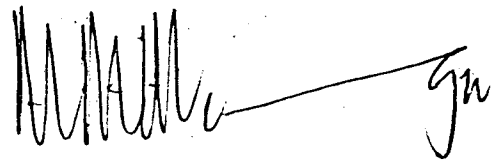


LEGAL INCENTIVES TO PRIVATE FOREIGN
INVESTORS AND ECONOMIC INDEPENDENCE
IN EMERGENT STATES WITH EMPHASIS ON
ZAMBIA



DECLARATION

I, Moono Mark Michelo Chaampali Munansangu
declare that this Dissertation has not been submitted
to any other University.

A handwritten signature in black ink, consisting of a series of vertical, wavy lines followed by a horizontal line that ends in a stylized 'M' or 'mu' symbol.

October 1980



A Dissertation submitted in partial fulfilment of
the requirements for the Degree of Master of Laws
of the University of Zambia

by

MOONO MARK MICHELO CHAAMPALI MUNANSANGU

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M.M.M.C. Munansangu

CONTENTS

PART I

Capital and Economic Development

CHAPTER I

THE ROLE OF CAPITAL IN ECONOMIC DEVELOPMENT. 1

CHAPTER II

FOREIGN INVESTMENT IN THE PAST AND ITS ROLE
IN THE UNDERDEVELOPMENT OF DEVELOPING
COUNTRIES. 18

CHAPTER III

ECONOMIC INDEPENDENCE: ITS MEANING AND
JUSTIFICATION. 44

CHAPTER IV

THE NEGATIVE EFFECT OF FOREIGN AID 58

PART II

Legal Obstacles and Incentives to Private Foreign Investment in Emergent States

CHAPTER V

OBSTACLES TO PRIVATE FOREIGN INVESTMENT IN
DEVELOPING COUNTRIES 77

CHAPTER VI

NATIONALISATION AND COMPENSATION 95

CHAPTER VII

LEGAL INCENTIVES TO PRIVATE FOREIGN INVESTORS
IN DEVELOPING COUNTRIES WITH EMPHASIS ON
EMERGENT STATES. 119

PART III

Legal Security for Private Foreign Investment

CHAPTER VIII

PROTECTION OF PRIVATE FOREIGN INVESTMENT
BY DEVELOPING COUNTRIES. 151

CHAPTER IX

SETTLEMENT OF INVESTMENT DISPUTES. 159

CONCLUSION 173

PART I

Capital and Economic Development

STATEMENT OF THE PROBLEM

Political slogans are generally out of date in the emergent states of Africa; at least the masses of the people are disillusioned about the unfulfilled promises of a better life after a decade of independence for most of these countries. African leaders therefore must embark on concrete projects of economic and social betterment.

To achieve this objective, capital is needed; a commodity which is obviously scarce in less developed countries generally. The solution therefore is to find it elsewhere - on the world money market where again it is in short supply. Therefore the satisfactory flow of foreign capital will depend on the incentives offered by emergent states.

African states have enacted laws whose primary objective is to lure foreign investors. However, whilst African investment laws should be attractive enough to woo foreign capital, they should at the same time guard against exploitation of African States to the entire benefit of foreign investors - hence the quest for ECONOMIC INDEPENDENCE. African States must reject the worst deals and extract much better terms.

The point intended to be pursued in the dissertation therefore is that the objective of African investment laws should be the creation and maintenance of co-existence

between the host country and the foreign investor. It would be nonsensical to argue for the retention of the colonial laws on foreign investment in an independent state and equally it would be foolish to advocate for the expulsion of all foreign investors or to condemn all imports of capital. Clearly both parties, the host country, and the investor have a common interest: economic development for the host and a fair return for the foreign investor.

CHAPTER I

THE ROLE OF CAPITAL IN ECONOMIC DEVELOPMENT

In the view of many economists, capital occupies the central position in economic development. Capital formation increases income which makes possible more capital formation; once the process is started it feeds on itself. According to Walter Heller,¹ capital is the "main key to economic development."² Abramovitz² argues that "It is probably safe to say that only the discovery and exploitation of new knowledge rivals capital formation as a cause of economic progress. Deficiency of capital is therefore "the most nearly omnipresent limiting factor and one that is frequently also the most severe."³

However not all economists give capital a central position in economic development. Bauer⁴ is probably the leading critic; he and Yamey argue that recent events and development have shown that although increased capital may be a necessary condition to economic growth, it is not a sufficient condition--merely to supply a backward country with capital funds or with most modern equipment will not ensure economic development; "Economic development is the result of a combination of social, cultural, political and economic changes which in turn brings about further changes - it is accompanied, inter alia, by a heightened spirit of enterprise, by capital formation, by improvements in production techniques

and by improvement in the economic qualities and productive capacity of labour." "It seems impossible therefore to isolate any one of these as the inevitable prime mover in the process of economic development and change."⁵ Thus in a nutshell Bauer and Yamey hold the view that it is more accurate to say that capital is created in the process of development than that development is a function of capital accumulation.

⁶ Cairncross advances a similar argument; "There is an unstated assumption that growth hinges on capital accumulation and that additional capital would either provoke or facilitate a more rapid rate of economic development even in circumstances which no one would describe as involving a shortage of capital. Yet there seems no reason to suppose that capital accumulation does by itself exercise so dominant an influence on economic development - in most developed countries the rate of capital accumulation out of savings is equal to about ten percent of income. If one were to assume that innovation came to a standstill and that additional investment could nevertheless yield an average return of five percent, the consequential rate of increase in the national income would normally be more than half percent per annum."⁷ Similarly Colin Clark⁸ argues that theories about economic development and shortage of capital are out of date; "It is more correct to say that

capital is created during growth than that growth is a creation of capital. The principal factors in economic growth are not physical but human . . . and human factors develop steadily but slowly."⁹

And some African leaders argue to the same effect. In the "Watershed"¹⁰ speech President Kaunda argues that while "it is true (that) we need capital investment . . . , if you want my own beliefs, I will tell you that nothing is more important than the capital we have which is the five million
Zambians and their vast natural resources."¹¹ President Nyerere has "firmly rejected the proposition that without
foreign aid we cannot develop."¹²

The issue intended to be pursued in this dissertation, however, is not whether or not capital is the most important factor in economic development; not only will such an issue be beyond the scope of this work but it would also be beyond the intellectual capability of a student of law. It has therefore been taken for granted in this dissertation that capital is one of the factors necessary for economic development. And economists including extremists like Bauer and Yamey accept this proposition (the only point of conflict being whether or not capital is the most important condition). Thus the point intended to be pursued is the proposition that one of the obstacles to economic development in Emergent States and the developing countries generally is the deficiency of capital.

As early as the early fifties, a group of United Nations¹³ experts estimated that the total amount of investment required to increase the per capita income of all developing countries (by then known as less developed countries, L.D.C.'s) by two percent per annum was 19 billion dollars but only 5.8 billion dollars was saved and invested at that time. This estimate has been criticised as being exaggerated¹⁴ for two reasons:

(a) That it did not take into account investment made in subsistence economy;

(b) That it assumed capital needs at a rate of \$2,500 per employed industrial worker which is the average in highly developed countries where labour is expensive and where a maximum of labour saving devices is therefore used. It is therefore inappropriate to developing countries faced with a shortage of capital and surplus labour.

¹⁵
Paul Hoffman (Executive Director of the United Nations Special Fund) estimated that during the decade of the 1960's developing countries would need a yearly capital influx of \$7 billion in order to accelerate their economic development and reach 2 percent annual rate of increase in per capita income.

¹⁶
According to Professor Alpert, a more realistic estimate¹⁷ is that made by Professor Hagen who calculated annual capital requirements for investment as from 9 to

12 million dollars, and the deficit, after deducting existing savings and investments, at 4 to 7 billion dollars.

18

At about the same time, Jan Tinbergen made a calculation of the amount of needed foreign aid by developing countries to raise the 1.5 percent income per head to not less than 2 percent. Tinbergen relied on the estimates prepared by the Netherland Economic Institute (1959) which show that to achieve this objective about \$7.8 billion additional investment annually will be needed as a minimum. Tinbergen then concluded that the developed countries, which at that time contributed more than \$7 billion annually should at least double their contribution to a level of about \$15 billion annually, and later increase it by an additional smaller amount to a still higher level.

And in December 1961 the United Nations set up a target to be achieved by all developing countries by 1970 - known as the target of the "Development Decade" - a minimum annual rate of growth of 5 percent. This would require capital inflows to developing countries in the sum of about \$20 billion.

George D. Woods, then President of the World Bank put the figure at 3 to 4 billion dollars a year for the same period.

19

20

Another estimate was made by P. Rosenstein. His estimate, however, is based on the foreign exchange require-

ments of all developing Countries to achieve self-sustaining economic growth: \$1.6 billion from 1961-66; \$1.6 billion from 1966-71, and from 1971-76, \$0.7 billion higher than the \$3.65 billion of assistance estimate for 1960.

Rodan's estimate is considered to be "more realistic and practical"²¹ because it is designed to help developing countries to reach a stage of self-sustaining growth and once such a state is attained, these countries will not need aid - although they may of course require funds from traditional sources: Loans on conventional terms and private investment.

BUT CAN THIS CAPITAL NOT BE GENERATED LOCALLY?

The Vicious Circle: The obvious and popular answer is that the level of savings available for productive investment in developing countries is low because of the low level of income. The low level of real income is a result of low productivity, which in its turn is largely due to lack of capital. The lack of capital is a result of the small capacity to save, and so the "vicious circle"²² is complete.

²³ Bauer and Yamey, however, argue that all the developed countries began as countries which were as poor as some of the less developed countries today - yet internal capital accumulation took place as part of a process of economic development and change. Thus, conclude Bauer and Yamey, the vicious circle has been broken in the past. Perhaps the

first answer to this argument is that opportunities and circumstances which were favourable for economic growth have changed. For instance, France; until 1890, French industry grew very slowly and even thereafter it utilised little machine and power equipment. This type of industry made less demand on the savings of the people than modern industry which is capital intensive.²⁴ Admittedly, British industry was capital intensive but this was the very source of British wealth: it accumulated from the rapidly enriching returns of new industrial mastery coupled with resources of imperial domains.²⁵

Conspicuous Consumption: In addition to the vicious circle and changed circumstances, is the psychological outlook of both the lower and higher income groups which discourages them from saving. But, it has been argued that the unequal distribution of income in England at the beginning of the industrial revolution facilitated the achievement of high rates of savings and investment. Professor Arthur Lewis,²⁶ however, points out that this can only happen when income inequality is chiefly due to entrepreneurial profits.

Professor Lewis' point is indeed valid in the case of high income groups in developing countries. They are not true capitalist entrepreneurs; their lifestyle is quite different from that which prevailed among the puritan entrepreneurs of eighteenth century England who abstained from all non-

essential, conspicuous consumption and ploughed most of their profits back into their businesses. They are certainly very different from the French who lived largely upon themselves without any desire for foreign goods. As Feis²⁷ puts it, in France, "in the villages, towns, and small cities of the provinces, there was little pecuniary display, little luxury, much sobriety of living, cautious in spending, an economy often described as 'pinching meanness' by the French authours." The high income groups in developing countries represent static positions of privilege and power: the traditional upper classes, the large land owners and the politicians who "invest" in luxurious houses and jewelry. Coupled with this is what economists call the "demonstration effect": this same privileged group invest its surplus income in luxurious cars and gadgets, aping Western consumption habits. Moreover they are (especially the politicians) among the exporters of the much needed foreign exchange; they invest their money in Swiss banks to protect themselves against social reforms and political changes - military coup d'etats. It is even worse with the oil-producing countries of the Middle East; the amount that the oil sheiks have shipped to Swiss banks is an open secret - one has only to look at the valuable property that they have bought in Geneva and London.

There are, however, some high income groups who are akin to the true capitalist entrepreneurs - mostly traders

and moneylenders. But this group is mainly an immigrant minority, the Chinese in South East Asia, the Syrians and Lebanese in West Africa and the Indians in East Africa - and therefore an easy target for economic discrimination and a scapegoat for any popular discontent, for instance, Idi Amin's so-called economic reforms in Uganda. This group obviously is reluctant to use its resources for long-term investment - and indeed it has become one of the big exporters of foreign exchange legally or illegally.

Taxation: Admittedly taxation apart from consumption is the other major method of withdrawing resources from consumption and make them available for productive investment.

²⁸
Kaldor argues that "Taxes or other compulsory levies provide the most appropriate instrument for increasing savings for capital formation out of resources. By reducing the volume of spending, taxes make it possible for the resources of the country to be devoted to building up capital assets."

²⁹
And Professor Arthur Lewis argues that all developing countries should be able to raise 20 percent of their national income through taxes. But taxes are really forced savings and as already argued the level of savings available for productive investment in developing countries is low. Any sharp increase in domestic savings in any form will result in a reduction in consumption and impose intolerable hardships especially on the low income groups. Coupled with

this is the exemption of the bulk of the politicians' income from taxation - what certainly would have been a considerable source of revenue. In most developing countries not only the President's income is exempt from taxation but incomes of Ministers as well. With the fusion of the party into government especially in African countries, incomes of top party officials are also exempt from taxation. Corporate taxation is obviously an important source of revenue in developing countries. However, to be effective, it requires comprehensive and accurate disclosure of financial and operational information of the company to the tax department which assesses the taxable income. In some developing countries, company codes are deficient on the rules of disclosure. The Zambian Company's Act is a glaring example: it does not require even domestic companies to submit annual returns, profit and loss account, balance sheet and Director's report. It is obviously impossible for the tax department to accurately assess corporate tax without these documents. As regards foreign companies the requirement is simply an audited balance sheet. However, the efficiency of the tax system is not just a matter of appropriate laws, but depends on the efficiency and integrity of tax administration. It is a well known fact that developing countries lack effective tax administration either because of unskilled and inexperienced personnel or because of corruption or both. Auditors on many occasions

certify as correct books of accounts of some companies even if they may not be correct, for purposes of evading taxation. The overall result is that a developing country collects very little revenue from taxation; as Kaldor says "It is probably not exaggerated to say that the typical underdeveloped country collects in direct taxation not more than one fifth or possible one fifth of what is due." 31

International Trade: International trade is one of the other major sources of capital for developing countries.

However, the existing pattern of international trade of the developing countries reflects two basic disadvantages: dependence on the export of primary products and dependence on the markets of western industrialized countries where they have little or no control of prices (with of course the exception of OPEC countries). The maintenance of reasonably favourable and stable terms of trade is therefore essential to sustain economic development at an even pace. But both during the interwar period and after World War II there have been violent fluctuations in the prices of primary products which have caused considerable damage to the economies of developing countries as revealed by the fourth United Nations Conference on Trade and Development: 32 "Whereas this period (from the end of the Second World War to the early 1970's) brought unprecedented expansion and prosperity to the developed market - economy countries, the experience

of the developing countries provides a disquieting contrast. Taking the 20 years from 1952 to 1972, the total gross product of the developed market economies rose from \$1,250 billion to about \$3,070 billion, in terms of 1973 prices, the increment alone (\$1,810 billion) being three-and-a-half times the aggregate gross product of the developing countries in 1972 (\$520 billion). In terms of per capita real income, the contrast is even greater. Real income in the developed market-economy countries rose by \$2,000 per head of population (again, valued at 1973 prices) from 1952 to 1972, to a figure of almost \$400 the latter year. The corresponding real per capita income for the developing countries in 1972 was about \$300, the increase since 1952 being only \$125. Thus, the increment in per capita real income over this amounted to 16 times the increment in per capita real income of the developing countries during the same period. As a result of this uneven development, the global income inequality gap has widened even further. Today, the developed market-economy countries, with 20 percent of world population, enjoy about two thirds of total world income. By contrast, the developing countries (excluding China) with almost 50 percent of world population, receive only one eighth of world income. Within the latter total, the poorest developing countries, with some 30 percent of world population, have only 3 percent of world income;

their average per capita income of approximately \$120, is only about one fifth of that for all other developing countries, and only about 3 percent of the average per capita income in the developed market-economy countries."

