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German Development  
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Discussion Paper

8/2010

# The Role of South African FDI in Southern Africa

*Peter Draper  
Sheila Kiratu  
Cézanne Samuel*



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Peter Draper  
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Cézanne Samuel

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Governance, and for Developing Countries”

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## Abstract

Since 1994, the pivotal year in which South Africa held its first democratic elections, its companies have engaged in a sustained outward foreign direct investment (OFDI) thrust with substantial impact on Southern Africa, in the process generating some controversy. The paper revisits those debates and updates them in light of recent data and developments concerning the evolution of institutions supportive of South African regional OFDI, notably regulations governing investment and trade respectively. We find that South African OFDI to Africa is private sector dominated, concentrated in Southern Africa albeit evincing a discernible shift to West Africa in recent years, and its impact is on the whole beneficial. However, the actions of the South African government to support the activities of their nationals in the region are schizophrenic, particularly in its use of BITs, which seem to favour an approach that provides substantial advantages to its companies at the possible expense of host-nation policy space. We recommend therefore that in its ongoing review of its model approach to BITs the South African government should remedy this ambiguity.

Peter Draper, Sheila Kiratu, and Cézanne Samuel

Bonn, July 2010



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## Abbreviations

BIT	Bilateral Investment Treaties
COMESA	Common Market for Eastern and Southern Africa
CRIA	COMESA Regional Investment Agreement
FDI	Foreign Direct Investment
FIP	Finance and Investment Protocol
GDP	Gross Domestic Product
LDC	Least Developed Country
M&A	Merger and Acquisition
MFN	Most Favoured Nation
MNC	Multinational Corporation
MTN	Mobile Technology Networks
OFDI	Outward Foreign Direct Investment
RTA	Regional Trade Agreement
SACU	Southern African Customs Union
SADC	Southern African Development Community
SARB	South African Reserve Bank
UNCTAD	UN Conference on Trade and Development



## 1 Introduction

Since 1994, the pivotal year in which South Africa held its first democratic elections, its companies have engaged in a sustained outward foreign direct investment (OFDI) thrust. Since South Africa's economy is so much larger and more diversified than those of its neighbours, and indeed the rest of the continent, much of that OFDI has targeted non-African destinations. But the investment which has found its way into the continent, particularly Southern Africa, has had substantial impact and in the process generated some controversy. That debate raged in the early years of this millennium but fortunately for South African policy makers the advent of Chinese OFDI into Africa, and now an emerging Brazilian and Indian thrust, distracted the attention of those who are critical of the process.

This paper constitutes a desk-top based attempt to revisit those debates and to update them in light of recent data and developments concerning the evolution of institutions supportive of South African regional OFDI, notably regulations governing investment and trade respectively.

Section 2 reviews the purported benefits that South African OFDI into the region brings, focused essentially on provision of network services infrastructure which otherwise would probably not be built. It qualifies this by noting that South Africa does not have the economic muscle to drive economic development through FDI and trade in the manner of Japan's impact on Southeast Asia. It also addresses arguments pertaining to the perceived costs of such OFDI, but finds most of these arguments do not hold up to scrutiny barring potential national security concerns. Even those need to be considered against the manifold development needs of recipient states. Section 3 reviews the data and notes that South African OFDI is private sector dominated, and whilst Southern African countries are still the largest recipients notes that in recent years there has been a discernible shift to West Africa, particularly Nigeria. Section 4 reviews the evolution of regulations relating to investment in Southern Africa, particularly investment and trade. Concerning the former the key framework pursued by the South African government is bilateral investment treaties; whereas trade is – at least in principle – fairly comprehensively covered by the Southern African Customs Union and Southern African Development Community Arrangements. Section 5 concludes.

## 2 South Africa's African FDI: The debate

Table 1 and Figure 1 (see annex) show that South Africa dominates Southern Africa economically; dwarfing the next largest economy, Angola, such that South Africa accounts for 58 percent of the Gross Domestic Product (GDP) of the Southern African Development Community (SADC) versus Angola's 17 percent. Furthermore, the South African economy is much more diversified than any other in the region; in Angola's case its GDP and exports are overwhelmingly concentrated in the oil sector. The two next largest Southern African economies in 2008, Tanzania and Zambia, are both least developed countries (LDCs); each accounts for a negligible proportion of the combined SADC GDP (4 percent and 3 percent respectively). Zimbabwe, once a regional manufacturing and agricultural powerhouse, has slipped virtually off the radar screen amidst its ongoing political crisis and now has a smaller economy than Botswana. Unsurprisingly, as Table 2 and

Figure 2 (see annex) reveal, there is a similar picture on the export front although with relatively high oil prices in the first half of 2008 Angola's export figure is accordingly somewhat distorted.

Consequently South Africa is believed to have substantial impact on growth in other African countries (Arora / Vamvakidis 2005), and its outward Foreign Direct Investment (FDI) and associated trade expansions are likely to have substantial impacts on its neighbours and other countries in the sub-continent. Here we explore the contours of that impact by reviewing relevant literature, focusing initially on OFDI then turning to trade since it is often closely tied to investment.

The origins of South Africa's corporate expansion into Africa lie primarily in the conjuncture of two simultaneous and related processes: the demise of Apartheid; and the end of the Cold War and associated triumph of the "Washington consensus" development paradigm pursued by the Bretton Woods institutions (BWIs) globally. The former provided the outward impulse; the latter the opportunities as countries across the continent liberalized their economies under structural adjustment programmes. Figure 1 (see annex) shows that overall regional markets are reasonably open by developing country standards, at least as measured by average import tariffs.

