitute only a small fraction of overall net resource flows into Zambia. In 1999 and 2000, however, FDI constituted 36 and 26 percent respectively of net resource flows.[1]

UNCTAD World Investment Report 2002 also gives a comprehensive picture of FDI inflows into Zambia, from 1985-2001. Assuming that the 1985-1995 period is the base year, a snap shot analysis of the data reveals that the performance of FDI flows to Zambia has exhibited a decreasing trend over time, of course not withstanding the peak recorded in 1997. Again, an analysis of the UNCTAD FDI Performance Index reveals that, for Zambia, the value of the index has fallen from 4.2 during the 1988-1990 period to 1.7 during the 1998–2000 period. However, on a score of 0–1, the inward FDI potential index for Zambia has risen from 0.111 in the 1988–1990 period to 0.160 during the 1998–2000 period.

Table: Foreign Direct Investment in Zambia, Overview, Selected Years (US$mn)						
FDI Flows	**1985–1995 (Annual Average)**	**1997**	**1998**	**1999**	**2000**	**2001**
Inward	104	207	198	163	122	72
Outward	Nil	Nil	Nil	Nil	Nil	Nil
Source: UNCTAD, World Investment Report 2002						

FDI and the Mining Sector

FDI in the mining sector in Zambia, historically, was not attracted by fiscal incentives but by the potential high rents that it offered. The contribution of the mining sector to the Zambian economy cannot be over-emphasised. Copper still accounts for about 60 percent of the country's foreign exchange earnings. Since early 1980s, however, the mining output has declined, largely because of declining copper ores, poor re-investment into new and existing mines and unsupportive management techniques. For instance, the fear of the closure of Konkola Copper Mines (KCM), following the withdrawal of Anglo-American Corporation (AAC) in 2001, not only affected the Copperbelt province but the entire mining sector, due to its interdependence, and the entire system could have become economically unsustainable. However, with the timely intervention of the government with the assistance of international agencies avoided the closure of KCM.

As a result of the withdrawal of ACC from KCM, the World Bank expects FDI to Zambia to fall by more than 40 percent, while its Gross Domestic Product (GDP) to decrease by more than 3 percent. The government had previously expected the GDP to grow by 4 percent by 2002. The decrease in export earnings, according to the World Bank, would make Zambia's external debt situation, currently totalling to almost US$7.3bn, unsustainable, from both the export ratio and government revenue collection. Even the funds expected from the enhanced Highly Indebted Poor Country (HIPC) initiative would prove insignificant[2].

Civil Society Perceptions of FDI

A civil society survey, in the form of a questionnaire, was conducted in Zambia among trade unions, the media, business associations, NGOs and charitable organisations. There were 43 respondents to the survey. The survey intended to obtain the views/perceptions of the civil society on a number of issues pertaining to FDI in Zambia. The survey was mainly conducted in Lusaka and the Copperbelt Provinces. Most respondents agreed on the positive aspects of FDI, which include bringing in valuable new technologies and management techniques, improving the competitiveness of the national economy, making up for insufficient domestic investment, increasing access to world markets, etc. Paradoxically, the respondents also showed a high degree of agreement on taking steps to increase FDI to Zambia, though they would like to restrict it in the retail business, energy and small-scale mining sectors.

It was a general perception in the country that Zambia has attracted many warehouse investors who, after the tax-free period, wind up business and leave the country. This trend, it was felt, is responsible for the country's present economic woes. Thus, many perceive foreign investors as only interested in getting access to the country's resources. They cite the example of the Kapiri Glass Factory, which, after being privatised, was ripped of its assets and abandoned. The respondents who held this view were predominantly from the Zambian Copperbelt. This is because most of them had bread-winners or relatives who were directly affected by the privatisation of the mines, which resulted in most miners being declared redundant, as a result of the ensuing down-sizing strategy embarked on by the new mine owners.

Added to this is the perception that foreign investors are exploitative, in order to maximise profits by keeping unskilled casual employees for years at meagre salaries. It is a fact that, since Zambia has been generous in giving incentives to foreign investors, the same should also be given to local investors, who are likely to be less exploitative and would reduce capital flight.