To conclude this chapter it must be admitted that although the role of capital has sometimes been exaggerated by some economists, nevertheless when all important factors required for successful economic development are considered, the fact remains that the lack of financial resources - capital funds - represents a serious obstacle. There are basically two solutions: domestic capital and importation of capital; but as Professor Alpert ³³ points out, as long as productivity and per capita incomes remain at their present low levels in developing countries any sharp increase in domestic saving would result in a reduction in consumption and impose intolerable hardships on the population. Therefore importation of foreign capital is really the better solution.

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CHAPTER IIFOREIGN INVESTMENT IN THE PAST AND ITS ROLE
IN THE UNDERDEVELOPMENT OF DEVELOPING COUNTRIES

It has been established in Chapter One that capital is a necessary factor for economic development though not necessarily the main factor. It has also been established that developing countries need large amounts of capital funds either to raise their per capita income per annum, or to reach a stage of self-sustaining growth; further still it has been established that domestic sources of capital in developing countries are too deficient to meet the vast capital requirements and therefore importation of capital is the solution. As Bauer and Yamey admit, though it is generally agreed that underdeveloped countries have in the main to rely upon their own resources, "the important role of foreign capital in the progress of many parts of the now developing world is also generally recognised."¹

Indeed this is not a new phenomenon: foreign capital contributed greatly to the economic development of many of the developed countries today with the United States as the outstanding example. Historically the biggest source of foreign capital was Britain followed by France and later by Germany.

BRITAINFACTORS RESPONSIBLE FOR ACCUMULATION AND OUTFLOW OF CAPITAL

In 1914, it was estimated that the annual income of

the British people was about 11 billions of dollars and of this 1.8 billions were saved.² Basically three factors were responsible for this huge accumulation of capital: the machine industry, a direct result of the industrial revolution, expanded the manufacturing capacity and consequently the volume of exports. The industrial revolution was itself a child of the agrarian revolution which was responsible for large-scale production of raw materials needed for the manufacturing industry. Secondly, British commerce expanded throughout the world. And thirdly, the British economy benefited from the development of resources of distant areas.

But why did British investment spread overseas? The natural resources and industrial operations of the British Isles were too limited to absorb all the capital, so virgin lands were needed to absorb the huge surplus capital. Secondly, there grew banks and financial institutions to handle and channel British investment. London became the financial market of the world.

It is said that a large number of financial institutions played an important part in the process of investment of British capital. However, basically only three types really appear to have played a major role: first the huge commercial banks, which were the greatest source of credit, and the banks of the British Dominion: the Commonwealth Bank of Australia, the Imperial Bank of India and the National Bank

of South Africa. Their chief concern was short-term financing. Secondly, the Financial Houses whose area of operation was basically long-term financing (the Rothschilds, Barings, etc.).³ Naturally, they undertook only the issue of government and railway bonds. Thirdly there were smaller private banks, acceptance houses and issuing brokerages which handled many of the small government and railway loans and colonial borrowing.

Coupled with these factors was the development of quick and cheap communications in the form of ships, trains, cables, etc. British capital acquired greatest mobility.

GEOGRAPHICAL SPREAD AND PATTERN OF INVESTMENT

There were very few governments to which the British did not make a loan. Europe naturally was the biggest borrower (especially Spain, Portugal and Greece - the earliest borrowers). English money, for instance, financed the first important railway in France linking Paris and Rouen.

By the end of the 19th century, however, British capital spread to young agricultural countries largely peopled by the British race. But why? Paris, Frankfurt and Berlin began to compete with London as financial markets in Europe. Coupled with this were the continuous defaults by recipient countries especially Portugal, Spain and Greece while Russia's political instability provided nothing but insecurity to the

British investor. Probably the most important factor was the new and vast opportunities that the new lands offered to the British investor together with the national sentiment since these lands were peopled by their own race (British-India, South America, Canada, Australia and the United States). It simply meant that these people would produce commodities necessary to feed British industry. And, of course, it provided security to the investor. And finally, the glint riches of Africa became the target of British investment.

The bulk of British investment was in the form of long-term publicly issued capital. Then there was not less than 300 millions of pounds in private investment. It was in the railroad and mining fields that British capital and enterprise felt the strongest attraction. These of course were the fields which provided a high return on investment. In addition British capital was used to exploit raw materials to feed the British industry - hence rubber, tea, coffee and sugar industries in the colonies.

GOVERNMENT POLICY TOWARDS FOREIGN INVESTMENT

There was little or no control of investment by government; investors claimed and got the right to carry on their activities without hindrance or control - a laissez faire attitude. It is interesting that the government did not even

impose legal reserve requirements for banks; gold could enter and pass out freely, private individuals determined the direction of the Bank of England and the Stock Exchange was allowed to manage itself as a private institution. Government only intervened to prevent fraud and activities that were against public policy. Buy why did government adopt such an attitude? There are several explanations: Britain was a staunch supporter of FREE TRADE commercial policy and the notion of freedom of capital movement fitted naturally with the free trade policy. British foreign investment brought in additional sustenance to commerce. In the case of competition with other investors (the French for instance) the British were confident that it would be met. Investment went into fields which benefited British industry (railroad construction, mines, shipping, land development). All these required capital and skilled labour from Britain. Investment was building up the British Empire especially in lands developed and owned by Englishmen - thus creating a market for British goods. However, this does not mean that there was no intercourse between government and the investor. There were occasions which provided informal exchange of views: Banks would be guided by a speech in the House of Commons, at a political dinner, or a statement in the press. The Bank of England also provided an important medium - being a bank of the state, meetings of Board of Governors brought together representatives of

large investment houses. It should also be pointed out that those who wielded financial power also wielded political power or at least they belonged to the same class - the British bourgeoisie. Partners of important Issue Houses would be members of the House of Commons, or the House of Lords. Sir Ernest Cassel and Lord Rothschild would belong to the same club, mingle in country weekends or take part in shooting parties together.

FRANCE

France was defeated by Prussia in the Franco-Prussian War in 1870. She had to pay five billion francs which she did in less than three years by selling her previous foreign investment plus the interest proceeds obtained. Thereafter she resumed the outflow of capital and after fifty years, Paris ranked as the first rival to London as a money market.

FACTORS RESPONSIBLE FOR LARGE SCALE ACCUMULATION OF CAPITAL

Unlike Britain, France did not undergo an industrial revolution. French technology was simple and individualistic. It therefore needed little capital. It did not call upon French people to finance vast and rapid transition to industrialisation. So the French accumulated enough money for their needs plus a surplus to save. It is estimated that two to three billion francs were saved each year during the last

4
decades of the 19th century.

Secondly, the French people lived in little or no luxury. They were sober people - cautious in their spending habits. Their social habits did not change much - maintaining family ties. This simply meant that France did not lose much foreign exchange to buy foreign goods (the demonstration effect, to use an economics term, is one of the contributing factors to loss of foreign exchange in developing countries today as discussed in Chapter One). Britain of course did not lose much foreign exchange also but the explanation is different. Britain was a manufacturing and therefore an exporting country using her advanced industrial technology. From export earnings, the British accumulated capital. Thirdly, unlike in Britain, the distribution of wealth in France was generally even - again as a result of French technology which was widespread and individualistic. In Britain only a few accumulated great wealth since it was those few who had capital in the first place to finance industries. Thus in France out of a population of 40 million, 10 million were shareholders in various enterprises.⁵ Fourthly, the population in France remained stationary and therefore there was less need for urban construction and development. It simply meant that government borrowing was small. Ultimately, therefore, Paris became a leading money market with the lowest interest rate in the world (it never rose above 4%).⁶

Like in Britain, however, French accumulation and exodus of capital was handled by the banks. First there were the huge private banks of which the head was the Paris House of Rothschild (which played a major role in bringing out loans required to pay German indemnity). Almost all larger loans were arranged through the agency of these banks. Out of these banks emerged smaller ones in Paris and the Provinces with limited liability. They were referred to as "Industrial Banks" because of the nature of their business. And then came the Deposit Banks; it was these banks which effectively reached the scattered savings of the French people.

GEOGRAPHICAL SPREAD AND PATTERN OF INVESTMENT

Whereas British investment spread to almost every country, that of the French was concentrated in regions penetrated by its banks, its instruction and culture primarily Europe and the Mediterranean shores. Although British capital was also invested in Europe initially (for instance, British money built the first important railway in France linking Paris and Rouen) at the end of the 19th century, it spread to young, agricultural countries largely peopled by the British race. It was for this reason mainly that France's investment concentrated in Europe. And unlike British foreign lending, that of the French was guided and often controlled by government and opinions of financial in-

stitutions. It reflected French sympathy, tradition, emotion and politics. Thus until 1914 Europe remained the biggest consumer of French money even after French acquisition of a large colonial empire.⁷ After 1887 due to the conclusion of the Franco-Russian alliance, Russia consumed a quarter of France's total foreign investment. Due to historic and religious tradition, the French bestowed upon the Sultan of Turkey and the Khedive of Egypt the right to borrow "up to the cold dawn of bankruptcy. . . ." In the Balkans, French political sympathy with the European provinces of Turkey was converted into financial support after their liberation. Spain and Portugal were France's earliest and heaviest borrowers due to racial kinship, religious and political sympathies between reigning families. In the case of Italy and Austria-Hungary, French capital increased and decreased depending on the political tide. In Latin American Republics, French investment increased in the two decades before 1914 when the republics started to look forward to France for pleasure and education. In the colonies, due to little migration by the French people, investment was small, little over a few billion francs. The French had not yet developed strong ties with the colonies. To sum up, the bulk of French investment went to foreign governments and mostly those governments whose treasuries were perpetually empty. It went to countries that lived beyond their means. Some of it, however, served a direct economic pur-

pose: it constructed railroads, bridges, ports, power plants and public utilities in Russia. It developed copper mines in Spain, coal mines in Turkey, gold mines in Africa and silver mines in Mexico.

GOVERNMENT POLICY TOWARDS FOREIGN INVESTMENT

It is in this field that French foreign investment differed greatly from that of the British. The British investors claimed that business should be left in the hands of businessmen and the government accepted this laissez faire argument. The Stock Exchange was a private enterprise and so was the Bank of England. French government policy with regards business was the very opposite. Traditionally business was subject to Imperial regulations. The government controlled the Stock Exchange in Paris and in the provinces through the Ministries of Finance, Commerce and Foreign Affairs. For instance, the Decree of 1880 provided that "The Minister of Finance can always forbid the negotiation in France of a foreign security." Thus success of any large foreign security depended on listing on the official Bourse or some direct manifestation of government favour. As already pointed out, French investment was determined not solely by sound economic principles; the Minister of Finance made this clear in 1873:

"It is necessary that the Minister of Finance and Minister of Foreign Affairs judge,

one from the point of view of the Treasury, the other from the point of view of political interest, whether there is any reason for opposing the official listing of foreign government securities, while the Stock Exchange has the duty of forming a judgement as to whether the negotiation is useful and opportune considering the Public interest."¹⁰

French banks and investors sometimes disagreed with government but their opposition and defiance were cautious and concealed. Government admitted to quotation only those foreign loans which assured France political and economic advantages. This was publicly stated in 1913 by the Minister of Finance, Caillaux. The Chamber of Deputies resolved that "the financial resources of the country should be kept above all for national needs."¹¹ Government conformed to the resolution passed by the Paris Chamber of Commerce "that whenever a foreign loan is admitted to official listing, admission should be made conditional upon the concession of advantages to French commerce and industry."¹² Thus in 1909 the government refused listing to a proposed Argentine loan because Argentina decided to purchase cannon in Germany despite the recommendation of a technical commission to purchase French cannon. Also loans to directly competing industries were sometimes kept off the French market: in 1909 government refused to grant official listing to the common stock of the United States Steel Corporation.¹³ Government insisted that the borrower should spend the money within France especially in the case of loans extended

to the Balkan states and to Turkey for purposes of purchase of steel and war materials. The same desire to secure orders prompted the government to urge banks and the Stock Exchange to secure places for Frenchmen on the board of directors or in the management of borrowing enterprises.

Over and above the economic advantages, investment was used by France to save her political interests. Government acted to prevent loans to countries whose political actions were deemed unfriendly or whose political alliance and interests seemed to clash with those of France. Secondly, admission of loans for official listing was made conditional upon pledges, assurances or compensations of a political order.¹⁴ Thirdly, government used its connections with financial circles, its influence over public opinion and press to facilitate the borrowing by states with which it was allied, or to arrange sale of loans in return for which political advantages had been secured. In some cases government itself arranged the borrowing and then selected some banking group to execute it. Where banks were reluctant, it pressurised bank executives on ground of national welfare.

The French government also used diplomatic pressure (like the British government did in the Chinese Empire, Persia, India and Africa) to secure concessions where proof of mutual benefit and other forms of inducement failed. Sometimes forceful menaces were applied to prevent these regions from escaping French hegemony. In Tunis, due to

threat of rivalry with Italian enterprise, the French government assumed political control. In Morocco French capital depended upon its government's help. In the Balkans, Turkey and the Far East, French diplomacy worked to make those governments sympathetic to France - to regard France as a rich and reliable friend. In China, by treaty, the French government caused to be set aside for French finance the main railroad and mining opportunities in the provinces bordering on its colony of Indo-China. Thus, like the British, the French proceeded with caution in securing concessions in the case of countries with strong and organised governments. They were, however, aggressive in the case of weak and disorganized empires of China, the Far East and Africa.

GERMANY

Germany has gone into history as a poor country. 15
 (Voltaire even said that it was condemned to eternal poverty).
 There was no great accumulation of capital like in France and Britain. In fact it is surprising that any outflow of capital took place at all.

Between 1870 and 1914, there was massive domestic demand of capital available in Germany. The population increased from forty million to not far short of seventy million ¹⁶ unlike France where capital accumulated but the popu-

lation remained stagnant. Available capital was also needed to finance the vast mechanised German industry. Again this was unlike French industry. British industry which had similar characteristics had more than enough capital. Cities grew in Germany and money was needed for public works and services. The rate of interest was very high on the German money market - about 5% compared to that of the French which never rose above 4%. In fact, English and French banks gave short-term loans to Germany.

It was the German great banks which stimulated and maintained foreign investment. In 1872 there were 130 deposit banks in Germany with four leading (the FOUR D's): Deutsche Bank, Diskonto-Gesellschaft, Dresdner Bank, and Darmstadter Bank. The banks possessed large capital, commanded all needed varieties of expert knowledge and judgment and their support and guidance were behind the development of the great German corporate enterprises which expanded abroad. The German great banks could not lead German savings into gambling adventures with foreign governments as easily as could the French banks. German investment leadership was more informed, vigorous, and conscientious than that of the British.

17

GEOGRAPHICAL SPREAD AND PATTERN OF INVESTMENT

Unlike in France where politics largely determined where French money should be invested, and economics in

Britain, there was no dominant factor in the case of German foreign investment. Almost until the end of the 19th century, German foreign investment was concentrated in countries on the eastern frontiers. These countries were bound by alliances and German national power as shown in the Franco-Prussian War. German capital in Europe was limited by French capital which was more freely and cheaply available. (However, by 1914, over half of total foreign investment was on the European continent). At the same time, German commercial interests and political aims began to extend to many parts of the globe. Latin America appeared to be more open to German finance and trade. Also the rapid development of the United States, Canada and other dominions attracted German capital. In fact, out of all the German investment overseas the largest share was in the American continents. In Asia the most important German investment was in China's railways. In Africa, Germany invested more in territories that were not her colonies than she did in hers. She was more interested, for instance, in South Africa's gold mines than in German plantations in Tanganyika which yielded more losses than profits. More than half of German investment was in fixed interest-bearing securities especially bonds of foreign governments, followed by the railroad securities in America, Canada, Mexico, Russia, etc. Investment in other public utilities was small and widely scattered in Turkey, Russia, the Balkans and South America. Little capital was

invested in mining since the Germans had little experience in this field and left it to the British. Other investments included interests in foreign banks, commercial, mortgage and plantation companies.

