PRIVATE SECTOR ASSESSMENT: SOUTHERN AFRICA REGION

Final Report

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ACRONYMS

ADB	African Development Bank
AIDS	Acquired Immune Deficiency Syndrome
BOOT	Build-Own-Operate-Transfer
CBI	Cross Border Initiative
COMESA	Common Market for East Africa and Southern Africa
FDI	Foreign Direct Investment
FIAS	Foreign Investment Advisory Service
GATT	General Agreement on Tariffs and Trade
GDI	Gross Domestic Investment
GDP	Gross Domestic Product
GEIS	General Export Incentive Scheme
GEM	Growth With Equity Model
GII	Global Information Infrastructure
HPE	High-Performing Economies
HPE-3	Selected HPEs - Korea, Malaysia, Thailand
IBRD	International Bank for Reconstruction and Development
IFC	International Finance Corporation
IMF	International Monetary Fund
IRRC	Investor Responsibility Research Center
JAA	J.E. Austin Associates, Inc.
JSE	Johannesburg Stock Exchange
MAPS	Manual for Action in the Private Sector
MIGA	Multilateral Investment Guarantee Agency
NII	National Information Infrastructure
RCSA	Regional Center for Southern Africa
RILS	Regional Industrial Location Strategy
RSA	Republic of South Africa
SACU	Southern African Customs Union
SADC	Southern African Development Community
SAR	Southern Africa Region
SME	Small and Medium Enterprise
SOE	State Owned Enterprise
UNCTAD	United Nations Conference on Trade and Development
UNESCO	United Nations Educational, Social, and Cultural Organization
USAID	United States Agency for International Development
WAEN	West African Enterprise Network
WTO	World Trade Organization

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On behalf of the team, I would like to thank the many people who gave of their time for this exercise. As over 100 people were interviewed, they are too numerous to name. Many were entrepreneurs who are changing the face of their economies with big ideas and who shared their struggles and hopes with us. USAID officers in Washington and in the field also gave of their time. I would especially like to thank Ken Lanza, Mike Unger and Grant Morrill for their invaluable comments.

Finally, I would like to thank other staff members of J.E. Austin Associates who provided input and logistical assistance, including Joyce Lamoreux, Kristina Midha and Jamie Morin.

This study focuses on analysis rather than description, and therefore only that data essential to the analysis is repeated here. The best sources of regional data were provided to USAID/RCSA by the team.

It has been challenging to assess the private sector needs in a region as diverse as this and to develop proposals that make sense from a regional point of view. It is hoped that this report and the materials that accompany it will provide USAID/RCSA with inputs that will be useful in formulating its strategy, and that this will lead to an important impact on the SAR region and its future private sector development, upon which so much else depends.

Kevin X. Murphy
Team Leader, June 1996

EXECUTIVE SUMMARY

At the request of the USAID Regional Center for Southern Africa, J.E. Austin Associates conducted a constraints analysis and strategy assessment for private sector development in the southern Africa Region (SAR), which includes Angola, Botswana, Lesotho, Malawi, Mozambique, Namibia, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe.

The purpose of the study was to identify the most critical constraints to rapid, sustained, and broad-based private sector growth; to assess which of these could be addressed on a regional basis; to consider which interventions might provide the greatest impact for the level of resources available; and to suggest specific options.

The methodology for the study included a review of over 300 reports, interviews with over 100 stakeholders in 9 countries of the region, focus groups with southern African stakeholders and strategy sessions with southern African consultants who were integral parts of the team. The team used, as analytical frameworks, the Austin Policy Impact Matrix and the Growth with Equity Model.

The SAR economy and private sector have performed poorly over the last 20 years. The real growth rate has been only 3.4% over the last 20 years which translates into a real per capita growth rate of less than .25% during the last generation.

The problem is not lack of investment. The region, surprisingly, does not suffer from a lack of investment resources. The SAR has been investing over 25% of its GDP consistently over the last 20 years. Simply providing more resources will not solve the growth problem.

The problem lies with the quality of investment, or the GDP output achieved with a given level of investment. The team analyzed 20 years of data for the SAR and for selected Asian countries and looked at the incremental GDP output achieved for the level of incremental investment. While 100 units of investment produced 25 units of growth in the Asian countries, the SAR countries achieved, on average, only 12 units of growth for the same investment.

The quality and efficiency of investment in the SAR has been adversely affected by government policies. Socialist policies have deterred growth in Tanzania, Zimbabwe, Zambia, Angola and Mozambique. Apartheid distorted the economies of South Africa and Namibia. Poor government investment decisions and heavy parastatal investment have also led to poor returns on overall investment.

Even private sector investment has been rather inefficient in most countries of the region (Botswana is an exception). In South Africa and Malawi, the environment favored large, concentrated private sector firms. Protectionism has reduced the efficiency of the private sector in other countries such as Zimbabwe.

A comparative policy analysis confirmed that the SAR has had a very poor policy environment (in terms of trade, investment, institutionalization of business dialogue) not conducive to rapid private sector-led growth. The team found that the region, as a whole, would rank on only the 29^{th} percentile in terms of the quality of its policy, which partly explains why the region receives only 25% of the average world income per capita. The poor policy environment was re-confirmed in many studies and was a common theme in the 100 interviews across 9 countries of the region.

Trade barriers are the biggest impediment to growth, but investment policy and the lack of an institutionalized dialogue between private and public sectors in most countries and at the regional level are also important. Foreign investment, on average, has also been weak. Net inflows amounted to under $800M for 1994. This has now turned upwards, but foreign investors are still tentative.

Human resource constraints include low literacy rates and the lack of specific technical, managerial and entrepreneurial skills. The region actually invests a similar proportion of its GDP in education and within educational budgets a similar percentage to basic education as the high-growth Asian countries. However, in the SAR, the teacher-pupil ratio is nearly twice as high as in the high-performing Asian economies. Early school-leaving is also a problem, as only 62% of those starting primary education in the SAR finish, as compared to 92% in the Asian HPEs. Furthermore, the curriculum has placed little emphasis, until recently, on preparing people for careers in the private sector.

Despite complaints, the absolute lack of capital and credit is not the underlying problem. The financial sector suffers from lack of depth and breadth, and from an absence of mechanisms to link the formal financial sector to small and medium enterprise. While savings mobilization is low in the region and inflation has been a problem in most countries, credit to the private sector has been expanding. The problem is lack of access by small, emerging and especially African businesses. Some excellent models, such as community banking, are found in South Africa. But there is a dearth of such non-traditional financial institutions serving the needs of this sector.

While the lack of infrastructure, and its poor maintenance, has been well-documented, the cause of the problem is excessive parastatal involvement and the lack of involvement of the private sector in the planning, delivery and maintenance of energy, transport and telecommunications. The results are shortages of energy, poor telecommunications service, bad roads, delays at ports and poor railway service. With South Africa's integration into the regional economy, transportation networks and usage patterns are changing. The regional development strategy centers around a number of transportation corridors. However, private sector input is currently lacking; it must be a part of the planning and implementation of such schemes if they are to stimulate growth effectively.

Entrepreneurs and business leaders repeatedly stated that they lack access to information, contacts, markets and networks, and that this is a major constraint to business expansion. The potential for growth is further limited by the poor quality and high cost of communications in the region. However, plans by the World Bank and the USAID Leland Initiative soon could help link the region to the Internet and the World Wide Web by contributing to the development of a Global Information Infrastructure (GII).

Because of the legacies of apartheid, colonialism and socialism, the role of Africans in the formal economy is well below levels needed for either equity or efficiency. The formal economy is largely perceived as being state-run, foreign or in the hands of an ethnic elite. As a result, policies to promote the formal private sector do not always find broad popular support. African entrepreneurs face many barriers to entry to the formal private sector.

Despite these problems, the region has excellent potential. A survey of economic sectors revealed great potential in agriculture and agribusiness, some manufacturing sectors, mining, construction, tourism, energy, commerce and professional and personal services. There is also potential to capture more value through regional coordination and promoting the freer flow of goods throughout the region.

Many recent changes now improve prospects for private sector development in the region. These new changes include the end of regional conflicts, the end of apartheid, the removal of sanctions, the broadening of SADC, the openness of governments to market-oriented policies, the availability of direct and portfolio investment, the rebound in commodity prices, the end of the drought, and the trend towards democratization. On the other hand, the world is more competitive today than ever before, there are still some ethnic tensions in the region, donors have shrinking budgets, and AIDS is taking its toll on talented southern Africans. On balance, however, the prospects are positive.

To respond to the constraints, several regional approaches with potentially high impact have been recommended. These include a policy initiative for regional policy reform, assistance in broadening and deepening financial markets and linking them to SMEs, enhancing productivity of small and medium business through improved access and networking, and a regional counterpart to the USAID Leland Initiative to help make the "Information Revolution" a reality in the region. If the private sector program will have access to training resources, several such initiatives have been suggested.

Attention should be given to process, timing and sequencing. A 6-12 month scenario planning exercise could provide a means to bring together southern African leadership which has no current effective voice at the regional level. This core of leaders would lay out a vision for the region while also developing in more detail the results packages which have been presented here. But USAID should avoid creating its own regional actor or prematurely choosing inappropriate or unproven counterparts. The proposed strategic options are presented in summary form on the following page. The special needs of small business, African business and women-owned-business would be addressed in the context of these initiatives.

USAID/RCSA STRATEGIC OPTIONS

Constraint Category	Strategic Option
Policy	Encourage Regional Policy Reform and Institutionalized Public-Private Dialogue (Results Package 1)
Infrastructure	Facilitate Internet and Telecommunications through Regional Leland Support (Results Package 2)
Access	Enhance Small and Medium Regional Business Productivity through Access and Networking (Results Package 3)
Finance	Broaden and Deepen Regional Capital Markets and Link them to SMEs (Results Package 4)
Human Resources	Handled in the Context of All Other Options

I. CONSTRAINTS ANALYSIS

The following analysis of the constraints to rapid and sustained private sector growth in the southern Africa Region (SAR) was conducted for the USAID Regional Center for Southern Africa (RCSA) as an input for strategy development. The J.E. Austin Associates (JAA) team utilized a comprehensive methodology to ensure that the widest possible array of opinions, views and experiences were brought to bear on the constraints analysis.

A. MAJOR COMPONENTS OF THE CONSTRAINTS ANALYSIS

The JAA team consulted a variety of sources to inform the constraints analysis. These included: 1) a Literature Review; 2) interviews in nine SADC countries; 3) Focus Group discussions with stakeholders in the region; 4) the Austin Policy Impact Framework; 5) a comparative policy analysis; 6) the Growth With Equity Model; 7) a financial sector analysis; and 8) USAID MAPS exercises.

1. Literature Review (Annex I)

<u>The team reviewed over 300 documents, studies, analyses and reports which revealed salient constraints on private sector development</u>. The team contacted major donors including United Nations agencies, the World Bank and European Commission, requested a search of USAID/CDIE for relevant documents, procured Economist Intelligence Unit Reports, searched university libraries, conducted on-line searches of data bases and contacted relevant embassies in the Washington area. Of the 300 documents consulted, approximately one-third contained timely and useful information relating to private sector constraints in the region. Although not in the scope of work, the team acquired additional copies of the best materials and brought these to the USAID/RCSA Mission to create a core private sector library on southern Africa.

<u>The Literature Review provided an extensive list of over 50 constraints, based on expert opinion and supported by data, evidence and analysis</u>. The review enabled the team to conduct a ground-up analysis which revealed the major constraints. The purpose was to take advantage of the collective wisdom of others, rather than replicate already existing findings. With the encouragement of USAID/RCSA, the team refrained from imposing an analytical structure or jumping to conventional conclusions. Instead, the team let the studies and later the interviews speak for themselves and inform the analysis.

<u>The list of constraints generated from the Literature Review formed the starting point for the analysis and allowed for subsequent categorization of the constraints</u>. These fell under five major constraint categories: 1) government policy; 2) the financial sector; 3) human resources; 4) infrastructure; and 5) lack of access (to information, markets, contacts and networks). The issues of Africanization and legitimization of the private sector (also raised in the literature) are

analyzed in the Special Focus section of this report. The constraints revealed by the Literature Review are presented in summary tables located at the end of this report **(Exhibits 1-2)**.

The Literature Review had significant limitations. Analyses conducted more than two years ago usually did not reflect the fast pace of change in the region, the ending of apartheid in South Africa, the removal of sanctions, the expansion of SADC, and the resolution of wars and conflict. Even relatively recent data is often already out-of-date. Overcoming these limitations necessitated direct visits to the region to complement and broaden the constraints analysis.

2. Country Interviews

Over 100 interviews were conducted in 9 SAR countries by a joint team of southern African and international specialists. Mauritius was not visited as it was not in the original scope of work (it joined SADC later). Angola and Mozambique were not visited because of country clearance issues. South Africa had been covered in a private sector assessment in early 1994, and while selected interviews were conducted, they were not as extensive as in other countries. Interviewees included public and private sector representatives, both local and foreign. The J.E. Austin team included 10 southern African private sector specialists, who played a key role in gaining access to private and public sector leaders. This contributed significantly to both the interview process and subsequent analysis. A common interview format which allowed for open and free-flowing commentary was developed. For each country visit, a report was prepared.

The constraints revealed by the interviews were added to those highlighted by the Literature Review to obtain a more comprehensive constraints listing. Altogether, the J.E. Austin team analyzed 484 findings, judgments and conclusions regarding constraints to private enterprise in southern Africa. These were then narrowed down to 51 specific constraints (many people cited the same constraint). These constraints are found in **Exhibit 3**.

The 51 specific constraints were grouped into six broad categories for further analysis. These categories are found in **Exhibit 4**. The team then reviewed the interviews by constraint category and prepared a summary of the constraints analysis that flowed from the interviews **(Exhibit 5)**.

The interviews highlighted local concerns not fully captured in the Literature Review. The interviews confirmed the findings from the Literature Review regarding policy, human resource, infrastructure and financial sector constraints. However, the interviews placed much greater emphasis on the issues of lack of access to information, the need for networking, and the relative isolation of the region. The interviews also focused more on the problem of Africanization, the lack of which severely undermines popular support for pro-private sector policies. In addition, the interviews confirmed private sector frustration in non-SACU countries at not being able to access the South African market. This theme dovetails and confirms many of the studies which were reviewed. The interviews also focused on the lack of an institutional dialogue process involving the private sector (except in South Africa).

Finally, the interviews demonstrated the rapid pace of change in southern Africa. In response to political and economic reforms in most countries, foreign investment is growing in sectors such as mining, minerals, agribusiness and consumer goods. South African exports and investments to the region are up sharply. Regional business linkages such as the Africa Business Roundtable are developing. Tanzania is showing greater small business ferment than might be expected. Zambia's liberalization has resulted in a certain degree of de-industrialization, as cheaper imports are displacing domestic producers. The relative dominance of South Africa, which constitutes roughly 75% of the SAR GDP, has become the major economic issue for the private sector in neighboring countries.

3. Focus Groups (Annex II)

Focus Groups held in three countries, with broad regional representation, confirmed the basic findings of the constraints analysis and added additional insights and clarification. Five Focus Groups (discussion sessions comprised of 6-15 public and/or private sector representatives) were held in Harare, Johannesburg and Gaborone dealing with Small and Medium Enterprise (SMEs), Human Resources, Africanization, Trade and Investment, and Policy Reform. Presentations of the findings from the Literature Review and country interviews stimulated lively discussion among southern African business leaders. A list of participants and summaries of these discussions are found in the annex.

The Focus Groups allowed the J.E. Austin team to take a regional view of constraints which had been raised at the country level. By bringing together individuals from different nationalities, Focus Group discussions provided for a cross-fertilization of ideas, viewpoints and experiences, and thus contributed to a more thorough region-wide constraints analysis. Focus Group conclusions are summarized in **Exhibit 6**.

Southern Africans agreed that the constraint categories were useful and that policy constraints are paramount in the region. Furthermore, the southern African business community agreed that government policy is the single most important constraint for private sector development. A summary of the major points discussed in these sessions is found in **Exhibit** 7.

4. The Austin Policy Impact Framework

The Austin Policy Framework was used to link public policy to specific impacts on private companies. The framework, presented on the following page, illustrates the practical impacts of policy on the financial, marketing, production and organizational aspects of private enterprise management in developing countries. Governments impact these managerial areas and affect company operations through various mechanisms which can be identified as legal, administrative and direct market operations. By understanding and applying this framework to the broader constraints analysis, the J.E. Austin team was able to identify the macroeconomic influences on SAR private sector actors, and analyze their specific impact on day-to-day company operations. This provided a practical view of the policy constraints affecting SAR business growth and lent valuable support for the formulation of appropriately targeted strategic interventions (see Table 1 below).

Table 1:

Austin Policy Impact Framework					
Policy		*Company Impact Points***			
Category	Instrument	Finance	Marketing	Production	Organization
Monetary	interest rates (A)*	X			
	loans (O)	X			
Fiscal	tax rates (L)	X			
	investment credits (L)	X		X	
	govt. sales (O)			X	
	govt. purchases (O)		X		
Income	price controls (A)		X		
	wage controls (A)	X			X
Trade	tariffs (A)	X	X		
	import quotas (A)		X	X	
	export incentives (L)	X	X		
	exchange rates (A)	X	X		
Foreign Investment	ownership requirements (L)	X	X		
	repatriation regulations (A)	X			
Sectoral	technology licensing (A)	X		X	X
	production licensing (A)			X	X
	SOE operations (O)	X	X	X	X

* Types of policy instruments: L= Legal; A= Administrative; O= Direct Market Operations
** Management control aspects of each of the four functional areas could also be affected
Source: Austin, James E., Managing in Developing Countries: Strategic Analysis and Operating Techniques, 1990

5. Growth with Equity Model (Annex III-A)

The Growth with Equity Model (GEM) is an analytical tool devised by J.E. Austin Associates based upon a recent World Bank study on the high-performing Asian economies entitled The East Asian Miracle. The J.E. Austin team, after consulting with the study author, applied the World Bank findings to the SAR region by creating a series of GEM analyses. These analyses provided useful benchmark data and an analytical tool to assist in the evaluation of the critical policy-related constraints to private sector growth in the SAR region. Private sector development in Asian countries has led to both high rates of growth and better distribution of income. It has led to higher life expectancy, reduced infant mortality, better health and sanitation, and increased educational attainment (especially for women). Removal of specific constraints to private enterprise will promote overall economic growth which, in turn, leads to gradual improvement in broader, non-economic development objectives.

The GEM analyses yielded three critical factors explaining rapid and sustained growth in East Asia. These were: 1) the level of investment, particularly private sector investment; 2) productive human resources as measured by functional literacy and the age of school-leaving; and 3) total factor productivity (or the efficiency with which productive inputs are utilized). These factors are, in turn, influenced largely by sound government policies and an openness to market forces. Taking its lead from these findings, JAA conducted an analysis of these three critical factors for growth in the region.

6. Comparative Policy Analysis (Annex III-B)

The Comparative Policy Analysis evaluated 10 critical policy areas: trade policy, taxation, government consumption of economic output, monetary policy, capital flows and foreign investment, banking, wage and price controls, property rights, regulation and parallel market activity. The analysis determined that SAR policies are ranked very low in terms of the degree to which they promote free enterprise. Furthermore, trade policy received the lowest ranking. Botswana has the most pro-private enterprise policies while Angola and Mozambique, with legacies of civil war and Marxist control, remain the most anti-free enterprise in the region. While overall policy scores improved slightly in the last year, they still fall far short of what is needed to achieve rapid and sustained economic growth. The Comparative Policy Analysis is presented in **Annex III-B**.

7. Financial Sector Analysis (Annex IV)

A Financial Sector Analysis was conducted for the region and shed additional light on financial sector constraints. A summary of this analysis is presented in Section II-C below; the full Financial Sector Analysis is presented in the Annex.

8. USAID MAPS Exercises

USAID MAPS exercises and other private sector assessments provided important data and analysis on the constraints affecting African business. The recent USAID MAPS exercise in South Africa focused on black economic empowerment and the problem of Africanization of the economy. While apartheid was an extreme case, the issue of Africanization was encountered throughout the region and will be discussed below. In Mozambique and Angola, MAPS-like exercises which had been undertaken independently of USAID were used as proxies.

9. Results of the Above Analyses

The above activities and analyses provided multiple confirmations of the critical constraints to private sector growth in the SAR region. The constraints which were identified and ranked did not flow from an armchair exercise but were the result of multiple and cross-cutting methodologies which included economic analyses of existing data, multiple policy reviews, extensive field interviews and regional Focus Groups. These were measured against the experiences of high-growth countries, which confirmed that the variables that led to such growth were not present in the SAR or present to the same degree.

Thus, the J.E. Austin team is confident that the following are the key constraints to private sector growth in southern Africa: 1) unfavorable government policies, especially as they relate to trade, investment and the institutionalization of dialogue; 2) weak financial sectors; 3) underdeveloped human resources; 4) poor infrastructures; and 5) insufficient access to information, contacts and networks. In addition, the formal private sector in many SAR countries does not resemble the larger population. Hence, it lacks legitimacy and broad popular support. Africans are active in the traditional agricultural sector, the informal sector and the public sector, while the formal sector is disproportionately foreign, state-owned, or in the hands of ethnic elites. Any long-term private sector strategy must address this anomaly.

Having identified and documented the above constraints, each will be analyzed in greater detail using the results of the above-mentioned exercises and summarizing the more complete analyses found in the Annexes. The sources in which each constraint was found are detailed in **Table 2**.

Table 2: Broad Summary of Constraints and Their Sources of Validation

Constraint	Literature Review	Inter-views	Focus Groups	GEM Anal.	Comp. Policy Anal.	Financial Sector Assessment
1. Policy						
i. Policy: Trade	x	x	x	x	x	
ii. Policy: Investment	x	x	x	x	x	x
iii. Policy Process		x	x	x	x	
iv. Policy: Other	x	x	x	x	x	x
2. Financial Sector	x	x	x	x	x	x
3. Human Resources	x	x	x	x		
4. Infrastructure	x	x	x	x		x*
5. Access to Information, Contacts and Networking		x	x	x		
6. Special Focus: Africanization	x	x	x	x		x

* Better telecommunications is a prerequisite for regional financial integration and cross-border capital flows.

B. ANALYSIS OF KEY CONSTRAINT AREAS

The following section presents the summary analyses of the key constraint areas identified and confirmed through the aforementioned exercises.

1. Policy Constraints

The J.E. Austin team utilized several methodologies to analyze policy constraints in the region. After reviewing the policy analysis work of many sources, the JAA team relied most heavily on the Austin Policy Framework, the Growth With Equity Model, the Heritage Foundation Index of Economic Freedom, country interviews and Focus Groups. Overall, the worst area of policy for the SAR was trade, while the best was wage and price control

SADC Policy Ranking

Rank	Policy Area	Score
#1.	Wage/Prices	2.90
#2.	Government Consumption	3.00
	Property Rights	3.00
#4.	Banking	3.10
	Foreign Investment	3.10
#6.	Monetary Policy	3.50
#7.	Regulation	3.60
	Taxation	3.60
#9.	Parallel Market	3.80
#10.	Trade	4.40

* 1 = best, 5 = worst

a. Domestic and Foreign Investment Policy

Southern African countries annually invested a relatively high 26.4% of GDP, on average, over a 20-year period, dispelling the myth that the region suffers from lack of investment resources. While this figure is skewed by the extremely high investment levels of Botswana in the 1970s and Lesotho in the 1980s and 1990s, it is clear that the principal problem is neither lack of capital nor the overall level of investment. While the overall level of investment was slightly less in the SAR region than in selected Asian countries included in our analysis, it was not the major constraint to private sector growth **(Exhibit 8)**.

The SAR suffers from a quality of investment problem. The J.E. Austin team analyzed levels of investment and subsequent incremental growth in GDP over a 20-year period for all countries of the region for which data were available and compared them with selected Asian countries. From this data, the team constructed an Incremental Investment to Incremental GDP Output Ratio (presented in **Exhibit 9**). In the selected Asian countries, 100 units of incremental investment produced 25 units of incremental GDP output. In the SAR countries, the same investment achieved only 12 units of GDP output. In other words, it took the SAR double the investment level to achieve the same impact on growth. Investment was less than half as productive in the SAR in achieving economic growth. More investment resources alone will not solve the problem facing SAR countries.

Botswana actually surpassed the Asian countries in terms of quality of investment, while Malawi came in a poor second. In Zambia, investment resources were massively squandered--100 units of investment yielded only 5 units of growth, meaning that the country would have to invest 160% of its annual GDP to achieve an Asian-level 8% growth rate per annum. The efficiency and quality of investment in South Africa was also near the bottom for the region over the same 20-year period **(Exhibit 9)**.

The low quality of investment is partly, but not fully, explained by the percentage of public vs. private investment. World Bank data show that private investment accounts for 57% of total investment in SAR countries, a higher percentage than that found in the rest of Sub-Saharan Africa **(Exhibit 10)**. This percentage of private investment, while lower than some high-growth countries, is respectable. However, private investment data often includes the parastatal sector, and SAR countries have invested large amounts of capital in inefficient state-owned enterprises. Zambia, which has the worst quality of investment score, is characterized by high parastatal involvement in the economy.

The quality of investment problem is primarily driven by the poor policy environment. Having demonstrated that the SAR's critical bottleneck to private sector growth is not the absolute level of investment but the quality, efficiency and productivity growth of that investment in the SAR policy context, one must examine SAR policies in greater detail.

Private sector investment has also been inefficient in poor policy environments. In South Africa, for example, even private sector investment was inefficient in the context of apartheid, sanctions and a highly protected environment stressing self-sufficiency and import-substitution. Protected private sector companies in other countries are also inefficient in allocating resources to their most productive uses.

Small-scale investment has been discouraged by over-regulation, taxation and other barriers to entry. SME investment has been discouraged by a number of policy-related measures which discourage entry into the formal sector and the subsequent accumulation of capital. The environmental bias towards large companies in South Africa and Malawi, and towards socialism in Angola, Mozambique, Tanzania and Zambia, discouraged the growth of small and medium private sector companies in these countries. The licensing, regulatory and taxation impediments to formalization have been well-documented.

Such impediments have had a particularly damaging effect on the emergence of indigenous African business – a result which stands in sharp contrast to the stated policy goals of Africanization in highly regulated SAR economies. These impacts on indigenous African business have not been studied adequately at a regional level, but were well-documented in the interviews that the team conducted throughout the region.

Foreign direct investment (FDI) figures show relatively low levels of net inflows to the region but do not capture recent increases since 1994, especially in South Africa. FDI levels in the SAR have been low in comparison to other regions. According to recent United Nations Conference on Trade and Development (UNCTAD) data, for example, Sub-Saharan Africa accounted for only 4.3% of total foreign direct investment flows to developing countries in 1994 while the Asia-Pacific region accounted for over 50% of total flows during the same year. Foreign investor interest, however, is growing in response to political and economic reforms in many countries. According to the World Bank, net foreign direct investment flows to the SAR region were US$747M in 1994, up from US$578M in 1993 **(Exhibit 11)**.

The Comparative Policy Analysis indicates that government investment policies are mediocre but that barriers to investment are declining (Table 3 below). The region has only moderate barriers to foreign investment. South Africa and Zambia now have the lowest barriers to foreign investment in the region while Angola, Zimbabwe and Mozambique have the highest. However, Angola's investment impediments have neither stopped major petroleum companies from investing in the country nor discouraged new South African investment. Interviews in South Africa revealed more eagerness for liberalizing the country's investment regime than trade regime. Furthermore, most SAR countries have recognized the positive contribution of foreign direct investment (through the provision of capital, technology, managerial expertise, and international marketing and distribution linkages) in promoting economic growth.

Table 3:

Capital Flows And Foreign Investment Policy Summary

Rank	Country	Score*	Trend	Assessment
1.	Zambia	2	Improving	Low barriers to foreign investment
2.	South Africa	2	Stable	Low barriers to foreign investment
3.	Namibia	2.5	Improving	Moderate barriers to foreign investment
4.	Botswana	3	Improving	Moderate barriers to foreign investment
5.	Lesotho	3	Stable	Moderate barriers to foreign investment
5.	Malawi	3	Stable	Moderate barriers to foreign investment
5.	Swaziland	3	Stable	Moderate barriers to foreign investment
5.	Tanzania	3	Stable	Moderate barriers to foreign investment
9.	Zimbabwe	4	Improving	High barriers to foreign investment
10.	Mozambique	4	Improving	High barriers to foreign investment
11.	Angola	4	Stable	High barriers to foreign investment

* 1 = Best; 5 = Worst

Although foreign direct investment in the SAR is growing, it remains constrained by investor concerns regarding political stability, trademark and intellectual property protection, and labor productivity and reliability. These concerns were confirmed by country interviews with private sector stakeholders in the region and by a recent survey by the Investor Responsibility Research Center.

Likewise, portfolio investment is constrained by undeveloped capital markets and lack of common standards which would facilitate cross-listing. Significant portfolio investment has begun to flow to Southern Africa, but most of this has been to South Africa. Although the International Finance Corporation (IFC) presents data for stock markets in 7 SAR countries, South Africa accounts for over 98% of the traded value and market capitalization **(Exhibit 12)**.

South African investment in other countries grew sharply in 1995. Opposition to the apartheid regime greatly limited the role that South African capital could play in the economies of the region, although Botswana, Lesotho and Swaziland all experienced significant inflows, especially in the mining sector. Following all-race elections, South African direct outward investment in Africa has increased, totaling 3.8 billion Rand (US$1.1 billion) in 1995. The non-RSA countries of the SAR received more investment from South Africa than from the rest of the world combined.

