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Foreign Direct Investment in Africa-Rhetoric or Reality of Development: A Review of Literature

Mulonda Munalula[1,*], **Mubita Aurick**[2]

[1]Department of Development Studies, University of Zambia, Lusaka, Zambia
[2]Department of Social Work and Sociology, University of Zambia, Lusaka, Zambia
*Corresponding author: benniemulonda86@gmail.com

Abstract This paper discusses Foreign Direct Investment (FDI) in Africa. It is a review of literature that tries to explore and give a more nuanced understanding of the realities of FDI in development in Africa. The paper first shows in the preamble that the world today has become more integrated than ever manifested in high levels of capital flows across different economies. Africa as a continent has been one of the biggest beneficiaries of such capital flows inform of FDI especially given the huge resource endowment and other investment opportunities that the continent presents. The paper then addresses the question of whether this increased inflow of FDI has translated into development for the continent and how. To answer this broad question, the paper uses information collected from secondary sources including published books, articles, seminar papers and research findings from different studies that have been done on the topic across different countries on the continent. These findings help in presenting the empirical side of the debate. The paper shows that FDI's role in development in Africa has been and still remains positive and crucial. African has benefited in various ways including reduced poverty through economic growth and employment creation among others. Notwithstanding this, there have also been some negative sides to this investment. Based on this, the paper recommends that African countries must be made attractive business environments by strengthening institutions, rule of law, its connectivity with the world and reducing the thickness of their borders. In addition, it is important that host countries must have the right and correct policies for FDI. Countries must develop and strengthen their institutional capacities not only to attract FDI but also to be able to extract some benefits from the foreign firms for their own development. Governments must also enhance human capital development in their countries so that firms can employ and utilize the local human capital.

Keywords: *foreign direct investment, development, Africa*

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1. Introduction

Today the world is in a global village. There is a high level of economic, political and social integration. The wave of globalization has increased the level of capital openness among countries. With high levels of capital openness, there has been unprecedented flow of capital across borders and nations of the world. One transmission mechanism for this kind of capital is Foreign Direct Investment. As Ntuli points out, the most visible features of globalization have not only been an increase in trade but also in investment flows and largely in form of Foreign Direct Investment [1]. Today the world is increasingly recognizing FDI as an impetus for development and many developing countries are becoming even more receptive to FDI inflows [2].

Foreign Direct Investment Refers to a cross-border investment by a resident entity in one economy with the objective of obtaining a lasting interest in an enterprise resident in another economy. The lasting interest implies the existence of a long-term relationship between the direct investor and the enterprise and a significant degree of influence by the direct investor on the management of the enterprise. Ownership of at least 10% of the voting power, representing the influence by the investor, is the basic criterion used [3]. The element of control is crucial in defining FDI as this is the main distinguishing feature from other types of investments like portfolio investment. FDI involves the establishment of income generating assets in a country which implies control of the operations. It involves in addition to capital the transfer of management, technology and organizational skills [4].

This investment can be in form of Greenfield which involves assembling of all the elements from the scratch. Such can take the form of putting up a plant and all the necessary infrastructure in order to start operating. This is a good kind of investment especially for developing economies as it helps in Infrastructure development. FDI can also take the form of take-over which implies acquisition of an existing company and this can also be in form of mergers and acquisitions [4].

Against this background, this paper reviews literature on Foreign Direct Investment in Africa with special attention to the role that this type of investment plays in the development process of the continent. The paper reviews literature on the nature of FDI in Africa, recent trends and the effects that this investment has on the development process of the continent. Further, a personal view will be given based on the arguments in the paper and some recommendations made for policy purposes.

2. Foreign Direct Investment in Africa

Africa has for a long time been portrayed as a backward continent beset by war, high disease burden, high levels of poverty and ethnic conflict [5]. Despite this, the continent presents a very high level and attractive investment opportunities. Many institutional investors and multinational corporations have found African markets as presenting the best and utmost yielding investment destinations [5].

Coupled with the various investment opportunities, the continent's development policy landscape has changed radically over the last three decades. Liberalization and privatization measures both geared at opening up to global market forces and attracting private investment have replaced state intervention and public ownership [6].

