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Linkage Between foreign Direct Investment, Trade and Trade Policy

AN ECONOMIC ANALYSIS WITH APPLICATION TO THE FOOD SECTOR IN OECD COUNTRIES AND CASE STUDIES IN GHANA, MOZAMBIQUE, TUNISIA AND UGANDA

Norbert Wilson, Joyce Cacho

OECD

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Joint Working Party on Agriculture and Trade

LINKAGES BETWEEN FOREIGN DIRECT INVESTMENT, TRADE AND TRADE POLICY
An Economic Analysis with Application to the Food Sector in OECD Countries and Case Studies in Ghana, Mozambique, Tunisia and Uganda

OECD Trade Policy Working Paper No. 50

by Norbert Wilson and Joyce Cacho

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ABSTRACT

Through empirical analysis and case studies, this document explores the relationships amongst foreign direct investment (FDI), trade and trade-related policies in OECD and four African countries (Ghana, Mozambique, Tunisia and Uganda).

In OECD countries, tariffs and market price support may have an effect on how FDI is distributed geographically. FDI may be used to avoid or "jump" tariffs. Also, investors in a home country may invest in a host country to exploit the preferential tariffs that the host has with a third country. Participation in a regional trading agreement or customs union, e.g. NAFTA or the EU, may create investment opportunities. Market price support to agriculture may encourage outward investment and discourage inward investment. In aggregate, FDI and trade appear to complement one another.

The four case studies in Africa highlight the interactions amongst regulations, foreign investment and trade. For example, FDI is useful in helping the firm develop the resources to meet the standards of OECD markets. Investment promotion agencies and export processing zones appear to prepare countries to attract FDI. Preferential trading agreements like the Everything but Arms with EU and the African Growth Opportunity Act with the US may have an impact on trade and investment.

Beyond trade policies, other policies and factors contribute substantially to the location and distribution of FDI. As seen amongst OECD countries, factors like the GDP of a country (i.e. market size) and cost of production and transport can have an effect on FDI. Another factor that influences FDI is the degree of market competitiveness. For the four African countries, the country risk and the level of infrastructure can influence the volume of FDI attracted.

ACKNOWLEDGMENTS:

This project was carried out by Norbert Wilson[1], an OECD economist, and Joyce Cacho, consultant, under the supervision of Anthony Kleitz of the OECD Trade and Agriculture Directorate. At the OECD, colleagues inside the Trade and Agriculture Directorate provided inputs and helpful comments. The authors wish to thank the Investment Promotion Authority offices in Ghana, Mozambique, Tunisia and Uganda. Leadership and efforts to identify possible companies that, through their experiences, illuminate the opportunities and challenges in expanding the FDI in the food processing industry in emerging markets, are especially appreciated. Lastly, for the companies' willingness to allocate business time to give specific details, we are especially appreciative for their commitment to catalyzing increased and sustained FDI flows to the food processing industry in emerging market countries and regions.

The Joint Working Party Agriculture and Trade of the OECD discussed this report and agreed to make the findings more widely available through declassification on its responsibility.

[1] Norbert Wilson has left the OECD and is currently an assistant professor at Auburn University, AL, USA.

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EXECUTIVE SUMMARY

Through empirical analysis and case studies, this document explores the relationships amongst foreign direct investment (FDI), trade and trade-related policies in OECD and four African countries. Although a great deal of analysis of aggregate trade and FDI exists, the contribution of this study is that it focuses on the international trends in the food sector, a sector crucial to many developing countries. With a deeper understanding of the nexus between FDI, trade and trade policy in the food sector, policy makers will be better equipped to design and implement policies, in both the food and related sectors.

From 1982 to 2002, aggregate outward stock of FDI grew from USD 802 000 million to USD 7 123 000 million. The distribution of the outward stock in 2002 was 87% for OECD countries and 13% for non-OECD member countries. The inward stock positions were 67% for OECD countries and 33% for non-OECD countries. The estimated share of FDI that Africa received in 2003 was 2%, the smallest share of any region. In 2001, this sector accounted for about 1.1% of total FDI inflows. For developed countries, FDI for the food sector accounted for about 0.9% of FDI, and for developing countries this sector accounted for about 1.5% of FDI inflows (UNCTAD).

This study suggests that FDI and trade policy are linked. In OECD countries, tariffs and market price support may have an effect on how FDI is distributed geographically. FDI may be used to avoid or "jump" tariffs. Also, investors in a home country may invest in a host country to exploit the preferential tariffs that the host has with a third country. Participation in a regional trading agreement or customs union, e.g. NAFTA or the EU, may create investment opportunities. Market price support to agriculture may encourage outward investment and discourage inward investment. In aggregate, FDI and trade appear to complement one another. Therefore, policies that open trade may also increase FDI and vice versa.

The four case studies in Africa highlight the interactions amongst regulations, foreign investment and trade. BLUE SKIES, a Ghanaian-British joint venture, is an early adopter of private standards. This early adoption helped it avoid an interruption in sales when the standards came to be considered necessary by the purchasers. Amfri Farms, a Uganda firm with a unique story of FDI, faces differing standards and certification bodies to provide OECD markets with organic fruits. In both country cases, FDI is useful in helping the firm develop the resources to meet the standards of OECD markets. Investment promotion agencies and export processing zones appear to prepare countries to attract FDI. Preferential trading agreements like the Everything but Arms with EU and the African Growth Opportunity Act with the US may have an impact on trade and investment.

Beyond trade policies, other policies and factors contribute substantially to the location and distribution of FDI. As seen amongst OECD countries, factors like the GDP of a country (i.e. market size) and cost of production and transport can have an effect on FDI. Another factor that influences FDI is the degree of market competitiveness. For the four African countries, the country risk and the level of infrastructure can influence the volume of FDI attracted.

The main lesson from this study is that trade and trade-related policies matter to FDI. Nevertheless, further trade liberalisation alone will not improve the geographical and sectoral distribution of FDI. To increase a broader distribution of FDI, the coordination of policies within and between countries to promote economic development is necessary. Additionally, the coordination of policies between the public and private sectors is also vital.

I. FDI IN THE WORLD AT A GLANCE

Introduction

1. This paper is a completed draft of the research begun under the title "The impact of trade policies on foreign direct investment in the food sector: a work proposal." [COM/TD/AGR/WP/RD(2003)57] This project has two major components: the first component is an empirical analysis of foreign direct investment (FDI), trade and trade policy among OECD countries. The second component is four case studies of FDI, trade and trade policy in four African countries (Ghana, Mozambique, Uganda and Tunisia).

2. Through empirical analysis and case studies, this document explores the relationships amongst foreign direct investment (FDI), trade and trade-related policies in OECD and four African countries. We consider in this study FDI and investments via transnational corporations (TNCs), specifically through joint ventures as means for foreign firms to invest abroad. While we call all of these investments "FDI", the specific definitions delineate the differences are available in Box 1 and the Annex 1. Although a great deal of analysis of aggregate trade and FDI exists, the contribution of this study is that it focuses on the international trends in the food sector, a sector crucial to many developing countries. With a deeper understanding of the nexus between FDI, trade and trade policy in the food sector, policy makers will be better equipped to design and implement policies, in both the food and related sectors.

Box 1. Defining Foreign Investments

Foreign direct investment (*FDI*) reflects the objective of obtaining a lasting interest by a resident entity in one economy ("direct investor") in an entity resident in an economy other than that of the investor ("direct investment enterprise"). The lasting interest implies the existence of a long-term relationship between the direct investor and the enterprise and a significant degree of influence on the management of the enterprise. Direct investment involves both the initial transaction between the two entities and all subsequent capital transactions between them and among affiliated enterprises, both incorporated and unincorporated OECD (1996) p, 7-8.

Transnational corporations (TNCs) are incorporated or unincorporated enterprises comprising parent enterprises and their foreign affiliates. A *parent enterprise* is defined as an enterprise that controls assets of other entities in countries other than its home country, usually by owning a certain equity capital stake. A *foreign affiliate* is an incorporated or unincorporated enterprise in which an investor, who is resident in another economy, owns a stake that permits a lasting interest in the management of that enterprise (an equity stake of 10 per cent for an incorporated enterprise or its equivalent for an unincorporated enterprise) (UNCTAD, 2003 p. 231).

A *joint venture* involves share-holding in a business entity having the following characteristics; (i) the entity was established by a contractual arrangement (usually in writing) whereby two or more parties have contributed resources towards the business undertaking; (ii) the parties have joint control over one or more activities carried out according to the terms of the arrangements and none of the individual investors is in a position to control the venture unilaterally (UNCTAD, 2006).

3. This study begins with an overview of FDI in the food sector in OECD countries and around the world. Following the overview, a focused literature review provides a discussion of FDI and the factors that affect its location. This discussion is followed by an econometric analysis of FDI in OECD countries, which provides with a series of policy conclusions. The four case studies look at FDI in Africa by

reviewing of the country risk, investment and trade agreements, the state of FDI in the country, and a review of firms receiving FDI.[2]

The Location and Distribution of FDI

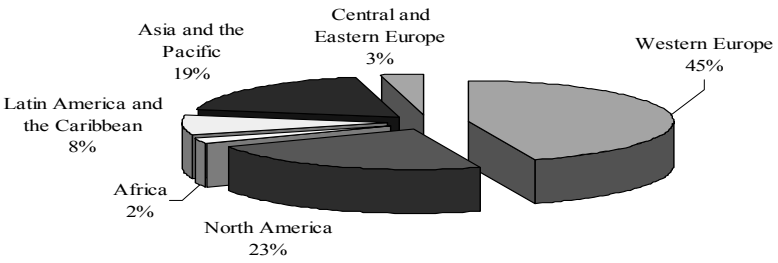
4. The location and distribution of FDI can be described by a set of stylised facts, reflecting aggregate patterns as well as patterns for the food sector: FDI has grown noticeably in recent years. The distribution of FDI among OECD and non-OECD countries has favoured OECD countries as both the host and home countries. For some OECD countries, FDI in the food sector is equivalent to as much as 3% of GDP. A few corporations in the food industry represent a large portion of FDI. One indication of the economic importance of foreign affiliates can be seen by the fact that the sales of foreign affiliates outside the home country are generally greater than exports from the home country. These stylised facts prompt further analysis to understand better how FDI and trade affect one another.

FDI in the World

5. Before discussing FDI in the food sector, consider first aggregate FDI in the world. *The World Investment Report* 2003 (UNCTAD, 2003) states that in 1982 inward stock of foreign direct investment worldwide was USD 802 000 million by 2002, the value increased to USD 7 123 000 million. Outward stock also increased over this period from USD 595 000 to USD 6 866 000 million (see Annex 1 for definitions for FDI terms).

6. This FDI is concentrated in OECD countries. World FDI inflows in 2002 were USD 651 188 million. Of this, OECD countries received 73% of the world total and non-OECD countries received 27% of the total. FDI outflows in 2002 came predominately from OECD countries: world FDI outflows were 647 363 million USD of which OECD countries accounted for 93% and non-OECD countries 7%. Similar results are seen in inward stocks (OECD countries 67% and non-OECD countries 33%) and outward stocks (OECD countries 87% and non-OECD countries 13%). Considering FDI inward stock on a regional basis, Western Europe (45%) and North America (23%) are the major hosts of FDI inward stock based on 2003 estimates. Africa has the smallest share with only 2% of inward stock (Figure 1).

Figure 1. FDI Inward Stock by Host Region, 2003 Estimate



Source: UNCTAD (2004)

2. Norbert Wilson of the OECD Secretariat completed the analysis of OECD countries and summary information. Joyce Cacho, an external consultant, completed the analysis of the four African country case studies.

7. The distribution of FDI masks the relative importance of FDI in developing countries.[3] In 2002, inward FDI stock in developing countries, using the UNCTAD definition of developing country, was equivalent to about 33% of their GDPs. For developed countries, FDI inward stock was equivalent to 19% of their GDPs. These percentages reflect significant growth in importance of FDI in both country groups because the percentage equivalents in 1980 were 13% and 5% for developing and developed countries. With this global perspective, one can begin to see the general state of FDI in the world. Let us now turn our focus to FDI in the food sector, first among OECD countries then to a select group of African countries.

3 . For UNCTAD, "developed countries" are OECD countries except for Korea, Mexico and Turkey plus Gibraltar, Malta and Israel (Andorra, Guernsey, Jersey, Liechtenstein, Man Island, and Monaco are sometimes included). Developing countries are all the others.

II. FDI AMONGST OECD COUNTRIES IN THE FOOD SECTOR

Introduction

8. The analysis of FDI amongst OECD countries considers the effects of trade and trade-related policies on the location and distribution of FDI in the food sector. Initially, this analysis begins with a brief review of the empirical results of this paper, which is followed by a review of the trends of basic statistics on FDI in the food sector in OECD countries. To establish the hypotheses for the empirical section, a focused literature review is provided. The chapter is completed with a discussion of the empirical results of the econometric models. Further discussion of the models and data analysis is in Annex 3.

Research Findings

9. The analysis of this chapter argues that FDI and trade policy are linked. In OECD countries, tariffs and market price support can have a significant effect on how FDI is distributed geographically. FDI may be used to avoid or "jump" tariffs. Also, investors in a home country may invest in a host country to exploit the preferential tariffs that the host has with a third country. Participation in a regional trading agreement or customs union, e.g. NAFTA or the EU, generally creates investment opportunities. Market price support to agriculture can encourage outward investment and discourage inward investment. In aggregate, FDI and trade appear to complement one another. Therefore, policies that open trade may also increase FDI and vice versa.

FDI for the Food Sector in OECD Countries

10. These aggregate figures in Chapter 1 provide a context to understand FDI. Nevertheless, the focus of this paper is on the food sector.[4] In 2001, this sector accounted for about 1.1% of total FDI inflows. For developed countries, FDI for the food sector accounted for about 0.9% of FDI, and for developing countries this sector accounted for about 1.5% of FDI inflows (UNCTAD).[5]

11. While only a small component of FDI, the FDI in the food sector of OECD countries has grown over the 1990s. The four largest host and home countries were the United States, the United Kingdom, the Netherlands and France (see Figures 1 and 2 also see Annex 2 for additional figures).[6] The United Kingdom and the United States had outward FDI stocks, on average over the decade,[7] of USD 30 600 and

4. For the food sector, much of the OECD FDI data, discussed in this paper, relate to "manufactured products of which food." Further investigation of these data reveals that, at least for the United States, this sector includes beverages and tobacco products 15 and 16 ISIC Rev 3. These data are compatible with the trade data in the OECD STAN.

5. These data are based on a subset of 50 countries which account for 89% of total FDI inflows in the world.

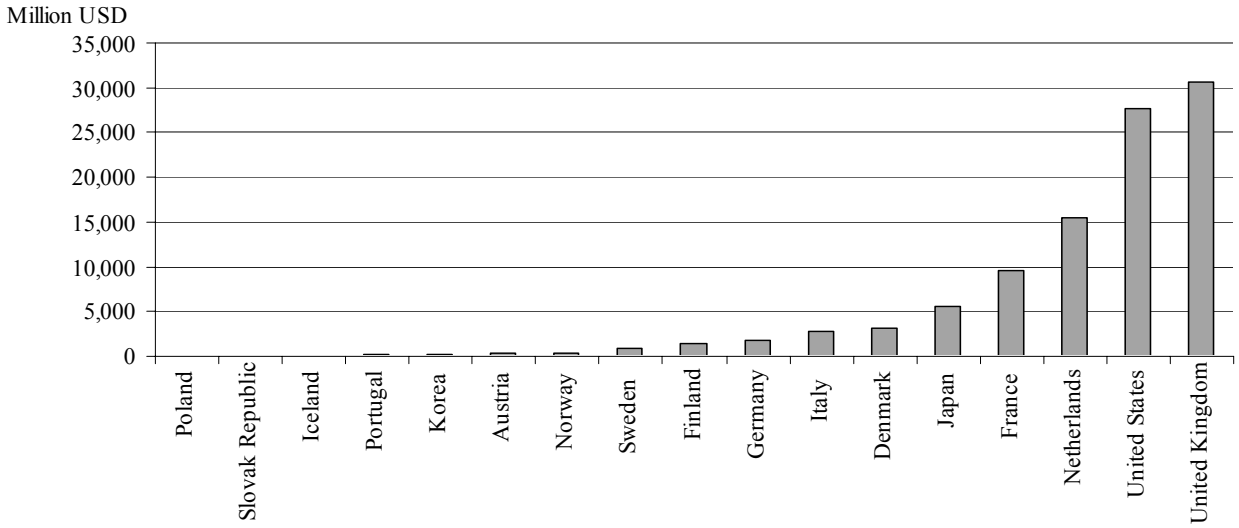
6. FDI data are not available for all OECD countries. For many of the countries reported, data for all years are not available. Therefore, care should be taken in the cross-country comparisons.

7. Note several countries reported no data: Outward stock: Australia, Belgium, Canada, Greece, Hungary, Ireland, Luxembourg, Mexico, New Zealand, Spain, Switzerland and Turkey and Inward stock: Canada, Belgium, Greece, Ireland, Luxembourg New Zealand, Spain, Switzerland, and Turkey.

USD 27 642 million in constant USD (Figure 2). In terms of average inward stocks over the 1990s, the United States at USD 22 104 million was more than twice as large as the next largest host, the United Kingdom at USD 9 097 million in constant USD (Figure 3). Other countries of note because of their size and growth include Japan, Denmark, Italy and Germany in terms of their outward stocks, while Austria, Mexico, Italy and Germany are of note for their inward stocks.

Figure 2. Outward Stock FDI in the Food Sector

Averages 1990-2000

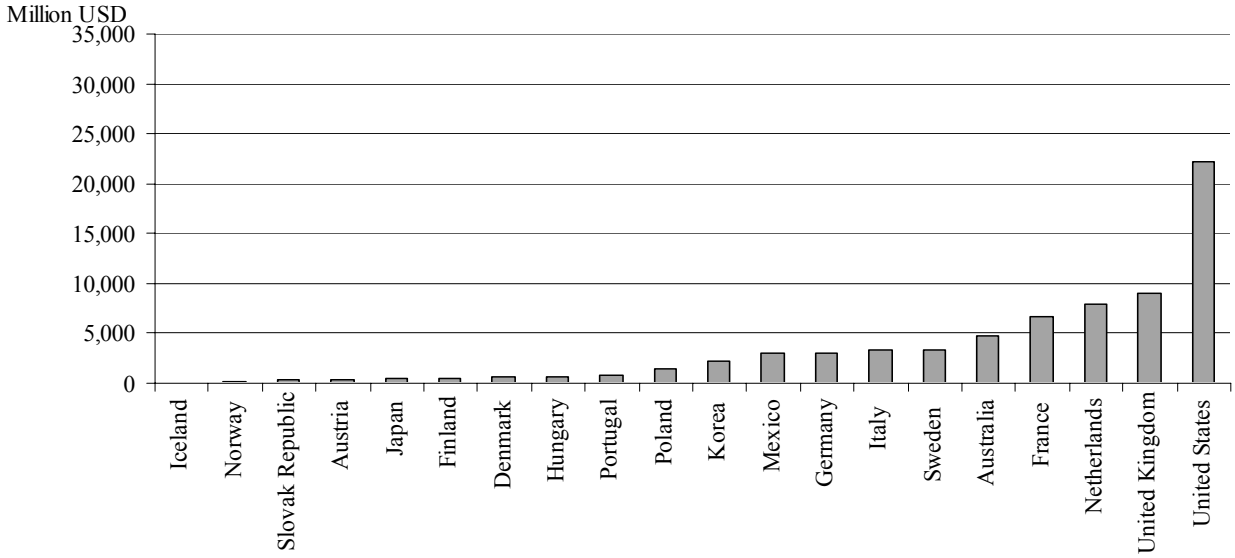


NB: Data for every year are available for Austria, France, Germany, the Netherlands, the United Kingdom and the United States. Iceland, Poland and Slovak Republic had average FDI outward stocks below 100 million USD. The averages are from the author with current year 2000.

Source: OECD (2004)

Figure 3. Inward Stock FDI in the Food Sector

Averages 1990-2000



NB: Data for every year is available for France, Germany, Iceland, Italy, Mexico, Netherlands, Norway, United Kingdom and United States. Iceland had average FDI inward stocks below 10 million USD. Korea only reports data for 2000 and 2001 so their average is for those two years. The averages are from the author with current year 2000.

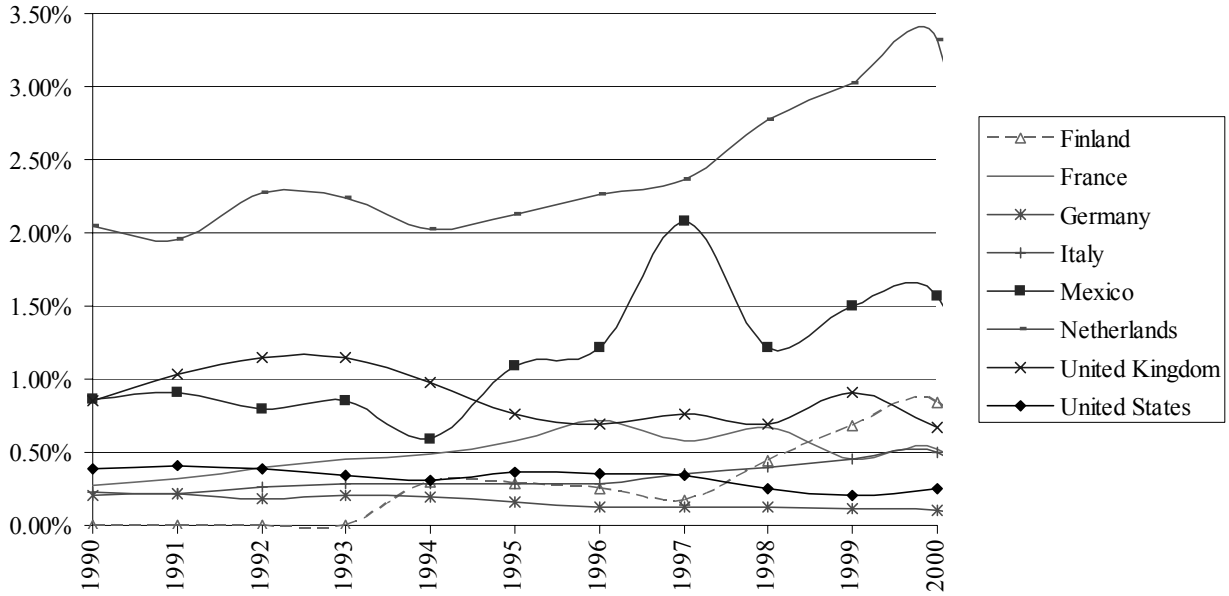
Source: OECD (2004)

12. For FDI in the food sector, the overall distribution of different groups of countries is difficult to calculate because of data limitations. However, data relating to the United States provide some indication of this distribution. In 2003, the United States had total FDI outward stock of USD 22 717 million, of which USD 19 152 million or 84% was invested in OECD countries and USD 3 564 million or 16% in non-OECD countries (BEA, 2002).[8]

13. The stock of FDI as a per cent of the GDP of host countries reveals the relative importance of the FDI (see Figures 4). The most striking percentages during the decade of the 1990s are for the Netherlands. The inward FDI stock was equivalent to 2.0% to 3.5% of GDP with only a few periods of decline. The United Kingdom had an inward FDI stock that was equivalent to 0.75% to 1.25% of GDP. Also notable are Finland, France, Iceland and Mexico. Each had inward FDI stock that was equivalent to at least 0.5% of GDP during the 1990s.

8. Country categories used here are similar to those referred to earlier. Note for both developed and developing countries, there are negative values for some individual countries. The results here are net results.

Figure 4. Inward Stock FDI for the Food Sector as a Percentage of GDP



The averages are from the author with current year 2000.

Source: OECD (2004)

14. In absolute terms, most OECD countries increased their stocks as host or home countries of FDI during the 1990s. Korea is a relatively small home country of FDI outward stocks, averaging USD 242.50 million during the 1990s. Relative to the base year 1990, the outward stock of Korea was six times greater in the year 2000. Similarly, Italy increased its outward stock by almost six times between 1990 and 1999 (see Annex 2). The FDI outward stock of Denmark grew from USD 679.97 million in 1991 to 5 USD 632.43 million in 2000 (8.3 times greater). However, Finland experienced a reduction in FDI outward stock.

15. Results have been similar for inward stocks. Over the 1990s, Germany experienced a diminution of its inward stock of almost 30%. Mexico, however, experienced a great deal of growth, with substantial rises and falls, resulting in an inward stock 21 times greater than the base year.

16. Countries of note with respect to inward stocks include Austria, which grew from USD 114.30 million in 1990 to USD 615.67 million in 2000 (5.4 times greater). Poland in 1994 had inward stocks of USD 519 million and grew 5.5 times greater to USD 2 873.4 million in 2000. The greatest increase of FDI was in Iceland, whose inward stock grew 59.6 times by 2001, from USD 0.44 million to USD 26.16 million.

17. A firm-level perspective of FDI in the sector reveals that the top firms are the home corporations for a substantial portion of FDI (see Table 1).[9] The data in Table 1 indicate that many transnational firms in the sector are substantially invested abroad. For example Danone has 75.46% of its assets aboard while Diageo has 85.81% of its sales abroad.

Table 1. Top Corporations Involved in FDI in the Food Sector

Ranked by Assets in 2001

Rank in 2001 by Foreign Assets Amongst Top Corporations	Corporation	Home	Assets (million USD)		Sales (million USD)	
			Foreign	Total	Foreign	Total
21	Nestlé SA	Switzerland	33 065	55 821	34 704	50 717
25	Unilever	UK/Netherlands	30 529	46 922	28 675	46 803
47	Diageo Plc	UK	19 731	26 260	13 747	16 020
49	Philip Morris Co. Inc.	US	19 339	84 968	33 944	89 924
59	Coca-Cola Co.	US	17 058	22 417	12 566	20 092
86	Danone Groupe SA	France	11 429	15 146	9 950	12 972
92	British American Tobacco Plc	UK	10 355	16 403	11 613	17 352

Source: UNCTAD (2003)

18. The ratio of foreign affiliate sales relative to exports and imports on a national level reflects sales produced through FDI relative to international trade. Available data on foreign affiliate sales is limited to the home countries of Germany, Italy, Japan and the United States.[10] The foreign affiliates abroad of the United States- and Italian-based parent corporations sold 3.21 and 1.34 times as much as was exported by the parent corporations (see Figure 5). In contrast, foreign affiliate sales for German-based parent corporations were less than 22% of exports.