There has been modest improvement in the level of gross domestic investment in SAR countries. Indeed, the percentage of GDP allocated towards investment was above 30% for most of the 1990s, approaching Asian levels. Overall investment productivity is affected by the large role of state-owned enterprises in many SAR economies **(Exhibit 13)**.

b. Trade Policy

Among 10 policy areas which were rated by the Comparative Policy Analysis, the region scored the worst in the area of trade policy (Table 4 below). The region continues to operate within a protective cocoon. Zambia is now rated as having the least protectionist policy in the Southern Africa region. Angola, Mozambique, South Africa and Zimbabwe are still rated as highly protectionist. The need for deregulation of domestic economic activity, lower tariff barriers and greater orientation towards export markets is evident. However, all SAR countries are either stable or moving in a positive direction. This trend will likely continue as SAR countries begin to implement trade policy reforms in accordance with World Trade Organization (WTO) guidelines, albeit to differing degrees and schedules.

Table 4:

Trade Policy Summary

Rank	Country	Score	Trend	Assessment
1.	Zambia	3	Improving	Moderate level of protectionism
2.	Botswana	4	Stable	High level of protectionism
2.	Lesotho	4	Stable	High level of protectionism
2.	Malawi	4	Stable	High level of protectionism
2.	Namibia	4	Stable	High level of protectionism
2.	Swaziland	4	Stable	High level of protectionism
7.	Angola	5	Improving	Very high level of protectionism
7.	Mozambique	5	Improving	Very high level of protectionism
7.	South Africa	5	Improving	Very high level of protectionism
7.	Zimbabwe	5	Improving	Very high level of protectionism
11.	Tanzania	5	Stable	Very high level of protectionism

* 1 = Best, 5 = Worst

Barriers to trade in the SAR take a variety of forms. Most nations impose moderately high tariff rates, but the majority of protection takes the form of import licensing, quotas and bans. Mozambique and Angola, still recovering from civil war, suffer particularly from corruption in customs service, while Botswana has the fewest non-tariff barriers. With the re-entry of South Africa into the regional market, there are increasing trade tensions. The Southern African Customs Union (SACU), while reducing barriers to trade among member countries, also includes a high external tariff. This imposes high costs on trade with non-SACU countries.

Relaxation of trade barriers is crucial for SME growth. Cheaper imports and liberalized regulatory procedures would promote specialization and expansion, reducing the cost of business activity. Reduced dependence on domestically-produced inputs and parastatal channels of supply and distribution would facilitate SME entry into productive sectors of the economy.

c. Institutionalization of Business-Government Policy Dialogue

Institutionalized dialogue is weak in many SAR countries and almost non-existent at the regional level due to historical reasons. South Africa is one of the few countries with strong business associations and the dialogue process has been emphasized and expanded by the current government. At the regional level, there is no effective private sector counterpart to the Southern African Development Community (SADC). It is hoped that one result of the recent SADC liberalization will be the development of strong business associations that, in turn, can develop regional networks. The African Business Roundtable has had only limited impact to date in fostering regional policy reform in Africa. The West African Enterprise Network has been relatively successful in that region in mobilizing business-government interaction. Umbrella regional Chambers of Commerce have proven weak in their ability to provide effective representation to local businesses. More targeted, sectoral and industry associations may hold greater promise in this regard.

Investors, both domestic and foreign, now look beyond the current policy environment, favorable or unfavorable, and focus on whether there is a transparent and institutionalized process whereby the government consults the private sector on major policy changes. This view was confirmed by officials at the Foreign Investment Advisory Service (FIAS), a member of the World Bank Group which advises developing country governments on investment promotion strategies. It is no longer enough for a government to implement pro-investment policies. If these policies are hermetically designed and influenced, sophisticated international investors are more reluctant to make major investments. However, if a government has institutionalized a regular and open consultation process with the private sector, investors perceive the overall investment environment as less risky. Such a consultation process is particularly critical for investors in the infrastructure sector, given the high up-front capital costs and long time horizons associated with large-scale infrastructure projects. The institutionalization of consultative mechanisms may occur through tripartite consultative groups (such as those that currently exist in South Africa), by requiring a comment period on new legislation or regulation, or by having a judiciary which impartially and fairly examines private sector claims for arbitrary changes in government contracts or regulations.

Institutionalizing the business process helps achieve not only growth objectives but also civil society objectives. The decentralization of power and the institutionalization of dialogue contribute to the ongoing development of a favorable business climate while simultaneously limiting arbitrary and concentrated economic power in the hands of political authorities. Such an environment engenders both business growth and greater political legitimacy.

d. Other Policy Issues

While trade and investment are critical, other policy areas also affect private sector growth. The Comparative Policy Analysis (Annex III-B) highlighted additional policy areas unfavorable to private sector growth. Tax rates in the region are moderate to high, but the formal sector often bears a disproportionate burden. Taxes on exports, imports, trade and travel have also been prominent due to ease of collection.

Monetary policy varies sharply in the region, but the overall trend is positive. Zambia, Angola and Mozambique suffer from very high inflation while Botswana and Swaziland have lower levels. (Clearly, Swaziland's inflation rate is determined to a large extent by that of South Africa by virtue of its membership in the Common Monetary Area.) Overall inflation levels in most countries, including South Africa, have been declining in recent years, suggesting greater budgetary discipline and macroeconomic management.

Restrictions on banking also vary sharply in the region. Botswana and Zambia have relatively low restrictions, while several countries, such as Mozambique and Lesotho, maintain high restrictions.

Wage and price controls, while still a factor, are not as prominent an issue. A high incidence of wage and price controls still exists in Angola and Lesotho. South Africa, Tanzania and Zimbabwe all have low levels of wage and price intervention, although South Africa, with a strong union movement, is not regarded as having competitively priced labor.

The degree of property rights protection varies in the region. Policies and practices which safeguard property score highest in Botswana and low in Zambia and Malawi. Angola and Mozambique scored the worst, but the situation has shown signs of positive movement.

Modest improvements in the policy environment have been registered. Both the GEM analysis and the Index of Economic Freedom confirmed these recent improvements. Zambia, for example, liberalized its trade and investment regime significantly. Tanzania has also created a better environment for the emergence of small enterprise. Zimbabwe lowered several tariff barriers. Overall, the SAR policy environment ranks slightly higher than Sub-Saharan Africa in general, and is improving at a slightly faster pace.

Overall, Botswana has the most pro-private enterprise policies while Angola and Mozambique, with legacies of civil war and Marxist control, are still the most anti-free enterprise (Table 5). However, Mozambique has made the most year-to-year progress in this area since 1992. Some counter-intuitive results are noted. Zambia ranks higher than other countries which have stronger private sectors, but its reforms are very recent.

Interviews in the region tended to corroborate that government policies were the single largest impediment to private sector growth. In the absence of a commodity boom, the region is unlikely to achieve high rates of growth in income per capita unless significant policy changes are made.

Table 5:

Summary of Overall Scores

Rank	Country	Score	Trend	Assessment
1.	Botswana	2.8	Improving	Primarily committed to free enterprise
2.	Swaziland	2.9	Stable	Primarily committed to free enterprise
3.	Zambia	2.95	Improving	Primarily committed to free enterprise
4.	South Africa	3.0	Stable	Moderately committed to free enterprise
5.	Namibia	3.2	n/a	Moderately committed to free enterprise
6.	Malawi	3.4	Stable	Moderately committed to free enterprise
7.	Tanzania	3.45	Improving	Moderately committed to free enterprise
8.	Lesotho	3.65	n/a	Moderately committed to free enterprise
9.	Zimbabwe	3.7	Worsening	Moderately committed to free enterprise
10.	Mozambique	4.05	Improving	Not committed to free enterprise
11.	Angola	4.35	Stable	Not committed to free enterprise

* 1 = Best, 5 = Worst

2. Financial Sector Constraints

Lack of long-term capital, the underdeveloped nature of capital and stock markets, a disproportionately heavy focus on short-term trade and inventory finance, excessive collateral requirements and the lack of institutional mechanisms to meet the needs of small- and medium-scale enterprises are among the constraints facing the financial sector in the SAR region, especially outside of the Republic of South Africa.

<u>The lack of convertibility of SAR currencies represents a further obstacle to regionalization of the financial sector, a key step in encouraging growth</u>. Most of the countries in the region face continued macroeconomic instability, which discourages active currency markets and reduces convertibility. Because the currencies are so thinly traded, exchange rates are extremely volatile. Additionally, the high transaction costs associated with using SAR currencies tends to discourage foreign investment as it makes repatriation of profits difficult.

<u>The focus of existing lending institutions is on short-term finance to the detriment of long-term loans needed to spur private sector development</u>. High and erratic inflation rates, political instability and a lack of long-term savings have combined to make long-term finance difficult. Such loans, however, are essential for small and medium enterprises seeking to expand. Recent political and economic developments have improved the situation, but effective policy responses to the new opportunities are still needed.

<u>Small and medium enterprise access to credit is further restricted by extremely high collateral requirements and the lack of effective institutions to serve SME needs</u>. Collateral requirements are especially onerous for start-up ventures in rural areas, where land is often held communally, but they also stifle small businesses in general. Solutions to this problem are difficult – lending institutions are averse to the risk of lending to small start-ups and prefer extending loans to well-

established firms. This situation is likely to improve as the regional economy stabilizes and lending risks decline, but policy and sectoral level solutions are still advisable.

Commercial banks suffer from extensive over-lending to the public sector, extremely poor savings mobilization and high levels of insolvency. **Exhibit 14** shows the asset levels of the 17 banks in the region which were among the top 100 African banks in 1994. Government involvement in the banking sector has been particularly prominent in Angola, Mozambique and Tanzania. Institutional insolvency and extensive non-performing loans (often to governments or parastatals) tend to encourage lenders to be even more risk-averse, further reducing the likelihood that they will lend to marginal clients.

Extensive interviews showed that while availability of credit does not appear to be a constraint, access to credit by small and medium enterprises is a serious problem. This indicates a need for developing mechanisms of intermediation, such as financially viable NGOs, *stokvels* or credit unions which can capture credit from larger institutions, channel credit downwards and manage credit allocation effectively.

3. Human Resource Constraints

The GEM Analysis illustrates that a surprisingly large percentage of the performance of Asia-Pacific countries is explained by human resources. Levels of investment and productivity of investment explain only part of the high growth. Much of it is due to the ability of Asian economies to provide people with productive jobs. It is harder to achieve high growth while a significant percentage of people are idle or underemployed.

The most basic impediment to participation and productivity is not knowing how to read; 40% of SAR adults are illiterate **(Exhibit 15)**. Universal literacy must be a priority and has been in the high-growth economies.

The problem is not just one of low spending on education. SAR countries are investing about the same percentage of their budget in education as the "Asian 8." While the Asian High Performing Economies spent somewhat more of their GDP on education in 1960 (2.5%, compared to 2.0% for the SAR), by 1992 the SAR was spending a significantly higher percentage (6.15% to 4.4% for the HPEs) **(Exhibit 16)**.

Furthermore, SAR countries are investing relatively similar percentages of their total educational budget in basic education. Interviews and comments led the team to believe that SADC countries spend disproportionately on university education for elites at the expense of basic education for the population at large. But this is not supported by World Bank and UNESCO expenditure statistics. SAR countries spend 42% of their educational budget on primary education, about the same as the HPEs **(Exhibit 16)**.

The SAR suffers from poor teacher to student ratio (42:1) compared to the HPEs (24:1). Part of the difference lies in the quality of education as measured by the student/teacher ratio. While the

SAR and the HPEs had similar student-to-teacher ratios in the 1960s, the differences today are dramatic.

The drop-out rate is a major problem – only 62% finish primary school. In the average SAR country, 90% of the eligible population is enrolled in the first grade, inferior but comparable to the 96% in the HPEs. However, while virtually all students in the HPEs complete their primary education, only 62% of enrolled students do so in the SAR. These two differences explain much of the gap in literacy between the regions.

Educational curricula are inappropriate to the needs of the private sector. In South Africa, historically black schools focused on educational areas which prepare people for clerical jobs, lower-level government administration or personal services (teaching, nursing); there was only one black university program geared to preparing people for business. While the apartheid system is clearly a special case, Focus Groups revealed that the educational systems in most other countries have also been biased towards preparing Africans primarily for public sector jobs. Role models and invited speakers at educational institutions are usually public sector representatives. Only recently has the emphasis shifted towards preparing students for the private sector.

Specific technical and managerial skills are also lacking. Although it was beyond the scope of this exercise to conduct a thorough training needs assessment, the interviews and Focus Groups revealed a shortage of trained technical and managerial personnel in areas as diverse as electrical repair and marketing management. The need for business/management training was frequently mentioned in the country interviews.

Some SAR countries have regulations or laws which suppress the use of unpaid or low paid apprenticeships, creating an artificial barrier to private sector entry. Case studies in the region ave demonstrated that these apprenticeship arrangements can be an important path to the acquisition of technical skills. Focus Groups revealed that secondary education does not always focus on the technical skills required in the marketplace. By providing practical, on-the-job training as a complement to formal education, apprenticeships can help alleviate the human resources constraint prevalent in the SAR region.

The region also lacks appropriate mechanisms to link private sector demand to public education. The private sector can play a role in supporting local education and in articulating its needs to the educational system. Outside assistance can also play a role in this area. South Africans, for example, have asked for help from the United States in developing entrepreneurial-oriented curricula appropriate to secondary schools. This kind of endeavor, however, has not yet become widespread in the region.

Education is not only a constraint to private sector development - the latter also affects the former. One does not need to wait until the human resource and education problem has been solved. Rather, it has been found that strong private sector growth also stimulates demand for education and provides greater incentives and motivations for parents to ensure that their children receive appropriate schooling. Creating a climate conducive to foreign investment, for example, encourages large companies to invest in the education and training of their workforce. This part of the education equation is too often overlooked, but it opens the possibility of creating a virtuous cycle in which education breeds investment and vice versa.

The southern Africa region is also characterized by relatively low labor productivity and stringent labor regulations. Labor problems such as strikes and instability were mentioned often during the course of analysis. Focus Groups presented examples of labor regulations which are inflexible and add to the costs of employment. From the GEMS analysis, it is clear that one of the factors which helped Asian countries achieve high growth was lack of industry-wide unions. An implicit social pact between the government and the people, combined with government discouragement of powerful unions, contributed to a pro-growth environment in these countries. Such a finding goes against the grain of Western, particularly American, values. However, it is also true that these Asian countries experienced dramatic declines in absolute poverty and even rapid improvement in income distribution. Developing a growth-with-equity *modus vivendi* between business and labor will improve prospects for growth. A recent IRRC survey of US investors found that for those investing in manufacturing or other blue-collar areas, this issue was especially important as inflexible labor regulations and labor unrest create an added risk to the investment environment.

Health issues, including AIDS, also act as a constraint to private enterprise. AIDS has and will continue to have a disproportionate impact on highly skilled, managerial and entrepreneurial talent. Unlike in the United States, AIDS has affected the more educated segments of the African population. In addition, malaria, malnutrition and other endemic health problems result in employees with poor physical and mental capacities. The private sector can play some educational role in this regard, but the solution to such problems does not fall under the purview of a private sector program. Rather, it requires a targeted health sector initiative.

4. Infrastructure Constraints

The region suffers from numerous absolute constraints of physical infrastructure - lack of infrastructure, poor quality and specific blockages. The availability of telecommunications, transportation (including ports), power, and water and sanitation is severely limited in the southern Africa region. **Exhibit 17** shows that the density of infrastructure (i.e., roads, telephone connections, electricity connection) in the SAR is considerably lower than in the HPEs and OECD economies. Even South Africa, which has the most highly developed infrastructure in the region, has only about 90 telephone mainlines per 1000 population.

The availability and condition of infrastructure are major constraints to private enterprise throughout the region and the situation is improving only slowly. While plans are now underway for expansion of regional infrastructure (e.g., Walvis Bay, Highlands Water Project, Trans-Caprivi Road), these will not fully meet the needs of private enterprise largely because the private sector does not play a sufficient role in the planning and delivery of infrastructure and services.

Moreover, compared to the HPEs, infrastructure availability has grown much more slowly in the SAR. For example, both per capita electrical generating capacity and per capita telephone connections have increased much more quickly in the HPEs than in the SAR **(Exhibit 18)**. The HPEs have placed a strong priority on investment in infrastructure. This investment has been both public and, especially recently, private.

In many SAR countries, infrastructure is highly degraded and either cannot be effectively used or can only be used at high cost. Current infrastructure projects, which focus on building new networks, divert funds from the equally important goal of infrastructure maintenance. Some countries in the region, particularly South Africa, Botswana and Namibia, have maintained their infrastructure in good condition. In others, however, the rate of road decay exceeds that of road construction. The situation is similar with other forms of infrastructure. Poor maintenance and management of existing infrastructure compounds the restrictions placed on private enterprise development by insufficient network. Also, the costs of service and usage in the region are high when compared to international costs. The percentage of road infrastructure in acceptable condition (Table 6) is a good measure of these costs, as poorly maintained roads increase travel time and expense. The World Bank recently warned that adequate spending on infrastructure maintenance avoids much higher reconstruction costs. Indeed, in Africa alone, US$12 billion in maintenance spending would have prevented US$45 billion in infrastructure decay (*World Development Report 1994)*.

Table 6:

Road Maintenance in the SAR

Country	Percent in Good Condition
Botswana	94.00
Lesotho	53.00
Malawi	56.00
Mozambique	12.00
Namibia	n/a
South Africa	n/a
Swaziland	n/a
Tanzania	25.00
Zambia	40.00
Zimbabwe	27.00

Source: JAA Infrastructure Summary

The lack of infrastructure investment and inefficient delivery of infrastructure services are, as numerous studies and interviews emphasize, a constraint to private enterprise and economic growth. Insufficient infrastructure increases costs and multiplies barriers to entry; government policy and inefficiency often exacerbate these problems. Examples of these costs and barriers include high costs and delays of moving goods through ports, delays at borders, poorly maintained roads vital to regional transport, energy shortages, water shortages, poorly functioning telecommunications and restricted access to (and high cost of) basic telecommunications. Delays in obtaining telephone linkage, for example, are dramatically higher in the SAR than in the HPEs.

Constraints also arise due to a lack of cross-border cooperation and coordination. Complicated customs procedures at border crossings, differing axle load standards and requirements to change trucks when shipping between some countries are a few examples of barriers to trade and low-cost movement of goods.

In countries in which parastatal companies provide transportation, port operations, water, telecommunications and other services, service constraints - high costs, poor quality and barriers to entry - are particularly severe. Services are generally poorly planned and delivered, and are not coordinated either within or between countries. Furthermore, there is insufficient stakeholder voice in service planning and little customer focus.

Historically, the region's transportation network was highly dependent on South Africa, and both infrastructure and services were structured to depend on (and in some cases serve) South Africa. As alternatives to dependence on South Africa in the transportation sector, networks connecting to Angolan and Mozambican ports became important but were damaged and unused because of civil war. Connections through Tanzania were developed but have been notably inefficient.

The regional transportation network and usage patterns are changing rapidly. New and revived regional connections (e.g. Trans-Kalahari Road, Trans-Caprivi Road, Mozambique corridors, Walvis Bay port) are being developed and offer opportunities for new linkages and competition between networks. In South Africa , several transportation and development corridors are to be developed, including a corridor to Maputo, for which concession agreements are being tendered (June 1996). At the same time, the South African transportation network, particularly the port system, is overburdened. With this new infrastructure, usage patterns and costs will change enormously in Southern Africa in years to come.

A great emphasis has been placed on improving the extent, quality and management of infrastructure and services in the southern Africa region. The World Bank and other agencies are supporting infrastructure upgrading and management programs of immense national and regional import - in countries such as Tanzania, Zambia, Malawi and Mozambique.

While major opportunities are available to SAR through modern telecommunications, the lack of private involvement in telecommunications planning threatens these possibilities. The interviews and Focus Groups highlighted the region's isolation: 1) lack of access to information about markets, suppliers, partners, finance; and 2) inability to network with colleagues and contacts in other countries. Rural areas and smaller urban areas are particularly isolated and ill-served. The region is being assisted by USAID, the World Bank and other donors to develop its telecommunications infrastructure, increase availability of service and decrease costs. However, private sector stakeholders have thus far been given little voice in public sector programs for telecommunications. Furthermore, while telecommunications offers an opportunity for an active private sector role in service provision, private involvement is still resisted by governments in several countries in the region (notably Zimbabwe).

Although privatization and public-private partnerships in infrastructure and related service provision have become viable options world-wide, there is significant opposition, uncertainty, delay and backsliding in the SAR. Public budgets are insufficient to provide the world-class infrastructure and related services that are needed in the region. Private enterprise and investment has an important role to play: state-owned enterprises can be privatized, and infrastructure and services can be provided on a public-private partnership basis. This is a subject of ongoing dialogue and a point of focus in the region. Constraints to participation of private enterprise in this sector need to be removed through the creation of an enabling policy and legislative environment. Public-private partnering is an increasingly acceptable approach to leveraging finite public budgets and should be promoted.

Foreign investment has a key role to play in the private financing of infrastructure. South Africa, for example, has actively sought private financing for toll roads. The government is seeking foreign investment on a concessional basis for the Johannesburg-Durban tollway and the Maputo Corridor. South Africans have invested in port infrastructure in Mozambique, and several railways (i.e., Malawi) in the region are discussing possible privatizations which would involve foreign capital. Infrastructure development models which involve foreign private sector participation and expertise such as BOOT (Build-Own-Operate-Transfer) are becoming increasingly accepted in the SAR region. In support of this trend, multilateral institutions such as the Multilateral Investment Guarantee Agency (MIGA), a member of the World Bank Group, are providing useful risk insurance coverage to international investors in the infrastructure sector to encourage greater private sector participation in the operation, management and maintenance of infrastructure services.

5. Access Constraints: Information, Contacts and Networks

Field interviews and Focus Groups stressed access constraints. The interviews and Focus Groups mentioned insularity, poor linkages between small and large firms, inability for small business to access government contracts, need for improved export marketing, and lack of information. These problems were highlighted more frequently in the field than in the review of literature because they are practical problems felt by real business people. Generally, businesses feel isolated from knowledge of markets outside their immediate region. They are anxious to be exposed to better technologies and processes. They want a better understanding of the logistics involved in exporting and importing. They need business partners. And they would like to forge strategic networks with other businesses in the region and abroad.

Lack of access to information is felt acutely and is further limited by poor communications services. The need for better export marketing, better information, improved communications, and knowledge of quality standards, prices and potential buyers abroad were all mentioned in the field. Furthermore, the continued government monopoly in the telecommunications sector in many countries contributes significantly to the problem of poor access to telephones and the high cost and low quality of communications in general. Bilateral and multilateral donor agencies have begun initiatives to address these constraints. For example, both the World Bank and USAID have announced programs to try to link Africa to international sources of information via the World Wide Web. The Multilateral Investment Guarantee Agency (MIGA), a member of the World Bank Group, recently launched the IPA*net*, an on-line information network on investment opportunities in Africa designed to bridge the communications gap between national investment promotion agencies and potential foreign investors.

Lack of access to markets includes the lack of linkages between small business and government procurement, between small and large business, and between African business and international markets. Lack of access to particular national markets in the region is also a salient constraint to private sector growth. Small businesses complain about not knowing how to market to larger businesses and their national governments. Many complain about not being able to access the South African market, confirming the trade policy problem discussed earlier. In general, African businesses exhibit a great thirst for knowledge about international markets, products, prices and partners.

The lack of regional and international networks, associations and service providers is an important constraint. Business people want to be linked with partners and sources of information in the region and internationally but lack mechanisms to do so. This is partly explained by the relatively recent movement towards regional cooperation and commerce. The legacy of apartheid, sanctions, civil disruption and internally-geared economic policies have reinforced this isolation. While there is a West African Enterprise Network functioning in that region, no such initiative has yet been successful in the SADC region. Efforts in the past to create and finance an over-arching regional business association have been notably unsuccessful (and such top-down approaches should be viewed with caution). However, sectoral and industry associations are developing international linkages on the basis of real cross-border business that is beginning to emerge.

C. SPECIAL FOCUS: AFRICANIZATION OF THE PRIVATE SECTOR

Lack of Africanization also acts as a constraint on private sector development. Private sector development, as a popular cause, has often lacked legitimacy in African countries because the formal private sector does not resemble the majority of would-be beneficiaries. As a result, this lack of legitimacy acts as a brake on policies which would benefit private enterprise as these policies would be seen as benefiting groups which have often been a target of popular resentment (i.e., the experience of Asians in Tanzania, the Portuguese in Mozambique and Angola, and white farmers in Zimbabwe). On the other hand, the lack of indigenous entrepreneurs is a severe symptom of an underdeveloped private enterprise sector and has important causes which must be understood if they are to be corrected.

Causes of this problem include the historical legacies of apartheid, colonialism and socialism. The formal sector in many African countries usually includes foreign multinationals, state-owned enterprises and companies controlled by ethnic elites. In South Africa and Namibia, the legacy of apartheid concentrated most of the private sector in large white-owned firms. While this is an extreme case, the situation is not so different in other countries. In Tanzania, black entrepreneurship was discouraged just as effectively by policies of socialism including resettlement, village collectives in rural areas and state-owned enterprises in the cities. In Zambia, Angola, Mozambique and even Zimbabwe, the legacy of socialism also retarded the development of local African entrepreneurs. The legacy of colonialism led to a predominance of

Asians in Tanzanian commerce and a predominance of whites in Zimbabwean manufacturing. In Mozambique today, the largest private sector company is a Portuguese subsidiary. These historical forces shaped the situation in which African entrepreneurs were at an initial disadvantage, a disadvantage exacerbated by an emphasis on state ownership.

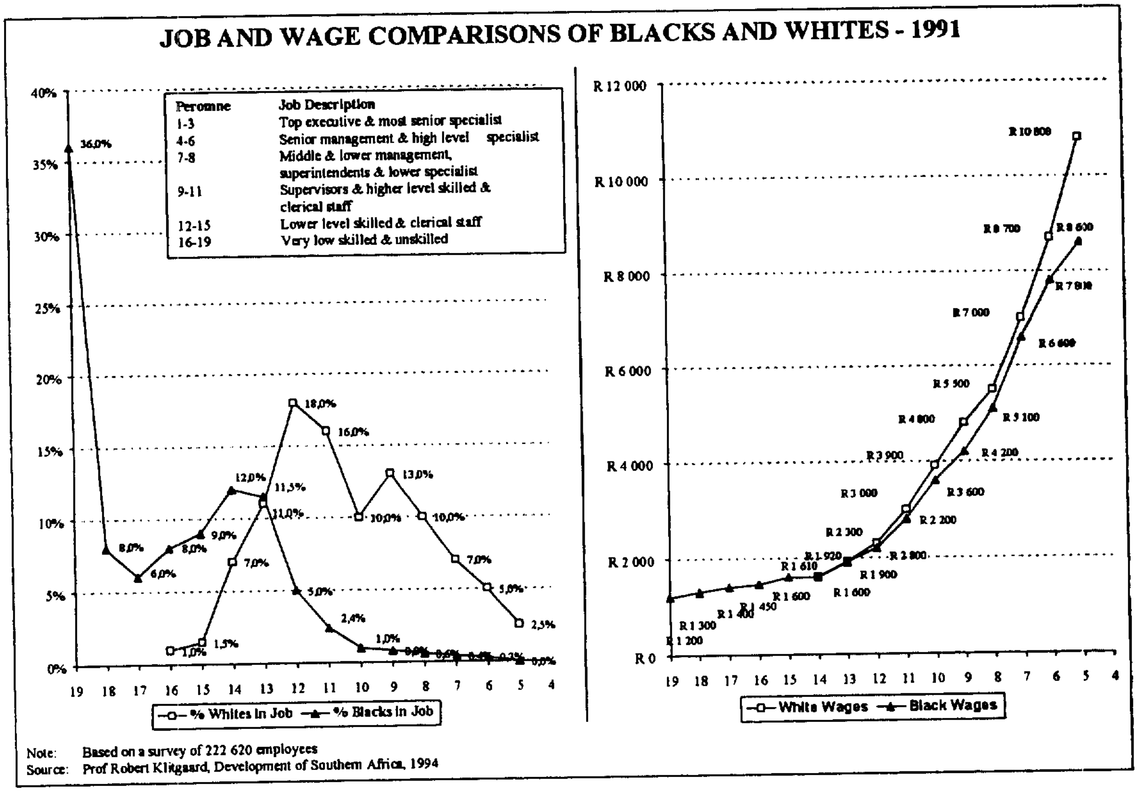
Barriers to entry impede Africanization of the economy. Interviews revealed that many governments, ironically, prevent entry by Africans into the economy as business owners even while posturing in favor of indigenization. For example, the Government of Zimbabwe has blocked one African telecommunications entrepreneur from competing with the state-owned monopoly. Many governments still have onerous licensing and taxation policies which stifle and discourage the transition from informal to formal sector business. In Malawi, for example, two firms account for a majority of the private sector GDP of the country and free competition has thus far not been encouraged.

The South Africa MAPS exercise focused on critical barriers to Africanization of the private sector. The USAID MAPS exercise, conducted in 1995, established benchmark data on black economic empowerment, presented an analysis of those sectors which could provide the most rapid expansion of Africanization, and presented alternatives for donors and stakeholders which could speed this process. This exercise was one important source of data and analysis for this private sector assessment. Similar benchmark data and study is needed for the other countries in the region, to quantify the anecdotal information available through focus groups, interviews and other sources.

