Impact of South-South Cooperation and Integration on the Zambian Economy: The Case of Chinese Investment

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Introduction

This paper seeks to evaluate the impact of south-south cooperation and integration on the Zambian economy. Of the total 48 Least Developed Countries (LDCs) in the world, Zambia is one of the 33 in Africa which require Foreign Direct Investment (FDI) and integration into the global economy for their social and economic development. It is for this reason that assessment of FDI’s impact on the country’s economy becomes an essential element to the monitoring process of the country’s socio-economic development. FDI is critical to the LDCs, because their income levels and domestic savings are so low that external capital is essential for investment in the extraction and beneficiation of their natural resources and other economic opportunities for value addition and enhanced economic growth. In the LDCs FDI promotes social and economic development through technology and skills transfer, higher employment opportunities, increased productivity and enhanced access to export markets with higher value product offerings. Improved market access, is in particular, critical to the development of the LDCs in Africa, because they typically have small domestic markets, which are not attractive to market-seeking FDI. Linking the LDCs to larger export markets enhances their export earnings, balance of payments and development (Asiedu, 2002; UNCTAD, 2010).

Although FDI is critical to social and economic development of the LDCs, they have traditionally received the least proportion of the global FDI flows. The FDI flows to the LDCs in Africa were particularly poor throughout the 1980s and early 1990s, the so-called “lowest decades”, due to poor economic performance in most of the African LDCs during those decades. Most of the LDCs in Africa, however, undertook structural and macro-economic reforms and opened up their economies to FDI in the 1990s. Though the
FDI flows to the LDCs in Africa remained quite subdued throughout the 1990s, they picked in the post 2000 period. In that regard, the FDI flows to the LDCs in Africa increased from a paltry 1.4% of the global FDI flows in 1990 to 5.4% in 2000. Most of the FDI in the LDCs in Africa, however, went only to a handful of resource-rich countries. In fact, 50% the total FDI flows to Sub-Saharan Africa in the 2001-2010 decade went to just four countries, namely; Angola, Equatorial Guinea, Sudan and Zambia. These countries have substantial oil and mineral reserves. However, FDI to these countries was also fueled by the increased demand for primary commodities in the emerging and transitional economies (UNCTAD, 2011). The emerging economies can therefore play a significant role in the development of the LDCs in Africa as they are potential sources of affordable manufactured goods and services and could provide new export markets for these countries. However, while FDI from the emerging economies like Brazil, China, India and even South Africa has substantially grown in the LDCs in Africa, only China and India have developed platforms for engaging with the African LDCs. The increased involvement of the emerging economies in the LDCs of Africa has not, however, been welcomed in some quarters. Increased Chinese involvement in these, for example, has been observed with alarm, suspicion and even regarded “controversial” (Brautigam and Xiaoyang, 2011). Most African countries have, however, welcomed the new investments from the emerging economies, because shortage of capital remains the main constraint to the social and economic advancement of these countries.

By examining the role and impact of Chinese investment on the Zambian economy, this paper throws some light on the potential positive roles of south-south cooperation and integration in the development of the LDCs. Zambia is an appropriate case study, because it is one of the mineral-rich LDCs in Africa that failed to diversify its economy over the last five decades and reduce vulnerability to fluctuations in the price of copper, its main export commodity. It is also one of the four African countries that accounts for the bulk of the recent Chinese FDI to the LDCs in Africa. Chinese FDI to Zambia also increased from just US$5.5 million in 2003 to US$214 million in 2008, and was expected to reach US$1.5 billion by the end of 2010 (ZDA, 2011). China was also Zambia’s fastest growing export destination, as exports grew at 310.9% per annum between 2003 and
Economic interaction between China and Zambia, therefore, should provide appropriate insights into the impact of south-south cooperation and integration on the LDCs.

It is also appropriate to examine the economic interaction of China with the LDCs, because it is not just one of the largest emerging economies and an alternative source of FDI, but also the second largest economy in the world, after the United States of America, since its economy surpassed that of Japan in terms of size in 2008. The Government of China, however, still regards the country as a developing country, as it still has to lift millions of its citizens out of poverty. It also portrays its increasing economic involvement in other developing countries, especially in LDCs in Africa as south-south cooperation, aimed at assisting other developing countries (Haglund, 2008; Tull, 2006). Close examination of Chinese investment in Zambia should, therefore throw some light on the potential impact of FDI from the south on the economies of the LDCs. It should also throw some light on the nature of FDI originating from the south and its implications for the LDCs.

To effectively assess the role and impact of Chinese investment on the Zambian economy, we examine FDI and trade flows between China and Zambia, and their impact on employment creation, technology transfer and know-how, productivity, domestic firms, public revenue, and trade, as well as on the economy as a whole. We begin, however, with a review of Zambia’s economic policies and attitudes to FDI. Conclusions regarding the role and impact of Chinese FDI on the economy of Zambia are drawn, as are the measures that ought to be taken to maximize the positive and minimize the negative impacts of Chinese FDI on one of the LDCs in Africa.

**Zambia’s economic policies and FDI**

At independence in 1964, Zambia was a middle income country, largely on account of its large copper mining enclave economy and revenues thereof (Lungu, 2009). The mining sector was, however, owned and controlled by two foreign mining firms: Anglo-American Corporation and the Roan Selection Trust. Other sectors of the economy were
extremely underdeveloped and most of the population was not directly involved in the mainstream economy of the country. The Agricultural sector, for example, which employed most of the country’s labour was dominated by small-scale farmers, using mostly hand tools and traditional farming methods. They grew mainly food crops and raised livestock mostly for subsistence. Commercial agricultural production in the overall economy was also insignificant, and confined mainly to the land along the line rail that connects the Copperbelt to the Southern African seaports. It was also dominated by expatriate farmers growing mostly maize and raising livestock for the domestic urban market and tobacco for export.

To take control of the economy and develop other sectors of the economy, the post-independence Government of Zambia gradually moved from an open market economy to a controlled economy anchored on state centered development policies. The commanding heights of the economy, including the mining sector were, therefore, nationalized through compulsory state acquisition of majority share holdings in the firms operating in the country. State involvement in the production of goods and services was gradually extended to all sectors of the economy, including banking, manufacturing and the wholesale and retail sectors between 1968 and 1975. As a result, an estimated 80% of the economy was in the control of the Government by 1985 (Thurlow and Wobst, 2004).

The Government also extended agricultural in-put subsidies to small-scale farmers throughout the vast country, to boost agricultural production, keep urban food prices low, and bring the small-scale farmers into the mainstream economy. In addition, the Government introduced consumer subsidies on essential commodities, including maize meal, milk and bread to raise the urban living standards, in particular, and to keep wage increases in the sensitive mining sector under control. Rising oil prices and falling copper prices in the mid 1970s, however, led to increased Government borrowing, to maintain consumption and the state-led economy. This borrowing was based on the assumption that, the low copper prices would recover in the short-term and would, therefore, not have any long-term adverse effects. When the copper prices failed to recover and the economic situation begun to deteriorate, on account of declining copper production, due to lack of
reinvestment in the mining sector, however, the Government failed to take any remedial measures. Zambia’s external account and debts thus continued to deteriorate, until the foreign debt burden became unsustainable as the debt service ratio begun to take a large proportion of the country’s income (Thurstow and Wobst, 2004).

The low copper prices and failure to address the macro-economic imbalances that emerged eventually led to a prolonged economic crisis characterized by declining revenues, a high foreign debt burden, economic stagnation and decline. By the late 1980s, this economic crisis degenerated into a political crisis as well. As a result, the Government undertook some political reforms and held the first multi-party elections in 17 years, two years ahead of schedule. The elections resulted in a change of Government, with the Movement for Multi-Party Democracy (MMD), which campaigned on the platform of political and economic liberalization forming the new Government on November 1, 1991.

The new Government with the support of the international financial institutions and western bilateral development agencies embarked on political and structural economic reforms, aimed at transforming the county into a liberal democracy with an open export oriented economy. Ensuring transparency and democracy in governance were the goals of the political reforms, while limiting the role of the state in economic activities to regulation and enabling enterprises to produce goods and services at competitive prices were the goals of the economic reforms (Rakner, 2003). In the short-term, the main goal of the economic reforms was to stabilize the economy and create a favorable environment for rebuilding a private sector-led economy, with domestic and FDI as the engines of economic growth so as to propel more balanced and equitable development. The Government also embarked on divesting from the economy by selling the state-owned enterprises to domestic and foreign firms through the privatization programme so as to facilitate the development of a private sector-led economy and increased FDI participation in the economy.