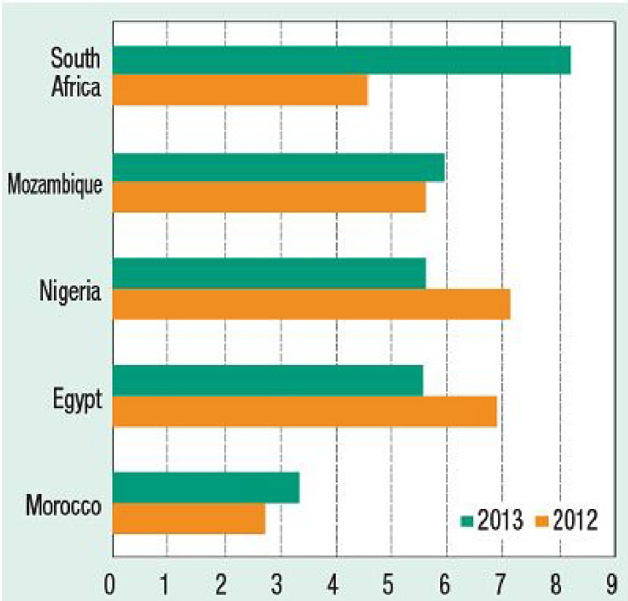
FDI to Africa takes both the form of Greenfield as well as Takeovers. These are also spread across different sectors ranging from extraction, construction, manufacturing, retail trade, etc. Historically, FDI in Africa in general has been in extractive Greenfield investment [7]. Africa is endowed with so many natural resources such as copper in Zambia, oil in Nigeria and Angola etc. Since the advent of the industrial revolution in Great Britain, many Western countries turned to Africa as a source of raw materials to feed into their growing industries. These mostly took the form of Greenfield where the investors starts everything from the scratch. This is because many Africa countries do not have the required resources to set up industries and start up production, hence they always rely on western investors to start up production processes in unexploited and unutilized natural resource endowed sector or area of their economies. This corresponds with Beckett and sudarkasa's [5] indication that the main hosts to Foreign Direct Investment on the African continent tend to share some common characteristics such as natural resource endowments.

Takeovers in terms of Acquisitions and Mergers in Africa mostly took place towards the late 1980s and early 1990s. This was the time when most of these countries liberalized their economies and opened up to the rest of the world. In countries like Zambia, the government embarked on a massive privatization programme as part of institutional and structural reforms under the IMF and World Bank Structural Adjustment Programmes [8]. This privatization programmes fostered takeovers as new investors started buying companies in these countries.

2.1. Recent FDI Trends in Africa

Recent data on FDI inflows to Africa shows that FDI has been on the increase on the continent. Country outflows of FDI are mostly a diversion to another country within the continent. Foreign Direct Investment inflows to the continent according to the latest statistics by the UNCTAD's World Investment Report show that FDI rose to $57 billion reflecting a 4% increase from the previous year and this has been driven mainly by international and regional market seeking investments and infrastructure investment [9]. By region, North African had a decline of 7% to $15.5 billion despite the overall levels of FDI remaining relatively high in the region, West Africa also recorded a decline of 14% to $14.2 billion mainly as a result of declining flows to Nigeria while Central Africa managed to attract $8.2 billion of FDI in 2013 reflecting a decline of 18% from the previous year, and in East Africa, there was an increase by 15% to $6.2 billion and orchestrated by rising flows to Kenya and Ethiopia, and Southern Africa inflows have recorded the highest growth basically because of high flows to South Africa and Mozambique [9]. In this region, FDI inflows have almost doubled. Overall, FDI investments in Africa are increasing with Southern being the highest in terms of inflows mainly because of unprecedented improvements in infrastructure development [9].

The graph below shows the top 5 recipients of FDI inflows, 2013, 2012 (billions of dollars)



Source: UNCTAD, World Investment Report 2014.
Note: Countries are ranked on the basis of magnitude of 2013 FDI flows.