The survey results show that civil society respondents recommend that, in order to achieve broad benefits, government intervention is necessary to impose requirements on foreign investors for, among others, creating jobs, employing local managers and sourcing supplies from local firms. Respondents also emphasised the need for the government to invest in physical infrastructure, strengthening sectoral policies, making appropriate approaches to investment locations, increasing information disclosure, strengthening labour laws, marketing the country for tourism, reducing corporate tax, strengthening competition policy, making stable and comprehensive trade policies as well as tackling corruption, with its attendant effects of high transaction costs.

CHAPTER-3

Stakeholders' Views on FDI

Stakeholders' Views on FDI

Three National Reference Group meetings were organised in Zambia in April 2002 and February and April 2003. The meetings discussed the research report on investment policy, performance and perceptions in Zambia. Some of the highlights of the NRG meetings are given below:

Economic Liberalisation and FDI

NRG members expressed the view that economic liberalisation programmes introduced in Zambia since early 1990s made the economy much more competitive than before. Liberalisation has also brought in higher value for money for consumers, as their choices are reflected in the market due to increased competition in the economy. Zambia should adopt measures to enhance competition not only among the state-owned enterprises but also the private sector and TNCs. Further, the country requires enabling conditions for more effective outcome of the liberalisation.

The Regulatory Environment and Privatisation

It was discussed that, since early 1990s, Zambia has attempted to improve its business climate as a way of attracting foreign companies. Establishing a competitive business climate is a difficult task because it takes time not only to implement policies but also to convince potential investors. The state participation in productive, service and trade sector activities has declined considerably during the period. Certain state-owned enterprises, such as the Zambia Electricity Supply Corporation (ZESCO), Zambia Telecommunications Company Ltd (ZAMTEL) and Zambia State Insurance Corporation (ZSIC), still are monopolies, or exercise rights, in their respective field of activity.

The Telecom Sector

Zambia initiated the process of privatising its state-owned enterprises through the Zambia Privatisation Agency (ZPA), established in June 1992 (under an Act of Parliament) as an independent body, with an in-built majority of private-sector representation. In the case of Zambia, the pace of reform in this regard has been rather significant, as nearly 80 percent of the total of 300 odd state-owned firms have been privatised in 10 years. Prominent among these has been the state owned mining companies. The liberalisation of the telecommunications sector has seen the emergence of direct investment, through the establishment of mobile phone operators, namely, TELECEL and CELTEL.

These are providing the much-needed competition to the national state-owned enterprise, ZAMTEL. This has brought with it consumer benefits, in terms of quality of service and reliability, to a certain extent. The Communications Authority (CA), the sector regulator, has also invited other investors to consider investing in this sector. VODACOM of South Africa, in mid-2002, expressed its willingness to invest in the Zambian mobile phone business sector.

The Energy Sector

The Zambian Government has unbundled the energy sector. The importation of crude oil, which was originally a monopoly function of the state through the Tanzania-Zambia Pipeline, Indeni Refinery and the Zambia National Oil Company, has now been completely liberalised, with a view to attracting private sector participation. The government now places tenders in the open market to eligible companies that have the capacity to import crude oil on behalf of the state.

The Energy Regulation Board (ERB), the sector regulator, which was established by an Act of Parliament, oversees the activities of both local and foreign investors in this area. There is also scope, in the short-term, to attract private sector participation in the water sector. Currently, the provision of water services is commercialised, in line with the government policy. The regulation of the sector is undertaken under the auspices of the National Water and Sanitation Council (NWASCO). These reforms, it is hoped, will serve as a stimulus to attracting not only local investment but also FDI, as is the case with South Africa.

It is to be noted that the success of privatisation should not be measured in terms of the speed by which firms are privatised. It should be measured in terms of the rationale for liberalisation and the benefit accrued from liberalisation, *viz.* productivity, quality, profitability and competitiveness. It is a popular belief that privatisation of loss-making state-owned enterprises will make them profit-making. It might not be true in Zambia or even in other countries. The privatisation experience of Britain suggests that, rather than the issue of who owns the company, it is the competitive environment within which a firm operates that weighs more as the most crucial factor influencing its performance.

Trade Policy Reforms and Investment

The tariff levels of Zambia are much lower than the average regional level. As a result, many cheap goods enter the market and pose unfair competition for the domestic sector. Most Zambian-owned manufacturing firms face problems while doing business in the country, due to the existing policies. Zambia has attracted mainly warehouse investors, who have come for retail business of goods produced elsewhere, but not for setting up production facilities in the country.