Measures for stabilizing the economy included realigning the public expenditure with its revenues. As a result, the producer and consumer subsidies were abolished in 1992. A
cash budget was also introduced to keep the public expenditure under control, and avoid the persistent budget deficits that had been fueling hyper inflation. Furthermore, prices, interest and exchange rates were liberalized, and the Foreign Exchange Control Act was repealed. The latter was essential to facilitate trade, which was also simplified by reforming the tariff structures and lifting all the quantitative restrictions on imports and exports. New institutions to oversee the sale of the state-owned enterprises and facilitate the entry of FDI into the country were also created. The Zambia Privatization Agency (ZPA) and Zambia Investment Centre (ZIC) were, therefore, established by legislation.

The sale of the state-owned enterprises begun in 1992 after the legislation of the Zambia Privatization Act. In general, the ZPA sold the state-owned enterprises on the basis of competitive tenders, whose evaluation prioritized reinvestment and retention of as many workers as possible. For the nationalized firms, however, the former owners and/or the minority shareholders had pre-emptive rights. The sale of the state-owned enterprises also begun with the smaller less complicated trading and service firms, before moving on to the medium sized agricultural and manufacturing firms, and ultimately the more complex and larger mining, finance, telecommunication and energy firms. A few state-owned enterprises, especially in the energy and infrastructural sectors are yet to be privatized two decades on.

At the regional level, the Government took measures to make the country a part of larger preferential markets to compensate for the small domestic market. Zambia was consequently instrumental in the establishment of the Preferential Trade Area (PTA) for Eastern and Southern Africa and the Southern Africa Development Coordination Conference (SADCC). These regional initiatives have since evolved into a common market and a free trade area. Zambia is therefore a member of the Common Market for Eastern and Southern Africa (COMESA) and hosts its Headquarters in Lusaka; and the Southern African Development Community Free Trade Area (SADC FTA). These regional trading blocs have potential markets of more than 350 and 230 million people respectively.
Zambia is also a founding member of the World Trade Organization (WTO), and has entered into the Economic Partnership Agreements with the EU. The country is also a beneficiary of the Africa Growth and Opportunity Act (AGOA), which provides duty free access to the US market for goods produced in the LDCs of Africa. Furthermore, Zambia has signed multilateral and bilateral investment protection agreements with multi-lateral institutions and the major and potential trading partners, as well as most of the potential sources of FDI, including China, India and South Africa, to promote FDI from these institutions and countries.

**Zambia’s macro-economic performance and FDI 1992 to 2010**

Although Zambia liberalized her economy and established one of the most open trade regimes in Africa in the early 1990s, high levels of FDI eluded the country until 2003. This is evident from Figure 1, which shows Zambia’s inward FDI between 1991 and 2010.

![Figure 1: Zambia: Inward Foreign Direct Investment 1991-2010](image)

It is evident from Figure 1 that between 1991 and 2000 Zambia attracted FDI ranging from US$34.3 million to US$314 million recorded only in 1993. In the ten year period the average inward FDI to Zambia was a paltry US$133.7 million per annum. This was far below the FDI that was going to Zambia’s peers even within the Southern African region.
Zambia’s failure to attract higher levels of FDI between 1991 and 2000 could be attributed to its poor economic performance, which was evident from the negative and predominantly low annual real GDP growth rates recorded throughout the 1990s. The poor and subsequent improvements in Zambia’s annual real GDP growth rates can be gleaned from Figure 2, which shows Zambia’s Annual Real GDP Growth for the two decades between 1991 and 2010.

Zambia experienced wild fluctuations in its annual real GDP growth rates particularly between 1990 and 1995. Thus, Zambia’s first five years of consistent macro-economic reforms were marred by poor economic performance, while the next five years also posted low positive economic growth rates averaging only 2.6%, while the population was growing at 2.8% per annum. The economy only begun to consistently post positive GDP growth rates after 1999.

The marginal economic growth rates recorded between 1991 and 2000 were also accompanied by high inflation of about 30% per annum. Zambia therefore failed to create a stable macro-economic environment in its first ten years of consistent macro-economic reform. The unstable economic situation before 2000 can also be gleaned from Figure 3, which shows Zambia’s annual inflation rates between 1991 and 2010.
Figure 3 shows that economic stability only returned to Zambia between 2001 and 2010, when the annual inflation ranged between 9 and 22% and averaged 15% per annum. Zambia also recorded higher economic growth rates consistently only in the last ten years. The GDP growth rates ranged between 3.3 and 7.6% and the average growth rate was a more reassuring 5.6%.

FDI inflows into Zambia mirrored the country’s economic performance between 1991 and 2010. The first five years of consistent macro-economic reforms were marred by high annual inflation rates and economic decline. The country also failed to attract higher volumes of FDI. In that regard, the FDI inflows ranged from a paltry US$34.3 million in 1991 to an exceptional US$314 million recorded only in 1993. As a result, on average Zambia only recorded inward FDI of US$106 million per annum between 1991 and 1995. Similarly, though Zambia’s FDI inflows improved slightly between 1996 and 2000, on average it was an equally paltry US$117.1 million per annum in that period. Zambia’s FDI inflows between 1991 and 2000 were no where near to the FDI that was going to its peers even in the SADC region. Between 1991 and 2000 Zambia had in fact one of the lowest FDI inflows in the SADC region (ZDA, 2010).
The low FDI Zambia recorded between 1991 and 2000 is evident from Figure 4, which shows FDI inflows into Zambia between 1991 and 2010.

![Figure 4: Zambia Inward Foreign Direct Investment 1991-2010](image)

It is evident from Figure 4 that FDI inflows into Zambia only picked up to levels never recorded before in 2003, when the country recorded nearly US$350 million in FDI. The FDI inflows have since picked to levels never experienced of between US$616 and US$1,324 million. Admittedly, the high FDI inflows into Zambia have coincided with recovery of prices of its main export commodities, copper and cobalt. However, while there might be a correlation between higher levels of FDI inflows and higher commodity prices, Zambia had also undertaken additional reforms aimed at boosting FDI inflows into the country. The country had, for example, taken measures to reduce the cost of doing business and minimizing the bureaucracy involved in the registration of companies. A one-stop-shop for prospective investors had also been created by amalgamating all the public institutions involved investment promotion, the sale of state-owned enterprises and the promotion of small-scale enterprises and exports into the Zambia Development Agency.

However, the little FDI that Zambia received between 1991 and 2000 was mostly as a result of the acquisitions of state-owned enterprises mostly by the minority shareholders.
or firms and individuals that were familiar with the country. Most of the FDI that came into Zambia between 1991 and 2000 was, therefore, from the United Kingdom and South Africa, which have since the colonial times been the traditional sources of FDI for Zambia. Most of the investor firms were also either minority shareholders in the nationalized firms that were being privatized, or had previous knowledge of the firms. Some fresh FDI was, nevertheless, also recorded in the early 1990s. It went mostly into the agricultural sector and the production of fresh flowers, fruits and vegetables, as well as coffee, cotton and tobacco for export. In terms of the volumes of investment, most of these were individual projects of no more than US$10 million per project and indeed many were as little as a few thousand dollars. Investments into these Non-Traditional Exports (NTEs) were also spurred by a number of incentives, including the 100% retention of foreign exchange earnings and other traditional incentives, including the 15% company tax for the agricultural sector and exemptions of agricultural machinery and equipment from import duties (ZDA, 2010).

Attraction of FDI to Zambia during the stabilization and consolidation phases of the structural and economic reforms was hampered by lack of economic stability and the rather modest economic growth rates recorded during the late 1990s. Larger volumes of FDI into Zambia were therefore, only realized after 2004. The unprecedented FDI inflows, however, coincided with higher copper prices rising from US$2,500.00 per metric ton in 2000 to US$9,000.00 per metric tons in 2010. The sources of Zambia’s FDI have also become much more diversified than in the 1990s. They include all the large emerging economies, such as Brazil, India and China among many others within the region. FDI from these countries is therefore playing an increasingly bigger role in Zambia’s economy and completing the traditional FDI from South Africa, the EU and the OECD countries.