GOVERNMENT POLICY TOWARDS FOREIGN INVESTMENT

There was never in Germany a huge accumulation of capital and government intervention was therefore inevitable to satisfy the domestic demand. In addition socialists and agriculturalists were opposed to the outflow of capital. The agriculturalists argued that foreign investment was responsible for high interest rates for agricultural credit. They further argued that growth of financial and industrial interests abroad would cause agricultural interests at home to be sacrificed in tariff bargaining. The socialists opposed foreign investment because it would bring "oppression of weaker races" and would ultimately lead to international conflict. It was not surprising therefore that unlike in England where laissez faire reigned the government in Germany had to control foreign investment by legislation. The following were the guidelines to government control of the outflow of capital: "issue of foreign securities in the home market was permissible only after the domestic demand for capital was satisfied. Secondly, international commercial dealings as well as international floatation had

to be used to achieve national ends and must be placed in the service of national labour. Thirdly, even after the above conditions were fulfilled, greatest care would have to be used in selecting the securities to be floated.¹⁸

The government was, however, reluctant to formally and regularly involve itself into the money market and to a large degree it trusted private investors and the great banks for the advancement of these purposes. But if it had to intervene it had enough legal power through several institutions. In 1892 a Stock Exchange enquiry was carried out due to renewed defaults of foreign governments. The enquiry resulted in the Stock Exchange Act, 1896, an act passed to regulate admission of securities for listing and trading on the German Stock Exchange. Thus Germany adopted a kind of control that was exercised by the French government unlike in Britain where the running of the Stock Exchange was the business of businessmen. The act and subsequent acts created Boards of Admission. Various state governments and several stock exchanges had power to intervene in the decisions of these boards. The government had powers of dictation to the Central Bank - the Reichsbank and large banks depended on it as a source of credit. In addition, like in Britain, there existed private, direct, unofficial communication between heads of important banks and the Kaiser and the Foreign Office. This communication became very effective when Germany decided to become a world

power. Although there was no legal requirement, banks now consulted the Foreign Office about the political implications of foreign investment. Thus in Germany, like in France, the English theory that even in the absence of special provisions foreign lending will benefit British commerce was not subscribed to by the government.

The German government intervened to prevent foreign loans to protect domestic securities: In 1911 it prevented listing of American railways bonds since Germany itself was under the necessity of borrowing heavily - the discount rate had risen to 6% while the rate for short-term advances reached 7%.¹⁹ The government also intervened to stop certain foreign loans purely on political grounds, like the French government. For instance, whereas German capital played an important role in building Russian railways, Bismarck ordered the Reichsbank to refuse acceptance of Russian bonds as collateral security each time Russian diplomacy came into conflict with Germany. Like France, Germany in case of certain loans made it a condition that the money must be spent in Germany. In addition, like Britain and France, Germany intervened to secure concessions for its investors; the type of intervention depended on the strength of the government within whose domain the concession was sought. In Europe intervention was no more than cultivation of friendship. In the Balkans it took a sharper turn but was moderated by due regard to the interests of other powers.

It was in China, Near East and Africa that German intervention was most effective. The German government secured exclusive opportunity for German capital in the Chinese province of Shantung bestowing mining and railway rights.

German capital financed railway construction in the Boer Republics in South Africa and hence the Kaiser's telegram to President Kruger created an impression of friendship and support against the British. In Morocco, Germany used gunboat diplomacy to secure opportunity for her capital. As for the colonies Bismarck had declared that he was not a colonialist. He was satisfied with Germany's hegemony on the continent of Europe. He, however, had to give in to pressure of German nationalism which demanded that Germany should become a world power. Even so he only gave protection to private enterprise when it was clearly necessary, but still Bismarck avoided political responsibility especially where it involved conflict with foreign powers. After Bismarck, however, the government forsook the policy of continental politics (Kontinental Politik) and extended aid and protection against rivals to German enterprise. Later, acquisition of colonies became an active aspiration and the government engaged all its diplomatic skill and power to secure concessions that could lead to extension of the German Empire.

THE NEGATIVE ROLE OF FOREIGN INVESTMENT IN THE COLONIES

From the above account, it is evident that foreign investment is not a new phenomenon in today's developing countries; it dates back to the day when Western countries began the colonial process. Admittedly the amount of capital invested was minimal when compared to the amount invested at the same time in some of the developed countries today: the United States of America, Canada and Australia, for example.

The question then is why have developing countries remained economically backward - underdeveloped, notwithstanding their long economic association with the world's capital markets.- the industrialised countries? Why, for instance, did foreign investment not transform developing countries into the United States or into Canada or indeed into Britain or into France? Bauer's ²⁰ answer would most probably be--because merely to supply a backward country with money without social, cultural, political and economic changes will not bring about development. This is the modern version of the theory advanced especially by some British colonialists - that "Africans in the subsistence economy are not economically rational." This theory is thoroughly false canard when one looks at the remarkable economic transformation accomplished by Africans responding to economic incentives of the Ghanaian economy through cocoa

development, of Uganda and Tanzania through cotton and coffee; and the rapid development of Nigerian entrepreneurs, for instance. What then is the answer? It is the very colonial political and economic nexus which led to the exploitation and therefore perpetuation of underdevelopment in developing countries. As the industrial production of Western Europe expanded, and the purchasing power of its population increased its requirements for raw materials and foodstuffs expanded. Measures were therefore taken to secure the needed supplies at the lowest possible cost. Industrialised countries, in certain cases compelled developing countries to cultivate products for Europe. The Portuguese forced African farmers to plant a certain minimum area in coffee in Angola and cotton in Mozambique - the produce had to be sold to Portuguese companies at prices established by the colonial government.²¹ This continued until the fall of Caetano's fascist regime. The Dutch colonial authorities in Java forced peasants to deliver fixed quantities of coffee, sugar, tea and spices in lieu of taxes under the system of "mandatory deliveries."²² Industrialised countries made use of abundant and cheap manpower of developing countries - importing labour into areas where it could produce materials to feed their industries: the importation of Africans - so-called Negroes into the United States to work on cotton, sugar, and tobacco plantations and to Haiti and other Caribbean Islands to produce coffee and sugar; recruit-

ment of the Chinese and Indians (so-called Collies) to work on rubber plantations and tin mines in Malaya and Indonesia. In Africa, the poll tax was used as a labour recruitment device to compel the subsistence farmers to work on white farms in Kenya or in the gold and diamond mines in the Transvaal in South Africa.

Developing countries also became markets for manufactured goods produced by industrialised countries: colonies were therefore prohibited from creating industries that would compete with those of the Metropole. "The monopoly position of the mother country in relation to the supplies and markets of its colonies was considered to be the main justification for the efforts and sacrifices that the conquest and development of these colonies demanded." ²³ In France the prohibition was done under the doctrine of Pacte Colonial. As late as the fifties, 1954 to be precise, the United States Congress prohibited the Export-Import Bank from granting loans for the establishment overseas industries that might compete with American exports. The British were no exception - in their colonies practically no local processing or manufacturing industry was developed. In the Gold Coast (Ghana), the world's largest cocoa producer, a consumer who wanted to purchase cocoa for domestic use had to purchase processed cocoa from Europe or the United States. Northern Rhodesia (Zambia) a principal supplier of copper had no copper processing plant. Even

logs of rare tropical timber were not squared off in Africa but were shipped overseas in their raw form.

The money that the colonies earned was shipped to shareholders in the Metropole. The financial institutions which managed the economies kept their surpluses in the home countries, the colonial powers, thereby bolstering the economies of England and France. The little that was left was drained off through "invisibles" - insurance, shipping costs, et cetera. According to Professor Paish,²⁴ Britain up to 1952 was engaged in passing a large proportion of the imports of capital received from the colonies in the form of rapidly rising sterling balances to the non-colonial sterling area, and from 1953 to 1955 effected a net transfer of L13 million worth of capital from the colonies to herself. Britain always had a trade deficit but a balance of payments surplus with her colonies and dependencies.²⁵ Arthur Lewis once remarked that Britain talks of colonial development but on the contrary it is the African and Malayan peasants who are putting capital into Britain.

In conclusion, it is evident that the failure of foreign capital to invest in the industrialisation and diversification of the economies of developing countries has been responsible for the lop-sided development and built-in instability; the economies of developing countries today are entirely dependent on exports of primary products to the markets of industrialised countries. And with the exception

of the oil producing countries, they have little or no control over the prices. Foreign capital therefore laid the foundation for under-development of developing countries today. The internal economies were divided into two sectors: the export enclave and the hinterland. The export enclave using indigenous labour with incomes at or below the poverty datum line produced raw materials. The hinterland inevitably came to be dependent on the export enclave just as the economy as a whole was dependent on markets of industrialised countries. This then was the economic regime that prevailed at independence: nationalist governments had little or virtually no control over their economies. This is the root cause of ECONOMIC NATIONALISM. This Chapter has shown, in historical perspective that foreign capital, which was basically responsible for the development of today's developed countries, was also used to exploit others. It gives a lesson to developing countries today that they should reject foreign capital which is intended to benefit the investor alone; that developing countries should now use their bargaining position which has been reinforced by newly found political power, to extract the best deals out of foreign capital. This chapter does not, however, flatter developing countries - that they should reject all foreign investments.

FOOTNOTES

1. P.T. BAUER and B.S. YAMEY, THE ECONOMIES OF UNDER-DEVELOPED COUNTRIES, p. 142, London, J. Nisbet (1957).
2. The information in this Chapter is largely based on H. FEIS, Europe the World's Banker, 1870-1914.
3. Ibid, p. 7.
4. Ibid, p. 35.
5. Ibid, p. 35.
6. Ibid, p. 33.
7. Ibid, p. 55.
8. Ibid, p. 52.
9. Ibid, p. 120.
10. Ibid, p. 120.
11. Ibid, p. 122.
12. Ibid, p. 123.
13. Ibid, p. 125.
14. Ibid, p. 134.
15. Ibid, p. 60.
16. Ibid, p. 60.
17. Ibid, p. 68.
18. J. RIESSER, The German Great Banks and Their Concentration, p. 384, Jena, G. Fischer (1910) (in German).
19. H. Feis, opt. cit. at p. 170.
20. Bauer, "Europe Developed Without Aid . . .", CERES, FAO REVIEW Vol. 3 No. 1. Jan.-Feb. 1970 pp. 33-41.

21. C.F. SPENCE, *The Portuguese Colony of Mozambique* (Capetown and Amsterdam: A.A. Balkeman, 1951), pp. 52-56.
22. PAUL ALPERT, *Economic Development Objectives and Methods*, p. 39, N.Y., Free Press of Glencoe (1963).
23. *Ibid*, at p. 200.
24. *Lloyds Bank Review*, New Series No. 41, July, 1956, pp. 31-32 cited in *Public Enterprise and Economic Development*, A.H. Hansen, at p. 30.
25. *Financial Times*, Jan. 16, 1952, cited in *Ibid*, at p. 30.

CHAPTER III

ECONOMIC INDEPENDENCE:

ITS MEANING AND JUSTIFICATION

Like most concepts, 'Economic Independence' does not have a clear-cut definition. It must, however, be pointed out right from the start that whatever economic independence means, it certainly does not mean expulsion of all existing foreign investors from developing countries, nor does it mean condemnation of capital by developing countries. Economic independence may therefore be defined as "the ownership of the means of production of a country by the state or by the nationals or both either in total or in partnership with foreign entrepreneurs, as opposed to the total or substantial domination by aliens of the economic life of a country."¹ As Lord Feuner Brockway has emphatically put it, "Africans resent alien economic control as much as they resent alien political control. They are frustrated by alien ownership of mines, plantations and factories, and by the racial inequality of alien managements, alien skilled craftsmen, alien workers paid more than African workers on similar jobs. . . . They resent the way in which white settlers and financial corporations have taken possession of their best particularly in many parts of Africa. They regard themselves as living under an economic occupation and identify their economic masters with the colonialism which they are in revolt."² From this defini-

tion, it is clear that the quest for economic independence in developing countries today is the result of the colonial system of economic development which totally or substantially excluded nationals from the economic life of their countries as shown in the concluding part of Chapter Two. The colonies were firmly bound in a system of dependence upon the metropole and the internal economies were sharply divided into two sectors: the foreign dominated export market using indigenous labour (the Hinterland) with incomes at or below the poverty datum line, produced raw materials. The Hinterland came to be dependent on the world system of international trade - on the Metropole to be precise. The colonial governments granted extensive economic and political concessions to foreign nationals (usually those of the colonising powers) often on the basis of inequality with native interests, privilege and exploitation. Through these concessions, colonial economies came to be virtually controlled by foreign interests, a matter little affected by the formal achievement of political independence. And, as Schwarzenberger puts it, "without a minimum of political, economic or military de facto independence, de jure independence is meaningless."³ Ann Seidman points out that "it is evident, . . . that to leave critical investment decisions entirely to private enterprise motivated by the search for profits was to leave the economy essentially as it was inherited from the colonial

era: a dual economy hinged through the export enclave to the uncertainties of the world market. If the structure of the economy was to become more internally integrated, geared to increasing productivity to raise the levels of living of the entire population it was necessary for the state to intervene to ensure the implementation of a meaningful development strategy." ⁴ It must be emphasized that it is the state which must intervene because due to prolonged economic discrimination, individual indigenous entrepreneurs have neither the capital nor the skill to participate in the economic life other than as employees or as consumers.

With particular reference to Emergent States (African countries), the quest for economic independence has also been generated by ideologies which have one basic similarity, SOCIALISM. African leaders argue that meaningful economic development can only be brought about through a socialist mode of development. ⁵ This obviously is in direct conflict with the status quo left by the former colonial powers which is basically capitalist. The solution therefore is either to restructure or to completely overhaul the inherited economic institutions. In Uganda the 1970 nationalisations were announced as a move to the left and the Tanzanian policy of self-reliance - Ujamaa has been part of an explicitly socialist policy. ⁶

ZAMBIA - A PECULIAR CASE STUDY OF ECONOMIC DOMINATION

Among the emergent states, Zambia was probably the most extreme example of economic domination; virtually the whole of the manufacturing, mining and financial sectors and a large part of other service sectors (including retailing) were owned by foreigners.⁷ (As will be seen below, it is this fact which has been responsible for the "nationalisation" measures which the government has taken beginning with the 1968 Mulungushi reforms - and not therefore the result of ideological commitment as in the case of Tanzania.) At independence therefore all economic power was concentrated in the hands of a minority of white expatriate farmers, businessmen and industrialists. Zambians occupied inferior positions in both the public and private sectors as copy typists, messengers, clerks, interpreters in Government offices, labourers on European farms and as lashers in the copper mines. The position of Asians and Euro-Africans was not as bad - the former were especially prominent in the retail trade. And to add insult to injury, most businesses were owned and controlled from the racist and fascist regimes in Rhodesia and South Africa.

The larger profits from the copper mining industry (the backbone of the Zambian economy) were expatriated to Europe, America and South Africa - very little was reinvested. During the Federation of Rhodesia and Nyasaland, 1953-1963,

the revenue from copper mining was allowed in large amounts to be invested not in Zambia but in Southern Rhodesia or to subsidise Nyasaland, now an independent country - Malawi. At independence therefore the Zambian economy had the following characteristics: it was dominated by the copper industry, secondary industries were virtually insignificant. Agriculture was underdeveloped except along the line of rail on European farms. Transport facilities were poor with long and costly transport routes to the sea. And education facilities were inadequate - there were only about 100 university graduates and 1,000 secondary school graduates who were mostly absorbed into government leaving the senior positions in the private sector overwhelmingly in the hands of expatriates.

When the nationalist government was constituted in 1964, it was inevitable for it to adopt a deliberate and vigorous policy of involving Zambians in the economic life of the country by encouraging individual ownership of business. In a nutshell, economic independence to the Zambian government meant Zambianisation of foreign businesses and industrial enterprises.