We begin with the alleged costs involved for countries hosting South African FDI, since much of the initial debate focused on this issue; then we turn to the purported benefits. We conclude with a brief review of trade dimensions and impacts.

#### *Investment: Costs*

Concrete examples of the direct costs concerning South African OFDI for African host states include the citing of twelve South African companies for allegedly looting mineral resources in the Democratic Republic of the Congo (UN 2002, cited in Daniel / Naidoo / Naida 2003, 386), and alleged flouting of labour standards by some companies (Pillay 2004). There is also anecdotal evidence of alleged corporate malfeasance and arrogant behaviour reminiscent of Apartheid attitudes. This is in line with concerns within some quarters of the South African government, based on evidence sourced through its missions across the continent, that the South African corporate community in general may not be behaving like good corporate citizens in host markets.<sup>1</sup>

There is also the risk of domestic market dominance: McGregor's (2004, 2) found that some 17 percent of South African investments in Africa enjoyed a market share of greater than 75 percent. However, this was offset by the finding that 67 percent of investments held less than 25 percent market share. So whilst host governments must be vigilant, it appears from this evidence that the risk is overstated. Furthermore, the Chinese OFDI thrust into Africa is forcing South African (and other) investors on the continent to adjust to the competition to up their game and provide better quality products at lower prices (Salter 2009). Furthermore, the majority of South African investments are small – it is generally the large-scale projects that capture the headlines.

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1 Discussions with government officials.

What of the problem of enclave investment associated with resource-extractive FDI? South African FDI is more diversified than that traditionally sourced from developed countries, covering network services (telecommunications; finance; transport; and energy). Furthermore, the Business Map Foundation noted that in the case of the Mozal aluminium smelter in Mozambique, for the first time on the continent a serious and successful attempt was made to build linkages to the local economy thereby minimising the potential for enclave development (Rumney / Pingo, 21). This indicates a degree of sensitivity on behalf of the South African government to regional concerns. Furthermore, the pattern of greater market-seeking FDI builds host country markets thereby enhancing long-term prospects for economic diversification. Crucially, this process is driven substantially by economic reforms in host countries (South Africa Foundation 2004, 20), thus qualifying (although not necessarily nullifying) the conventional wisdom that structural adjustment packages have caused the continent's deindustrialization.

Finally, and in light of a growing international debate on this issue, there is the theoretical possibility of South African (and other foreign national) FDI into regional host markets posing a national security threat. Moran (2009) identifies three threat typologies concerning M&As:

1. the host country becomes dependent on the supply of goods and/or services from the acquiring firm (sometimes linked to that firm's home government);
2. the acquisition would allow transfer of sensitive technology away from the host country to potential rivals;
3. The acquisition would allow insertion of potential capability for infiltration, surveillance, or sabotage into the host country.

Furthermore he notes that for any of these threats to obtain the industry concerned must be tightly concentrated, the number of close substitutes limited, and switching costs high. In the case of FDI into Southern Africa in general it is relatively easy to imagine conditions (1) and (3) obtaining in 'sensitive sectors' (network services; defence) but condition (2) is fanciful. Furthermore, as noted above South African companies tend to dominate regional markets in which they operate since there is not a great deal of competition in those markets as they remain pretty unattractive to Multinational Corporations (MNCs) owing to their small size.

So if we accept Moran's analysis then it follows that national security may feature in host states' consideration of South African OFDI into their markets. This would seem to apply particularly to investment sourced from parastatals since they are arms of the South African government; in a few cases OFDI by these companies is substantial. A related question is whether South African OFDI in finance and communications in particular could be linked to the South African state's security interests in the region. Unfortunately it is beyond the scope of this paper to address that issue

#### *Investment: Benefits*

South African FDI flows into the continent are more diversified than those sourced from developed countries, with significant flows taking place in network services activities. (UNCTAD 2005b, 11) argues that these are driven more by merger and acquisition (M&A) activity than greenfield investment, implying that on aggregate they are more

market – or asset – rather than resource-seeking. According to the South Africa Foundation (2004, 16) market-seeking FDI, measured on the basis of number of projects, was concentrated on SADC markets prior to 2004, whereas FDI into non-traditional African markets was targeted primarily at the mining and energy sectors (South Africa Foundation 2004, 17).

Hence South African companies are directly contributing to the slow build up of crucial productive infrastructure in network services (Draper / Kalaba / Alves 2006). Since most African economies face significant challenges in developing their supply-side capacities, which in turn is a function of the underdevelopment of network services infrastructure, this is to be welcomed. However, given South Africa's domestic growth problems and the relatively small size of its economy there are limits to this process. Consequently South Africa's expansion into the continent in the long-run is unlikely to result in the same dramatic development benefits which Japanese FDI wrought in Southeast Asia; in this sense the "flying geese" analogy does not hold since there is no other goose available to lead from the front once the South African goose is exhausted.

While concerns about deindustrialisation or crowding out of domestic companies must be carefully addressed, the so-called "new scramble for Africa" by South African companies is, according to studies based on interviews with South African companies operating on the continent, yielding substantial benefits for the continent. These include job creation; upgrading of existing and building of new infrastructure including investment in backbone services; technology transfer through human resource development (McGregor's 2004)<sup>2</sup>; increased tax revenues; increased consumer choice; and boosting general investor confidence in host countries (Games 2003; Grobbelaar 2004a).