**Role of FDI in the Zambian Economy**

Although FDI in Zambia is associated with the large-scale mining sector, it has also played an important role in most of the other sectors, since the emergence of the modern economy in the country in the 1920s. The volume of FDI that has gone into the other
sectors of the economy including, agriculture and agro-processing, manufacturing (mostly food processing, beverages and cable wire production), finance, tourism, wholesale and retail trade has, however, tended to be modest and smaller in terms of the amounts invested per project. Thus, while the capital required for individual projects in large-scale copper mining could range from at least US$200 million, the individual projects in the other sectors of the economy could be as little as US$50 000. In fact, until recently, it was rare in Zambia to have FDI volumes of more than US$300 million per project in sectors outside large-scale mining, energy and infrastructure development. Domestic participation has also tended to be higher outside the large-scale mining, energy and infrastructural projects. The domestic participation should not, however, be exaggerated as it is low to modest even in the non-traditional export(NTE) sectors, where it is concentrated in the agricultural sector, through contract farming and out-grower schemes. Domestic participation is also relatively high in the small-scale mining sub-sector, which includes gemstone mining and base metals to a little extent. The Zambian economy in general and its export sub-sectors in particular, is therefore highly dependent on FDI.

The sectors of the Zambian economy that are not directly associated with export earnings, such as transport and communication, finance, tourism and the wholesale and retail trade also play crucial roles in employment generation. FDI in these sectors also plays crucial roles in the facilitation of trade. Large-scale mining, however, still accounts for most of Zambia’s FDI and indeed most of the country’s FDI stock, export earnings and employment generation in the mining regions. The large-scale mining sector also still accounts for more than 70% of the Zambia’s export earnings. This is despite the appreciable growth of the NTE sector, which grew from less than 15% in the 1980s to around 30% in the late 1990s. Export earnings from large-scale mining are, however, bound to increase even further in the near future, since copper production is expected to increase to more than two million metric tons within the next few years, from the lowest production level ever of 257 000 metric tons produced in 2000, before the complete privatization of all the mines. Zambia in 2010 moreover recorded a massive 838 605 metric tons of copper from the large and small-scale mines. The expected high levels of
copper production are within Zambia’s reach, provided the prices remain competitive and all the planned green-field large-scale investments in the sector are realized. The substantial investments in the privatized mines and in the newly opened green-field mines are also already bearing fruit. The Government, therefore ought to do more to diversify Zambia’s economy.

**Origins of Zambia’s FDI and China’s Contribution**

To establish the origins of Zambia’s FDI and contribution of Chinese investment, we ought to examine the contributions of different countries to the country’s total FDI stock over a number of years. Table 1, therefore presents Zambia’s total FDI stock and the contributions of the top fifteen countries from which Zambia draws its FDI.

<table>
<thead>
<tr>
<th>Country</th>
<th>Total FDI Stock (US$)</th>
<th>Proportion (%)</th>
<th>Total FDI Stock (US$)</th>
<th>Proportion (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td>2009</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Canada</td>
<td>1154.2</td>
<td>17</td>
<td>1433</td>
<td>19</td>
</tr>
<tr>
<td>India</td>
<td>975.9</td>
<td>15</td>
<td>1277.9</td>
<td>17</td>
</tr>
<tr>
<td>Australia</td>
<td>920.2</td>
<td>14</td>
<td>810.4</td>
<td>11</td>
</tr>
<tr>
<td>Switzerland</td>
<td>865</td>
<td>13</td>
<td>805.4</td>
<td>11</td>
</tr>
<tr>
<td>China</td>
<td>540.1</td>
<td>8</td>
<td>595.5</td>
<td>8</td>
</tr>
<tr>
<td>Netherlands</td>
<td>451.7</td>
<td>7</td>
<td>524.2</td>
<td>7</td>
</tr>
<tr>
<td>South Africa</td>
<td>512.2</td>
<td>7.7</td>
<td>510</td>
<td>6.8</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>588.7</td>
<td>8.9</td>
<td>465.7</td>
<td>6.2</td>
</tr>
<tr>
<td>Ireland</td>
<td>74.5</td>
<td>1.1</td>
<td>214.2</td>
<td>2.9</td>
</tr>
<tr>
<td>Mauritius</td>
<td>183.7</td>
<td>2.8</td>
<td>168.6</td>
<td>2.3</td>
</tr>
<tr>
<td>Spain</td>
<td>87.5</td>
<td>1.3</td>
<td>99.6</td>
<td>1.3</td>
</tr>
<tr>
<td>France</td>
<td>151</td>
<td>2.3</td>
<td>97.2</td>
<td>1.3</td>
</tr>
<tr>
<td>USA</td>
<td>100.8</td>
<td>1.5</td>
<td>93</td>
<td>1.2</td>
</tr>
<tr>
<td>Panama</td>
<td>54.6</td>
<td>0.82</td>
<td>71.7</td>
<td>0.96</td>
</tr>
<tr>
<td>Sweden</td>
<td>62.1</td>
<td>0.94</td>
<td>55.8</td>
<td>0.75</td>
</tr>
<tr>
<td>Zambia Total FDI Stock</td>
<td>6634.1</td>
<td></td>
<td>7473.5</td>
<td></td>
</tr>
</tbody>
</table>

Source: Adapted from ZDA (2010) Foreign Private Investment and Investor Perception Survey, Lusaka: ZDA

Although Table 1 suggests that Canada, India, Australia, Switzerland and China in that order were Zambia’s largest foreign investors, most analysts consider the United
Kingdom and South Africa as Zambia foremost sources of FDI in that order. This is likely because of the historical links between the three countries and South Africa’s proximity to Zambia. The data in the Table 1 is therefore most probably based on the FDI in the privatized mines, which does not include the recent green-field mining investments opened by the Chinese firms. It is also our considered view that most of Zambia’s FDI stock is still held by firms from the UK, South Africa and China in that order. However, we are also mindful of the challenges of assembling Chinese FDI in the LDCs. It is difficult to accurately estimate Chinese FDI in the LDCs, because it involves many actors ranging from individual to private entrepreneurs and large state owned firms controlled by either the central, the provincial or municipals authorities in China. Thus, as Steven and Freemantle (2010) observed:

“While figures are hazy and opaque, given China’s interest in South Africa, Angola, the DRC, Nigeria, Sudan and Zambia alone, it is more plausible that Chinese cumulative FDI into Africa is well above US$30 billion, making it the most dominant developing investor in Africa” (Steven and Freemantle, 2010, p.8).

The above assertion is certainly true for Zambia, especially when Chinese investment since 2009 is taken into account. Moreover, Chinese investment has been the fastest growing FDI from the south in Zambia. For example, it grew from US$144 million in 2003 to US$844 million in 2009. Many new projects were also under consideration, while Chinese investment pledges in the first five months of 2011 amounted to an unprecedented US$2.4 billion. Such levels of investment entail that Chinese FDI is poised to ascend to summit of the list of top source of Zambia’s FDI. The large-scale investments in their initial stages included, the Juchuan Mining Groups’ investment in Munali Nickel Mine at the height of the 2009 global financial crisis, which saved the mine from certain closure and NFC Africa Mining’s acquisition of Luanshya Mine and its investment in the Mulyashi green-field copper mine. The Zhougi Mining Group also started developing their Ichimpe copper and cobalt mine in Kalulushi in April 2011.

Furthermore, Zambia is host to two of the six Special Economic Zones China pledged to help develop in Africa during the 2006 and 2008 FOCAC summits in Beijing and Egypt respectively. The two Special Economic Zones, Chambishi and Lusaka East, were expected to inject US$900 million and US$1.2 billion in each of the sites respectively.
Comparisons of FDI flows to Zambia from China and South Africa between 2003 and 2010 given in table 2 also support the assertion that, China has since 2006 substantially increased its investment in Zambia. It should therefore be in contention for either the top or the second slot on the list of Zambia’s top sources of FDI. Though table 2 has some gaps, the Chinese FDI to Zambia was much higher than the South African FDI flows to Zambia.