THE MULUNGUSHI ECONOMIC REFORMS, APRIL 1968

The Mulungushi economic reforms prohibited financial institutions from lending capital to non-Zambians and non-

Zambian companies except where permission had been granted by the Bank of Zambia.⁹ A Zambian was defined as "a person holding a Zambian passport or a green national registration card." And a Zambian company was defined as "a company owned by Zambians 100 percent." If it was a partnership, all the partners had to be Zambians. Secondly, retail trading licenses would only be granted to Zambians in geographical and business areas popularly known as 'Second-Class' trading areas. And lastly 27 companies were 'invited to sell 51 percent of their shares to the government, at book value, to be paid for out of future profits. These measures were taken to put business firmly in the hands of Zambians. As President Kaunda put it, ". . . time is now that we must take urgent and vigorous steps to put Zambian business firmly in the hands of the people themselves just as political power is in their hands. This must be done because experience shows that since independence we have tried to assist the Zambian public with loans, as well as know-how in the firm hope that in this way we would establish and build up Zambian entrepreneurship. I regret to report to the nation that this method has been very slow and, I am afraid, it has failed. We can lend very little money to our people and this is mainly for fixed capital development. If they run short of working capital they are unable to obtain credit facilities to see them through. The banks, the

insurance companies and the other commercial financial institutions have not been very willing to assist the Zambian businessman. So the level of Zambian business has remained low and unless we take firm action now our Zambian businessmen will never catch up with the level of the resident expatriate businessman. These people have access to loan funds from banks, building societies, insurance companies, hire purchase companies, and every financial institution that exists in the country. It is therefore time to take more drastic steps to assist the people's business to bridge the gap that exists between it and the resident expatriate business."¹⁰

THE MATERO ECONOMIC REFORMS, AUGUST 1969

At Mulungushi, disappointment was expressed with the slow rate of new mining development and according to the mining companies, it was the royalty system which was responsible for this situation. The royalty system was concluded in 1950 between the Northern Rhodesia Government, the British South Africa Company and the British Government - that the British South Africa Company would enjoy royalties until 1986 subject to payment of 20 percent of royalties to the government of Northern Rhodesia. On June 17, 1969, the Zambian Government won a referendum which approved constitutional changes¹² permitting, inter alia, compulsory pur-

chase of property (without compensation in the case of absentee landlords). (The legal aspects of the takeovers is adequately discussed in Chapter VII - Nationalisation and Compensation.) The result of the referendum together with the constitutional amendment which followed enabled President Kaunda to announce the takeover of the giant copper mines at Matero.¹³ The copper mines would be taken over on a 51 percent basis and all existing private rights of ownership or partial ownership of minerals would revert to the state and all the grants in perpetuity made by the British South Africa Company would be cancelled. The 'notorious' system of royalty payments was abolished.¹⁴

THE MULUNGUSHI HALL SPEECH, NOVEMBER 1970

To complete the economic reforms, President Kaunda announced the takeover of the two main commercial banks, Barclays Bank Zambia Limited and the Standard Bank Zambia Limited, and all the building societies and the transfer of all insurance business to the State-owned insurance company - the Zambia State Insurance Corporation. He also announced an additional list of companies in which the State would purchase a 50 percent interest.¹⁵ It must, however, be pointed out that with respect to the banks, the Banking Act of 1971¹⁶ did nothing more than providing that the banks should maintain paid up equity capital amounting to not

less than K2,000,000. There has been no official explanation as to why the Banking Act fell short of providing for a 51 percent government takeover. Research (though informal) has revealed that the government was advised that due to lack of indigenous skilled manpower, such a measure would have caused financial suicide. A clear example was the corruption and mismanagement of the national bank, the National Commercial Bank.

Thus during the period 1968-70 the Zambian Government secured control over a large part of the country's economy. But there is one vital point to note: in all the economic reforms, President Kaunda has emphasized the need for foreign investment in Zambia's economic development:

"Zambia recognises the importance of attracting foreign capital. The economic reforms I have outlined today are not aimed against foreign investments, They are designed to implement in the business world the philosophy of Humanism. First, by giving the Zambian people a chance to make their way against resident expatriates who refuse to become citizens of Zambia and yet continue to enjoy, by exploiting us, our economic boom, and second, by letting the State and ultimately the common man control the activities of certain types of large-scale business and share in its rewards." ¹⁷ Dr. Fortman ¹⁸ points out that Zambian

Humanism is not for socialism which condemns private enter-

prise. Zambian Humanism will tolerate any economic system which can be guided along the right lines insofar as economic growth and human relations are concerned. Zambian Humanism believes that free enterprise can work - the problem is how to control it. This is the basic message of Mulungushi. It will be easier for the Government to communicate its ideas to Zambian businessmen than to expatriates. Zambia's quest for economic independence therefore has not been a product of commitment to ideology - socialism like in Tanzania. There is a remarkable difference between Tanzania's Arusha Declaration and Zambia's Mulungushi Declaration: basically Tanzania does not believe in private enterprise. Zambia, on the other hand, believes in controllable private enterprise, allowance being made for profits but not to exploitation. The 51 percent takeovers might be regarded as controlling measures. If the aim was not to control but to run the firms in question, the government would have fully nationalised them. Zambia's encouragement and accommodation of foreign investment is based on a pragmatic approach to economic development in the developing countries where capital is scarce and this policy has been underlined by successive Finance Ministers in their budget speeches. As early as 1968 Elijah Mudenda made this point clear, "Since we have not reached a stage where we can develop our own technology and undertake research, we still have to depend,



in some measure, upon industrial countries to provide this service. The most effective way of embodying the results of such endeavours in our economic expansion is to encourage other nations to participate in the development of Zambia.

20
 . . . " John Mwanakatwe made the same point in his 1977 budget speech: "It is equally important for us to recognise the role of foreign private investment in our development. His Excellency the President in his address to this session has already made the point that 'there are a number of sectors of the economy with tremendous scope for private investment.' His Excellency has in fact gone further to say that the Industrial Development Act will be promulgated this year. In this way we can encourage foreign private investors to come and participate in the noble task of developing the rich potential of Zambia. I should like to reiterate that in order to attract private investors, we have consistently offered them the required facilities and reasonable incentives by way of a fair return on investment and reasonable externalisation of profits."
 21

Economic independence therefore accommodates foreign investment - there is only one condition - it must be strictly participatory and developmental and nothing else and this point was made very clear by President Kaunda in the 1968 Mulungushi reforms, "We shall welcome foreign capital as in the past. . . . All we seek of investors is the understand-

ing that we welcome them as participants, and not controllers, of our economic development process. Zambians, like Europeans, Americans, Scandinavians, Soviets or Chinese, in their respective countries, must be controllers of not only the political but the economic destiny of this country." ²²

Indeed this is the theme of this dissertation: it would be unrealistic to condemn or expel all foreign investors from developing countries. There is obviously a large area of common interest. The concern of developing countries should be to see that investment arrangements fall within the area of common interest and if possible nearer to the host country's needs than hitherto.

FOOTNOTES

1. My own definition.
2. FENNER BROCKWAY, *African Socialism*, p. 14 (1963).
3. SCHWARZENBERGER, *The Principles of International Economic Law* 117 *Re cueil de Cours* (1966) 1, 31.
4. ANN SEIDMAN, *Comparative Development Strategies*, in *East Africa*, p. 75, Nairobi, E.A. Pub. House (1972).
5. *The Arusha Declaration and Tanu's Policy on Socialism and Self-Reliance*, Dar es Salaam (1967).
6. *Ibid.*
7. MARK BOSTOCK and CHARLES HARVEY ed., *Economic Independence and Zambian Copper*, Praeger, 1972, pp. 3-4.
8. *Ibid.*, at p. 4.
9. KENNETH KAUNDA, *Zambia's Economic Revolution*, address to UNIP National Council at Mulungushi, April 19, Govt. Printer, Lusaka (1968).
10. *Ibid.*, p. 24.
11. M. Bostock and C. Harvey, *opt. cit.* p. xix.
12. *Ibid.*, p. 125.
13. See the *Matero Reforms*, *Ibid.*, note 1.
14. *Mines Acquisition (Special Provisions) Act No. 28, 1970.*
15. KENNETH KAUNDA, *This Completes Economic Reforms, Now Zambia Is Ours*, pp. 9-12.
16. *Act No. 43, 1971.*
17. *Zambia Towards Economic Independence*, *Ibid.*, note 9, p. 44.

18. FORTMAN, Humanism and the Zambian Economic Order,
After Mulungushi, p. 99.
19. See the Arusha Declaration.
20. Hansard No. 13: Debates of the 4th session of the
First National Assembly, 1968, Col. 51.
21. Budget Address, Han. 1977 at p. 12.
22. Towards Complete Independence, Ibid, note 1, p. 43.

CHAPTER IVTHE NEGATIVE EFFECT OF FOREIGN AID

The theme of this dissertation is that foreign capital is necessary for economic development in the developing countries and therefore incentives must be given to foreign investors to ensure satisfactory flow of foreign capital. It would be unrealistic to argue for either the expulsion of all foreign investors or for the condemnation of all importation of capital. What is needed is a greater awareness among developing countries of the dangers so that they can reject the worst deals. The full bargaining strength of developing countries has not been used because of inexperience and ignorance. This chapter discusses one form of foreign capital, popularly known as foreign aid - to show that it is one of the forms of foreign capital which may have little or no economic value to a developing country. It is important, however, to define foreign aid before proceeding any further.

The United Nations has insisted that the term "foreign aid" should be restricted to mean "grants and long-term loans¹ for economic purposes." It has also been argued that aid should include virtually all aspects of economic relations between developed and developing countries, not only grants and loans but private investment and trade.² There may be some merit in including into the definition official loans

at commercial rates on the basis that the economic and political climate in some developing countries is such that private commercial sources would not hazard their money but, it is submitted, there is no convincing reason why foreign aid should include private foreign investment. For the purposes of this work, the definition which has been adopted is the definition given by Raymond F. Mikesell: "I shall define official foreign aid as a transfer of real resources or immediate claims on resources (for example, foreign exchange) from one country to another, which would not have taken place as a consequence of the operation of market forces or in the absence of specific official action designed to promote the transfer by the donor country." ³ This definition includes:

(i) Bilateral loans and grants of commodities, services, and foreign exchange, by governments to foreign countries.

(ii) Loans and grants of commodities, services, and foreign exchange, by multilateral agencies out of funds supplied directly by governments or from funds borrowed in private international capital markets, guaranteed by member governments.

(iii) Assistance to compensate countries for balance of payments deficits arising from unforeseen or temporary causes or for short-term fluctuations in prices of exported commodities or in export earnings.

(iv) Government sales of commodities to foreign countries for local currencies which are subject to restriction as to use by the recipient.

(v) Importation of commodities by governments at prices (or by private entities required by their government to pay higher than international market prices), including participation and cooperation by governments designed to raise or maintain prices of commodities at levels higher than would prevail in the absence of such arrangements.

(vi) Private loans, credits, or direct investments, guaranteed by the government of the capital exporter against loss from all or specific risks.

By the above definition therefore private foreign investment which is wholly induced by the operation of market forces or devoid of specific government action cannot constitute aid. And the argument in this dissertation is that developing countries will benefit more economically from private foreign investment than from economic aid - hence the emphasis on incentives to foreign investors. The task then is to justify this proposition; why should developing countries discourage or reject foreign aid? To answer this question, it is proposed to discuss critically the motives of the donors of foreign aid - are the motives economic? Is foreign aid really designed to develop the recipient countries?

AID FROM THE DONOR'S POINT OF VIEW

It is obviously beyond the scope of this work to discuss the motives of all donors of foreign aid - consequently only the objectives of the biggest donors of foreign aid will be discussed.

THE UNITED STATES OF AMERICA

The preamble of the Foreign Assistance Act, 1961 states the overall purpose of American foreign aid as the promotion of the foreign policy, security, and general welfare of the United States by assisting peoples of the world in their efforts toward economic development and internal security, and for other purposes." ⁴ Section 102 of the Statement of Policy is even more expository:

"It is in the sense of the Congress that peace depends on wider recognition of the dignity and survival of free institutions in the United States can best be assured in a worldwide atmosphere of freedom.

To this end, the United States has in the past provided assistance to help strengthen the forces of freedom by aiding peoples of less developed friendly countries of the world to develop their resources and improve their living standards, to realise their aspirations for justice, education, dignity, and respect as individual human beings, and establish responsible governments.

The Congress declares it to be a primary necessity, opportunity, and responsibility of the United States, and consistent with its traditions and ideals, to renew the spirit which lay behind these past efforts, and to help make a historic

demonstration that economic growth and political democracy can go hand in hand to the end that an enlarged community of free, stable, and self-reliant countries can reduce world tensions and insecurity.

It is the policy of the United States to strengthen friendly foreign countries by encouraging the development of their free economic institutions and productive capabilities and by minimising or eliminating barriers to the flow of private investment capital.

Also, the Congress reaffirms its conviction that the peace of the world and the security of the United States are endangered so long as international communism continues to attempt to bring under communist domination peoples now free and independent and to keep under domination peoples once free but not subject to such domination. It is, therefore, the policy of the United States to continue to make available to other free countries and peoples, upon request, and assistance of such a nature and in such amounts as the United States deems advisable and as may be effectively used by free countries and peoples to help them maintain their freedom. Assistance shall be based upon sound plans and programs; be directed toward the social as well as the economic aspects of economic development; be responsive to the efforts of the recipient countries to mobilize their own resources and help themselves be cognizant of the external and internal pressures which hamper their growth; and shall emphasize long-range development assistance as the primacy instrument of such growth."⁵

The objectives of the United States for providing aid can therefore be summarised as follows: National Security, Humanitarian, National Economic Benefit and Political.

NATIONAL SECURITY

After the Second World War, the United States assumed the role of "big brother" or "father and custodian" of democ-

racy against the suspected or actual threat of communism. This kind of thinking is reflected in writings of Americans like Lloyd D. Black: "Between 1945 and 1950 communist aggression in Europe and Asia subjugated some 14 nations covering over 5 million square miles and including more than 700 million people. The Free World is still threatened by the most dangerous aggression of aggressive power in history. The Soviet Union and Communist China maintain the largest collection of men under arms ever assembled in peace time. They possess nuclear weapons and are striving steadily to increase their nuclear capabilities. They possess or control great quantities of raw materials. Uninhibited by moral or humanitarian considerations, their leaders have imposed a massive system of domination under which all human and material resources are marshalled in pursuit of the extension of communist power. Their leaders have vowed that their system will eventually dominate the entire world." ⁶ The main objective of the United States in providing aid is evidently defence; the United States has to be satisfied that its aid will enable to maintain a military establishment capable of dealing with actual or threatened aggression which would lead either to communist domination or to domination by a group, under foreign influence to the United States security. The most glaring examples of this objective are Turkey, South Vietnam, South Korea, Thailand, Formosa and Iran which have received the largest bulk of

of American aid not because they are the most needy but because they are the most anti-communist.⁷ In the Middle East Israel receives the biggest volume of American aid while a poor country like Egypt receives very little.⁸

HUMANITARIAN

The humanitarian objective of American aid is directly related to the national security objective and it is usually expressed by the President in his foreign aid message. In his foreign aid message to Congress, President Johnson stated the objective of American aid as follows: "For our own security and well-being and as responsible freemen, we must seek to share our capacity for growth and the promise of a better life, with our fellowmen around the world. That is what foreign aid is all about."⁹ The humanitarian objective of American foreign aid was also stated by President Kennedy: "The 1960's can be - and must be - the crucial 'decade of development' - the period when less developed nations can make the transition into self-sustained growth - the period in which an enlarged community of free, stable, and self-reliant nations can reduce world tensions and insecurity. For we are reaching a 'decade of development' on which will depend, substantially, the kind of world in which we and our children will live."¹⁰ The humanitarian objective is so related to the national security objective that it can

be argued that the former simply legitimises the latter. This is reflected in President Eisenhower's Annual Report to the Congress on the Mutual Security Program: "We have had as our goal the promotion of peaceful change for millions of our people in Latin America, Asia, and the Middle East who are seeking domestic tranquility and a better way of life. We have responded to the hope of these millions for a decent future for themselves and their children through well-conceived programs of economic and technical assistance. . . . Our common safety has been of equal concern and it has the free people of the world in a sustained common defense against overt attack or suppression of liberty. . . ." 11

NATIONAL ECONOMIC BENEFIT

American aid provides an indirect subsidy for U.S. exporters and in fact an examination of United States foreign assistance since 1960 indicates the growing importance of export promotion as an objective of aid policy. 12 In 1965 the promotion of United States exports became an explicit criterion for selecting capital projects and commodities for aid financing. In order that the export promotion objective works, the United States insists that the developing countries must take collateral measures to induce local importers to shift their purchases to United States suppliers. The measures may include the removal of discriminatory bar-

riers to importing United States goods, the reduction of tariffs so as to favour United States goods, and the use of licensing to favour exports from the United States. It is indeed a case of aid for the aiders; if American aid was intended for the development of the recipient country, the latter should be allowed the option of purchasing from the cheapest source. Thus aid acts as the modern measure by developed countries to ensure that developing countries remain markets for their goods.