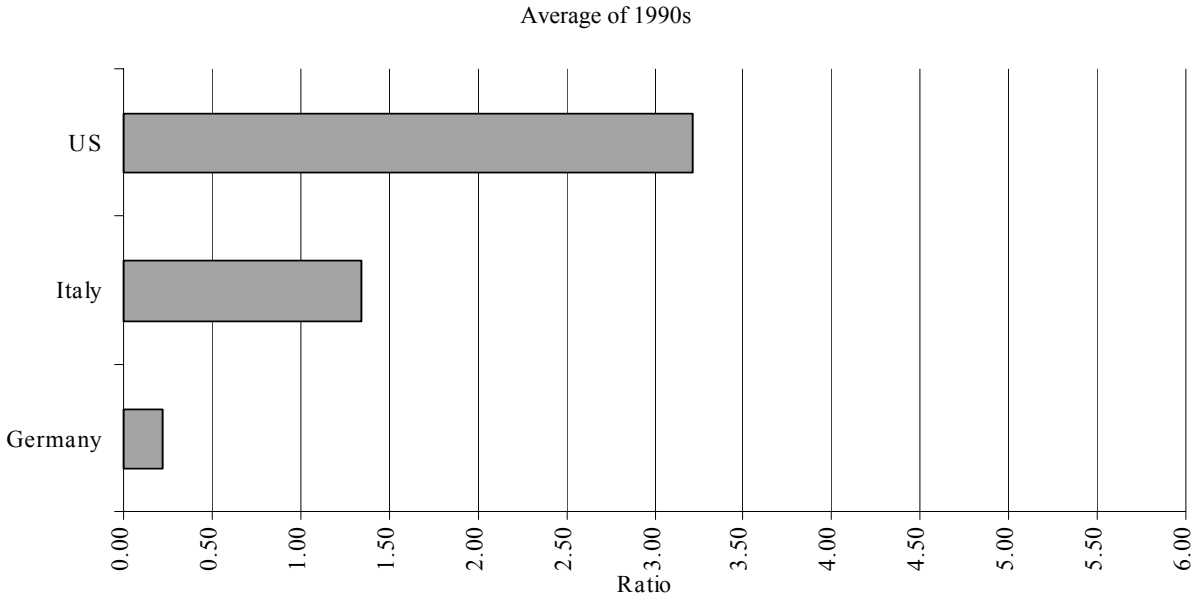
19. In terms of imports, the ratio of foreign affiliate sales relative to imports in the same country is greater than one for ten out for the 15 reporting OECD countries.[11] Hungary and Poland consumed 5.52 and 3.30 times more products from foreign affiliate sales than imports in the food sector (see Figure 6). Only Italy, Germany, Mexico, Finland and Portugal consumed more imports than production from foreign affiliates. These data suggest that FDI may in some cases substitute for trade. However this result could be the result of trade and sale of intermediate products.

9 . All data are based on the annual reports of firms. If a firm does not release its annual report, the firm may not be included in this list.

10 . Foreign affiliate sales from a country reflect sales in another country by an affiliate whose parent corporation is in the home country. For example, the foreign affiliate sales from a country for Germany are the sales of an affiliate in Italy and all other host countries. Japan was excluded because the sales data included "growing of cereals" and "growing of vegetables." The US data underestimate the actual foreign affiliate sales for the food sector because tobacco products were excluded.

11 . Foreign affiliate sales in a country reflect the sales of an affiliate, whose parent corporation is based in another country. For example, the sales of an affiliate of an Italian-based parent in Germany (and all other foreign affiliates) are the foreign affiliate sales in a country for Germany.

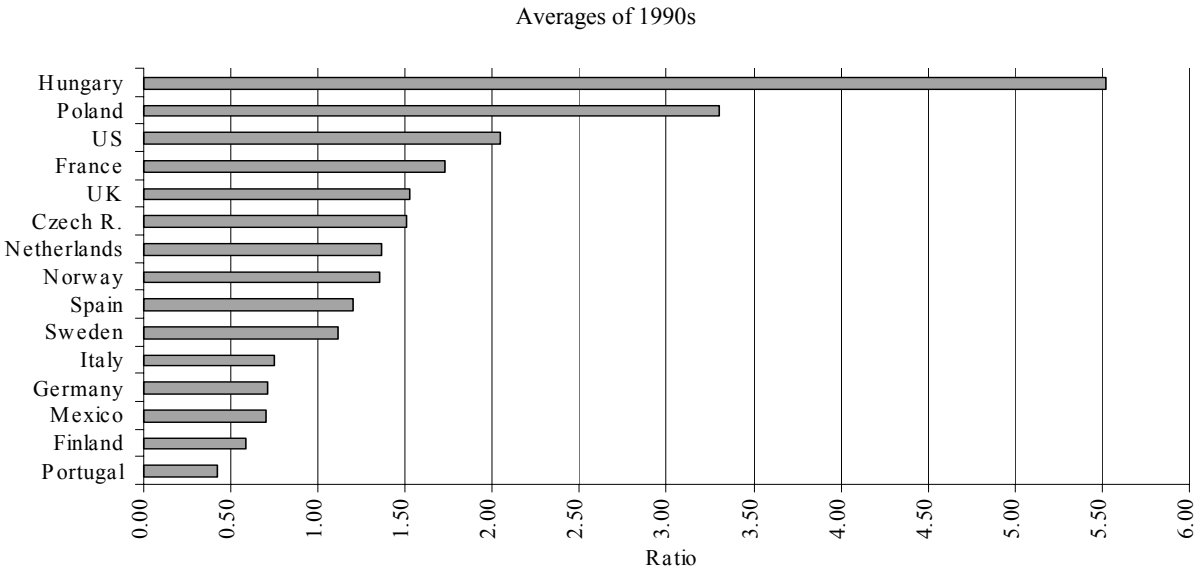
Figure 5. Foreign Affiliate Sales Relative to Exports



The averages are from the author. The averages are over the years of available data.

Source: OECD (2004)

Figure 6. Host Country Foreign Affiliate Sales Relative to Imports



The averages are from the author. The averages are over the years of available data.

Source : OECD (2004)

20. However, another explanation is also possible. During this period there has been growth in both exports and imports (see Annex 2). One assessment of trade and FDI data is that while foreign affiliate

sales relative to imports and exports are greater than one, international trade has still increased for most countries. However in others cases, FDI and trade may actually complement, and not replace, one another.

21. Related to the issue of substitution versus complementarity between FDI and trade is the effect of trade policy. Is the relationship between FDI and trade influenced by trade policies, and if so, how and to what extent? Additionally, further analysis will be useful because trade in the food sector is frequently discussed among governments and with civil society. Therefore, better understanding of this sector, its FDI and trade is of great importance.

22. Often the notion of FDI and trade as complements or substitutes is presented in simplistic terms. Describing the notion as if the ideas were diametrically opposed may be misleading if not simply wrong. A firm could treat investments in different product lines as if some investments were complements and others were substitutes. By the same token, firms, in the same country, could have firm-wide consistent investment policies but across the country, the different firms could have different investment strategies. Therefore, the notion of complement versus substitute investment does not reflect the continuum of investment strategies that firms can choose. Despite these complexities, statements about the relationship of FDI and trade in aggregate can still be made. These statements tell the general tendency of FDI and trade, which may be useful for policy discussions.

Literature Review

23. The literature on FDI has attempted to address many of the concerns discussed above. In particular, the literature has dealt with the issue of whether FDI serves as a substitute for trade or a complement to trade. This issue is often described in the context of trade policy; that is, do home countries invest in other countries to avoid trade barriers in host countries? This question is an important one because the economic and trade effects will be different. If FDI is a substitute for trade, then FDI represents a diversion away from local production and exports to foreign production and affiliate sales. Conversely, if FDI and trade are complements, then local production benefits from investments aboard. An extension of the complement versus substitute discussion is do firms invest in other countries to outsource different levels of production (vertical investment); do firms produce the same product in multiple countries (horizontal investment) or do firms locate FDI for other reasons? Another consideration is if trade barriers encourage FDI, then these barriers are a source of efficiency loss because capital used for FDI is diverted from other productive uses to avoid tariff barriers (or "jump tariffs"). These possibilities are stylised, but they illustrate the concerns covered in the literature and the policy questions that arise from these concerns.

24. To give a full review of this large literature is beyond the scope of this paper. A discussion of a narrow group of papers will help sharpen the focus on the questions raised in the current project.

Industrial or Manufacturing Perspective

25. We divide this literature into three categories based on the questions the research tries to address: Are trade and FDI substitutes or complements? Is the location of FDI based on a horizontal, vertical or proximity-concentration theory? How do trade and trade-related policies affect trade and investment?

Complements verses Substitutes

26. OECD (1997) uses a gravity model of trade to test the effects of FDI on trade flows for France, Sweden and the United States.[12] Overall, the results suggest that FDI is a complement to trade, with

12 . The data set of bilateral FDI flows, FDI stock and trade for 1984-1995 was constructed with the assistance of the governments of the countries and Eurostat. OECD data complement the data set.

differential effects among countries and type of FDI. In particular outward FDI generates trade surpluses, and inward FDI creates trade deficits. The complementary is potentially the result of the spillover effects between industries. OECD (1998) updates OECD (1997) with a more advanced statistical model and adds the United Kingdom. Similar results are observed in the updated version: FDI (outward and inward flows) is complementary with exports and imports. However, outward FDI does not generate the trade surpluses as in OECD (1997). In a synthesis of the OECD 1997 and OECD 1998, Fontagné (1999) reports that, for 15 OECD countries, USD 1 outward FDI flow generates about USD 1.70 bilateral trade surplus; however, the opposite is true for inward FDI flows. Additionally OECD (1997) and Fontagné (1999) report, using causality testing, that before the mid-1980s trade caused investment. The direction of the causality reversed after the mid-1980s.

27. By using product-level data, Blonigen (2001) is able disentangle the substitution and complementarity effects of Japanese exports and foreign affiliate sales in the US for automobile parts and consumer products. In a review of the literature, the author points out that much of the theoretical literature is split over the substitution and complementarity effects, but the empirical literature leans toward the complementarity effect. Researchers have found it difficult to find the substitution effects because the level of aggregation in the data is too great. With his disaggregated data, the author provides evidence of a substitution effect and the substitution occurs over a short period of time. First he looks at the automobile industry. He shows empirically the theoretical complementary of automobile parts exports and automobiles produced by foreign affiliate and the substitution between automobile exports and foreign affiliate production. Using only consumer product data, he shows the substitution effect between exports and foreign affiliate production.

28. Chakrabarti (2003) states that the FDI literature is "a diverse and somewhat unwieldy literature where most investigators have considered only a small number of explanatory variables at a time in an attempt to establish a statistically significant relationship between inbound FDI and a particular variable or a set of variables of interest. The absence of a consensus on a theoretical framework to guide empirical work on FDI is rather conspicuous." (Chakrabarti, 2003, p. 151) Therefore, the author developed a theoretical model to help direct an empirical model. He recommends that an FDI model should include the following factors: own wage, own tariff, own political stability, rival market size, rival market wage, rival tariff, rival political stability, exchange rate and transport cost.

Horizontal, Vertical and Other Theories of FDI Location

29. Markusen and Maskus (2002) identify three models of FDI: the horizontal theory, the vertical theory and the knowledge-capital theory. The vertical theory asserts that firms produce parts of products in geographic diverse locations to capture the benefits of factor intensities, while the horizontal theory asserts that firms produce the same products in different locations. The knowledge-capital theory asserts the firms may build multiple plants or geographically separate headquarters and a single plant because knowledge is mobile and is an input in multiple production facilities. The authors conduct a "horse race" among three models for FDI to see which perform the best using aggregate data. Their results suggest that the horizontal model cannot be distinguished from the knowledge-capital model and the vertical model is rejected for aggregate multinational activity. Much of the FDI literature assumes (either explicitly or implicitly) one of these models.

30. Barrell and Pain (1996) investigate the effects of demand, relative factor prices and exchange rate expectations on the level of FDI in the US They begin with a firm that maximizes its net worth by maximising the current discounted value of profits. The firm can produce goods at home and abroad through a foreign affiliate; in this case, the firm has a domestic and foreign cost function. The authors recognise that exports may stimulate foreign direct investment in downstream services. In this light, the effects of barriers to trade may encourage FDI, but the authors argue that year to year changes of such

policies are small and not necessary to include in their model. The authors find that the level and change in GNP increase FDI. Relative labour costs (US to another country) increase FDI outward investment in the long run. A similar result is found with capital costs. Additionally, expected, short-term appreciation of the exchange rate postpones investment. Contemporaneous exchange rates appreciations increase FDI, while past exchange rate changes place a drag on FDI.

31. In contrast to the work of Barrell and Pain (1996) and other relative factor cost work, Brainard (1996) explores the proximity-concentration hypothesis.[13] The hypothesis predicts that firms are more likely to expand production horizontally across borders when transport costs and trade barriers are relatively high and when investment barriers and the scale economies at the plant level are relatively low. The proximity-concentration hypothesis and the prevailing factor-cost hypothesis are not mutually exclusive. A firm chooses to invest depending on the relative importance of the two choices. Using a gravity model framework and US data, Brainard (1996) provides evidence that affiliate share of total sales is increasing inline with trade barriers, transportation costs and corporate scale economies but decreasing in investment barriers and production scale economies. Affiliate share of total sales increases also with shared language, increased risk and adjacency of countries. Brainard (1996) suggests that the proximity-concentration hypothesis, relative to the factor-costs hypothesis, helps explain the reason a country tends to invest in countries that are more similar to it. Although these hypotheses are compatible, the evidence in support of the proximity-concentration hypothesis provides an explanation for the distributional differences between FDI among developed and developing countries.

32. Helpman, Melitz and Yeaple (2003) extend the proximity-concentration trade-off literature by introducing intra-industry heterogeneity. Previously the literature had considered only the representative firm in general equilibrium models, the result had been that the representative firm either is involved in FDI or not. Extending the approach to consider intra-industry heterogeneity permits a number of additional results that help explain the involvement of firms in trade and FDI. The models show that the most productive firms are involved in foreign activities, and of those firms, the most productive are involved in FDI. The extent of intra-industry heterogeneity is a determining factor in the volume of FDI relative to volume of exports. So for example, the larger markets disproportionately serve as the home market for many firms while small markets are disproportionately served by foreign affiliate sales and exports from other countries. The intra-industry heterogeneity also suggests that the more diverse the productivity levels across firms the larger the FDI sales to exports. An empirical analysis of US based firms in 38 countries and 52 industries confirms the role of firm heterogeneity and relative FDI sales to exports.

33. Tadesse and Ryan (2004) argue that the traditional FDI literature generally states that FDI is categorised as either horizontal, investments to produce final goods in another market, or vertical, investments in another market to produce intermediate goods for an another production process. They continue by arguing that mature markets, those with "institutions and policies [that] provide foreign firms a market environment characterized by the presence of voluntary exchange, competition, and secure private property rights," host horizontal FDI while less mature markets host vertical FDI (Tadesse and Ryan, 2004, p. 200). The authors counter this argument because of the increased fragmentation of the production process where final product may not go to the home or host country. The potential of the host market to

13 . Brainard hypothesizes that there are three possible equilibriums: 1) a pure multinational equilibrium, where there is no trade but all multinationals with foreign affiliates that supply the foreign market; 2) a pure trade equilibrium, where all firms have a single plant at home and export products abroad; and 3) a mixed equilibrium of multinationals with foreign affiliate sales and exports. Nations move from pure a multinational to a mixed to a pure trade equilibriums based on lower transportation costs and trade barriers and higher investment barriers and size of scale economies at the plant level compared to the corporate level.

serve as a platform into other markets may override the negative features of a less mature market. The authors then find empirical evidence, from Japanese outward FDI around the world, that market maturity and host country inflows are positively related, but market maturity lowers the FDI-trade complementarity. While typical FDI factors matter, the potential that the host may serve as an export platform is an equally important factor in attracting FDI.

The Effects of Trade and Regulatory Policies on FDI

34. Nicoletti, *et al*. (2003) provides evidence that border openness to trade and investment and competition-oriented domestic policies can increase OECD trade and FDI. For the analysis, the authors use a series of gravity model equations of aggregate FDI, trade (in products and services) and policies (domestic and border). To represent the various policy variables, the authors create, using OECD data, variables to represent product market regulations, labour market arrangements and infrastructure (telecommunication and electricity). The results of the models suggest that the removal of tariffs and non-tariff barriers could increase the export of goods. Based on simulations from the models, liberalising FDI restrictions to the most liberal OECD country could increase OECD-wide inward FDI stocks. Other simulations suggest that product market regulations (including intellectual property rights protection) alignment to the most liberal of OECD countries could increase inward FDI stock and within-OECD exports. Similar deregulation could increase the volume of within-OECD exports. Aligning labour tax wedges to the most liberal of OECD countries could increase within-OECD exports. Additionally improving infrastructure to the best-endowed OECD country would increase within-OECD trade in services.

35. Barrell and Pain (1999) are interested in how the replacement of tariffs by quotas and anti-dumping cases affected investment decisions in OECD countries by Japan in the 1980s. The authors argue that the location and amount of FDI depend on several factors, such as relative factor costs, market size and non-tariff barriers. The authors hypothesize that Japan invested in the EC and US in the 1980s to avoid non-tariff barriers, in particular, anti-dumping actions (successful and unsuccessful actions). On the aggregate and manufacturing firm levels, the authors provide evidence that the number of anti-dumping cases, relative labour costs and level of export penetration influence the decision to invest in a location.

36. Dee and Gali (2003) use a gravity model to look at the effect of preferential trade agreements (PTAs), especially "new age" agreements, on trade and investment. New age agreements consider other non-trade issues such as investment, services, competition policies, etc. The study provides evidence to suggest many of the PTA caused trade diversion, especially the more liberal PTAs such as EU, NAFTA and MERCOSUR. These PTAs failed to generate greater trade among its members. The authors suggest that the reason for the poor results of the PTAs is because of additional provisions of the agreements hampered trade such as rules of origin. However, some of the other non-trade provisions of PTAs might have boosted investment flows. The increased investment is the result of non-members of the PTA investing in the members of the PTA.

37. In a theoretical paper, Raff (2004) looks at the effects of preferential trade agreements the on location of FDI, taking into consideration the influence of tax competition amongst countries. Free trade agreements may lead to FDI creation but does not lead to FDI destruction. The creation of FDI is a Pareto improvement regardless of the tax competition. In the case where a host invests in two countries involved in a free trade agreement, the integration will lead to a consolidation of the FDI, and tax competition will lower tax rates in the two countries.

38. Breuss, Egger and Pfafermayr (2001) use a gravity model to investigate the effect of Agenda 2000 structural expenditures on real stocks of FDI to EU countries. Overall the structural funds positively affect FDI outward stocks. From the estimated parameters, the authors simulate the effect of the proposed

reductions of the funds on EU members. The reduction in the funds on long-term, real FDI stocks is between 6.6% and 15.9%.

Food Sector

39. Most of the literature covers the industrial and manufacturing sectors, thus, giving a broad view of the issues of FDI. The research on FDI in the food sector attempts to address many of the same questions that the research on industrial and manufacture products attempts to answer. This subset of the literature however is more focused on the substitute and complement relationship. Interspersed throughout this literature are the questions of what are the effects of regulations and support to agriculture on FDI location. Since the present study is focused on the food sector, a review of the literature and FDI in the food sector is useful. Like the studies discussed below, the current research attempts to address many of the same issues.

40. In their study of FDI in the food industry of the Western Hemisphere, Bolling, Neff and Handy (1998) argue that liberalisation of FDI rules plays a role in the growth of investment. The growth of outward investment generates concerns that outward FDI moves production abroad and substitutes for domestic production and exports. However, Bolling, Neff and Handy (1998) suggest that for the US, some data show that the food exports and FDI increase together and are often complementary. Additionally, income and population growth supports the increase in demand for FDI and exports.

41. Vaughan *et al*. (1994) interviewed seventeen agro-food multinationals based in Canada, Switzerland, the United Kingdom and the US. The interviews reveal the different factors that influenced the location of production, the mode of entry into another market and the role of governmental policies on the strategies of firms. The most common reason for entry into another market was the slow growth of domestic markets to meet the growth objectives of the firms. The authors note several factors that influence production location decisions: the need to customise products for local interests, economies of scale, delivery costs, input issues and risk. The firms interviewed intimated a desire to own productive activities abroad. The process of obtaining this ownership is through a progressive approach: first exports, then licences and joint ventures and finally ownership. In terms of the role of government policy on these location and production decisions, the authors state "Government policy can also affect production location decisions, but for most of the firms interviewed it apparently is not often a primary factor." (Vaughan, *et al*., 1994, p. 5) Despite the lack of primacy, government policies such as non-tariff barriers, level of domestic support and trade did appear to have some influence.

42. In a review of different studies and reports Handy and Bamford (2000) lay out several factors that may influence FDI such as size of host market, growth potential of host market, regulatory regime, cost of labour and other factors. The authors contrast this list with another and argue that tax rates and investment incentives may not matter much in attracting FDI. The authors then discuss a study conducted by Deloitte and Touche on the factors that affect FDI in Canadian agriculture. The Deloitte and Touche study points to similar factors, most notably: market size, level of government intervention, taxes, environmental policies, wages, etc.

43. Gopinath, Pick and Vasavada (1999) explore the relationship between foreign affiliate sales by and exports from the US food processing industry. Based on a model of a profit maximising firm that produces at home for export and abroad through foreign affiliates, the authors find that foreign affiliate sales are substitutes for exports. The measure for agricultural protection Producer Support Estimate (PSE) in the host country increases foreign affiliate sales and lowers exports. Exchange rate appreciations lead to a fall in foreign affiliate sales. Foreign employment is negatively affected by per capita GNP and US interest rates, a measure of the opportunity cost of capital in the US outward FDI is positively influenced by per capital GNP and foreign affiliate sales but negatively influenced by the exchange rate.

44. Marchant, Saghaian, and Vicker (1999) investigate the relationship between US outward FDI stock to China and exports from the US to China of processed foods. The model is a test of the effects of exchange rate, GDP, export price and FDI on exports and the effects of exchange rate, GDP, US interest rate and exports on FDI. The model indicates that FDI and exports are complements. The GDP and exchange rate variable are not statistically significant, but the US interest rate appears to affect FDI.

An Assessment of the Literature

45. The overall literature has a number of common threads: the size of the market is positively correlated with FDI. Barriers to trade such as trade policies or travel costs may encourage FDI. The literature is divided on the issue of the role of relative factor costs. Most of the papers reviewed here support the relative factor costs hypothesis, but Brainard (1996) and Helpman, Melitz and Yeaple (2003) have evidence to support the proximity-concentration hypothesis. The literature is also divided over the issue of whether FDI and trade are complements or substitutes. Also the literature has differing views of the effect of policy variables on FDI.

46. It is important to note that this literature has a potential bias: many of the papers only use data of a single country. It is desirable to overcome this shortcoming and to shed additional light on the interplay between FDI, trade and trade policies, e.g. by considering a cross-section (or panel) of the FDI to and from countries (see Fontagné (1999), Nicoletti, *et al.*, (2003), OECD (1997), and OECD (1998)). Another contribution to fuller analysis can come from focusing on a particular sector, to disentangle the industry-wide effects which may obscure issues and patterns in individual sectors.

Hypotheses/Questions

47. From the literature some questions can be posed relating to trade and FDI in the food sector: 1) Across countries what is the relationship between investments and trade in the food sector? 2) What factors influence trade and FDI? In particular how do trade policies and market conditions affect trade and FDI?

48. This research provides evidence to address these questions. In particular, the present research provides evidence that trade policies and market conditions influence FDI and FDI influences trade flows. This suggests that policy makers may need to give broader consideration to the direct and indirect effects that trade-related policies, such as support to agriculture and tariffs, can have on trade and investment. We explore theses hypotheses and questions through the gravity model.

Box 2. The Gravity Model

The gravity model, which is analogous to Newton's equation of gravity, explains the factors that affect trade flows, foreign direct investment or other transactions: the incomes (economic masses) of the partners and the distance between these partners (economic distance). These models typically include dummy variables of other factors that may influence trade flows such as membership in a RTA, common language, etc. In such models the dummy variable(s) for the RTA explain how membership (or non-membership) in the RTA affected past trade flows.

New Empirical Models

49. An important way to begin to understand the relationship between FDI and exports is to ask the firms. From readily available sources,[14] two main (and often interrelated) motivations emerged for the

14 . The Secretariat is appreciative of the support from the Canadian Delegation of sharing their research on FDI in the food sector in particular through Ms Odette Vaughan of Agriculture and Agri-Food Canada.

location and distribution of FDI: to increase market share and to reduce costs. The interests of firms in market share has to do, in part, with a desire to capture new market share in emerging markets like those in Central and Eastern Europe during the 1990s (Jansik, 2004). Interest in emerging markets is also promoted by the slow growth in the mature food industry in most OECD countries. For this analysis market share is defined as the share of local production to total food consumption (total production plus imports less total exports). Therefore, we hypothesise that the more the market is saturated by local production, the greater the amount of FDI the country will send aboard. Another perspective on market share is that if a potential host market is also saturated by its own local production, this market may be less attractive for investment.

50. The other main motivation for firms investing abroad is to increase efficiency. Efficiency-seeking FDI provides a base for supplying a host country as well as worldwide markets (i.e., through exports). A host country can become more attractive when it is involved in free trade agreements (FTAs) that effectively enlarge its market, a notion close to the idea of gaining market share. The idea of an enlarged market comes from the possibility that an investor in a home country may invest in a host country that is a member of a FTA to exploit the preferential tariffs that the host has with other counties.[15] We hypothesise that membership in a FTA positively influences FDI and trade.

51. Increased efficiency is most frequently considered in the context of reduced costs, firms invest abroad to gain from cost differences or to take advantage of economies of scale or scope (OECD, 2004b). Such FDI is a means for expansion of supply opportunities (supplying products less expensively), while expansion by seeking increased market share is a response to demand-side opportunities. We hypothesise that factor costs are negatively related to inward investment and exports and positively related to outward investment and imports.