Table 2: Zambia Total FDI Stock by Selected Countries of Origin (US $ million)

<table>
<thead>
<tr>
<th></th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brazil</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>China</td>
<td>144</td>
<td>148</td>
<td>160</td>
<td>268</td>
<td>429</td>
<td>651</td>
<td>844</td>
<td>1000?</td>
</tr>
<tr>
<td>Cyprus</td>
<td>-</td>
<td>0.5</td>
<td>0.4</td>
<td>0.5</td>
<td>0.8</td>
<td>0.7</td>
<td>0.2</td>
<td>-</td>
</tr>
<tr>
<td>Denmark</td>
<td>-</td>
<td>0.2</td>
<td>-0.2</td>
<td>0.9</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>19.3</td>
</tr>
<tr>
<td>Norway</td>
<td>0.4</td>
<td>-0.3</td>
<td>0.3</td>
<td>-1</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>India</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>South Africa</td>
<td>62.5</td>
<td>73.2</td>
<td>92.6</td>
<td>59.3</td>
<td>51.2</td>
<td>81</td>
<td></td>
<td></td>
</tr>
<tr>
<td>South Korea</td>
<td></td>
<td></td>
<td></td>
<td>0.1</td>
<td>0.3</td>
<td>0.5</td>
<td></td>
<td></td>
</tr>
<tr>
<td>USA</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total FDI Stock</td>
<td>4688</td>
<td>5052</td>
<td>5409</td>
<td>6025</td>
<td>7604</td>
<td>8545</td>
<td>9504</td>
<td>10238</td>
</tr>
</tbody>
</table>

Sources: Adapted from UNCTAD (2010) Lessons Learnt of Decade

Chinese FDI was therefore the largest FDI from the south to Zambia. There were, however, also some FDI inflows from other developing countries, especially from India, Brazil and Mauritius. FDI from the south had, therefore, diversified the sources of Zambia’s FDI from the traditional EU and OECD countries. Southern sourced FDI was also playing significant roles in the Zambian economy.

**Is Chinese FDI different from FDI from other countries?**

Some analysts of Chinese FDI in Africa have suggested that it is different from the FDI that originate from the traditional sources, especially the US, EU and other OECD countries. Close examination of Chinese FDI in Zambia, however, suggests that it is not different, but complex in terms of its composition. In that regard, contrary to widely held
assumptions that Chinese FDI is made up of only state-owned enterprises, in Zambia
Chinese FDI consists of individual and private enterprises, as well as state-owned
enterprises controlled by both the central, provincial and municipal authorities in China.
The different ownership structures of Chinese FDI notwithstanding, its work ethic and
business orientation suggests that, like any other FDI from elsewhere it sought, first and
foremost, reasonable returns on capital. It also sought to provide goods and services at
competitive prices and to provide real value for money. In addition, it sought to cultivate
a good reputation and long-term business relationships with the host country. Chinese
FDI in Zambia did not appear to enjoy any subsidies or other undue advantages over
other investors. Its operations were subject to Zambian laws and regulations like FDI
from elsewhere. Thus, other than the normal commercial support that Chinese FDI might
obtain from the Chinese financial institutions, especially from the Bank of China, the
China Exim Bank and the China Africa Development (CAD) Fund, Chinese FDI in
Zambia did not enjoy any special privileges not granted to other foreign investors. Even
the small and medium-scale Chinese investors that entered Zambia, before the revision of
the minimum capital requirements for qualification to foreign investor status, grappled
with the same challenges that similar businesses in Zambian had to put up with.

B. impact of Chinese FDI on the Zambian economy
In this section, we examine the impacts of Chinese FDI on the Zambian economy. It
should, however, be noted that there is as yet very little research on the impacts of
Chinese FDI on the Zambian economy. Moreover, given that most of the Chinese FDI in
Zambia is yet to be in full operation, many of its probable impacts are equally yet to
manifest. We therefore focus, in particular, on those aspects of the economy that are
bound to be affected by FDI positively or negatively. These include: trade; public
revenues; technology transfer and know-how; productivity of labour and land; and
domestic firms. We examine each of these in turn in relation to Chinese FDI. The section
draws on a limited number of studies on Chinese investment in Zambia and other African
countries, as well as official reports on FDI in Zambia. We begin with analyzing
Zambia’s trade regime and trade flows, before examining the impact of Chinese FDI.
Zambia’s trade regime and Chinese FDI

Zambia has one of the most open trade regimes in Africa with minimum restrictions that mostly relate to security considerations. The open trade regime was considered critical to building a diversified, resilient and sustainable export-oriented economy. Exposure of domestic firms to an open competitive economy was regarded essential to competitiveness and efficiency.

Due to underdevelopment, Zambia imports most manufactured goods, including most processed foods, textiles, clothes and leather products, including footwear and furniture. Machinery, equipment, motor vehicles, spare parts and petroleum products make Zambia’s other major imports. The country’s exports are dominated by base metals, especially copper and cobalt, as well as a narrow range of engineering products, mostly copper wires and electric cables. Other exports are made up of a number of primary commodities and processed foods to a limited extent. The other main primary exports are: burley tobacco; cotton; fresh flowers, fruits and vegetable; and gemstones. Processed foods are dominated by refined sugar. In the regional markets, Zambia also exports cement and lime.

To assess Zambia’s trade performance we present trends in both exports and imports in Figure 5 for the period 2000 to 2010.
It is evident from Figure 5 that Zambia’s trade gradually improved between 2000 and 2010, with the total export earnings consistently increasing over the 11 year period. The improved performance was due to increased export earnings from both the traditional (copper and cobalt) and the Non-Traditional Exports. Zambia did not, however, experience large trade balances prior to 2003. That was largely due to increased imports of machinery and equipment for the rehabilitation and operations of the old mines and the new mines respectively.

The country experienced healthy trade balances over the last five years, in particular, except in 2008 and 2009. This was mostly due to increased exports of copper and cobalt, and some NTEs. Earnings from copper and cobalt, copper wires and electricity cables, as well as refined sugar benefitted from both increased production and the recovery of the metal prices. The increased production in all those products was due to sustained reinvestment in the mines and the relevant manufacturing processes. Increased export earnings from copper and cobalt were also buoyed by the unprecedented metal prices. Prices of copper, for example, rose from US$1560 per ton in 2002 to US$7126 in 2007 up to US $9000 currently. The copper prices have since remained relatively high, despite a decline to around US$3000 per metric ton during the 2009 global financial economic crisis. Forecasts of the metal prices, however, suggest that prices for metals would remain
high in the foreseeable future, largely due to increased demand for metals in the emerging economies, especially China and India.

Exports of fresh flowers, fruits and vegetables were in decline over the last decade, mainly due to lack of direct cargo flights to the major EU countries, which along with South Africa are the main markets for fresh produce. In contrast, exports of copper and cobalt, copper wires and electricity cables grew at a faster rate than most of the NTEs, except refined sugar, which benefited from both increased investment and access to the regional and EU markets. The performance of the NTEs was, however, mixed, because while there were significant increases in the production and export earnings of copper wires, electricity cables and refined sugar, the exports of fresh produce and cotton declined due to non-availability of cargo flights as observed earlier. Reductions in cotton production and exports, on the hand, have been due to uncompetitive prices. The sustained growth in the NTEs was therefore mainly due to the growth in the exports of the engineering products.

The large gap between export earnings from copper and the NTEs reflects the relative development and under development of the former and the latter respectively. Increased exports can, however, be expected from the manufacturing and agricultural sector in the not too distant future, given the increased investments in these sectors. Increased exports from the manufacturing and agricultural sectors will not, however, result in the NTEs closing the gap with the traditional exports, because the metal mining sector has received higher investments and a number of new copper mines are on schedule to begin production in the next few years. The copper and cobalt exports are therefore destined to remain dominant in Zambia’s exports.

**Impact of Chinese FDI on Zambia’s Trade Performance**

The impact of FDI on trade depends on its nature in terms of whether it results in the production of goods for export or the domestic market. Chinese FDI flows to Zambia though spread out in nearly all the critical sectors of the economy has not yet resulted in any noticeable changes in the country’s export trade across the sectors. The only visible
changes have been in the copper mining sector where Chinese FDI made in the late 1990s is currently contributing about 20% to Zambia’s copper exports. Besides, the recovery of the copper prices and the recent improved performance in Zambia’s balance of trade were due to the recovery of the copper prices and increased production of copper. Thus, Chinese FDI investment contributed to the latter directly, but had little to do with the increased demand for metals. Chinese FDI to Zambia was, however, bound to have a bearing on Zambia’s trade, especially in the mining, manufacturing, agriculture and tourism sectors. The FDI in the mining would not, however, contribute to the diversification of the Zambian economy. On the contrary, these massive investments were likely to further entrench Zambia as a producer of low value primary commodities. Investments in agriculture, while contributing to the diversification goal would similarly not help lift Zambia on the products value chains.