The South Africa MAPS study revealed that in many sectors, business associations have invented restraint-of-trade mechanisms to limit new entrants. The South African government, ironically, has often colluded with such efforts as it is politically important for it to cooperate with powerful labor unions to preserve the interests of larger companies at the expense of smaller ones. For example, by protecting the unionized textile factories with high tariff barriers, the government prevents the emergence of thousands of potential entrepreneurs in labor-intensive and smaller scale cut-and-sew operations. Such operations were found by Monitor, a Boston-based consulting firm, to be globally competitive if they did not have to rely on higher cost, protected and domestically-produced cloth.

Africans are under-represented in the RSA formal private sector. Data show the ebony ceiling in employment and demonstrate that black participation falls off dramatically as jobs get better and at the entry point for whites in South Africa **(Table 7)**. However, when blacks do obtain better jobs, they tend to receive equal pay. This shows that the problem is one of access rather than one of equal pay for equal work.

Table 7 ***(South Africa only)*:**



<u>Black business ownership, when it does occur, tends to be concentrated in low value-added sectors</u> such as trade and personal and social services rather than the high value-added categories of manufacturing or business services. **Tables 8 and 9** present data for South Africa. The Focus Groups and Interviews indicate that a similar situation exists throughout the region.

Table 8 *(South Africa only)*:

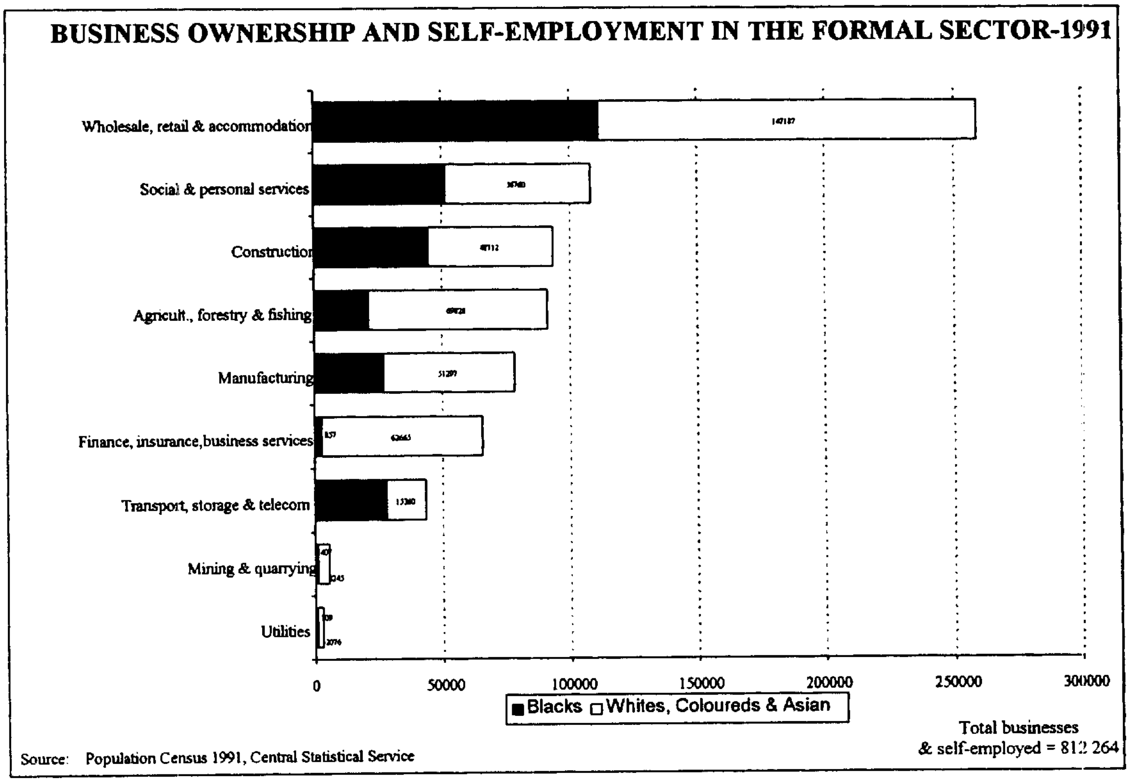
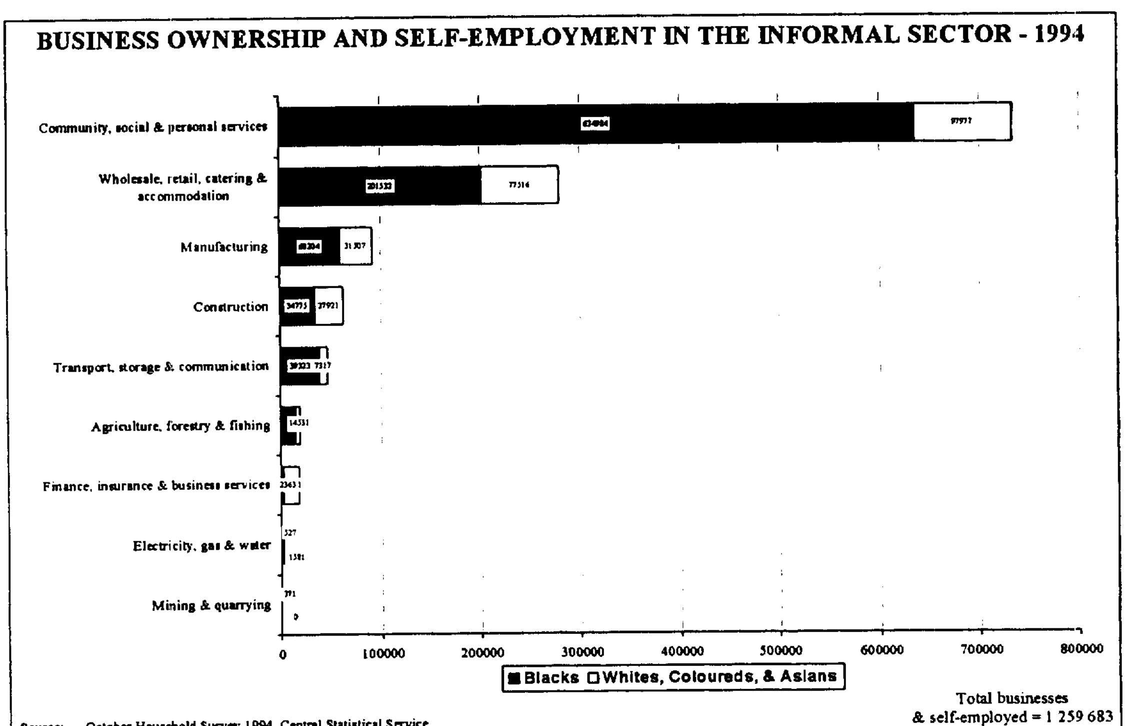


Table 9 *(South Africa Only)*:



While apartheid was an extreme case, most countries of the region were found to face a similar Africanization problem. Thus, the South Africa MAPS exercise has relevant implications for the region. The problem of under-representation of Africans as business owners in the formal private sector exists in most countries of the region. However, data on business ownership by ethnic background is hard to find in most countries. The South Africa MAPS exercise is generally regarded in that country as the most comprehensive benchmark exercise on black economic empowerment. As South Africa represents 75% of SAR GDP, the resolution of this problem in South Africa will indeed have broader implications for the region as a whole.

African entrepreneurs lack collateral. Southern African participants on the J.E. Austin team noted that as land is often held communally by Africans, there is a difficulty in providing collateral for loans and for starting or growing a business. This is especially true in rural areas.

Inappropriate education and curricula have also hindered the development of an indigenous private sector. The South Africa MAPS study demonstrated that higher education for blacks under apartheid had very little business content but stressed a role in services. The interviews and Focus Groups in the region confirmed that in most countries, civil service and government were, until recently, regarded as high-status occupations while business and entrepreneurship were not. As mentioned earlier, this is reflected in the content of the curriculum, which stresses basic language, math and social studies. Schools and curricula will have to change if the values of young people are to be directed towards a role in private enterprise in technical, managerial or entrepreneurial capacities. This anti-private sector bias is often subtle and appears in the kinds of role models which are presented to students or in attitudes by teachers and peers.

Constraints to private sector growth cannot be analyzed in the traditional way without taking into account the constraints to African business. The problem of African private sector development cannot ignore the challenge of stimulating a private sector which resembles the broader society. Therefore, the strategy must examine the impacts on the Africanization of the economy. As long as such Africanization does not occur, private enterprise will suffer from a lack of legitimacy which threatens to limit support from the public sector.

The Focus Groups revealed that lowering barriers to entry could have the single most powerful impact on indigenous business growth. This is more powerful than directed credit schemes channeled through venture capital funds. Six case studies done by JAA on disadvantaged businesses in South Africa provide lessons on the kind of support that could be most useful to African entrepreneurs (Black Enterprise and Entrepreneurship Support Project).

D. CONCLUSION

Multiple, cross-cutting analyses revealed that the critical constraints to private sector growth are poor governmental policies, inadequate education and training of human resources, an under-developed financial sector with inadequate mechanisms for serving SMEs, poor infrastructure with limited private sector input, and lack of access to information, contacts and networks. Furthermore, the lack of Africanization is both a constraint to the region's long-term private sector development and a result of government policies which kept entry barriers to the formal sector unnecessarily high.

Unfavorable government policy (i.e., policy which fails to provide an effective enabling environment for business growth) is the largest constraint to private sector development in the SAR region. The above analyses have provided multiple confirmations that poor policies are the single largest constraint to private sector development in the region. The region suffers from a "quality of investment" problem which more resources alone cannot solve. Of these policies, the most important are those related to trade, investment and the institutionalization of policy dialogue. Tax policy, banking policy and protection of private property are also important for private sector growth.

Financial sector constraints do not refer to an absolute shortage of capital but to a lack of efficient systems of intermediation which allocate resources to the best investments, and mechanisms to link formal financial institutions to small and medium enterprise. Common accounting standards, reporting requirements and listing procedures could all help stimulate capital markets on a regional basis and raise additional portfolio investment from abroad. There is a need to understand better how SMEs meet their financing needs and to encourage non-traditional financial intermediaries that can link SMEs to the formal credit system.

Human resource constraints are critical, yet educational budget allocations are not the central cause. Early school-leaving, high levels of illiteracy, inadequate curriculum and poor teacher-to-student ratios all contribute to this problem. Specialized technical and managerial skills are also lacking.

Continued public sector control of critical infrastructure continues to impede private sector growth, raising the cost of doing business and hurting the returns on investment. Mechanisms to increase the private sector's voice in planning infrastructure improvements are needed.

Access to information, contacts and networks is perceived as a constraint by southern Africans. No equivalent of the West African Enterprise Network currently serves southern Africa, and there is no effective private sector counter-weight to SADC.

In this section, the JAA team has presented the most salient constraints to private enterprise, documented the sources and evidence from which they were derived, and organized these into a conceptual framework to serve as a basis for development of strategy. Such a strategy must look not only at overcoming constraints but at the overall potential of the region.

II. POTENTIAL OF THE REGION

The following section discusses recent changes in the region which have significantly altered the prospects for private sector development, reviews the potential of various economic sectors, and looks at the potential growth targets for the region and how they can be achieved. This section concludes by reviewing what other donors have been doing to remove the constraints described in Section I.

A. TEN CHANGES IMPROVING PROSPECTS FOR PRIVATE SECTOR GROWTH

Recent events have transformed the landscape for private sector development in the SAR. As a result, historical data may not fully capture the current trajectory of the region. Some of the more salient changes include the following:

1. War and civil unrest have decreased dramatically. This removes one of the largest constraints to investment, a constraint that was often mentioned but that will not be analyzed in great detail in the context of this report. The independence of Namibia, peace in Mozambique, and progress towards peace in Angola have improved the investment climate dramatically.

2. Apartheid has formally ended. This has opened 75% of the region's economy to broader-based participation, while simultaneously ending sanctions. This creates new opportunities for foreign direct investment, foreign trade, and regional economic integration. This has also led to a gradual freeing of South African capital (and the technology and management that goes with it), which is now moving throughout the region and which can help to stimulate the private sectors in other SAR countries.

3. SADC has been broadened to include South Africa and now has a strong economic focus. This promotes region-wide integration in a number of important areas and may serve to stimulate cross-border investment and trade in areas as diverse as energy, environment, tourism and finance.

4. Governments are now open to market- and enterprise-driven economic growth strategies. The failure of socialist-run economies, the election of new governments in some SAR countries, donor encouragement, and simple common sense have all conspired to create a new openness to sound economic policy.

5. Continued liberalization of world trade through the latest GATT/WTO agreements offers the prospect of expanded access to world markets for competitive producers, including southern African producers - although this also presents important challenges.

6. The rise of international portfolio investment and emerging market funds provides new sources of potential capital. Local and regional companies that reach a threshold level of size

and sophistication can list themselves on the stock exchange or otherwise attract attention from one of a growing number of venture/equity/country funds.

7. Commodity prices seem to be on a rebound. Most commodities from the region have been on a downward spiral from the peaks in the early to mid-1980s. Gold, silver, platinum and copper; petroleum; and sugar, coffee and maize were in bear markets for much of the 1980s. In the early-to-mid 1990s, the bottom was reached and prices rebounded. While prices will continue to be volatile, growing demand from Asia and elsewhere should keep them relatively high over the medium to long-term.

8. The drought seems to be over. Lack of rain has a substantial effect on the regional economies, especially those based on agriculture. However, the recent drought seems to have ended and this should give a boost to GDP and investment in the short-term.

9. The trend towards democratization may also help spur private sector development by institutionalizing dialogue and giving the private sector a stronger voice in policy.

10. The Global Information Infrastructure (GII) and the Internet will help reduce isolation and remove barriers to SAR integration in the world economy. While Africa shows the lowest level of Internet connectivity, the World Bank and USAID Leland initiatives promise to provide this critical linkage.

Important challenges remain for the SAR to become a globally competitive region. The international environment is far more competitive today than 20 to 30 years ago when the Asian countries gained their export foothold in world markets. Developed countries are now less open to one-sided trade arrangements and insist on *quid pro quo*. The end of the Cold War and budget cutbacks mean less aid and a less generous attitude towards providing trade concessions. Although wars among nations and ideologies have lessened, there is a worrying trend toward ethnic violence. This has expressed itself close to SADC borders in Rwanda and Burundi. Ethnic tensions in South Africa, while limited, affect the overall environment for investment from abroad and cooperation from within. The AIDS epidemic is removing some of the most talented entrepreneurs from the scene, while putting strains on the social system. The sheer number of new entrants to the labor force, stemming from a high population growth rate, will also impose major challenges on SAR economies. Progress towards liberalization, trade reform and private enterprise is still hesitant. As illustrated during JAA's first presentation to USAID/RCSA, the SAR economy, when viewed as a region, is quite diversified. The region has much to offer and can be quite competitive based on the potential of its key productive sectors.

B. REVIEW OF KEY PRODUCTIVE SECTORS

The key productive outputs of the SAR region include agriculture, manufacturing, mining, energy, construction, tourism, commerce and professional and personal services. As private sector development can often best be achieved through and with sector associations and industry groupings, it is important to get a feel for which sectors offer the most potential.

1. Agriculture and Agribusiness

There is excellent potential for agribusiness and agricultural growth, and SAR is competitive in many areas. Our review revealed a number of excellent investment possibilities, such as: Namibian fisheries, Angolan and Tanzanian coffee, Mozambican cashews and prawns, and South African agro-industries.

Improvements in agriculture can help poorer income groups. Over 70% of the labor force in Malawi, Mozambique, Tanzania, Swaziland and Angola derive their livelihood from agriculture. Impacts that improve productivity and incomes in this sector can have a large human impact in these countries and a favorable impact on poorer income groups.

There is potential for building regional linkages. South Africa has some very powerful agro-industrial and supermarket retailing companies which can provide demand for regional production. Linking them to potential sources of new supply in other SAR countries could stimulate regional trade and investment. The perishable nature of agricultural products could lead to setting up satellite plants which process close to the production zones, which could stimulate less developed regions. Different climates allow for offsetting products—from temperate to tropical—which could be traded within the region, as well as exported. A regional approach also offers greater opportunity for specialization—some regions are better for tomatoes, others for wine. Regional quality standards could spur a market with appropriate critical mass. Bilateral agreements and business deals are already following this logic. For example, Swaziland is the major supplier of sugar and sweeteners for the South African soft drink industry.

Pest problems can best be controlled regionally as well. It is in the national self-interest to have regional pest control and disease control programs because investment by one country alone will not eliminate the problems. Regional initiatives could also include common standards and grades. This would facilitate greater cross-border trade and eventually even lead to regional branding and expanded export potential.

USAID has significant experience in this area as a catalyst and facilitator. Activities in missions such as Mozambique place great stress on this sector and could benefit from an approach which encourages regional integration. Such initiatives should be led by the private sector, but can be donor-stimulated. The U.S. Department of Agriculture Cooperators Program is an excellent model for such assistance. Connections with major US agribusiness companies could also speed a transfer of technology while enhancing commercial and investment ties with the US.

2. Manufacturing

The region has a relatively strong manufacturing base, but most of it is located in South Africa, which represents about 75% of the SAR GDP. However, manufacturing as a percent of GDP is actually higher in Swaziland and Zimbabwe. The South Africa MAPS study highlighted competitive industries within the manufacturing sector which had the potential for expanding jobs and business opportunities for Africans.

South Africa's neighbors are upset at the influx of RSA manufactured goods. Liberalization is leading to de-industrialization in Zambia and elsewhere. There is a sense of desperation that this will not be replaced by a sound manufacturing base. Such a fear is exacerbated by the fact that many neighboring countries cannot export their products to South Africa. Indeed, at the time of this study, South Africa still subsidized its exports to other countries while keeping its own barriers high. Once again, policy is the key factor for expansion of a competitive manufacturing sector which could hold potential for providing some of the growth and jobs needed in the region.

Manufacturing can generate a large number of jobs for new entrants with few skills, but government policies have not always been helpful. In the textile sector, the RSA government hurts the chances for massive job creation for relatively unskilled cut-and-sew workers by protecting a smaller number of unionized jobs in fabric manufacturing companies. Meanwhile, Mauritius generated many jobs by establishing an export processing zone. Angola may have the potential to establish some manufacturing industries on the basis of its oil industry.

Current thinking on industrial development is being led by the Government of South Africa which is seeking a SADC sponsorship for its Regional Industrial Location Strategy Study (RILS). This regional competitiveness study seeks to identify regional linkages which might exist among South African firms and their regional counterparts. However, this is a government-sponsored study. USAID could assist by providing analytical capability and a forum for generating a private sector response to RILS.

Manufacturers' associations and other sector groups could serve as information clearinghouses and match-makers to identify opportunities. Manufacturing associations, at a regional level, could help develop regional standards and promote trade and investment within industries. A cooperators program geared to the needs of industry sectors could be designed to support this activity.

3. Mining

Mining has been a major economic driving force. Examples of regional mining impact include the role of diamonds in Botswana, copper in Zambia and gold in South Africa. While mining contributed to the economic dynamism of the region in earlier periods, prices slumped for most of these commodities in the 1980s. Poor parastatal management in Zambia also contributed to a major decline in output and revenues.

Investment is concentrated in few hands. The role of large companies is well-known, but governments have tried to promote artisans working with gemstones and precious metals. The South African government has promoted schemes to sell these directly to tourists. These efforts to add value and train artisans have, however, had very limited success.

There is increasing regional activity in mining. South African companies have been involved in Botswana for a long time. Anglo-American and DeBeers are now involved in the privatization efforts of Zambia. The scope for regional activity is increasing as South African companies look to diversify through international investment.

The mining industry seems able to meet its own needs. The United States has expertise in technology, training, worker safety and environmental protection. However, the mining sector should not be a priority sector for USAID involvement. The industry has its own resources and companies seem to have a good understanding of their technologies and markets. For example, few companies have managed a cartel as well as DeBeers in the diamond industry.

4. Energy (See Infrastructure Section in Constraints Analysis)

Angola has become an important supplier of oil to the United States. Furthermore, Angola was the largest recipient of net foreign investment during the sanctions period. The prospects for energy-driven growth have also motivated South Africans to begin investing in Angola despite continued civil unrest and a poor policy environment.

Energy projects could stimulate cross-border economic activity. Sources of hydro-electric and other energy supplies are located in some countries while demand exists in others. There is an important regional dimension to such projects and a regional power grid and network will be developed.

Shortages of energy affect small and emerging business disproportionately. Interruptions in the supply of energy impose a severe cost to the private sector, especially to smaller companies. Production is lost, time is spent unproductively, and investment in backup systems is costly.

5. Tourism

The southern Africa region has great potential for tourism. The natural beauty, fishing, wildlife, climate, and linguistic or cultural affinity with English, Dutch, German, and even Asian visitors provide the region with great potential. Tourism-related industries are coming close to generating 10% of world GDP, but, for example, currently only generate about 3% of RSA GDP. There is room to grow. Tourism is already a leading foreign exchange earner in Tanzania.

Tourism offers great potential for job creation, even for relatively unskilled workers. The tourism sector creates jobs at many different levels - from maids and janitors to highly trained artists and managers.

South Africa can help spur regional tourism growth. The time and expense of travel to South Africa from Europe, North America and Asia means that the average tourist stays for a longer period of time and can be enticed into additional side-visits and tours. There has already been some regional coordination, such as tours which combine a visit to South Africa with a visit to Victoria Falls in Zimbabwe. More could be done. Also, the South Africa tourism industry could help in many ways through direct investment, regional training, logistics, customer service, marketing and financial management.

Regional tourism sector associations could be supported. The eco-tourism potential of countries of the region could be added to South African tour packages. One could help to set standards so that tourists considering travel to the region would know what to expect. The region as a whole could be a hub for attracting tourists.

Working with a small but critical mass of owners and investors could also achieve results. One observer suggests: "Don't start just with the associations, these are managed by professional administrators and often have been created by the public sector or have heavy public sector involvement. An approach must be innovative. Don't start with mass conferences, but rather, with key people who are able to invest and make things happen."

Start with a simple pilot and learn from the recent USAID experience in Ghana. Rather than an ambitious scheme, one could simply assist a local group with a promising pilot, such as a visit to Cape Town followed by a trip to Victoria Falls in Zimbabwe and ending with the full African cultural and historical experience in the old city of Zanzibar. Europe and the Caribbean have been successful in combining stops in 3 to 4 countries. USAID has a recent successful project experience in providing a multi-faceted tourism package in Ghana that combines visits to castles, museums on the slave trade, safaris and beaches.

6. Construction

The construction sector generates employment. There has been pent-up demand in many countries and construction is now growing. Construction activity is labor-intensive, making it attractive in terms of job creation. In addition, the barriers to entry for African businesses are lower than in many other sectors.

Innovative approaches to low-cost housing are needed. There are good regional innovations which could lower costs considerably for low-income housing. Hydraform, a South African company, has come up with a way to reduce the cost of manufacturing cement block by 30% and is now marketing this innovation internationally.

There are regional opportunities for developing pre-fabricated low cost housing. A regional market could provide larger economies of scale for private sector production of modular and lower cost housing.

There is an interest in forming regional bidding consortia. Some companies in the region indicated interest in bidding against non-regional companies on international contracts, but they need to form consortia to gain the size and capabilities to bid effectively. Such strategic joint ventures can help African-owned companies gain the access to capital, technology and market skills needed to participate in international contracts.

Housing ownership also promotes other private sector objectives. Home-owners have instant collateral with which to operate a business. They also have a premises which can serve as a business site in many cases.

7. Commerce and Services

The South Africa MAPS study showed that there were lower barriers to entry for African firms in commerce and personal services. However, professional services provide more value-added. The service industry includes wholesale and retail trade, personal services and business services. These sectors are less subject to competition, serving a local clientele. African businesses in South Africa were largely found in commerce and personal services. However, business services, such as architecture, engineering, accounting, law, consulting, computer and software services offer higher value-added and greater opportunity for higher income. Data were not available to analyze African involvement in these higher value service sectors in other SAR countries.

Expansion of business services provide a double benefit for private sector development. It not only creates opportunities for new entrepreneurs, but can improve the overall enabling environment for the private sector by helping other businesses become more productive. For example, the computer industry not only creates jobs but helps make people in other jobs more productive.

The information sector is becoming a critical sector which could affect the business prospects for many other sectors. Just as the energy sector affects all manufacturing firms, so, too, the computer and communications sector now has the potential to affect the prospects for all businesses.

8. USAID Approaches to SAR Sector Potential

USAID cannot have a project for each sector, but policy reform and business development can often best be pursued on a sector basis through umbrella projects which provide flexible, market-driven responses that leverage sector resources. Sector associations know best how to articulate their needs to government and to promote growth within their industries. In the SAR region, they are still relatively weak and poorly linked at a regional level. One USAID approach would be to provide matching funding for local southern African initiatives by such industry and sector associations. Criteria for funding and technical assistance would include potential for generating significant new cross-border trade and investment, the demonstrated ability to manage funds, the ability to mobilize some matching funds, and the presentation of a sound strategic plan. The impact on small business, women-owned business, and African-owned business could also be considered in selecting these initiatives. While such an approach could be open to most sectors, special attention might be given to agriculture, tourism and commerce which could have the most impact for quickly expanding jobs and regional trade.

C. POTENTIAL OF THE REGION VS. RECENT RESULTS

The economic potential of a region, under excellent macroeconomic, private sector and human resource policy environments, can be determined by examining the real performance of countries which had such environments. The Growth with Equity Model presented in Annex III-A illustrates the kind of performance which is achievable when the policy environment is right. Table 10 below presents such potential performance and the recent results of SAR countries.

Table 10:

EAST ASIA VS. SAR: SELECT INDICATORS
(1980-1993/4 average)

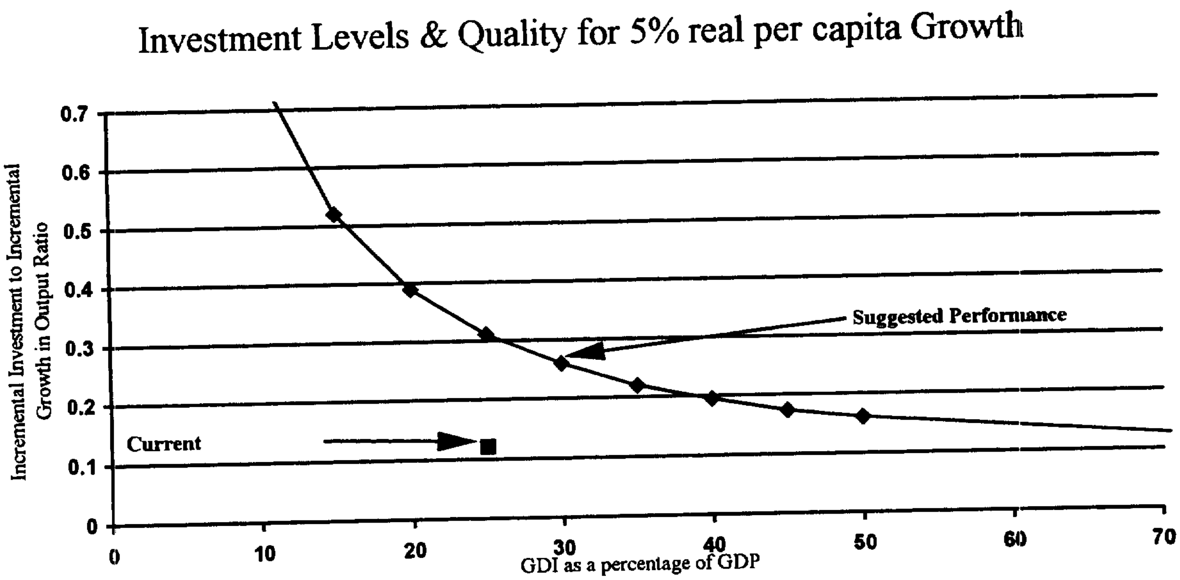
	Potential	Recent Performance
Real Growth Rate	7.8%	3.17
Real Per-Capita Growth	5.0%	.25
Investment as % GDP	30%	26%
Private Investment %	15-20%	8-14%
Incremental Investment to Incremental GDP Output	**.25**	**.12**

Source: World Development Report 1995; World Tables 1995; JAA.
Official private investment figures often include parastatal investment.

The countries of the region should develop aggressive strategies to achieve 5% real per capita growth over the next decade. To achieve a this level of growth, the region would have to achieve nearly 8% real growth in GDP. Population growth averages 2.7% in the region (1995 figures) which means that only real GDP growth above the 2.7% level will result in rising incomes per capita. A 5% real per capita growth rate, considered excellent in most SAR countries compared to recent performance, would result in less than a 2.25% real per capita increase in income.

A 5% real per capita growth rate will require a modest increase in the level of investment, a vast improvement in the quality of investment, attention to improving the productivity of human resources, and improvements in productivity which can come through greater openness to market forces. Table 11 below is a chart of the potential change in investment levels and productivity which could lead to 7.8% real growth in the SAR (5% real per capita growth). The most realistic scenario for achieving this rate of growth would be a slight increase in gross domestic investment (GDI) to 31% with a marked improvement in the quality and productivity of investment from a ratio of .12 to the .25 level which currently prevails in the high growth countries of Asia. As the graph shows, the 7.8% target is simply not achievable at the present ratio of investment to output, as the .12 ratio requires levels of investment far greater than are attainable. Without any improvement in the level of investment, one would have to achieve a ratio of investment to output of approximately .30, which is greater than that achieved in the selected Asian countries. Therefore, the best strategy would be to seek slightly higher investment levels while making such investment more efficient through an improved policy enabling environment.