52. FDI is also influenced by costs arising from trade-related policies. Researchers and individuals involved in the industry have suggested that trade-related policies are not generally a direct cause for the location and distribution of FDI (West and Vaughan (1995); and Vaughan, *et al.* (1994)). Rather, they may indirectly affect location and distribution through the increased cost that these policies may have on inputs in the country of production. Such trade-related policies include tariffs, NTBs and domestic support classified as market price support (MPS). The MPS reflects the additional costs of primary agricultural inputs into the food industry. We hypothesise that tariffs are positively related to investment and negatively related to trade. The MPS (and relative MPS for bilateral trade partners) is positively related to outward investment and imports and negatively related to inward investment and exports.

53. Throughout the literature, a theoretical notion related to empirical specification surfaces: trade and FDI are related. The empirical specification necessary to deal with this is to recognise that there exists the possibility that FDI and trade flows are endogenous. This endogenous relationship suggests a relationship of substitutes or complements. This relationship must be tested and considered in the modelling of FDI and trade. Given the nature of the trade data, another empirical specification that is appropriate to consider is whether there exists a pattern among the activities of a single country to the others, such a pattern suggests that the data are to be handled in a particular fashion, panel versus pooled. If a pattern does exist, is the pattern fixed or random? That is, should the models be specified as a random or fixed effects model? More of these details are available in Annex 3.

15 . Bolling and Somwaru state "U.S. Companies see FDI as an opportunity to expand their markets beyond the continental United States, and liberalized investment rules that are often included in regional trade agreements allow food companies to expand their markets." (Bolling and Somwaru, 2001 p. 24)

Model Results

54. The trade and investment models used in this study are based on the traditional gravity models. Beginning with the variables that are found in many studies of FDI and trade, we see that the model results are as expected, the GDPs of the home and host country are positive and statistically significant. The FDI equations have only the GDP of the relevant country, and these equations do not have the distance variable. The reason for these and other omissions is that the FDI variable does not represent bilateral investment like the dependent variables on trade. The FDI data are of total outward investment from or inward investment into the world not just OECD countries. Therefore, bilateral relationships are not relevant (see the appendix for further details). The cost of production variable, wage is not statistically significant in most of the model specifications, except for one of the import regressions.[16] One reason for the insignificance of this variable is compared to advertising and other capital costs, labour costs are small for process food, tobacco and beverage products. The distance variable, a proxy for transportation costs, is negative and significant.

55. In light of the hypotheses, the models are constructed to provide evidence of an existence of a relationship between FDI, trade, and trade policies. From the analysis, evidence exists to suggest that FDI and trade flows are related. In terms of outward investment the relationship does not appear strongly because of the weak statistical significance of the endogenous variables, ln(*Exports*). The tests, which are not reported, indicate a strongly, statistically significant endogenous relationship. Therefore, a relationship exists but the relationship is weak and the opposite of what was hypothesised. In terms of inward investment, the relationship was stronger and positive, suggesting that inward investment is positively influenced by imports. One of the import regressions shows a strong positive relationship also. The implication of this result is that policies that increase trade may also increase FDI and vice versa.[17]

56. The competitiveness of a market is measured by market share, which is the ratio of domestic production to domestic consumption (production less exports plus imports).[18] Market share, which is endogenous, has a positive effect on outward investment and exports. The larger domestic production is to domestic consumption the greater the tendency to invest abroad and export. This result is consistent with the idea that a firm in a highly competitive market will look for other markets to invest to find new market share in other countries. Because of statistical problems with the market share variable in the inward and import equation, market share was omitted from the equations.

57. The trade and trade-related policy variables provide evidence that trade policy has an influence on FDI and trade. Each model has the applied or the bound tariff rate for food products in the receiving country. For the export and outward investment models the tariff rate is the one that the exporter/host country would face in the recipient market. For the import and inward investment models, the tariff (bound or applied) rate is the tariff applied by the recipient country. The tariff rate variable is not statistically significant in the outward investment models; however, in one of the export models the bound tariff rate had a negative effect on exports, which was hypothesised. The positive sign on the tariff rate for the inward investment models are significant and as hypothesised. These results suggest that inward

16 . In earlier specifications, interest rates were included. This variable is seen in some of the literature; however, upon further reflection, the exclusion of the interest rate may be appropriate. Because investment may be funded from any number of locations, the interest rate of the home or host country may tell us little of the true cost of capital.

17 . Care needs to be taken when reviewing these results. The data sets for the inward and outward FDI are different because all countries did not report both. For example Mexico reports only FDI for inward investment and not outward. Therefore differential effects are possible.

18 . The import and export data in market share represent total trade to and from the world; therefore, they are different than the dependent variables which represent bilateral trade flows among OECD countries.

investments are used, in part, to "jump tariffs." The negative, statistically significant sign of the tariff for imports is as expected.

58. In addition to tariffs, MPS, which raises the price of domestic inputs, has an effect on FDI in the food sector. The models include MPS for the home and host country and the ratio of the MPS for the home to host country. For inward investment, the MPS is negative and significant suggesting that high MPS discourages investments. The import model has a positive and significant value for the relative MPS variable. This result indicates that large domestic support at home relative to the domestic support of the exporting country increases imports of food products. Like the tariff case, firms may "jump" domestic support through FDI. The relative MPS for exports is not statistically significant.

59. Lastly, membership in a customs union or free trade agreement has an effect on trade and investment. Membership in either the EU or NAFTA should increase investment and trade flows, and not being a member should hurt investment and trade flows. For all of the regressions, the dummy variables for non-membership in the EU and NAFTA are negative and statistically significant, which is consistent with the hypothesis. This result is consistent with the idea that an investor in a home country invests in a host country with preferential tariffs in a third country to exploit the preferential tariffs. The host country serves as a platform to export products into other countries. A host country that is a member of a free trade agreement is attractive for receiving investments.

Summary

60. OECD countries serve as hosts and homes to much of the FDI in the world. Many empirical studies only look at the outward investment. In this study, we review both outward and inward FDI to give a fuller picture of the trade and investment relationship. While the results of these models are based on analysis of OECD countries, some recommendations in the research findings may also be applicable broadly. Investment requires healthy, functioning markets. Low costs of production can also attract FDI; however, the inputs need to be of good value not just inexpensive. This point is particularly true if border measures reduce the efficiency of domestic inputs or slow the imports of needed inputs. Additionally, measures that reduce the distance between countries can increase trade flows which increase inward investment. The distance between countries can be reduced through trade facilitation. Improved regional cooperation and trade agreements may improve inward investment as suggested by the results of EU and NAFTA. With greater consideration of the effect of different policies on investment a more efficient flow of capital is possible.

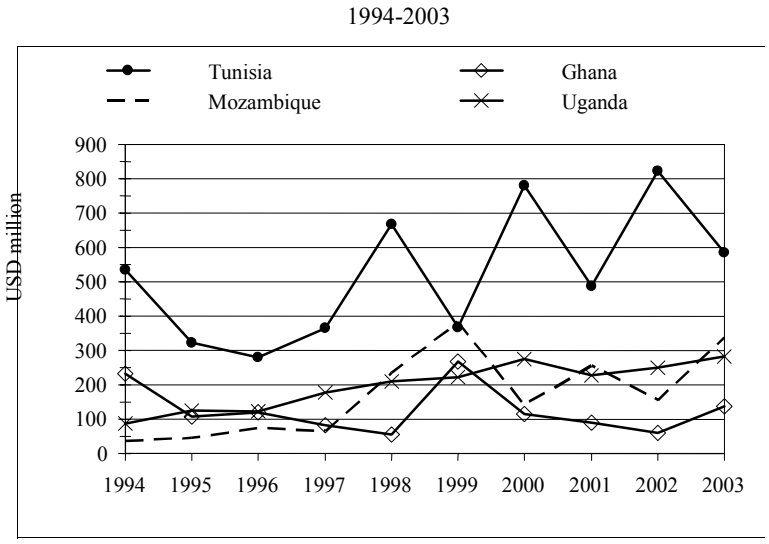
61. Amongst OECD countries, a complementary relationship between FDI and trade seems to exist. However, the underlying basis of this complementarity is not clear from the models used here. Given the data, a reasonable assumption is that FDI and trade flows are reciprocated amongst OECD countries because most FDI is exchanged amongst OECD countries. The reciprocity does not hold when considering FDI and trade in Africa. As the cases that follow reveal, FDI, in its various forms, from OECD countries to African countries may be one of the mechanisms or channels by which African countries export food products to OECD countries. By considering FDI and trade between OECD and African countries provides a different perspective that will shed light on a better understanding of the relationship between FDI and trade.

III. CASE STUDIES OF FDI IN FOUR AFRICAN COUNTRIES

Introduction

62. The introduction to this paper presents the state of FDI stocks around the world. For 2003, the estimated share of FDI inward stock that Africa possess is only 2%. If for no other reason than the small share of FDI hosted by Africa, research on the FDI on the African continent is of interest. Why has Africa hosted so little of the world's FDI? The FDI that Africa has received has been erratic (see Figure 7). What can be done to improve this situation especially given the development aspect of FDI? The complete answers to these questions are beyond the scope of this paper; however, the following case studies of FDI in the food sector in four African countries provides us some ideas of how some firms have been successful with FDI.

Figure 7. Foreign Direct Invest Inflows for Selected Countries



Source: UNCTAD

63. Broadly, this research is to understand better the effects of trade and trade-related policies on FDI in the food sector. As suggested in the statistical analysis of OECD countries, such policies can have an effect on the FDI amongst OECD countries. Domestic support and membership in regional trade agreements or customs unions can have an influential affect on FDI, at least in OECD countries. The four case studies make the point that FDI may be affected by trade-related policies, such as standards and food safety regulations and the interaction of such policies with private standards. It may also be affected by opportunities for preferential market access, as accorded through regional or bilateral trade agreements or non-reciprocal preferential arrangements. While trade policies may matter, factors such as political stability, the business environment, physical infrastructure, institutional knowledge and social capital may matter more. The risk and political stability of countries in Africa may matter more than trade policies in influencing the host of FDI.

64. The case studies review four African countries. We considered the African continent because of the limited FDI that goes to Africa. The continent also reflects two different socio-economic regions: Middle East and North Africa (MENA) and Sub-Sahara Africa (SSA). We chose Ghana, Mozambique, Tunisia and Uganda because they reflect different geographic regions of Africa. They have different historical and linguistic connections with OECD countries, in particular England, France and Portugal. The four countries participate in different preferential trade agreements with OECD countries, in particular the European Union and the US. While other countries could have been chosen, we had contacts in many of these countries thus facilitating the research.

65. In each country, we interviewed government officials, agents with investment promotion agencies and FDI-supported firms, which are active in the agro-food sector. An interesting characteristic of each of the four firms is they are all predominantly involved in exporting food products to mature markets like most OECD countries. This common characteristic was not intended, because from the outset we assumed that a significant goal of FDI in Africa would be to develop the markets in different African countries. The fact that none of the four firms mainly supply the local market is not to suggest the absence of FDI for developing local, emerging markets. However, the result does suggest the prominence of FDI for developing exporting firms in Africa.

Research Findings

66. Interviews in the four countries with investment promotion agencies, officials in government ministries of trade, firms and data analysis, are the basis for the following research findings.

1. FDI has helped African firms comply with regulatory policies that affect international trade such as food safety regulations.

2. Investments in public goods, e.g. roads, sanitation, sea ports, airports, tertiary education in finance and management, are very much needed for FDI to be sustainable. Such investments generally are from the public sector and are a prerequisite for successful private sector investment of both domestic and international origin.

3. Investment promotion agencies (IPA) are common in emerging markets, with the 'one stop shop' concept being rapidly adopted by the IPAs.

4. Export processing zones are becoming the primary focus of IPAs, with the result that investment is concentrated in infrastructure and manufacturing industries.

5. For financiers and investors, there is a bias towards large investment projects, which creates disadvantages for sectors with smaller, productive units.

6. Telecommunications and service industries are out-competing agro-based businesses for FDI, probably because of their profitability and growth potential. Moreover international markets can be a factor.

7. The private sector—within foreign and emerging markets—is moving ahead with investment in processing agricultural commodities. However, the scale is relatively small and does not have the forceful impact on the economy to achieve the wealth creation for poverty reduction goals – through marked increases in employment or significant decreases in food based price.

8. Investment, including FDI is attracted by the prospect of new trade opportunities in emerging markets. For example, North African countries are "bullish" on exporting processed foods to countries in sub-Saharan Africa.

9. Investors may establish joint ventures to benefit from complementarities of knowledge and financial resources.

10. A potentially important trend in FDI is the role that can be played by the movement of natural persons. In particular persons with access to foreign and human capital (experience and contacts) may be particularly effective in fully utilising FDI.

Methodological Issues

67. A challenge to understand FDI in the food sector in Africa is the limited availability of appropriate data. Good data are hard to find in general, and in particular for developing countries and even more difficult for a particular sector. Therefore, the approach taken in this project is to use case studies. The results discovered in the case studies go beyond the results that could have been possible with standard statistical analysis of FDI and trade data. Therefore, the data limitation provides a unique opportunity to look at FDI in a different light.

Review of Factors that Affect FDI

68. Each case study considers three factors that influence FDI in Africa, namely investment and trade agreements and country risk and business ratings. For each case major trade and investment agreements are reviewed to provide a context for the type of liberalisation and the FDI opportunities in each country.

69. Beyond bilateral investment or trade treaties, and broader multilateral trade policies, characteristics of the FDI recipient country's business environment are instrumental to the investment decision.

70. Historically, to gather this information or get a feel for the business climate, or even the country risk, an investor needed to travel to the prospective recipient country because there were few reputable, readily accessible tools to make an assessment from a distance. With the historically hefty transaction cost of information gathering, FDI was limited to companies or individuals with the resources to explore speculative investment. The country risk and business ratings are tools used by foreign investors to help better understand the opportunities and risks in a country. These tools can sway an investor's interest in a potential host. Through technological innovation, public-private partnership, and support from emerging market countries, there are credible, objective tools to compare business environments and country risk across countries, and regions. The International Finance Corporation (IFC) and World Bank conduct surveys for several emerging market countries on key aspects of the business life-cycle, including setting-up business, the operating environment, and closing down a business. The most recent survey results are published in the report *Doing Business in 2005: Removing Obstacles to Growth*. Specifically, *Doing Business* benchmarks regulations in the business areas such as Starting a Business, Hiring and Firing Workers, Registering Property, Getting Credit, Protecting Investors, Enforcing Contracts and Closing a Business.

71. A second, new tool assisting foreign investors in comparing potential investment markets is Standard & Poor's sovereign credit rating. Although the Standard & Poor's sovereign rating has existed for many years, the portfolio of countries covered by these ratings has tended to be OECD member countries. Through a United Nations Development Program (UNDP) initiative to extend sovereign credit ratings to previously unrated economies in Africa, several countries including Ghana, Mozambique and Tunisia have been issued short-term and long-term sovereign ratings. Standard & Poor's ratings are frequently used by financial investors in making business decisions. Including emerging market countries in Standard & Poor's ratings is a significant step in creating market transparency and highlights the

business investment potential as financiers seek to manage the risk of saturated, mature markets in OECD member countries by diversifying their investment portfolio.

72. The Economist Intelligence Unit's (EIU) Country Risk Service complements *Doing Business* and Standard & Poor's credit rating. Specifically, it monitors emerging and highly indebted markets on a continuous basis, producing two-year forecasts for the economic variables that are most important for risk assessment. Variables include current-account balance, financing requirements, foreign reserves, short-term debt, "hot money inflows" and the vulnerability of the banking sector. Together, these independent, transparency-enhancing assessments underpin a key section of the case studies, where each country's economic and business characteristics are discussed with specific attention to the implications for attracting investment (See Table 2).

73. Additionally, each case has a discussion of the state of FDI in the country. In this section, the investment promotion efforts of each country are discussed. Investment promotion agencies (IPA) provide a service to attract FDI into the country. Additionally the State of FDI section also looks at the legal and donor support to attract or improve FDI in each country. While these are not trade policies, the impact of these IPAs and donors along with the legal institutions can have a tremendous affect on the level of FDI in countries. The effect of these policies and institutions are hard to model even if data were readily available; therefore, the case studies provide indications of the influences of these factors on FDI. Like the previous sections of the case studies, the state of FDI in the country is a broad discussion and not specific to the food sector. However these discussions provide a useful context to understand the potential of FDI.

Firm Reviews

74. Each case has a discussion of an agribusiness firm that receives FDI. Three of the four cases reflect FDI in the form of joint ventures (JVs). The other case is an investment through the movement of a natural person. The firm reviews are to provide specific examples of FDI in the agro-food sector. Each review provides a view of how FDI functions in the firms. In particular, the reviews point out some of the challenges in terms of trade and trade-related policies that affect FDI. Many of the assessments of each case are based largely on the information gathered from each firm.

Table 2. Country Risk Rating Score

as of December 2004

	Maximum Score	Ghana	Mozambique	Tunisia	Uganda
Political Stability	10	5	n.a.	5	9
Political Efficacy	12	7	n.a.	6	9
Monetary Policy	6	4	n.a.	1	3
Fiscal Policy	6	3	n.a.	2	4
Exchange Rate Policy	6	3	n.a.	2	1
Trade Policy	6	3	n.a.	3	2
Regulatory Policy	4	2	n.a.	1	2
Global Climate	4	3	n.a.	2	3
Growth/Savings	7	2	n.a.	2	3
Current Account	6	4	n.a.	1	4
Debt Structure	6	2	n.a.	1	3
Financial Structure	4	3	n.a.	2	3
Liquidity	23	14	n.a.	9	7
Total	**100**	**53**	**n.a.**	**38**	**52**

Source: EIU (2005)

A. GHANA

Assessment

75. Ghana's experience in FDI and trade, illuminated through BLUE SKIES, a fresh fruit joint venture in Ghana, highlights the challenge of the demands on investor skills, local and foreign, and on the government to move into integrated, market economies. Political stability, while pivotal to attaining a sovereign credit risk score that is acceptable to local or foreign investors, is only a first step. Rapid, reliable infrastructure development, for road and air, is a must for both export directed FDI and FDI that targets Ghana and neighbouring countries. Investment in infrastructure development is a high priority for government. Collaboration in infrastructure development to link the Greater Accra region with other regions in Economic Community of West African States (ECOWAS) may deliver the broadest return in terms of accessing consumer markets and diversifying the location of FDI that generates the most employment opportunities.

Investment and Trade Agreements

76. Ghana, along with 15 other countries, founded ECOWAS in May 1975.[19] The initial objectives of ECOWAS include economic integration to enhance economic stability and relations between member states. Although there have been several challenges to achieving complete integration, ECOWAS is making strides with aspects of market integration such as, free movement of good and persons, harmonization of some economic and finance policies. Development of physical infrastructures for regional road, telecommunication and energy networks are high on the ECOWAS project list.

77. Beyond ECOWAS, Ghana has signed several bilateral investment treaties (BIT). The BITs serve as a strategic tool for shaping the nation's competitiveness. Between 1989 and 2003, Ghana signed 25 BITs, eight of which have entered into force (Table 3). Of these eight treaties five are with European countries, including the Netherlands and United Kingdom which have historic trading ties with Ghana. Of the others BIT partners, China and Malaysia are newer economic and trade giants.

19 . ECOWAS members are: Benin, Burkina Faso, Cape Verde, Ivory Coast, Gambia, Ghana, Guinea, Guinea-Bissau, Liberia, Mali, Niger, Nigeria, Senegal, Sierra Leone, and Togo.

Table 3. Ghana: Bilateral Investment Treaties

Concluded by 1 June 2005

	Partner	Date of Signature	Date of Entry into Force
1	Benin	18 May 2001	n.a.
2	Botswana	04 July 2003	n.a.
3	Bulgaria	20 October 1989	n.a.
4	Burkina Faso	18 May 2001	n.a.
5	China	12 October 1989	22 November 1990
6	Côte d'Ivoire	04 November 1997	n.a.
7	Cuba	02 November 1999	n.a.
8	Denmark	13 January 1992	06 January 1995
9	Egypt	11 March 1998	n.a.
10	France	26 March 1999	n.a.
11	Germany	24 February 1995	23 November 1998
12	Guinea	18 May 2001	n.a.
13	India	18 August 2002	n.a.
14	Italy	25 June 1998	n.a.
15	Malaysia	08 November 1996	18 April 1997
16	Mauritania	18 May 2001	n.a.
17	Mauritius	18 May 2001	n.a.
18	Netherlands	31 March 1989	07 January 1991
19	Romania	14 September 1989	n.a.
20	Serbia and Montenegro	14 November 2000	19 November 2002
21	South Africa	09 July 1998	n.a.
22	Switzerland	08 October 1991	16 June 1993
23	United Kingdom	22 March 1989	25 October 1991
24	Zambia	18 May 2001	n.a.
25	Zimbabwe	30 June 2003	n.a.

Source: UNCTAD (2005)

78. These investment treaties are instrumental to shaping the risk/return relationship for investment in agri-based industries in Africa because they create a preferential link to convertible currency and high income markets. The umbrella nature of the initiatives presents the option to derive rewards from primary and secondary processing of agricultural commodities-- at the firm, industry, and macroeconomic levels.

79. Industry and company strategies are influenced by market liberalisation and the related trade and investment opportunities and constraints. Specifically, for industries and companies, the key implications of global market liberalisation are (a) increasing competition for market share and consumer spending and (b) declining commodity/raw material prices. The possible responses to shifts in factors shaping the business' host environment are to (a) push to maintain the status quo, (b) lobby to delay the changes or (c) accept the changes as new facts and seek ways to capture gains from the market globalization trend. In many ways, industries, businesses, and even governments of non-OECD member countries, as commodity producers and finished goods marketers, have limited market power to push or lobby against global market liberalisation changes and therefore focus on choice "c" – identifying mechanisms to foster positive outcomes from the changes. These positive outcomes invariably fit into the category of 'new tools' to respond to economic development challenges that prior to the market liberalisation (or globalization) trend were the focus of discussion, programming and funding by two parties—governments and (bilateral and multilateral) economic development institutions. With market liberalisation came the realisation that the private sector is pivotal to positive macroeconomic performance. This view was assumed to be the case for many OECD member countries, but was a new idea for non-OECD governments and economic development institutions.

Box 3. Trade Agreements with the EU and the US

Beyond regional trade expansion strategies and bilateral investment treaties, plurilateral preferential trade agreements addressing market access for goods shape the more general response to macroeconomic liberalisation. The trade relationship of African, Caribbean, and Pacific (ACP) countries with the EU has historically been guided by the Lomé Convention.[1] This convention provided preferential access to EU markets for the commodities from ACP countries and technical assistance.

In 2000, the EU and ACP countries adopted the Cotonou Agreement, which is a framework trade, development assistance and political cooperation treaty that replaces the Lomé Convention. Under the Cotonou Agreement, the parties agreed to negotiate a separate set of individual bilateral treaties between the EU and the participating ACP countries. These individual arrangements will provide specific rights and obligations tailored to each ACP region. With the exception of South Africa and Cuba, trade relations will be guided for all other 76 ACP countries by the bilateral arrangements or Economic Partnership Agreements (EPAs). EPA negotiations began in September 2002 and are expected to be completed in time for implementation, which is to begin by October 2008.

The EU launched the Everything-But-Arms (EBA) initiative on 26 February 2001 when the General Affairs Council adopted an amendment to the EU's Generalised Scheme of Preferences (GSP). The EBA amendment extends duty and quota free access to products originating in Least Developed Countries (LDC), except arms and ammunition.

The US has a trade initiative specifically for Sub-Saharan Africa. The African Growth and Opportunity Act (AGOA) which was launched on 2 October 2000 and was extended on 12 July 2004. Through the extension, AGOA extends preferential access for imports from beneficiary Sub-Saharan African countries until 30 September 2015. "The US President determines which countries are eligible. Besides basic requirements concerning core human and worker rights, the country must have eliminated barriers to U.S. trade and investments, must have shown continual progress towards fighting corruption and establishing a market-based economy that protects private property rights, the rule of law, and must pursue economic policies to reduce poverty in order to be eligible for preferential treatment." (Lippoldt and Kowalski, 2005, p. 72)

1. Of the countries in this case study, Ghana, Mozambique, and Uganda are countries that are ACP countries.

Country Risk and Business Rating

80. Standard & Poor's, in partnership with the UNDP, developed sovereign credit ratings for previously unrated economies in Sub-Saharan Africa.[20] Standard & Poor's issued Ghana a 'B' short term sovereign rating, a 'B+' long term sovereign rating, and a 'stable' call.[21] In January 2005, the EIU, a different business analysis company, indicated concern about the liquidity risk in the near term for Ghana. The EIU concern centres on increased liquidity risk in 2005-06. Demand for imports was expected to continue to outpace Ghana's exports, even as inflation was expected to increase from 12.7% in 2004 to 17.3% in 2005. Nonetheless, Ghana's overall EIU rating is 'C,' which indicates a country that often offers foreign investors "exciting" but risky opportunities (Table 2) (EIU, 2005).

81. Few reputable tools can summarize a country's business environments in a single rating. However, the International Finance Corporation (IFC) and World Bank conducted surveys on key aspects of starting, operating, and closing a firm in many countries. The most recent survey results are published in *Doing Business in 2005: Removing Obstacles to Growth*. Specifically, *Doing Business* benchmarks regulations in the business areas of Starting a Business, Hiring and Firing Workers, Registering Property, Getting Credit, Protecting Investors, Enforcing Contracts and Closing a Business (Table 4). Clear rigidities and inefficiencies exist in formal business regulation environment. The non-competitiveness of

20 . The six other previously unrated economies in Sub-Saharan Africa to be assigned sovereign credit ratings and their corresponding short-term/call/long-term ratings are: Ghana (B+/Stable/B; September 2003); Cameroon (B/Stable/B; November 2003); Benin (B/Stable/B+; December 2003; Burkina Faso (B/Stable/B; March 2004); Mali (B/Stable/B; May 2004); and Madagascar (B/Stable/B; May 2004).