Concerning job creation, 24 355 jobs are said to have been created in Mozambique by South African companies from 1998–2002 (Grobbelaar 2004b). Similarly, in a survey of 40 top South African companies invested on the continent McGregor's (2004, 2) found that a total of 71,874 people were employed across 232 investments outside of South Africa. Of these, only 2,257 were South African expatriates, mostly in managerial and technical positions. It is not clear whether M&A's associated with these investments have led to retrenchments. If so, such job losses would have to be offset against the employment numbers cited here. Furthermore, UNIDO (2006, IX) found that South African investors pay the highest wages, on average, of all foreign direct investors in Africa. This is partly due to the skill-intensive nature of South African subsidiaries.

Some examples concerning investments in infrastructure are also pertinent. Mobile Technology Networks (MTN), the South African telecommunications MNC, has had to build roads to service rural coverage requirements stipulated by telecommunications licensing conditions in several countries (McGregor's 2004, 2). The South Africa Foundation (2004, 12) noted that 27 percent of projects covered in their survey were in the infrastructure sector, especially power, whilst telecommunications accounted for 5 percent. South

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2 The report notes that most South African investors have a policy of transferring skills to local employees over a period of three to five years from the initial investment. South African companies are particularly sensitive to such concerns given the centrality of black economic empowerment policies to their bottom line in South Africa.

African banks have also expanded rapidly into the continent, in the process upgrading often antiquated financial systems (Jekwa 2005).

These benefits are reportedly linked to a general view amongst the South African corporate community that they are in Africa for the long-term and hence need to play their part in sustainable investment. This view has helped them to unseat European competitors who, according to McGregor's (2004, 2), have a reputation for dumping inferior technology and quality at premium prices. South African companies are quite prepared to adapt products to local market conditions, and in many cases already do so in the domestic market (McGregor's 2004, 3).

### *Trade*

In Southern Africa many useful productive inputs and capital equipment items that aren't domestically produced are sourced from South Africa. The South Africa Foundation (2004, 9) noted with respect to South Africa's exports to the continent that:

*“There is a high proportion of value-added exports to the rest of Africa, with machinery, mechanical appliances, iron and steel articles, transport goods, chemicals, and plastics and rubber goods accounting for close to 70% of the total. This is an important consideration, as it ties in with South Africa's domestic economic structure, based traditionally on mining, agriculture, engineering and chemical products, and their allied industries. These are also the areas that are attracting the most (investment) interest in other African countries.”*

Clearly this does not negate political concerns associated with rising trade imbalances between South Africa and its neighbours, which feed perceptions of “recolonisation”. Indeed, there is in all likelihood a strong connection between OFDI by South African companies in these and other sectors, and increasing exports from South Africa. That is because most of the countries into which such OFDI is destined do not have well-developed supply capacities; consequently it makes business sense for the South African companies concerned to export from their home base until such time as those products can be competitively sourced in the host market.

Nonetheless, there is a long history behind regional fears of South African domination, most notably the Apartheid state's destructive destabilization of its neighbours from the late 1970s. However, the charge that this trade imbalance implies exclusively negative consequences should be challenged: what matters are the drivers of these imbalances, rather than the fact of their existence (Corden 1997, chs 17–18; Draper / Freytag 2008). The basic point is that if the deficit is driven by imports of productive equipment and other inputs, there is little cause for concern in the long-term. Deficits become problematic when finished consumer products are their principal drivers. Furthermore, the bulk of the region's commodity exports are destined for developed country markets and, increasingly, China, whereas South Africa possesses many of those commodities and hence does not need to import them from the region.

### *Concluding observations*

From this brief survey of the literature, it is apparent to us that on balance South Africa's OFDI footprint and associated trade expansion into (Southern) Africa are mostly positive.



Where there are negative impacts these are principally associated with rogue operators and sometimes nebulous national security concerns. In the next section we review recent empirical data concerning OFDI in particular in order to gauge the contours of South Africa's regional OFDI thrust.

### 3 Updating the analysis: Data review

Figure 2 (see annex) shows that South Africa's total OFDI is primarily directed outside the Southern African region; the latter rarely exceeded 10 percent of the total between 1997 and 2007 albeit it showed a tendency to increase from 2001. Furthermore, Table 3 (see annex) shows that until recently South Africa's outward FDI to Africa was concentrated in SADC countries, particularly Mauritius (see the box). However, it is evident that in recent years there has been a substantial shift into the rest of sub-Saharan Africa. This may reflect relative saturation of market opportunities in Southern Africa, although it is widely expected that two countries in the region will be the target of substantial South African OFDI flows in the coming years: Angola and Zimbabwe.<sup>3</sup> Nonetheless, the United Nations Conference on Trade and Development (UNCTAD 2009, 67) note that South Africa's intra-African OFDI flows have shifted from Southern to West Africa in particular, presumably representing opening up of opportunities in the latter especially Nigeria – as shown in Figure 3 (see annex).

#### Box 1: Mauritius

The data from the SARB shows that out of all the countries in Africa, South Africa has the largest share of foreign assets in Mauritius, nearly 30 percent to be precise. While this is interesting it is hardly surprising. Mauritius in recent years has become an internationally acclaimed tax haven. It offers some of the most lucrative investment opportunities and was recently voted the best place to do business on the African continent according to the World Bank's Doing Business Report.