What measures has Zambia taken to deal with export subsidies given by neighbouring countries, which create difficulties for the Zambian producers? The members of the NRG felt that COMESA and SADC should not allow export subsidies, as this adversely affects the member countries. However, the COMESA Treaty allows member states to invoke trade remedies in cases of dumping or subsidies being provided to exporting companies from other member states.

How can Zambia reduce the production cost, which, at present, is much higher than other countries in the region? Export subsidies give an advantage to the exporters and this usually hurts competing companies in the importing economy. However, one should not use the competition authority for protecting the high cost local industry but use trade and industrial policies.

Poor Interest of Investors in Zambia

Many who participated in the NRG meetings expressed the view that, even in the absence of statistical evidence of the amount of FDI inflows to Zambia, it can be concluded that much has not happened with respect to FDI. Maybe, the question to address is why Zambia, despite all the efforts in terms of structural adjustment and additional foreign investor incentives, has not been much of an FDI destination?

The NRG was of the opinion that Zambia did attract a few foreign investors, *e.g.* in the mining sector. However, the NRG members felt that most foreign investors have not established new firms. Rather, they took over already existing firms and especially those that were vibrant. It was believed that the privatisation of loss making state-owned enterprises will make them profit-making. However, this did not happen in Zambia, or in many other countries.

Inadequate Infrastructure and Skilled Personnel

Inadequate infrastructure facilities are a major roadblock in attracting FDI in Zambia. There is a need to find ways of improving the overall investment climate, by taking into account infrastructure provision, strengthening labour laws and guaranteeing workers' rights as well as seeing to it that the government steps up its investment in human capital. Technology transfer and skill-sharing are neglected at present. The country also lacks skilled manpower, due to the absence of quality education and training institutions.

Enabling Conditions to Attract FDI

Concerning the enabling conditions for provision of credit facilities to investors, it was clarified by a representative of the Zambia Investment Centre that potential investors are required to give evidence that they do not have sufficient funds in order to make them eligible for credit facilities. Regarding the question of allowing foreign investors to use financial intermediaries in the country for credit, it was clarified that some proof of verification needs to be done by the Investment Centre before allowing investment by foreigners. This will ensure that the foreign investor has sufficient funds and need not depend on local credit for running the firm.

With regard to the issue of inadequate collaboration between domestic firms and MNCs, it was suggested that, ideally, there should be a strong domestic sector for this. It should be ensured that domestic investors do not exit the market. Some members suggested that there should be separate policies governing domestic and foreign investors. This is because what is good for foreign investors need not be good for domestic investors.

Investment incentives include direct instruments (grants or subsidies, tax holidays, investment tax credits, depreciation allowances, etc.) to reduce the fixed costs of making an investment, and indirect instruments, (trade tariffs and quotas and foreign exchange restrictions) that affect the decision to invest.

It was suggested that more export processing zones should be set up to give a boost to the export sector. At present, about four Indian companies are operating in these zones. The requirement for EPZ should be worked out by the Ministry of Commerce, Trade and Industry, Export Board of Zambia (EBZ), Zambia Investment Centre, etc. It was observed that though foreign investors are welcome to Zambia, it should not be at the expense of the local ones. Currently, foreign investors are offered certain incentives and it was suggested that local investors should also enjoy the same.

The present investment policy does not induce local investors, as they feel that foreign investors are given priority. At the same time, Zambia should be made hospitable to foreign investors.

For attracting FDI to Zambia, there is need to also look at the economic, social, political and cultural climate in the country. Fiscal incentives and regulation alone are not sufficient to attract FDI and this is supported by studies on the Zambian economy. The government should also seriously consider investing in education, beyond what is currently prevailing. It is through education that a lot of problems can be tackled – poverty, HIV/AIDS, sustained availability of skilled human resources, etc.

External Pressure

In the 1998 Paris Club meeting of international donors, it was conveyed to Zambian authorities that they would not support the Balance of Payments crisis, unless Zambia liberalises its economy. Moreover, political and economic governance issues were put as conditions for aid. NRG members opined that donors should stop giving policy prescriptions which are alien to the country. Zambia should not be asked link structural adjustment with the Poverty Reduction Strategy Paper (PRSP), which many African countries do. It needs to have an increasing level of awareness on structural adjustment. It was commented that the withdrawal of AAC from KCM seems to be an embarrassment for the World Bank as it had pushed for privatisation of the mine a few years ago as a condition for lending.