THE POLITICAL OBJECTIVE

Lloyd D. Black points out that any kind of American aid ultimately serves a political purpose.¹³ As a matter of fact the political rationale is frequently preponderant in decisions to provide aid. As stated in AID's Fy 1966 Summary Presentation to the Congress: "It (Aid) is provided primarily to enable larger defense efforts to be undertaken in less-developed nations threatened by Communist expansion and to avert situations of dangerous instability in sensitive areas. In a few instances it is also provided to encourage independence of action in nations susceptible to Russian or Chinese Communist domination, to assure access to U.S. military bases and in other ways to support or promote economic or political stability."¹⁴

As the number of independent developing countries increased, American aid was used and it is still being used

to bolster political leaders believed best for U.S. interests or to tip the balance against the recognition of the Chinese Communists or to swing critical votes in international organisations like the United Nations and its agencies. It is said by Europeans that during the late forties and early fifties, the administrators of the Marshall Plan yielded more power than the U.S. Ambassador; ¹⁵ as the old adage goes, "He who pays the piper calls the tune."

FRANCE

French colonial policy was the integration of her colonies into Metropolitan France. France therefore provided her colonies with substantial amounts of budget support and technical assistance in the form of teachers, administrators, technicians and advisers and by supporting the prices of their commodities which were shipped to France. When her colonial policy was thwarted, much the same type of assistance was continued, even after the colonies became independent. France's aid constitutes the largest proportion of national income of any of the donor industrial countries and much of it takes the form of grants. ¹⁶ The special preferential trade treatment given by the European Economic Community (E.E.C.) to the former African colonies of the E.E.C. members was a brain child of the French.

OBJECTIVES

One common objective of European aid is to maintain the link with former colonies. France strives to maintain a French community of nations characterised by membership in the French franc area, the existence of the French language and culture, close economic relationships, and a strong French influence over the foreign policy of these countries. French aid objectives can therefore be summarized as:

POLITICAL: France hopes to derive diplomatic support from the recipient countries in regional and international organizations.

ECONOMIC: France derives economic advantages from supplying in the form of aid high quality machinery and installations. Part of French aid is designed for industries which use French machinery.

MILITARY: Although the national security objective is not as predominant as in the case of American aid, French aid has a military objective; France obtains international facilities for telecommunications and transport from recipient countries.

BRITAIN

Britain was the first country to give aid to developing countries under the Colonial Development and Welfare Acts; the aid was, however, confined to her colonies and dependencies. It was provided in the form of grants and to a lesser extent in the form of long-term loans. As observed above, the common objective of European aid is to maintain the link with their former colonies. Thus in the case of Britain only about ten percent of her aid has gone to countries other than colonies and independent Commonwealth countries - and even much of this has gone to countries which had been British mandates or dependencies like Jordan¹⁷ and Sudan. This in fact is a deliberate British aid policy as stated in the White Paper - OVERSEAS DEVELOPMENT: THE WORK OF THE NEW MINISTRY (the Ministry of Overseas Development): "Countries which are members of the Commonwealth have a special claim on us. . . . We shall hope, nevertheless, to be in a position to increase our aid to foreign countries as our resources permit."¹⁸

OBJECTIVES

In addition to the basic objective of maintaining a link with former colonies, the White Paper states four other objectives of British aid: moral, political, national economic benefit and development of the recipient country.

MORAL: "Our aim is to do what lies in our power to help the developing countries to provide their people with the material opportunities of using their talents, of living a full and happy life and of steadily improving their lot. The basis of the aid programme is therefore a moral one. . . ."

POLITICAL: "It (our aid programme) can at the same time be defined in political terms. The international discussion to which it gives rise is an important part of international politics. . . ." ²⁰

NATIONAL ECONOMIC BENEFIT: Britain hopes to derive economic benefit from aid as a trading nation - aid will increase the prosperity of developing countries thereby expanding international trade. ²¹

ECONOMIC DEVELOPMENT OF THE RECIPIENT COUNTRY: The White Paper states that in the allocation of aid, ". . . preference should be given so far as possible to those countries and regions where it will have the greatest effect on development in the long run. . . ." ²² Admittedly, Britain, unlike other donor countries, has maintained a good record in ensuring that its aid has an economic rationale for the recipient country. Since the passing of the Colonial Development and Welfare Acts, a substantial part of British aid made available for economic and Social development

generally undertaken in the framework of comprehensive development plans.

AID FOR THE AIDERS

In view of the uncertainties that surround foreign aid, as seen above, it is submitted that developing countries should discourage and in certain respects reject it. It is evident that the selfish motives of the donor countries is paramount over the economic development of the recipient country of which foreign aid is supposed to serve. Usually the donor country not only feels that it is entitled to know for what purpose its money will be spent; it also wants to be assured that its money will be spent on projects which will meet with its approval. The donor country normally sends its own experts to execute its aid programmes. The priorities worked out therefore become the priorities of the donor country. As Kamanda put it, aid is 'aid for the aiders.'

23

EXTERNAL DEBT AND THE PROBLEM OF DEBT-SERVING

One of the adverse effects of foreign aid is the worsening indebtedness and the debt-service position of developing countries. UNCTAD IV (Report of the Secretary General) estimated the external indebtedness of the developing countries from \$9 billion at the end of 1956, to \$90

billion at the end of 1972, and \$120 billion today (for the non-oil exporting countries alone). The overall payments deficit of the non-oil exporting developing countries was \$12 billion in 1973, \$45 billion in 1975 and it can be expected to remain in the region of \$35-40 billion in the years immediately ahead. Latin America, which has a long history of foreign aid, has the largest debt among the developing countries and even more so is its debt service. In the mid-1950's, the debt amounted to \$4 billion only and yet by the end of 1967 it had amounted to \$14.1 billion. This means that the debt has been increasing at an annual rate of 11 percent. Although the debts of other developing countries are not as high, they are likely to be worse; their debts have been accumulating in recent years at a faster rate. At the end of 1970 Africa's external debt amounted to approximately US \$10,693.5 million (see Table on the next page).

THE INTERNATIONAL FINANCIAL INSTITUTIONS

Foreign aid, as defined above, includes 'Loans and grants of commodities, services, and foreign exchange by multilateral agencies out of funds supplied directly by governments or from funds borrowed in private international capital markets, guaranteed by member governments.'

TABLE I

AFRICA'S EXTERNAL PUBLIC DEBT OUTSTANDING BY COUNTRY AND
TYPE OF CREDITOR
31 DECEMBER 1970

Million US \$

Country	Disbursed only	Total
AFRICA-TOTAL	<u>7,625.5</u>	<u>10,693.5</u>
Botswana	12.4	13.3
Burundi	7.3	9.5
Cameroon	114.7	218.3
Cent. African Rep.	20.4	29.4
Chad	40.9	50.7
Dahomey	39.5	54.8
East Afr. Community	151.1	245.8
Egypt (Arab Ref. of)	a/	a/
Ethiopia	169.0	270.2
Gabon	95.3	115.4
Ghana	498.8	571.5
Guinea	283.6	378.4
Ivory Coast	a/	a/
Kenya	282.3	393.8
Lesotho	7.1	7.5
Liberia	157.5	176.8
Malagasy Rep.	95.4	137.7
Malawi	121.1	155.8
Mali	236.2	287.7
Mauritania	27.8	38.6
Mauritius	27.9	43.0
Morocco	636.4	854.7
Niger	32.0	62.8
Nigeria	463.6	683.4
Rwanda	1.9	11.6
Senegal	84.1	114.4
Sierra Leone	66.0	84.5
Somalia	74.0	105.2
Southern Rhodesia	247.9	247.9
Sudan	285.5	339.0
Swaziland	27.9	27.9
Tanzania	220.7	575.7
Togo	35.7	39.9
Tunisia	522.7	787.3
Uganda	122.5	183.6
Upper Volta	20.4	30.7
Zaire	307.5	579.4
Zambia	491.6	615.8

Source World Bank Annual Report, 1972 Table 5, p. 82

a/ An estimate for this country was included in the overall total

b/ Less than US \$50,000

Including undisbursed

Country	Bilateral official	Multi- lateral	Private		
			Suppliers	Bank	Other
AFRICA-TOTAL	6,052.4	2,011.3	1,207.9	425.9	995.0
Botswana	5.7	6.1	0.6	-	1.0
Burundi	1.4	6.7	1.3	-	0.0
Cameroon	126.5	85.6	5.7	-	0.0
Cent. African Rep.	18.9	8.7	1.8	-	-
Chad	34.3	7.1	8.0	-	1.0
Dahomey	36.6	9.1	9.0	1.0	0.0
East Afr. Commu.	32.1	146.3	-	0.3	67.0
Egypt (Arab Ref. of)	a/	a/	a/	a/	a/
Ethiopia	112.2	113.7	9.5	34.2	-
Gabon	40.4	39.2	27.9	-	7.0
Ghana	277.6	73.5	220.4	-	-
Guinea	246.5	64.5	51.3	16.1	-
Ivory Coast	a/	a/	a/	a/	a/
Kenya	237.9	102.0	7.7	4.1	42.0
Lesotho	2.7	4.1	-	0.7	-
Liberia	123.5	16.5	28.0	8.8	-
Malagasy Rep.	80.9	42.1	4.3	6.2	4.0
Malawi	103.3	32.8	2.5	0.9	16.0
Mali	265.2	17.3	4.5	0.7	-
Mauritania	17.0	12.5	8.4	0.7	b/
Mauritius	30.8	5.6	-	1.9	4.0
Morocco	589.7	159.3	53.5	20.2	32.0
Niger	34.7	8.2	19.9	-	-
Nigeria	321.1	266.0	63.6	18.1	14.0
Rwanda	1.9	9.3	0.4	-	-
Senegal	82.4	26.8	-	-	5.0
Sierra Leone	33.9	17.3	26.1	0.7	6.0
Somalia	96.2	9.1	-	-	-
Southern Rhodesia	46.8	44.1	-	-	157.0
Sudan	167.3	126.1	7.7	36.4	1.0
Swaziland	8.6	8.9	8.6	1.8	-
Tanzania	390.8	99.6	0.9	23.2	61.0
Togo	32.2	3.7	4.0	-	b/
Tunisia	472.8	111.3	88.4	103.9	10.0
Uganda	115.9	46.2	-	0.3	21.0
Upper Volta	21.8	7.5	1.3	0.1	b/
Zaire	132.4	25.0	231.7	60.0	130.0
Zambia	92.4	137.7	9.2	9.7	366.0

Source World Bank Annual Report, 1972, Table 5, p. 82

a/ An estimate for this country was included in overall total

b/ Less than US \$50,000

Foreign aid therefore includes loans made by the International Bank for Reconstruction and Development, I.B.R.D., popularly known as the World Bank, and its affiliates, the International Development Association I.D.A. and the International Finance Corporation, I.F.C.

The World Bank was primarily founded to revive the war damaged economies of European countries. By the mid-fifties, however, owing to additional capital under the Marshall Plan, the economies of European countries had sufficiently recovered and the Bank's emphasis shifted to development of the economies of developing countries. It cannot be denied that the World Bank has played an important role in the economic development of developing countries. Perhaps of great importance is that unlike bilateral aid, World Bank loans are not tied. However, there are very strict rules which limit the Bank's capacity: the most serious being the rule that the Bank will only finance the foreign exchange component,²⁶ and the requirement that the borrower must submit a specific project - a serious handicap to developing countries which lack skilled manpower. And, although it is expressly stated that the Bank verifies that funds are used as specified in the loan agreement . . . "without political considerations," nothing should obscure the fact that such institutions are financed by developed countries especially the United States and--"he who pays the piper calls the

tune." And as Buchanan and Ellis put it, "such institu-
tions are bound to act in the light of a basic conservatism. 27

FOOTNOTES

1. See H.J.P. ARNOLD, *Aid for Development*, p. 7.
2. Ibid.
3. RAYMOND F. MIKESELL, *The Economics of Foreign Aid*, p. 194. Chicago, Aldine Pub. Co. (1968).
4. See Lloyd D. Black, *The Strategy of Foreign Aid*, p. 14.
5. Ibid, pp. 14-15.
6. Ibid, p. 16.
7. A.H. HANSON, *Public Enterprise and Economic Development*, p. 30. London, Routledge and S.K. Paul (1960).
8. Ibid.
9. *New York Times*, Jan. 15, 1966, p. 12, cited by Mikesell, opt. cit. p. 6.
10. US Department of State Bulletin, April 10, 1961, cited by Ibid, p. 6.
11. Cited by Ibid, p. 6.
12. V. Massaro, *Aid from the Donor's Point of View*, vol. 2 No. 2, J.W.T.L. (March-April) 294.
13. Opt. cit. p. 19.
14. Ibid, p. 18.
15. Ibid, p. 20.
16. H.J.P. Arnold, opt. cit. p. 99.
17. Ibid, p. 110.
18. Cmnd 2736; HMSO - August, 1965.
19. Ibid.
20. Ibid.

21. Ibid.
22. Ibid.
23. Kamanda was Kamanda, CERES, FAO Review on Development July-August, 1973.
24. J.W.T.L., opt. cit. at p. 121.
25. Mikesell, opt. cit. at p. 195.
26. PAUL ALPERT, Economic Development, Objectives and Methods, London, p. 281 (1963).
27. Cited by A.H. Hanson, opt. cit. at p. 28.

PART II

Legal Obstacles and Incentives to Private Foreign

Investment in Emergent States

CHAPTER V
OBSTACLES TO PRIVATE FOREIGN INVESTMENT IN
DEVELOPING COUNTRIES

As discussed in Chapter One, economists do not agree on the actual amount of capital funds which developing countries need either to raise their per capita incomes or to reach a stage of self-sustaining growth. They also argue as to whether or not capital is the principal factor in economic development.¹ However, they all agree that it is one of the most important factors.² The question which this Chapter attempts to answer is, why do developing countries receive capital far less than they need? It is certainly beyond the scope of this work to discuss all the reasons why developing countries receive less capital; it is proposed therefore to limit the discussion to the legal obstacles to foreign investment obtaining in developing countries. Further the discussion will not cover foreign aid as it has already been discussed in Chapter IV; in this Chapter, emphasis is on private foreign investment. It is proposed first to discuss the advantages of private foreign investment to developing countries.

ADVANTAGES OF PRIVATE INVESTMENT

Direct private industrial investment provides the most dynamic element in economic development compared with foreign

3
aid. Private foreign investors will not invest unless there is an economic benefit. Unlike donors of foreign aid who will invest money to achieve political, humanitarian, military or economic objectives, the objective of private foreign investors is to make an economic return. This in itself is an advantage to a developing country because it is hardly possible to conceive of an investment which could make profits without at the same time contributing to the development of the host country in foreign exchange, skills,
4
employment and taxation. As Buchanan and Ellis put it, "most importantly, private capital moves on a sound business basis of mutual profit - without involving moral problems concerning the duty of a creditor country to supply capital. It therefore provides a firmer foundation for long-run economic relations than does public capital."
5
Private foreign investment also plays a vital role in transfer of technology to developing countries; it ". . . brings with it managerial and technical talents lacking in public capital."
6
Coupled with transfer of technology, private capital creates employment thereby alleviating unemployment in the host state. If effectively regulated, private foreign investment may lead to reinvestment of profits within the host state. It must be pointed out, however, that experience has shown that usually the host state loses the much needed foreign exchange through repatriation of profits abroad; this has led to a

serious balance of payments problem for most developing countries - hence imposition of severe restrictions. In Hanson's view, another advantage of private foreign investment is that ". . . it is more likely than other kinds to produce a parallel importation of money and goods, thereby acting, to some extent, as a counter-inflationary force."⁷

Perhaps the most direct advantage of private foreign investment to the host state is its contribution to revenue through corporate taxation. As pointed out in Chapter One, if developing countries had effective laws and administrators, corporate taxation would have been the major source of revenue after the chief export commodity; but as Kaldor says "it is probably not exaggerated to say that the typical under-developed country collects in direct taxation not more than one fifth or possibly one fifth of what is due."⁸

The overall advantages of private foreign capital to developing countries were summarised by the late President Nkrumah as follows, ". . . The government receives by way of company tax eight shillings in every pound of profits made by companies both Ghanaian and Overseas established in Ghana. This is equivalent to a non-voting shareholding for which the Government invests no capital. Overseas capital invested in companies in Ghana, provides buildings, plant and machinery which remain permanently in Ghana and become immediate assets of Ghana. In most cases, a large proportion of the turnover

of an industrial company remains in Ghana in the form of wages and salaries to employees. These wages and salaries in turn attract taxation and also purchasing power which encourage further enterprises. In good companies, of which there are many, a share of the profits is ploughed back into the company for development of its enterprises. This is in fact, further investment. . . ."