The Chinese investments in the manufacturing and service sectors, on the other hand, were bound to contribute to the diversification of the Zambian economy. Their contribution to extricating Zambia from being a producer of low value primary commodities would depend on their level of value addition. Since most of the products of most Chinese FDI in the manufacturing sector were yet to mature, it is difficult to assess the extent to which it would help Zambia participate in the production of goods at the upper and medium levels of the product value chains. Investments in manufacturing would, nevertheless have a bearing on Zambia’s trade, as some of the manufactures that are currently imported might be produced locally. This likely impact is already evident in the case of steel imports. Chinese investments in the foundries has resulted in the relative reduction in imports of steel products, as some of the demand for steel were being met in the domestic economy by Chinese-owned steel foundries. The level of foreign exchange savings from the Chinese steel foundries are, however, difficult to assess in the absence of data relating to their foreign exchange inputs. However, their output has had a bearing on Zambia’s imports of steel. Chinese FDI in the manufacturing sector has huge potential impacts on trade. However, most of the Chinese FDI in the manufacturing would be mostly in the Special Economic Zones, which were currently under construction. As a result, we cannot as yet assess what the impacts of these zones would be on trade but we
can reasonably deduce that products from the Zones will find their way into the export markets, especially China, and will therefore have a positive impact on Zambia’s foreign earnings due to higher values.

With regard to the balance of trade between Zambia and China, recent trade statistics showed China currently imports refined copper, cotton lint, leather and unprocessed hides from Zambia. Its imports from Zambia were therefore predominantly low value raw materials. Zambia, on the other hand, imported a wide range of manufactures from China, especially textiles and clothes, leather goods, furniture, plastic products and toys. The balance of trade between the two countries was currently in favor of Zambia, because of China higher volumes of imports of refined copper. In that regard, China accounted for about 10% of Zambia’s exports. Imports from China, on the other hand, accounted for only 3-4% of Zambia’s imports. Zambia’s imports from China were currently low, mainly because the country imports most of its manufactured goods, consisting of processed foods, machinery and equipment mainly from South Africa. This is largely due to proximity to South Africa, established trade relationships and the bigger presence of the South African wholesale and retail firms in Zambia. However, South Africa is also the major importer of Zambia’s NTEs, especially refined copper, copper wires, electricity cables, fresh flowers, fruits and vegetable. The balance of trade between Zambia and South Africa was in favor of the latter as nearly 50% of Zambia’s imports were from South Africa. Zambia’s exports to South Africa, on the other hand, accounted for 25-30% of Zambia’s total exports.

Chinese FDI in Zambia is yet to result in significant changes in the patterns of trade. As a result, South Africa was still Zambia’s principal trading partner. China’s investments in the manufacturing and agricultural sectors would in the long-term, nevertheless, have a bearing on Zambia’s current trade orientation and patterns. In the absence of the bulk of the actual products of Chinese FDI in the manufacturing sector coming to realization, we cannot ascertain for sure how the changes in the trade orientation and patterns would shape up. The huge investments that Zambia continues to attract in its mining sector shall pose serious challenges in terms of changing the broad orientation of the Zambian
economy. In the absence of concerted efforts to increase investments in the manufacturing sector, Zambia risks continuing as a producer of low value primary products. The Zambian authorities ought to take more proactive measures aimed at reorienting the country’s production and trade patterns. The Zambian authorities, therefore, ought to manage FDI in a manner that could promote more balanced development and specifically help the country move its production activities to the upper levels of the product value chains. Such investments would help Zambia discard the status of a LDC, as participation in the production of high value goods would raise incomes faster than the current concentration on the production and export of primary commodities. Such investments also tend to be more valuable, because they not only earn the country foreign exchange through high value exports, but also creates additional economic opportunities through forward and backward linkages. They also create both direct and indirect employment opportunities and higher quality employment than the production of primary commodities.

**Impact of Chinese FDI on Public Revenue**

Governments that rely on the private sector for the production of goods and services traditionally depend on tax revenues to raise resources for the provision of public goods and services, including security and infrastructure, which are critical to facilitation of production of goods and services, trade and development.

In Zambia the Government raises tax revenues by charging taxes on incomes, transactions of goods and through customs and excise duties on imported goods. The Government also raises some revenues on its mineral resources by charging a mineral royalty tax. Zambia does not, however, have a uniform tax regime, because the Government has over the years granted generous tax exemptions to some sectors of the economy, especially mining through Development Agreements with the investors in the sector. In principle, the income taxes are charged on income. Companies therefore pay company or corporation income tax on their profits. Similarly, individual employees also pay income tax on their wages, the so called Pay-As-You-Earn (PAYE). This is a
progressive tax in which the tax paid is based on an individual’s earnings, with high income earners paying more than those with low incomes.

For companies, income taxes depend on the sector in which they operate. The company taxes, however, range from 15% for firms in the agricultural sector and the Special Economic Zones to 30, 35 and 45% for the mining firms, other firms including the manufacturing and firms in the service sector, except the banks, which pay the top rate of 45%. On transactions in goods and services, the Government charges a Value Added Tax (VAT) currently pegged at 16%. The main trade taxes are the import customs and excise duties. Import duties, however, range from 0 to 25%. The top rate being for finished products. In addition to the company tax and VAT, firms in the mining industry are also charged a mineral royalty currently pegged at 3%.

In the absence of a uniform tax regime, taxes paid by firms vary depending on the sector. The provision of generous tax exemptions, however, erodes the Government tax base and constrains its ability to discharge its regulatory functions and the management of social and economic externalities. This has been evident from Zambia’s experience with the development agreements that were signed with the mining firms that purchased the privatized mines. We discuss that experience briefly to provide a basis for assessing the impact of Chinese FDI on public revenues in Zambia.

Zambia’s experience with the provision of generous tax exemptions to the mining firms, which acquired the privatized mines, suggests that it effectively amounted to giving up tax revenues from those mines. Although the Mines and Mineral Development Act of 1995 had prescribed the fiscal regime for the mining industry, the Government entertained waving some taxes to avoid the widespread loss of jobs, especially on the Copperbelt, where the mines were the principal employers. This situation arose because the mines were privatized at a time when the prices for copper were very low and were posing a major burden on the Government budget to sustain their operations so as to protect jobs. As a result, there was a risk of some firms closing down some mines if the situation would lead to the mining firms losing money.
To avoid any mine closures the Government signed the development agreements with the individual mining firms that had acquired its privatized mines. These agreements resulted in the Government reducing the mineral royalty tax to 0.6% from 3%. Similarly, the company tax was reduced from 30 to 25%, while customs duties and VAT on imported mining machinery and equipment were waived. In addition, the mining firms were granted 100% tax deductions on capital investments. Losses could also be carried forward for tax purposes for periods ranging up to 15 to 20 years. The development agreements resulted in the Government not collecting any significant taxes from the mining companies for about 8-10 years, even though the mining sector was the most significant sector of the economy. As a result, the income tax paid by the workers (PAYE) became the main principal source of revenue. The main contributions, however, came from the workers in the mining and manufacturing sectors. This was due to the low wages found in the agricultural and service sectors, including tourism.

From 2003 copper prices begun to recover and by 2006 had more than doubled. Attempts by the Government to renegotiate the developments agreements were, however, frustrated by the mining companies, because they wanted to maintain the status quo. In 2008 the Government imposed a new mining tax regime for the privatized mines to share in the unexpected record high copper prices. The new tax regime raised the mineral royalty tax to 3% and the company tax to 30%. Capital allowance was reduced to 25% from 100%, and most importantly, a windfall tax which was to be surcharged on profits when ever the copper prices at the London Metal Exchange or any Exchange recognized by the Director General of the ZRA reached three different thresholds. For copper prices of US$2.50 per once, a 25% windfall tax was to be surcharged. It increased to 50 and 75% for prices of US$3-3.50 and more than US$3.50 per once respectively.

The new tax regime was expected to raise US$415 million for the treasury in 2008 alone. In response to the new mining fiscal regime one of the firms, First Quantum Minerals threatened not to pay the new taxes and take the matter to the courts. When the global financial crises resulted in reduction of copper prices, the mining firms begun to agitate for reduced taxation. The new Minister of Finance and National Planning appointed by
the new President after the death of the then President agreed to review the mining tax regime. As a result, the windfall tax was repealed and replaced by a 15% variable tax on revenue. Lack of reasonable income from the mines forced the Government to audit the mining firms. The audit revealed high levels of tax evasion through under-invoicing and transfer pricing. All the audited mines were found to have under paid and have since been asked to pay their fair share to the Government treasury.