Perception of high levels of corruption is another invariable factor that discourages FDI in Zambia. The Transparency International Report of 2001 placed Zambia at 76 out of 90 countries on its scale of 'Corruption Perceptions' Index', which is only 14 places from the bottom. The NRG members recommended that the government should address this fundamental issue.

Impact of FDI in Selected Sectors

The NRG members discussed that the sectors that are important in assessing the impact of FDI in Zambia are mining, tourism, food and agro-processing and agriculture. Some of the impacts are discussed below.

The condition of the mining sector is not encouraging, though the sector continues to be a major recipient of FDI inflows. The country received a jolt when the AAC announced its withdrawal from the KCM and Konkola Deep Mining Project (KDMP) in 2002.

The withdrawal of AAC showed that the investment climate and the economy is vulnerable to external shocks and that the investment legislation in Zambia does not compel investors to look at corporate ethics and social impacts. The timing of privatisation is also an important aspect which policy-makers should take note of. It is not advisable to privatise a mine when the market price of that mineral is at its lowest. Also, one needs to be cautious about undue donor pressure for privatisation programmes. The NRG members also opined that public investment in the infrastructure sector is crucial to attracting FDI in the sector.

It was recommended that, in terms of small-scale mining (*i.e.* emeralds), most of which is labour intensive, very little policy support goes to the sector. Marketing of gem-stones also remains a problem for the sector.

The tourism sector is a fertile ground for foreign investors, but some of them are not serious investors. In certain cases, the investor acquires sites on a priority basis and, after a period of time, sells it off and leaves the country. The Investment Centre needs to investigate these matters. There were allegations that investors in the tourism/resorts sector sometimes violate the rules governing wild life protection. It was opined that Zambia Wild Life Authority (ZAWA), which is under the Ministry of Tourism, should be the right agency to examine and deal with these allegations. Local investors may not have sufficient resources to invest in the tourism sector, which is the reason for attracting FDI.

CHAPTER-4

Agenda for Action – Government

The most important task of bringing about changes in a national investment regime rests with the government. It should also liaise with other stakeholders, *e.g.* business, civil society and inter-governmental organisations, on this issue. Zambia needs to move faster in a number of policy and regulatory areas, in order to make the economy competitive. Further, along with economic liberalisation other changes, such as elimination of subsidies and administrative allocation of goods and services, have to take place.

The Need to Create an Enabling Environment

Good governance is the most important factor facilitating investment into a country. The perception of high levels of corruption discourages investment into Zambia. This is a fundamental issue that needs to be addressed by the government. Agencies and departments such as the Ministry of Legal Affairs (MLA), the Immigration Department, the Anti-Corruption Commission (ACC), Transparency International (TI) and Afronet should co-operate to eliminate corruption from the country.

Privatisation has been an important channel of FDI inflow in many developing countries. The Zambia Privatisation Agency (ZPA) should continue to put in place effective and transparent policies to attract FDI. The country also needs effective intermediaries such as banks and credit institutions to strengthen the investment climate. The responsible ministries, which can achieve this, are the Ministry of Finance and National Planning (MOFNP), the Bank of Zambia (BOZ) and the Ministry of Commerce, Trade and Industry (MCTI).

The country also needs to find ways to reduce the high cost of production for the companies. This can be done by the government though creating better policy and operational environment, with less bureaucratic red tape and achieving economic stability. EPZs are an important step in this regard, if they are able to function professionally. Infrastructure is another area on which the government should concentrate. Further, ZIC should function as a one-stop-shop for the investors, so that they can get all the investment-related approvals and facilitations swiftly from one place by ensuring better coordination with concerned departments.

The government should continue to implement a competitive incentive framework for facilitating investment, while simultaneously leveraging its comparative advantage in mineral resources and improve the supply of skilled manpower, infrastructure and institutional capacity, distribution networks and technological capabilities. The responsible institutions for this should be the MOFNP, the MCTI and the Export Processing Zones Authority (EPZA).

The Zambian legal and judicial systems are inadequate to support the needs of investors in Zambia. The responsible ministry should carry out reforms in corporate contract, bankruptcy, labour laws and property rights. Judicial reforms are critical to ensure their implementation. It should also be ensured that the judiciary is not involved in corrupt practices.