The 'roadblocks' to the flow of foreign capital into developing countries are found both in host states and in capital exporting countries. However, this chapter deals with those obstacles obtaining in host states. These obstacles are diverse in character - economic, legal, social and psychological. The emphasis in this chapter is on legal obstacles, others will simply be summarised.

As seen in Chapter Two, Britain, as the major source of foreign capital between 1870 and 1914 was investing at an annual rate of L158 million during the decade preceding the first World War. Most of this investment was private and spontaneous. The United States became the giant source of capital after the second World War; however, it has invested less capital relative to what Britain invested - and most of this investment has been largely due to International Finance Institutions like the World Bank and aid. Commenting on this obvious decline in private international investment, Buchanan and Ellis point out that it is partly due to inadequate rates

10
of return. With the exception of oil producing countries, private foreign investors have experienced low rates of return in developing countries. There are other factors.

INADEQUATE MARKETS

The domestic markets in developing countries are usually small; coupled with this is the low purchasing power of their populations. Consequently, private foreign investors will not invest where the market is too small to permit a reasonably sized industry as well as future expansion. This is one of the reasons why private foreign investment has concentrated on industries producing for the export market and not on manufacturing industries.

The inadequate basic infrastructure in developing countries is another obstacle to private foreign investment - railways roads and electric power facilities are inadequate and the few that are available are poor and expensive.

The term 'unfavorable investment climate' refers to the general attitude in the host state toward foreign investment. In developing countries generally, especially during the early years of independence, private foreign investment was viewed with hostility and suspicion and to a certain extent it is still regarded as a form of economic imperialism. This hostility and suspicion is not, however, unfounded because in the past such investment has been associated with colo-

nialism and other forces of political and economic domination. A similar obstacle to private foreign investment in developing countries is the adoption of the Marxist mode of economic development which abhors private ownership of property - private foreign investment is viewed therefore as a contradiction.

Coupled with the above is political instability in developing countries; a private investor needs security of his investment. The investor has to be reasonably certain of the future - that there is little or no possibility of a situation which will be detrimental to his investment. Most of the developing countries, especially the emergent states, are in a process of dynamic social, political, economic and legal changes. It is impossible to predict with confidence that conditions of stability and security will exist; a government may welcome private investment today but tomorrow it may be overthrown and be replaced by a government which is hostile to private investment.

LEGAL OBSTACLES

It must be emphasised that obstacles to private foreign investment follow no fixed hierarchy of importance; economic obstacles may deter private investors just as much as political obstacles would and similarly will legal obstacles. The reason for the emphasis on legal obstacles in this chapter is

simply that the whole subject - private foreign investment is looked at from a legal point of view in this dissertation.

RESTRICTIONS ON ENTRY OF PRIVATE FOREIGN INVESTMENT

Most developing countries have imposed regulations on the admission of private capital.¹¹ These regulations provide for a body which has to approve private capital before it is admitted, popularly known as screening boards. International law allows a state to impose restrictions on the entry and residence of aliens;¹² it seems therefore that the legality of screening boards cannot be contested. But it is argued by private investors that the boards become bureaucratic; they become rigid, arbitrary and sometimes corrupt. Their inquiries into the proposed industry are detailed to the point of absurdity. On the other hand, developing countries argue that screening is necessary on the following grounds:

- (i) To avoid excessive concentration of foreign investment in a few fields - such concentration may create difficult long-range problems.
- (ii) To regulate the condition of the capital-importing country's balance of payments.
- (iii) To exclude foreign investors from certain sectors of the economy - to avoid the possible inflationary effects.

(iv) Control over the entry and direction of capital is indispensable to any country for the operation of national economic planning.

In conclusion, it cannot be seriously argued that screening is a major obstacle to admission of private capital; admittedly there may have been cases of miscarriage of justice, but that is no reason for wholesale condemnation of screening. What should be advocated for is reform. In any case, as will be seen in the next Chapter, once approval is given, the host state grants various incentives to the foreign enterprise.

OTHER RESTRICTIONS

Developing countries generally have passed legislation to either exclude foreign investment in total in certain sectors or to provide for a majority shareholding by the state. The most popular sectors are mining, petroleum extraction, transportation, banking and insurance. The legality of such measures cannot be contested; international law permits a state ". . . to regulate all matters pertaining to the acquisition and transfer of property within its territory as well as to determine the conditions for the exercise in it of the economic activities of natural or legal persons."¹³ It is argued, however, that most of the industries in question are industries which can be better managed by private enterprise.¹⁴ These industries also offer some

of the highest rates of retain. But, it can be intolerable that major industries of great sensitivity should be run and owned entirely by foreigners notwithstanding controls the government may have at its disposal.

As for the majority shareholding by the state, most private foreign investors do not regard it as a serious obstacle. When Zambia nationalised the copper mines, it was immediately pointed out in Western countries that: "it would be a pity if potential investors in Africa are mistakenly led to believe that there is no longer a future for them; although doing business in independent Africa now calls for a high political acumen, the opportunities available to those who possess it are good; anyone contemplating a stake in Zambia ought to be asking about future political and economic stability of that country rather than with the principles of nationalisation - 49% stake whose success is underwritten by government participation may be more than 100% of a concern exposed to all the political winds that blow." ¹⁵ Indeed, local participation brings with it many advantages - local personnel can be useful for business connections while of course the host state also benefits from the training of indigenous entrepreneurs.

EMPLOYMENT OF LOCAL LABOUR

In developing countries, the training of nationals is

as important as foreign capital itself. Thus one of the conditions which go along with grant of special or approved status for a foreign industry is an undertaking that the industry will employ nationals and where they are not available, the industry will train them. Egyptian company law of 1954 stipulates that a minimum of 75% of the administrative, technical, clerical and accounting personnel of branches of foreign companies operating in Egypt must be its nationals receiving not less than 65% of the total emoluments paid by the branch.¹⁶ In addition, Egyptian nationals must constitute at least 90% of the unskilled labour force and be entitled to 80% of the total wages paid by the company.¹⁷

The Liberian Investment Incentive Code,¹⁸ provides that the sponsor of an approved new investment project is obliged to promote the employment of Liberian workers and to select and train Liberian workers on a systematic basis in skills required in the operation of the project.

The Algerian Investment Code¹⁹ achieves this objective by giving power to the Ministry of Finance and Planning or the National Investment Commission to control recruitment of foreign personnel and so does the Dahomey Investment Code.²⁰

Other countries like Kenya, and Uganda emphasize upon Africanisation. In addition to Zambianisation, Zambia imposes a selective employment tax to enterprises that employ foreign personnel in disregard of equally qualified Zambians.

In international law a state has a right to control the entry of aliens in its territory and to regulate their economic activities²¹ and therefore the legality of the above legislation cannot be contested.

It is argued by investors that such restrictions should only apply to unskilled labour which developing countries have in abundance and not to skilled labour because developing countries have very few skilled personnel; employment of unskilled personnel will lead to inefficiency and mismanagement. This argument is obviously valid and most investment codes contain exceptions - that where local labour is not available, the foreign enterprise may recruit foreign personnel. It is unfortunate, however, that some investors have taken unfair advantage of these exceptions; they do not undertake training programmes for the indigenous personnel thereby perpetuating recruitment of labour from abroad. Two problems have arisen: unemployment and repatriation of salaries of the expatriate personnel leading to loss of much needed foreign exchange.

RESTRICTIONS ON DIVIDENDS AND REPATRIATION OF PROFITS

In some developing countries, the companies act²² makes it mandatory for every company to set aside a prescribed percentage of profits for reinvestment before dividends are declared. This obviously is an obstacle to private investment

as it takes money directly from the investors' earnings. But it can be argued for developing countries that in the absence of such legislation, experience shows that foreign firms will simply 'milk' the country. The management will take advantage of traditional company law, which does not impose restrictions on declaration of dividends to declare almost all profits as dividends with little or nothing left for reinvestment. In Dodge v. Ford Motor Co,²³ it was held that directors, and directors alone have the power to declare a dividend of the earnings of the corporation and to determine its amount. Similarly in Burland v. Earle,²⁴ Lord Devey stated that ". . . These lordships are not aware of any principle which compels a joint stock company while a going concern to divide the whole of its profits among its shareholders; whether the whole or any part should be divided, or what portion should be divided and what portion retained, are entirely questions of internal management which the shareholders must decide for themselves, and the court has no jurisdiction to control or review their decision, to say what is a 'fair' or 'unreasonable' sum to retain undivided or what reserve fund may be 'properly' required. . . ." Foreign firms took advantage of this principle of company law in Zambia as soon as independence was evident by repatriating almost all the profits they made; the trend in the repatriation of profits by one foreign enterprise from 1960-1967 was as follows:

	<u>Balance Attributable to the Company as Profit</u>	<u>Retained in Business</u>	<u>Balance Distributed Net Dividend</u>
1960.....	K9,384 (L4,692)	K5,142 (L2,571)	K4,242 (L2,121)
1961.....	K6,610 (L3,305)	K3,514 (L1,757)	K3,196 (L1,598)
1962.....	K11,248 (L5,624)	K2,626 (L1,313)	K8,622 (L4,311)
1963.....	K11,858 (L5,929)	K2,310 (L1,155)	K9,548 (L4,774)
1964.....	K11,798 (L5,899)	K2,334 (L1,167)	K9,464 (L4,732)
1965.....	K17,366 (L8,683)	K3,852 (L1,926)	K13,514 (L6,757)
1966.....	K20,464 (L10,668)	K3,132 (L1,566)	K15,332 (L7,666)
1967.....	K20,668 (L10,334)	K5,312 (L2,656)	K15,356 (L7,678)

This practice led to the following consequences in Zambia:

(a) Gross undercapitalisation.

(b) Excessive local borrowing: for instance, the foreign company with L200,000 paid up capital acquired L2 million overdraft rights of which it promptly used L1 million.

(c) There was 100 percent increase in foreign exchange expenditure on invisibles; it jumped from L16.459 million in 1965 to L31.887 million in 1967, although goods purchased in that year amounted to only L44 million. The difference cannot be accounted for even as payments for personnel.

Developing countries impose restrictions on repatriation of capital through foreign exchange regulations. International law recognises the right of control by a state over its currency as an attribute of sovereignty.²⁶ Thus a general devaluation of currency or reasonable and necessary restrictions on transfer of currency cannot constitute an international delinquency. It is argued that provision must be made for repatriation of profits since to the investor the value of the enterprise is the earnings of profits which he can remit home.²⁷ This is a valid argument and no country which genuinely welcomes investors will unreasonably restrict repatriation of profits.

FEAR OF NATIONALISATION

(Chapter VII is devoted to the subject of nationalisation and compensation and therefore it will not be covered in detail here.) No authority seriously argues against the right of a state in international law to nationalise or expropriate foreign owned property within its territory in the public interest. What is regarded as an obstacle is the inadequacy of the compensation. The argument is that nationalisation, as opposed to expropriation, has given rise to a new minimum standard, i.e., the quantum of the compensation should be a fair market value - obtaining in the nationalising state or simply a fair value of the nationalised

property, to be paid not promptly, but within a reasonable time and in convertible currency, not necessarily in the currency of the state to which the alien is a national.

TAXATION

There are basically two ways by which taxation can be a deterrent to a foreign investor: his earnings on his investment may be taxed twice, by the host state and the capital-exporting state, double taxation as it is often referred to. Secondly, certain taxation measures may discriminate against aliens by taxing them excessively. Double taxation is lawful in international law ²⁹ but because of its adverse effect on the flow of foreign investment most developing countries have concluded treaties to eliminate it. International law also recognises the sovereign right of each state to tax aliens resident or owning property within its territory ³⁰ but confiscatory or discriminatory taxation ³¹ is contrary to international law; Professor Wortley calls it 'expropriation without compensation.' In general, however, taxation in developing countries is not as heavy as in developed countries. In fact developing countries lose a lot of revenue from ineffective tax laws or due to poor administration. The multinational corporation, which represents the bulk of private investment, is notorious for tax evasion; Professor Kaldor reveals how it is done: "... it is

well known that an international concern operating through a chain of subsidiaries can easily shift its profit from one place to another by changing the price which the subsidiaries, or associated companies, charge to one another.

. . . Since the war international companies have made increasing use of the so-called 'tax havens,' and have established holding companies or subsidiaries in territories where the profits are subject to little or no tax or in countries which do not bring into charge the profits earned in the overseas operations of their resident companies.

These are then some of the obstacles to the satisfactory flow of private foreign capital to developing countries. The solution has been to enact investment codes which provide incentives to private investors, the subject of chapter VII.

FOOTNOTES

1. See Chapter 1.
2. Ibid.
3. W.M. CLARKE, *Private Enterprise in Developing Countries*, p. 3.
4. F.T. Pedler, *The Problem in East and West Africa*, in *The Encouragement and Protection of Investment in Developing Countries*, I.C.L.Q. Supp. Publication No. 3 (1962), at p. 64.
5. BUCHANAN, N.S. and ELLIS, H.S., *Approaches to Economic Development*, p. 351. N.Y. 20th Century Fund (1955).
6. Ibid.
7. HANSON, A.H., *Public Enterprise and Economic Development*. London, Routledge and K. Paul (1960).
8. N. KALDOR, *Taxation for Economic Development*, in *Taxation for African Economic Development*, Ed. by Milton C Taylor at p. 160. London (1970).
9. Speech delivered over Ghana Radio in Oct. 1960.
10. Opt. cit. at p. 343.
11. *Investment Laws of the World, The Developing Nations*. Oceana Pub. N.Y. (1972).
12. C.C. HYDE, *International Law* 216-18. 2d re. ed. Little, Brown and Co. Boston (1945).
13. Ibid.
14. E.I. NWOGUGU, *The Legal Problems of Foreign Investment in Developing Countries*, at p. 15. Manchester Un. Press

(1965).

15. Cited in Foreign Investment in Tanzania, OKUMU-WENGI, R.O. (Internal Circulation).
16. No. 26 of Jan. 10, 1964.
17. Ibid.
18. Liberian Investment Incentive Code, 1966.
19. Article 9.
20. Article 17.
21. Hyde, opt. cit.
22. Nwogugu, opt. cit. at p. 17
23. (1919) 204 Mich. 459.
24. (1902) A.C. 83.
25. KENNETH KAUNDA, Zambia Towards Economic Independence, Mulungushi Speech, April 19, 1968, p. ii.
26. HACKWORTH, Digest of Int. Law, Vol. 3 (1942).
27. Nwogugu, opt. cit. 20.
28. Hyde, opt. cit.
29. Albrecht: 29 B.Y.B.I.L. (1952), 145.
30. WORTLEY, B.A., Expropriation in Public International Law, pp. 106-07. Cambridge Un. Press (1959).
31. Ibid.
32. Kaldor, opt. cit. note 8.

CHAPTER VINATIONALISATION AND COMPENSATION

Although nationalisation per se has become an acceptable phenomenon, the chaotic and conflicting rules for valuation of compensation still make it a serious obstacle to foreign private investment; it therefore deserves a chapter.

It has been shown in Chapter Two how economies of emergent states and other developing countries came to be virtually controlled by foreign nationals because of the extensive economic and political concessions which were granted to them by the colonising powers. It has also been pointed out that de jure independence left the situation unaffected. Inevitably, these countries resort to measures of expropriation and nationalisation of foreign-owned interests either to localise the economy, as in the case of Zambia, or to completely overhaul the capitalist institutions and replace them with socialist institutions as in Tanzania, for instance.