South Africa's investment is concentrated in the private non-banking sector and specifically in long-term capital. In UNCTAD's World Investment Directory for Mauritius, it is shown that the largest South African affiliate in the country is an insurance company called Munich Mauritius Reinsurance Company (although this is a subsidiary of the European Multinational Munich Re). They offer primary insurance and reinsurance. The government has introduced numerous incentives for companies specialising in financial services amongst other things.

Table 3 shows that in 2006 there was a huge increase in South Africa's OFDI to Mauritius, accounting in that year for 33 percent of total FDI into Mauritius. The Board of Investment in Mauritius confirms that this FDI was concentrated in the IT and Business Process Outsourcing (IT/BPO) services sector. This sector is a substantial contributor to economic growth in Mauritius accounting for 5.7 percent of GDP in 2007. This South African investment occurred in line with the development of the Ebene Cyber City in the capital of Port Louis, the new information technology hub. In 2007 six South African companies began operations in Mauritius; they were all IT/BPO companies.

3 President Zuma made his first overseas trip to Luanda in August 2009, and was accompanied by a large business delegation eager to take advantage of Angola's post-conflict reconstruction needs which will be financed by its financial windfall owing to the oil price boom. In Zimbabwe's case, the assumption is that within the next few years a sustainable political settlement will be reached; major South African parastatal organizations and private sector institutions stand poised to reinvest on a significant scale once that occurs. Given political uncertainty in Zimbabwe much play has been made of the recently signed bilateral investment treaty.

With regards to the composition of South Africa's foreign assets in Africa, Figure 4 (see annex) shows that direct investment is the dominant form. Table 4 (see annex) shows that the private sector, particularly the banking sector, dominates South African OFDI flows. Given the large amount of portfolio inflows into South Africa from the rest of the world, it may be that those inflows are recycled into FDI outflow into the region; in other words it is possible that South Africa's sophisticated financial markets are being used to channel resources across Africa. Parastatal institutions are also significant outward investors into the region, but since 1997<sup>4</sup> this has been primarily concentrated in two Southern African countries: Mozambique (associated with the construction of the Mozal Aluminium smelter and development of the Maputo corridor); and Lesotho (associated with the Highlands water project). Since 2003 public corporations have picked up their OFDI into Namibia and Zambia; and in 2007 significant amounts were invested in Nigeria and the rest of Africa.

Overall, whilst South African OFDI into Southern Africa is a relatively small portion of its global footprint, it has grown in recent years and is relatively diversified. In light of the discussion in the previous section this growth is to be welcomed, albeit any rough edges would need to be attended to. Next we turn to the interesting question regarding the South African government's approach to securing its companies' OFDI into Southern Africa, dealing first with investment related regulations then turning to trade.

#### **4 Regulations governing South Africa's OFDI in Southern Africa**

First we address South Africa's resort and approach to bilateral investment treaties (BITs), then we turn to the utility of the SADC Finance and Investment Protocol (FIP). In the case of BITs South Africa has recently resorted to securing more favourable regulations concerning treatment of its companies, having come from a long history of reliance on inward FDI. We also discuss trade related regulations and incentive structures, particularly the impact that South African OFDI has on building regional economic integration. This is important because securing regional markets through regional integration arrangements is in the interest of South African MNCs.

##### *Investment: BITs and other international investment agreements*

Given the sizeable intra-Africa investments made by South African companies, the country is concerned with how best its citizens' investments may be safeguarded. This raises difficult questions with regard to the appropriate model for agreements, bilateral or regional, that contemplate South Africa's OFDI and that equitably balance investors' rights with the sustainable development needs of African countries. Complicating this situation is the fact that South Africa is historically reliant on inward FDI and has had mixed experiences with BITs negotiated with developed country partners (Peterson 2006) which are now seen to unduly intrude into domestic policy preferences – especially concerning black economic empowerment.

South African companies and organized business appear to support their government's negotiation of bilateral investment treaties (BITs) with other African countries. Table 5

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4 Data is sourced from the South African Reserve Bank (SARB) and is available on request.

(see annex) shows that South Africa has 5 BITs with countries in the SADC region, of which the Democratic Republic of the Congo is really Central African. Interestingly none of those countries are members of the Southern African Customs Union (SACU), the governing agreement of which does not contain any investment protection provisions (Kiratu 2008). Yet this has not prevented substantial South African investment in those markets over many years Mozambique, which has seen substantial South African OFDI not least by parastatals; Mauritius – the largest destination country; and Tanzania which is a substantial investment destination in Southern Africa are covered. Concerning potential OFDI destinations in Southern Africa Angola is included in the BIT net, and a BIT with Zimbabwe has just been signed amidst considerable controversy since the terms exclude land acquired since the onset of the Zimbabwean government’s controversial land reform programme. The Zimbabwean BIT is motivated by genuine fears from South African investors that their investments would not be secure in light of the prevailing political-economic climate in that country. The East African BIT net seems to be in place, and covers Kenya, Uganda, and Rwanda. Interestingly South Africa does not have any BITs with its major West African OFDI destinations in Nigeria and Ghana, whereas Senegal is covered.