Investment in Health and Education

There is an urgent need to increase investment in health and education in Zambia. While it is the government's job to improve the health and education indicators, it should also create an environment for private sector investment, so as to use the resources of the latter. Further, it should utilise public resources in the health and education sectors, to improve the productivity and skill-base of the workforce. Through education, a lot of problems can be tackled – poverty, HIV/AIDS and sustained availability of skilled human resources, among others.

There is a role too for the private sector for supplying medicines for diseases such as HIV/AIDS and malaria, where consumers are willing to pay for preventive treatments and this can be monitored by the public sector. AIDS is a development catastrophe in Zambia, as it is killing people in the prime of their working and productive lives. The responsible institutions, which should co-ordinate with each other and come up with an action plan for improving investment in health and education, are the MOFNP, the Ministry of Health (MOH) and the Ministry of Education (MOE).

The Need to Co-ordinate with Other African Countries

LDCs compete with large developing countries and industrialised countries in attracting foreign investors. Many of the LDCs lose out in this competition because their markets are often not large enough and they have shortage of resources. One way to overcome this is to enter into regional co-operation, which can also facilitate inward investment from the countries of the region.

National efforts by different African countries towards investment promotion activities are not co-ordinated with each other, though there is a strong case for the LDCs, such as Zambia for increasing such co-ordination.

Given the general image problem, Zambia would benefit by co-operating in FDI promotion programmes. This would involve consolidating investment codes and other regulatory provisions across countries and pooling advertising efforts. If accompanied by effective lowering of trade barriers in COMESA or SADC, Zambia would also benefit from the larger market size in the region, overcoming one of the major handicaps of investing in the region. The responsible institutions in the government that should deal with regional co-operation are the MCTI, the ZIC and the ZEPZA.

International Marketing of Investment Opportunities

Despite Zambia's acceptable levels of economic growth in the recent past, low political risk, policies to promote both domestic and foreign investment and an abundance of natural resources, it still fails to attract adequate levels of investment to further boost growth and reduce poverty. The country requires intensive investment promotion. It is necessary that the government concentrates more on international marketing, negotiating with companies and enforcing ethical behaviour by its public officers. The responsible bodies are ZIC and ZEPZA.

However, the main task of investment promotion belongs to the ZIC. The functioning of the ZIC will have to be improved, before it can undertake vigorous investment promotion measures. Since the ZIC lacks resources for carrying out investment promotion, the services of Zambian embassies and consulates abroad should be utilised for promoting the country as a good investment destination.

CHAPTER-5

Agenda for Action – Inter-Governmental Organisations

Inter-governmental Organisations (IGOs) and donor agencies have played an important role in providing resource support to developing countries for the past few decades. These organisations have also carried out extensive research and analysis on the subject of FDI and have developed considerable database. IGOs have also undertaken training and capacity building exercises of government officials in the recent past and have the resources to do so. Clearly, there is a role for them in improving national FDI policies.

Using Aid More Effectively

IGOs contribute substantially to Zambia by providing developmental and capacity-building aid. There has been a lot of scepticism in the recent past about the effectiveness of aid in reducing poverty levels and stimulating economic growth and development. One way to increase the effectiveness of aid is by using it for building trade opportunities between the donor country and the recipient. For example, if an agro-processing plant was set-up in Zambia and financed by a donor, then the country could start adding value to its agricultural exports by extending its operations further down the value chain.

The other issues are the speed of aid disbursement and the effective use of the aid money. Disbursement and monitoring procedures should be overhauled first, while making sure that the target group does receive the benefit of aid. It is also important to increase the amount of aid available to developing countries, including Zambia, by raising the percentage of aid to 1.2 percent of the developed countries' GDP, as laid down by the Monterrey Consensus on financing for development.

Infrastructure projects need to be given special attention. More money should flow into this sector. There is a need to speed up and simplify the process of contract award for infrastructure. In the past, the World Bank was involved in the financing and privatisation of a number of infrastructure projects in developing countries. Some of the projects have been controversial and the outcome of the group's involvement has been disappointing. It is important that the World Bank, and IGOs keeps paying attention to the special conditions prevailing in a country before undertaking any policy ventures in it.

Improving the Social Role of FDI

IGOs should disseminate information among investors, governments and civil society on the use of FDI so that all are aware what to expect from it. They should emphasise the importance of the social dimensions of globalisation, by reiterating the need to benefit from FDI. IGOs should ensure that foreign investors, particularly trans-national corporations (TNCs), are socially and legally responsible and accountable too.