Customary international law provides for a minimum standard to be observed when a state expropriates foreign-owned interests: prompt, adequate and effective compensation must be paid.¹ The question intended to be answered in this chapter is, have emergent states observed the minimum standard in their nationalisation measures? If not, why? Has the law changed or should it be changed to meet with the changed circumstances?

EXPROPRIATION DEFINED

Expropriation may be defined as a "compulsory acquisition² of property by the State"; the individual is divested of ownership which is then vested in the State; for instance, the acquisition of land by the state to build a hospital or to develop a state ranch. On the issue of whether the State has a right to expropriate property, there is complete agreement³ among the authorities. This right has been well established for a long time both in positive law and legal theory although the emphasis was originally on the rights of property owners. Now the social function of property and the consequent duties of property owners are stressed.

It is on the issue of compensation that authorities are in disagreement.⁴ Sir John Fisher Williams, Cavaglieri⁵ and recently Friedman⁶ have all denied that there is a duty to compensate under international law. The majority of writers, however, argue that an internationally lawful expropriation is conditional upon the payment of full compensation⁷ paid promptly and effectively. This view is supported by the constitutional provisions of States before the era of nationalisations.⁸ It was also supported by the International Law Association⁹ in 1927 and 1932 and the Permanent Court of International Justice, in the Case of Certain German Interests in Upper Silesia.¹⁰ The court said: "The action of Poland which the Court had judged to

be contrary to the Geneva Convention is not an expropriation to render which lawful only the payment of fair compensation has been wanting." In conclusion therefore, expropriation is only lawful under traditional international law if adequate, prompt and effective compensation, i.e., the "full market value of the expropriated property is paid. 'Promptness' means "payment at the time or before the property was taken," and 'effectiveness' means "payment in cash and in convertible currency."

IS NATIONALISATION THE SAME AS EXPROPRIATION?

11

According to Michael Brandon, the term nationalisation is applicable to the transfer of private property to public ownership and if compensation is paid, such a transfer is expropriation. Fawcett¹² likewise argues that nationalisation with compensation is expropriation. Other eminent writers on the subject of nationalisation, however, have argued convincingly that nationalisation is different from the orthodox term used to describe the compulsory acquisition of property by the state--expropriation. Isi Foighel¹³ points out that the term 'nationalisation' was first heard of during the Russian Revolution when large sectors of the economy which up to then had been private property passed to the common ownership of the nation. Nationalisation therefore is the compulsory taking of private property by a state associated with a wider political aim, for instance, the

reconstruction of the economic and social structure of the State. Nationalisation is also associated with the takeover of industrial undertakings in the widest sense and not only for the takeover of property which exists without serving industrial interests. "Nationalisation is an action against private property of a distinctive character, and its special distinguishing marks show that the basis for the action and its purpose are other than those of traditional actions. Unlike traditional expropriation and the usual restrictions on private property, nationalisation is not motivated by the desire of the State to take over or restrict the use of property to serve a special purpose of the State different from that pursued hitherto as, for example, the compulsory surrender of land for the construction of roads or railways or the restriction of building rights for the purpose of creating new roads, in each case objectives which have no connexion with the normal use of the property as practised by the owner. The action of nationalisation on the contrary seeks its justification in the very circumstance that the state will not permit private persons to exploit property for so-called private economic purposes and, therefore, wishes to take over or extend the uses of the property as previously practised."¹⁴ Foighel emphasizes that in nationalisation the way the private person utilises the property and the way the State utilizes it after the taking

are the same; it is the distribution of the profits which is different. He therefore defines nationalisation as "the compulsory transfer to the State of private property dictated by economic-political motives and having as its purpose the continued and essentially unaltered exploitation of the particular property."¹⁵ Nationalisation therefore has three basic characteristics:

- (a) It has a primary economic motivation.
- (b) The property which is nationalised becomes part of publicly owned or controlled property.
- (c) After nationalisation the property should be exploited for the public benefit and not in the interests of private persons.

For instance, in Zambia, part of the 1968 Mulungushi Reforms which merely transferred foreign owned interests to Zambians in the second class trading areas were not nationalisation measures. Indeed Soremekun¹⁶ has stated that the reforms were made, inter alia, to promote 'mini-capitalists' among Zambians. But, the fact that the property or enterprise taken over is vested in a legal entity, different from the state would not change its character as a nationalisation provided the legal entity is a public one and manages the property or enterprise in the public interest. Thus part of the 1968 Mulungushi Reforms which 'invited'²⁷ companies to sell 51 percent of their shares to the govern-

ment were nationalisation measures because although state participation was effected through a legal entity, the Industrial Development Corporation, INDECO, this legal entity is a public corporation doing business in the public interest. Similarly the 1970 Mulungushi Hall Economic Reforms were nationalisations because again a number of state enterprises were assigned the task of taking over and running the nationalised companies in the public interest: INDECO, the Zambia State Insurance Corporation, the Zambia National Building Society, and the United Bus Company of Zambia. The Matero Reforms, 1969, were nationalisation measures because, although the Zambian government created the Zambia Industrial and Mining Corporation Limited, ZIMCO, a legal entity, to hold the government's interest in the mining companies, ZIMCO is not a private enterprise but a public enterprise doing business in the public interest.

The question, however, is why should a distinction be made between nationalisation and expropriation? Is there any practical value? Has nationalisation changed the law so that if a taking of private property is proved to be nationalisation, there will be some legal benefit which would not be obtained if a taking is found to be 'traditional' expropriation? Authorities like Wortley,¹⁷ White,¹⁸ and Domke¹⁹ argue that there is no legal value because even in cases of nationalisation, the taking of an alien's pri-

vate property must be accompanied by payment of adequate, prompt and effective compensation. Other authorities like Foighel,²⁰ Katzarov,²¹ Jessup²² and Lauterpacht²³ have taken the view that the changing conditions in the world have brought about the creation of new law in general. Amerasinghe submits that nationalisation, although a species of expropriation, "has become sufficiently distinguished from other kinds of expropriation in kind, so much so that the sources have produced special rules in regard to it. These are to be differentiated from the rules relating to other cases of expropriation."²⁴ He gives three grounds for his submission:

- (i) The changes that have taken place in the law have been concerned with cases of nationalisation as defined above.
- (ii) The changes in the law have all been for the benefit of the nationalising state to the alien's detriment, therefore they should be considered as applicable to the special sphere of nationalisation.
- (iii) The elements contained in an act of nationalisation themselves justify a special treatment: economic motivation, public ownership, and exploitation for the public benefit.

The next question that must be answered is, what then are the changes in the law that have been brought about by nationalisation?

THE RIGHT TO NATIONALISE

The right of a State to take aliens' property has always been recognised in modern international law as part of its sovereignty.²⁵ Even the most conservative countries on the idea of the sanctity of private ownership of property recognise this right; for instance, the United States, which has been very explicit on this issue several times. Secretary of State Hull said, during the Mexican Agrarian Reforms of 1938, "My Government has frequently asserted the right of all countries freely to determine their own social agrarian and industrial problems. This right includes the sovereign right of any government to expropriate private property within its borders in furtherance of public purposes."²⁶

The General Assembly passed a resolution in 1952 to the effect that 'the right of peoples freely to use and exploit their cultural wealth and resources is inherent in their sovereignty.'²⁷ In 1962 the General Assembly was more explicit in recognising 'the inalienable right of all states freely to dispose of their natural wealth and resources in accordance with their national interests and

the economic independence of States.'²⁸ Needless to say that a General Assembly resolution does not create law but it has value in that it is evidence of the practice of States; the resolution was in fact passed by an overwhelming majority of 87 votes to 2 with 12 abstentions.

IS THE RIGHT TO NATIONALISE ABSOLUTE?

The Union of Soviet Socialist Republics, U.S.S.R., has always maintained that the State's right to nationalise is absolute; international law does not impose any limitations on the nationalising State.²⁹ Other states that have claimed an absolute right are Iran and Indonesia.³⁰ There are, however, many states which have recognised the obligations of the nationalising State under international law: Zambia, for instance, has been consistent in respecting its obligations in all her nationalisation measures. The General Assembly resolution on the Permanent Sovereignty over Natural Resources recognises certain limitations imposed by international law on the nationalising state; these are:

- (i) That the Nationalisation should be for a Public Purpose.
- (ii) That there should be no discrimination against the aliens.
- (iii) That the nationalising State should observe a minimum standard in its treatment of aliens;

the form of nationalisation must conform to international standards.

THE PUBLIC PURPOSE LIMITATION

The United States Circuit Court of Appeals in the Sabbatino Case³¹ held that the Cuban nationalisations lacked a true public purpose because of their retaliatory purpose. In the Mexican Oil expropriation, the government argued that it lies in the host state's subjective determination as to whether the expropriation is in the public interest.³² Indeed the issue really is who determines the public interest? It is submitted that the test should be a subjective one, the host state. Even conservative writers on the subject, like Domke³³ agree that the determination of public interest by the nationalising state could hardly be challenged unless it were wholly beyond any reasonable limit. The foundation of the definition of nationalisation itself is the public interest and it would surely be illogical to argue that the taking of private property in a given case is nationalisation but it is not in the public interest! If a taking of private property lacks a public purpose, it is not nationalisation. In fact, all post-war nationalisations have not been seriously challenged on the issue of lack of public interest.

NON-DISCRIMINATION

This limitation is a vital one because as Amerasinghe puts it, "it rests on a fundamental principle of justice and is vital to ordered relations based on mutual respect as between all states."³⁴ The question, however, is, what is meant by discrimination? A clear case of discrimination would be where the host state nationalises 90% of the business of an enterprise belonging to nationality A while only 10% of the business of the same kind of enterprise belonging to nationality B is nationalised. But what is the position where virtually all business enterprises are in alien hands and the nationals of the host state own nothing? Will it not be idle to argue that the nationalisation is discriminatory because only alien property is nationalised? The question is important because in emergent states and in developing countries generally, virtually all business enterprises were in alien hands at independence. Consequently only alien property could be nationalised. There is no rule of international law which prohibits nationalisation of alien property in the field where nationals have no interest of the same kind on the ground that such nationalisation would be discriminatory.³⁵ And a German Court decided that 'the duty not to discriminate against aliens or particular aliens did not apply to the nationalisation of Dutch enterprises in Indonesia because the equality

concept means only that equals must be treated equally and that the different treatment of inequals is admissible. . . .³⁶ Needless to say that this decision has been criticised as not representing the law.³⁷ But this is the position that most emergent states have taken, that since the colonial powers discriminated the indigenous population economically, the nationalist government must do the same to correct the situation and only then can one talk of non-discrimination. This is the principle upon which the Zambian government justified the 1968 Mulungushi Reforms which prohibited financial institutions from giving credit to non-Zambian entrepreneurs, companies and partnerships and prohibited issue of trading licenses to aliens in the second class trading centres.³⁸ It is therefore submitted that as regards nationalisation of alien property where nationals of the host state have no interests, it is not discrimination if the nationalisation is a corrective measure.

FORM

Authorities are not explicit as to the form a nationalisation should take to be lawful under international law. It has, however, been said that a taking of alien property in violation of municipal law by the host state amounts to a violation of the forms required by international law. Friedman³⁹ states that outrageous treatment of the alien in carry-

ing out the expropriation would violate internationally required forms; an obvious example is Idi Amin's expropriation measures against Asian interests in Uganda and their expulsion from that country. Apart from such isolated cases, emergent States have carried out their nationalisation measures in an orderly fashion in their desire to retain the confidence of would-be foreign investors. As President Kaunda has consistently pointed out, "Zambia has a clean record as an honest nation in dealing with aliens and their property."⁴⁰ The Asians were given four years to wind up their businesses in the second class trading areas to give way to Zambians.⁴¹ And they were given the option of obtaining Zambian citizenship if they wished to continue trading in these areas.

COMPENSATION - THE CONTROVERSIAL LIMITATION

As seen above, expropriation of alien property can only be legal if it is accompanied by adequate, prompt and effective compensation. The question is, is there a similar limitation in cases of nationalisation? As expected, the Soviet Union has always denied that there is a duty to compensate.⁴² Iran and Indonesia have taken the same attitude in principle.⁴³ Mexico also denied the existence of such a duty, at least in cases of nationalisations which are general and impersonal in character.⁴⁴ On the other hand,

there are several nationalising states which have conceded that even in cases of nationalisation, there is a duty to pay compensation: Egypt, Cuba, Burma, Ceylon, Tanzania and Zambia. President Kaunda has always stressed the duty to pay compensation in his speeches on Economic Reforms.⁴⁵ The state of the law on this issue is therefore not settled yet and as Amerasinghe⁴⁶ points out there are basically three schools of thought:

- (i) That there is a duty to pay compensation.
- (ii) That there is never a duty to pay compensation; it is at the discretion of the nationalising state whether compensation is to be paid.
- (iii) That there is a duty to compensate except in the case of nationalisations of a general character for the purpose of changing a social structure after independence.

The theme of this dissertation is that both the investor and the host state have a common interest, the investor must get a fair return on his investment. The school of thought which states that no compensation is due to the investor in the case of nationalisation benefits the host state to the complete detriment of the investor and it must therefore be rejected. The law must strike a compromise and it is submitted that even in the case of nationalisation, there is a duty to pay compensation. It is also significant to note that Resolution 1803 of the General Assembly⁴⁷ recog-

nised the duty to pay compensation in the case of nationalisation, expropriation, or requisition.

THE AMOUNT OF COMPENSATION

As seen above, the majority of authorities hold the view that expropriation can only be legal in international law if it is accompanied by adequate, prompt and effective compensation. The terms, 'full,' 'fair' and 'just' compensation are sometimes used to define the term, 'adequate compensation. The basis of the rule of adequate compensation seems to be based on either of the following theories:

acquired rights: that since the alien's property rights were lawfully acquired under municipal law, the expropriating state must protect them; the state is incapable of destroying acquired rights at its discretion. Under this theory therefore adequate compensation is not only the "full market value" of the alien's property, but also indirect damages such as incidental contracts, goodwill and future prospective profits.

Unjust Enrichment: according to this theory, the alien must be compensated to the extent that the expropriating State will not be unjustly enriched. The practical effect would be that the alien will get a full market value of the property, and prospective profits but not damages for loss of incidental contracts.

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acquired rights: that since the alien's property rights were lawfully acquired under municipal law, the expropriating state must protect them; the state is incapable of destroying acquired rights at its discretion. Under this theory therefore adequate compensation is not only the "full market value" of the alien's property, but also indirect damages such as incidental contracts, goodwill and future prospective profits. 48

Unjust Enrichment: according to this theory, the alien must be compensated to the extent that the expropriating State will not be unjustly enriched. The practical effect would be that the alien will get a full market value of the property, and prospective profits but not damages for loss of incidental contracts. 49

The Soviet Union has always refused to pay compensation on the ground that nationalisation merely restores the property to the people. ⁵⁰ Apart from such an extreme position, other nationalising States have taken the view that whatever the quantum of compensation, it certainly does not mean the full market value, goodwill and damages for loss of incidental contracts. President Kaunda has consistently emphasised that whatever the amount which the state must pay as compensation, it should not include goodwill. "I shall leave it to INDECO to negotiate values and terms of payment but I want to make it clear that what they will pay is a fair value represented by the book value. There is no such thing as business goodwill or paying for future profits as far as I am concerned." ⁵¹

Zaire adopted an extreme position in 1967 against the Union Miniere du Haut Katanga. ⁵² When the Union Miniere was nationalised, it claimed 40,000 million Belgian francs as compensation. Zaire on the other hand argued that since the Union Miniere had already taken out 200,000 million Belgian francs as net profits, it was not entitled to any compensation. In fact, Zaire argued, it was the company which owed Zaire 7,500 million Belgian francs. Zaire also claimed 17.95 percent of the value of the Union Miniere assets outside Zaire valued at 40,000 million Belgian francs.