Typical clauses in South Africa’s BITs revolve around the scope of an investment, definition of investment and investor, geographic application of the agreement, duration and termination, standards of treatment (national treatment and Most Favoured Nation – MFN), expropriation, transfer of funds and dispute resolution. The last item is puzzling to see in “South–South” investment agreements because it is widely recognized that this model of BITs perpetuates imbalanced relationships (between the home and host states) and inequitable outcomes (for the host state). Whereas developing and especially African countries want to attract inward investment the usefulness of binding international rules on investment is controversial as they tend to limit a host state’s policy choices and do little to attract investment (Hallward-Driemeier 2003). Affirmations of a state’s rights to development, its right to regulate in the public interest or to pursue other social goals are largely absent from these agreements. Even the preambles which are supposed to reaffirm the purpose of these treaties, and which may be crucial for later interpretation of the treaty provisions in dispute settlement contexts, are bereft of reference to more ambitious social or developmental goals.

The World Bank study (Hallward-Driemeier 2003) concluded that investment rules found in BITs had little impact on investment decisions and warned that these could “*expose policy makers to potentially large scale liabilities and curtail the feasibility of different policy options as is demonstrated by the recent tide of investor-state arbitrations challenging government measures pursuant to investment rules.*” South Africa is acutely aware of this imbalance having being subjected to judicial processes<sup>5</sup> that challenge its public policy stances, resulting in the Department of Trade and Industry’s recent assessment as to whether investment rules strike the right balance between investor protection and the reservation of host state policy space.<sup>6</sup> Now that the country understands the potential impact

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5 The current pending dispute in which Italian investors are challenging South Africa’s Black Economic Empowerment Code is an example of how public policy goals can be challenged under BITs. See further, Piero Foresti and others vs. Republic of South Africa ICSID Case No. ARB(AF)/07/1); online: <http://icsid.worldbank.org/ICSID/FrontServlet>

6 South Africa’s Bilateral Investment Treaty Review accessible at [http://www.thedti.gov.za/ads/bi-lateral\\_policy.pdf](http://www.thedti.gov.za/ads/bi-lateral_policy.pdf).

of BITs on a country's domestic policies and the need to inject greater balance in such agreements, it will be interesting to watch if it will continue to negotiate BITs in the region that seem to be stacked in favour of South African investors without the necessary safeguards to preserve flexibility in critical policy areas for African countries.

Furthermore, whereas this model gives investors rights against the excesses of governments there are no comparable rights for governments. In the region this creates a situation where smaller county governments cannot discipline the excesses of South African companies without political consequences and the risk of being sued. The South African government is cognizant of this imbalance, from a host state perspective, and its aforementioned assessment argues that any new BIT template arising out of the review should create obligations for home states that may be expected to provide certain information, assist in combating corruption and ensure that investor liability extends to the home state in an appropriate manner. The fact that South Africa, through its OFDI in the region, is also a home state means that it should be in a position to shoulder obligations that it would like to level on other home states in terms of any new BIT template that may arise out of this review.

In South Africa's BITs protection for investors is offered only in the post-establishment phase; in other words pre-establishment rights are not accorded. South Africa's BITs normally include MFN exceptions which permit the contracting parties to deny investors of the other contracting party more favourable treatment resulting from either's membership of a regional trade arrangement (RTA) where the other party is not a member. The rationale for this exception stems from the nature of regional economic integration which purports to grant privileges to the member countries in exchange for reciprocal preferential treatment. This exception prevents these privileges from being extended to those contracting parties of BITs that are not members of the RTA concerned.

In addition to the above BITs South Africa has ratified the agreement on investment protection and promotion in SADC, the Finance and Investment Protocol (FIP). The South African Treasury was a key motivator behind this agreement, reflecting its desire to make the region more secure for investment in general, and presumably South African OFDI in particular.<sup>7</sup> Annex 1 (Investment) of the FIP creates a framework for FDI promotion in SADC and in some aspects emulates the provisions typical of BITs. However, this instrument only seems to cater for inward FDI and does not cater for intra-SADC investment, a factor that is directly relevant to South Africa in respect of its sizable investments in the region.

Unlike most regional treaties, however, the FIP's benefits are not limited to the treaty signatories. For example the definition of investor in the FIP extends to any persons admitted to make an investment in the SADC region, thus it does not accord any preference to SADC member states. The status of the FIP contrasts with the Common Market for Eastern and Southern Africa's (COMESA) Regional Investment Agreement (CRIA) which only applies to COMESA member states, that is it caters for intra-COMESA investment. The CRIA also provides for both pre and post establishment national treatment and MFN

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7 Remarks made by a senior Treasury official at a closed seminar on the FIP.

treatment. Furthermore, 8 out of 15 SADC member states are member states of COMESA which raises questions about which agreement should prevail.

Overall, it is essential for South Africa to carefully assess the risks and benefits associated with the different agreements it is party to and to understand how they inter-relate. The government should also analyze the efficacy of “regional investment agreements” which can easily be held ransom to political processes that can delay ratification. For example, 4 SADC members have not ratified the FIP and experience in the region shows that protocols take, on average, two and half years to implement due to difficulties in domesticating the obligations and Protocols into the legal sphere of Member States.