However, the new mining tax regime is difficult to manage. In consequence, there have been calls for simpler mining tax regime and improved capacities at the Zambia Revenue Authority to ensure the Government collects its fair share of the country’s mineral wealth (Lungu, 2009).

As argued earlier, in the absence of a uniform tax structure the contribution of Chinese FDI to revenues in Zambia would depend on the sector in which it operates, and the tax concessions there in. The contribution of FDI to development moreover varies across sectors and depends on the institutional conditions of the host country, especially where investor-specific incentives are provided (Haglund, 2008). We therefore ought to tease out the sectors in which Chinese FDI is involved and the institutional conditions the Government of Zambia has provided. The investment incentives in Zambia moreover tend to be reserved specifically for large-scale investment of more than US$500 000 except in the agricultural and tourism sectors where most incentives tend to be sector-wide. Thus, we ought to identify the sectors in which Chinese FDI operates and the tax concessions granted to them in the sectors and to which investment the incentives apply in order to assess the potential contribution of Chinese FDI to Government revenue and consequently social and economic development.

Chinese FDI in Zambia can be found in nearly all sectors of the economy. However, the large state-owned firms are concentrated in mining, energy, manufacturing, construction communication, finance, agriculture and the wholesale and retail sectors. The small and medium size investment is predominantly private and concentrated in agriculture, construction, manufacturing, tourism, wholesale and retail trade, as well as in the
transport sector. The agriculture, tourism, energy and mining sectors in Zambia have been granted sector wide incentives. FDI in these sectors therefore make the least contributions to the country’s tax revenue. In the manufacturing and communication sectors the generous tax incentives are confined to investment based in the special economic zones (Multi-Facility Economic Zones). However, only firms with at least capital of US$500 000 can operate in these zones. Thus, the small and medium scale investors in the manufacturing sector have not been granted any special tax incentives. As a result, they should be making significant contributions to the tax revenues. Similarly, FDI in the finance, construction, transport, wholesale and retail sectors have not been granted any general incentives unless at the time of investing, they were expressly granted specific tax incentives. As a result, most investment in finance, construction, transport and the wholesale and retail sectors regardless of origin could be expected to be making their contribution to the tax revenues. In general, however, large-scale Chinese FDI is concentrated in mining, energy and manufacturing and enjoys the generous tax incentives. Thus, large-scale Chinese FDI is unlikely to make significant contributions to Zambia’s tax revenues apart from PAYE due to the higher employment levels they generate. Predominantly small and medium scale Chinese investment in the construction, manufacturing, transport, wholesale and retail sectors could be expected to be contributing significantly to the tax revenues subject to the institutional capacity of the tax authorities to collect taxes in these sectors. Thus, the contribution of Chinese FDI to the tax revenues is dependent on the sector in which it operates and the incentives provided by the Zambian authorities. Chinese FDI also operates just like any FDI to Zambia, because it is governed by the institutional framework, laws and regulations provided by the Zambian authorities.

On the basis of Zambia’s experience with tax exemptions in the mining sector, it is obvious that Chinese FDI in manufacturing in the Special Economic Zones, agriculture, tourism and mining would not yield any significant revenues directly from the firms involved those sectors. The only significant revenue would come from the income tax that would be collected from the workers employed in these sectors. Responsibility for inadequate tax revenues that might come from the large-scale FDI, however, lies with the
Zambian authorities, which established the institutional framework in which FDI regardless of origin operates. The Chinese government and firms should not be blamed, because as Brautigam and Xiaoyang (2011) observed:

“From all accounts, the Chinese government has taken a “hands off” attitude towards African policies on these zones. We could find no evidence or even rumors of conditionality or quid-pro-quos imposed on host governments by the Chinese government in return for the development of the zones” (Brautigam and Xiaoyang, 2011, p. 35).

The Zambian Government perhaps ought to rethink its fiscal policies governing not just FDI, but all the investments in the country, because in the absence of adequate revenues, the Government would not be able to discharge its responsibilities and the expected reduction of poverty and enhanced living standards in Zambia may not be realized. The recent independent audits of the mining companies which have shown tax evasion is not a preserve of the firms from the south, but those from the north too. They also revealed serious weaknesses in ensuring tax compliance, as firms and individuals alike engage in tax evasion when not effectively managed.

**Impact of FDI on employment, skills and technology transfer, and productivity**

In this section, we turn to the impact of Chinese FDI on some of the assumed benefits of FDI, including employment generation, skills and technology transfer, and productivity of labour and land.

With regard to employment generation, there is no doubt that Chinese FDI has created employment opportunities which would otherwise not have been realized. The volume of employment created, however, remains hazy as there have been no specific employment audits for Chinese FDI, let alone FDI in general. Like any FDI, Chinese FDI creates employment opportunities for both the Chinese and Zambian nationals. In terms of the proportion of jobs taken up by the Chinese nationals, Haglund (2008) observed that 45% of the jobs during the construction of the Chambishi Special Economic Zone went to the Chinese, but the proportion of the Chinese workers, however, dropped to 20% during installation of machinery and equipment. In the nearby Chambishi mine Chinese workers
accounted for 17.5% of the labour force. Similarly, at the BRIGMM factory, which exploded in 2005, only 5 out of 59 workers employed at the factory or 8% were Chinese nationals. The bulk of the employment generated by Chinese FDI in Zambia, therefore, goes predominantly to Zambian nationals. Although the exact number of jobs created by Chinese FDI in Zambia is difficult to pinpoint, estimates of jobs created by the large to medium scale Chinese FDI, however, has been put at between 15,000 and 20,000. It is likely that these estimates do not include most of the jobs created by Small and Medium Scale private Chinese FDI. Inclusion of jobs created by the Chinese FDI in the medium and small-scale sector could probably account for 10,000 jobs, which would raise the total number of jobs created so far to between 30,000 and 50,000 jobs. The increasing Chinese FDI in Zambia also means that the jobs created are also increasing in tandem.

The high proportion (45%) of Chinese nationals employed during the construction phase of the special economic zone and in most construction projects, including the stadium in Ndola has been attributed to the need to complete the projects on schedule, and thereby keep the construction costs low. The argument suggests that the Zambian workers are not as productive as their Chinese counterparts. Low productivity among Zambian workers can be due to lack of skills and social attitudes or culture. The low productivity among Zambian workers was observed in the assessment of Zambia’s investment climate. The World Bank (2003) put the value added per Zambian worker at US$2700 per annum, far below countries like Kenya, India and China. Similarly, skills shortages have been observed by some local and foreign investors and have consequently been asking the Government to ease the restrictions on the entry of skilled foreign workers. To increase productivity of Zambian workers, most firms, including Chinese firms FDI, provide training on the job. This is true, especially for the construction and agricultural sectors where most crafts level skills are acquired on the jobs.

Whereas there is evidence of Zambians obtaining technical skills, such as brick-laying and carpentry skills from their Chinese counterparts, while working, there is so far little evidence of technology transfer taking place. The special economic zones are,
nevertheless, intended to be incubators for technological innovation. Once they are operational they might bring about some technology transfer. However, the extent to which technology might be transferred to Zambians would depend on whether the special economic zones would be isolated enclaves or would foster interaction and exchange of ideas with Zambian firms. On the basis of the current arrangements, it seems the special economic zones would be enclaves, because unlike in China where the special zones were linked with local universities, technology and research centres, the two special zones in Zambia do not have such linkages. Possibilities of Chinese FDI resulting in technology transfer would therefore depend on fostering interaction between Zambian and Chinese firms, especially in the special economic zones. In that regard, Thus, as Brautigam and Xiaoyang (2011) observed:

“At a minimum, having local investors in the zones is critical …for them to take advantage of learning opportunities. Building linkages to African research and development institutes is critical for the same reason” (Brautigam and Xiaoyang, 2011, p. 47).

Thus, for Chinese FDI and indeed any other to transfer technology to Zambia, its interaction with Zambians at the technical level ought to be provided for and enhanced.