Recent trends have also seen an increase in Chinese Foreign Direct Investment onto the continent. Chinese investment in Africa has increased about thirtyfold in the past decade from $500 million in 2003 to almost 15 billion by 2012 [10]. Many African countries have now established close economic and political relationship with China as a guarantee to ensure future economic prosperity basically because of the recent economic achievements or performance of China's economy [11]. Beginning the 1990s, there has been an increase in Chinese Investment in Africa and its relationship with the continent has blossomed to include issues of trade, investment, development assistance, technology transfer and training [12]. China's recent growth into an economic power house has increased demand for raw materials such as crude oil, iron ore, precious stones etc that Africa has in abundance in order to sustain its growing economy, and at the same time to use the continent to expand market for its manufactured products [13]. Because of this, there has been a reduced domination of western FDI on the continent.

3. Methodology

This paper has been written based purely on secondary sources of data. In particular, it employed the use of published books, articles (especially those from Google Scholar as a way of ensuring authenticity of information sources), and seminar papers. In order to gain detailed understanding and empirical evidence on the role of FDI in development in Africa, the paper also did a desk review of research findings of different studies that have been done in different countries across Africa. This helped in making comparisons across countries that have hosted FDI and also establishing some patterns.

4. In What Ways Does Foreign Direct Investment Contribute to Development?

4.1. Theoretical Perspectives

4.1.1. FDI and Economic Growth

There are various ways in which growth can be induced by this kind of investment. One key way is through the transfer of technology. FDI are considered as a source of technology and know-how and they foster linkages with local firms and this can help in Jump-starting growth [14]. By engaging in backward linkages with a local firm that supplies the company with inputs into their production processes, an FDI firm can help the local firm with technologies and knowledge of production so that they produce high standard products mainly because those products feed into the company as inputs into their production. This is one key transmission channel of technology transfer into the local economy. Alfaro et al (2006) [14] postulate that FDI creates positive effects on growth through the adoption of technology and know-how and these can take place through licensing agreements, imitation, employee training and the introduction of new processes as well as products by foreign firms and also through the creation of linkages with domestic firms.

FDI especially MNCs are also among the World's top source of corporate Research and Development (R&D) and because of this, they tend to have high levels of technology in their production systems [15]. Many Third World Countries do not devote or do not have enough resources to engage in Research and Development, hence they lag behind in terms of technology. Thus through the activities of MNCs, there can be some spill-over effects to the host economy in terms of technology transfer.

Besides, FDI can also help in Human capital development. Human capital development is key to economic growth. This mostly happens through employment creation that Foreign Investors create to the local people. According to [15], once these individuals are employed, their skills may be improved through training and on-the- job training. This can also have spill-over effects that can influence growth in an economy. Spill-over effects mainly take place when trained manpower moves to other firms especially the local firms where they can employ the new skills to boost productivity or they can become entrepreneurs themselves and boost productivity in the country. Above all, FDI can also contribute to economic growth through provision of infrastructure According to the Economy Watch (2010) [16], one way in which FDI contributes to development is through the provision of infrastructure such as health, education, and water supply among others. This can be done especially when the companies invest in these sectors and make them more efficient or through corporate social responsibility where the companies just give something from their profits to the local communities.

4.1.2. FDI and Employment

Unemployment is one of the greatnesses challenges of many developing countries and every government endeavors to formulate and implement policies centered on the objective of employment creation. However, for countries that have succeeding in attracting FDI, this has presented them with an opportunity to enhance employment creation in their economies. According to Javorcik (2013) [17], one of the key reasons why many policy makers strive to attract Foreign Direct Investment into their economies is to have investments that would create jobs for its population. Everyone wants a job, and especially a good job. Capturing from a worker's point of view, a good job is one that leads to higher standards of living by providing higher earnings or wages as well as greater potential for growth in earnings and high satisfaction. FDI plays a crucial role in employment creation especially for developing countries that have high levels of unemployment. This employment is mainly created by hiring people to work in the new plants that these investors set up. They help in improving aggregate domestic employment through types of jobs they create, regional distribution of new employment as well as wage levels [18].

Some scholars have also argued that FDI can indirectly create employment in private-domestically owned firms presumably caused by spill-overs [19]. This can happen in many ways for example through joint ventures. By engaging in joint ventures with local firms, FDIs can help in expanding and modernizing the company which will mean employment new people, both skilled and semi-skilled. The other indirect way of job creation is when Foreign Companies source raw materials from the local producers. Thus, the raw materials that these companies need in their production processes can be supplied by the local people and already this means employment for the people.