IGOs should support the implementation of the International Labour Organisation (ILO) Tripartite Declaration of Principles concerning Multilateral Enterprises and Social Policy (which are related to the Organisation of Economic Cooperation and Development (OECD) Guidelines on Multinationals) on training/industrial relations, setting out principles in the field of employment, training, working conditions and industrial relations.

The international donor community should also support developing country efforts to improve the impact of FDI on wages of low-skilled workers. They should support good quality and appropriate education and general training for low-skilled workers. They should recognise the potential benefits from vocational training schemes, which is an appropriate element of a private sector development programme.

CHAPTER-6

Agenda for Action – Civil Society

Civil society organisations can play an important role in the policy making process of a country. Often, they carry out research on the investment regime and economic development matters of a country and are in a position to spread information and build capacity of civil society and government officials on this. Civil society can also act as a check on government and business activities. The civil society and business facilitation organisations, which could be involved in investment policy related issues, are the ones that have carried out research and advocacy on this subject in Zambia. Organisations such as Zambia Trade and Investment Enhancement, (ZAMTIE), Zambia Association of Manufacturers (ZAM), Zambia Chamber of Commerce and Industry (ZACCI), Private Sector Development Programme (PSDP), Transparency International (TI), Women for Change (WFC), Zambia Congress of Trade Unions (ZCTU), CUTS-ARC, etc., among others, could be involved.

The Need to Co-operate with the Government

Civil society should work closely with the government in bringing about changes in investment policies and practices. It should involve itself with the policy-making process though consultation, lobbying and research. Civil society should co-operate with the government to reduce inefficiency within the civil service, devote more resources in the development of physical and social infrastructure and speed up projects to completion with fewer delays. It should ensure that the government defines property rights properly.

It should also effectively co-operate with the government in the anti-corruption drive. Corruption is particularly manifest in securing licenses and tendering process, clearing of goods through customs, obtaining permits and clearing tax assessments. Civil society representatives should be engaged with the work of ZIC more closely and ensure that the ZIC co-operates with the MOE, the ACC, the CSO and other relevant departments.

Need to Work with the Business

Civil society should co-operate with business associations and chamber of commerce for setting up business and investment councils, which promote effective dialogue between business and the government and business and civil society. Companies and civil society can also collaborate in the elimination of corruption from the country. Investors can tackle corruption from the supply side and provide evidence of corrupt procedures hindering investment. Thus, it is important that investors also introduce an element of self-regulation through corporate ethics and avoid closing deals negotiated on extortionate terms detrimental to the country.

Civil society should raise awareness on this issue and inform the people of the country about corporate social responsibility standards and principles. It should also help in developing and implementing corporate social responsibility standards by co-operating with each other, companies and the government.

Civil society should impress on the foreign investors that their investment should create jobs, employ local managers, transfer technology, source supplies from local firms and transfer skills and know-how to them.

The Need to Build Capacity/Generate Awareness

It is important that informed civil society organisations build capacity and disseminate information on investment-related matters. Working with the media, holding debates and discussions, and distributing documents and publications can do this. They should also use their research to propagate information and build capacity of government officials on investment issues. They should work closely with IGOs to carry out further research and analysis on this. Civil society plays a major role in evolving the perceptions of a country.

CHAPTER-7

Conclusion

A facilitative FDI regime remains fundamental for attracting FDI. But, today's globalising investor has a wide choice of developing country locations and desires those that are capable of enforcing competition, providing stable and transparent rules for private business and, over time, improving the quality of their local productive factors. While there have been significant improvements in the policy regime for FDI in Zambia, it has not been significant enough to attract FDI, which facilitates integration of the state economy with the global economy and has a positive influence on development.

Unfortunately, Zambia continues to suffer from a poor image as an investment location, despite efforts to promote and market the country. The declared pullout of AAC from KCM and KDMP has sent negative signals to the international investor community.

Most crucially, the economic disparities between Zambia and other developing regions (with the exception of the natural resource sector) remain considerable. Infrastructure, human capital, supplier and distribution network, technological capabilities and support institutions are all relatively weak in Zambia.

For Zambia, therefore, the way forward should be to continue implementing a competitive incentive framework, while simultaneously leveraging the country's comparative advantage in mineral resource endowments and continuing to improve the supply of skills, infrastructure and institutions. While the main task of improving the investment regime remains with the government, other stakeholders such as civil society organisations, inter-governmental and other international organisations can play a role in this.