Chinese FDI and indeed FDI from elsewhere have not brought about any conflicts with local people over land in Zambia. This is mainly because land acquisition for investment has been acquired by the government, which has also usually taken land under its control. Moreover, where the land was occupied by squatters, like was the case for the land allocated to the Lusaka East Special Economic Zone, the Government gave the people who had been living on the land adequate notice, provided alternative land and assistance with relocation and resettlement expenses and thus avoided any public outcry. Similarly, the private Chinese investors have either bought or rented land/buildings from local people and avoided conflicts with Zambians. In any case, due to the low population density, Zambia does not generally have the problem of shortage of land and serious conflicts over land.
Impact of FDI on domestic firms

Here, we examine the impact of Chinese FDI on domestic firms. Currently, there is hardly any research on the impact of Chinese or any other FDI on the domestic firms. Political commentators and newspaper reports have nevertheless suggested that the small-scale Chinese investors have worsened competition in the already over-crowded small-scale sector. The Chinese investors have in particular proved to be very competitive in terms of pricing and, we dare say, customer service despite their local inadequate language skills. People on low incomes have, in particular, found Chinese small-scale traders and farmers a good source of competitively priced goods and farm products, while the Zambian small-scale traders and farmers have resented their competitive Chinese counterparts. Over time, however, the Chinese small-scale traders and farmers seem to have been accepted by the local population as part of Zambia’s economic landscape (Mwanawina, 2008).

Chinese FDI in the construction sector also seems to have had very serious impact on both the domestic and foreign construction firms operating in Zambia, because they tend to win most construction projects put out for tender. The success of the Chinese construction firms on the Zambian market has been attributed to three main factors: competitive pricing; high quality work and timely competition of projects, usually ahead of schedule. Critics and their competitors have tended to attribute their success to payment of low wages and poor working conditions for employees. However, whereas Chinese firms generally struggled on the Zambian market with regard to wages paid to unskilled workers, most seem to have adjusted very well and are generally not worse than their competitors. In the case of large-scale Chinese firms, they have not only improved their wages, but also their industrial relations. In this regard, Brautigam and Xiaoyang (2011) observed thus:

“By 2010, Zambian workers in the CNMC mines had managed to increase their salaries on average by 12-15% and had won other benefits through their unions.” In addition, a the General Secretary of the Zambia Congress of Trade Unions acknowledged that the larger Chinese enterprises were abiding by local labour law” (Brautigam and Xiaoyang, 2011, p. 45).
Similarly, Haglund (2009) observed:

“There had been significant improvements in compliance with safety regulations by CNMC, and that industrial relations had improved… although they still had far to go” (Haglund, 2009, p. 92).

The changing behaviour and perceptions of the Chinese investors in Zambia over time show that like any other investors, they are committed to maximizing returns on their investment. Accordingly, upon entering the Zambian market, they assumed the wages were low and did not wish to pay much. Similarly, they were also willing to cut corners with safety and environmental concerns if they could reduce their operating costs and get away with it. The onus is therefore squarely on the shoulders of the Zambian authorities to regulate and enforce the laws and regulations.

**Sensitivity of the authorities to the Impact of Chinese FDI**

The Zambian authorities have been sensitive to the conduct and public perception of Chinese FDI and foreign investors generally, because the voters can show their displeasure through the ballot box. In the 2006 general elections, for example, a perception that the Government was more sympathetic to foreign investors and was “failing to collect taxes from them” and “condoning poor working conditions” contributed to the ruling party’s loss of parliamentary seats in the urban centers generally. In response, the Government revised the mining sector fiscal regime in 2008 and included a windfall tax to ensure the public treasury share in the benefits of the unexpected high prices for metal. Similarly, since 2006 it is not uncommon for Government ministers to visit Chinese owned enterprises, including mines and factories and expose and condemn any non-compliance with the safety, health or industrial working conditions. Such visits and public condemnation of the Chinese enterprises that did not conform to the regulations have certainly contributed to the improved working conditions observed in the previous section.

However, the involvement of politicians in the inspection of industrial sites suggests a failure of the regulatory institutions to effectively carry out their work. This is not surprising, because most regulatory institutions, and especially the Mines Safety
Department, the Labour Inspectorate, Environmental Council of Zambia and even the Zambia Revenue Authority to some extent have for a long time not been properly staffed and funded (Haglund, 2008). As a result, these regulatory institutions have not been able to conduct physical inspections and make the firms, including local firms accountable. There is therefore need for the Government to strengthen its regulatory institutions by providing them with adequate resources, including qualified and motivated staff, as well as adequate operational equipment, transport and funds to enable them to effectively do their work. There is also need in some cases to review the legislation governing the regulatory institutions and the labour, environmental and fiscal regulations and policies to ensure they are relevant and effective for an open private sector-led economy.

The Government has also been instrumental in ensuring harmony between the foreign investors and their workers and the Zambian populace in general. However, the friendly nature of the Zambian people generally has been the key to the prevalence of a welcoming atmosphere for foreigners, free of xenophobia. Training of some public officers, especially in the regulatory institutions in languages like mandarin could greatly improve the regulation of Chinese FDI in particular, as some challenges and problems experienced between the Chinese investors and their workers in particular, have been largely due to poor communication, because of the language barrier and poor English communication skills among the Chinese investors and workers alike.

**Conclusions and Recommendations**

In this paper we set out to evaluate the impact of FDI originating from the south on the economy of Zambia, a mineral-rich African county, but one of the 48 LDCs in the world. The paper explores the nature and behaviour of FDI originating from the south and assessed whether, it was different from the traditional FDI, which originates from countries in the north. Zambia’s economic policies, trade regime and disposition towards FDI were also reviewed, before attempting an assessment of the impact of Chinese FDI on Zambia’s trade, public revenues and on the widely perceived benefits of FDI, including employment generation, skills and technology transfer, productivity of labour and land. The impact of Chinese FDI on domestic firms was also assessed, as was the
sensitivity of the Zambian authorities to the conduct of Chinese FDI and FDI generally. Some conclusions on the outlined issues and recommendations are the drawn.

The review of the Zambia’s economic policies, trade regime and disposition towards FDI shows that the country has created an attractive policy environment for profit-seeking FDI. Zambia’s favorable investment climate has consequently attracted FDI originating from not only the traditional sources, but increasingly from the south and China in particular. Chinese FDI has been in fact, the fastest growing FDI in Zambia. It increased from US$144 million in 2004 to US$844 in 2009 and was believed to have risen to US$1.5 billion by the end of 2010. Chinese FDI in Zambia was widely spread and in many sectors ranging from agriculture, tourism, manufacturing, to energy, communication, transport, construction and mining. However, increasingly large amounts of Chinese FDI have recently gone into green-field mining projects. This investment is bound to increase Zambia’s already large mining sector further, and probably entrench the economy in the low value mineral extraction sector. Chinese FDI in Zambia’s mining sector is, however, diversified and includes mining and processing minerals other than copper, such as manganese, nickel and coal. Most Chinese FDI projects have also been in manufacturing and Zambia is host to two of the six Special Economic Zones China committed itself to develop in Africa, to enhance industrialization during the 2006 FOCAC summit. While the zone located adjacent to a Chinese owned mine is specialized in activities that seek to add value to refined copper and cobalt from the mine, the zone located in Lusaka would engage in manufacturing consumer electronic goods, textiles, clothes, toys and plastics. It would also have a hotel and an international convention centre. Both zones are still under construction, but the Chambishi Zone already has 13 Chinese firms operating there.

Chinese FDI in Zambia was also diverse as it was made of large state-owned enterprises, controlled by the central, provincial and municipal authorities, as well as the small and medium scale private enterprises and individuals. Chinese FDI operating in Zambia was not different from the traditional FDI, because it was also primarily profit seeking. Its commercial orientation was evident from choice of only economically viable ventures,
competitiveness and tendency to maximize returns on capital, as well as interest in cultivating long-term relations and upholding good reputations. As a result, Chinese FDI has dominated the construction industry in the country. Similarly, the small and medium scale private Chinese entrepreneurs in the wholesale and retail sectors, and those in agriculture have proved too competitive for many of their domestic and foreign competitors within the Zambian market. As a result, they have been unpopular among their competitors. Competitive pricing and superior customer relations have, however, endeared the Chinese traders and farmers to consumers, particularly, those in the low income groups, who appreciate affordable Chinese consumer goods and fresh produce and poultry. As a result, the Chinese small and medium scale entrepreneurs have become part of the Zambian economic landscape.