### *South Africa and Southern African economic integration*

South African OFDI and trade with Southern African countries, and associated development of investment regulations, are mirrored in development of regional trade agreements (RTAs) and deeper forms of integration. RTAs are important complements to investment since they allow goods to flow relatively freely to and from subsidiaries located in foreign locations that are part of the RTA, and as such promote a favourable investment climate. This depends somewhat on the coverage of the RTA concerned; for our purposes the most relevant provisions concern trade in goods and, where possible, regulations concerning “trade” in services including movement of people associated with corporate personnel. Considered holistically provisions which liberalize these regulations should have the added benefit of promoting regional value-chains and integrated production, thereby developing economies of scale to compete beyond the immediate sub-region.

In this light South African OFDI into Southern Africa has been aided by the two RTAs that South Africa is part of: the Southern African Customs Union (SACU) and Southern African Development Community (SADC). Unlike BITs which largely offer protection clauses, the SACU agreement and SADC’s Trade Protocol cover not only free movement of goods but also in the case of SADC and via various protocols, mooted competition policies, proposed liberalization of FDI in services, proposed harmonization of broader property rights and contract enforcement, provide access to a large market and stable and predictable trade policies. These regulatory harmonization initiatives are important for investors since they level the playing field and promote smooth transfer of assets and the conduct of business. However, whilst numerous such initiatives have been negotiated, implementation has been patchy.

The South African government has actively promoted the use of trade instruments in the region particularly through tariff liberalization incorporating both SACU and SADC: the former is characterised by duty free movement of goods within the customs union; the latter has established a free trade area. As things currently stand the South African government’s broad vision continues to promote the former as the building block of the latter. Unfortunately, it has been complicated by ongoing political ructions concerning the problem of overlapping memberships<sup>8</sup> (Draper / Halleson / Alves 2007) and negotiations concerning establishment of economic partnership agreements with the European Union (Draper 2009). This has led the South African government to rethink the utility of SACU,

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8 Whereby countries in the region are members of two or more regional groupings.

and in light of this what approach should be taken to SADC as the broader region moves to resolve the overlap problem through potentially establishing a SADC-COMESA-EAC (East African Community) RTA in some form.

Overall, the record concerning RTAs from the South African business community's perspective is rather mixed, with the substantial exception of regional tariff liberalization which, though patchily implemented, presumably encourages exports and associated FDI.

## **5 Concluding remarks**

Overall we find that South African OFDI is essentially beneficial to its (Southern) African hosts. Notwithstanding the fact that far more South African OFDI is destined for non-African shores, but also increasingly for West Africa, this is an important factor in Southern African economic development.

Concerning regulatory support by the South African government to the activities of their nationals in the region, we find that trade regulations concerning goods are appropriately specified, albeit the regulatory dimensions are not and are bedevilled by a host of challenges. Consequently investment-related regulations are important, but the South African government's approach appears to be schizophrenic - particularly in its use of BITs. On the one hand South Africa is a major recipient of inward FDI, which is regulated by many BITs signed with developed country governments, and has recently been subjected to international arbitration which it found intruded uncomfortably into its domestic policy space. On the other hand it seems to favour an approach to BITs with African countries that provide substantial advantages to its companies. This ambiguity may be remedied through its ongoing review of its model approach to BITs, and is the one concrete recommendation arising from this paper.



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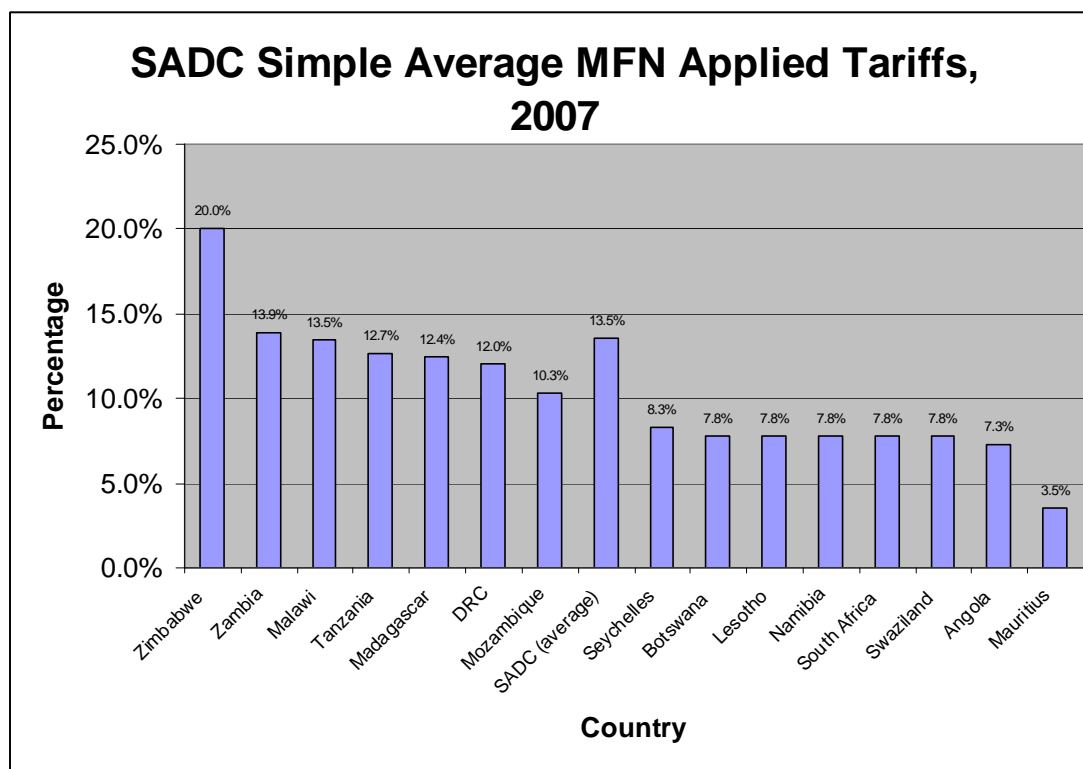
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## **Annex**