Table 11:



Source: JAA analysis.

D. CRITICAL REQUIREMENTS TO ACHIEVE POTENTIAL GROWTH

In order for a 5% real per capita annual growth rate *potential* to become reality in SAR countries, the GEM analysis highlighted three critical variables: 1) gross domestic investment, particularly private sector investment; 2) human capital, and 3) productivity growth.

1. Investment

The SAR region has invested over 30% of GDP in three of the last five years, showing that such a level is attainable. However, the quality and productivity of that investment must be boosted substantially. The Incremental Investment to Incremental GDP Output Ratio devised by J.E. Austin Associates revealed that 100 units of incremental investment in Asian countries over a 20-year period produced 25 units of incremental GDP output, versus only 12 units of incremental GDP output in SAR countries over the same period. This is partly explained by the fact that investment in many SAR countries is largely public-sector driven.

However, the private sector component of GDI must grow by about 5% of GDP. Private investment in East Asia over a 20-year period was 15-20% of GDP on average, but accounted for only 10% of GDP on average in SAR countries. Reliable targeting is made difficult because World Bank data on private investment often includes investment in state owned enterprises and there is no standardized reporting. Nevertheless, it is certain that more private investment is required.

The quality of investment is largely a function of market-oriented government policies which promote an open economic environment. The maintenance of macroeconomic stability, prudent public spending policies, and the liberalization of trade and investment regimes will induce higher private savings by engendering confidence in the economy. Recent policy changes in the SAR region should help to improve quality of investment indicators, although greater liberalization is necessary.

2. Human Resources

Part of the growth objective could be met by simply generating productive employment for those currently unemployed. If a country has 3% annual growth in population and labor force, and these people get average jobs, this could add 3% a year to GDP. This requires not only investment promotion but a simultaneous focus on making human resources more productive.

SAR and East Asian countries spend roughly similar amounts of GDP on education and roughly similar amounts of total educational expenditure on basic versus higher education. However, SAR countries lag behind their Asian counterparts in two key areas: 1) the quality of education as measured by the student/teacher ratio; and 2) the average age of school-leaving.

The student to teacher ratio must be reduced from 42:1 to below 30:1. School completion rates must become an important focus of education policy. A much lower percentage of SAR students continue to the 4th grade level compared to their East Asian counterparts (77% versus 100%). The discrepancy is even worse at higher grade levels. This leaves them ill-equipped to make productive contributions to economic growth.

Government policies which improve the quality and effectiveness of educational expenditure will help alleviate the human resources constraint in the SAR. These policies include the promotion of apprenticeships, greater emphasis on technical and managerial skills training, a refocusing of educational curricula towards private sector needs, and programs which help students (especially female students) to stay in school by assisting economically disadvantaged families.

3. Productivity Growth

Certain types of productivity growth are not explained by either increased levels of investment or human resources. The HPEs were also able to improve their "total factor productivity," which refers to this type of productivity increase. To get this kind of additional productivity, one must improve certain intangible factors such as economic organization, innovation, absorption of technology, and dynamic synergies that link business strategy, technology, finance and organization.

Total factor productivity seems to be highly correlated with the openness of an economy. Such openness to market forces is not prominent in the SAR, and would seem necessary for improvements in overall productivity.

E. DONOR INITIATIVES CURRENTLY UNDERWAY IN THE REGION

Some of these critical requirements have long been part of the foreign aid donor agenda, so the J.E. Austin team researched the efforts of other donor agencies in the region. Given the investment, human capital, productivity and overall macroeconomic policy constraints to growth in the SAR region, multilateral agencies such as the World Bank and the European Union have responded with various forms of assistance on both country-specific and regional levels. These initiatives not only provide a window on under-assisted areas in which USAID activity could prove useful, but they also offer an opportunity for USAID to leverage its resources and pool its expertise in joint assistance programs.

1. World Bank (IBRD and IDA)

The World Bank is the most active donor agency in the SADC region in terms of total lending. In 1994 and 1995 combined, total World Bank lending to the region in the five key constraint areas of policy, financial sector, human resources, access to information and infrastructure amounted to over US$1.1 billion.

Human resources and infrastructure constitute the largest areas of current World Bank lending to SADC countries. Over the last two years, the World Bank has approved over $600 million in infrastructure projects and over $120 million in human resource-related projects in SADC countries (World Bank Annual Report 1994 and 1995). Furthermore, infrastructure and human resource-related projects with a projected total cost of over $2.7 billion and $750 million, respectively, are in the current pipeline for fiscal year 1996 (World Bank 1996 Projects Catalog). **Table 12** summarizes current World Bank projects in the SAR by constraint addressed; **Exhibit 21** lists the projects summarized in the table.

Table 12:

Country	Policy (Trade, Investment)	Financial Sector	Human Resources	Physical Infrastructure	Access to Information, Contacts	Small and Disadvantaged Enterprise
Angola			x	x		
Botswana						
Lesotho	x		x	x		
Malawi		x	x	x		x
Mozambique	x	x		x		x
Namibia						
South Africa						
Swaziland				x		
Tanzania			x	x		
Zambia	x	x	x	x		x
Zimbabwe	x			x		x

Sources: World Bank Annual Report 1994; World Bank Annual Report 1995; World Bank Public Information Center, 1996 Projects Catalog.

2. European Union

European Union activity in southern Africa is undertaken in the context of the Lomé Convention. Since 1975, over 360 million ECU has been allocated in four Lomé disbursements. In addition, the Cross-Border Initiative (CBI) designed to facilitate intra-regional trade and investment currently receives 80 million ECU in financial support. **Table 13** on the following page depicts total European Union commitments (in millions of ECU) to the region in all sectors (except CBI) over a twenty-year period.

Table 13:

EC COMMITMENTS TO SOUTHERN AFRICA: 1975-1995				
	Lomé I (1975-80)	**Lomé II (1981-85)**	**Lomé III (1986-90)**	**Lomé IV (1991-95)**
Total Allocation	30	70	141	121
Infrastructure:	20	23.1	91	60
Railways	10	10.5	19	
Roads	10	10.5	24	45
Ports			48	
Airports		2.1		5
Other				10
Human Resources	8.8	13.8	14	21
Food, Agriculture, Natural Resources	0.8	23	27	18
Energy, Industry and Mines		1.8	5.5	12.5
Technical Assistance		3.9	1.5	7.1
Other		2.2	2	2.4

Source: Southern Africa and the European Union, European Commission, July 1994.

3. Other Notable Efforts

The UNDP, which has historically worked more closely with the public sector, recently commissioned a Private Sector Guide which was distributed to all resident representatives as part of a larger strategy to promote private sector-led growth. The UNDP is still struggling with its approach but has hired a number of private-sector specialists at the country level. The UNDP still suffers from a civil service mentality and cumbersome bureaucratic processes. As repeated requests for information were not answered, the JAA team visited UNDP offices in New York and Johannesburg.

Many bilateral donors have country-level SME and other private sector development projects. The team found no other major bilateral programs at the regional level making a major private sector development intervention.

III. USAID RCSA STRATEGY

A. CONSTRAINTS AMENABLE TO A REGIONAL SOLUTION

After identifying the key constraints to private sector development, and after looking at the changing environment and emerging possibilities for private sector development in the region, the team proceeded to analyze the extent to which the constraints lend themselves to regional solutions. This analysis is presented below:

Resolution of the policy constraints can be facilitated regionally. Economic and private sector policies are determined by sovereign countries at the national level. However, they can be facilitated at the regional level.

Trade policy, by nature, usually requires a regional approach. Countries are not normally willing to unilaterally reduce trade barriers, although in some cases they may decide to or be forced to do so. Zambia, for example, accepted unilateral reductions at IMF insistence. However, trade negotiations normally involve cross-border agreements.

A regional approach on investment policy can also facilitate reform. Cross-border investment agreements, common policies and other mechanisms can increase the flow of investment in and to the region. One can also conceive of marketing the region as an investment destination. The World Bank's Foreign Investment Advisory Service (FIAS) has been active in this regard.

A regional and institutionalized approach to private-public dialogue is needed as a counterweight to the public sector SADC. While institutionalized dialogue is normally considered a national matter, there is a real vacuum at the regional level. While the inter-governmental bodies of SADC have been established, there is no effective private sector counterpart for most of these. One can also conceive of the need to provide regional level networking, backstopping, technical assistance and support to advocacy and policy reform groups operating in the region.

The financial constraint is partially amenable to regional solutions. The harmonization of accounting standards, reporting requirements, stock exchange listing procedures and other measures could help broaden and deepen financial markets. On the other hand, the need to develop mechanisms of intermediation between banks and small business is harder to address regionally. Projects could provide regional training, technical assistance, and identification and dissemination of best practices. Other initiatives could provide for a regional re-insurance scheme. But this seems to be stretching the matter to fit a regional approach. It is not clear that micro-enterprise promotion and small business credit schemes are best addressed regionally. There may be a limited role, but these areas are usually better handled at the local and national level. The SAEDF is a regional venture capital fund and its regionality may help it to achieve a sustainable scale. Surely, legal, policy and organizational issues will be triggered in the process of providing a regional coverage.

The human resources constraint is only minimally addressed through a regional program. National education programs, locally-driven specialization programs and other interventions are best conducted at the national and local level. Only in very specialized cases would it be cost-effective to fly people to a regional center for special training. While there could be some regional sharing of resources and some regional interaction on matters of basic education, curriculum reform, use of CD-ROM and Internet resources, and entrepreneurial training, this area lends itself less to a regional solution.

The infrastructure constraints are amenable to and sometimes even require a regional solution. There are many cross-border aspects to infrastructure. Energy supply may be abundant in one country, but severely lacking in another. Water resources are scarce and could provoke regional tensions - and availability could be addressed on a regional basis. The problems facing road and rail transport require cross-border solutions as well. The strategy of developing corridors is inherently regional in nature and forms perhaps the most central piece of the region's current infrastructure development initiative.

Access to information, contacts and networks also lends itself to a regional solution. The need for regional sharing of information, access to markets, identification of joint venture partners and networking have been amply demonstrated in the constraints analysis.

Expanding African involvement in the economy and dealing with the needs of small and otherwise disadvantaged enterprise can best be addressed through a regional removal of the above constraints. While there can be some sharing of approaches on a regional basis, this is a difficult challenge to address directly in a regional context. However, some of the initiatives mentioned above can have an impact in this area by lowering barriers to entry and by resolving bottlenecks that have disproportionate and negative impacts upon small and disadvantaged business. The SAEDF is a regional approach to venture capital funding of disadvantaged firms. Promoting networks among black firms can also fit in a regional approach.

B. CONSTRAINTS APPROPRIATE FOR RCSA PRIVATE SECTOR STRATEGY

USAID strategy must look at appropriateness to U.S. objectives, scale of funding, historical expertise and current administrative capacity. The strategy and options must promote USAID stated goals, be consistent with the likely scale of funding, reflect USAID and U.S. expertise, and should be chosen in light of a realistic assessment of the administrative capacity of RCSA. They should also not replicate already existing initiatives, but should dovetail with other donor activities and provide appropriate regional support to other USAID initiatives.

USAID should play a secondary role in policy reform by helping to institutionalize and strengthen the private sector voice. The World Bank and IMF are playing the lead role in macro-economic policy reform. USAID can play a supporting role by helping to empower the local private sector and encourage NGOs to contribute to this process. USAID has considerable experience in this area, which also dovetails with the concern for building a civil society. However, groups must be chosen carefully. Private sector policy advocacy is not, per se, a good thing. Many business associations lobby heavily for the status quo to protect the interests of their members rather than the broader interests of the consumer or the overall goal of rapid economic growth. Because of the sensitive nature of many of these policy reforms, they must come from the legitimate southern African leadership, even if such leadership receives funding and assistance to "level the playing field" versus protect entrenched interests.

USAID has considerable expertise in the financial sector. USAID has helped to create a number of venture funds. U.S. companies have taken the lead in setting up emerging market growth and country funds. Financial sector reform projects have been implemented in many countries with USAID assistance. However, this does not mean that USAID should necessarily supply the capital, as the scale of the need is beyond the scope of the budget. Furthermore, there are adequate resources in the region and among international investors.

Human resource projects may best be handled outside the realm of the private sector. The need for basic education should be handled in the context of another USAID/RCSA area. However, there could be a training component to private sector initiatives such as curriculum reform, entrepreneurial training and business exchanges.

USAID does not have the resources to play a major role in infrastructure, but can play a role in promoting stronger private sector participation in the planning and delivery of infrastructure. USAID should stay away from half-measures, such as trying to improve the management of poorly-run state enterprises such as TAZARA. Rather, it should focus on institutionalizing a stronger role for the private sector in articulating its needs, evaluating projects and delivering results.

USAID has considerable and positive experience in promoting access to information, contacts and networking. The West African Enterprise Network and the African Business Roundtable are two regional examples. USAID has also supported national efforts to assist delivery of such access by local groups which can now be linked regionally.

USAID also has considerable experience dealing with micro, small and disadvantaged business. The U.S. pioneered various approaches to micro and small business. By lowering the barriers to entry through policy reform and by enhancing access to networks and information, USAID could play an effective role in an area in which it has expertise.

C. EVALUATING RETURN ON USAID INVESTMENT

The biggest payoff of USAID involvement will come with policy reform and through an institutionalized role for private and NGO participants. This is not something that happens automatically after reforms are adopted. Rather, it requires careful and often painstaking efforts—efforts which are currently being pioneered by many southern African organizations and individuals, many of whom are featured in the Annexes. These persons and groups deserve and need support, but must be carefully selected. However, the initial investment by USAID in their efforts could yield ongoing and sustainable returns.

Linking the region to the Internet and World Wide Web also could provide a large return. The World Bank and the USAID Leland Initiative will deal with connectivity and policy. However, there is a great need to provide a local and regional interface to empower local groups to make use of the new access with developmental applications to serve their constituents. There will be a great void which can be filled by initial training, networking and exposure to existing and potential applications. In addition, there will be a great need for technical assistance. The returns for eliminating communications barriers through this new technology are not immediately predictable but could be massive.

Improvement of the educational curriculum and practices could produce a profound impact. Direct investment in education will not solve the problem. However, policy support, curriculum reform and involving the local private sector in educational development could be extremely useful interventions which could change the dismal return currently being seen for the investment in education in the region. Linking the region to the Internet (mentioned above) also has profound and powerful implications for transforming the educational system at large.

Returns on the SAEDF and accompanying technical assistance project may be modest and should be monitored. USAID venture capital funds have not enjoyed notable and unquestioned success, according to at least one recent study. Direct funding, even when leveraged, has a finite potential impact even if the fund is continually re-capitalized through re-flows from well-managed investments. Nonetheless, the initiative may serve as a lightning rod for other efforts of this nature and is a visible demonstration of the political commitment of USAID to help African entrepreneurs.

Improving savings mobilization and supporting linkages between the formal financial system and small business can provide a higher return than providing direct capital. The leverage USAID receives from transforming a financial system so that it mobilizes more savings, allocates them efficiently to the best investments, and provides mechanisms for providing access to small business is relatively large compared to what can be expected from the direct provision of capital to firms.

Similarly, USAID return in the area of infrastructure should come not from direct investment or even direct technical assistance but from institutionalizing a capacity in the regional private sector to guide the process and help implement it. To improve the low return on public investment, private sector groups should be institutionally involved in the consultation process before costly investment corridor projects are planned by governments and financed by donors. USAID could play a creative role in facilitating this dialogue process.

The barriers to expansion of African-owned business are poorly understood, despite much discussion and rhetoric. Few bother to learn from the African enterpreneurs themselves. There are many top-down approaches. USAID could shed light on this issue by building upon initial efforts which have produced case studies which would indicate bottom-up approaches.

IV. PROGRAMMATIC DIRECTIONS AND OPTIONS

The following recommendations for programmatic direction were the result of extensive consultations and brainstorming with southern African leaders and have been designed to respond directly to the constraints identified above and to do so in ways that take into account a realistic appreciation of USAID budgetary resources and organizational capacity. These options are expanded upon and explored in greater detail below.

A. OPTIONS

Results Package #1: Policy: Regional Reform and Institutionalized Dialogue

Constraint: Poor Policy Environment

Results Package: Results include reformed policies and enhanced capabilities of local civil society organizations to effectively influence government policy. These will result in a much improved environment for private sector development, leading to improved levels and quality of private sector investment and subsequent private sector growth.

Concept: The preceding analysis has shown that poor government policy is the leading impediment to rapid and sustained private sector growth. Many of these policy bottlenecks, particularly in regard to trade, can be dealt with best in a regional context. The creation of inter-ministerial committees in SADC to coordinate policies and approaches to various regional problems creates an opportunity to design and implement regional solutions. However, there has been very limited private sector participation in the design and implementation of such policies. SADC as a political community preceded SADC as a commercial and economic reality; there is no effective and truly representative regional private sector organization able to articulate needs, assist in policy design, and help mobilize private sector participation. A number of emerging regional and cross-border groups do exist but they are quite weak. Regional linkages among such groups in different countries are also weak. This activity would strengthen the capacity of these groups while simultaneously providing important private sector input to the policy process.

Activities: These would include grants, technical assistance and training exchanges provided to private and public sector policy leaders through civil society institutions working on private sector policy reform. These would include business associations, consumer groups, universities, think-tanks and others. Training and exchange visits would also be funded that would allow joint private-public delegations to visit countries where well-designed and well-implemented policy reforms achieved their desired results.

These activities would concentrate on those policy issues which are regional in nature and where reforms could produce a substantial impact on private sector development. Trade-related policy issues will figure prominently. These include the harmonization of tariff schedules within the region and the resolution of numerous non-tariff and logistical barriers to regional trade. The activity would also help the private sector to articulate its needs and to provide input on infrastructure projects and the development corridors.

Civil society organizations would receive assistance at the outset in preparing initial proposals, conceptualizing their initiatives and launching dialogue initiatives. Special effort would be made in countries where capacity is weakest.

Implementation: There is no regional organization which can or should be the sole implementing agency. Rather, USAID would select an implementing contractor which would work with different organizations in each country. The participating organizations would enable the activity to be grounded in local participation in the absence of a regional implementing entity. If the activity is successful, then a regional organization may be formed at the initiative of the participants in this activity.

The contractor would field 3-4 international experts and would have a roster of about 15-20 regional policy experts and private sector specialists. Additional short-term technical assistance from outside the region would also be available. These specialists would assist the participating organizations in identifying the critical policy issues to be addressed. The technical assistance team would carry out, together with participants, any analytical work needed in order to design policy reforms. The participating organizations would then utilize this analytical work as the basis for presenting reforms to policy makers. Key government policy analysts and private sector leaders must be involved in this process and high level briefings of these leaders should be an integral part of the activity.

The long-term advisors would build on the work done in this private sector assessment in terms of identifying potential centers of policy expertise and key individuals. They would also network and work with the key people in government who would be designing and implementing various reforms and who participate on the SADC inter-ministerial committees.

The advisors would make stakeholders aware that the project would fund studies and initiatives designed to provide important private sector perspectives and analyses of key policy problems. USAID funding would provide umbrella grants to civil society organizations in the region that can help bring about stronger private sector participation through policy analysis and dialogue. The effectiveness of the groups would be re-evaluated over time as part of the disbursement process for additional grants.

The USAID-funded field team would be carefully selected. They should be highly experienced experts in policy development in diverse political and economic environments. They must be able to develop and maintain excellent personal relationships that will enable them to obtain the confidence of and work with public and private sector leaders. They must have solid grounding and training in policy, and have worked in situations where policy has been developed and implemented effectively through public- private sector dialogue.

One focus of this effort would be on easing the constraints to African business, especially those legal and regulatory issues which impede the development of new businesses. Being able to compare the ease of entry, licensing, tax and restraint-of-trade practices on a regional basis will enable the implementing organization and its participants to rectify these barriers and to champion the interests of small and disadvantaged business. The advisors would help to ensure that the interests of small business, women-owned business, and African businesses are adequately represented in the policy dialogue.

No one is filling this niche at the moment. The IMF, World Bank, the bilateral USAID missions and others are working on policy constraints through a variety of individual initiatives. Bilateral donors, including the Germans in South Africa, are providing technical assistance to various ministries. However, there is a need to launch an activity designed to strengthen the private sector capability to provide input on regional policy issues. This would also strengthen SADC by providing it with a stronger private sector counterpart.

Results Package #2: Facilitate Internet Connectivity/Improve Telecommunications: Regional Interface with Leland Initiative

Constraints: Infrastructure: State Control of Communications, Lack of Access.

Results Package: Improved access to markets, technologies, business partners, international technical assistance and communications media.

Concept: Within 10 years, the United States will have developed a national information infrastructure (NII) which will allow its citizens to have instantaneous and very low cost access to text, graphic, audio and video media and to be inter-linked with others around the globe and with commercial and other sources of data, information and services. A worldwide, global information infrastructure (GII) is also expanding rapidly.

The World Bank has recognized the revolutionary importance of these new technologies for development purposes in Africa, and already has learned much about the need for both African ownership of the project and business-like management of the network from the implementation of a pilot networking project in Mozambique. USAID, through the recently announced Leland Initiative, plans to link 20 African countries to the Internet. Building on-ramps to the "Information Superhighway" is not enough. A regional and local interface will be needed to take advantage of this infrastructure so as to maximize its impact. While the potential benefits are hard to predict, they could be enormous and would probably far exceed the initial cost. This project would respond squarely to the "access" constraint mentioned earlier and also provide a cost-effective way of helping to resolve at least one of the important infrastructure constraints. It dovetails nicely with other USAID activities and the work of other donors.

The advantage of the Internet infrastructure is that it permits the two-way flow of information. While one often thinks about publishing information useful to small and emerging businesses, the Internet's possibilities go much further. The businesses, with some assistance, will be able to announce their projects and services to a wide audience. The will be able to ask questions and get answers from fellow business operators as well as experts. For all this to happen, assistance in the form of specialists who can create the Web pages, fora, intra-nets, and new discussion groups pertinent to the issues of these groups will be needed.

From the private sector perspective, information technology could also play a key role in helping to facilitate access to regional and international trade opportunities, partnering, market information and technology. This means of communication could also put southern African producers in immediate contact with millions of potential buyers and consumers worldwide through the Internet. It could be used to market tourism products and services. The technology can also permit service professionals, including accountants, economists and consultants, to export their services from their home base.

The project would support Leland Initiative objectives by helping to ensure that Internet/World Wide Web lines out-of-country are not subject to current high long distance rates, circumventing telecommunications monopolies (where they continue to exist). It would also help get these capabilities out beyond the capital cities into the country and into the hands of civil society, NGOs and small businesses. The activity would engage local business associations as distribution channels for expanding access and applications.

Activities: The USAID project would begin where the Leland Initiative or World Bank leave off—after the basic hardware has been installed and the satellite communications have been made. The project would focus on helping to ensure the emergence of access providers. In the United States, such access providers offer both access and proprietary material (e.g. America On-Line) or just access (e.g. Netscape and countless local providers). In African countries, they often do not exist. An access provider must have a powerful computer and multiple telephone lines, so as to sell the service of connecting people to networks. There is also a significant need for the development of skills in creating applications such as Web pages, creating intra-nets and developing other materials.

Implementation: The project would finance 2-3 people for 2-3 years. These people would have to understand the Internet and how it works. They would have to know how to program in UNIX-based systems. They would also need to be familiar with Hypertext Markup Language (HTML -- the language used for the World Wide Web), Hypertext Transfer Protocol (HTTP), CGI scripting (the language that gives instructions to servers using UNIX operating systems) and other technical aspects of connecting computers to the Internet through wired and wireless telecommunications systems. The job of the experts would be to help diffuse the technology and applications with potential impact for development.

At least one of these experts would focus on spreading the use of this technology through small business support programs, trade associations, NGOs and universities. Assistance would be provided in helping various kinds of organizations get access to and use this technology. This should not be limited to business, but should be expanded to include the following:

- Health NGOs
- Educational and literacy organizations
- Democracy and governance NGOs

- Environmental groups
- Micro-enterprise support organizations
- Women's groups
- African business associations
- Human rights monitoring groups
- Policy advocacy and dialogue groups (see Option 1)

This project responds to the specific access constraint. It is regional in nature, providing crucial and immediate communication for the people of the region. It complements and builds on other USAID activities. It provides assistance in an area in which the United States has been the pioneer. It would also be one of the first initiatives of its kind at the regional level and, as such, would be creative and generate a fair amount of excitement and interest. Most importantly, it could have a very large impact while involving modest levels of resources and manageable administration.

Results Package #3: Enhance Regional Trade, Investment and Productivity of Small and Medium Business: Access and Networking

Constraints: Lack of Access to Information, Markets and Networks; Lack of Productivity of Investment; Lack of Rapid Accumulation of Human Capital.

Results Package: Increased growth in productivity, particularly among African small and medium enterprises doing business in more than one country; increased managerial and technical skills of managers in these companies.

Concept: While the policy initiative would help remove barriers to regional trade, investment and productivity, this initiative would help empower southern African businesses, and especially African and small businesses to formulate and implement practical initiatives which can, boost such regional trade, investment and growth. Modeled on the successful USDA Cooperators Program, the project would co-finance projects which: 1) enhance the productivity of the participating firms; 2) expand cross-border trade and investment; 3) are pioneered by the local leadership; and 4) account responsibly for the money. USAID would work through national sector associations (as no effective regional umbrella chamber currently exists) to identify and eliminate constraints to regional trade, investment and productivity of small and medium business in the region. Stakeholders would drive this activity and USAID would not be wedded to one implementing agent but would see the results of many such agents. This activity would leverage USAID funds with local counterpart funding in order to increase their impact.

Implementation: USAID would implement the project through a contractor who would make initial contacts with pertinent groups throughout the region. The contractor, with prior USAID agreement, would establish specific technical assistance and training elements for those organizations selected for participation. Cooperators would submit proposals for assistance through their local business organization. The proposals would then be evaluated for consistency with the objectives of the activity and for the ability of the organization to monitor the use of funds.

Some priority could be given to those sectors which were flagged as offering great potential in the sector-by-sector review presented above. Potential initiatives that were uncovered in our assessment include:

- Construction groups that want to form regional consortia bid on regional projects;
- Food processors who want to access raw materials in other SAR countries;
- Transport societies that want to end border delays;
- Wholesalers and retailers that want to lower trade barriers;
- Manufacturers that want to harmonize standards for the region;
- Agribusiness groups that want common grades/standards/contracts;
- Financial groups that support common reporting and listing requirements; and
- Regional tour operators wanting to develop multi-country tour offerings.

This activity, in addition to focusing on intra-regional trade, might also assist small and medium businesses to establish linkages outside the region. This might involve access to new markets and improved technology, the feasibility of higher value-added products, and connections to international buyers. In short, assistance would be provided in areas where the small and medium businesses require some technical assistance in order to meet the demands of new markets.

Results Package #4: Broaden and Deepen Regional Capital Markets and Link Them to SMEs

Constraint: Financial Sector: Lack of Access to Capital and Credit

Results Package: Financial sector is deepened to reach smaller businesses through broader use of non-traditional financial intermediaries who can get access to formal sector credit and then retail it to small business according to sound and self-sustainable commercial principles.

Concept: USAID would provide technical assistance for two major regional level interventions. First, it would help associations of accountants and relevant ministries to work on the standardization of accounting principles with an eye to establishing SAR equivalents of Generally Accepted Accounting Principles (GAAP) and perhaps even developing a regional Financial Accounting Standards Board (FASB) in order to facilitate cross-border investment, partnering and even eventual joint-listing on equity markets. USAID, as a neutral broker, could play a catalytic role in bringing stakeholders together. Accounting firms and South African commercial banks have a clear interest in regionalization and might even help co-finance this initiative. From there, USAID technical assistance would proceed to assist regional stakeholders in developing regional listing requirements and harmonized reporting.

The second part of the initiative would begin with an in-depth assessment of the non-traditional financial institutions in the region and current best practices for small business lending. This analysis would include in-depth case studies on African businesses and how they meet their needs for capital and credit. Based on the assessment, USAID would select 3-4 countries where non-traditional financial intermediaries should be strengthened and developed. These countries would probably not include South Africa, where such institutions already exist and have been well-documented. Countries where recent changes have promoted more small businesses (Tanzania, Mozambique and Zambia) would be likely candidates.

Implementation: Over the next 6 months, USAID would commission an in-depth assessment of non-traditional financial institutions, the credit and capital needs of small business, and the feasibility of meeting such needs through these institutions. USAID would also provide models of commercially successful institutions that serve this client base in ways that are financially self-sustainable. Larger banks would also be brought to the table to review this study and to play a role in helping the intermediary institutions and mechanisms develop. USAID would not provide a grant of direct funds, but would help encourage the start-up of such institutions through technical assistance and loans.

B. PROGRAMMATIC DIRECTIONS: PRIORITIES, SEQUENCING AND TIMING OF INTERVENTION

The following section presents recommendations for the priorities, timing and phasing of interventions.

1. Scenario Planning Exercise

USAID should proceed immediately, even before results packages have been designed, with a scenario planning exercise. Many of the southern African leaders who could contribute have been identified in this exercise. The case study exercises on African businesses could also be funded with existing training resources, if these are available.