21 . Standard & Poor's provides credit ratings, indices, risk evaluation, investment research, data and valuations.

business environment relative to OECD member countries is hardly surprising and is an opportunity for public/private partnerships, given the experience of OECD countries with private contractors managing public institutions. Reducing the overall business operating and transaction costs is an imperative for stimulating FDI and having the *expected* gains from FDI. Effecting efficiency improvements in the business environment will increasingly become a key competitive factor in attracting FDI.

Table 4. Business Environment Indicators for Ghana

	Ghana	Regional Average	OECD Average
Economic Characteristics (2003)			
Region	Sub-Saharan Africa		
Income Category	Low Income		
Gross National Income (GNI)	320	562	25773
Informal Economy (% GNI)	38.4	42.3	16.8
Population (million)	20.43	19.46	41.5
Starting a Business (2004)			
Number of Procedures	12	11	6
Time (Days)	85	64	25
Cost (% of Income per Capita)	87.5	223.8	8
Minimal Capital (% of Income per Capita)	31.4	254.1	44.1
Hiring and Firing Workers (2004)			
Difficulty of Hiring Index	11	53.2	26.2
Rigidity of Hours Index	40	64.2	50
Difficulty of Firing Index	50	50.6	26.8
Rigidity of Employment Index	34	56	34.4
Firing Costs (Weeks of Wages)	25	59.5	40.4
Registering Property (2004)			
Number of Procedures	7	6	4
Time (Days)	382	114	34
Cost (% of Property per Capita)	4.1	13.2	4.9
Getting Credit (2004)			
Cost to Create Collateral (% of Income per Capita)	37.9	41.8	5.2
Legal Rights Index	5	4.6	6.3
Credit Information Index	2	2.1	5
Public Credit Registry Coverage (Borrowers per USD 1 000 per Capita)	0	1.1	76.2
Private Bureau Coverage (Borrowers per USD 1 000 per Capita)	1	39.4	577.2
Protecting Investors (2004)			
Disclosure Index	2	2.1	5.6
Enforcing Contracts (2004)			
Number of Procedures	23	35	19
Time (Days)	2000	434	229
Cost (% of Debt)	14.4	43	10.8
Closing a Business (2004)			
Time (years)	1.9	3.6	1.7
Cost (% of Estate)	18	20.5	6.8
Recovery Rate (%)	28.2	17.1	72.1

Source: IFC and World Bank (2005)

Foreign Direct Investment in Ghana

82. Ghana seeks to shift to export-led economic development, with the private sector as a key ally in the overall goal of Ghana becoming a middle income country by 2020. Foreign direct investment is *expected* to be instrumental in shifting the economy to (value-added) export-led growth. With several other non-OECD member countries also seeking to capture gains from market liberalisation with export-

led economic growth and with the private sector and FDI at the centre of the investment strategies of several countries, competition to attract foreign investors is intense. Investment promotion agencies (IPAs), tax holidays, designations of priority sectors and free trade zones (FTZs) are common instruments for attracting targeted investor groups.

83. In 1998, Ghana won support from the multilateral institutions for the Ghana Trade and Investment Project. The principal objectives of the Gateway Project are to ease trade and attract a critical mass of export-oriented, private sector firms. Under the Gateway Project, the Ghanaian agencies, which are the first interaction points for investors with the government, will be re-engineered into agencies that help trade. Investors' first contact with the government of Ghana is with one of the following agencies: Customs, Excise and Preventive Services, the Ghana Immigration Service, the Ports and Harbours Authority, the Ghana Civil Aviation Authority, the Ghana Free Zones Board and the Ghana Investment Promotion Centre (GIPC). The Gateway Project also provides support to off-site infrastructure for privately developed and owned FTZ enclaves in the cities of Tema, Ampabame, and Sekondi. Although FTZs are targeted for support under the Gateway Project, business sites designated as FTZs and the broader business community will benefit from FTZ off-site infrastructure investments. Successful implementation of the Gateway Project will be instrumental in Ghana achieving its goal of becoming a middle income country by 2020.

84. Ghana passed an investment law in 1995 that articulates incentives for foreign or domestic investors. The investment advantages of investing in a manufacturing enterprise for export are greater than trading investments, for example. Currently, Ghana is particularly interested in investors for the three FTZ enclaves.[22] Although a minimum size of investment is not stipulated, it is easier to capture the attention of frontline government agencies with projects of noticeable financial size (initial capital and operating cash flows) that target Ghana's priority sectors: Information and Communication Technology (off-shore back office); Textile/Apparel Manufacturing; Agro-food Processing (cocoa, cashew, tropical fruits and vegetables); Seafood Processing (tuna); Jewellery/Handicraft Production; Metal/Hand Tool Fabrication; Floriculture (fresh cut flowers); Light Industry/Assembling Plant; Ceramic Tiles Manufacturing; Pharmaceuticals; and Ethnic Beauty Products.

85. FDI flows to Ghana have been erratic (See Figure 7). The peak years are 1997 and 1999 when FDI was USD 474.6 million and USD 226.7 million. These peak years appear to be explained by a few large transactions that were in line with privatisation of state-owned enterprises. Since 1999, FDI decreased annually, until 2003 when it was USD 88.1 million. Over the past 10 years, Britain, India, China, Lebanon and the US accounted for close to 50% of the 1 745 FDI projects in Ghana. The service and manufacturing sectors, which include food processing, dominate the economic activity profile of FDI.[23] Although the number of projects in the service and manufacturing sectors tend to be about the same, the total investment cost for service projects is double that of manufacturing projects. Over the past ten years, agricultural projects accounted for approximately 8% of total number of projects and over 12% of the total investment. In the late 1990s, Ghanaian/foreign national joint ventures (JV) were the ownership structure for 762 projects, more than double that of 322 completely foreign owned enterprises (see Table 5). From the period 1994-2000 to 2001-2004, the total number of FDI projects declined from 1084 to 545 projects. The investment per project also decreased from 1.48 million USD to 0.61 million USD. The share of completely foreign owned investments increased from 29.7% to 38.0%. All of which indicated a weakening of the investment in Ghana.

22 . Once established, the advantage of operating in one of the FTZs is the prospect that on-site and off-site support infrastructure will be in place, which eases exporting.

23 . The Economic Activity Profile compiles data for the following sectors: agriculture; building and construction; export trade; general trade; manufacturing; services; and tourism.

Table 5. Ownership Structure of Projects and Investments

		FDI Projects		Total Investment		Investments per Projects
		number	*%*	*USD million*	*%*	*USD million*
January 1994 to June 2000	100% Foreign	322	29.7	455.87	28.3	4.42
	JVs	762	70.3	1152.64	71.7	1.51
	Overall	**1084**	**100.0**	**1608.51**	**100.0**	**1.48**
January 2001 to June 2004	100% Foreign	207	38.0	118.59	35.7	0.57
	JVs	338	62.0	213.21	64.3	0.63
	Overall	**545**	**100.0**	**331.80**	**100.0**	**0.61**

Source: Investment Promotion Agency of Ghana

86. FDI has been said to have a greater impact on economic development than development assistance in the form of grants (*fDi Magazine*, 2005). FDI adds elements of competition and broadens the opportunity set of labour, financial and product markets. The challenge is to balance aggressive pursuit of FDI whilst bolstering support for public goods that creat, connect and grow markets, such as transportation networks, functional and technical education, water supply and treatment and legal institutions. The strong multiplier effect of well synchronized FDI attraction programmes and (broad) investment in the noted public goods is much needed to catalyze economic development today when financial capital markets are open globally.

Example of Foreign Direct Investment in Ghana: BLUE SKIES Company

87. BLUE SKIES, a privately owned, joint venture company was incorporated in 1998. It maintains an administrative base in the UK and has operations in Ghana and in Egypt.[24] BLUE SKIES investors are a UK national, with extensive experience in the fruit trade business, and Ghanaian nationals, with many years experience in structured finance in the US and in several countries in Africa. Day-to-day operations are overseen by a UK expatriate with Ghanaians in all other business office, technical and factory roles. BLUE SKIES factories in both countries support the local farmers and population in the surrounding area.

88. BLUE SKIES produces ready-to-eat fresh fruit salads at source, retail ready, as opposed to processing fruits in the UK which have been imported as whole fruits. The factory in Ghana prepares tropical fruit (such as pineapple, mango, passion fruit, papaya and coconut) and a factory in Egypt prepares temperate fruits (such as grapes, melon, citrus and strawberries). BLUE SKIES products are flown on a daily basis to many European countries in ready-to-serve, plastic pots. In the UK, BLUE SKIES products are sold in major supermarkets under the brand of the supermarket and to caterers (FoodQuality News.com).

89. In Ghana, BLUE SKIES' factory is approximately a two-hour drive from Accra. All produce is grown within 80 km of the factory on small farms with the assistance of BLUE SKIES agronomists, who help the farmers in matters such as soil management and best planting and picking times. The cold chain begins at the fruit receiving area of the factory. With packaging facilities at the source, freshness and nutrient quality are conserved within the fruit.

24 . As a joint venture, BLUE SKIES is a stand-along enterprise, which is a unique ownership structure in emerging/developing markets. Typically JVs in emerging/developing markets are part of the conglomerate structure. The popularity of the conglomerate business structure, with its diverse portfolio of businesses, serves as a critical risk management tool that is important in developing markets where there are limited opportunities to hedge financial and operational risks.

90. BLUE SKIES met EurepGap standards. BVQI, an independent certification body, has certified BLUE SKIES compliant with the Ethical Trade Initiative. BLUE SKIES ethical approach to business means that clean water is produced from all waste water and effluent, all plastics are recycled and all organic waste is composted and returned to the soil.

Box 4. What is EurepGAP?

EurepGAP started in 1997 as an initiative of retailers belonging to the Euro-Retailer Producer Working Group (EUREP). It has subsequently evolved into an equal partnership of agricultural producers and their retail customers. The mission is to develop widely accepted standards and procedures for the global certification of Good Agricultural Practices (GAP).

Technically speaking EurepGAP is a set of normative documents suitable to be accredited to internationally recognised certification criteria such as ISO Guide 65. Representatives from around the globe and all stages of the food chain have been involved in the development of these documents. In addition the views from stakeholders outside the Industry including consumer and environmental organisations and governments have helped shape the protocols.

It is possible for producer organisations to seek an independent and transparent recognition of equivalence with the EurepGAP standards and procedures through a benchmarking system thereby facilitating global trade and aiding the harmonisation of technical criteria.

EurepGAP members include retailers, producers/farmers and associate members from the input and service side of agriculture. Governance is by sector specific EurepGAP Steering Committees which are chaired by an independent Chairperson. Both the standard and the certification system is approved by the Technical and Standards Committees working in each product sector. These committees have 50% retailer and 50% producer representation...The work of the Committees is supported by FoodPLUS a not for profit limited company based in Cologne, Germany.

Source : EurepGAP (2005)

91. The BLUE SKIES factory is designated an export processing site by Ghana's IPC and Free Zones Board. Factory operations located outside government designated Export Processing Zones (EPZ) in Tema, or Ampabame or Sekondi, means that BLUE SKIES uses the infrastructure that is publicly available away from the factory site.

Box 5. Challenges of Transportation for a Perishable Product and FDI Needs

BLUE SKIES focuses on its core business and as a designated export processing site, is permitted to import packaging conserves the fresh and nutrient characteristics of the fruit in the cold chain. Imported packaging includes plastic pots/bowls in which the product is sold at retail and the related gas flushing and heat sealing automated machines and materials (FoodQuality News.com). Materials imported to maintain the integrity of the cold chain are temperature control sheets in which pallets loaded with export product, are wrapped. Maintaining the integrity of the cold chain is a particular challenge in the heat and humidity of coastal, tropical Africa.

Efficient, low risk (reliable) and low cost logistics is a recognized challenge for BLUE SKIES' Ghana operations. Transportation issues relate to both the road and air freight areas. Located west of Accra, the capital of Ghana, there is tremendous transportation demand -- heavy truck and equipment, as well as personal and public service vehicles -- on the road network from the BLUE SKIES factory to the Kotoka International Airport. As an area that has become an increasingly popular residential area of employees of businesses in the area and Accra city, there is increasing demand for transportation by private and public service vehicles. In addition, there is marked increase in traffic flow and pressure on existing road networks from heavy trucks and equipment from several investments in agri-processing in the area. However, the extraordinary factor boosting ground transportation flow from areas west of Accra is the on-going civil conflict in Ivory Coast. The increased throughput is a potential 'positive' for public sector revenues and is supportive of the Gateway Project model of Ghana being a regional hub, it is a daily business operation problem for BLUE SKIES and other agri-processing companies located in the area west of Accra city. Efforts to improve the situation centre on building a new road of more durable material and with more lanes. Under a World Bank funded project that is being implemented by China, work has begun but the work is progressing slowly.

Air freight transportation is increasingly a challenge as BLUE SKIES overseas sales increase. The problem is exacerbated by a reduction in the number of airlines that service West Africa. Ghana Airways, historically the 'network' airline of West Africa, went out of service in August 2004, was sold to a new Ghana-USA JV company, Ghana International Airlines Limited, which plans to start flying within the ECOWAS region in the third quarter of 2005. Direct, non-stop routes to Europe are serviced by KLM, Al Italia, British Airways and Lufthansa. South Africa Airlines, Egypt Air and Kenya Airways provide direct, non-stop service to major cities in south, north, and east Africa. However, the combination of limited allocation of cargo space on these international carriers and increasing export demand by high value products, affects the cost of operations directly and indirectly by increases in air freight rates and transaction costs. More time required to execute shipments and increased engagement with the informal market are included in the indirect impact.

92. Locating the factory close to the fruit production is only a first step in reducing the risk of inconsistent flow and quality of tropical fruit. BLUE SKIES' program of extension services to farmers helps build relationships that can be as strong, if not stronger, than a contract. These relationships can serve as an agent of risk mitigation in emerging markets where contract enforcement tends to be weak.

93. BLUE SKIES has diversified its source of tropical fruit and temperate fruit processing and packaging by expanding operations in Egypt. Such diversification has been an integral part to developing a consistent flow and quality of fruit. BLUE SKIES sources mangoes from northeast Brazil to supplement Ghana supplies. Brazil, through historic links with West Africa and geographic similarities to Ghana, produces mangoes of a same variety as those grown within the area of the BLUE SKIES factory. Brazilian mangoes fill seasonal raw material supply gaps that arise from the strong retail demand in UK. The Egyptian expansion increases the likelihood that BLUE SKIES will be able to deliver any kind of fresh-cut, ready-to-eat package fruit to retail outlets and wholesalers in Europe. BLUE SKIES can guarantee European food retailer suppliers of ready-to-eat fruit, either tropical, temperate or a mix.

94. Trade and investment agreements, and other policy instruments that lower trade barriers, are the crucial links to markets where consumers that are willing to pay for fruits that are exotic, hygienically prepared, fresh rather than conserved by canning or quick frozen processes. Accessing markets in the northern temperate geographical zone, where tropical fruit availability is import dependent is pivotal to the BLUE SKIES business proposition. Willingness to pay for intangible characteristics –convenience and safety– is predominately found in high income countries where an increasing share of the population is middle class. Also the demographics in these markets tilt toward an aging population. In high income countries, consumers are emphasizing nutrition to manage their health (Wilson, 2005). When combined

with the previous point about willingness to pay for a consistent supply fresh fruit, these factors are drivers of growth for BLUE SKIES. This consumer group drives food retail markets in temperate northern hemisphere and is a critical component in supermarket industry-led regulations such as EurepGap.

95. BLUE SKIES was incorporated in 1998. It was able to include in the original business plan the costs of designing and implementing EurepGap requirements. The result was uninterrupted European sales by BLUE SKIES in January 2005 when EurepGap regulation compliance became mandatory. However, many small- and medium-size enterprises in Africa's burgeoning horticultural industry are finding EurepGap to be a significant cost hurdle, from information, design and implementation points of view. Entrepreneurial enterprises in emerging markets/developing countries, especially those without FDI, are more aware of international manufacturing standards, such as ISO 9000. As a potential source of international business uncertainty, initiatives like EurepGap could further dampen FDI flows to Africa where food safety and traceability are valued by consumers but are cost for producers.

B. MOZAMBIQUE

Assessment

96. FDI and trade, as with other aspects of the economy, are greatly aided by investments in infrastructure and education. The experience of PESCAMAR, a seafood firm in Mozambique, suggests that domestic infrastructure networks are very important to the financial performance of export enterprises. Further improvement in banking services in Mozambique, by providing service outside major cities would also avail PESCAMAR, and other companies' management agenda for market demand/value issues. Transparent regulation coordination in importing countries, especially between industry, environmental, and trade groups, would reduce the FDI risk. Catalyzing FDI and trade in the future is more about improving the business investment environment investing in infrastructure by the public sector, and supporting training than providing preferred access for specific products to high-income markets.

Investment and Trade Agreements

97. Mozambique has signed several BITs (Table 6). It is interesting to note that the earliest BITs are with countries that are Mozambique's major trade partners. In addition, the regional diversity of BIT partners reflects, to a certain extent, Mozambique's openness to shifting away from historic relationships.

98. Mozambique's trade agreement portfolio includes two broad Africa-wide agreements with the EU and the US, and a sub-regional agreement. See Box 1 in the case study of Ghana for a further discussion of the agreements with the EU and the US. Mozambique's membership in the Southern African Development Community (SADC), an economic grouping of fourteen East, Central and Southern African countries,[25] is an opportunity to leverage the country's strategic location as a gateway for its four landlocked neighbouring countries and possibly provide a critical mass of consumers for agricultural commodities, such as rice and electricity. Implementation of the somewhat complicated rules of origin, tariff reduction schedule and dismantling non-tariff barriers have slowed the evolution of SADC. Beyond SADC, the Mozambique-Zimbabwe trade agreement signed in March 2005,reflects the importance of intra-regional trade. [26]

25 . SADC includes Angola, Botswana, Democratic Republic of Congo, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe. These were the founding Members of SADC with the exception of the Democratic Republic of Congo and Seychelles. There are several protocols under SADC such as those on agriculture, fisheries, Trade and telecommunications.

26 . Goods covered by the Mozambique-Zimbabwe trade agreement must enter or leave Mozambique at the four main border posts: Machipanda and Espungabera in Manica province, Chicualacuala in Gaza, and Cuchamano in Tete.

Table 6. Mozambique: Bilateral Investment Treaties

Concluded by 1 June 2005

	Partner	Date of Signature	Date of Entry into Force
1	Algeria	12 December 1998	25 July 2000
2	China	10 July 2001	26 February 2002
3	Cuba	20 October 2001	26 February 2002
4	Denmark	12 October 2002	n.a.
5	Egypt	08 December 1998	25 July 2000
6	Finland	03 September 2004	n.a.
7	France	01 January 2002	17 February 2004
8	Germany	06 March 2002	n.a.
9	Indonesia	26 March 1999	25 July 2000
10	Italy	14 December 1998	n.a.
11	Mauritius	14 February 1997	28 July 1998
12	Netherlands	18 December 2001	26 February 2002
13	Portugal	28 May 1996	31 October 1998
14	South Africa	06 May 1997	28 July 1998
15	Sweden	23 October 2001	26 February 2002
16	Switzerland	29 November 2002	17 February 2004
17	United Kingdom	18 March 2004	12 May 2004
18	United States	01 December 1998	08 December 2004
19	Zimbabwe	12 September 1990	n.a.

Source: UNCTAD (2005)

99. Market liberalisation and the related trade and investment opportunities and constraints influence industry and company strategies. Specifically, for industries and companies in OECD member and non-member countries, the key implications of global market liberalisation are increased competition for market share and consumer spending and declining commodity/raw material prices. The broad EU and US trade agreements are important to decisions to invest in Mozambique, if for no other reason than to export primary or secondary processed goods to high income markets. These exports offer greater potential to recover costs for higher value products than regional trade. The challenge for Mozambique remains attracting, on a large scale, agri-industry investment that uses cash crops as raw material.

Country Risk and Business Rating

100. In July 2004, Mozambique was assigned a sovereign credit risk rating of 'B' for short term and long term, and a "Positive" call by Standard & Poor's. Mozambique's strategic location (proximity to South Africa, gateway to four landlocked countries and long coastline on the Indian Ocean) and diverse and deep natural resource base underpin the "Positive" outlook by Standard & Poor's.

101. Distinct strengths and weaknesses characterize Mozambique's business environment from *Doing Business* (Table 7). Strengths include aspects of Registering Property, such as the time (33 days for Mozambique, 114 for Sub-Saharan Africa, and 34 days for OECD countries) and Cost which is the percentage of Property Per Capita (11.9% for Mozambique; 13.2% for Sub-Saharan Africa). However, the number of steps it takes to Register Property is seven, which means that business transaction costs are higher relative to the region and OECD. The result is greater opportunities for the informal market to become a factor affecting business. The cost of enforcing contracts, measured by the percent of debt, is closer to the indicator for OECD countries than to the Sub-Saharan Africa indicator. The indicator for protecting investors in Mozambique is two out of seven, which is close to the Sub-Saharan Africa regional average score of 2.1. Both scores are lower than the average of 5.6 for OECD countries.

102. Challenges in Mozambique's business environment include Starting a Business, Protecting Investors, the labour market and investment recovery rate. The average requirement of 14 procedures and

153 days to start a business may deter investors from establishing an enterprise in Mozambique. The Investment Promotion Centre (CPI) recognizes the possible negative impact on the investment decision and is beta-testing on-line company registration. Expanding and prompting Mozambique's formal economy to increase per capita income will help to reduce the share of per capita income required to cover the initial cost and minimum capital requirement measure for starting a business. Overall the labour market appears to be more rigid and much more costly when it comes to terminating an employee, than the average in Sub-Saharan Africa. However, this is a plausible legacy of Mozambique's political and economic history. A weakness that requires intense focus is the dismal USD 0.123 on the dollar recovery rate when closing a business. This rating is below the average of USD 0.171 for Sub-Saharan Africa and even lower than the average of USD 0.721 for OECD countries.

Table 7. Business Environment Indicators for Mozambique

	Mozambique	SSA Average	OECD Average
Economic Characteristics (2003)			
Region	Sub-Saharan Africa		
Income Category	Low Income		
Gross National Income (GNI)	210	562	25773
Informal Economy (% GNI)	40.3	42.3	16.8
Population (million)	18.79	19.46	41.5
Starting a Business (2004)			
Number of Procedures	14	11	6
Time (Days)	153	64	25
Cost (% of Income per Capita)	95.8	223.8	8
Minimal Capital (% of Income per Capita)	14.5	254.1	44.1
Hiring and Firing Workers (2004)			
Difficulty of Hiring Index	72	53.2	26.2
Rigidity of Hours Index	80	64.2	50
Difficulty of Firing Index	40	50.6	26.8
Rigidity of Employment Index	64	56	34.4
Firing Costs (Weeks of Wages)	141	59.5	40.4
Registering Property (2004)			
Number of Procedures	7	6	4
Time (Days)	33	114	34
Cost (% of Property per Capita)	11.9	13.2	4.9
Getting Credit (2004)			
Cost to Create Collateral (% of Income per Capita)	5	41.8	5.2
Legal Rights Index	4	4.6	6.3
Credit Information Index	4	2.1	5
Public Credit Registry Coverage (Borrowers per USD 1 000 per Capita)	5	1.1	76.2
Private Bureau Coverage (Borrowers per USD 1 000 per Capita)	0	39.4	577.2
Protecting Investors (2004)			
Disclosure Index (out of 7)	2	2.1	5.6
Enforcing Contracts (2004)			
Number of Procedures	38	35	19
Time (Days)	580	434	229
Cost (% of Debt)	16	43	10.8
Closing a Business (2004)			
Time (years)	5	3.6	1.7
Cost (% of Estate)	8	20.5	6.8
Recovery Rate (%)	12.3	17.1	72.1

Source: IMF and World Bank (2005)

Foreign Direct Investment in Mozambique

103. Foreign direct investment into Mozambique has been erratic, peaking in 1999 at USD 382 million before dropping to USD 139 million in 2000 and fluctuating over the other years (see Figure 7). In 2003, FDI inflows to Mozambique were USD 337 million, which is close to 1999 levels. The objectives of investment, by law, are directly linked to "development, rehabilitation, modernization or expansion of economic infrastructures for the operation of productive activities or for rendering services necessary for supporting productive economic activities and promoting the country's development." (Assembly of the Republic of Mozambique, 1993, Article 7) Beyond the objectives of investment in Mozambique, the investment laws 1) define forms of direct and indirect investment by foreigners and nationals, 2) delineate the required certificates for investment approval, fiscal benefits, industrial free zones, rapid developments zones, and special economic zones and 3) establish councils to create and implement policies for these special areas. In 1993, Mozambique established the CPI, a network to facilitate investment. The CPI disseminates information, reviews project proposals and generally assists prospective investors through the processes associated with site identification to setting-up a company.

104. Additional incentives help to align investments with Mozambique's development goals. For example, there are additional fiscal incentives for investing in eligible activities in the "Rapid Development Zones" (ZRD) designated in the law as the Zambezi Valley, Niassa province, Nacala district, Moçambique Island and Ibo Island. The Zambezi Valley comprises specific districts in Zambezia province – including the port city of Quelimane and specific districts in Sofala and Manica provinces. 'Eligible' activities for ZRD's are agriculture, forestry, aquaculture, livestock raising, lumbering, game animal exploitation, water supply, electric energy (generation, transmission, and distribution), telecommunications, construction of public utility infrastructure, housing, agricultural infrastructure, hotel, tourism, cargo and passenger transport, education and health, among others. The breadth of this list is indicative of the extensive needs of the Mozambican economy. Generally, customs duties are 5% for equipment and machinery but 25% for consumer goods. Overall, the incentives emphasize investing to catalyze economic growth through efficiency gains and new capacity for existing resources.

105. Export earnings are not overlooked; however, if the basket of activities is an indicator, the initial strategy in attracting FDI appears to focus on large scale projects that will have an immediate impact on the economic base of Mozambique. Mega projects such as the USD 1 000 million Mozal aluminium smelter, a USD 1 000 million natural gas pipeline and a titanium mine all leverage Mozambique's natural resources and will eventually reduce the trade deficit. Privatisation of state-owned enterprises has proceeded smoothly. With the sale of Banco Austral to South Africa headquartered ABSA in 2002, all banks in Mozambique are privately owned.