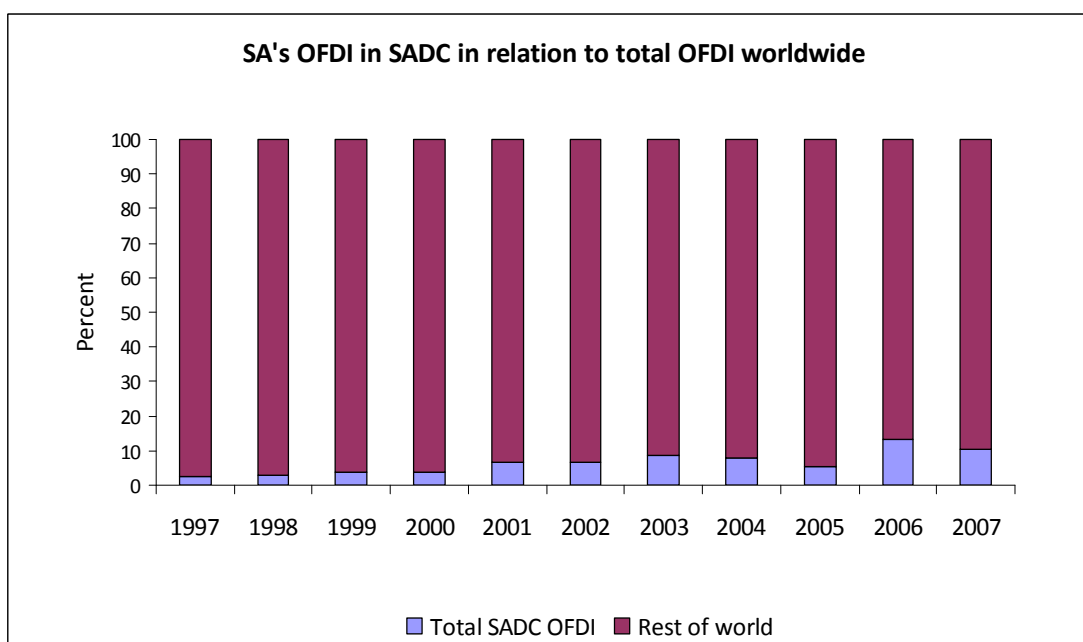


**Figure 1: SADC countries' MFN applied tariffs, 2007**



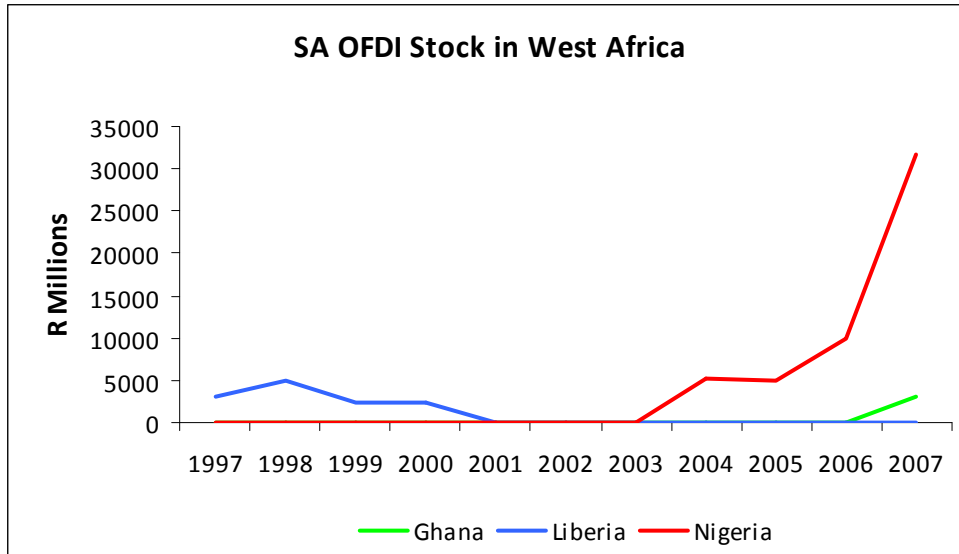
Source: SAIIA's calculations from UNCTAD data