ANNEXURE

Summary of NRG Discussions

One of the most important activities of the IFD project was the formation of a National Reference Group (NRG) in each project country to provide a sounding board and quality check on the research outputs. Another purpose of the NRG meetings was to attract attention to the project at the national level.

First NRG Meeting

April 25, 2002, Lusaka, Zambia

NRG members expressed the view that economic liberalisation in Zambia, since early 1990s, was fast paced, to increase the level of FDI. However, FDI has remained constrained due to inadequate infrastructure, lack of skilled personnel, weak labour laws and high inflation and interest rates.

The view of the participants was mainly that the FDI that has come into the country, especially in the manufacturing industry, has predominantly been warehouse-investing for selling goods produced elsewhere, instead of setting up production facilities in the country. Even in terms of trade policies, the tariff levels of Zambia are lower than the regional level. As a result, many cheap goods enter the market and exert unfair competition. Therefore, the blame for this should be apportioned to the policy-makers, local producers and the importing countries.

The participants also criticised not only the speed of privatisation of the mines and the donor pressure but also the timing of privatisation, as it is not intelligent to privatise a mine when the market price of that mineral is at the lowest. The reference was to the privatisation of copper mines. They also expressed concern that even when regulatory reform reached an advanced stage through the creation of the Zambia Competition Commission, Energy Regulation Board, Communications Authority, Pensions and Insurance Authority, etc. true competition remained elusive. Certain parastatals such as the Zambia Electricity Supply Corporation (ZESCO), Zambia Telecommunications Company Ltd (ZAMTEL), and Zambia State Insurance Corporation (ZSIC), are still monopolies or exercise rights in their respective field of activity.

The participants also raised the issue of export subsidies being given by the neighbouring countries, which created difficulties for the Zambian producers. They warned against the use of the competition authority to protect the local industry, when trade and industrial policies could be improved upon and used effectively.

They lamented the fact that, at present, no private enterprises in Zambia are able to take over firms owned by foreign investors. The domestic industrial sector is not in good shape and several industrial units in towns such as Luanshya, Ndola, etc., have either closed down or relocated.

In order for the majority to benefit from FDI, the participants recommended an enabling environment of appropriate regulation. They also felt that Zambia needed to protect its domestic industry, by keeping track of FDI flows into the country and carefully choosing foreign collaborators. It should also find out the role of donors.

It was also discussed that Zambia has done well in many areas, including the setting up of the export processing zones. However, the NRG members suggested that in order to attract FDI Zambia needed to invest in electricity, telecommunications, infrastructure such as roads, waste disposal, etc. The law and order environment should also be improved.

The present investment policy does not attract domestic investment. Foreign investors are given priority and are also extended various incentives. While Zambia does not want to bring foreign investors at the expense of domestic ones, there is need to make the country hospitable to them. Potential areas identified by NRG members for case studies include investment in tourism, manufacturing/machinery industry, agriculture and food processing, and small-scale mining sectors.

Second NRG Meeting

February 13, 2003, Lusaka, Zambia

Discussions in this meeting centred on the need for analysing Zambia as a competitive destination of FDI. The participants felt that while it is important to look at the economic, social, political and cultural climate in the country, fiscal incentives and regulations alone are not sufficient to attract FDI. The participants were concerned about perceptions of high levels of corruption – Zambia stood at 76 out of 90 countries on Transparency International's scale of 'Corruption Perceptions' Index', only 14 places from the bottom. This is another invariable factor that discourages FDI to Zambia.

However, three sectors dominated the discussions as priority destinations of FDI *viz*, tourism, agro-processing and mining. Although evidence indicated that the mining sector continued to be a major recipient of FDI, a dark cloud was cast over the sector when AAC announced its withdrawal from the KCM and KDMP. This adversely affected the country's employment, state revenue and the gross domestic product. To mitigate the impact of future pullouts, it was recommended that the sector re-introduce the gem stone exchange and plant hire schemes as well as create a community development fund to develop backward and forward linkages with downstream industries and other spin-offs.

The participants also felt that private sector participation could be enhanced, especially in the tourism sector, by the creation of an enabling environment for the private sector, through the provision of adequate infrastructure and legislation to support growth. At the same time, these actions could be supported with a proactive marketing strategy by the government to attract investment in the sector.