106. Over the period 1990-2002, South Africa led the list of foreign investments in Mozambique with USD 1 400 million, and South Africa led the list in 2004. Australia is a distant second. Portugal, United Kingdom, and Mauritius complete the list of top foreign investors in Mozambique between 1990 and 2002. Japan and France are in the top ten, while Italy, the US and Spain rank eleventh, fifteenth and sixteenth. The diversity in the country of origin of investments is quite strong and indicates a wide appreciation for Mozambique's resource wealth and strategic geographic position for central-southern African countries. However, an overwhelming share of FDI to date is concentrated in Maputo. CPI trade fair presentations of August/September 2004 emphasized road and rail infrastructure projects highlighting the links to prospective investment in agri-based processing and giving information about the potential markets for products. The trade agreement that features most prominently in the CPI investment opportunities promotion presentation is the US African Growth and Opportunities Act (AGOA). Investment projects to revitalize Mozambique's textile industry for exports to the US under AGOA are highlighted. The European Union Cotonou Agreement is noted in the CPI promotional materials. The 2004 Mozambique investment promotion presentation specifies that investment partners are being sought. Foreigners are

required to invest a minimum of USD 50 000, while the requirement for Mozambican nationals is USD 5000.

Example of Foreign Direct Investment in Mozambique: Pescamar, Lda.

107. PESCAMAR is headquartered in Beira, Sofala province, and includes investments in the companies of Pesacabom (100%) and Pesca Angoche (60%) and Carrelomar (51%). PESCAMAR is a joint venture between the Pescanova Group, a publicly traded, branded seafood company headquartered in northwest Spain, and EMOPESCA (Empresa Mocambicana de Pescas) a government company. PESCAMAR's fleet of 25 freezer-trawlers conduct the company's principal business of industrial, open-catch shrimp for export. Portugal and Spain account for 80% of PESCAMAR's sales. PESCAMAR and Efripel, a joint venture with a Japanese firm, combine to account for 70% of Mozambique's industrial shrimp catch. Ranked twenty-eight in KPMG's most recent survey of the Top 100 companies in Mozambique, PESCAMAR is the leading company in the combined agriculture and fishery sector. In 2002, PESCAMAR's financial performance included revenues of USD 18 million; USD 981 865 in net profits from USD 17 million in net assets.

108. PESCAMAR's relationship with Pescanova dates back to 1980 when Pescanova acquired 43% of PESCAMAR from Emopesca. At that time, Pescanova provided much needed financing assistance to PESCAMAR through an inter-company loan. Through PESCAMAR's focus on investing in human resources and re-investing in their fleet over the period 1989-1996, PESCAMAR has evolved into a self-reliant component of Pescanova's worldwide network. Pescanova increased its shareholding in PESCAMAR and by 2001 held 80% of the shares. Today, PESCAMAR independently sources financing from the improved Mozambican banking sector. The relationship with Pescanova is integral to PESCAMAR's spare parts supply and export market logistics.

109. PESCAMAR maintains a strong commitment to the community in Beira. In 1980, PESCAMAR had 16 expatriates in the management team of 20 persons. Today, only two expatriates are members of PESCAMAR's 20 person management team. The transition in the composition of PESCAMAR's management team has been achieved mostly through investment in national employees going through a training program in Maputo. Employee benefits for PESCAMAR's 603 workers include a free health clinic that provides free access to a medical doctor. PESCAMAR's decision to rebuild the interior of a longstanding landmark in Beira was a significant vote of confidence for a city that is slow to emerge from the impact of a protracted war. In September 2004, PESCAMAR acquired a 60% share of the company Beiranave, a boat repair and maintenance company that also owns a dry dock.[27] PESCAMAR seeks to leverage Beira's location as the largest shipyard between Durban, South Africa and Mombassa, Kenya.

110. PESCAMAR's business model pivots on the widely acknowledged high quality of prawns along the coast of Mozambique, access to consumers who are willing and able to pay for quality, and the technology that delivers that quality. The EU's EBA of duty free imports of open-catch shrimp from Mozambique is integral to the success of PESCAMAR's business model.[28] Pescanova's initial financial investment provided the means to grow a business in war time. Pescanova's continued additional financial investment provides benefits from the economies of size associated with a global business structure, which is especially important in managing business costs in Mozambique. In addition, by being part of a global

27 . The other shareholders in Bieranave are BIM Bank (20%) and Bieranave workers (20%).

28 . Only within the past three years did Mozambique apply to the EU for similar treatment of aquaculture prawns. Export sales to the EU from an aquaculture prawn joint venture investment with the Chinese in Sofala province was delayed, and cash flow was delayed for one year, when it was discovered that aquaculture products required separate approval from EU regulators.

business group, PESCAMAR is current on technologies and practices for product traceability and maintaining the prawn stocks and biodiversity.

111. Threats to PESCAMAR's business model and commitment to sustainable growth are predominantly external to the company. Poor infrastructure—such as ports and roads, leads the list of potential business threats, and education, such as university and especially technical schools—is a threat to PESCAMAR. Mozambique's continued political stability and increasing credibility are instrumental to the future of the broader private sector investments – domestic and foreign. Lastly, environmental policies in importing countries, such as legislation in the US regarding turtle protection, introduce additional fisheries investment uncertainty. These issues also add to economic development tensions between focusing on artisanal or industrialized fisheries.

C. TUNISIA

Assessment

112. In contrast to most of SSA, Tunisia has had a broader and longer experience with FDI and trade. This experience provides insights into possible sources of opportunities and additional risks that may occur as FDI and trade increase in importance to a developing/emerging market country's macroeconomy. In today's intensely competitive FDI market, Tunisia can continue to leverage the experiential knowledge about FDI by opening financing to FDI and linking new finance products with FDI to sectors that best deliver on job creation for skilled labour.

113. Although market access for Tunisia's agri-based products to EU countries has evolved, the bilateral trade agreement trend puts an administrative burden on exporting countries. It can be costly and time consuming to be aware of trade opportunities under different preferential arrangements and to meet the requirements to take advantage of the opportunities. For example, there is a list of agri-based products in the Tunisia-EU Association Agreement that are permitted entry into the EU only at specific periods of the year. Better coordination between members of bilateral or regional trade agreements may reduce the administrative burden of trade. Such improvements can go a long to catalysing FDI and trade. Despite these challenges, the example of Borges Tunisie illustrates the potential that FDI has to help companies overcome regulatory difficulties.

Investment and Trade Agreements

114. Since 1990, Tunisia has signed several bilateral investment and trade agreements (Tables 8, 9, and 10). EU and Middle Eastern countries dominate the list of trade agreements, permitting Tunisia to serve as a link between Africa, Arab and Mediterranean nations. Investment flows are determined by access to markets and social and political conditions, Tunisia, as a cornerstone or link country between three regions, can gain significantly from bilateral and regional trade agreements. Tunisia has one bilateral trade agreement with a single country, and four bilateral trade agreements with regions. In addition, Tunisia has lower-level investment and trade agreements with four countries, also listed below.

Table 8. Tunisia: Bilateral Investment Treaties

Concluded by 1 June 2005

	Partner	Date of Signature	Date of Entry into Force
1	Albania	30 October 1993	n.a.
2	Argentina	17 June 1992	23 January 1995
3	Austria	1 June 1995	1 January 1997
4	Belgium and Luxembourg	8 January 1997	18 October 2002
5	Bulgaria	24 November 2000	15 October 2003
6	Burkina Faso	07 January 1993	n.a.
7	Chile	23 October 1998	n.a.
8	China	31 October 1992	n.a.
9	Côte d'Ivoire	16 May 1995	n.a.
10	Czech Republic	06 January 1997	08 July 1998
11	Denmark	28 June 1996	11 April 1997
12	Egypt	08 December 1990	02 January 1991
13	Ethiopia	14 December 2000	14 December 2000
14	Finland	04 October 2001	04 September 2003
15	France	20 October 1997	18 January 1999
16	Germany	20 December 1963	06 February 1966
17	Greece	31 October 1992	21 April 1995
18	Guinea	18 November 1990	n.a.
19	Hungary	13 May 2003	n.a.
20	Indonesia	13 May 1992	12 September 1992
21	Iran, Islamic Republic of	23 April 2001	27 February 2003
22	Italy	17 October 1985	24 June 1989
23	Jordan	27 April 1995	23 November 1995
24	Korea, Republic of	14 September 1975	28 November 1975
25	Kuwait	14 September 1973	n.a.
26	Lebanon	24 June 1998	4 June 2000
27	Libyan Arab Jamahiriya	06 June 1973	n.a.
28	Mali	01 July 1986	n.a.
29	Malta	26 October 2000	12 May 2002
30	Mauritania	11 March 1986	n.a.
31	Morocco	28 January 1994	n.a.
32	Netherlands	11 May 1998	n.a.
33	Niger	05 June 1992	n.a.
34	Oman	19 October 1991	1 March 1992
35	Pakistan	18 April 1996	n.a.
36	Poland	29 March 1993	22 September 1993
37	Portugal	28 February 2002	n.a.
38	Romania	16 October 1995	08 August 1997
39	Senegal	17 May 1984	n.a.
40	Spain	28 May 1991	20 June 1994
41	Sweden	15 September 1984	13 May 1985
42	Switzerland	02 December 1961	19 January 1964
43	Togo	13 September 1986	n.a.
44	Turkey	29 May 1991	07 February 1993
45	United Arab Emirates	20 April 1996	n.a.
46	United Kingdom	14 March 1989	04 January 1990
47	United States	15 May 1990	7 February 1993

Source: UNCTAD (2005)

Table 9. Trade Agreements with Tunisia

Countries	Date of Signature	Date of Entry into Force	Description
Norway, Iceland, Switzerland and Liechtenstein (*European Free Trade Association 2004*)	17 December 2004	1 June 2005	Covers exchange of industrial goods, including agricultural and fish products of the food-processing industry
Turkey	29 September 2004	2005	• Import duties dropped immediately for raw materials, semi-finished goods and capital equipment • Import duties decline to zero over 8 years for : industrial goods with competitive local equivalent • Import duties lifted over 8 years, beginning in 2007 for all other industrial goods • Tunisian main exports to Turkey: phosphates and phosphate derivatives, electrical cables, leather and dates • Turkey main exports to Tunisia: imports iron, steel and mechanical and electrical equipment
Jordan, Egypt and Morocco (Agadir Declaration)	25 February 2004	2004	• Removal of tariffs phased to zero by 1 January 2006. • Harmonise legislation with regard to standards and customs procedures.
Libya	14 June 2001	n.a.	• Tunisia started dismantling tariffs in 1996 before the effective date of the Association Agreement. • From January 2001, Tunisia has obtained better access to the EU market for olive oil (increase in the annual quota and duty set to zero), cut flowers, tomato concentrate, new potatoes and oranges for which an increase in tariff quota has been agreed. • From January 2001, EU obtained gradual reduction in customs duties on certain Community products like wheat and vegetable oils. • The agricultural regime has been brought into the Association Agreement. • Tunisia has also signalled its intention to swiftly implement the new Pan-Euro-Mediterranean system of accumulation of origin, a protocol agreed to at the Third Euro- Mediterranean Trade Ministerial Conference in Palermo, in July 2003.
EU (*Association Agreement*)	July 1995	March 1998	

Source: Various Sources

Table 10. Investment Agreements with Tunisia

Countries	Date of Signature	Date of Entry into Force	Description
Iran	6 Mach 2005		Covers industrial and trade exchange including joint investments, engineering and technical services exports, flower and plant exports and production of vehicle parts
China			Two agreements concerning bilateral trade and reciprocal encouragement and protection of investments
Pakistan	October 2002		
US (*Trade and Investment Framework Agreement*)	October 2002	October 2003	

Country Risk and Business Ratings

115. Sovereign risk rating agencies appear to be in relative agreement. Standard & Poor's assigned Tunisia a BBB/Stable/A-3 for foreign currency credit rating in March 2000. EIU's rating is more recent (December 2004) and rates Tunisia Country Risk as 'B', indicating that economic policy and political risks need to be watched carefully (Table 2). Countries in the EIU 'B' rating band generally have no significant foreign exchange constraint and in no way approach the need for negotiations with donors about external debt rescheduling. The risks centre on the ability to maintain political stability as the pressures to transition to a more open political system builds and persistent high unemployment rate – an issue with magnified importance in a society with 'youthful' demographics.

Table 11. Business Environment Indicators for Tunisia

	Tunisia	Regional Average		OECD Average
		MENA	SSA	
Economic Characteristics (2003)				
Region	Middle East & North Africa			
Income Category	Low Middle			
Gross National Income (GNI)	2240	6096	562	25773
Informal Economy (% GNI)	38.4	27.4	42.3	16.8
Population (million)	9.9	20.75	19.46	41.5
Starting a Business (2004)				
Number of Procedures	14	10	11	6
Time (Days)	11	39	64	25
Cost (% of Income per Capita)	327.2	51.2	223.8	8
Minimal Capital (% of Income per Capita)	31.4	856.4	254.1	44.1
Hiring and Firing Workers (2004)				
Difficulty of Hiring Index	61	22.6	53.2	26.2
Rigidity of Hours Index	0	52.9	64.2	50
Difficulty of Firing Index	100	40.7	50.6	26.8
Rigidity of Employment Index	54	38.7	56	34.4
Firing Costs (Weeks of Wages)	29	74.3	59.5	40.4
Registering Property (2004)				
Number of Procedures	5	6	6	4
Time (Days)	57	54	114	34
Cost (% of Property per Capita)	6.1	6.8	13.2	4.9
Getting Credit (2004)				
Cost to Create Collateral (% of Income per Capita)	22.4	18.5	41.8	5.2
Legal Rights Index	4	3.9	4.6	6.3
Credit Information Index	2	2.1	2.1	5
Public Credit Registry Coverage (Borrowers per USD 1 000 per Capita)	93	20.6	1.1	76.2
Private Bureau Coverage (Borrowers per USD 1 000 per Capita)	0	126	39.4	577.2
Protecting Investors (2004)				
Disclosure Index (out of 7)	6	2.6	2.1	5.6
Enforcing Contracts (2004)				
Number of Procedures	14	38	35	19
Time (Days)	27	437	434	229
Cost (% of Debt)	12	17.9	43	10.8
Closing a Business (2004)				
Time (years)	1.3	3.9	3.6	1.7
Cost (% of Estate)	8	13	20.5	6.8
Recovery Rate (%)	50.1	28.6	17.1	72.1

Source: IMF and World Bank (2005)

116. Regional differences between MENA and SSA are stark: GNI per capita, USD 2 240 for MENA and USD 562 for SSA, and the informal economy, 27.4% for MENA and 42.3% for SSA. However, the average population for countries comprising each region is not markedly different, 20.8 million for MENA and 19.5 million for SSA. Differences between both regions and the averages for OECD countries are significant, as would be expected given differences in economic and political evolution.

117. Tunisia is closer to the OECD average for Starting a Business, except for the cost of USD 246, which is below the averages for SSA, MENA and the OECD. In terms of Hiring and Firing Workers, Tunisia's profile more closely matches that of SSA, except in terms of the cost of firing workers, where investors can expect a cost of 29 weeks of wages which is well below the cost in SSA, MENA, or the OECD. Time required and cost of Registering Property in Tunisia is about the same as elsewhere in MENA, which is about half of what it will take for a similar business task in SSA region. In the area of Getting Credit, which is especially important for the local investment partners, surprisingly it appears Tunisia has the strongest advantage in Public Credit Registry coverage. Tunisia's rating in Protecting Investors is as good as the rating for OECD countries. Ratings for Enforcing Contracts are also similar for Tunisia and OECD countries, with the additional advantage of it taking an average of 27 days in Tunisia as opposed to an average of 229 days in OECD countries. Lastly, the transaction cost of closing a business in Tunisia is a close match to OECD member countries in terms of the time and share of estate. However, the Recovery Rate of closing a business, which is measured by cents on the dollar, is USD 0.501 for Tunisia compared to USD 0.286 for MENA, USD 0.171 for SSA, and USD 0.721 for OECD countries. Also, businesses that invest outside their home markets are usually seeking to balance geographic production and/or marketing risk and well structured financing can influence the investment Recovery Rate if a business closes.

Foreign Direct Investment in Tunisia

118. Foreign direct investment into Tunisia has been erratic but follows a positive trend (Figure 7). The pace of privatisation of government enterprises has been noticeably slow. The service, mining and finance sectors remain closed to FDI. In addition, financial capital flows are not fully liberalised. The combination of slow privatisation, requisite approvals for outward financial capital flows, and limited growth FDI sectors, such as services, all contribute to the erratic FDI into Tunisia.

119. Tunisia established the Agriculture Investment Promotion Agency (APIA) many years ago. Today, the number of investment promotions agencies has increased and are specialized. Agriculture and agri-processing investment is supported by the Agency for the Promotion of Industry (API), established over 32 years ago; the Centre for the Promotion of Exports (CEPEX); and the Foreign Investment Promotion Agency (FIPA). Since 1989, the FIPA is a one-stop shop for investors, and through FIPA, it is possible to create a company within 24 hours. The API registers firms electronically and provides the registration certificate. In addition to these support institutions for investors, there are two Free Trade Zones: Bizerta in the north and Zarzis in the south. Through the 1994 Investment Incentives Code, Tunisia abandoned differentiating between foreign and domestic investors for the permitted industries.[29]

120. Tunisia frequently participates in trade fairs overseas, and in October 2004, APIA held their fourth SIAT, partnership fair, to showcase specific agriculture value chain investment opportunities to prospective investors. Beyond the typical menu of financial and fiscal investment incentives, Tunisia actively promotes the EU Association Agreement as a reason to invest and advertises that the focus of their investment promotion is partnerships or joint ventures. The menu of investment incentives expands for companies that are "wholly engaged in export" of agricultural or fishery based products and expands even

29 . Industries permitted for FDI are manufacturing (includes textiles), agriculture, agro-industry, export- and industry-related services and public works.

further for companies in the organic agriculture business.[30] Foreign investors are only permitted to lease land. However, the time period of the lease depends on whether the land is private or public, and on the product that will be produced on the land. Private land may be leased for a minimum of three years, and a maximum of 20-25 years, and the lease may be renewed. Public lands may be leased for 10 to 25 years, with the option of renewal. For companies wholly engaged in export, four expatriate technical managers will be issued work permits. Additional expatriate employees require a request from the government.

121. Top joint venture investing countries in Tunisia are France, Italy, Switzerland and the UK. A significant majority of FDI is in exporting firms. That trend has strengthened over time, especially in the last five years. For example, in 2004, 93% of the new foreign investments to Tunisia in 2004 were into companies dedicated to exports. (Table 12) In 2004, agri-industry attracted investment into 119 firms, 51 dedicated to exporting. Enterprises that cool and dry agricultural products and foods attracted the greatest number of foreign investment enterprises. Vegetable oil and cooling businesses topped the list of enterprises that export less than 70% of their products.

Table 12. Foreign Direct Investment Project Details in Tunisia

1990-2004 in USD 1 000

Year	Exports Only			Total		
	Number of Firms	Investment	Number of Employees	Number of Firms	Investment	Number of Employees
2004	132	79,019.67	7589	142	91,918.61	8167
2003	129	48,538.29	7320	169	85,580.84	8377
2002	157	91,108.38	7392	190	491,866.04	8834
2001	165	81,486.73	10574	205	173,358.35	11976
2000	156	128,404.97	13108	204	619,607.23	16272
1999	118	56,723.19	9634	151	195,642.45	11691
1998	160	74,549.01	13946	198	598,187.91	16094
1997	94	88,691.71	9311	133	212,477.59	12196
1996	100	51,914.74	6566	144	185,630.67	9062

Source: Agence de Promotion de l'Investissement Extérieur

Example of Foreign Direct Investment in Tunisia: Borges Tunisie, S. A.

122. The Borges Group created Borges Tunisie, S.A. through a joint venture in 1996. Since 1896, the Borges Group has produced and traded in olives and almonds, the typical agricultural products of Tárrega, Lleida province in the Catalonia region of Spain. The product portfolio of the Borges Group has expanded to include a variety of nuts, dates and olive oil. In 1978, the Borges Group launched an internationalisation expansion plan that includes acquiring agricultural lands, creating subsidiary companies in product supply and consumer markets, and acquisition of Star Fine Foods, a leading food distribution company headquartered California, US. Borges Russia was created in 1997. That expansion was followed by the creation of Borges Andalucía. Today, Borges Group is a leading producer of foods of the Mediterranean diet, exporting its products to more than 95 countries.

123. Borges Tunisie's primary business is exporting high quality olive oil in bulk. Network companies of the Borges Group are instrumental in marketing the premium olive oil Borges Tunisie produces within the EU and to newer markets for Tunisian products, such as the Argentina, Australia, Brazil and US. More recently, Borges Tunisie has been producing bottled, high quality olive oil under contract for a leading specialty branded food company and shipping direct to the US for retail distribution. The scale of Borges Group operations enables Borges Tunisie to have access to leading bottling technology

30 . "Wholly engaged in export" is defined as exporting 70% or more of product.

and equipment, and multilingual labels and bottles at lower cost than if the Tunisia plant was a stand-alone operation. Borges Tunisie maintains its own olive oil testing/profiling laboratory.

124. In addition to specific advantages of being a subsidiary of a multinational company that specialises in Mediterranean foods, the benefits of FDI in food processing are instrumental to Borges Tunisie's business success. The point of alignment between the Borges Group business growth goals and the focus of the Tunisian government's investment goals centres on diversifying export destinations away from the EU. Key to Borges Tunisie's successful business operations and growth are consistent flow of quality olives; excellent storage and packaging; efficient low risk (reliable) and low cost logistics (within country and to export destination); and strong marketing and distribution channels to food processors and branded retail, in importing countries, especially new markets.

125. As recently as the mid-1990's, a consistent flow of quality from Tunisia olives may have been an almost insurmountable challenge because there had been limited investment in managing the productivity of Tunisia's olive trees. The combination of aging olive trees, principally owned by smallholder, rural farming families and price guarantees by the Tunisian government agency, did little to encourage farmers or industry to focus on possible financial gains from tree replanting. The decrease in the olive purchasing monopoly power of Office Nationale de l'Huile helped to increase the supply of olives to the private sector market. In addition, the Tunisian government recently launched a replanting and handling program for farmers to improve olive tree productivity, reducing olive supply risk over time. Lastly, the emergence of wide availability of mobile telephone technology greatly facilitates efficiency in olive price discovery. Borges Tunisie is located close to the olive growing area and is in constant communication with sellers.

126. Excellent storage and packaging are instrumental to maintaining the high quality of Tunisia's olive oil which is used extensively in blending because of its distinctly pure characteristics. Borges Tunisie has several large stainless steel lined tanks where olive oil is held before exporting. The storage system is an integral component of Borges Tunisie's traceability system. The tanks are manufactured locally to international standards. Borges Tunisie can easily import packaging material for exporting as a foreign company with investment in food processing.

127. The location of the Borges Tunisie plant, close to the olive growing area and within a 30 minute drive to Sfax, drives in-country logistics gains. A transportation subsidy supporting Tunisia's goal of diversifying export markets is instrumental in lowering the cost hurdles to reach new markets in the US, Canada, Brazil, and Argentina. The number of trade agreements that Tunisia has recently signed also helps it to diversify the export markets for Tunisian olive oil, which supports Tunisia country branding, a marketing tool that is becoming increasingly important in the context of globalisation. Expanding consumers' expectation that premium olive oil can come from Tunisia, as well as from the well known sources and brands from Italy and Spain, is integral to Tunisia moving out of the bulk only category for olive oil exports.

128. Tunisia's well functioning and constantly improving infrastructure means that product distribution, from processing plant to export points, can be accomplished without uncertainty or informal markets coming into play. Borges' offices in the US, handles retail and wholesale distribution to 21 US states for Borges Tunisie's bulk and branded products. Distribution to South America is managed from Borges' headquarters in Spain. As a company wholly engaged in export in an agri-based business, Borges Tunisie benefits from many investment incentives. Planned expansion of Borges Tunisie bottling and storage operations should be completed by June 2005. The branding and distribution assets that Borges brings to the investment in Tunisia's olive oil industry are excellent compliments to Tunisia's distinct FDI interest in joint venture, agri-based industries, and expanding export markets.

D. UGANDA

Assessment

129. The Amfri Farms, a fresh and dried fruit firm in Uganda, provides an example of FDI facilitated through the movement of natural persons. One of the challenges that Amfri Farms has faced is the differing regulations for organic produce in the EU and the US. Key to FDI and trade contributing to economic growth in emerging markets is mutual recognition or harmonization of organic certification requirements. The cost of meeting differing regulations may prevent firms in emerging market from exporting to multiple markets. These costs could limit the FDI of some investors.

Investment and Trade Agreements

130. Investment and trade agreements are instrumental to Uganda's drive to incorporate private sector resources in the economic growth strategy. European countries were early signatories of BITs with Uganda. Egypt, which is connected to Uganda geographically and economically by the Nile River, signed a BIT in 1995. After 1999, Uganda experienced a marked increase in the number and geographic dispersion of investment partners (Table 13 for a complete list). See Box 1 in the Ghana case study for a discussion of trade agreements with the EU and the US.

Table 13. Bilateral Investment Treaties with Uganda

Concluded 1 June 2005

	Partner	Date of Signature	Date of Entry into Force
1	Belgium and Luxembourg	01 February 2005	n.a.
2	China	27 May 2004	n.a.
3	Cuba	01 January 2002	n.a.
4	Denmark	26 November 2001	n.a.
5	Egypt	04 November 1995	n.a.
6	Eritrea	30 June 2001	n.a.
7	Ethiopia	02 July 2003	n.a.
8	France	01 January 2002	n.a.
9	Germany	29 November 1966	19 August 1968
10	Italy	12 December 1997	24 September 1999
11	Netherlands	30 May 2000	n.a.
12	Nigeria	15 January 2003	n.a.
13	Peru	27 February 2003	n.a.
14	South Africa	08 May 2000	n.a.
15	Switzerland	23 August 1971	08 May 1972
16	United Kingdom	24 April 1998	24 April 1998
17	Zimbabwe	01 July 2003	n.a.

Source: UNCTAD (2005)

Country Risk and Business Ratings

131. In July 2005, EIU rated Uganda 'C', indicating the "exciting" opportunities for foreign investors that should be approached with caution. The caution surrounding the exciting opportunities is significant because the risk of foreign-exchange crisis and political problems hovers nearby. Although the 'state of

flux' of the Ugandan economy is persistent, the government is taking measures to control the internal and external imbalances (Table 2).