4.1.3. FDI and Poverty Reduction

Many developing countries have huge proportions of their population wallowing in abject poverty. There are several ways in which FDI can help in reducing poverty in the host countries. The route of this influence is mainly captured through its effects on growth. By increasing or contributing to economic growth, FDI is said to have an influence on poverty reduction. Because FDI enhances growth mainly through its rapid and efficient transfer and adoption of best practices across borders, this broad based growth is likely to have spillover effects on poverty reduction [20]. Growth always carries with it some benefits and its fruits can be redistributed to the poor through government led programmes that improve social safety nets and effectively redistribute assets and income. An illustration of this is the generation of taxes that FDI pays to the host government and these taxes can be used to support the development of safety nets by the government for the poor.

In addition, as earlier alluded to, FDI is a major source of employment in the host country. They create jobs that provide livelihoods for people and this gives them an income and ultimately lifting them out of poverty [21]. Thus FDI presents a very good opportunity for the many unemployed and those wallowing in poverty to be able to have a source of income through job creation. Job creation is also crucial for an economy as a whole in that it increases the number of tax payers in the country. Increases in tax payers mean more revenue for the government which can helps it to provide social and public services to the poor.

4.2. Empirical Evidence on FDI and Development in Africa

Today the world adores the successful and tremendous path to industrial development that the East Asian tigers followed. One lesson from this success story is the role played by FDI. FDI is said to have played a crucial role to the unprecedented growth. With this realization, many African countries are endeavoring to reorient their policies in ways that attract such kind of investment. While it is acknowledged that FDI is now a critical factor in financing development and as a means of integrating into the global economy especially in Less Developed Countries, the attraction of such kind of investment has always remained an elusive goal for many African Countries [22]. There are many reasons as to why many African Countries struggle to attract FDI. Prominent among the factors include small market size, poor infrastructure, weak regulatory frameworks, debt problems and in some instances debt problems. Important to note however is that the recent decades of structural reforms have seen a turn-around with FDI inflows being on the increase.

One good illustration of this turn-around is Morocco. Morocco today stands as one of the largest recipient of FDI in Africa and it is at the forefront of changing the image of Africa. Morocco has attracted more FDI mainly due to improvements in the macro-economic frameworks, the establishment of sound institutional and legal framework for FDI and the liberalization of the economy, simplification of administrative procedures, incentives as well as modernization of the stock exchange market, reforms of the banking sector and a massive privatization programme [23]. Important to point out also is that Morocco is used here just to give a good example of what many African countries have done in a bid to attract quality or good foreign direct investment.

The increase in FDI inflows however varies between countries depending on the attractiveness of the country. According Basu and Srinivasan (2002) [24] there is compelling evidence that FDI flows have been attracted to the continent mainly because of several factors including location advantages, investment driven by host country policies that are targeted at FDI, and also investments in response to recent economic and structural reforms.

The increase in this inflow of FDI has of course come with its own benefits. In countries like Zambia, FDI has been found to be contributing to development in several ways. FDI in Zambia has brought some technology and know-how. FDI has been instrumental in transferring skills and knowledge in the Horticulture and tourism sectors [25]. In horticulture, foreign investors have introduced new varieties of flowers and vegetables and have also helped local farmers to gain knowledge on the use of new pest and control methods as well as irrigation methods [25]. Besides, several Zambians are being trained in quality control and agriculture so as to enable them gain the necessary knowledge in agriculture sciences, and some Managerial staff employed in Foreign Firms are also being trained at various agriculture colleges under the sponsorship of the Firms so as to boost their skills development [25].

The other crucial contribution of FDI to development in Zambia has been to employment creation especially in the mining sector. Zambia is a mining economy with decades of experience in mining related activities [25]. With this, Foreign Direct Investments in this sector plays a crucial role in employment creation in the country.

In Tanzania, several registered projects are owned by foreign affiliates or companies that have operations in the country in form of FDI especially in sectors like agriculture, manufacturing, tourism, telecommunication, services, petroleum and mining. Its impact to the local economy has been in terms of job creation, government revenue, transfer of technology and skills, capital invested and foreign exchange earnings [26]. The benefits of FDI in Tanzania are also very visible in the telecommunication industry. The coming in of FDI in the telecommunication industry has created both direct and indirect employment mainly through selling of cell-phones by the local people. Airtime (phone credit), making calls and money transfer services. In additions, there is also now efficient delivery of social services like mobile telephone banking to the villagers, tax revenues and also technology transfers [26].