The scenario planning exercise would have several benefits. First, it would be the mechanism by which the above projects are designed and led by southern Africans, an important aspect of the Regional Center strategy. It would also test the ideas presented here and would develop the results packages, activities, plans for implementation and terms of reference. Second, it would allow USAID to assemble a group of talented and forward-looking business leaders from the region who might become an eventual core for guiding the regional policy reform activity described above. The group might even coalesce into a network that could build a regional institutional voice to fill the current void. A third benefit of this exercise would be to help shape a forward-looking vision for the region and its potential, and to refine and diffuse this vision through the kind of extensive dialogue sessions which were undertaken during the South African scenario planning exercise. The activity was enthusiastically supported by the southern Africans who were consulted.

The scenario planning option would link progressive business leaders in the region on a temporary and ad hoc basis, offer technical and analytical support, empower them to move towards a regional reform agenda and provide some impetus for a private sector-led regional reform agenda. The output would be a coherent vision and set of policies for the region which would be vetted in dialogue sessions. The exercise would require a budget of $600,000 - $800,000 over the next 6-12 months.

2. Priorities

The scenario planning exercise would lead naturally into the regional policy reform activity which should be the first priority of the Private Sector Office. However, the USAID/RCSA should not be too quick to attach itself to one particular implementing agency, as was noted above. Effective regional policy organizations have yet to emerge and USAID can play a role in helping them to emerge, identifying the best ones, and then working with and through them.

After this, the Internet activity should be launched as the next major priority. Lane Smith, who is managing the Leland Initiative at USAID/Washington, told the study team that he sees an important potential complementary role for the field. The Leland Initiative will work on installing the basic infrastructure. It will encourage an appropriate policy framework. It will also encourage service providers. However, it will then need local and regional cooperation to ensure robust development applications and widespread diffusion.

The Regional Center, with its ability to work in many countries, will have a good window on the content side of Internet applications in different settings and could help identify, promote and diffuse such applications on a region-wide basis as they emerge. The Regional Center can also be a champion for using the Information Infrastructure to promote policy reform, small business development, financial sector deepening, regional networking, and other valid developmental purposes.

The third priority would then be the activity of enhancing small and medium enterprise productivity through improved access. The scenario planning activity will also help RCSA to become more familiar with those sector and business associations that would be effective collaborators with such an effort.

The financial sector/SME project would take last priority and would depend on the findings of the review of non-traditional financial institutions serving SMEs. It is still unclear whether this major area of need warrants a regional focus. Helping the financial sector move towards regional standards is also extremely useful but USAID may find that its support is not crucial to success or that budgets will not allow for an additional activity.

3. Human Resource Initiatives

Human resource initiatives are normally the responsibility of another office at USAID. However, the above projects would address the human resources constraint in various ways. The **Policy project**, as envisioned, would have a component which would train policy analysts while bringing them together for cross-fertilization of ideas and for learning from the experiences in different countries. The **Productivity project** for small and medium enterprise would also be able to respond to specific critical technical and entrepreneurial training needs. The **Internet project** would speed the transfer of critical technical skills.

<u>If the Private Sector Office has access to training resources from the broader Mission, the team would caution against traditional approaches in the regional context</u>. Entrepreneurial training has a limited return on investment and can probably best be handled through local or sector associations. It is also difficult to envision a regional business school in the SAR, such as those which worked well in Central America (INCAE) or East Asia (AIM). The region is too diverse and there are linguistic and cultural barriers which would create challenges for a regional school. Another training approach that has worked elsewhere is to send a critical mass of young emerging policy makers to graduate education at market-oriented schools which teach sound economic policy. In Indonesia, for example, such a group has become the technocratic core designing and implementing policy. This approach, however, is not recommended for USAID/RCSA because there are too many countries and there would not be an adequate budget.

<u>If resources are available, the first priority should be to help reform curricula in the region</u>. This would include the development of a number of in-depth case studies of real African businesses and the struggles they have faced. A notable effort in South Africa has begun to record the stories of "black business heroes" who succeeded even in the midst of the great adversity of apartheid and who can serve as role models today. Another example was the production of six case studies by the USAID-funded Black Enterprise and Entrepreneurship Support Project (BEES) in South Africa, which revealed the true constraints facing African business. These case studies called into question many of the assumptions on which current programs of assistance are based. They challenged old stereotypes and revealed potentially important new vehicles for strengthening the African business sector.

By collecting and developing such in-depth case studies, USAID would contribute to the learning process for its own interventions. It would be able to influence the approaches used by other donors, host governments and NGOs. It would contribute to the effective design and implementation of the other projects mentioned above.

These case studies would form part of a larger effort which would provide technical assistance to help reform the curriculum content at various levels of the regional educational systems. The materials would be used for multiple purposes to do the following:

- Train entrepreneurs;
- Train NGOs which help small business;

- Inform policy makers;
- Provide materials for secondary school curriculum;
- Supplement training at vocational schools; and
- Provide African case studies to business schools.

4. Africanization of the Private Sector

<u>Throughout this exercise the critical issues facing African entrepreneurs have been of vital concern, and these should be incorporated into the above initiatives</u> rather than trying to create some specially focused initiative. The interventions presented here would have a major impact on lowering the barriers to entry for African entrepreneurs, for strengthening and expanding their capabilities, and for providing regional linkages among them.

There is a lot of rhetoric about African business, but few efforts have been made to conduct in-depth, ground-up case studies to learn from the real situations and problems. When such efforts have been made, they have generated more effective approaches to reaching this sector, such as utilizing the existing networks of small bookkeepers to serve these businesses. The importance of apprenticeships as a means of entry to the formal sector was also revealed by case studies. The real impediments to African business are poorly understood and USAID could make a significant contribution here.

The entire program of activities presented above should be seen as leading to a democratized economy – an economy that resembles the majority of the people.

V. SUPPORTING EXHIBITS

Exhibit 1

Literature Review: Summary of Constraints Noted

Category of Constraint	Specific Constraint Noted
1. Policy Constraints	
i. Policy: Trade	Insufficient access to external markets (Botswana, Lesotho) Ideology of self-reliance, insularity (Tanzania, Zimbabwe) Import licensing restrictions (Angola, Zimbabwe) Cumbersome bureaucratic procedures and trade documentation requirements (Angola, Lesotho, Malawi, Mozambique, Tanzania, Zambia) Poor trading linkages between large and small businesses (Namibia, South Africa) Burdensome tax regime for imported goods (Mozambique) Absence of forward exchange cover mechanisms increases trade risk and uncertainty (Swaziland) High protective tariffs act as barrier to intra-regional trade and hinder long-run export competitiveness (South Africa)
ii. Policy: Investment	Availability of /difficulty of obtaining (internal and foreign) capital and credit (regional, Angola, Botswana, Malawi, Mozambique, Namibia, Swaziland, Tanzania, Zambia, Zimbabwe) Burdensome taxes on imported goods (Mozambique) Ineffective legislation to attract foreign investment (Mozambique, Swaziland) Exchange and interest rate fluctuations (Zambia) Uncertainties related to system of foreign exchange allocation (Zimbabwe) Unsustainable fiscal deficits (Zimbabwe) Investment controls (Zimbabwe) High/restrictive regulation of business/the economy; restrictive licensing requirements (Namibia, Zimbabwe) State permitted to forbid economic activities (Namibia)

iii. Policy: Process	Lack of government appreciation for the contribution of the private sector to the economy; hence, little attention given to private sector needs (Lesotho, Malawi) Lack of appropriate dialogue between government and private enterprise regarding trade constraints and opportunities (Namibia)
iv. Policy: Other	Poor performance of the civil service/inefficient bureaucracy (Lesotho, Swaziland, Mozambique, Tanzania) Parastatals are barriers to entry and block competition (Namibia) Extent of state involvement in the economy is too great, inefficient parastatals weaken the economy (Namibia, Swaziland)
2. Financial Sector	Availability of/difficulty of obtaining (internal and foreign) capital and credit (regional, Angola, Botswana, Malawi, Mozambique, Namibia, Swaziland, Tanzania, Zambia, Zimbabwe) High interest rates/cost of finance (Zambia) Exchange and interest rate fluctuations (Zambia) Flight of capital to South Africa (Lesotho) Land tenure: land cannot be used as collateral (Mozambique, Swaziland, Zimbabwe) Difficulty of obtaining foreign exchange; uncertainties related to system of foreign exchange (Mozambique, Zimbabwe)
3. Human Resources	Lack of skills/skilled manpower (Namibia, Swaziland, Zambia) Need for improved basic education, wider education, more appropriate curricula (Angola, Lesotho) Need for business and entrepreneurship training and development (Angola, Botswana, Mozambique, Tanzania, Zambia, Zimbabwe) Need for management and artisan training (Malawi, Tanzania, Zambia, Zimbabwe) Flight of labor to South Africa (Lesotho) Rapidly rising population (Lesotho) High unemployment (Lesotho) Lack of entrepreneurial culture (Malawi)

3. Human Resources (Continued)	Negative attitudes toward private employment (Tanzania) Labor market restrictions (Zimbabwe, South Africa)
4. Infrastructure	Damage due to war (Angola, Mozambique) Inadequate basic infrastructure (Botswana) Inadequate public services (Swaziland)
5. Access to Information, Contacts and Networking	Lack of information on trade/market opportunities in the region (Namibia, Tanzania, Zambia) Trade institutions lack informational resources necessary to promote and support local exporters (Zambia)
6. Special Focus: Small and Disadvantaged Enterprise	Limited and undiversified indigenous production base (Angola) Cumbersome regulation of private enterprise (Botswana, Namibia) Laws do not facilitate starting and operating a business (Angola, Mozambique) Informal sector is too large (Mozambique) Non-formal sector needs more linkages to formal business - e.g. as suppliers (Namibia) Dominance of, bias towards large business (Namibia, Tanzania) Poor trading linkages between large and small business sectors (Namibia) Unfair competition arising from liberalization (Zambia)

Exhibit 2

Literature Review: Summary of Constraints Noted

Constraints	Angola	Botswana	Lesotho	Malawi	Mozambique	Namibia	South Africa	Swaziland	Tanzania	Zambia	Zimbabwe
Policy: Trade	x	x	x	x	x	x	x	x	x	x	x
Policy: Investment	x	x		x	x	x		x	x	x	x
Policy: Process			x	x		x					
Policy: Other*			x		x	x		x	x		
Financial Sector	x	x	x	x	x	x		x	x	x	x
Human Resources**	x	x	x	x	x	x		x	x	x	x
Access to Information/Contacts						x			x	x	
Infrastructure	x	x			x			x			

Special Focus	Angola	Botswana	Lesotho	Malawi	Mozambique	Namibia	South Africa	Swaziland	Tanzania	Zambia	Zimbabwe
Africanization	x	x			x	x			x	x	

***Includes policies biased towards the parastatal sector, land tenure issues, restrictive labor policies.**

****Includes: 1) technical/business skills; and 2) labor productivity.**

NOTE: The above constraints were identified by the J.E. Austin Associates team through an extensive review of over 300 documents and studies on the southern Africa region. They do not constitute an exhaustive list of constraints to private sector growth in each country. Rather, they reflect the opinions of the academic/intellectual community and expert views on the subject to date. The Literature Review, as the first stage in our overall private sector assessment, served as a filter of ideas and perspectives which formed the basis for further analysis of constraints to private enterprise.

Exhibit 3

Tabulation of Named Constraints to Private Sector Development

Need for business/management training	58
High customs/tariff barriers (SACU)	25
Cultural and attitudinal issues	22
Over-dependence on RSA	21
Inadequate transport infrastructure (roads, ports, bridges, airports)	20
Need to attract foreign and local investment	17
Corruption	13
Lack of dialogue between public and private sectors	12
Lack of access to information	12
Need to resolve land title/tenure issues	11
Need for artisan training	10
Political risk and instability	10
Lack of will and/or initiative	10
General infrastructure (power, telecommunications, water)	9
Need for pro-private sector regulation and laws	9
Dependence/need for continued access to external markets	9
Existence of monopolies	9
Lack of adequate support to micro/small businesses and citizen entrepreneurs	9
Inefficient, bloated bureaucracy and inadequate public services	8
Need for improved export marketing	8
Weak legal system and associated contracting and dispute resolution uncertainties	8
Prohibitive tax regulations	8
Restrictive/discriminatory licensing/permit requirements (work, residency, industry)	7
Lack of prudent resource management	7
Acute shortage of foreign exchange, insufficient allocation	7
Health and nutrition problems (i.e., AIDS epidemic)	6
Rapidly rising population and expanding labor force/rising unemployment	6
Insularity (i.e., protectionism, anti-foreigner sentiment, regional focus)	6
Over-dependence on agricultural sector which has poor output and productivity	5
Persistent inflation and currency devaluation	5
War/civil strife	4
Basic education/skills training	4
Need for policies that ensure macroeconomic reform and stability	4
Poor performance of the civil service	4
Need to bring informal entrepreneurs into the formal commercial system	4
Dependence on imported technical and managerial manpower	3
Labor problems (i.e., strikes, instability)	3
Inadequate industrial base (i.e., factories, plants, capital goods)	3
Mineral dependence	2
Poor local knowledge of foreign trade and investment opportunities	2
Lack of international networking	2
Lack of transparency in public sector actions	2
High interest rates	2
Brain drain	1
Capital flight	1
Poor trading linkages between large and small business sectors	1
Suspension of the structural adjustment program	1
Exchange rate overvaluation and associated discrimination against agriculture	1
Weak savings base	1
TOTAL	484

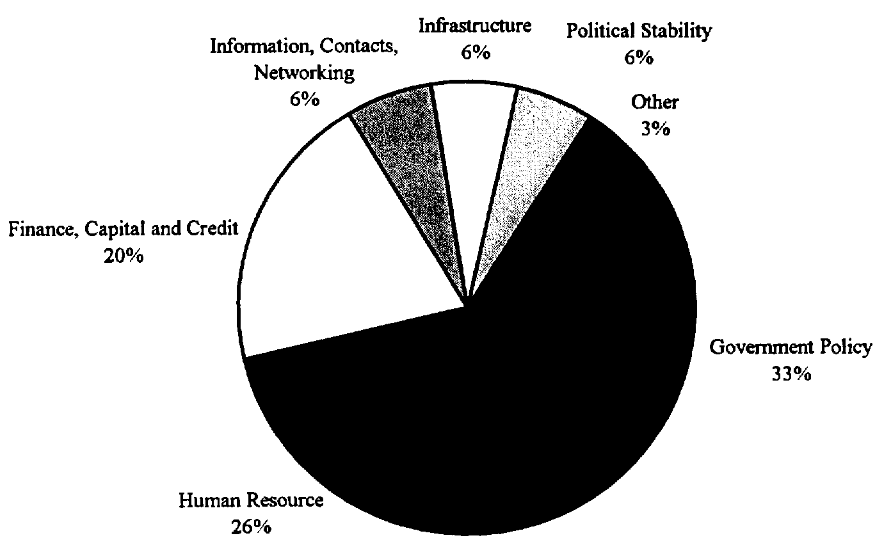
Source: Studies analyzed and interviews conducted by J.E. Austin Associates, Sept.-Dec. 1995

Exhibit 4

Constraints on the Private Sector in the SAR

Government Policy (Including Trade/Investment Restrictions)	157
Human Resource Constraints	127
Finance, Capital, And Credit Constraints	98
Access To Information, Contacts, Networking	30
Infrastructure	29
Political Stability	27
Other	16
Total	484
Source: Studies analyzed and interviews conducted by J.E. Austin Associates, Sept - Dec 1995	

Constraints Affecting the SAR



Source: Studies analyzed and interviews conducted by J.E. Austin Associates, Sept - Dec 1995

Exhibit 5

Interviews/Country Reports: Summary of Constraints Noted

Category of Constraint	Specific Constraint Noted
1. Policy Constraints	
i. Policy: Trade	Countries in the region compete in the manufacture of similar goods (Botswana) Differences in currencies in the region (Botswana) SACU-imposed restrictions (Lesotho, Namibia, Zambia) Severe formal trade barriers (Namibia, Tanzania, Zambia) Serious informal trade barriers (Lesotho, Namibia, Swaziland, Tanzania, Zambia) High cost of finance (Zambia, Zimbabwe) Export subsidies from RSA (Botswana, Zambia) Differing standards within the region (Namibia) Lack of standard taxation in the region (Angola, Malawi, Namibia, Tanzania) Inward-looking business (Botswana, Namibia, Swaziland, Zambia)
ii. Policy: Investment	Lack of access to capital (all countries) Lack of availability of short-term finance (Lesotho, Namibia, Swaziland, Tanzania, Zambia) High interest rates (Botswana, Swaziland, Zambia, Zimbabwe) Exchange controls within the region (Zambia) High inflation (Malawi, Zambia, Zimbabwe) RSA export subsidies (Botswana, Lesotho, Zambia) High transaction costs, corruption (Tanzania) Poor tax policy, high corporate taxes (Botswana, Swaziland, Zambia, Zimbabwe) Competition from imports (without investment in country) (Botswana) Low level of technology (Botswana, Zambia) Restrictive, heavy regulatory and procedural requirements (Swaziland, Zambia, Zimbabwe) Priority given to SOEs (Zimbabwe)

Category of Constraint	Specific Constraint Noted
iii. Policy Process	No holistic planning approach (Botswana) Lack of dialogue between private enterprise and public sector (Botswana, Lesotho, Namibia, Malawi, Swaziland, Zambia, Zimbabwe) Private enterprise not organized to influence public sector (Botswana, Lesotho, Malawi, Zambia) Lack of transparency in public sector decision-making (Namibia, Swaziland, Zambia) Insufficient/poor legal framework (Namibia, Swaziland, Zambia, Zimbabwe) Lack of private participation in SACU renegotiations (Namibia, Zambia)
iv. Policy: Other	Poor quality of the civil service (skills, service, corruption) (Lesotho, Malawi, Namibia, Swaziland, Tanzania, Zambia, Zimbabwe) Strength of monopolies, oligopolies (Malawi, Namibia, Zambia)
2. Financial Sector	Insufficient availability of banking services to small-scale and indigenous entrepreneurs (Botswana, Lesotho, Malawi, Namibia, Swaziland, Zambia) Dependence on RSA (Botswana, Lesotho, Namibia, Swaziland, Zambia) High cost of finance (Zambia, Zimbabwe) Few lending instruments (Zambia) Bank lending to private sector restricted to "blue chip" firms or "old boy" networks (Botswana, Namibia, Zambia, Zimbabwe) Restricted currency convertibility (Angola) Land tenure issues/inability to use land as collateral (Botswana, Malawi, Namibia, Swaziland, Tanzania, Zambia, Zimbabwe) Lack of regional accountancy and other standards (Zambia) Lack of domestic savings (Zambia) Large amount of government borrowing (Zambia)
3. Human Resources	Incentive and attitude problems among civil servants (Botswana, Malawi) Absence of training, skills required for business - entrepreneurial, managerial, technical (all countries)

Category of Constraint	Specific Constraint Noted
3. Human Resources, continued	Restrictions on who can provide training (Namibia) High cost of labor (Botswana) High unemployment (Botswana, Lesotho, Namibia) "Brain Drain" (Lesotho, Zambia) Low labor productivity (Botswana, Namibia) Unproductive habits, attitudes towards entrepreneurship and business (Botswana, Lesotho, Malawi, Namibia, Zambia, Zimbabwe)
4. Infrastructure	High cost of services and utilities (Botswana, Lesotho, Namibia, Swaziland) Regional electricity grid/water supply not integrated (Botswana) Poor quality, lack of infrastructure (all countries) Focus/dependency on RSA (Namibia) SOE predominance (Namibia)
5. Access to Information, Contacts and Networking	Lack of information, lack of networking (Lesotho, Botswana, Namibia, Tanzania, Zambia) Lack of access to market information (Botswana, Lesotho, Namibia, Tanzania, Zambia) Lack of regional communication, networking (all countries)
6. Special Focus: Small and Disadvantaged Enterprise	Lack of availability of banking services to small-scale entrepreneurs (Botswana, Namibia) Corruption in the government tendering system (Botswana, Tanzania) Availability of capital (all countries) Lack of basic business, management, technical skills (Botswana, Malawi, Namibia, Swaziland, Tanzania) Lack of outsourcing by big business (Malawi, Zambia) Small business neglected by government (Botswana) Large non-formal sector (Malawi, Namibia, Zambia, Zimbabwe)

Exhibit 6

Interviews/Country Reports: Summary of Constraints Noted

Constraints	Angola	Botswana	Lesotho	Malawi	Mozambique	Namibia	South Africa	Swaziland	Tanzania	Zambia	Zimbabwe
Policy: Trade	x	x	x	x		x		x	x	x	x
Policy: Investment	x	x	x	x	x	x	x	x	x	x	x
Policy: Process		x	x	x		x		x		x	x
Policy: Other*			x	x		x		x	x	x	x
Financial Sector	x	x	x	x		x		x	x	x	x
Human Resources**	x	x	x	x	x	x	x	x	x	x	x
Access to Information/Contacts		x	x			x			x	x	
Infrastructure	x	x	x	x	x	x	x	x	x	x	x

Special Focus	Angola	Botswana	Lesotho	Malawi	Mozambique	Namibia	South Africa	Swaziland	Tanzania	Zambia	Zimbabwe
Africanization	x	x	x	x	x	x	x	x	x	x	x

*Includes poor quality of civil service (corruption, skills) and policies which promote monopolies/parastatal sector.

**Includes: 1) technical/business skills; and 2) labor productivity.

NOTE: The above constraints were identified during field interviews conducted by the J.E. Austin Associates team from October-December 1995. They do not constitute an exhaustive list of constraints to private sector growth in each country. Rather, they reflect local stakeholder perspectives and opinions. Field interviews served as one component of the overall private sector assessment and provided valuable input for subsequent stages of analysis.

Exhibit 7

Focus Groups: Summary of Constraints Noted

Category of Constraint	Specific Constraints Noted
1. Policy Constraints	
i. Trade Policy	Trading patterns distorted by past civil strife RSA high unemployment causes RSA to maintain high barriers Excessive depth of government involvement in the economy
ii. Policy: Investment	Unstable money markets / exchange rates High interest rates RSA investment is moving out of the region Investment so far dominated by old companies coming back - new investment is waiting Excessive depth of gov't involvement in the economy Government harassment and interference Policies have fostered extensive growth of SOEs, and nationalization/public control Practices (regulation, procedures, bureaucracy) restrictive to private sector 5-year plans are rigid -not conducive to private sector input, needed policy change
iii. Policy: Process	The region's business has no voice; There are few organizations to give the region's business a voice 5-year plans are rigid and not conducive to private sector input and needed policy change Lack of agreement between public and private sectors on status, motives, requirements
iv. Policy: Other	Policies have fostered extensive growth of SOEs, and nationalization/public control SOEs have been operated on non-business lines Practices (regulation, procedures, bureaucracy) restrictive to private sector
2. Financial Sector Policy	Unstable money markets Uncertain exchange rates High interest rates Restricted private sector capital accumulation Lack of absorptive capacity (too many other barriers to doing business) to allow capital to be put to use

Category of Constraint	Specific Constraints Noted
3. Human Resources	**Lack of specific skills needed by business: entrepreneurial, managerial, technical** **Strong labor unions constrain flexibility, mobility in RSA** **Environment (social, political, business) has not fostered entrepreneurial skills**
4. Infrastructure	**Underdeveloped infrastructure (various)** **SAR countries lack the (Asian-style) resources to invest in infrastructure**
5. Access to Information, Contacts and Networking	**Lack of access to information and technology**
6. Special Area of Analysis: Africanization	**Excessive depth of government involvement in the economy** **"Cultural" constraints** **Many regulatory barriers** **Government crowds out initiatives from indigenous entrepreneurs (Zimbabwe)** **Lack of national consensus/ open discussion (Zimbabwe)** **Strength of labor unions restricts growth of small operations (South Africa)** **Government harassment and interference** **Practices (regulation, procedures, bureaucracy) restrictive to private sector**

Exhibit 8

Gross Domestic Investment as a percent of GDP

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	Average 1973-93
Botswana	49.90	51.70	46.00	38.30	28.10	34.60	34.90	37.70	40.60	43.60	30.10	26.30	30.40	16.20	24.50	7.30	40.80	40.80	40.80	40.80		35.17
Lesotho	18.60	17.70	18.70	36.10	25.00	25.90	34.60	42.40	43.10	49.30	33.70	41.70	49.40	46.10	45.40	49.30	63.80	73.70	69.90	69.60	75.70	44.27
Malawi	22.40	27.30	33.70	26.30	24.70		30.20	24.70	17.60	21.40	22.80	12.90	18.60	12.30	15.70	18.70	21.20	19.70	20.10	18.80	12.30	21.07
Mozambique								22.50	22.80	22.80	12.20	13.90	9.10	18.80	26.20	34.80	34.60	38.10	39.00	38.40	41.50	26.76
Namibia								32.40	30.40	22.40	17.10	16.70	13.50	12.50	14.80	19.10	15.90	19.60	10.40	11.50	9.60	17.56
So. Africa	27.70	33.40	31.70	29.10	22.40	23.20	23.00	28.30	34.20	29.40	24.40	25.70	20.10	18.20	17.90	20.20	20.50	17.10	16.30	15.10	15.20	23.48
Swaziland	23.40	26.90	17.80	29.60	27.00	43.90	39.70	30.30	31.10	32.30	30.00	33.40	26.20	20.00	14.80	23.60	24.20	20.70	17.70	19.70	17.60	26.19
Tanzania	21.10	22.00	21.10	22.90	26.10	25.20	26.10	23.00	24.70	21.00	13.60	15.30	17.70	25.30	50.00	12.90	44.80	43.00	47.90	48.90	50.70	28.73
Zambia	28.90	36.90	40.90	31.50	24.70	23.90	14.10	23.30	19.30	16.80	13.80	14.70	14.90	23.80	13.90	11.40	10.80	17.30	14.70	14.10	15.30	20.24
Zimbabwe	25.40	27.50	26.30	17.90	19.10	11.90	12.70	18.80	23.10	21.20	15.90	18.90	19.80	18.60	17.20	21.80	19.00	24.20	25.00	24.30	22.50	20.53
Korea	24.20	31.60	27.00	25.40	27.30	31.30	35.40	32.00	29.80	28.90	29.10	29.80	29.40	28.70	29.80	31.10	33.60	36.90	38.90	36.60	34.30	31.00
Malaysia	25.50	30.90	25.30	23.60	25.80	26.70	28.90	30.40	35.00	37.30	37.80	33.60	27.60	26.00	23.20	26.00	28.60	31.50	37.00	33.80	33.20	29.89
Thailand	27.00	26.60	26.70	24.00	26.90	28.20	27.20	29.10	29.70	26.50	30.00	29.50	28.20	25.90	27.90	32.60	35.10	41.10	42.20	39.60	40.00	30.67
Average SAR	27.18	30.43	29.53	28.96	24.64	26.94	26.91	28.34	28.69	28.02	21.36	21.95	21.97	21.18	24.04	21.91	29.56	31.42	30.18	30.12	28.93	26.77
Average HPE 3	25.57	29.70	26.33	24.33	26.67	28.73	30.50	30.50	31.50	30.90	32.30	30.97	28.40	26.87	26.97	29.90	32.43	36.50	39.37	36.67	35.83	30.52

Note: Regional averages are unweighted.
SAR averages before 1980 exclude Mozambique and Namibia.

Source: World Tables, 1995; JAA calculations

Exhibit 9

Quality of Investment

	GDI as % of GDP 20 Yr. Average 1973-93	GDP Ave. Growth Rate 1973-93	Incremental Investment to Incremental GDP Output Ratio
Botswana	35.1	9.9	0.28
Malawi	21.0	3.4	0.16
Swaziland	26.1	3.4	0.13
Zimbabwe	20.5	2.5	0.13
Lesotho	44.2	4.9	0.11
Tanzania	28.7	2.9	0.10
Namibia	17.5	1.8	0.10
So. Africa	23.3	1.7	0.08
Mozambique	26.7	1.7	0.06
Zambia	20.2	0.9	0.05
Korea	31.0	8.4	0.27
Thailand	30.6	7.5	0.25
Malaysia	29.9	6.8	0.23
Average SAR (Unweighted)	26.4	3.4	0.12
Average HPE 3 (Unweighted)	30.5	7.6	0.25

Notes: Regional averages are unweighted.
SAR averages before 1980 exclude Mozambique and Namibia.
Countries listed by rank, from highest Incremental Investment to Incremental GDP Output Ratio to lowest.

Source: World Tables, 1995; JAA calculations.