The discussions on the agro-processing sector centred on the need to build its capacity to expand production, productivity and competitiveness, to meet the challenges of local and international demands, by directing the policy at encouraging synergies between large and small-scale producers through out-grower schemes. Meat processing in the agro-processing sector is one area where more data could be collected to unravel its potential in attracting FDI inflows. It was felt that, since the majority of people in Zambia are poor and rely, to a great extent, on agriculture, investment policies should take a direct approach at this sector.

Third NRG Meeting

April 16, 2003, Lusaka, Zambia

The third NRG meeting took up three issues for discussion, *viz.* (a) Investment Policy, Performance and Perceptions in Zambia, (b) the National Advocacy Document (the current report: Investment Policy in Zambia – An Agenda for Action) for Zambia and (c) co-ordination among sector regulators for a sustainable FDI environment. The meeting called for the adoption of a national investment policy for Zambia, which would harmonise the conflicting regulations on investment, to enhance FDI inflows.

Apart from the conflicting areas in legislation, the participants also discussed other negative factors for FDI that were apparent in Zambia, including the delay in processing permits and lack of appreciation of each others' legislation by all sector regulators. Ordinarily, the ZIC has to liaison with a minimum of three or four sector regulators while processing an investment application in any sector.

The participants recommended that measures that would identify conflicting Acts under which they operated should be put in place. This would then serve as a lynchpin for sector regulators to harmonise, streamline and synchronise all aspects of investment procedures.

The participants also reviewed the country's investment policies in attracting FDI to Zambia, the prominent ones being the restoration of macroeconomic stability through monetary and fiscal reforms, the facilitation of private sector growth by removal of price controls and exchange-rate and, import and export controls as well as shifting agriculture and industry from public monopolies to the private sector in decentralised institutions.

Although the above policies were important, the participants observed that the existing Investment Act of Zambia was nothing to boast about, from the perspective of an investor, because it is outmoded and cannot match with investment policy legislations of other countries in the region. Having been formulated as part of the economic liberalisation strategy of the early 1990s, the Act failed to address several investor concerns. This has resulted in an investment making process that is, at best, uncoordinated and, at worst, driven by bilateral institutions. They contended that the Zambia Investment Act is a fragmented piece of legislation, which is inadequate for business purposes, let alone investment promotion. They suggested that Zambia should emulate the investment promotion practices of countries such as Namibia and Botswana, in terms of facilitating all the investment registration formalities under the same roof within a set time frame.

One of the hurdles in attracting FDI to Zambia was identified as excessive and insensitive bureaucracy. The case of Zambia Wildlife Authority (ZAWA) towards investment was cited in this context where genuine investors and those who do illegal activities were treated in a similar manner of suspicion and lack of trust for eco-tourism projects. They argued that this hurdle is the reason for little FDI in the other sectors as well.

The participants were also concerned about the weak linkages among the sectors of the economy and a shrinking economy that has negative effects on FDI in Zambia.

It was observed that since an investor looks for opportunities to spread risk across the borders, Zambia needs to become a production platform for exporting to other countries at low cost, in an efficient and stable macroeconomic environment. In order to do this, under the COMESA platform, Zambia should provide a comparative investment environment and base, which allows the investors to produce not only for the local market but also for the regional markets. In doing this, Zambia will be establishing its position in the regional Common Investment Area, under the auspices of Regional Integration Facilitation Forum (RIFF) and COMESA. After all, among the COMESA countries, Zambia was still a high recipient of FDI in the region, despite the decline of foreign investment in the past few years.

The participants also recommended diversification of the economy, from a mineral-based to knowledge-based one such as former mineral-based economies like Finland and Hungary. Further, policies of various departments dealing with investment issues, including the immigration, customs, environment and wildlife, etc., should be harmonised in attracting investment.

On the national advocacy document, the participants observed that the advocacy document needed to include a time frame with names of responsible institutions in order to have a clear picture about who or which institution will implement the recommendations. It was suggested that the advocacy part should clearly specify the target in terms of influencing policy matters. In this regard, the meeting was informed that Cabinet Ministers, Deputy Ministers and Members of Parliament should be targeted, by making available to them copies of the advocacy document, as well as involving some of them in the meetings. CUTS–ARC was also asked to synergise its activities with other institutions such as Zambia Trade and Investment Enhancement (ZAMTIE).

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