In a study of some Sub- Saharan Africa countries, Adams (2009) [27] reviews that Foreign Direct Investment contributes to development through the augmentation of domestic capital and the enhancement of efficiency through the transfer of technology, marketing and managerial skills, innovations and best practices. In another study of 19 Africa countries by UNIDO (2011) [28], on the effects of FDI on Africa's development, it was reviewed that increased foreign presence in some sectors of the economy led to the improvement of performance by the local firms, though in other sectors, there were some opposite results. Increased performance of local firms happens through spill-overs.

Spillover benefits of Foreign Direct Investment can happen in various ways. In Ghana, Holger Gorg and Eric Strobl found that local firms that are operated by owners who once worked for a foreign firm in the same industry just before opening their own company tend to be more productive than rivals who started up on their own [29]. Another example of spillover is that of Mauritius where it was found that 6 years after the opening of Foreign Direct Investment-led growth, 50% of the capital invested in export processing zones was from indigenous firms founded by owners who first started in foreign firms [29]. This is an illustration of skills of performance spilling-over to the local firms and the economy as whole.

Besides, foreign firms especially Multinationals Corporations are a great source of technology and when they engage in backward linkages with local firms, they mostly tend to help the local suppliers so that they produce higher products since they go into the foreign firm as inputs in the production process. This is one of the main transmission mechanisms of technology transfers into the local economy. In addition, the entry of foreign firms imposes serious competition onto the domestic firms. The nature of market competition is that everyone has to provide service or goods of high quality failure to which your business will collapse. Thus competition ignites efficiency in production which increases the quality of goods produced in an economy. Consumers always look for the products of higher quality but at the cheapest possible price and for suppliers to meet, they need a high level of efficiency.

As earlier alluded, Africa today recognizes the increasing importance of Chinese Foreign Direct Investment on the continent. Chinese investment to Africa has presented an opportunity to reduce dependence on Western Investment [12]. China provides so many relatively cheaper products to Africa than western products [12]. Chinese Foreign Direct Investment in Africa has helped in job creation for the local people. In Zambia, China is said to have created about 15000 job opportunities in the year 2010, and more than 5, 500 positions from its 32 projects in Uganda [30]. In addition, local people have also benefited in terms of roads, building of houses, hospitals and schools. These projects are sometimes done through corporate social responsibilities on the part of the investing company.

However, despite these huge investments onto the continent, China has been accused of exploiting the continent's vast resources at the expense of the local people [31]. The Human Rights Watch in their study on labor practices of Chinese investment in Zambia focusing on the copper mining industry found that while Zambian workers working in Chinese run copper mines welcome the substantial investment and jobs created, they suffer from abusive employment conditions that fail to meet domestic and international standards [32]. Many Workers that were interviewed reviewed of poor health and safety standards, long working hours and threats of being fired if you refuse to work in unsafe places.

Still in Zambia, Mopani Copper Mines, a company jointly owned by Canada's First Quantum Minerals, Swiss firm Glencore International and the Zambian government, which has mining operations on the copper belt province, by accident, released some polluted water, after a pump malfunction failed to purify it, into the reticulated water system of a private water utility company which resulted in about 1,000 residents going to the clinic because of abdominal pains, severe diarrhoea and vomiting [33]. In addition, Research that have been conducted since 2004 in Namibia's mines which are Berg Aukus, Kombat and Tsumeb have reviewed that soil and some crops grown around these mines had higher levels of metal elements in them such copper, zinc, lead, mercury and arsenic higher than the level stipulated by the World Health Organization [34]. This is also another area where mining FDI activities in Africa especially in the mining sectors have had negative effects.

5. Remarks on FDI and Development in Africa

Much as we can emphasize the benefits of Foreign Direct Investment in Africa, it is important to bear in mind however that FDIs are into business and their objective is to maximize profit. The onus there largely lies on the host country to ensure that they have the right policies to be able to not only attract FDI but also to be able to extract benefits from the firms.