132. According to *Doing Business* Starting a Business and Hiring and Firing Workers is Uganda is more business friendly than other countries in the region. Uganda's characteristics in the area of Registering Property approach the characteristics of OECD countries. A key gap in the entrepreneurship and broader business context is in the area of Getting Credit and Protecting Investors. The absence of institutions for independent assessment of creditworthiness is particularly stark in the Getting Credit area, even when compared to other countries in Sub-Saharan Africa. Uganda surpasses other countries in the region in the three components of Enforcing Contracts: Number of Procedures, Time, and Cost. Uganda lags behind the regional average in the area of Closing a Business.

133. Together, these comparisons of transaction costs of investing in business in Uganda indicate the returns to some of the measures taken by the Uganda Investment Promotion Board (IPB). The fact that Uganda has lower transaction costs in the majority of the *Doing Business* measures than the Sub-Saharan Africa region means that the country can actively pursue attracting private sector investment, domestically and internationally. However, similar to other countries in the region, the financial capital trap of the difficulties of re-deploying funds, either from an unsuccessful venture or from the sale of an enterprise, persists. Constraining financial capital in enterprises, for good and bad performing businesses, limits the energy that the investment capital can give to the overall economy.

Table 14. Business Environment Indicators for Uganda

	Uganda	SSA Average	OECD Average
Economic Characteristics (2003)			
Region	Sub-Saharan Africa		
Income Category	Low Income		
Gross National Income (GNI)	240	562	25773
Informal Economy (% GNI)	43.1	42.3	16.8
Population (million)	25.28	19.46	41.5
Starting a Business (2004)			
Number of Procedures	17	11	6
Time (Days)	36	64	25
Cost (% of Income per Capita)	131.3	223.8	8
Minimal Capital (% of Income per Capita)	0	254.1	44.1
Hiring and Firing Workers (2004)			
Difficulty of Hiring Index	0	53.2	26.2
Rigidity of Hours Index	20	64.2	50
Difficulty of Firing Index	0	50.6	26.8
Rigidity of Employment Index	7	56	34.4
Firing Costs (Weeks of Wages)	12	59.5	40.4
Registering Property (2004)			
Number of Procedures	8	6	4
Time (Days)	48	114	34
Cost (% of Property per Capita)	5.5	13.2	4.9
Getting Credit (2004)			
Cost to Create Collateral (% of Income per Capita)	11.9	41.8	5.2
Legal Rights Index	5	4.6	6.3
Credit Information Index	0	2.1	5
Public Credit Registry Coverage (Borrowers per USD 1 000 per Capita)	0	1.1	76.2
Private Bureau Coverage (Borrowers per USD 1 000 per Capita)	0	39.4	577.2
Protecting Investors (2004)			
Disclosure Index	2	2.1	5.6
Enforcing Contracts (2004)			

Number of Procedures	15	35	19
Time (Days)	209	434	229
Cost (% of Debt)	22.3	43	10.8
Closing a Business (2004)			
Time (years)	2.1	3.6	1.7
Cost (% of Estate)	38	20.5	6.8
Recovery Rate (%)	35.5	17.1	72.1

Source: IFC and World Bank (2005)

Foreign Direct Investment in Uganda

134. Uganda Investment Authority (UIA) was created by an Act of Parliament (1991) to attract, promote and facilitate investment. To achieve the goal of welcoming the private sector as economic development partners, the UIA markets Uganda to companies in Europe and the United States and is a one-stop facilitator for investors, domestic or foreign. Uganda's commitment to supporting investors can be gleaned from its persistence in reforming many areas of the investment climate.

135. Ugandan laws and regulations generally are investor-friendly. Foreign investors may form 100% foreign-owned companies and majority or minority joint ventures with local investors with no restrictions. The government permits foreign investors to acquire or takeover domestic enterprises and encourages greenfield investments. Ugandan courts generally uphold the sanctity of contracts, though the courts, at times, are subject to political pressure (US State Department, 2005).

136. The government plans to use a USD 24 million credit from the World Bank to set up export processing zones (EPZs) to stimulate investment and promote exports. Under draft legislation, investors locating in these zones would be provided with a variety of incentives, including tax holidays, duty drawbacks, and the removal of export taxes on goods produced within the EPZs.

137. The investment code guarantees that investors who have invested USD 500 000 can repatriate their investment and dividends and receive foreign exchange to pay debts incurred in the business. Investors have no trouble obtaining foreign exchange. However, few investors have reached the point where they wish to repatriate profits; most are reinvesting profits in their businesses in Uganda.

138. To favour new investment, the Income Tax Act of 1997 eliminated tax holidays for certain foreign investments, replacing them with differential depreciation allowances of variable benefit. In addition, losses may be carried forward indefinitely. The government will work with foreign investors to tailor incentive programs to specific projects. This ad hoc approach, which can include tax incentives, government subsidies or the provision of land, may benefit specific investors.

139. Uganda is a signatory to the Multilateral Investment Guarantee Agency (MIGA) of the World Bank and is a member of the International Center for the Settlement of Investment Disputes (ICSID). In 1965, the US and Uganda entered into an investment incentive agreement. An updated agreement was signed in 1998 by both parties but has yet to be ratified by the Ugandan government. In 2003, Overseas Private Investment Corporation (OPIC) signed a master guarantee agreement with Citigroup to establish a lending risk-sharing facility for local loans. In 2004, Export-Import (ExIm) Bank signed a similar master guarantee agreement with the Development Finance Co. of Uganda (DFCU) Bank.

140. Foreign direct investment into Uganda has increased, consistently over the 1994-2003 period. With inward FDI at just under USD 100 million in 1994, flows have almost tripled to just under USD 300 million by 2003 (Figure A4.1). The consistency of FDI inflows that characterizes Uganda's experience is not observed in any of the three other case study countries. In 2003, agriculture, forestry and fishing

accounted for almost 50% of the projects registered with UIA. Water and energy, followed by manufacturing recorded the second and third largest values.

Table 15. Value of Projects Licensed by the Uganda Investment Authority in USD in 2003

Agriculture, Forestry, and Fishing	159,901,446
Construction	15,440,000
Financial Services	3,672,000
Manufacturing	39,022,200
Mining and Quarrying	8,431,000
Other Business Services	22,754,000
Professional Services	13,574,000
Real Estate	150,000
Social Services	10,197,970
Tourism	12,852,000
Trade	2,000,000
Transport, Communications, and Storage	13,903,583
Water and Energy	53,017,583
Total	**354,915,199**

NB: The values quoted above should not be relied upon for any investment decision. The figures provided by the UIA are highly variable and inconsistent, both year and by sector. According to the UIA, the values tracked are only for projects listed. No investors provide periodic updates after the initial registration. Historically, actual investment has trailed planned investment totals by a factor of five.

Source: US State Department (2005)

Example of Foreign Direct Investment in Uganda: Amfri Farms

141. Amfri Farms Ltd. is family business owned and operated by Mr Amin Shivji, a trained engineer, together with his wife and daughter. Amfri Farms is a different story of FDI because the firm is based on capital that was attached to the movement of natural persons. In 1972, former President Idi Amin threatened Ugandans of Asian heritage and nationalized their businesses, and Mr Shivji immigrated to Canada. Upon returning to Uganda in 1990, Mr Shivji reclaimed his farm and used the capital that he raised in Canada to develop Amfri Farms.

142. The fruit business of Amfri Farms leverages Uganda's advantage of low prevalence of fertilizer use and uses organic fruits for the dried and fresh exports through African Organic. The vanilla export business is a more recent addition to Amfri Farm operations. Amfri Farms is certified by the Institute for Marketecology (IMO) Control-Switzerland in compliance with EEC Regulation 2092/91. The Company was the first to be certified dealing in organic produce from Uganda.

143. The offices and packing shed are situated in Kampala, Uganda. The farm is located 85 km from Kampala, in Luwero and has 430 acres of certified land and is equipped with a packing house and a produce cooler. The predecessor to Amfri was Suntrade and Consulting INT (U) LTD that started in 1990 with 25 individual out-growers and co-operative farms. Today, the company works with over 100 out-growers. Based on the principles of free trade, Amfri's pineapple farmers purportedly received over USD 4 500 as a premium in 2004. Amfri Farms absorbs the cost of the annual inspection and auditing visit by IMO certification officials from Switzerland who ensure compliance with the regulations and standards, on every farm that delivers produce to African Organic.

144. African Organic concentrates on ensuring quality control of its export products through:

1 Certification by IMO to process and market organic products in compliance with the Regulation (EEC) No. 2092/91.

2 Compliance with the recently established national US Organic Program, USDA, AMS 7CFR Part 205 National Organic Program. Amfri Farms was among the first companies in Uganda to participate in the USDA Organic Program.

3 Advising, supporting and continually training out-grower farmers in methods and techniques of Organic/Sustainable farming and certification.

4 Continuous development of the Company owned farm in Organic production and a pack-house facility at the farm.

145. Amfri Farms is one of the most respected dried fruit producers and exporterd in Uganda. A solar drying plant consisting of 50 driers is located at the farm in Luwero. The fruits are peeled, sliced and solar dried while maintaining the standards of hygiene of the personnel, the equipment and the facilities. All dried products are organic and are preservative free. Warm air-drying has been introduced to shorten the drying process through all weather conditions.

146. African Organic grows and exports the following fresh products: fresh pineapples (organic and conventional), fresh apples and bananas (organic and conventional), ginger (fresh) (organic and conventional), passion fruits (seasonal) (organic and conventional), baby aubergines, okra, hot pepper (conventional), mangoes, avocadoes, and papaya (organic). Amfri Farms export to Canada, Denmark, Germany, Italy, Lebanon, Netherlands, Norway, Poland, Sweden, Switzerland, United Kingdom and United States.

Box 6. Observations from Africa: General Challenges and Opportunities for African Firms

Multilateral and regional trade agreements have recently targeted formal trade barriers particularly tariffs. However, non-tariff trade measures are increasingly a source of uncertainty, especially when they emerge from industry rather than from governments. For example, in an effort to bolster consumer confidence, the European food retail industry decided that traceability was the solution, the implicit assumption being that all food value-chain participants, in Europe or elsewhere, have the financial and technical wherewithal to comply. In many OECD countries, food retail industry initiatives are communicated through different channels than trade initiatives. In the integrated, global markets that continue to emerge, international trade and domestic industry coordination within OECD countries is needed; that is, policy coherence not only within government but also across the government and industry. Without it, the action of one department/institution may nullify actions of the other department/institution.

In emerging markets, especially in Africa, there are institutional gaps in connecting agriculture to finance – a critical bridge for catalyzing the shift from an agricultural production to agribusiness focus. Institutions such as warehouse receipting systems, commodity exchanges, financing structures focused on the value-chain, at commercial rates, serve to integrate agriculture in other (now liberalised) financial capital markets; yet this tends to be lacking in Africa.

Entrepreneurs are instrumental in market economies because they provide macroeconomic flexibility by absorbing the unemployed labour and are the best incubators for new ideas for the local market. Privatisation will attract large sums of financial capital but is a finite source for FDI. For FDI to move from varying widely to a constant flow, fostering entrepreneurship is pivotal. Today, the focus of FDI is on partnerships that enables technology and management knowledge transfer, and can increase export earnings for the FDI host country. Greenfield FDI projects in developing countries/emerging economies are more difficult to finance commercially. Economic development funding is declining and the business skill set in these institutions is not their strong suit. Entrepreneurial businesses are the pipeline for tomorrow's FDI flow.

ANNEX 1. FOREIGN DIRECT INVESTMENT (FDI): DEFINED

Foreign direct investment (*FDI*) reflects the objective of obtaining a lasting interest by a resident entity in one economy ("direct investor") in an entity resident in an economy other than that of the investor ("direct investment enterprise"). The lasting interest implies the existence of a long-term relationship between the direct investor and the enterprise and a significant degree of influence on the management of the enterprise. Direct investment involves both the initial transaction between the two entities and all subsequent capital transactions between them and among affiliated enterprises, both incorporated and unincorporated (OECD 1996, p, 7-8.)

Transnational corporations (TNCs) are incorporated or unincorporated enterprises comprising parent enterprises and their foreign affiliates (UNCTAD, 2003 p. 231).

A *joint venture* involves share-holding in a business entity having the following characteristics; (i) the entity was established by a contractual arrangement (usually in writing) whereby two or more parties have contributed resources towards the business undertaking; (ii) the parties have joint control over one or more activities carried out according to the terms of the arrangements and none of the individual investors is in a position to control the venture unilaterally (UNCTAD, 2006).

A *parent enterprise* is defined as an enterprise that controls assets of other entities in countries other than its home country, usually by owning a certain equity capital stake (UNCTAD, 2003 p. 231).

A *foreign affiliate* is an incorporated or unincorporated enterprise in which an investor, who is resident in another economy, owns a stake that permits a lasting interest in the management of that enterprise (an equity stake of 10 per cent for an incorporated enterprise or its equivalent for an unincorporated enterprise) (UNCTAD, 2003 p. 231).

FDI flows comprise capital provided (either directly or through other related enterprises) by a foreign direct investor to an FDI enterprise, or capital received from an enterprise by a foreign direct investor. FDI has three components: equity capital, reinvested earnings and intra-company loans (UNCTAD, 2003 p. 231).

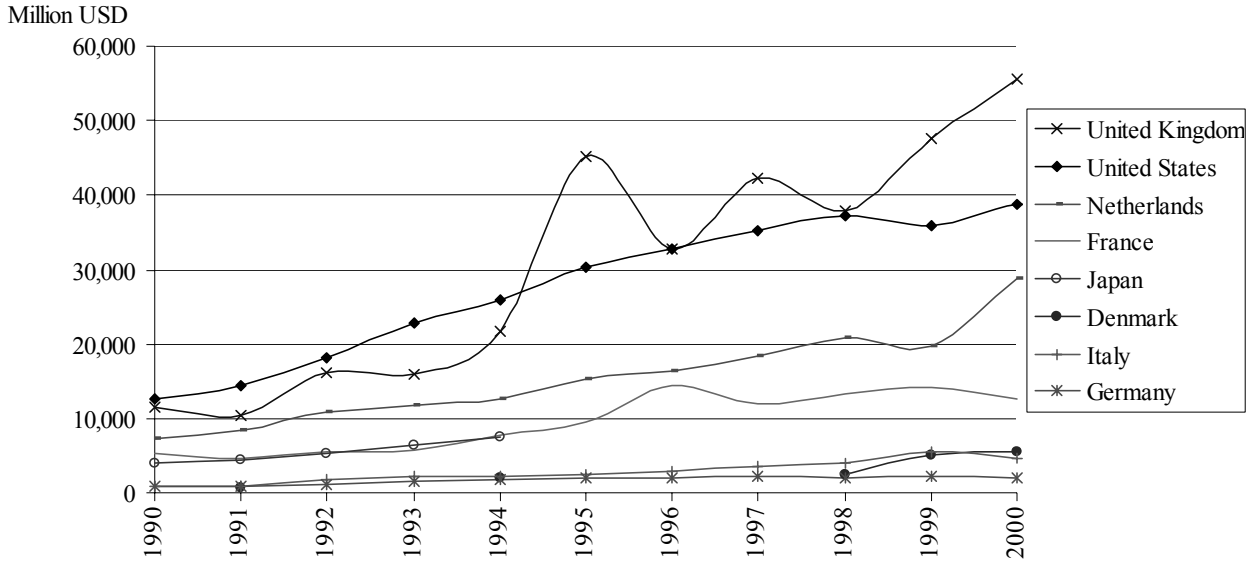
FDI stock is the value of the share of their capital and reserves (including retained profits) attributable to the parent enterprise, plus the net indebtedness of affiliates to the parent enterprise (UNCTAD, 2003 p. 232).

Host country is the country that receives FDI.

Home country is the country from which firms send out FDI.

ANNEX 2. FIGURES OF OECD FDI IN THE FOOD SECTOR

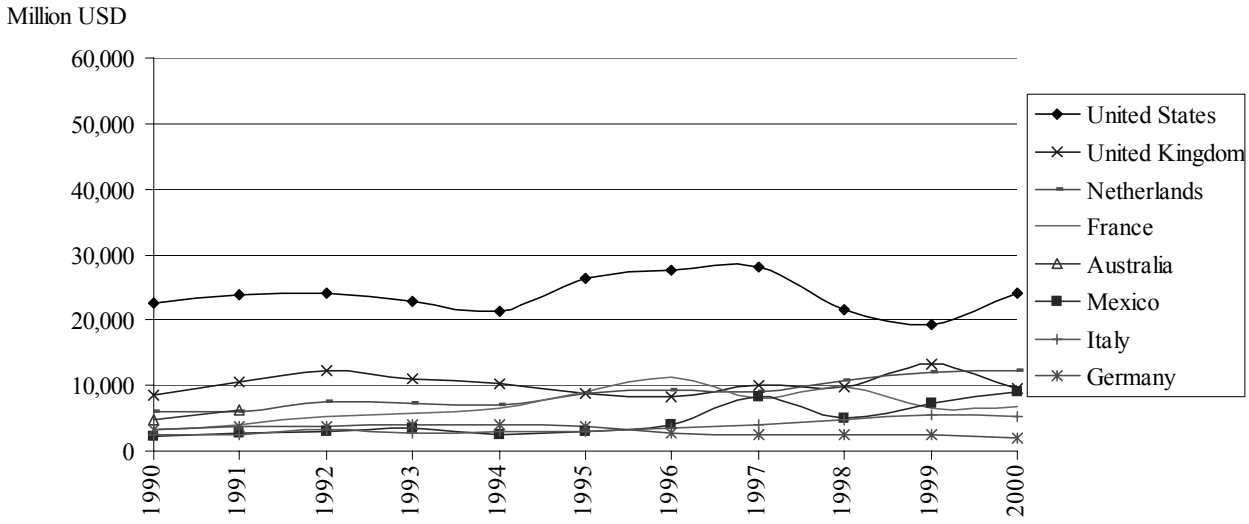
Figure A2.1 Outward Stock FDI of the Food Sector



a. The current year is 2000. Data for Japan are not available beyond 1994. Data for Denmark is available for only 1991, 1994, and 1998-2000.

Source : OECD (2004d)

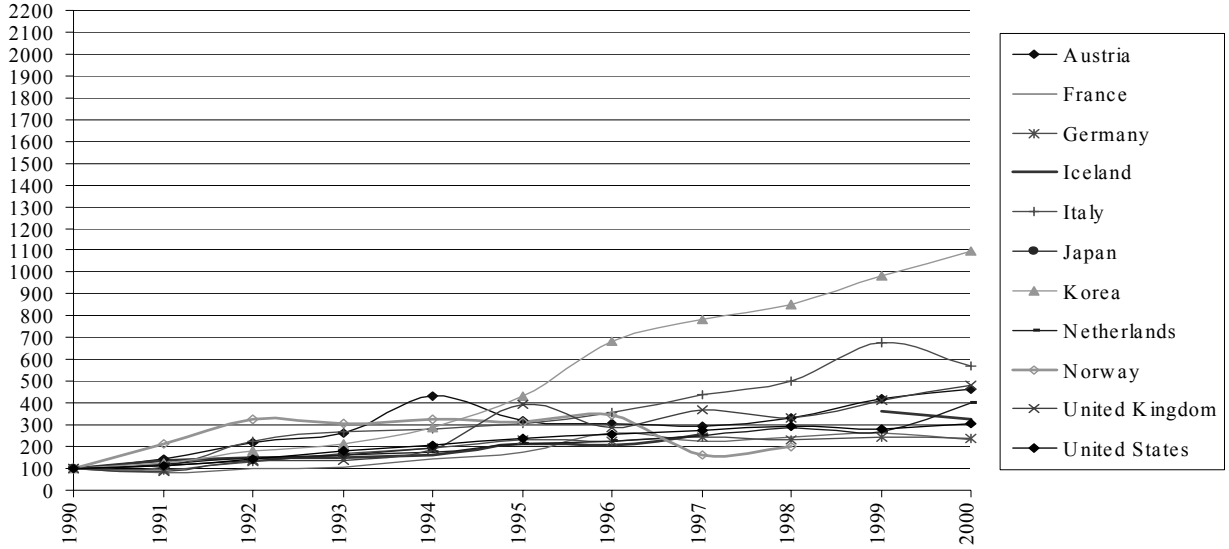
Figure A2.2 Inward Stock FDI of the Food Sector



a. The current year is 2000.

Figure A2.3 Relative Outward Stock for the Food Sector

Base Year 1990=100

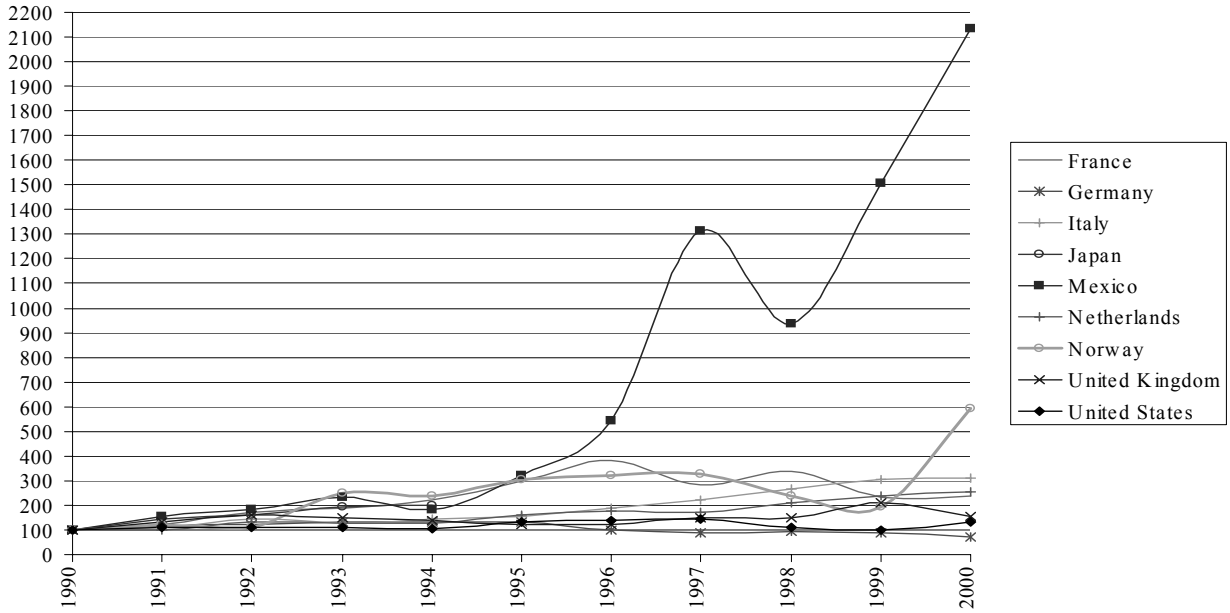


a. The data for Iceland 1998 Norway 1999 and 2000 are not available.

Source : OECD (2004d)

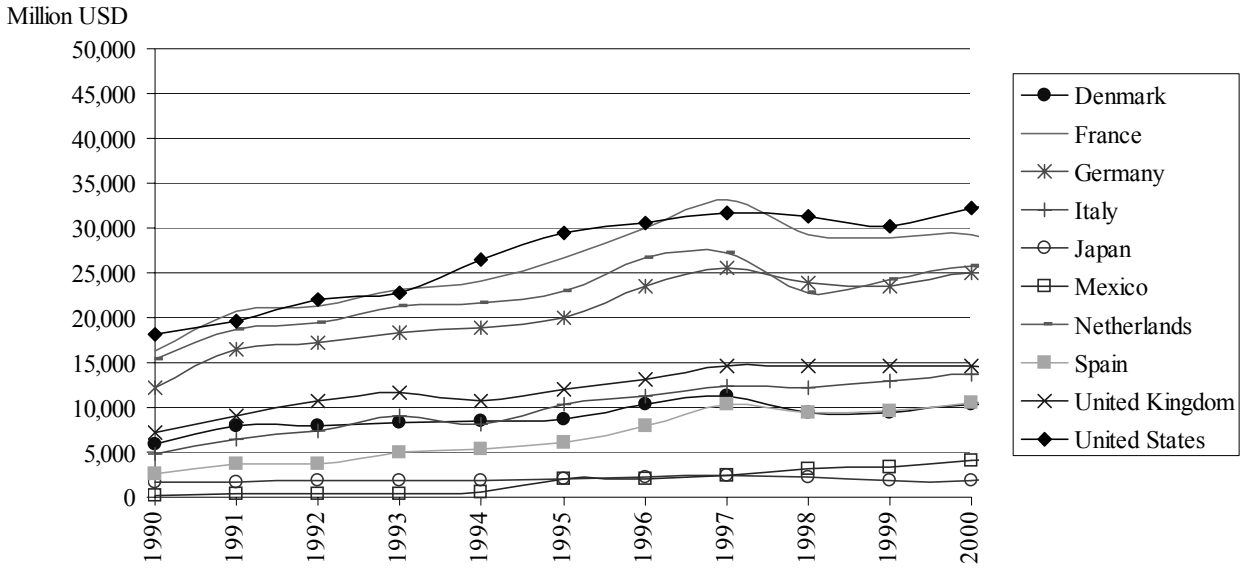
Figure A2.4 Relative Inward Stock for the Food Sector

Base Year 1990=100



Source : OECD (2004d)

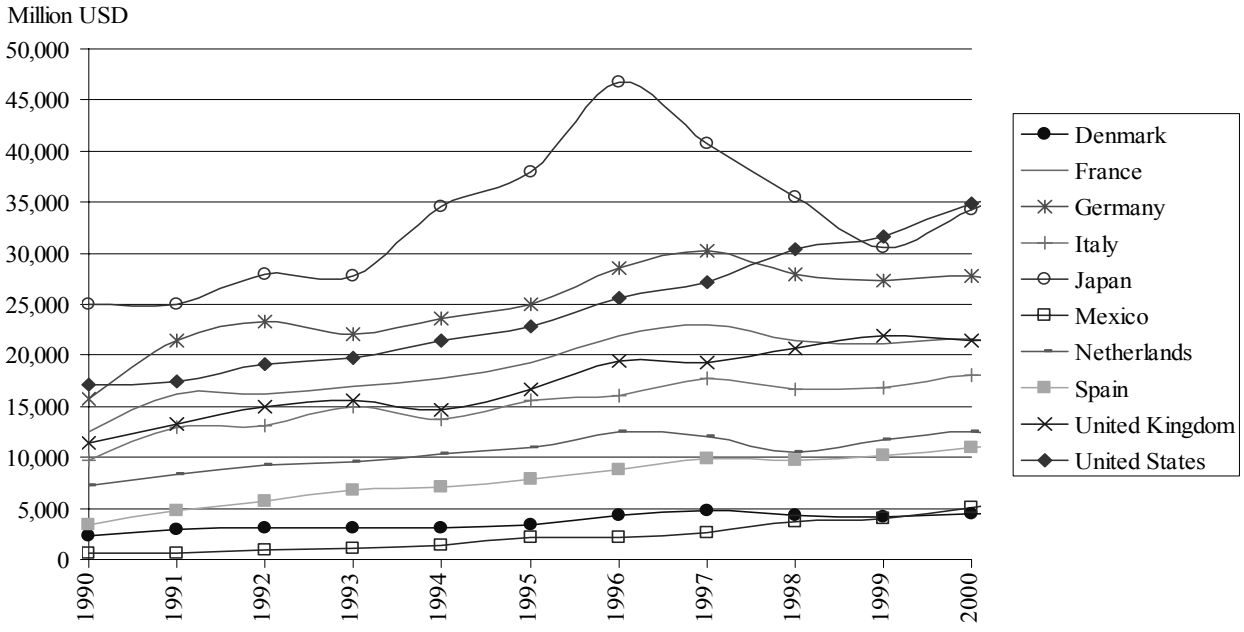
Figure A2.5 Exports of the Food Sector



a. The current year is 2000.