Exhibit 10

Public investment as a Percentage of GDI

	Percentage of GDI												Annual average		
	1980	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994		75-84	85-89	90-MR
Botswana	0.38												0.47		
Lesotho							0.61	0.58	0.55	0.52	0.54		0.74		0.56
Malawi	0.79	0.62	0.76	0.57	0.53	0.46	0.48	0.48	0.58	0.74	0.86		0.66	0.58	0.61
Mozambique		0.46	0.41	0.44	0.47	0.51	0.53	0.47	0.41	0.34	0.41			0.46	0.42
Namibia		0.63	0.56	0.54	0.46	0.36	0.37	0.44	0.42	0.40	0.39			0.51	0.40
South Africa	0.49	0.44	0.43	0.39	0.34	0.36	0.34	0.33	0.31	0.30	0.27		0.47	0.39	0.31
Swaziland		0.66	0.55	0.33	0.26	0.30	0.34	0.37	0.40	0.42	0.34			0.42	0.38
Tanzania		0.34	0.20	0.27	0.33	0.35	0.29	0.29	0.30	0.29	0.30			0.30	0.30
Zambia		0.35	0.70	0.34	0.57	0.77	0.46	0.69	0.64	0.34	0.62			0.53	0.54
Zimbabwe	0.31	0.59	0.46	0.23	0.25	0.24	0.22	0.18	0.18	0.19			0.44	0.34	0.19
SAR Region	0.49	0.52	0.48	0.38	0.39	0.40	0.45	0.45	0.43	0.40	0.44		0.54	0.43	0.43
excluding South Africa	0.41	0.54	0.49	0.38	0.40	0.41	0.46	0.45	0.44	0.41	0.48		0.45	0.43	0.44
SUB-SAHARAN AFRICA	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5		0.51	0.52	0.521

Private investment as a Percentage of GDI

	Percentage of GDI												Annual average		
	1980	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994		75-84	85-89	90-MR
Botswana	0.62												0.53		
Lesotho							0.39	0.42	0.45	0.48	0.46		0.26		0.44
Malawi	0.21	0.38	0.24	0.43	0.47	0.54	0.52	0.52	0.42	0.26	0.14		0.34	0.42	0.39
Mozambique		0.54	0.59	0.56	0.53	0.49	0.47	0.53	0.59	0.66	0.59			0.54	0.58
Namibia		0.37	0.44	0.46	0.54	0.64	0.63	0.56	0.58	0.60	0.61			0.49	0.60
South Africa	0.51	0.56	0.57	0.61	0.66	0.64	0.66	0.67	0.69	0.70	0.73		0.53	0.61	0.69
Swaziland		0.34	0.45	0.67	0.74	0.70	0.66	0.63	0.60	0.58	0.66			0.58	0.62
Tanzania		0.66	0.80	0.73	0.67	0.65	0.71	0.71	0.70	0.71	0.70			0.70	0.70
Zambia		0.65	0.30	0.66	0.43	0.23	0.54	0.31	0.36	0.66	0.38			0.47	0.46
Zimbabwe	0.69	0.41	0.54	0.77	0.75	0.76	0.78	0.82	0.82	0.81			0.56	0.66	0.81
SAR Region	0.51	0.48	0.52	0.62	0.61	0.60	0.55	0.55	0.57	0.60	0.56		0.46	0.57	0.57
excluding South Africa	0.59	0.46	0.51	0.62	0.60	0.59	0.54	0.55	0.56	0.59	0.52		0.55	0.57	0.56
SUB-SAHARAN AFRICA	0.47	0.46	0.46	0.47	0.51	0.49	0.49	0.47	0.48	0.48	0.47		0.49	0.48	0.48

Source: World Bank Data

Exhibit 11

Net FDI Inflows to SADC Region 1986-1994

(in US$ Million)

Country	1986	1987	1988	1989	1990	1991	1992	1993	1994
Angola	234	119	131	200	-335	664	288	206	386
Botswana	70	114	40	42	38	40	40	39	40
Lesotho	2	6	21	13	17	8	3	15	8
Malawi	0	0	0	9	23	18	2	3	8
Mauritius	7	17	24	36	41	19	15	15	16
Mozambique	2	6	5	3	9	23	25	30	26
Namibia					37	105	56	66	76
South Africa	-120	-160	98	10	-5	-8	-5	-8	5
Swaziland	23	54	38	72	39	77	56	40	58
Tanzania	0	0	0	6	-3	3	12	20	12
Zambia	28	75	93	164	203	34	134	124	97
Zimbabwe	7	-31	4	-10	-12	3	15	28	15
TOTAL	253	200	454	543	52	986	641	578	747

Sources: Cockcroft, Laurence and Riddel, Roger C., Foreign Direct Investment in Sub-Saharan Africa, 1995; World Investment Report, UNCTAD, 1995; World Bank, Africa Region, Country Department IV, Country Operations Division, June 1996.

NOTE: Although data for 1995 was not available, anecdotal evidence suggests a significant increase in foreign direct investment, particularly in South Africa.

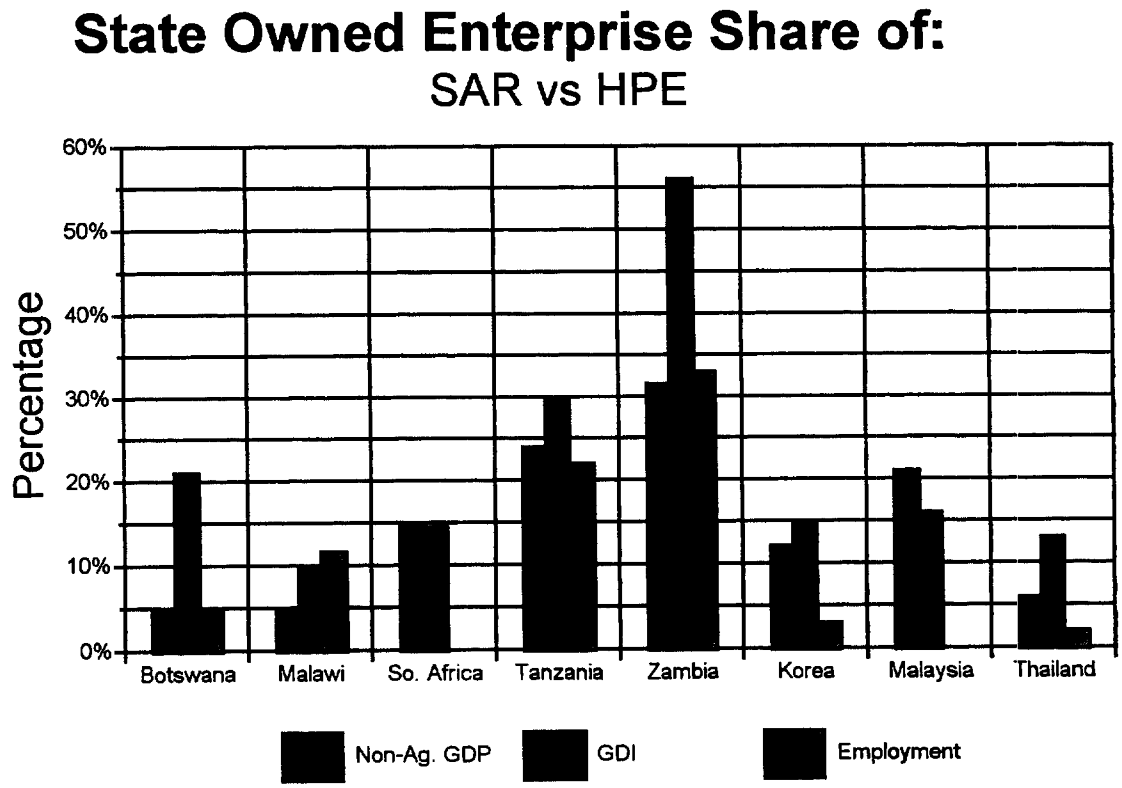
Exhibit 12

Stock Market Capitalization

Country	Number of Listed Companies	Traded Value, USD m	Market Capitalization, US$ m
Botswana	11	31	377
Mauritius	34	83	1,579
Namibia	9	16	196
South Africa	640	20,657	259,536
Swaziland	4	2	339
Zambia	8	N.A.	N.A.
Zimbabwe	65	188	1,810
TOTALS	763	20,976	263,838
South African share	83.9%	98.5%	98.4%

Source: Compilation of various sources and years; International Finance Corporation (IFC) data.

Exhibit 13



Source: Bureaucrats in Business, 1995.

Exhibit 14

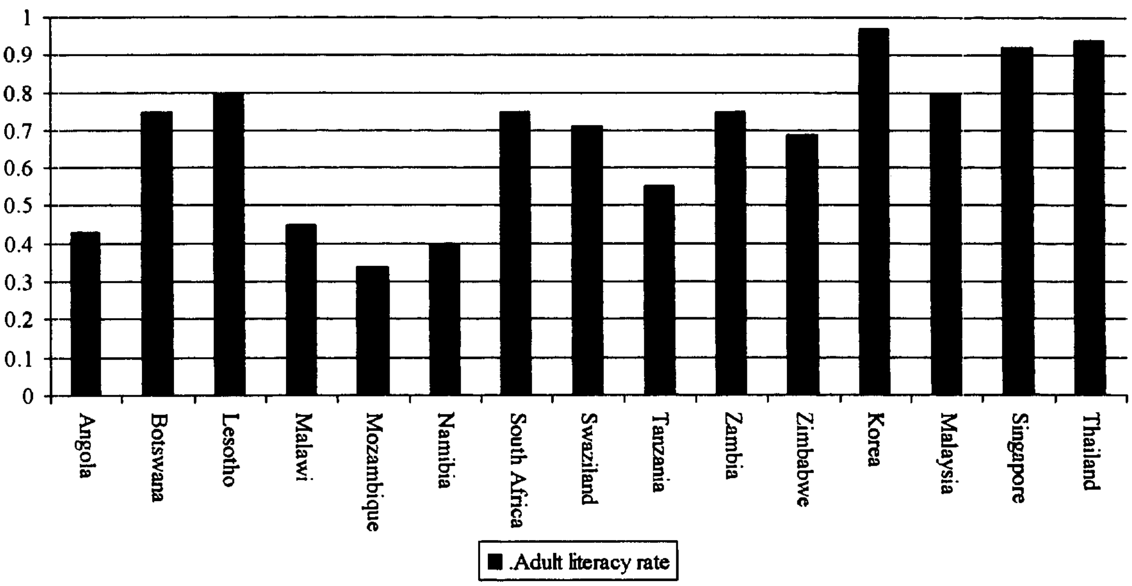
Leading SAR Banks and Asset Value

Country	Number of Banks	Assets (USD millions)	Assets % of Total
South Africa	8	89,498	98.966
Malawi	2	399	0.004
Lesotho	1	222	0.002
Zambia	2	215	0.002
Zimbabwe	3	98	0.001
Swaziland	1	1	0.000

Source: IFC, 1995.

Exhibit 15

Educational Expenditures and Results



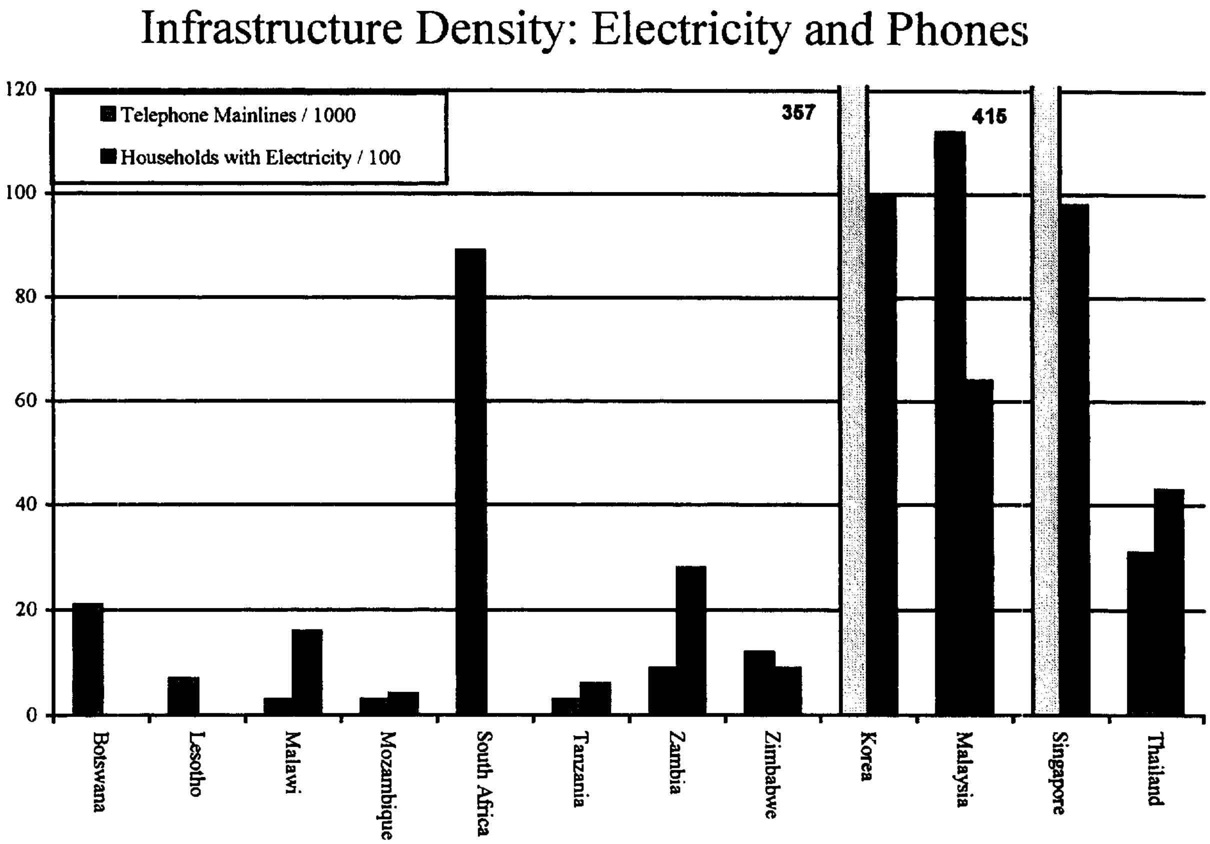
Source: Relevance of Asian Development Experiences to African Problems

Exhibit 16

Education Summary Table		
Indicator	**SAR Average**	**HPE Average**
% of Cohorts Persisting to Grade 4 (Female/Male): 1970	**81/81**	**97/97**
1988	**78/77**	**99.7/99.5**
Education Expenditure as a Percentage of GDP: 1960	**2.03**	**2.5**
1992	**6.15**	**4.4**
% of Education Budget spent on: Primary education	**42.6**	**41.3**
Secondary education	**29.2**	**33.6**
% of Adults Literate	**60**	**92**
% Enrolled in First Grade	**90**	**96**
% Completing Primary Level	**62**	**96**
Student-to-Teacher ratios: 1965	**50:1**	**44:1**
1992	**42:1**	**24:1**

Source: World Development Reports, World Bank, 1987 - 1995.

Exhibit 17



Source: World Development Report, 1994; 1995

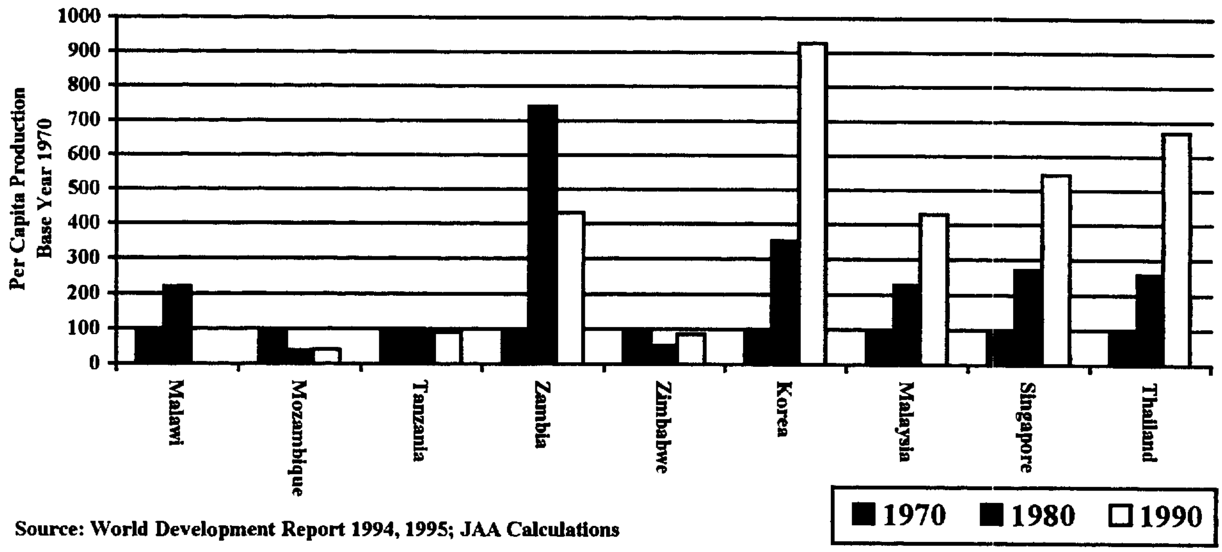
Infrastructure Density: Paved Roads

	Average km Paved Roads	Percent of Roads Paved	Paved Roads per 1000 Square km	Paved Roads per Million Pop.
SAR excluding RSA	4175	5.87	7.21	345
Average HPE	8462	56.56	237.80	969
Average OECD	1001388	n/a	783.83	17865

All data 1990 with the exception of Percentage Paved for Asian countries: 1986.
Sources: East Asian Miracle, (1993); World Development Reports, 1992, 1994, 1995; World Tables, 1995; Management and Financing of Roads (1995); JAA Infrastructure Summary Report (1996); JAA calculations.

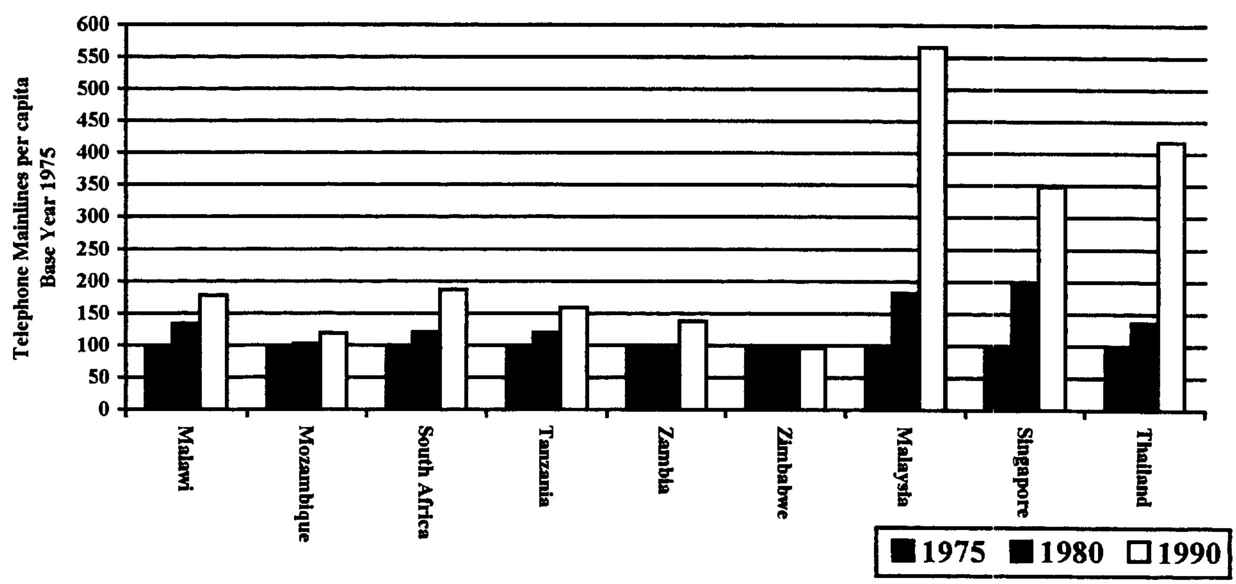
Exhibit 18

Relative per capita Growth in Electricity Production



Source: World Development Report 1994, 1995; JAA Calculations

Relative per capita Growth in Telephone Mainlines



Source: World Development Report, 1994; JAA calculations

Exhibit 19

Current World Bank Projects in the SAR Addressing the Listed Constraints

Country	Project Description	(US$m)	Year*
Angola	Labor Force Skills Development & Training	35	1996
Angola	Lobito Port Transport System	30	1996
Angola	Urban Water Supply and Sanitation	14	1996
Lesotho	Highlands Water Project	1,100	1996
Lesotho	Privatization & Private Sector Development	11.4	1996
Lesotho	Road Rehabilitation & Maintenance	129	1996
Malawi	Education Sector Credit III	300	1996
Malawi	Entrepreneurship Development	266	1996
Malawi	National Water Development	94.1	1996
Malawi	Power VI Project	90	1996
Malawi	Primary Education Project	0.2	1996
Malawi	National Water Development	79.2	1995
Malawi	Railways Restructuring Project	16.16	1995
Malawi	Entrepreneurship Development	4.6	1995
Malawi	Entrepreneurship Development	40	1995
Malawi	Civil Service Training	22.6	1994
Malawi	Entrepreneurship Development	4.3	1994
Mozambique	National Water Development	1	1996
Mozambique	Financial Sector	9	1994
Mozambique	Financial Sector	200	1994
Mozambique	Transport Sector Rehabilitation	188	1994
Swaziland	Urban Infrastructure Development	29	1995
Tanzania	Human Resource Development Project	22.5	1996
Tanzania	Urban Infrastructure Rehabilitation	178	1996
Tanzania	Transport Sector	170.2	1994
Zambia	Road Sector Project	500	1996
Zambia	Road Sector Investment Program	380	1996
Zambia	Urban Restructuring & Water Supply	33	1995
Zambia	Health Sector Support Project	38.7	1995
Zambia	Financial Sector	18	1994
Zambia	Financial Sector	10	1994
Zambia	Privatization	16.8	1994
Zambia	Trade Reform/Macroeconomic Policy	150	1994
Zimbabwe	Power Sector Project	200	1996
Zimbabwe	Hwange Power Station	90	1994
TOTAL:	**1994 and 1995 only ****	**1,119.56**	

* 1996 figures represent total projected costs and not the amount of World Bank lending.

**1996 projects not included as the exact amount of World Bank lending as % of total cost is not yet known.

Sources: World Bank Annual Report 1994 and 1995; Public Information Center, 1996 Projects Catalog.

PRIVATE SECTOR ASSESSMENT: SOUTHERN AFRICA REGION, ANNEXES I THROUGH VI

Final Report

U.S. Agency for International Development

Prepared for: USAID/RCSA

Prepared by: J.E. Austin Associates

Sponsored by: Private Enterprise Development
Support Project III
Contract No. PCE-0026-Q-00-3031-00
Delivery Order Nos. 16 and 41
Prime Contractor: Coopers & Lybrand, LLP

June 1996

Coopers
&Lybrand

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ANNEX I:
LITERATURE REVIEW AND BIBLIOGRAPHY

Literature Review

Objectives

The objectives of this pre-assessment literature review related to private sector development in Southern Africa are:

1.To make a comprehensive and intensive effort to gather the most recent and most reliable available data;

2.To evalute and build on the analyses, expertise and data present in more than 300 documents and studies so as to enhance subsequent phases of this private sector strategy development effort; and

3.To create a data bank of relevant studies for the newly formed RCSA and to offer this as a core contribution for a private sector USAID regional library.

Methodology

To accomplish the above objectives, the team used the following methodology:

1.Contacted major donors such as the UN, World Bank, IMF, European Commission, and others to obtain recent relevant studies;

2.Requested a search of USAID/CDIE for relevant documents and contacted other government agencies for country documentation;

3.Procured Economist Intelligence Unit and other commercial data sources;

4.Conducted a search of on-line services, Internet sources, and recent articles and periodicals containing relevant information; and

5.Contacted embassies in Washington, D.C.

These methods were complemented by a comprehensive on-the-ground search by J.E. Austin team members who visited 9 of the 11 countries of the region in October and November 1995, which resulted in additional materials published by local governments, consulting firms, banks and other institutions.

Results and Findings

The effort resulted in the procurement of more than 300 documents. To be of assistance to USAID personnel, although this was not mentioned in the scope of our contract, J.E. Austin Associates prepared a library of these materials, many of which have already been delivered to the RCSA.

Extremely useful documents and studies were available even concerning countries where little work has been done historically on private sector development. For example, we have a private sector strategy for Angola done by the UN and also the results of the First Private Sector Conference in Mozambique.

The most comprehensive study of the region was completed for the European Commission by the Club de Bruxelles.

Many studies had conflicting data which required further analysis and harmonization. This has strengthened our confidence in some cases, but has also revealed the still rather poor data base that exists for some countries in the region.

In general terms, the most important constraints which are revealed by these studies are: (1) policy impediments to private sector growth (i.e., trade, investment, enabling environment); (2) lack of technical/business skills education; (3) the lack of entrepreneurial training; (4) the need for increased access to capital; and (5) the need for government regulations and laws that make starting and operating a business easier.

These studies mainly served as inputs for the specialists working on the analysis of constraints. However, to make these as user-friendly as possible and to enhance the utility of this exercise to USAID and to others who may follow, we present below a brief synopsis of the regional as well as country-level studies and their principal findings.

Regional Studies

A major study completed in October 1995 for the European Commission by the Club de Bruxelles as an input into SADC-EU Cooperation and as a Guide to European Enterprise Investment in SADC contains 500 pages of useful text, data and exhibits. The study is strong on description and short on analytical richness but can serve as one of the most comprehensive and recent compendiums on the region. There are sections on the various sectors: agriculture, fishing, forestry, mining, manufacturing, transport and communications. The work also contains SADC country profiles on geography, demography, macroeconomics, social features, and investment policy environment and incentives.

Most studies of the Southern Africa region found unavailability of capital a leading constraint to growth. They also noted the future impact of AIDS, the limited and undiversified indigenous production base, the shortage of foreign exchange and the artificially high productivity-adjusted real wages in South Africa as constraints to the growth of private enterprise.

Angola

The cease fire that resulted from the peace accords signed on November 20, 1994 seems to be holding, although sporadic fighting continues, leaving many farmers afraid to return to their fields. About 85% Angola's 2.8 million economically active workers (of an estimated total population of 10 million, July 1995) are currently employed in subsistence farming, although this provides less than 15% of Angola's GDP of $6.1 billion. The remaining estimated 15% of the population is employed in industry. About 60% of Angola's GDP comes from oil production. Furthermore, Angola has promising natural resources--oil, gold, diamonds and arable land, but clearly needs peace and government stability to take advantage of them.

The Government of Angola's Round Table on Reconstruction and Rehabilitation Private Sector Strategy report, completed in September 1995 as part of a collaborative effort of the European Union and the United Nations Development Programme, outlines "Angola's investment potential with a view to determine a basis of competition within the sub-region." It describes Angola's resources, pre-war productive history and potential to be one of the richest countries in Africa. The report analyzes Angola's economic sectors, including agriculture, manufacturing, mining, services, energy, transportation and communication, and proposes options to enhance investment, competitiveness and private sector development.

A September 1995 European Union paper entitled Programme of Community Rehabilitation and National Reconciliation contains an overview of Angola's current economic crisis after two decades of war and outlines the macroeconomic reforms which Angola initiated in July 1995. The paper also highlights the program of humanitarian assistance sought by the Angolan Government and the Programme of Community Rehabilitation.

First and foremost of the cited constraints to the growth of the private enterprise sector of Angola is war and its effects, such as the large number of remaining land mines, damage to infrastructure and the difficulties of maintaining ongoing business investment and relationships in an unstable environment. Although most of the constraints cited in studies of Angola can be traced in some way to the effects of the war, the Angolan private enterprise sector is constrained by many of the same factors cited in other Southern African countries. These constraints include a need for trained managers, improved education, increased access to credit and a need for government regulations and laws that make starting and operating a business easier. Furthermore, bureaucratic procedures, import licenses and foreign exchange authorization requirements remain significant obstacles to trade.

Botswana

The economy has been driven since the 1970s largely by its mining industry. Botswana possesses natural supplies of diamonds, copper, nickel, salt, soda ash, potash, coal, iron ore, and silver. Diamonds alone accounted for 25% of GDP in 1980 and 50% of GDP in 1991, and diamonds make up 78% of Botswana's $1.7 billion in exports. About 80% of the population (of an estimated total of 1,359,352, July 1994) is dependent on agriculture for its livelihood. Only 50% of food needs are met by this predominantly subsistence farming, however, and Botswana uses much of its diamond earnings to import additional food supplies.

A report was concluded by Deloitte & Touche in July 1995 on the feasibility of establishing an international financial services center in Botswana. Botswana as an International Financial Services Centre describes the characteristics of international financial services centers, the demand for an international financial services center in the Southern African region and why and how to go about locating an international financial services center in Botswana.

Despite its exceptionally high, steady rate of growth, Botswana suffers from constraints to growth of the private enterprise sector that are common to most nations of the Southern African region. Studies state that the private enterprise sector needs more business training and entrepreneurship development, more access to capital and a less cumbersome approach to regulation of the private sector by the government. Studies also cited the risk of regional instability, the underdevelopment of locally-owned enterprises and their inability to effectively participate private sector, inadequate basic infrastructure, and the need for continued access to external markets as major constraints to growth. More specific to Botswana, insufficient investment in non-mineral sectors was cited as another leading constraint to growth.

Lesotho

Lesotho, with a GNP of $1.5 billion and GNP per capita of $750 in 1995, faces some particularly difficult challenges as a result of the end of apartheid in South Africa. Though Lesotho remains very poor and in need of international assistance, international donors are leaving Lesotho, no longer interested in Lesotho as a base from which to combat South African apartheid. Paralleling the donor movement from Lesotho to South Africa has been the flight of scarce capital and trained workers from Lesotho to South Africa. Wages are more attractive in South Africa and markets are growing faster. Small, landlocked, and mountainous, Lesotho's main resource is water. Lesotho hopes for the possibility of hydroelectricity from its Highlands Water Project, expected to become operational by 1997.