In addition, it is with no doubt that FDI has some benefits to the host country. However, there is a question of how much does the country benefit. Much of foreign investment into Africa is in extractive industries like mining. In here, it is true that many local people are employed but there is a question of the kind and quality of employment that is generated. It is common for most of these firms to only employ unskilled labor that mostly work as laborers in these industries with just meager allowances. This is so especially with Chinese Investors who have always been accused of ill-treating and exploiting workers with poor working conditions and salaries. Because of such, one wonders to what extent Foreign Investment really plays a role in employment creation and poverty reduction. Also in the manufacturing sectors, there tends to be a high usage of machines and hence there is a question of how much of local people will be employed in the firm. In terms of how technology and know-how are being transferred to the local people employed in the firm also depends on the knowledge gap and how well they are able to grasp what they see in the firm's operations. If a company employs unskilled labor, it definitely becomes difficult to have this knowledge spill-over to the local workers and ultimately unto the local economy.

In addition, it is also cardinal to consider the mode of entry in terms of green field or majors and acquisitions. Africa Foreign Direct Investment takes various forms. For those countries that have had so much of Greenfield, it is more likely that FDI has contributed to infrastructure development because Greenfield involves starting everything from the scratch. Green field increases industrial activity through establishment of new plants which means new employment opportunities being created. Acquisitions may help in bringing new technology into the country, but there are times when the new owners fire the old workers and employ their own.

Broadly speaking however, FDI is important for the development process of host countries. It presents new things and new opportunities that can easily benefit the country. As the popular adage goes; to every coin, there are two sides; implying that despite the benefits that FDI brings to the country, there are also costs. Hence, the bottom line is for the country to find a way of maximizing the benefits and minimizing the costs and at the same time ensure that they are able to attract the right investments into their country.

The review of empirical literature in this paper raises important issues that could be of interest to conduct further research on. One such area is that of Chinese investment in Africa. Literature reviewed here indicates mixed information as regards Chinese Investment on the continent. In one sense, it appears to be an opportunity to the host country to extract benefits for development and on the other side it appears as exploitation of the local people and their resources. Thus with the increase in Chinese Investment on the continent, it would be very interesting to go deeper into this investment and find out what it means from the perspective of the host country; whether as an opportunity for development or as exploitation of their resources and the local people. Further, this paper has reviewed that Africa hosts more Foreign Investors from both North countries and the south (China in Particular). In Line with this, it would be also interesting look further into the comparisons between firms from the North and those from China and what they present to the host countries on the continent and also what they mean to the local people.

6. Conclusion

In conclusion, it is clear from the above that Foreign Direct Investment has been on the increase in Africa especially in the last decade. This increase in FDI has carried with it some benefits that contribute to Africa's development process. Among others of the benefits include transfer of technology, employment creation and infrastructure development. There are also negatives such as environmental harms and exploitation of the local workers especially by the Chinese FDIs. Important to realize however is that Foreign Direct Investors are part of the larger business world and every business operates on the objective of maximizing profits. Because Foreign Direct Investment is into business, it is of course with no doubt that firms will try by all means to maximize its returns on investment and if there are no right policies in the country, then the benefits might not spill-over easily. It is therefore important that the host country takes it upon itself to have the right things in place, not only for attracting foreign investment but also to ensure that they are able to absorb the benefits that come along with these investors or such kind of investment.

7. Recommendations

i. Countries must improve and enhance their investment climates so as to make them more attractive to Foreign Direct Investment. African countries must be made business environments by strengthening institutions, rule of law, its connectivity with the world and reducing the thickness of their borders. This is actually evidenced in the case of Morocco which did the same and now stands as one of the largest recipients of FDI on the continent.

ii. It is important that the host country must have the right and correct policies for FDI. The country must develop and strengthen its institutional capacity not only to attract FDI but also to be able to extract some benefits from the foreign firms for their own development. Governments must enhance human capital development in their country so that firms can employ and utilize the local human capital in their firms. When this happens, technology transfer and know-how can easily spillover to the local economy through the same people employed by the company.

iii. Host governments should also ensure that they have a clear policy on environment so as to regulate the activities of the foreign companies and at the same time ensuring that there is compliance. This can help in protecting the environment effects associated with FDI activities especially in the mining sectors.

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