The General Assembly Resolution on Permanent Sovereignty over Natural Resources provides that in cases of expropria-

tion and requisitioning, "the owner shall be paid appropriate compensation. . . ."⁵³

In conclusion, it is evident that in cases of nationalisation, the alien is certainly not entitled to adequate compensation as defined above. What is he then entitled to? There is no clear-cut answer; it is a compromise between the interests of the nationalising state and those of the alien. Perhaps as Amerasinghe observes, the Havard Draft⁵⁴ of 1961 comes nearer to the compromise. Article 10 provides for two alternative standards:

- (i) "the fair market value of the property or the use thereof unaffected by the particular taking or other takings or by conduct attributable to the State and designed to depress the value of the property in anticipation of the taking; and
- (ii) in the absence of (i), the fair value of the property or the use thereof.

Compensation for loss of future profits and contracts should certainly be rejected because it is tantamount to granting a right in perpetuity to the investor to continue in business. Surely there must be a period of emancipation for the host state. Similarly, such subjective items as goodwill should be rejected.

EFFECTIVE COMPENSATION

It is not clear from authorities whether by "effective compensation" is meant that payment must be in the currency

of the alien's national state. However, it is now accepted both by host states and capital exporting countries that it is sufficient if payment is in convertible currency.⁵⁵ Indeed it is again a matter of balancing interests: it would be superfluous to expect a poor country, of which most nationalising states are, with meagre foreign exchange reserves to pay compensation in the currency of every alien's state. Amerasinghe even suggests that "where investment is possible in the nationalising state, the income from such investment being comparable with income from investment elsewhere and that income may be remitted abroad, payment may be made in the securities of the nationalising state."⁵⁶ On the other hand, it must be recognised in principle that merely by investing in a country an alien does not cease to be an alien, he must therefore be permitted to transfer his profits.

PROMPT PAYMENT OF COMPENSATION

The last facet of compensation is that it must be prompt, i.e., it must be paid before or at the time of the taking of the property and in a lump sum. It is further argued by some writers that if a country has no money to pay adequate, prompt and effective compensation, then it should have no right to nationalise.⁵⁷ Nationalising States have

rejected this rule as being tantamount to exercise of veto by aliens over the legitimate attempts of developing countries to achieve economic and social reforms. As the Mexican Ambassador put it: "The political, social and economic stability and the peace of Mexico depend on the land being placed anew in the hands of the peasants who work it. Therefore, its distribution, which implies the transformation of the country, that is to say, the future of the nation, could not be halted by the impossibility of paying immediately the value of properties belonging to a small number of foreigners who seek only a lucrative

58

end." How long therefore should it take for the nationalising state to pay compensation? It is submitted that it is unwise and unrealistic to prescribe a fixed period and therefore the term, "Within a reasonable time" is appropriate. This allows for flexibility depending on the monetary size of the nationalised enterprise and the nationalising state's foreign exchange position.

THE QUESTION OF INTEREST

Should the compensation accrue interest over whatever the 'reasonable period' is? State practice shows that interest is due. ⁵⁹ Logically, compensation is due as from the date of nationalisation and "If something is due on a certain date, it normally means

that it must be paid on that date." ⁶⁰ As Amerasinghe concludes: "The practice of nationalising states, then, involves a contradiction, unless one also concedes that no ⁶¹ interest accrues from the date of (nationalisation)."

It may, however, be argued for nationalising states that as from the date of nationalisation, whatever compensation is due, is treated as a loan upon which interest is obviously payable. If this is the case, it is then submitted that compensation should be paid out of future profits of the nationalised enterprise. Indeed the Zambian economic reforms of 1968 provided for payment of compensation out of ⁶² future profits.

In conclusion, it can be said that the law is far from being settled as regards cases of nationalisation of alien property, which is very unfortunate as this branch of law hinges on, not only the legal but also the economic, political and social relations among states. It is unrealistic to insist on the orthodox rules of international law just as it is unrealistic to be so revolutionary as to deny any compensation to an investor. The developing countries obviously need foreign capital for economic development and equally the investor is interested in the attractive returns on investment in these countries. Host states and capital exporting countries should therefore strive to evolve rules which accommodate their respective interests equitably.

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CHAPTER VII
LEGAL INCENTIVES TO PRIVATE FOREIGN
INVESTORS IN DEVELOPING COUNTRIES
WITH EMPHASIS ON EMERGENT STATES

The need to provide incentives to private foreign investment is not a new idea: as early as 1954, the United Nations General Assembly passed a resolution for the creation of a satisfactory investment climate.¹ Similar resolutions followed, passed not only by the United Nations but by international and regional organisations as well.² By 1960, fifty-six countries passed legislation or made policy statements relating to the conditions for the investment of private foreign capital.

The emergent states (the newly independent states of Africa) have more cause than most developing countries to encourage foreign investments; most of them are the poorest of the developing countries. These countries lack domestic capital to finance their ambitious development projects which are necessary to raise the standards of living of the people. They have to find foreign capital which again is scarce; as Elias puts it, "Their leaders are coming to grips with the realities of the severely competitive world of international economic and financial transactions."³ Thus investment laws of emergent states have to be attractive enough to lure private investments into Africa. But unlike

the colonial investment laws which were basically intended for the benefit of the investor and the metropole, investment laws of emergent states must prevent these countries from being stripped of their resources to the entire benefit of private investors. Private foreign investment must contribute to the economic development of the host state while the investor must get a fair return on his investment; foreign investment must not 'milk the cow without feeding it.' As President Kaunda put it, "We are willing to co-operate with anybody including governments provided it is on the basis of equality, mutual respect and for mutual advantage."⁴

The scope of African Investment Laws is very wide; they cover not only incentives to investors but almost all matters relating to private foreign investments:

- (i) Entry and approval procedures for new investments.
- (ii) Repatriation of profits and capital.
- (iii) Assurances concerning nationalisation.
- (iv) Tax exemptions.
- (v) Customs duties relief.
- (vi) And arbitration

However, with the exception of the Basic Investment Convention established under the Customs and Economic Union of Central Africa Treaty, EDEAC, not all African investment laws cover all these matters in one code. The potential

private investor has to consult various legislations dealing with foreign investment: foreign exchange regulations, fiscal legislation, customs and immigration regulations, labour legislation and other national laws in order to obtain a full picture of the legal framework within which his operation would be circumscribed.

SPECIAL STATUS

The common feature of colonial economic development in most African countries was the establishment of 'One commodity economies.' The colonial powers' main interest in its colonies was raw materials and once this objective was satisfied, it was not necessary to develop secondary or other industries. Sometimes the colonial power prohibited the development of manufacturing industries in the colonies in order to preserve these territories as markets.⁵ At independence African countries inherited these one commodity economies--Zambia, for instance inherited a copper economy, and Ghana a cocoa economy. The danger with such economies is obvious: prices for these commodities fluctuate and they are externally controlled usually by the institutions of the former colonial power. The sad story of the unstable copper prices is an obvious example. It has therefore become vital and inevitable to diversify the economies of most African countries. One way of doing it has been the granting of special or approved status to foreign investors

who wish to venture into 'neglected' areas of the economy. In Nigeria, Pioneer status is granted to an enterprise upon a finding that the industry intended to be developed is not already being carried on at all or not on a scale suitable to the country's economic requirements, and that it is "expedient in the public interest to encourage the development or establishment of the industry in Nigeria."⁶ The Lesotho Pioneer Industries Encouragement Act establishes a Pioneer Industries Board which will grant Pioneer status only if it is satisfied that the enterprise will contribute to the economic development of Lesotho.⁷ The Ethiopia Investment Code provides that approved enterprises are those that relate to agriculture, industry, mining, transport and tourism.⁸ The Dahomey Investment Code grants privileged status to any new industrial, agricultural or mining enterprise which is of interest or important to the economic development of the country.⁹ Niger is one of the African countries which attempts to provide an exhaustive list of the types of enterprises that qualify for beneficiary status: these are enterprises which produce energy, mining enterprises, enterprises engaged in mechanical spinning, weaving, dyeing, and knitting, the manufacture of fertilisers and products necessary for agriculture, articles and objects for general consumption, enterprises engaged in industrial stock raising, agriculture and fishing entailing a stage of processing of their products.¹⁰ Gabon grants preferential

treatment to enterprises engaged in industrial agriculture which includes the processing or packaging of products, stock raising with animal health facilities, forestry industries, fishing with facilities for canning or fish processing, producing or assembling manufactured articles, mining, petroleum prospecting, power production and tourism. Burundi¹² and Chad¹³ have similar lists while Rwanda has a longer list which includes enterprises engaged in real estate, rail transportation and the construction of cheap housing for the people.¹⁴ The Investment Convention established under UDEAC, lists all the enterprises which may be granted approval status and provides further that member states shall modify their national laws to bring them in line with the Convention.¹⁵

In contrast to UDEAC, the East African Community Treaty leaves it to the member states' Finance Ministers to determine what an approved enterprise should be. The Economic consultative and Planning Council of the Community has only a consultative role to play in the development planning of the partner states. As Akiumi¹⁷ points out, this lack of industrial coordination within the community would lead "not to the desirable diversification of industries, but to their wasteful and competitive duplication, within the community." In Tanzania, the Minister of Finance may grant a certificate of approval to foreign investments.

if he is of the opinion that the investments would further
the economic development of, or benefit Tanzania.¹⁸ The
Kenyan Minister of Finance has prescribed rules which specify
the enterprises in respect of which the Minister may issue
certificates of approval. The enterprises include financial
institutions, new industries, the products of which can be
absorbed in East Africa or exported, oil refining, the tourist
industry and other undertakings which provide employment for
a substantial number of Kenyans.¹⁹

The Sudan Organisation and Promotion of Industrial
Investment Act²⁰ provides that any enterprise may be granted
economic concessions if, inter alia, it will be of defence
or strategic importance, utilises local raw materials,
assists in increasing the national income and especially,
if it will directly or indirectly employ Sudanese and train
them to replace foreigners serving in the enterprise.

DEVELOPMENT PLANS

Upon the attainment of independence, nearly all African
countries, realising the importance of planning for their
economies, introduced development plans covering specified
periods of time. Development plans also assist private
investors to determine the economic objectives of the host
state.

Some African investment laws, therefore, lay emphasis on development plans. The Rwanda Investment Code provides that in considering applications by enterprises which may enjoy favourable status the Ministerial Commission responsible for such applications shall base its decision, first of all, on the "Special effectiveness of the enterprise within the framework of the plan of economic and social development."²¹ The Gabon Investment Code²² includes in the criteria to be taken into account when projects which may be granted preferential treatment are considered, the participation of the project in the execution of the economic and social plan. In Chad, one of the criteria is "participation in the execution of the plan for social and economic development." In Burundi, the enterprise must "help directly or indirectly to realise the objectives of the economic and social development plan."²³ In examining requests for privileged status, the Dahomey Investment Code takes into account, inter alia, participation of the project "in the implementation of the economic and social development plan."²⁴ Apart from Liberia, investment laws of English-speaking countries lay little or no emphasis on development plans. In Liberia, an investment incentives contract shall be granted only in respect of those projects or industries to which incentives may be granted "after taking into account priorities established by the National Planning Agency which can be expected to contribute effec-

tively to the economic development of Liberia." ²⁵

OTHER CRITERIA

Many French-speaking African countries lay down additional criteria for granting of special status. the volume of investment, creation of employment, improvement in the balance of trade or payments, adequate financial or technical guarantees, the existence of the enterprise in the host country, the existing ratio between the amount of investment and the number of permanent jobs created, effect of potential investment on annexed or complementary activities, rapidity of professional training and development of national cadres and the volume of production designed for export or replacing imports.

WITHDRAWAL OF SPECIAL STATUS

Naturally, there must be provision for withdrawal of a privilege in case it is abused, thus African investment laws provide for withdrawal of approval status if the investor fails to carry out his bargain.

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The Rwanda Investment Code provides that where the beneficiary enterprise is unable to fulfill its obligations such status may be withdrawn by application by the Minister of Finance based upon the report of the Commission of Planning and after hearing representatives of the enterprise

concerned. The Act also provides for a right of appeal to a competent judicial authority. In Liberia, the Secretary of Commerce may cancel an investment incentive contract only upon the decision of the National Planning Council on any of the following grounds:

(a) Misrepresentation or other illegal act committed by the sponsors in obtaining investment incentives.

(b) Intentional misuse of import duty exemption privilege.

(c) Failure to commence operations within the time stipulated in the investment contract.

(d) Failure to submit a report on the operations of the enterprise and the liquidation of the investment. An appeal lies to the Circuit Court.²⁶ In lieu of such an appeal, the matter may be submitted to arbitration. The Dahomey Investment Code²⁷ provides for withdrawal of privileged status after an unheeded Presidential warning, inadequate explanation on behalf of the enterprise and the consideration of the opinion of the Investment Commission by a withdrawal decree of the Council of Ministers. An appeal lies to the Administrative Courts.

²⁸
The Algerian Investment Code provides for withdrawal of benefits for a serious breach if commitments by an enterprise on the proposition of the technical committee involved at least three months after the notification of such breach.

In Kenya, the Minister of Finance may revoke the certificate of approved status if the factors justifying its grant had ceased to apply. The Ethiopia Investment Code makes an investor who violates any of the provisions of the code or obtains any of the benefits granted under it by false pretence guilty of a punishable offence and liable to pay all taxes and duties from which exemption may have been granted.

The Lesotho Pioneer Industries Encouragement Act provides that an approved manufacturer or an approved hotel or casino keeper or approved builder who fails to comply substantially with any of the conditions specified in respect of such approval, may first be called upon by the Pioneer Industries Board to show cause why the approval may not be withdrawn and if he fails satisfactorily to show such cause, the Board may, subject to the agreement of the Minister, revoke the approval. There is no right of appeal.

INCOME TAX HOLIDAY, CUSTOMS DUTIES RELIEF AND DEPRECIATION ALLOWANCES

The grant of special status to an enterprise is accompanied by economic benefits in the form of exemption from income tax, relief from customs duties for a specified period and depreciation allowance. The Investment Incentives Code of Liberia grants beneficiary investments exemption from customs duties for five years. The code also provides for

tax holidays from income tax from five years to ten years commencing from the first year of marketable production.

In Kenya, Uganda and Tanzania, generous depreciation allowances are granted to approved enterprises under income tax laws. Varying reliefs from import duty, preferential measures and financial assistance are provided for in other statutes, official statements and contracts.

Under the Lesotho Pioneer Industries Encouragement Act,³³ an approved manufacturer may elect to be exempt from income tax for an initial period of six years or pay income tax after special deductions representing depreciation, write-offs, investment, building and capital allowance.

In Ivory Coast, goods indispensable for establishing an industry are entitled to duty-free entry.³⁴ The Chad Investment Code,³⁵ exempts profits earned by a new enterprise during the first five years of its operation from income tax. In addition, such an enterprise is entitled to a deduction, for the purpose of tax calculation, of one-half of the profits applied to the construction of industrial buildings and the purchase of heavy equipment. The Ghanaian Capital Investments Act³⁶ entitled approved enterprises to exemption from income tax for a period of five years which may be extended up to ten years. These enterprises enjoy generous capital allowance after the five to ten years of tax holiday: 25% for machinery, plant, furniture, fixtures and fittings, followed by an annual allowance of 15%; 20% for

buildings, structures and roads and an annual allowance of 10%. Even Sudan which provides for relatively tougher conditions for grant of special status, offers a general profits tax relief: up to 5% of the profits of approved enterprises is exempt from taxation and profits in excess of this are taxed at half the normal rate. The length of this tax holiday depends on the amount of capital invested; for instance, if less than LS20,000 is invested at the end of two years, the period of relief will be two years.³⁷ The Nigerian Industrial Development (Import Duties Relief) Act³⁸ makes provision for extension of the tax holiday if losses are sustained during that period. In addition, dividends from tax-free profits are also immune from tax. And the Act authorises the repayment of import duties on materials brought into the country for use in the manufacture or processing of goods or in the provision of services--for a maximum period of ten years.

³⁹

The Rwanda Investment Code grants concessions in proportion to the value of the activities of the enterprise to Rwanda, which is reflected in the nature, size and duration of the concessions granted under the various regimes laid down in the code. This is the general pattern found in the investment laws of the French-speaking African countries. The concessions granted partly or in full, range over a wide field relating to such matters as income tax, import