Source : OECD (2004e)

Figure A2.6 Imports of the Food Sector



a. The current year is 2000.

Source : OECD (2004e)

ANNEX 3. MODELLING REASONING AND SPECIFICATIONS OF FDI IN OECD COUNTRIES

Empirical Modelling

The Relationship between FDI and Trade

The literature on FDI and trade is diverse, offering many theoretical frameworks to approach the questions on FDI and trade. The economics literature points to several relationships between FDI and trade (see Figures A3.1 and A3.2). In this mostly empirical study, we consider the relationship between FDI, trade and trade policies. We consider this relationship for both inward investment and imports and outward investment and exports. A positive relationship between the two implies that, FDI promotes exports and/or exports promote FDI. A negative relationship indicates that FDI serves as a substitute for exports and/or vice versa.[31] Rarely does the literature suggest that no relationship exists.

For this analysis, we hypothesised that FDI and trade move in the same direction. This hypothesis is mainly based on anecdotal evidence suggesting that there is an evolutionary process when entering another market (Weatherspoon, Cacho and Christy (2001); Vaughan *et al*. (1994)). The FDI data used in the econometric modelling is the stock of FDI in the food sector which includes manufactured food products, beverages and tobacco. In this evolutionary process, as a firm moves closer to FDI, exports are less of a source of serving the market. However, the total exports may maintain or increase because of intra-industry trade that provides inputs. Additionally, the change in the trade/investment strategy for one product line may permit the expansion of trade of other products.

Another reason for the hypothesised positive relationship is that firms simply are not limited by an either/or approach to servicing a market. A firm may find it more appropriate to service a market with some products produced at home and then export the products while other products are best produced through FDI.

The Relationship between Factors of FDI and Trade

Moving from the central relationship, the effects of the different factors on FDI and trade are important relationships to model. We use an investment model that is influenced by Barrell and Pain (1996); Chakrabarti (2003); Gopinath, Pick and Vasavada (1999); among others. We use a gravity model to explore these factors for the bilateral trade data. The approach is chosen for the trade flows model because of its connection to theoretical models (Bergstand 1985, Bergstand 1989 and Bergstand 1990) and its popularity in use (Otsuki, Wilson and Sewadeh (2001a and 2001b); Zahniser, *et al*. (2002); among others).

31 . Please note that these are not normative statements. The fact that the relationship between FDI and trade is positive (negative) is not to connote a desirable (undesirable) outcome or result. The positive (negative) relationship represents the sign on the coefficient in a model.

Data

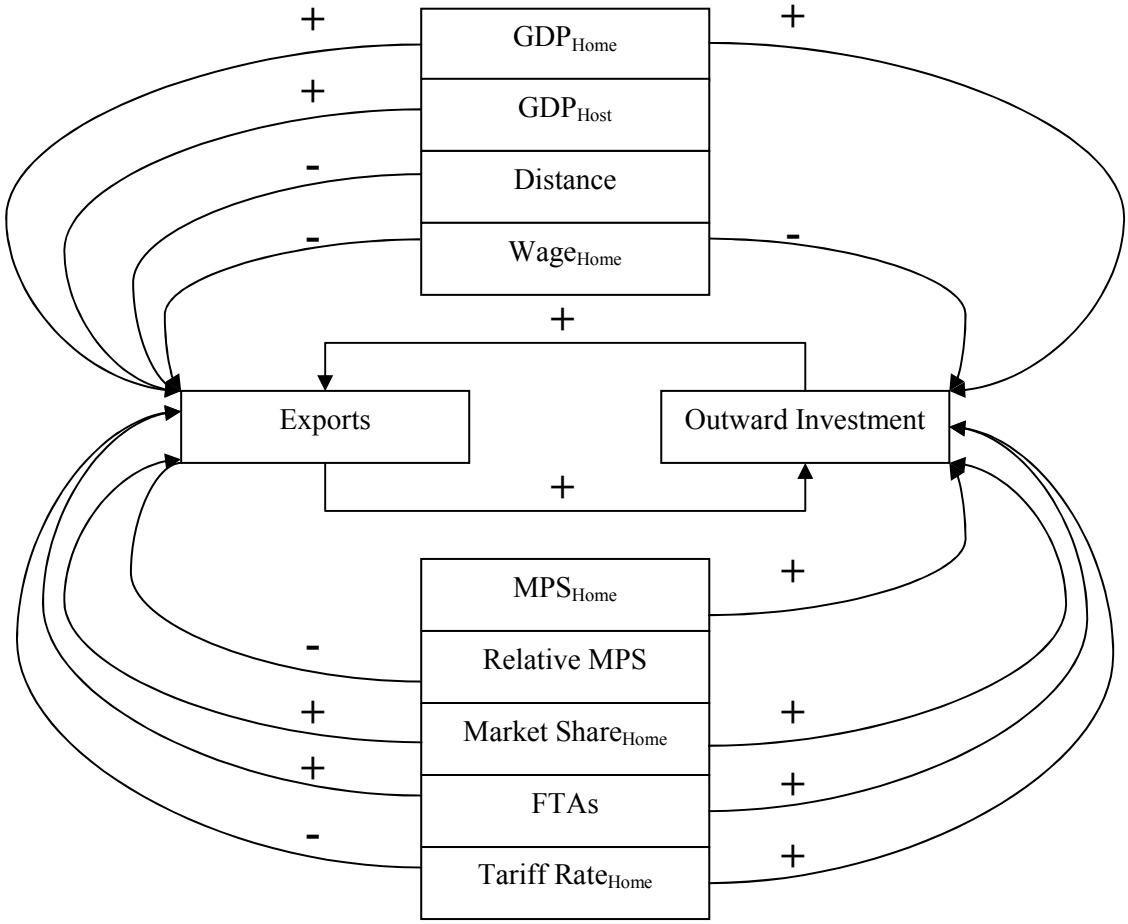
The World Integrated Trade Solution (WITS) data set provides data on trade flows in value of trade and tariffs using the ISIC Rev. 3 classification. The data are the bilateral trade and tariffs (applied and bound rates) of manufactured food and beverage products and manufactured tobacco products (divisions 15 and 16 of ISIC Rev. 3). These data only reflect trade amongst OECD countries. The OECD Structural Analysis (STAN) data set provides an assortment of industry level data such as value of production, exports and imports (the export and import data reflect total trade not just trade amongst OECD countries). The data set covers all OECD countries except for Iceland, Switzerland, and Turkey. The STAN data are reported for industries, and they are based on ISIC Rev. 3. The FDI data set is also based on ISIC Rev. 3. These data are from the OECD International Direct Investment Statistical Yearbook 2003. These data are of total FDI and do not reflect bilateral investments. All of the price data (trade, investment, GDP, etc.) are in constant USD base year 2000. The same price deflator, the GDP deflator, is used for all of the data. The market price support (MPS) data is from the OECD Agricultural Directorate, the economic data (GDPs and exchange rates) are from the OECD Economic Directorate, and the distance and border data for the gravity models are from CEPII. The data cover the years 1990 to 2000. However, there are missing observations. Some observations for MPS were negative. Because the natural log transformation, negative values were omitted. Please note that less than one percent of the original data base is lost through this deletion.

Preliminary Models

Theoretical Reasoning

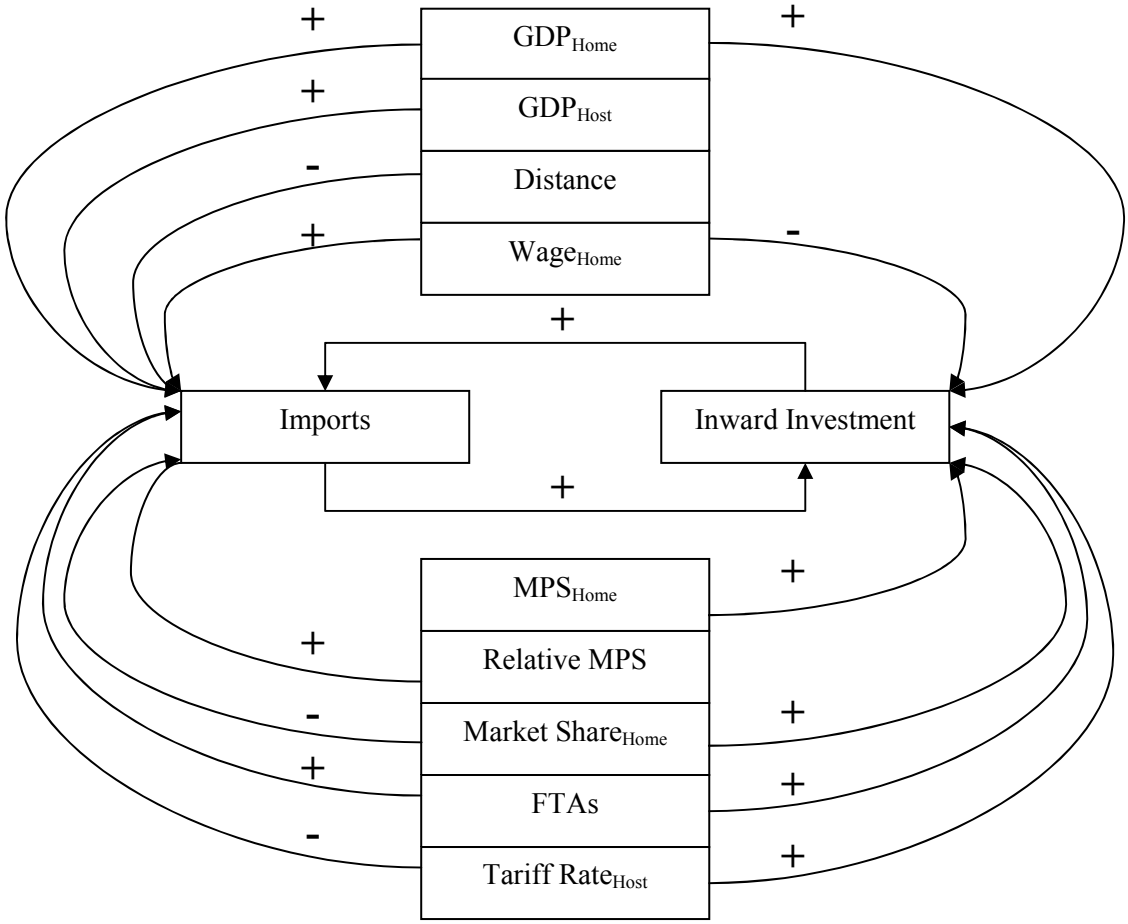
While we will not build up the theoretical model for this mostly empirical approach, we do present the expected results as can be seen in Figures A3.1 and A3.2. For the export model, we expect that outward investment is positively related to exports. That is there is a complementary relationship between FDI and trade. We expect that the GDPs of the trading partners will be positive because the larger the economy the more the economy will trade. We expect that the distance variable is negative. Distance between the trading partners is a proxy for transport costs. The relative MPS is the ratio of the MPS of the home country to its partner. We expect this variable to have a negative relationship with exports because the MPS represents, in part, the extra cost of domestic agriculture. If the MPS of the home country is larger than the MPS of its partner, one would expect that the food product is relatively more costly than the product produced in the importing country. Market share is relative domestic production to domestic consumption in the exporting country. We expect this variable to be positive. This variable represents the competitiveness of the domestic market. The more competitive the market the more the country will export. The market share variable is not based on the bilateral trade data of the dependent variable; rather, the data are from total trade with the world. Membership in a RTA (or non-membership) would be beneficial (detrimental) to exports if both partners are member of the RTA. Therefore, we assume that non-membership in the EU or NAFTA has a negative effect on exports.

Figure A3.1 Hypothesised Relationships between Outward FDI, Exports and Related Factors



For the import model (see Figure A3.2), we expect similar results except in two instances: relative MPS and market share. Relative MPS should be positive because as the MPS of the importer is larger than the MPS of the exporter, one would expect that the importer will import more food products because of lower cost of production in the exporting country. The market share variable should have a negative sign because the more competitive the market, the harder it is for the partner to penetrate the market of importing country. One additional difference is the import model includes the inward investment. To continue with the complementary relationship between trade and investment, we assume that inward investment is positive.

Figure A2.2 Hypothesised Relationships between Inward FDI, Imports and Related Factors



Model Specification and Statistical Concerns

We begin with a simplified model of trade that incorporates investment (see Table A3.1). The basic gravity model has bilateral trade flows regressed against the GDPs of the bilateral partners and distance. Often, gravity models include other variables such as membership in a RTA. All of the continuous variables are in log form. In the simplified model we also include relative MPS and investment stock, for the export model.

The literature suggests that FDI and trade are related so including FDI in a trade model requires investigating whether FDI is an endogenous variable in the trade equations. Therefore, the first step is to test for an endogenous relationship. For the export equation, we discovered that outward investment is endogenous, and for the import equation we discovered that inward investment is endogenous. Because the data are in panels, we had to decide on the best approach: a pooled model or a panel data approach. We estimated both types, and we used the Hausman specification test to determine if the fixed or random effects model is the best. For exports and imports the best models are presented in the tables.

Results

147. The best specification for the export model is the pooled model with robust standard errors. The R^2 is 0.65. All but two of the variables are statistically significant, and most variables have the expected sign except for relative MPS ($MPS_{Relative}$). We receive confirmation that investment complements trade. By the Hausman test, the random effects model is the better model of imports. The R^2 is 0.56. All of the variables are statistically significant. Only inward investment was not the expected sign.

Table A3.1 Preliminary Models of Trade and FDI

Dependant / Independent	**ln(*Exports*)** IV Pooled Model	**ln(*Imports*)** IV Random Effects
ln(*Outward Investment*)	0.23***[a]	
	(0.072)	
ln(*Inward Investment*)		-0.28*[a]
		(0.16)
ln(GDP_{Home})	0.43***	0.97***
	(0.085)	(0.13)
ln(GDP_{Host})	0.62***	0.22***
	(0.043)	(0.030)
ln(*Distance*)	-0.84***	-0.67***
	(0.072)	(0.066)
ln($MPS_{Relative}$)	0.043	0.061**
	(0.063)	(0.029)
Not EU or NAFTA Dummy	-0.77***	-0.44***
	(0.15)	(0.062)
Constant	3.036	3.43***
	(0.86)	(0.016)
σ_μ		1.17
σ_ε		0.35
ρ		0.92
R^2	0.65	0.56
n	2055	1602

a. Endogenous variable

NB: Significance at ***=1% level, **=5% level, and *=10% level. The standard errors are in parentheses below the estimated coefficient. RE indicates a random effects model. The pooled model has robust standard errors. IV indicates the use of instrumental variables to correct for endogenous variables.

The Full Model Specification

Theoretical Reasoning

In the theoretical reasoning for the preliminary model, we discussed most of the hypotheses for the export and import modelling. In the preliminary modelling we did not include the effect of wages, market share and tariffs. The full model includes wages because a cost of production variable may have a substantial effect on the export and import capabilities of country. As the cost of production increases such as is measured by wages, the ability to export decreases, and the demand for imports increases. Therefore we expect that wage is negatively related to exports and positively related to imports. Tariffs represent another cost of trading. Two tariff data are available: the bound rate and the applied rate. We use the simple average of the tariffs for division 15 and 16 ISIC Rev 3. We expect tariffs will have a negative expect on both exports and imports.

In the investment models, we attempt to address the complement or substitution relationship from a different direction. The expectation is that the results of the trade and investment models are consistent, reflecting that trade and investment are complements. Therefore, we hypothesise that for the inward investment model imports are positively related. For the outward investment model, exports are

hypothesised to be positively related. Like the export model, we expect that the GDP, the measure of the size of the market, will positively affect outward and inward investments. In a bilateral model with the assumption of a complementary relationship between trade and investment, distance will have a negative effect on investment because investment and trade follow one another. However, the data are not bilateral so this variable cannot be used in the model.[32]

For outward investment, costs such as wages and the MPS will have a negative effect because firms are less interested in local markets as cost of production increases. Additionally higher production costs will discourage exports because of the complementary relationship between exports and outward investment. Market share will have a positive affect on outward investment because a high market share encourages investment in other markets. Countries that are not a member of the EU or NAFTA will have lower outward investments because of the absence of links and improved market access to other members that the EU and NAFTA afford. Tariff jumping is assumed to occur; therefore, the outward investment will increase with tariff rates.

Inward investments will decline in the presence of high costs of production such as high wages and MPS because such costs discourage the placement of foreign affiliates in high cost areas. Non-membership in NAFTA or the EU should have a negative effect on inward investment because of the limited access to the larger markets that membership in the EU or NAFTA brings. Also tariffs will have a positive effect on inward investment to overcome tariffs.

Model Specifications and Statistical Concerns

We take the approach that to understand FDI more fully, both inward and outward FDI must be analysed. Therefore, four equations with the dependent variables inward investment, imports, outward investment and export are estimated. Handling each equation separately is reasonable given that the trade data are bilateral while the FDI data are total and not bilateral.

As mentioned in the preliminary models, the trade and FDI data are potentially endogenous. Therefore, we test the data for endogenous variables. For the outward investment, the tests indicated that market share is also an endogenous model. For the export model, the test result for an endogenous variable for outward investment is statistically significant at the 9% p-value; therefore, the result is a borderline case. The test indicates that market share is an endogenous variable. We estimated the model with and without the instrumental variable (IV) correction, and we decided that the better model is the IV model, which assumes that outward investment and market share are endogenous variables.

To test the robustness of the results we used the applied and bound tariffs. We use the Hausman test to determine whether the fixed or the random effects model is the best model. In all the cases, the Hausman test provides evidence that the random effects model is the better model; however, the outward and inward regressions revert to the simple pooled model. Many of the studies in the review use the fixed effect model. For the export model the random effects model is presented because of the results of the Hausman test. Therefore, care should be taken in reviewing the panel model of exports. The results of the models are presented in Tables A3.2 and A3.3 and discussed in the main text.

32 . Handy and Bamford (2000) offer a counter argument. They state "In some cases, transportation costs relative to product value limit the distance over which food products can be economically transported." (Handy and Bamford, 2000 p. 59) Given their argument, the distance may increase investment.

Table A3.2 Exports and Outward Stock

Dependant / Independent	(1) ln(*Outward Investment*) IV Model	(2) ln(*Outward Investment*) IV Model	(3) ln(*Exports*) IV Panel RE Model	(4) ln(*Exports*) IV Panel RE Model
ln(*Outward Investment*)			0.021[a]	0.040[a]
			(0.13)	(0.13)
ln(*Exports*)	-1.65[a]	-1.59*[a]		
	(0.93)	(0.86)		
ln(GDP_{Home})	1.95***	1.94***	0.74**	0.69*
	(0.48)	(0.40)	(0.34)	(0.34)
ln(GDP_{Host})			0.32***	0.30***
			(0.029)	(0.029)
ln($Wage_{Home}$) [b]	0.13	0.090	-0.20	-0.16
	(0.12)	(0.13)	(0.26)	(0.27)
ln(MPS_{Home})	0.75*	0.65		
	(0.41)	(0.37)		
ln($MPS_{Relative}$)			0.023	0.015
			(0.024)	(0.027)
ln(*Market Share*$_{Home}$)	16.12*[a]	15.78**[a]	3.18***[a]	3.21***[a]
	(7.57)	(6.45)	(0.79)	(1.00)
ln(*Distance*)			-0.60***	-0.63***
			(0.084)	(0.081)
ln(*Tariff Rate*$_{Host}$) [0]	0.0016	0.022	-0.030**	-0.0053
	(0.038)	(0.041)	(0.013)	(0.0048)
Not EU or NAFTA Dummy	-2.85***	-3.076***	-0.22	-0.47***
	(0.85)	(0.80)	(0.17)	(0.15)
Constant	2.57	-2.061	-11.59	4.52**
	(5.073)	(4.97)	(1.37)	(2.40)
σ_μ			0.93	0.94
σ_ε			0.22	0.22
ρ			0.95	0.95
R^2	0.58	0.60	0.66	0.68
n	109	106	924	921

a. Endogenous variable

b. The wage for regressions 1 and 2 is the labour costs of employees in the food industry while for the other regressions the wage of these employees.

c. The tariff is the simple average applied tariff rate for food and tobacco; the two tariffs are summed. For regressions 1 and 3, the tariff is the simple average bound tariff rate for food and tobacco.

NB: Significance at ***=1% level, **=5% level, and *=10% level. The standard errors are in parentheses below the estimated coefficient. RE indicates a random effects model. The pooled model has robust standard errors. IV indicates the use of instrumental variables to correct for endogenous variables. Regressions 1 and 2 are grouped by year, and regression 3 and 4 are grouped by country pairs.

Table A3.3 Imports and Inward Stock

Dependant / Independent	(5) ln(*Inward Investment*) IV Model	(6) ln(*Inward Investment*) IV Model	(7) ln(*Imports*) Panel RE Model	(8) ln(*Imports*) Panel RE Model
ln(*Inward Investment*)			0.18***	0.0069
			(0.063)	(0.028)
ln(*Imports*)	0.37**[a]	0.36**[a]		
	(0.16)	(0.15)		
ln(GDP_{Home})	0.22**	0.22**	1.37***	0.13***
	(0.10)	(0.094)	(0.26)	(0.032)
ln(GDP_{Host})			0.41***	0.79***
			(0.020)	(0.12)
ln($Wage_{Home}$) [b]	0.12	0.13	-0.77***	-0.025
	(0.10)	(0.10)	(0.27)	(0.13)
ln(MPS_{Home})	-0.79***	-0.62***		
	(0.17)	(0.13)		
ln($MPS_{Relative}$)			0.38***	0.0084
			(0.049)	(0.026)
ln(*Distance*)			-1.11**	-0.79***
			(0.043)	(0.097)
ln(*Tariff Rate*$_{Host}$) [c]	0.058**	0.064**	0.013	-0.020*
	(0.021)	(0.027)	(0.010)	(0.012)
Not EU or NAFTA Dummy	-0.57**	-0.52**	-0.76***	-0.34**
	(0.22)	(0.18)	(0.17)	(0.14)
Constant	-2.17	-2.075	2.41**	5.79***
	(1.041)	(1.03)	(1.13)	(0.84)
σ_μ			0.19	1.055
σ_ε			0.86	0.18
ρ			0.048	0.97
R^2	0.67	0.67	0.70	0.64
n	121	119	900	883

a. Endogenous variable

b. The wage for regressions 1 and 2 is the labour costs of employees in the food industry while for the other regressions the wage of these employees.

c. The tariff is the simple average applied tariff rate for food and tobacco; the two tariffs are summed. For regressions 6 and 7, the tariff is the simple average bound tariff rate for food and tobacco.

NB: Significance at ***=1% level, **=5% level, and *=10% level. The standard errors are in parentheses below the estimated coefficient. RE indicates a random effects model. The pooled model has robust standard errors. IV indicates the use of instrumental variables to correct for endogenous variables. Regressions 5 and 6 are grouped by year, and regression 7 is grouped by country pairs, while regression 8 is grouped by importer.

ANNEX 4. BACKGROUND MATERIAL FOR FOUR COUNTRY CASES

A. GHANA

Since independence in 1957, Ghana has a level of political maturity, which neutralizes political risk in investor decision making. Ghana successfully held free and fair, multi-party elections in December 2004 -- for the fourth time since the new constitution was approved in 1992.

Located in Western Africa, bordering the Gulf of Guinea, between Ivory Coast, Togo, and Burkina Faso, Ghana's total land size is 239 460 sq km of which 8 520 sq km is water, including Lake Volta. The major cities are in the south, Accra, the capital; in the centre, Kumasi; and in the north, Tamale. Arable land and land dedicated to permanent crops cover 16.3% and 9.7%. Because the irrigated arable land is only 110 sq km, much of the agricultural production is not irrigated and depends on rainfall. Ghana natural resources are gold, timber, industrial diamonds, bauxite, manganese, fish, rubber, and hydropower.

The population of Ghana is 20.8 million and nearly 40% of the population is less than 15 years of age. The population is estimated to increase 1.36% annually.[33] Ghana's history of a good educational system does not preclude it from ranking among the lowest income countries in Africa in per capita income terms. The gross national income (GNI) per capita is USD 270. This low GNI combined with a young population means that there is tremendous demand for jobs and public services (World Bank, 2004) .