Important studies gathered on Lesotho include a study of small-scale enterprises by Gemini and Development Alternatives, Inc. This 1990 study found that there were 102,968 small-scale enterprises employing 161,284 people, or 20% of the national labor force. Of these small-scale enterprises, about 80% were rural. Half of small-scale enterprise was in manufacturing, a third in trade or commerce and the rest in services.

Another important study, Lesotho's Long Journey, is a comprehensive overview by a Maseru-based firm called Sechaba Consultants that describes Lesotho's historical, social, economic and political development with a view to the future. This study provides a historical overview of Lesotho, its culture, geography, population, land use, schooling, health, housing, economy, government, relations with South Africa, foreign aid and other topics. This 200-page document presents a large volume of very recent socio-economic data in clear graphical form.

Poverty in Lesotho, 1994, produced by the Government of Lesotho, provides maps of the population distribution and distribution of resources throughout the country. The study discusses poverty in Lesotho and ways in which Lesotho copes with poverty. It contains 162 pages of text, socio-economic and demographic maps, tables that analyze Lesotho's poverty from a variety of approaches.

Constraints to growth of the private enterprise sector in Lesotho identified by studies include poor performance of the civil service, rapidly rising population and expanding labor force, rising unemployment, inadequate social and economic structure, deteriorating health and education standards, low percentage of children attending school, lack of relevance of education to occupational and social realities, failure to attract private foreign investment, capital flight out of the country, cumbersome bureaucratic procedures which restrict the flow of trade, over-dependence on the agricultural sector which has poor output and productivity, the absence of a domestic entrepreneurial class, and dependence on South Africa.

Malawi

One of the world's least developed countries ($180 per capita GNP in 1995), Malawi remains dependent on economic assistance from the IMF, the World Bank and other donors. The economy remains primarily agricultural, with agriculture accounting for 40% of Malawi's $7.3 billion GDP and 90% of Malawi's exports, which include tobacco, tea, sugar, coffee, peanuts, and wood products. About 43% of Malawi's estimated 428,000 wage earners (of a total population of 9.8 million, July 1995) are employed in agriculture. About 16% are employed in personal services, 15% in commerce and 7% in construction.

Studies on Malawi found that access to capital, the need to develop an entrepreneurial culture, the need for management and artisan training, shortages of foreign exchange, and significant obstacles to trade (particularly in the form of non-tariff barriers) were salient constraints to private enterprise growth.

Mozambique

Mozambique, with a population of more than 18.1 million (July 1995), a per capita income of about $80, and an unemployment rate of 50%, faces civil strife and recurrent drought. Still recovering from civil war, which ended with a peace accord in October 1992, foreign investors remain reluctant to invest. Foreign investment, which totaled $21 million in 1991,

$25 million in 1992 and $15 million in 1993, was lead by South Africans and Portuguese firms in agriculture, tourism, mining and trade.

The summary of the First Private Sector Conference in Mozambique, held in Maputo in July 1995, contains a condensed look at the leading thinking on necessary next steps for the development of private enterprise in Mozambique. Studies presented at the conference addressed topics including privatization, investment promotion, impediments to industrial recovery, constraints to small entrepreneurs in Maputo as well as in rural areas, and constraints to financing production and investment. The general conclusions of the conference were that the role of the private sector should be expanded, that the business environment should be improved, that business legislation should be revised and bureaucracy streamlined, and that an entrepreneurial culture should be developed.

Major constraints to growth of the private sector identified in studies of Mozambique include the need for successful war-to-peace transition, the need for internal and external financial resources, the need to remove bureaucratic red tape, the need to resolve land tenure issues, the difficulty of obtaining foreign exchange, the difficulty of obtaining credit, the need to bring informal entrepreneurs into the formal commercial system, the burdensome taxes on imported goods which encourage smuggling and prevent business growth, and the need for management training and entrepreneurship development in all areas.

Namibia

Key documents procured include the 1995 Action Plan and Project Profiles of the Namibian Government for the Development of Small Scale and Informal Industries, which proposes a strategy focused on increasing value added and incomes by diversifying the small informal sector away from its reliance on hawking, vending and other low value added retailing. The study concludes that the focus for development should be the manufacturing sector and, secondarily, artisanal mining, handicrafts, construction, transport, horticulture, and livestock.

A 1993 working paper on the private sector and employment prepared by the Namibian Economic Policy Research Unit comments on the reasons for the underperformance of the private sector and proposes possible solutions. This paper recommends that the businesses in the informal sector would best be developed by increasing links with the formal sector by serving as suppliers, for example. Government- and NGO-provided assistance to the informal sector is less effective. Deregulation, this paper argues, would serve to increase business--especially small business--development by allowing entrepreneurs to more freely try to meet small niches of unmet consumer demand in areas such as transportation and accommodation. Large parastatals exclude competition and also block opportunities for entrepreneurs. Finally, the paper concludes that the extent of state involvement in the national economy is too great and thus breeds inefficiency.

A 1993 Center for Applied Social Sciences working paper on Legal Obstacles to Small and

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Medium Size Business Development contains an outline of the legal environment for private business activities in Namibia. It examines the "long-standing tradition of restrictive regulation of the economy," and a national "mentality that takes it as within the State's discretionary power to allow or forbid economic activities."

Constraints to growth identified by studies include lack of access to capital, the restrictive regulatory and license requirements, the need to resolve land title issues, lack of know-how and expertise, the dominance of economic activity by large businesses, and poor trading linkages between large and small business sectors. In addition, due to heavy dependence on South Africa, Namibian private exporters lack adequate information on trade opportunities in the region, weakening Namibia's overall private sector export potential.

South Africa

Along with Country Reports and Profiles from the Economist Intelligence Unit, the EIU's Financing Foreign Operations and Investing, Licensing & Trading Conditions Abroad were procured.

A large collection of most recent and most reliable data is also included in the MAPS study of South Africa's private sector completed by J.E. Austin Associates in June 1995. That study, which includes a lengthy annotated bibliography, contains an analysis of the private enterprise sector and establishes benchmarks, such as income, literacy, life expectancy and unemployment, to monitor its future growth. That study compares the formal and informal sectors, indicating that the formal sector contributes more than 93% of GDP. The study examines black employment in South Africa and finds that although the manufacturing sector is the largest contributor to GDP, the trade sector is by far the largest employer of blacks in the country. The study concludes by highlighting key factors for rapid and sustained economic growth and by offering several strategic initiatives that could be developed into programs for helping to achieve rapid and sustained economic growth.

Constraints to private sector growth in South Africa highlighted in the literature review include high protective tariffs which hinder prospects for intra-regional trade integration, underdeveloped infrastructure, and the need for technical/managerial skills training for small and disadvantaged enterprises.

Swaziland

The Economist Intelligence Unit's Country Report for the 4th quarter 1995, procured for this study before official publication, shows mixed growth prospects for 1996, if long-term weather forecasts for more normal rainfall in 1996 prove correct. The report also warns of growing pressure on the currently dysfunctional dual system of traditional and civil service government following disclosures of misuse of public funds and difficulties in negotiations among government, employers and unions. There will be continued effort to rein in government spending, largely through commercialization of public enterprises, particularly the national airline, and to clarify the long-term development strategy for the nation. Total exports from Swaziland increased by 20% from 1993 to 1994, led particularly by increased sales of soft-drink concentrates, Swaziland's major export. Sugar output is projected to be down to 420,000 tons for 1995/96 from 485,000 tons in 1994/95.

Constraints to growth of the private enterprise sector in Swaziland that were named in studies include the lack of capital to start businesses, the need for modern legislation designed to attract badly needed foreign investment, the need to resolve land tenure issues, shortages of skilled manpower, an inefficient bureaucracy, inefficient parastatals that drag down the economy, and an inadequate level of public services. In addition, small and medium-sized exporters in Swaziland face a high degree of uncertainty due to the absence of forward exchange cover mechanisms.

Tanzania

Tanzania's population of over 28.7 million people (July 1995), consisting of well more than 100 tribes, Asians, Europeans, and Arabs, is economically heavily dependent on agriculture. Agriculture accounts for 58% of Tanzania's $21 billion GDP and 85% of exports and employs 90% of the labor force, mostly as subsistence farmers. Manufacturing, which accounts for another 8% of GDP, is largely agriculturally based. Growth in 1991-94 has been led by increased output of minerals, especially gold.

Studies of Tanzania found that constraints to the growth of the private enterprise sector include an ideology of self reliance that made Tanzanians resist foreign business ideas, an attitude the private work is "beneath contempt" and that state employment is the "only option" worthy of consideration for literate Tanzanians, a need for managerial, artisan and entrepreneurship training, lack of access to both local and foreign sources of finance, exaggerated bureaucratic procedures (including import and export licensing requirements), discriminatory industrial land allocation, and a bias toward the well-established businesses to the exclusion of new entrants. Furthermore, Tanzanian enterprises lack adequate trade information pertaining to the Southern Africa region.

Zambia

Prior to 1993, the Zambian economy (GDP $7.9 billion, $860 per capita in 1994) was in decline largely from Zambia's economic dependence on copper exports while world copper prices were weak and Zambian production was low. The finance minister announced a balanced budget plan in early 1995 that will be closely monitored by the IMF and other donors. To win IMF approval the Zambian government has begun a plan of privatization and targeted 60 companies for sale in 1995.

The leading constraints to growth identified in studies of Zambia include the scarcity of meaningful amounts of long-term finance, high interest rates or cost of finance locally, planning difficulties arising from exchange rate and interest rate fluctuations, unfair competition arising from liberalization as well as the increase in smuggling, the scarcity of skilled manpower, the need for management and artisan training, and the need for entrepreneurship development. The combination of high inflation and negative balance of payments has imposed a major constraint on trade. As a result, Zambia has a poor trade credit rating. Additionally, cumbersome bureaucratic procedures and documentation requirements have hindered the flow of exports.

Zimbabwe

With a population of more than 11.1 million (July 1995), a GDP of $17.4 billion and per capita GNP of $1,580, Zimbabwe remains economically vulnerable to drought, which caused GDP to drop 8% in 1992. Although growth rebounded to 2% in 1993 and 3.5% in 1994, recurring drought remains a serious threat. Agriculture, which accounts for 20% of GDP employs three-fourths of the work force and supplies almost 40% of exports. Manufacturing, based on agriculture and mining accounts for 35% of GDP, and mining contributes 5% of GDP.

Studies report that a major constraint to the growth of the private enterprise sector is a tendency toward insularity. They indicate that Zimbabwean entrepreneurs and enterprises distrust and seek to avoid contact with "outsiders." Internal self-sufficiency is a higher priority than growth.

Another major constraint is the low level of investment in the productive sectors of the economy. Studies indicate that investment has barely been adequate to maintain the capital stock, let alone increase it and raise productivity. Investment has declined because of the risks associated with unsustainable fiscal deficits, uncertainties and high costs associated with the foreign exchange allocation system, and the relatively high cost of doing business in Zimbabwe's highly regulated business environment, as a result of price controls, labor market restrictions and investment control procedures.

In the area of trade, Zimbabwe continues to maintain non-tariff barriers and import licensing restrictions on PTA imports. These barriers, coupled with poor quality products and weak product delivery systems, exert a negative effect on overall intra-regional trade.

Studies also point to access to foreign exchange as a constraint to growth. Foreign exchange is reported to be in tight supply and shortages disrupt access to supplies of inputs and equipment. This creates incentives for businesses to integrate vertically and maintain control over all aspects of production. Access to capital for financing businesses, land tenure issues, the need for management and artisan training, and the need for entrepreneurship development are also major constraints to private sector growth in Zimbabwe.

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ANNEX II:
FOCUS GROUP SESSIONS

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RESULTS OF FOCUS GROUP MEETINGS

I. *PURPOSE AND BACKGROUND*

In late January/early February 1996, a team of JAA consultants sought to investigate local stakeholder perspectives on the key constraints to private sector development in Southern Africa by holding Focus Group discussions with USAID officers and other field experts in the region. Participants in these discussions were invited from numerous countries, including representatives from both the public and private sectors. This broad attendance ensured an effective cross-fertilization of idea exchange. Participants were selected primarily on the basis of their proven understanding of issues affecting private enterprise growth in the region.

Findings of the private sector assessment entitled "Strategies for Regional Economic Development in Southern Africa," together with the comparative policy analysis, were presented in order to exchange ideas, gain additional input and, in essence, to conduct a reality check on the findings of the overall assessment report.

In order to achieve focused input from experts, and following the findings of the study, the workshops were divided to address the following themes: 1) Constraints to Small Business; 2) Human Resources and Indigenisation of the Private Sector (held in Zimbabwe); 3) Intra-Regional Trade & Investment; 4) Policy Reform for Private Sector Development (held in Johannesburg); and 5) SME/Policy Environment (held in Gaborone). These Focus Group topics were selected based on key issues identified in earlier phases of the Regional Private Sector Assessment.

Apart from a planned sixth session on issues relating to the financial sector which did not occur due to a SADC scheduling conflict, the Focus Groups were well-attended and achieved a healthy mix of expertise, country representation, and public and private sector perspectives.

II. *ACHIEVED OUTCOMES*

The following Focus Group reports highlight the discussion flow of the theme sessions, concepts discussed and possible approaches to redress constraints.

The key results achieved through the Focus Groups can be summarized as follows:

- Key findings of the regional assessment were confirmed;
- Insights into possible approaches to address constraints were identified;
- Additional stakeholders and centers of excellence were identified;
- The process toward "ownership" was furthered; and
- Participants achieved spin-off benefits like information exchange/networks.

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Report on "Constraints to Small Business" Workshop

January 26, 1996

I. Introduction:

The following report outlines the discussion and outcomes of issues identified during the working session of the Focus Group meeting on "Constraints to Small Business" held on the evening of January 25, 1996, at the Sheraton Hotel in Harare, Zimbabwe.

II. Background:

Following a regional assessment survey on the constraints to private sector development within the Southern Africa region conducted by J.E. Austin Associates and contracted by the USAID Regional Center for Southern Africa located in Botswana, the Focus Group meeting was convened to achieve the following objectives:

A. To offer feedback on the outcomes of the regional assessment with a particular focus on constraints to small, medium, and micro enterprise development within the Southern Africa region (SADC);

B. To provoke response on the findings of the study;

C. To gain a perspective on local initiatives in addressing the identified constraints; and

D. To brainstorm approaches to address the constraints to SME development in order to provide strategies to donors, including USAID.

Accordingly, the group of participants comprised experts from within the region, each having a particular focus in relation to SME development. (See attendance register at the end of this section).

III. Issues Raised:

Participants agreed with the outcomes of the study, as presented. Government policy was the general and most critical issue regarding constraints to private sector development (SME growth) and indigenisation.

In response to questions posed regarding structural issues (policy impediments), how to achieve geometric growth within the sector, and required technical assistance, the following issues were raised by the participants:

A. The depth of government's involvement in the economy is seen as a critical impediment to the growth of the private sector and, in particular, small business. In addition, anti-free-enterprise policies have stifled the indigenization of the economy.

B. Despite the new policy toward liberalization within the region and the privatization of parastatals, participants felt that unless market-related policies were followed, governments would continue to embed themselves.

C. In addition, cultural constraints relating to the concept of indigenisation rather than a commercial focus were important. The biggest lobby against reverting to capitalism came from "indigenous" groupings.

D. Past civil strife and its continuation have distorted the trading patterns of the countries in the region.

E. Doing business in the region in the private sector is difficult. Constraints faced by entrepreneurs include civil disturbance, government harassment and interference, unstable money markets, uncertain exchange rates, spiraling interest rates, lack of skilled human resources, low access to information and technology, and underdeveloped infrastructure.

F. A key issue raised was the lack of clarity underlying policy reform, namely, a lack of vision regarding economic principles.

IV. Outcomes:

The following outlines the key points raised in respect to the outcome of the discussion:

A. The role of advocacy and the strengthening of lobbying and advocacy groups are critical factors in developing market-related policies and government reforms. Cross-pollenization amongst the groups, intra-regionally, should be increased.

B. A holistic approach to developing the private sector should be followed, i.e., government reform with the implementation of a supportive strategy covering issues such as access to technology, etc.

C. Indigenization--active participation in the formal economy by the majority of the region's citizens--is seen as important, but should be based on commercial and market related-principles and not as an ideological objective. This point was strongly emphasized by all Focus Group participants.

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D. A special focus must identify/open routes for women in SME development. Constraints related to specific obstacles faced by women need to be identified and built into the strategy, i.e., policies need to have a high level of gender sensitivity.

V. Summary of Conclusions:

The restrictive legal and regulatory framework characteristic of Southern African countries figured high in the discussions, as did weak infrastructure. Both of these are factors that reflect direct government intervention.

However, a critical issue in achieving change to the policy environment is the role of the private sector itself. An essential component to the strategy would be to increase the advocacy and lobbying capacities of stakeholders within the region.

A primary focus in indigenization is obedience to the economic logic. Simply, economic growth is a more critical objective in achieving a level playing field (will create multiplier effects) than transferring ownership to distinct groups.

A support strategy for SME development needs to be identified to achieve a holistic objective. Simply leveling the playing field with regard to reforming government policy is one issue. This, however, needs to occur with simultaneous support programs.

VI. List of Participants:

Wellington Chadehumbe, Economist, Merchant Bank of Central Africa and President, Zimbabwe Economics Society, Harare
Joshua Mushauri, Managing Director, Southern Africa Foundation for Economic Research, Harare
Kevin Kane, BEES, Johannesburg, South Africa
Agrina Mussa, President, Classic Designs Ltd. and Vice Chairman, Malawi Business Women's Association, Blantyre, Malawi
Chris Darroll, Director, Small Business Project, Johannesburg
Donna Stauffer, Program Officer, USAID Regional Centre for Southern Africa
Dale Pfeiffer, Consultant, J.E. Austin Associates, Inc., Harare
Kevin Murphy, J.E. Austin Associates, Inc., Arlington, Virginia, USA

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Report on "Human Resources & Indigenization of the Private Sector" Workshop

January 27, 1996

I. Introduction:

The following outlines the discussion and outcomes of issues identified during the working session of the Focus Group meeting entitled "Human Resources and Indigenization of the Private Sector" held on the evening of January 26, 1996, at the Sheraton Hotel in Harare, Zimbabwe.

II. Background:

Following a regional assessment survey into the constraints to private sector development within the Southern Africa region conducted by J.E. Austin Associates and contracted by the USAID regional office (Botswana), the focus meeting was convened to: (1) offer feedback on the outcomes of the assessment with a particular focus on constraints to human resources development and indigenisation of the economies within the region; (2) provoke response and discussion on the findings of the study; (3) gain a perspective on local initiatives in addressing the constraints; and (4) brainstorm approaches to address these challenges in order to provide direction for a donor strategy.

Accordingly, the group of participants comprised experts within the region. (See list of participants at the end of this section).

III. Issues Raised:

As a general overview, initial discussion revolved around the problems of human resource development and the low representation in the formal private sector of the majority African population in the region. In essence, the following serves to summarize points raised:

In the years following independence within the region, development strategies followed by the independent governments were generally focused toward: (1) continuing cooperation with the economic interests that had been put in place during the colonial era; and (2) expropriation of these interests, through nationalization or other forms of control. Rapid indigenization was also seen as high on the political agendas.

A feature of these approaches was the development of an environment that has, in general, failed to foster indigenous entrepreneurial skills in the formal sector and which has shown a considerable extension of public ownership of new state-owned ventures which have been run on non-business lines and are highly subsidized. Restrictive practices have been kept and in many instances increased to ensure low competition from the private sector, thus favoring publicly-owned enterprises. The uncompetitive nature of the environment within the region (excluding South Africa) and limited local capital accumulation have led to restrictions on the development of an emerging indigenous entrepreneurial class. This has been exacerbated by the retention of many regulatory barriers which affects the growth of the small business sector.

This background was seen as important to the discussion, particularly as the region is only now beginning to emerge from this historical legacy.

In accordance with the above synopsis, a number of key factors were raised during the vigorous discussion. To encapsulate, the following are of note:

A. An interesting overview regarding the Malawian approach (see Country Report in Annex II) was that, following independence, President Banda chose an explicit route not to replace expatriate positions with affirmative action appointments. Consequently, and as opposed to neighbors, Malawi has a history of having the best run civil service in the region. This policy, however, has led to a high level of disenchantment among indigenous groups.

   The policy toward indigenization in Malawi is now focused toward the more formal sector (mainly due to the low level of SME activity), and consequently, disregards an approach towards developing small business as an objective to achieving growth in indigenous business.

   Privatization of parastatals is a critical issue in increasing indigenous ownership. However, access to capital is complex, and approaches regarding the establishment of mutual funds could be seen as a way to address this challenge.

B. In the case of Zimbabwe, a number of interesting points were raised in respect to the principles underlying privatization and indigenization. Regarding the dominance of the public sector in the economy with consumption patterns of the public sector quoted at over 50%, the question raised was: Who has the control? In respect to privatization, the question was: What form would this control take? Simply, "indigenization" is used to promote political agendas, whereas in reality, the indigenization of the economy should be based on market-related policies.

   Another point raised was that it is more the government which continues to crowd out initiatives from indigenous entrepreneurs, rather than the local white population.

   A recent case study regarding the privatization of telecommunications in Zimbabwe illustrates the government's continued dominance (despite rhetoric). Instead of facilitating growth for indigenous business, the government has strongly attempted to control, through unconstitutional means, the "privatization" of the parastatal.

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C. A further critical issue to the impediment of development is the lack of a national consensus to open discussion on private sector growth in Zimbabwe, which has resulted in a lack of vision, and most importantly, constructive debate. Government has an extreme vested interest in the issue of indigenisation and, in addressing this issue, one is seen to be tackling "sacred cows."

D. The confusion and muddle of objectives, that is, privatization for ideological and political reasons as opposed to economic reasons, has created a dichotomy in policy responses. A strong consensus of opinion was that, given the economic picture of the region, the issues of privatization and indigenisation should be separated and consequently dealt with to achieve an overall vision: economic growth.

IV. Summary of Discussion Outcomes:

The following summarizes the points agreed to during the discussion:

A. The underlying pressure within the region is to promote economic growth. Privatization and the issue of indigenisation must be seen to follow this objective.

B. Selling "shares" or developing mutual funds in order to provide access to parastatals would compound an ideological rut. It is a political, rather than a financial or economic, approach. Organizations should be sold to the highest bidder with resources then being reinvested to develop an enabling environment for the growth of indigenous business (particularly small business entrepreneurs). Further, by following economic logic in privatization, viable economic forces will naturally create satellite industries and activities, thus providing a multiplier effect.

V. Conclusions:

Given the above points, the following conclusions are drawn:

A. Following open market principles and involving the majority of the population is crucial for the economic growth of the region. Growth of the small business sector is as important, and may be more so politically, as large-scale investment to achieving this objective.

B. A broader definition and understanding of the "Africanization" concept needs to be realistic and based on pragmatic strategies. The region needs to move away from dominant ideological and political rhetoric.

C. Gender sensitivity, particularly in regard to addressing obstacles faced by women entrepreneurs, is important when developing an overall strategy.

D. Again, the role of advocacy in promoting policy change is critical to a strategy to empower indigenous business within the region.

E. An ethos towards developing an entrepreneurial culture within the region is pivotal, particularly against the backdrop of a burgeoning public service. Programs/strategies to introduce enterprise training into school curricula should be strongly promoted, and likewise, in secondary and tertiary education.

VI. List of Participants:

Strive Masiyiwa, Managing Director, Retrofit Holdings, Ltd, Harare, Zimbabwe
Fletcher Kankhwende, Partner, Deloitte & Touche, Lilongwe, Malawi
Agrina Mussa, President, Classic Designs, Ltd., and Vice Chairman, National Association of Business Women, Blantyre, Malawi
Joe Foromo, Chairman, Confederation of Zimbabwe Industries, Harare, Zimbabwe
Joshua Mushuari, Executive Director, Southern African Foundation for Economic Research, Zimbabwe
Donna Stauffer, Program Officer, USAID Regional Centre for Southern Africa, Gaborone, Botswana
Chris Darroll, Director, Small Business Project, Johannesburg
Kevin Murphy, President, J.E. Austin Associates, Inc., Arlington, Virginia, USA
Dale Pfeiffer, Consultant, J.E. Austin Associates, Inc., Harare

Report on "Trade and Investment" Workshop

January 30, 1996

I. Introduction:

Presented below is a summary of the Focus Group held on the topic of "Trade and Investment" which occurred in Johannesburg at the ESKOM Conference Centre on January 30, 1996.

II. Background:

An unavoidable conclusion of any study of Southern Africa's private sector has to be the status of the trade and investment climate and what potential exists to improve performance in these areas. The studies and interviews conducted in the course of carrying out an assessment of the region's private sector by J.E. Austin Associates, Inc., found that Southern Africa is a highly protected trade area. In terms of attracting foreign investment or encouraging domestic investment, the region also has a number of continuing barriers despite efforts in recent years to promote investment. After the findings of the study were presented to the participants, they were asked to react and give their viewpoints as they represented different countries and, in the case of South Africa, different organizations. All participants were in fact from government organizations. (See list of participants at the end of this section).

III. Issues Raised:

A. It was observed that investment, financing and capital *per se* are not major constraints in the region. Money is available, although perhaps not always as readily accessible as desired. One observer felt that the problem for the region with regard to capital was in fact a lack of "absorptive" capacity. There are too many other barriers to doing business which make it difficult to put available capital to sound use.

B. The main problem area was generally agreed to be that of policy. There is a need to put in place, throughout the region, policy regimes which are comparable to each other; removing disparities will facilitate cross-border business. Most countries are already engaged in policy reform to ensure improved trade and investment regimes, but it was felt that they were really at the beginning stages and that there was a need to have in place a regional mechanism to coordinate such policy development so that the desired comparability is achieved.

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C. It was apparent that there are varying views on the speed of change to open up the region's trade and investment environment. Tanzania's representative thought it should be immediate. But a South African suggested that this would expose the already weak economies to distorted relationships harmful to their development. Zambia was cited as an example of a country which had liberalized too fast and, as a result, was experiencing de-industrialization as imports drove domestic production out of business. South Africa said it did not see it in its interest to be surrounded by poor neighbors, and a more gradualist approach was needed.

IV. List of Participants:

Chris Darroll, Small Business Project, South Africa
Rachel Iafta, University of Stellenbosch, South Africa
Hans van der Merwe, South African Agricultural Union, Pretoria
Michael Leaf, Deloitte & Touche, Johannesburg
J.S. Pienaar, South Africa Agricultural Union,
Riaan Lombard, AHI, Pretoria
Dale Pfeiffer, J.E. Austin Associates, Harare
Roger Baxter, Chamber of Mines of South Africa, Johannesburg
Keith Lockwood, SACOB, Johannesburg

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Report on "Policy" Workshop

January 31, 1996

I. Introduction:

The meeting of the Focus Group to discuss policy constraints to private sector development was held at the ESKOM Conference Centre on January 31, 1996. Eight South African business representatives were present (see list of participants at the end of this section).

II. Background:

Policy is felt by many to be the primary obstacle to business development in Southern Africa. Despite efforts to liberalize the region's economies, there remain numerous policies which inhibit business growth. These affect not only national-based businesses, but those wishing access to the larger regional market. The participants were briefed on the findings of the assessment to date; they then offered their thoughts on the situation.

III. Issues Raised:

A. It was suggested that the difference between Southern Africa and the "Asia miracle" is the absence of strong labor unions in the latter. One outcome of organized labor in South Africa is that to protect unionized textile jobs, policies will make it difficult for small "cut and sew" entrepreneurs. An opportunity will be lost since they could become an asset in export trade in terms of taking advantage of EU and US access to such producers and open new enterprise opportunities.

B. Intra-regional trade policy presents a problem due to a lack of competitiveness among countries of the region. RSA has a 40% unemployment rate. This makes it difficult to lower barriers. An additional problem is that RSA can ship goods to other countries, but these countries have little to export to RSA. These countries need to industrialize first in order to be able to export intra-regionally.

C. RSA policy is still influenced by the apartheid period. It is now trying to become part of the world economy and adjust to economic realities. Meanwhile, numerous South African products are flooding the region. It was suggested that, although South Africa has committed to liberalization, domestic interests dictate a gradual pace. South Africa has signed the GATT and will inevitably achieve free trade in a number of years. Meanwhile, South African business is moving out of the region; this is a real threat to broader integration. In terms of economic adjustment in the rest of the region, it was felt that the various governments had a role to play in alleviating the negative impacts of investment and trade, whether from South Africa or elsewhere, by re-training and helping to identify industry investment niches.

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D. In terms of Southern Africa following the Asian model, it was felt that many countries did not have the resources to invest in the level of infrastructure and services that Asian governments have provided.

E. Harmonization of regulations, standards and improvements in currency exchange procedures in the region were seen as ways to help promote more business and attract investment. The rules of the game need to be known and certain, not arbitrary, and are likely to change over time. Southern Africa needs to be aware that conditions are always changing in the rest of the world and adaptation is crucial. To succeed in the regional context, each country needs to give up authority over such items as trade and tax as part of the harmonization process and the creation of a single market concept.

F. Some felt that a conflict between South Africa and the region might exist because the former is trying to do too much too soon, and its domestic focus at present prevented it from being a full member of the regional club. From the South Africa perspective, there was also doubt as to whether other governments in the region were willing or able to make the necessary changes--and do so with integrity. Governments still do not understand that they have to get their fingers out of the economic pie.

G. The group posed the question: What has happened to infrastructure, basic and industrial? Did policies or management cause the deterioration? Why is Malawi importing wood when it had a capacity to produce and even export in the past?