**Figure 2: SA OFDI to SADC countries versus total OFDI**



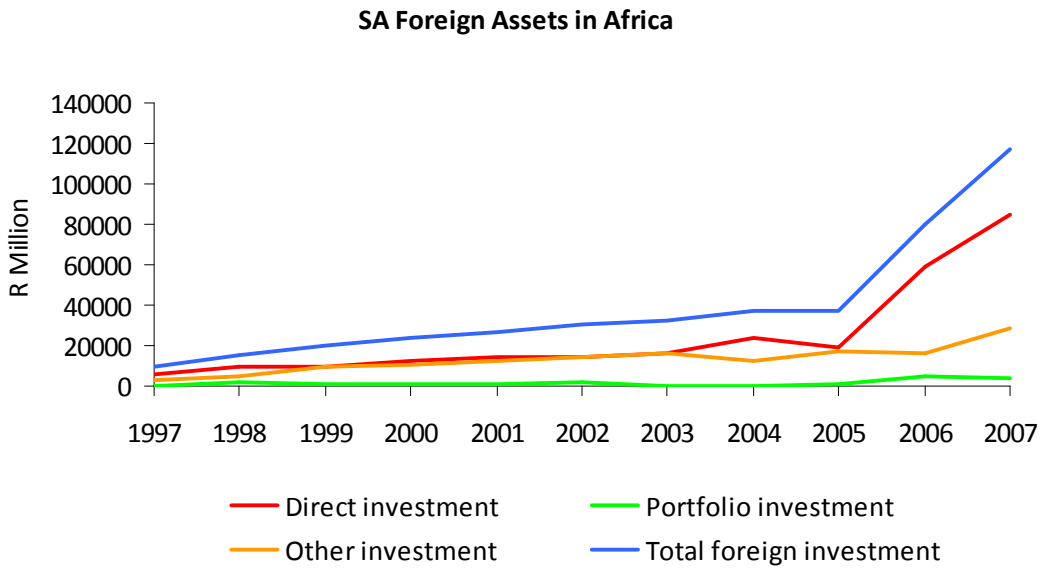
Source: SAIIA's calculations from SARB data

**Figure 3: SA OFDI stock in West Africa**



Source: SAIIA's calculations from SARB data

**Figure 4: SA foreign assets in Africa by type**



Source: SAIIA's calculations from SARB data

<b>Table 1: SADC member states GDP 2008, US Dollars (billions), current prices</b>	
Country	GDP
South Africa	277
Angola	83
Tanzania	21
Zambia	14
Botswana	13
Zimbabwe	12
DRC	12
Mozambique	10
Madagascar	9
Mauritius	9
Namibia	8
Malawi	4
Swaziland	3
Lesotho	2
Seychelles	1
Total	478
Source: SAIIA's calculations from SARB data	

<b>Table 2: SADC member states exports 2007, US Dollars at current prices in millions</b>	
ECONOMY	Amount
SA	<b>69,788</b>
Angola	41,109
Zambia	4,853
Botswana	4,005
Namibia	3,433
DRC	2,531
Mozambique	2,492
Swaziland	2,171
Mauritius	2,054
Tanzania	2,005
Zimbabwe	1,995
Madagascar	1,156
Malawi	813
Lesotho	795
<b>SADC Total</b>	<b>139,200</b>
Source: UNCTAD Database	



Country	2003	2004	2005	2006	2007	Share 2003	Share 2007
Botswana	197.7	222.6	229.9	334.6	625.4	4.6 %	3.8 %
Lesotho	152.6	164.1	155.3	216.7	190.4	3.6 %	1.1 %
Swaziland	181.2	200.7	168.8	344.6	385.3	4.2 %	2.3 %
Namibia	658.5	595.3	675.7	567.2	569.5	15.4 %	3.4 %
Zimbabwe	354.7	159.9	227.7	265.2	404.9	8.3 %	2.4 %
Mauritius	1116.7	1535.1	811.0	5230.2	4974.1	26.2 %	30.0 %
Mozambique	871.8	962.1	1040.0	1055.4	1204.1	20.4 %	7.3 %
Zambia	160.4	233.3	278.8	346.9	378.7	3.8 %	2.3 %
Rest of Africa	572.9	1604.0	2187.3	3428.5	7850.3	13.4 %	47.3 %
Total	4266.5	5677.2	5774.7	11789.1	16582.6	100.0 %	100.0 %

Source: SAIIA's calculations from SARB data

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Monetary authority	114	109	72	73	75	70	62	31	75	74	75
Public authorities	83	82	79	79	0	0	0	0	0	0	0
Public corporations	357	621	4399	6111	6983	9944	7873	7373	7848	8997	12398
Banks	696	1430	5396	6714	9068	9160	10701	6110	9074	7561	17548
Private sector	8090	13331	10492	11178	10675	10835	13663	23154	19845	63394	87206
Real estate	18	14	15	15	0	0	0	0	0	0	0

Source: SAIIA's calculations from SARB data

**Data note:**

When calculating investment flow data one would need to calculate the exchange rate to value the transaction at the time of it taking place. This will then be added to all other transactions in that period to find the final FDI flow. Information about each transaction could plausibly be collected from the exchange control department at the South African Reserve Bank however this would not be complete as a lot of these approved transactions never materialise. Therefore, the flows are calculated by subtracting each year's stock value from the previous for simplicity sake while it is acknowledged that it might not be entirely correct.

<b>Table 5: South African bilateral investment agreements in Africa</b>	
<b>Country</b>	<b>Date of Signature</b>
Algeria	24-Sep-00
Angola	17-Feb-05
Democratic Republic of Congo	31-Aug-04
Egypt	28-Oct-98
Equatorial Guinea	17-Feb-04
Ethiopia	1-Jan-08
Kenya	
Libya	14-Jun-02
Mauritius	17-Feb-98
Mozambique	6-May-97
Rwanda	19-Oct-00
Senegal	5-Jun-98
Tanzania	22-Sep-05
Uganda	8-May-00
Zimbabwe	Negotiations underway
Source: Department of Trade and Industry; as of October 2009	



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