General Economy

Agriculture continues to play a pivotal role in Ghana's economy. Agriculture accounts for approximately 35% of GDP and employs 60% of the work force. Economist Intelligence Unit (EIU) (2005) estimates GDP for 2004 to be USD 8 200 million (Ghana Cedi (GHC) 75 900 million), reflecting a real annual growth rate of 5.4% over 2003 which beat the real GDP growth target by two percentage points. Commodities continue to anchor Ghana's exports. (Table 1) Gold, cocoa beans and products, and timber and timber products are the principal exports of Ghana. An increase of 48% in cocoa production in the 2003/04 season explains some of the above target GDP growth in 2004. This is the second consecutive year of marked increase in cocoa production. Tourism is the standout performer in the service sector. Recent government investments, such as expansion of Kotoka International Airport in Accra and more general improvement in transport, trade and government services strongly support tourism gains.

Ghana's trade deficit persists. (Table A4.1) The significant level of imports of non-oil products presents a tremendous challenge to the Ghana's government gaining control of the economy, especially in today's open capital market era because the adverse terms of trade for commodities relative to manufactured goods

33 . This estimate explicitly takes into account the effects of excess mortality due to AIDS; this can result in lower life expectancy, higher infant mortality and death rates, lower population and growth rates, and changes in the distribution of population by age and sex than would otherwise be expected (July 2004 estimate).

means that strong import demand utilizes foreign exchange without generating the much needed multiplier effect through job growth and paying for services. The Ghanaian cedi continues to decline in value relative to the US dollar and the euro. Inflation is a persistent issue. Increases in primary processing of cocoa and other agricultural produce, that is slowly coming on-stream, are instrumental in any efforts to close the trade gap – either by increasing export earnings or by increasing availability in the domestic market of imported finished goods.

Table A4.1 Economic Structure and Annual Indicators of Ghana

Macroeconomic Figures					
	2000[a]	2001[a]	2002[a]	2003[a]	2004[b]
GDP at market prices (GHC million)	27200	38100	48900	65200[b]	75900
GDP (USD million)	5000	5300	6200	7500[b]	8400
Real GDP Growth (%)	3.7	4.2	4.5	5.2[b]	5.4
Population million	19.6	20.0	20.5	20.9	21.4
Exports of Gods (USD million)	1936.3	1867.1	2015.2	2562.4	3080.8
Imports of Goods fob (USD million)	2766.6	2968.5	2707.0	3276.1	3908.2

International Trade Figures			
Principle Exports 2003	USD million	Principle Imports 2003	USD million
Gold	830.1	Non-oil	2406.4
Cocoa beans & products	802.2	Oil	562.9
Timber & Products	174.7		
Main Destinations of Exports 2003[c]	% of Total	Main Origins of Imports 2003[c]	% of Total
Netherlands	11.2	Nigeria	21.2
United Kingdom	10.8	China	8.6
France	7.8	United Kingdom	6.7
Germany	6.2	Ivory Coast	5.8
Japan	5.2	United States	5.6

a. Actual

b. Economist Intelligent Unit estimates.

c. Based on partners' trade returns; subject to a wide margin of error.

Source: EIU (2005)

In addition to exporting gold, cocoa and timber, Ghana exports of tuna, bauxite, aluminium, manganese ore, and diamonds are notable. Together, these commodities accounted for over 70% of Ghana's USD 2562.4 million estimated exports in 2003. (Table 1) The majority of Ghana's exports are delivered to Europe. Commodity trade with developing countries is integral to European economic history. Specifically, Ghana's major export partners are Netherlands, UK, France, Germany, and Japan based on 2003 data.

As a non-oil developing country, Ghana's import profile is typically dominated by capital equipment, petroleum and foodstuffs. In 2003, approximately 50% of Ghana's USD 3 276.1 million in imports was supplied by Nigeria (21.2%), China (8.6%), UK (6.7%), Ivory Coast (5.8%) and US (5.6%).

On 13 July 2004, Ghana completed the debt-relief initiate for Heavily Indebted Poor Countries (HIPC) by the International Monetary Fund (IMF) and the World Bank. After deciding to participate in the HIPC initiative in February 2002, the Ghanaian government has been implementing policies that concur with the poverty reduction and growth facility (PRGF) requirements agreed with donors, which expire in May 2006. According to the EIU, there is a risk that debt relief under HIPC will be offset by "increased profit repatriation by foreign mining companies." Ghana continuing to rank among the highest in foreign remittances and continued donor support is not expected to prevent the current account from sliding into a deficit of 2.4% of GDP in 2005 and 3.9% of GDP in 2006, according to the EIU.

Ghana was one of the first countries of Sub-Sahara Africa (SSA) to sign onto the World Bank's structural adjustment program. The international trend of macroeconomic liberalisation begun in the late 1980's opened markets and increased the importance of trade agreements. Initially, the challenge in formulating the new trade agreements was to convert quantity defined trade barriers to tariffs. This effectively maintained historic trade relationships. As financial capital markets were liberalized, competition for investment capital intensified. Several factors, such as continued civil conflict in Ivory Coast, challenges related to the economic overpowering nature of oil endowed Nigeria and Ghana's political stability converged to position Ghana as the trade and economic growth gateway for West Africa.

B. MOZAMBIQUE

Mozambique's political history is the cornerstone of explaining its current economic structure and the openness of the economy to foreign investment. Mozambique gained independence from Portugal in June 1975, which was followed by 15 years of civil war. In November 1990, a new constitution was adopted that allows for political pluralism. In 1994 Mozambique held its first multi-party elections, which led to current political stability.

Mozambique's size, location and natural resource endowment are instrumental to its economic development strategy. Mozambique covers an area of approximately 799 380 sq km. of which 13 000 sq km is water. It is approximately two-thirds the size of neighbouring South Africa and about three times the size of Great Britain. Mozambique borders Tanzania in the north, Zambia, Malawi and Zimbabwe – all landlocked countries – to the west and South Africa and landlocked Swaziland to the south. Together, these six neighbouring countries share 4 571 km of Mozambique's border and ports along the 2 470 km coastline are instrumental to the economies of four landlocked neighbouring nations.

Mozambique is divided into 10 provinces. Zambezia and Nampula provinces in the north contain the richest agricultural land and 40% of the country's population. The Zambezi River is navigable from the city of Tete in Mozambique's most Western province, to the Indian Ocean, flowing between the Zambezia and Sofala provinces. One of Mozambique's two lakes is wholly contained in the country: Lake Cahora Bassa in Tete province and Lake Niassa in Niassa province, which is shared with Malawi. Maputo, the capital city of Mozambique, lies in the far south of the country, approximately 430 km east of Johannesburg. The next five largest cities in Mozambique, in order of estimated population are: Beira (a port city in Sofala province); Nampula in the north; Chimoio in the west, close to the border with Zimbabwe; Nacala (a port city in Nampula province); and Quelimane (a port city in Zambezia province).

Mozambique's population is estimated to be 18.8 million (approximately 1.1 million live in the capital city, Maputo) and is expected to grow at 1.22% per year. Although 67% of the population is estimated to live in rural area, the typical trend of rural-urban migration is occurring. Challenges of stemming the rural-urban flow, and even getting urban dwellers to relocate to rural areas, are exacerbated by vestiges of the war. Almost the entire population is under the age of 65 years: 43.6% of the population is 0-14 years, and 53.6% are 15-64 years. The life expectancy of Mozambique is 37 years. This and other social indicators, and the need for the private sector in all forms to play a principal role in economic development, define policy challenges for the government of Mozambique.

General Economy

Mozambique's economy is estimated to have generated GDP of USD 5 400 million in 2004 and USD 4 400 million in 2003. Real GDP growth is estimated to have been 8.2% in 2004, and 7.1% in 2003. The tremendous economic growth was achieved with relatively stable inflation of 13.4% in 2003 and an estimated 12.8% in 2004. Mozambique continues to import more than it exports; however, the trade gap is narrowing. Aluminium exports contribute significantly to the reduction of the trade deficit. As Mozambique invests to revitalise the economy, machinery and equipment imports account for approximately 11.3% of all imports. Additional investment projects in titanium extraction and processing, and garment manufacturing should further close the import/export gap (Table A4.2).

Table A4.2 Economic Structure and Annual Indicators of Mozambique

Macroeconomic Figures					
	2000[a]	2001[a]	2002[a]	2003[b]	2004[c]
GDP at market prices (MZM million)	56900	71100	85200	103700	124000
GDP (USD million)	3700	3400	3600	4400	5400
Real GDP Growth (%)	1.5	13	7.7	7.1[a]	8.2
Population million	17.9	18.2	18.5	18.9	19.2
Exports of Goods (USD million)	364	726	679.3	880.2	1,253.9
Imports of Goods fob (USD million)	1,046.0	997.3	1,215.7	1,228.2	1,448.5

International Trade Figures			
Principle Exports 2003	USD million	Principle Imports 2003	USD million
Aluminium	519	Machinery & Equipment	139
Prawns	64	Vehicles, Transport Equipment & Spare Parts	113.8
Cashew Nuts and Raw Cashews	17	Fuel	92.3
Manufacture	15	Textiles	43.4
		Metal Products	38.9
Main Destinations of Exports 2003[d]	% of Total	Main Origins of Imports 2003[d]	% of Total
Belgium	30.3	South Africa	34.5
South Africa	17.3	Australia	10.4
Italy	11.6	US	5.1
Spain	11.3	Portugal	5.0

a. Actual figure

b. Official estimates.

c. Economist Intelligence estimates

d. Based on partners' trade returns; subject to a wide margin of error.

Source: EIU (2005)

Mozambique's once substantial foreign debt has been reduced through forgiveness and rescheduling under the Heavily Indebted Poor Countries (HIPC) and Enhanced HIPC initiatives. The two initiatives were finalised in July 2004. Also, Brazil agreed to write off USD 314 million of bilateral debt, representing 95% of the USD 331 million that Mozambique owes to Brazil, further reducing the previously unmanageable debt of USD 3 702 million of 2002. Mozambique's total external debt was USD 3 988 million in 2003.

Agricultural production, including fishing and forestry, accounts for 20% of GDP and employs 81% of the labour force which was estimated to be 9.2 million in 2000. Although the 45% of the land area is considered suitable for agriculture, only 4% of that is cultivated. Farmed cash crops are cashew nuts, tea, sugar, sisal, cotton, copra, tobacco, oil seeds and some citrus fruits. Maize is the main subsistence crop, but cassava, millet, sorghum, groundnuts, beans and rice are also grown. Livestock products of beef and

poultry complete the list. Farming continues to be predominantly rain-fed, smallholder, cash crop, subsistence, and low technology.

Fishing is of increasing importance for Mozambique's economy, with open catch prawns continuing its dominating role in exports. The UK investment in a new jetty in Angoche, Nampula province on the Indian Ocean supports government research into prawn breeding, and Japan is a major importer of Mozambique prawns. The interest of both the UK and Japan, underscores the bright prospects for the fishing and prawn industry. Mozambique's sustainable fish catch is estimated at 500 000 tonnes including 300 000 tonnes of anchovies. The sustainable catch of prawns is estimated at 14 000 tonnes.

The industrial sector contributes 27.3% to GDP but employs only 6% of the labour force. Manufacturing industries such as food, beverages, chemicals (fertilizer, soap, and paints), aluminium, petroleum products, textiles, cement, glass, asbestos, and tobacco comprise approximately 15.5% of GDP. At 52.7%, the service industry accounts for the largest share of GDP but provides employment for only 13% of the labour force.

In 2003, Mozambique's exports, principally of the commodities aluminium, prawns, cashews, cotton, sugar, citrus, timber; bulk electricity, were estimated to be valued at USD 880.2 million. Data for 2003 show that Mozambique's major export trading partners are Belgium (30.3%), South Africa (17.3%), Italy (11.6%) and Spain (11.3%). Imports of USD 1 228.2 million in 2003, comprise machinery and equipment, vehicles, fuel, chemicals, metal products, foodstuffs, and textiles. The top four import suppliers to Mozambique are South Africa (34.5%), Australia (10.4%), the US (5.1%) and Portugal (5.0%). The four countries account for 55% of total imports for 2003.

C. TUNISIA

Traditionally included in the Middle East North Africa (MENA) country grouping, Tunisia's achievement of political stability sets it apart in a region. More recently, as North African countries have sought to diversify trading partners, there has been increased interaction between North African countries and Sub-Saharan African countries, especially those that share colonial history with France. In 1956, Tunisia gained independence and became a republic in 1957.

Bordering the Mediterranean Sea between Algeria and Libya, Tunisia has an area 163 610 sq km, which makes it the smallest country in North Africa.[34] Tunisia's proximity to Italy shaped its history and continues to play a role in Tunisia's economic development. The long coast line (1 148 km) on Tunisia's eastern and northern boundaries is pivotal to tourism and fishing industries and trade. Only 17.9% of the 155 360 sq km land area is arable and 13.7% of the land area is dedicated to permanent crops.[35] Irrigated land is estimated at 3 800 sq km, and Tunisia's only permanent river is the Medjerda in the west, which means that irrigation is instrumental to agricultural production.

Tunis (capital) and Sfax are the main economic and population centres. Gabes and Kairouan are important towns. Ports are situated at Bizerte and Sfax. Tunisia's 9.9 million population (approximately 1.8 million

34 . Tunisia measures 750 km from north to south but only 150 km from east to west.

35 . Fertile plains, especially between Sfax, Tunis and Bizerte account for the majority of Tunisia's arable land.

reside in Tunis), is estimated to grow at 1.01% annually. The young population will lead to increased demand for jobs and public services. Given that average life expectancy is already 74.7 years, it is reasonable to expect pressures on social services to increase.

General Economy

Agriculture and fisheries ranks a distant third (13.9%), behind services (53.9%) and manufacturing (20.6%) in their contribution to the Tunisian GDP. EIU estimates Tunisia's GDP for 2004 to be USD 28100 million (TND 35 100 million). The estimated real GDP growth rate of 5.1% for 2004 is a marginal slowdown from 2003 but is in line with historic GDP growth trends in Tunisia (Table A4.3).

Table A4.3 Economic Structure and Annual Indicators of Tunisia

Macroeconomic Figures					
	2000[a]	2001[a]	2002[a]	2003[a]	2004[b]
GDP at market prices (TND million)	26700	38700	29900	32300	35100
GDP (USD million)	19500	20000	21000	25000	28100
Real GDP Growth (%)	3.5	4.9	1.7	5.6	5.1
Population million	9.5	9.6	9.7	9.8	9.9
Exports of Gods (USD million)	5840.0	6628.0	6857.0	8027.0	9550.0
Imports of Goods fob (USD million)	8093.0	8997.0	8981.0	10297.0	11866.7

International Trade Figures				
Principle Exports 2003	USD million		Principle Imports 2003	USD million
Textiles	3301		Textiles	2285
Electrical Equipment	93		Machinery	1422
Petroleum & Derivative	80		Electrical Equipment	1311
Leather & Hide Products	487		Petroleum & Derivative	1310
Olive Oil	89		Vehicles, Cycles & Tractors	726
Main Destinations of Exports 2003	% of Total		Main Origins of Imports 2003	% of Total
France	35.6		France	31.0
Italy	22.8		Italy	23.0
Germany	12.1		Germany	10.0
Libya	5.4		Spain	5.6

a. Actual

b. Economist Intelligence Unit estimates.

Source: EIU (2005)

Tunisia's natural resources are petroleum, phosphates, iron ore, lead, zinc, and salt. Agricultural products are olives, olive oil, cereal (barley and wheat), dairy products, tomatoes, citrus fruit, beef, sugar beets, dates, and almonds. Industry comprises petroleum, mining (particularly phosphate and iron ore), tourism, textiles, footwear, agribusiness, and beverages. Principal exports are textiles, electrical equipment, petroleum and derivative and agricultural products. Interestingly, textiles, electrical equipment and petroleum and derivative are also critical components of Tunisia's list of imports. Machinery and vehicles, cycles and tractors complete the list of major imports.

Countries in the European Union (EU) are Tunisia's major trading partners. Specifically, France (35.6%) and Italy (22.8%) accounted for the majority of Tunisia's exports in 2003. The countries were also the leading sources of imports 31.0% and 23.0%. The list of leading export partners is rounded out with Germany (10.0%) and Spain (5.6%) based on data for 2003.

Although elements of the service industry, especially those related to tourism, are returning to a position of strength, Tunisia's economic vulnerability in the textiles component of manufacturing is a source of broader economic uncertainty. The 280 000 employees of the textile industry represent approximately half

of the labour force in the manufacturing sector. Stagnation of production and exports in Tunisia's textile industry has been pronounced in the past 2 years, after averaging 8% annual growth in the 1990's. Although Tunisia continues to be the EU's fourth biggest textile supplier, Tunisia's market share has been eroded by supplies from Eastern Europe and Asia. Most significantly, China recently became the main textile supplier to France.

The star performer in Tunisia's manufacturing sector in 2004 was the food processing industry. Food industry export sales rose 85% for the first 11 months of 2004, compared with a similar period in 2003, despite weak demand in the EU. [36] A surge in olive oil exports, the most important product of the food processing industry, accounts for most of the sales increase.

The performance of the agriculture sector was mixed in 2004. Tunisia's 2004 cereal harvest is estimated to be approximately 17.0% below the 2003 record harvest of 2.9 mt, principally as a result of damage caused by heavy rainfall and hailstorms in June and the related rust mildew damage. The revised cereal harvest estimate of 2.4 mt is well above the ten-year average of 1.7 mt. The negative impact from the cereal harvest results for 2004 was offset by production increases in olives, dates, apricots, peaches, plums, pomegranates and other tree fruits, as well as melons and many vegetables. Olive growth operates on a two-year cycle. The production year 2002/03 was a low production year with 72 000 mt of olives produced. The production year 2003/04 was a high production year with olive production increased to 260000 mt. The production year 2004/05 is expected to see olive production return to the "low year" levels. On the other hand, the 2004/05 date harvest is projected to reach 122 000 mt which would be a 10% increase over 2003/04 production. Approximately 80% of the 2003/04 date production was exported to the EU. The *deglet nour* variety of dates, most widely grown in Tunisia, is well known in the trade for superior quality.

Tunisia's merchandise trade deficit grew in 2004. Record level olive oil exports,[37] in weight and value terms,[38] was expected to account for approximately 50% of Tunisia's agricultural exports in 2004. Such an increase helped to counter marked increases in imports of capital investment oriented mechanical and electrical goods. According to EIU, increases in the value of exports of mechanical and electrical goods, and exports of mined products, principally raw phosphates and phosphate derivatives such as phosphoric acid and phosphate fertilizers, also helped to cushion the trade deficit impact of increases import increases. Increases in international food prices and the price for (refined) energy products, as well as higher world prices for non-oil industrial raw materials, together magnify the cost of Tunisia's import trend. A strong return of tourism receipts, as Tunisia seeks to expand its tourism market to include Eastern Europe and China, and remittances from Tunisians working abroad helped to contain the trade deficit from further widening and strengthened foreign exchange reserves.

36 . Construction materials, mechanical and electrical, and chemical industries also exhibited strong growth in the first 11 months of 2003.

37 . The increase in the quantity of Tunisian olive oil exports was the result of greater international demand following a fall in output in Italy and Spain, the two main suppliers of olive oil to the EU. The surge in the value of olive oil was due partly to the regional imbalance in supply and demand and also the larger quantities of Tunisian oil sold in higher-valued bottles, rather than in lower-valued bulk.

38 . By mid-October 2004 some 195 000 mt of olive oil had been exported, bringing in receipts of USD 545 million (TND 654 million), and the total was expected to exceed 200 000 mt by the end of the year. The previous export records were 193 000 mt, achieved in 1994, and, in value terms, TND 383 million, achieved in 1999.

D. UGANDA

Uganda is a member of the East African Community (EAC) and the Common Market for Eastern and Southern Africa (COMESA). One distinguishing characteristic of Uganda is that it is landlocked.[39] Uganda shares borders the Democratic Republic of Congo (765 km), Kenya (933 km), Rwanda (169 km), Sudan (435 km), Tanzania (396 km). Several of these countries have recently emerged from civil war. Despite a volatile, and at times oppressive, political history since it 1962 independence from the United Kingdom, Uganda evolved into a political stability and recently voted to transition to multiparty politics. However, political uncertainty continues to distract from the positive investment news.

Uganda's total area is 236 040 sq km. Although landlocked, Uganda's territory includes the majority of Lake Victoria. The lake's high rate of evaporation due to its location on the equator makes this immense body of water a major factor in the local climate. Lake Victoria supports a freshwater fishing industry including: Nile perch, Tilapia, and Omena. Agricultural production and freshwater fishing resources combine to provide an economic backbone for Uganda.

Kampala (capital), in central Uganda, is the main economic and population centre (an estimated 1.33 million in 2004). Gulu in northern Uganda is a second city with a population of 139 000. Over 50% of 26.5 million Ugandans are under the age of 15 years, and the literacy rate for persons over 15 years is approximately 70%.

General Economy

Agricultural production accounts for approximately 39% of Uganda's GDP, which was USD 7 700 million in 2004. With historically adequate rainfall for crop production, Uganda has negligible levels of investment in irrigation systems. Thus when there is poor rainfall, as was the case in the second half of 2004 and early 2005, agricultural output declines significantly. Real GDP growth was forecasted to be 5.4% in 2005, below the government's annual growth target of 7%. However, continued export growth in agricultural exports, such as horticultural and fish products, and continued growth in manufacturing, construction, transport and communications, may fuel the forecasted slight increase in real GDP growth to 6.2% in 2006 (EIU 2005). Much of the expansion in agricultural processing businesses and infrastructure is derived from foreign direct investment.

Uganda is landlocked, which is noteworthy in discussions of trade and foreign direct investment. Infrastructure for connecting markets within Uganda and linking the country to neighbouring Great Lakes countries and overseas markets is pivotal. For example, the impact of newly leased thermal generators, that are expected to be operational during the second half of 2005, should be widespread throughout Uganda's economy. Paved roads are instrumental to the Ugandan economy and the share of Uganda's road network that is paved is a paltry 6.7%, which is half the Sub-Sahara African average of 13.3% (Table A4.4). Various donor-funded road projects are stimulating construction and quarrying. The demand on the road network for trade alone is taxing on the road system. Consistent funding for road maintenance, upgrading of the existing road network and road network expansion, especially with regard to linking Uganda to neighbouring countries, will be instrumental in reducing macroeconomic volatility.

39 . The 15 landlocked countries in Africa namely: Botswana, Burkina Faso, Burundi, Central African Republic, Chad, Ethiopia, Lesotho, Malawi, Mali, Niger, Rwanda, Swaziland, Uganda, Zambia, and Zimbabwe.

Table A4.4 Paved Roads and FDI

	Pave Roads (%)	Inward FDI Flows *current USD millions*	
	1993	*1999*	*2003*
Uganda	6.7	140.2	194.2
Tanzania	4.2	516.7	248.0
Kenya	12.1	42.0	81.7
Sub-Saharan Africa	13.3	9,100.0	10,100.0
OECD Countries	88.0	864,700.0	390,800.0

Source : World Bank (2004)

With a 44.6% share of Uganda's imports in 2003, Kenya is Uganda's principal trade partner for imports. This results from the fact that Mombasa is the main drop-off point for Uganda's bulk imports – including petroleum and petroleum products. Other leading sources of imports for Uganda are South Africa, India, United Kingdom, and China, which together account for 22% of USD 1 242 million import bill in 2003. The annual rate of increase in Uganda's import bill reached 19% in 2004. This is significant, given that over the 2000-01 period the change in Uganda's import bill was just under 3%. In 2004, the value of imports into Uganda was USD 1 342.2 million (Table A4.5).

Table A4.5 Economic Structure and Annual Indicators of Uganda

Macroeconomic Figures					
	2000[a]	2001[a]	2002[a]	2003[a]	2004[b]
GDP at market prices (UGX million)	9500	10300	10900	128800	13800
GDP (USD million)	5800	5800	6100	6500	7600
Real GDP Growth (%)	5.5	5.1	6.7	4.7	5.0
Population million	23.5	24.2	28.0	25.8	26.5
Exports of Gods (USD million)	449.9	475.6	480.7	563.0	632.1
Imports of Goods fob (USD million)	949.7	996.9	1,073.2	1,241.7	1,478.3

International Trade Figures			
Principle Exports 2003[c]	USD million	Principle Imports 2003[d]	USD million
Coffee	123	Petroleum & Related Products	174
Fish	102	Road Vehicles	105
Cotton	39	Cereals	73
Tea	35	Non-metallic Mineral Manufactures	41
Main Destinations of Exports 2003[e]	% of Total	Main Origins of Imports 2003[e]	% of Total
Netherlands	15.8	Kenya	44.6
Belgium	10.2	South Africa	6.6
United States	9	India	5.6

a. Official estimates, calendar year
b. Economist Intelligence Unit estimates
c. Official estimates, fiscal year July to June
d. Official estimates, calendar year
e. Based on partners' trade returns; subject to a wide margin of error.

Source : EIU (2005)

The structure of Uganda's exports increasingly includes non-traditional products, such as organic fruits and vegetables, flowers, fish products, and technology based products (minimal but notable). The Netherlands accounted for largest share of Uganda's exports in 2003 followed by Belgium, the US, Germany, and Spain. Despite the 25% increase in exports for 2003-04, the trade gap widened because historically, exports lag imports in Uganda and only in the past 2 years have export increases kept pace with imports. Approximately 50% of Uganda's exports in 2004 (estimate) were accounted for by agricultural exports: coffee (USD 123 million), fish (USD 102 million), cotton (USD 39 million), and tea (USD 35 million) (see Table A4.5). Uganda's efforts to attract investment to diversify agricultural production and employ

science and technological innovation to improve crop production are crucial in catalysing additional investment along the food value chain. Further, it is imperative that these investments restructured Uganda's exports away from commodities to agriculture based, value-added products.

Uganda's economic vulnerability centres on extensive budgetary support from multilateral and bilateral donors and political changes, uncertainty and relationships with neighbouring governments. It is expected that the inter-relationship of these issues will dominate Uganda's climate for the rest of 2005 and throughout 2006. Changes in the way the Bank of Uganda (the central bank) finances the government's deficit is expected to open up the commercial banking portfolio to compete for investment business. The introduction of two- and three-year Treasury bonds in 2003/2004, combined with shifting multilateral and bilateral projects from the commercial banks, means that commercial banks will have to look for alternatives to fill the new gap in their portfolio. Until the new business stabilizes, it is reasonable to expect interest rates, currently just over 20%, to increase somewhat but with strong competition for solid investment projects, rates are forecasted to decline to 18.5% (EIU, 2005).

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