Zambia’s trade performance improved over the last decade, but there was no evidence of Chinese FDI having altered it. It increased demand for copper in China and other emerging economies, hence helping improve Zambia’s export earnings and balance of trade. Zambia is, however, still predominantly an exporter of primary commodities, and refined copper and cobalt, as well as a narrow range of associated engineering products, refined sugar and a handful of primary agricultural commodities, notably cotton, tobacco and decreasing quantities of fresh produce. The country is also still a big importer of manufactured and processed foods, machinery and equipment. South Africa, the regional economic power, was Zambia’s principal trading partner, accounting for 50% of Zambia’s imports and 25-30% of her exports. The balance of trade was in South Africa’s favor. China, on the other hand, has become Zambia’s third largest trading partner, accounting for 10% of her exports and about 3% of her imports. Textile and leather products, especially clothes, foot wear and furniture were Zambia’s main imports from China, while her exports were mainly refined copper, cotton and unprocessed leather and hides. The balance of trade is currently in Zambia’s favor.
Chinese FDI has so far not influenced Zambia’s trading patterns, because most of the investments in manufacturing and the agricultural sector are still in their inception stages. As a result, only the earlier copper mining and cotton processing investments were already contributing to Zambia’s trade.

With regard to the impact of Chinese FDI on public revenues, this study suggests the impact is unlikely to be uniform, because Zambia had a variable fiscal regime for different sectors of the economy. In general, the sectors with generous tax exemptions, such agriculture, tourism and manufacturing based in the special economic zones were unlikely to contribute to the country’s revenue. This was evident from Zambia’s experience with the tax concessions that had been granted to the privatized mines. For nearly ten years they did not make any significant contributions to the country’s tax revenues. As a result, when the prices of metals improved and the privatized mines proved reluctant to renegotiate the mining fiscal regime, the Government imposed a new fiscal regime in which it revised the company tax rate upwards from 25 to 30% and reduced the capital expenditure allowance from 100% to 25%. It also introduced a windfall tax on all taxable income. These measures raised the Government US$415 million from the mining sector in one fiscal year alone. In the wake of the 2009 global financial crisis, the mining companies pressed the government to review the mining fiscal regime introduced in 2008. To avoid reduced investment in the mining sector, the Government revised the mining fiscal regime again. It waived the windfall tax and replaced it with a 15% variable tax on taxable income exceeding 8% of the gross income. On the basis of Zambia’s experience with its previous generous mining tax regime, we have concluded that Chinese FDI in manufacturing based in the special economic zones, which enjoy generous tax exemptions on imports, 100% capital allowances, graduated company taxes and carrying forward of losses up to 10 years would not be able to make significant contributions to Zambia’s tax revenues in the short term.

Similarly, Chinese FDI in other sectors, which equally enjoy low taxes and various exemptions from import customs and excise duties, such as agriculture, tourism, information and communication technologies and energy would also not contribute
significantly to the country’s public revenues. Thus, FDI in the sectors with generous tax exemptions would not make significant contributions to the country’s public revenues. Nevertheless, Chinese FDI and indeed FDI from other countries in sectors which currently do not enjoy generous tax concessions, such as finance, including banking, transport, construction would significantly contribute to public revenues.

However, it should be noted that most tax exemptions in Zambia are granted to large-scale investment. For instance, to invest in the special economic zones and qualify for the tax exemptions, a firm ought to invest at US$500 000. Thus, most small and medium scale FDI, especially in the manufacturing sector outside the special economic zones will also make significant contributions to the country’s tax revenues. Thus, while most large-scale Chinese FDI will not contribute to Zambia’s public revenues, most small and medium investors would, depending on the tax authorities being able to collect the taxes due.

With regard to the potential impacts of Chinese FDI on employment creation, skills and technology transfer, as well as on the productivity of labour and land, this study has reached the following conclusions: (1) Chinese FDI has had favorable impact on employment and most of the jobs created have been taken up by Zambian rather than Chinese nationals. We have also conservatively put the number of jobs created by Chinese FDI at about 30 000 across all the sectors in which it is involved. Given that most Chinese investments were at the inception stage, it was evident that it was bound to create more jobs in future. (2) Chinese FDI also resulted in the transfer of skills, especially in the construction, tourism and agricultural sectors. We have therefore concluded that Chinese FDI has been critical to provision of practical skills and craftsmanship, such as bricklaying and carpentry skills, which can be learnt on the job. (3) With regard to transfer of technology, we have not found any evidence that Chinese FDI in its current form and as planned in the Special Economic Zones would result in any significant transfer of technology because of lack of linkages with the Zambian universities, technology and research institutes. Worse still, there is no clear indication that local firms would be involved in the special zones, and that they would interact and
learn from their Chinese counterparts, or even serve as suppliers. In the absence of significant local participation and involvement, technology transfer cannot take place.

Chinese FDI has also had some positive and negative impacts on some domestic firms. Most positive impacts have been amongst local suppliers who have had new increased opportunities to provide services to new clients. Negative impacts have mainly been felt by small and medium scale enterprises in the wholesale and retail sectors, as well as among small and medium poultry farmers, who have experienced increased competition resulting in loss of livelihoods in these sectors. While the small and medium scale Chinese entrepreneurs in the wholesale and retail sectors, as well as the poultry sub-sector have proved unpopular with their counterparts, consumers in the low income categories especially have appreciated the competitive prices and superior customer services of the Chinese entrepreneurs. Similar, domestic and foreign firms in the construction sector have lost a large share of the market to more competitive Chinese construction firms, both large and small, which are appreciated on the market not only for their competitive prices, but superior workmanship and timely completion of projects, usually ahead of schedule.

Chinese FDI has also helped to improve productivity of Zambian workers where the latter have acquired new skills and the Chinese work ethic, especially for workers in the construction and agricultural sector. The positive impact of Chinese FDI on productivity is, however, not sector wide, but only to those individuals with a disposition to learn and appreciate hard work. In addition, Chinese investment in the construction sector has provided additional evidence of productivity being low among Zambian workers. In this regard, Chinese firms have been working with up to 45% of Chinese workers in big construction projects to ensure completion of those projects on schedule.

Chinese FDI has therefore contributed to expansion of the Zambian economy by increasing the capital stock, employment opportunities and wider choices. It has also begun to increase the range of products produced in the domestic market thereby helping to reduce the volume of imports. For example, Chinese FDI has helped increase the
volume of steel bars produced in the domestic market and to some extent helped reduce prices and the volume of imported steel. It has, however, not yet sufficiently helped change Zambia’s trade patterns. The country is still predominantly an exporter of low value primary products and an importer of manufactured goods. On-going Chinese FDI especially in the manufacturing and agro-processing sectors could be expected to help alter Zambia’s current trade patterns. To make the most of Chinese FDI, however, the Government ought to address a number of weaknesses outlined in the next sections

Recommendations

Although Zambia has been successful in attracting significant levels of FDI, especially from China, the country has neglected the reform and upgrading of most of its regulatory laws and institutions dealing with the smooth running of an open, private sector led economy. We therefore suggest the following measure to ensure smooth running of the economy and efficient management of externalities that go with a private sector-led economy;

1. The Government should review all the laws and regulations dealing with compliance with the employment and labour laws, pollution control and environmental protection, as well as safety and health in the work place, especially in factories and mines to upgrade them and bring them in line with obtaining international best practices.

2. Government should ensure its staff in the regulatory institutions that have to regulate the operations of firms producing goods and services have appropriate skills and competences, as well as adequate equipment, machinery, transport and other resources to fulfill their mandates;

3. Given the low productivity of the Zambian workers, the Government should promote programmes to upgrade education, skills and attitudes towards productivity among Zambian workers;
4. Investors both local and foreign have complained about a shortage of appropriate skills in the Zambian economy, given the growing level of FDI. Government should take measures to ensure availability of highly trained workers. In the long term this means improved training and provision of skills and competencies required by industry. In the short term, Government ought to ease the employment and residence of foreign skilled workers in the country;

5. Given the need for a stable and predictable fiscal regime that is attractive to FDI, the Government should rethink its fiscal policies and ensure it has a stable fiscal regime that is attractive to FDI and capable of providing adequate revenue to ensure the Government fulfills its functions of providing public goods and services;

6. To ensure reduced tax evasion, especially in the extractive industries, the Government ought to upgrade skills of the staff of the Zambia Revenue Authority to ensure the collection of a fair share of taxes from all firms;

7. To ensure transfer of technology from FDI the Government should promote linkages between universities, technology and research centres with the Special Economic Zones for them to fulfill the promise of being incubators of technology;

8. Participation of local firms in the Special Economic Zones should also be promoted to ensure transfer of technology and promote partnerships with FDI and ensure the realization of technology transfer;

7. Given the increasing presence of Chinese FDI and the population of Chinese nationals, the Government should consider providing Chinese language skills to its staff in regulatory institutions that have to deal with Chinese investors on a regular basis to ease communication challenges;
References


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