H. Some participants expressed pessimism with regard to what investment can do in the region. It was also felt that much of the investment thus far has been illusory. It has been dominated by traditional companies coming back. Other international investors may be waiting to see what the political evolution will be in the region.

I. The long-term policy for RSA should be to have vibrant economies in neighboring countries in the region with more participation of the local African majority. Trade develops markets and can then lead to investment in production which would benefit local business. Foreign firms can bring technology, marketing expertise and management skills.

J. Education systems need revamping to reflect the needs of the private sector. Business should make its needs known and try to get school systems to turn out the type of trained individuals that they require for modern production.

K. A voice for the region's business is non-existent. ESABO is non-functional for all intents and purposes. South Africa did start an agricultural group in the region which tried to interface with SADC and national bodies to achieve a change in policy. Some thought that a sectoral approach in business may be better for success in lobbying governments.

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IV. List of Participants:

Ros Thomas, Development Bank of Southern Africa, South Africa
Dale Pfeiffer, Consultant, J.E. Austin Associates, Inc., Harare
E.P.A. Simwela, SADC Industry and Trade Coordination Division, Dar-es-Salaam
Zolelwa Mgungo, Department of Trade and Industry, Pretoria
Sonwabo Mateyisi, Industrial Development Corporation, Sandton
Stephen Thembinkosi Motsa, Ministry of Commerce and Industry, Mbabane, Swaziland
Anthony F. Julies, Department of Finance, Pretoria
Filomena Malalane, Ministry of Industry, Commerce, and Tourism, Maputo
Lolette Kritzinger-van Niekelle, DBSA, South Africa
Bongi Kunene, Department of Finance, Pretoria

Report on "SME Development/Policy Environment" Workshop

February 7, 1996

I. Introduction:

Presented below is a summary of the Focus Group discussion held on the topics of SME Development and Policy Environment, which met in Gaborone at the Grand Palm Hotel on February 7, 1996 (see list of participants at the end of this section).

II. Issues Raised:

A. The most important outcome of this session was the identification of an existing initiative similar to that which had been identified by the team as a useful potential intervention. The "Small Enterprise Promotion Advisory Council," or SEPAC, is a regional grouping of SME organizations started about 18 months ago which meets about every six months to learn from different experiences. The group includes members from all SADC countries except Swaziland, Lesotho and Angola. Also, the group includes representatives from government, the private sector and NGOs or business chambers. It is undertaking a regional directory of small enterprise-oriented NGOs and is seeking to identify expertise in the region. This initiative is financed by the Friedrich Ebert Foundation.

B. The group noted that each country has a different approach to SME development and hence there is much to exchange and learn. Botswana has the Financial Assistance Program (FAB); Zambia has a policy to decrease barriers to entry and may be the best model; and RSA is developing an approach based on interventions by NGOs with the government acting as a wholesaler whereby NGOs bid for financing.

C. On a separate note, the example of Mauritius was cited. One participant had visited the country and came away impressed. He found that not only were the policies good, but that civil servants had a positive attitude towards the private sector and actively spoke of how it helped bring more investment to the country. Civil servants would go out of their way; for example, the Minister of Industry, after checking out a potential investor, would call a meeting with that investor; and key public officials would approve various required licenses and permits and seek to make things happen smoothly. This indicated the need to go beyond good policy and train civil servants to be business and service-oriented, a situation which is not the case in the rest of SADC generally.

D. Also, the use of 5-year plans in the region sets a rigidity which is not conducive to ongoing private sector input and changes in policies to make things work better and adapt to new environments.

E. In Botswana, in particular, it was said that there was a difference in perception between private and public sectors with regard to the enabling environment. On the one hand, government feels it has set up an excellent enabling environment and indeed, the policies are not bad for the region. But there is also the sense that civil servants drag their feet a bit and are not service-oriented (hence the Mauritius example). The private sector is seen as asking for more subsidies or as abusing the incentives which do exist.

III. List of Participants:

Horatoi Mahloane, General Manager, Tswelelo
Eunice Radebe, Director, Business Development
Dr. Derek Hudson, Phaleng Consultants
Dr. Ngo'ngo'la, Lecturer, Law Department, University of Botswana
Andrew Briscoe, Director, Business School of Botswana
Dr. J. Isaksen, Director, Botswana Institute of Development Policy Analysis

ANNEX III-A:
GROWTH WITH EQUITY MODEL (GEM)

GROWTH WITH EQUITY MODEL (GEM ANALYSIS)

Since the mid-1980s, empirical studies of less developed countries have pinpointed the critical factors associated with high and sustained economic growth. By that time, empirical data had become available which allowed an objective study of the causality and correlation between high economic growth and many factors contributing to or impeding that growth. Important analyses by Paul Romer, Jeffrey Sachs, Andrew Warner, Alwyn Young and Mancur Olsen, the World Bank and others have contributed to an understanding of the causes and constraints of economic growth.

A World Bank Policy Research Report, The East Asian Miracle, a major study published in 1993, found that the 23 economies of East Asia grew faster than all other regions of the world between 1965 and 1990. This was mostly due to the performance of eight economies: Japan, Hong Kong, Korea, Singapore, Taiwan, Indonesia, Malaysia and Thailand. These countries achieved high rates of growth while simultaneously improving the distribution of income, thereby laying to rest the old argument that growth with equity was unattainable. The study identifies certain critical factors to explain most of the successful growth with equity. The RCSA MAPS Team leader consulted with the principle author of the above-mentioned World Bank Research Report, John Page. With Dr. Page's assent, the team took material from that report, primarily for four of the Asian eight. This analytical framework was then applied to the data gathered on SAR countries which were the subject of this private sector strategy exercise for USAID/RCSA.

The GEM framework is useful in the context of the RCSA MAPS exercise in four important ways. First, this analysis provides a useful overall economic model for USAID private enterprise development in the region with relevant benchmarks. Second, it pinpoints key strategic interventions which lead to improvements in the key benchmark indicators and shows how these are linked. Third, the study reveals key policy variables which led to high growth-with-equity and which should therefore receive priority attention in the Southern African region (SAR). Fourth, the GEM framework was used in the Focus Groups, and can continue to be used, as a means for promoting policy dialogue, discussion and analysis among stakeholders in the region.

I. PRIVATE ENTERPRISE STRATEGY: THE DEVELOPMENT CONTEXT

The private sector is the engine of growth for the modern economy. It is not surprising that the SAR countries, experiencing flat or slightly negative per capita growth over the last three decades, have poorly developed private sectors. In the case of both the African and Asian economies, independence left them ill-prepared to sustain growth. The situation could hardly be different today. As shown in the following graph, the SAR countries, despite billions of dollars in development assistance, have experienced limited and in some cases negative growth, while the High Performing Economies (HPEs), many of whom saw development assistance dry up shortly after independence, have enjoyed sustained growth rates exceeding 5.5 percent per year on average.

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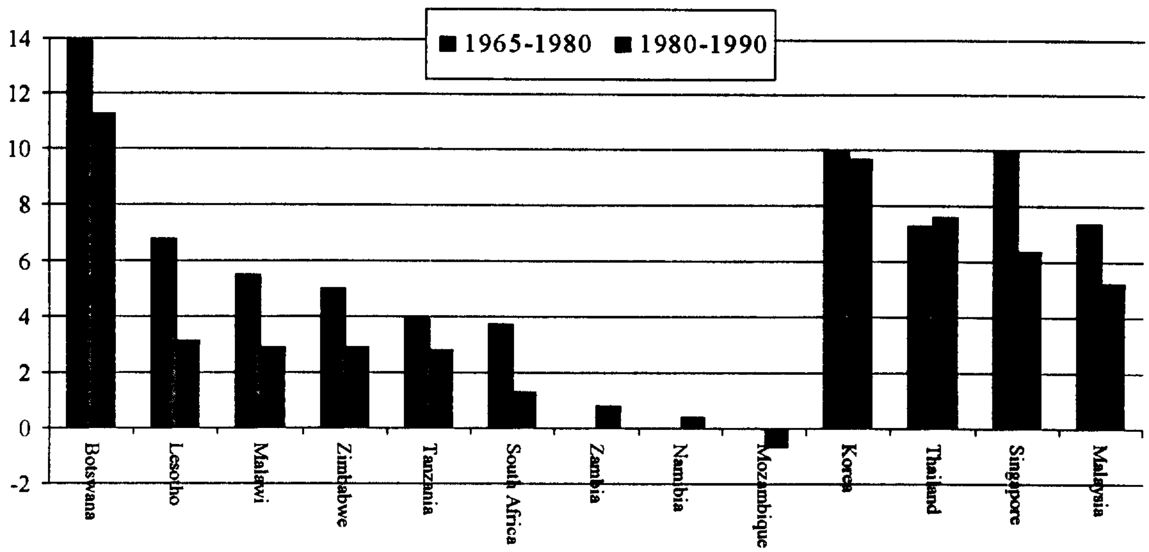
Table 1

Growth of Production, Average Annual Rate: % GDP



Source: Relevance of Asian Experience to African Problems, pp. 45-46

Private enterprise development must be seen in the context of an overall economic development strategy which has as its ultimate result the objective and measurable improvement in the human condition. One critical component of overall development is economic growth which not only expands human welfare in its own right but empowers individuals and the society to more effectively achieve broader development objectives such as health and education. Sustained and broad-based economic growth, it has been shown, can best be promoted through a strong private enterprise sector. Furthermore, a strong private enterprise sector helps to achieve developmental objectives beyond economic growth such as a decentralized economy fostering civil society.

Development objectives cover the broadest levels of improvement in the overall human condition as measured by a variety of economic and social indicators. Most institutions have adopted basic indicators similar to those in the Physical Quality of Life Index (PQLI), first presented by the Overseas Development Council in the 1970s. These, or others that are similar, present the ultimate test of human progress. The high-performing economies (HPEs) of East Asia serve as benchmarks for successful achievement of these ultimate, if imperfect, indicators of human advancement (spanning the period 1960-1989).

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HPE ECONOMIC AND SOCIAL INDICATORS

Life expectancy rose to 69 years
Infant mortality declined to 33 per 1,000
Literacy improved to 87 percent
Rapid, sustained economic growth, 5.5% real per-capita growth for 30 years
Equality of income distribution of 8.8, measured by the ratio of income shares of the richest 20 percent and poorest 20 percent for Korea, Singapore, Thailand and Malaysia

Comparable indicators for the SAR region during the same period are:

SAR ECONOMIC AND SOCIAL INDICATORS

Life expectancy of 54 years
Infant mortality of 98 per 1,000
Literacy of 68 percent
Economic growth, less than 1% real per-capita growth over 30 years
Equality of income distribution of 17.5, measured by the ratio of income shares of the richest 20 percent and the poorest 20 percent for Botswana, Lesotho, Tanzania, Zimbabwe and Zambia - SAR countries for which data were available

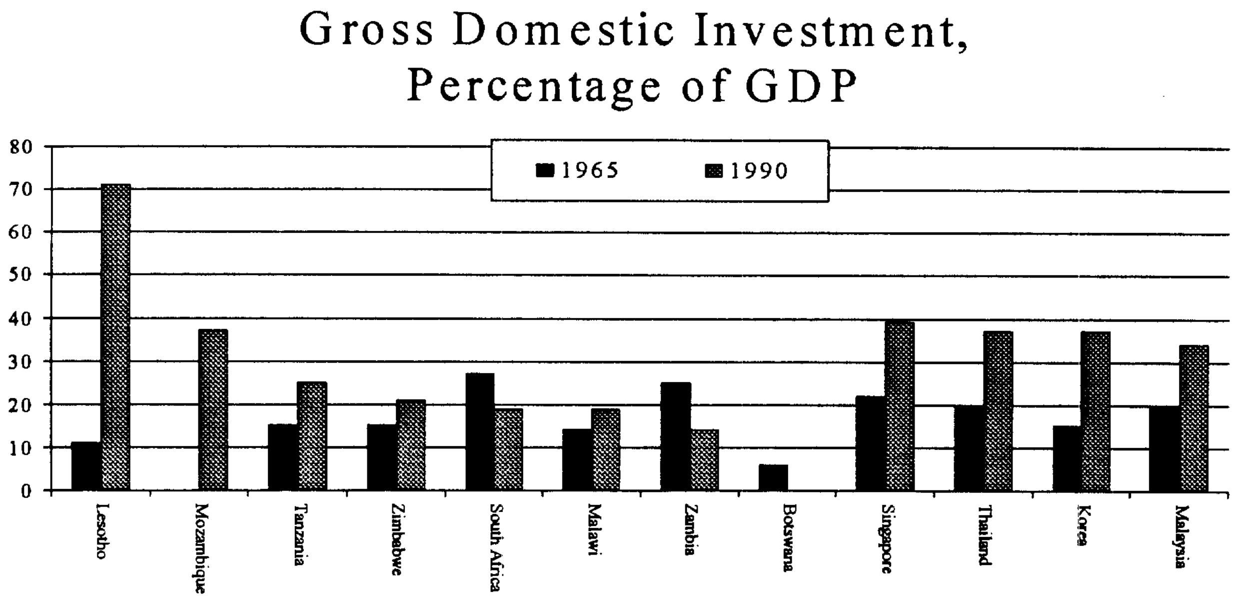
II. SUSTAINABLE ECONOMIC GROWTH AND PRIVATE ENTERPRISE

The Growth with Equity Model developed from the World Bank analysis points to three critical factors explaining rapid and sustained growth in Asia: 1) the **level of investment**, particularly private sector investment; 2) **human capital** as measured by functional literacy and the age of school-leaving; and 3) **total factor productivity**. These, in turn, are a function of favorable government policy and a general openness to market forces.

The overall economic policy environment must be conducive to investment. The conditions must be present to provide an adequate return to investors and the policy environment must be stable. Private investors will seek investment opportunities which minimize risk for a given return. If the economic policy environment is perceived to be unstable, investment decisions will be distorted towards opportunities elsewhere or towards opportunities which hold potential for high returns over a short period. This distortion may not lead to sustainable economic growth.

The above graph shows that in the 1960s the countries of the SAR region had very low rates of gross domestic investment (GDI). For most countries, there has been an improvement in the level of investment since the 1970s. The proportion of GDP devoted to investment is now approaching the levels seen in the Asian countries. While the total level of investment is important, the portion of total investment in the private sector was significantly higher in the Asian countries. The Asian countries averaged private sector proportions of total domestic investment on the order of 65

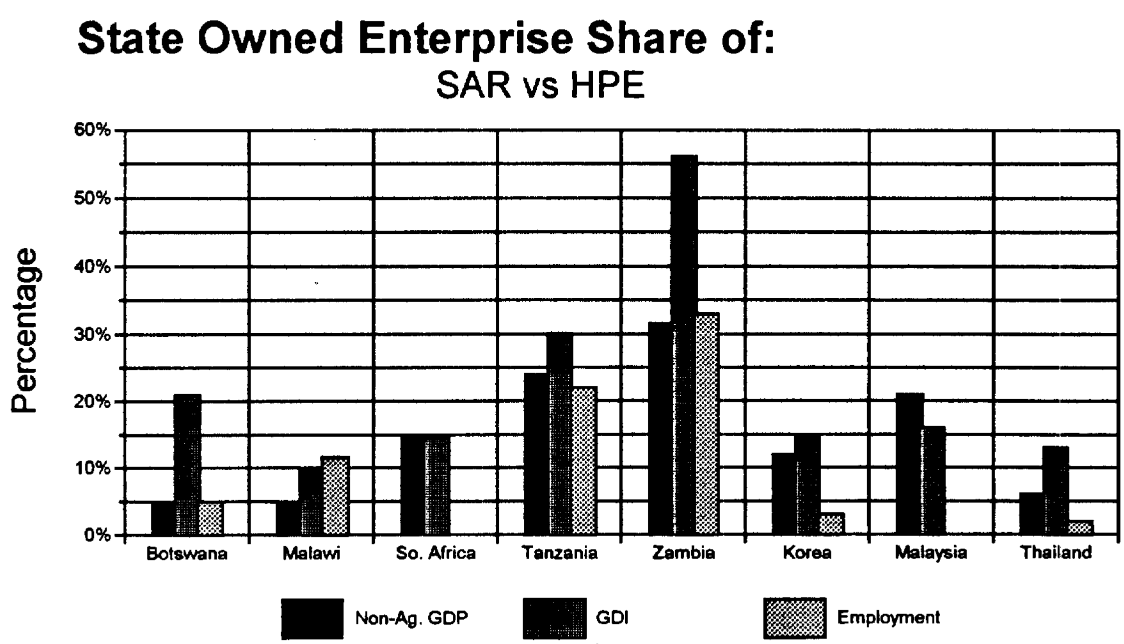
Table 2



Source: Relevance of Asian Development Experiences to African Problems, pp.55-56

percent or higher, while in the SAR region, levels varied from less than 20 percent in Tanzania to over 70 percent in South Africa. The flip side of private sector investment is the role of state-owned enterprises in the economy. The following graph shows the dominant role of SOEs in some of the SAR countries as of 1993:

Table 3



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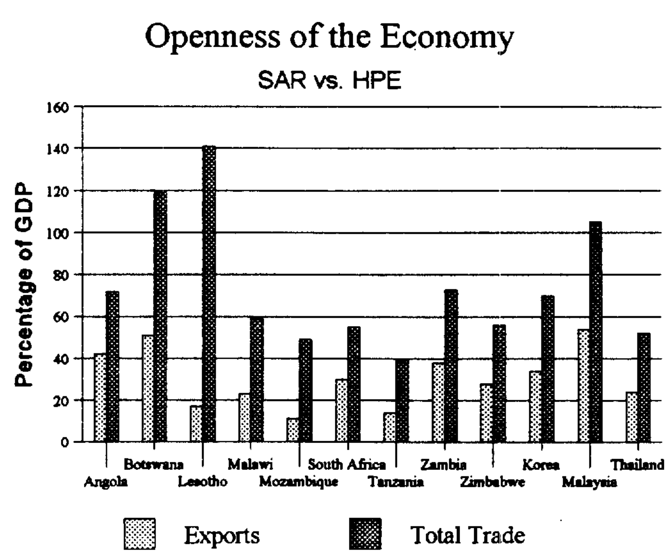
A number of studies have shown that SOEs tend to be inefficient (World Bank, *Bureaucrats in Business*, 1992). It appears that those SOEs in the Asian countries are more efficient than their African counterparts. As the data presented in the above graphs show, despite employing far fewer workers and utilizing a smaller share of gross domestic investment, the SOEs of Korea, Malaysia and Thailand contribute roughly the same proportion to non-agricultural GDP as the African SOEs.

Scarcity of capital alone may not be the critical bottleneck to sustainable growth. A recent study led by Mancur Olson of the University of Maryland showed that capital and knowledge are being "massively squandered in many poor countries" (Economist, May 25th, 1996, pg. 25). He contends that it is not more resources that are needed by poor countries. Rather, it is essential that they waste less of those resources they already have at their disposal. As noted in the constraints analysis, the main component of this report, the overall level of investment in the SAR countries over the last 20 years does not appear to be too low. A detailed analysis of the issues contributing to the apparent low productivity were beyond the scope of this study.

Investment levels and investment quality are influenced by economic policy. Investment in open free-market economies will be channeled to different sub-sectors than in command economies. Harvard's Dr. Jeffrey Sachs and Andrew Warner analyzed 111 countries which they classified as "open" (i.e., pursuing broadly free-market policies particularly with respect to trade liberalization and maintenance of secure property rights) and "closed." The open economies achieved much higher levels of sustained growth. The World Bank study on the high-performing East Asian economies confirms these findings. Economic policy is a critical determinant of the level of private investment, the quality and productivity of that investment and the improvement in human capital. The graph below measures the openness of the economies of the SAR and HPEs by comparing trade with GDP:

Table 4



Imports may be stimulated by overvaluedexchange rates and financed by foreign assistance. Likewise, exports are often hindered by export taxes and regulatory burdens, reducing their competitiveness. Lesotho is a case in point. While exports as a proportion of GDP are generally lower in the African countries than in Asia, total trade openness approaches the same level. Indeed, trade is only one indicator of openness. The Heritage Foundation study, which is contained in Annex IV-B, offers additional measures of the openness of the region based on an analysis of a number of policy variables.

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1. High Level of Savings and (Private) Investment

The "Asian 8" had savings and investment rates of over 30% of GDP between 1965-1990, and more importantly, rates of private investment of 15-20% of GDP during the same period. The absolute level of savings and investment was found to be important, but less important than might seem to be the case at first. While high growth countries saved and invested high percentages of GDP, so did many centrally planned economies, yet growth rates were quite different. How the savings are invested is also very important. It is this aspect which highlights the importance of private investment. "The Asian 8" had sustained levels of private investment significantly higher than other developing countries. Public investment levels, on the other hand, did not differ markedly until the 1980s when many of the other developing countries were experiencing structural adjustments resulting in curtailed public investment. The studies by the World Bank and others confirm, and are supported by the findings of a number of MAPS exercises, which demonstrated that investment levels were not the principle cause of low economic growth. For example, USAID/Nairobi in 1989 initially based a private sector strategy on the assumption that the most critical factor was raising investment levels. The MAPS study revealed that investment levels had not historically been that low as a percentage of GDP. Rather, there was a quality of investment problem that more investment would not remedy.

Relevant indicators (1965-1990) for the "Asian 8" for the critical factors mentioned above are:

Savings and Investment Rates over 30% of GDP
Private Investment Rates of 15-20% of GDP
Productivity Growth, per capita GDP growth of 5.5% per year

Comparable indicators for SAR region during this period are:

Savings and Investment Rates, savings ranged from less than 10% of GDP in 1965 to only 2 percent in 1990, while investment ranged from 16% of GDP in 1965 to nearly 30% in 1990 for the region
Private Investment Rates range from 6% of GDP in Malawi to 16-18% in Tanzania and Zimbabwe-1986-92
Productivity Growth, per capita GDP growth of less than 1% per year

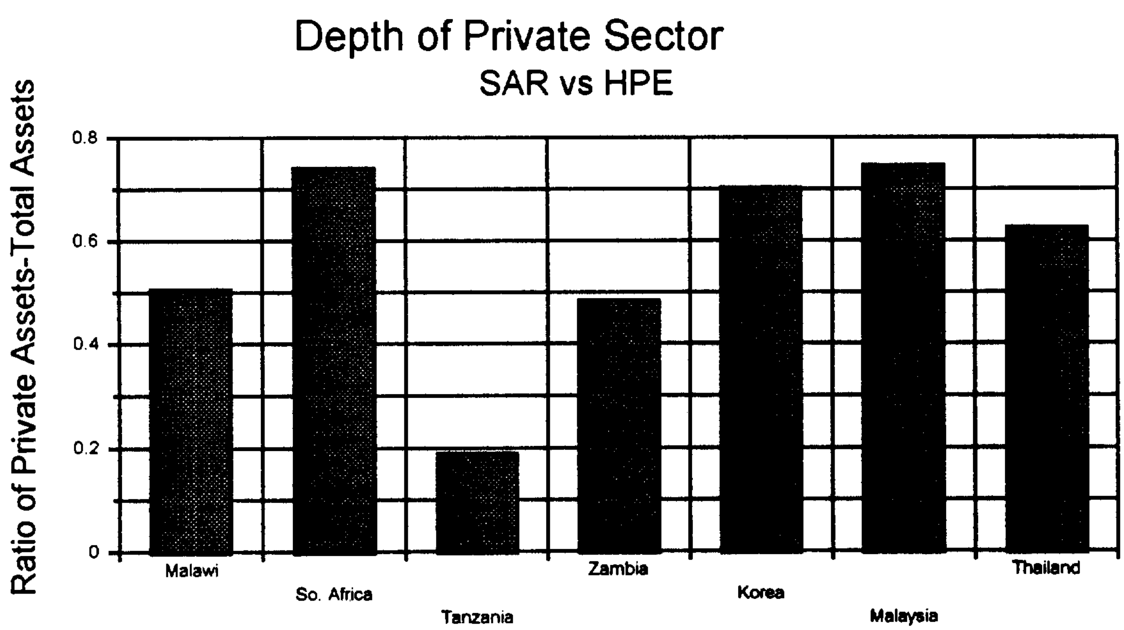
Today, a number of the countries of the region have public and private investment as a proportion of GDP approaching rates of the Asian countries. However, as mentioned elsewhere, the quality and apparent productivity of investment in SAR countries is significantly lower than the Asian HPEs. Savings is, of course, enhanced by rapid economic growth. Government policy may also encourage increased savings. Maintenance of macroeconomic stability will induce people to save. Sound and functioning financial markets and financial institutions are also a requirement. Low rates of inflation, influenced by prudent public spending policies, will have a positive impact on savings. If private savings are too low, government can generate public savings.

The depth of the private sector may be measured by comparing the ratio of private assets to total assets in the economy. The following graph displays this ratio for those countries for which data were available. With the exception of Tanzania, there were no sharp differences among the African and Asian countries between 1965-1990. Data were, however, not available for several of the countries which have had significant parastatal establishments during the period covered.

2. Emphasis on Human Capital

The second factor positively influencing the rate of economic growth mentioned by the World Banks study was human capital. Theodore W. Schultz was among the first economists to emphasize the importance of human capital to economic development. In <u>Transforming Traditional Agriculture</u> (1963), he posited two theses: "the acquired capabilities of farm people are of primary importance in modernizing agriculture and these capabilities, like capital goods, are produced by means of production." Acquired capabilities are not given at birth but require investment. Paul Romer' s path-breaking work in 1986 also highlighted the importance of human capital.

Table 5

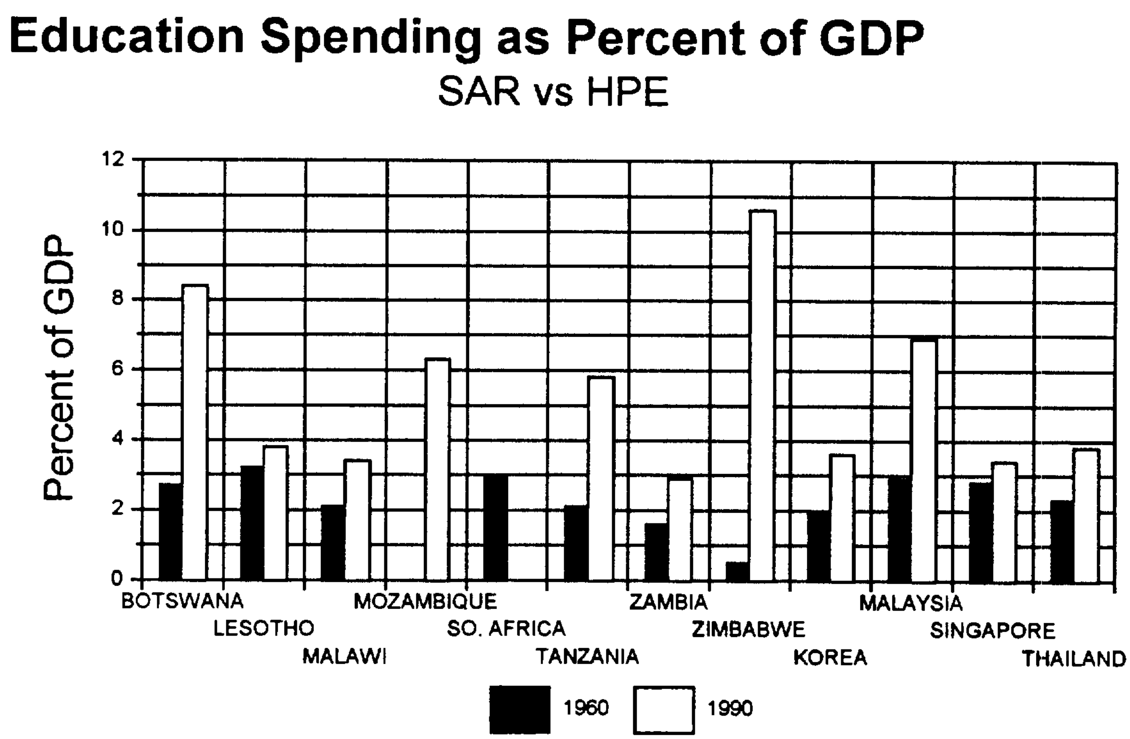


Literacy, as measured by the average year of school-leaving, explains an important part of the high growth performance of Asian countries. The gap between SAR and East Asian countries in literacy is particularly notable. Forty percent of the SAR population is functionally illiterate, compared to less than 8 percent among four emerging Asian economies.

Increases in primary and secondary enrollment were also found to explain a significant percentage of the above-average growth rate among Asian economies. While human capital formation contributes to rapid economic growth, growth makes the investment in education possible. For example, during the decade 1970-80, annual GDP growth averaged 8.3 percent in Singapore and 3 percent in Tanzania. This implies that, over the decade, a constant share of GDP allocated to education per year would have more than doubled the resources available in Singapore, while in Tanzania they would have increased by only one-third.

The amount of national income devoted to education cannot fully explain the larger accumulation of human capital in the "Asian 8." In both 1960 and in 1989, the percentage of GDP spent on education was not significantly different in the "Asian 8" (2.5% and 3.7% respectively) compared to Sub-Saharan Africa (2.4% and 4.1% respectively). Also surprising, the allocation of total public expenditure towards basic education (versus university or secondary) has been relatively similar in both the "Asian 8" and SAR countries over time (slightly more than 40%).

Table 6



As the graphs on the following page demonstrate, the major difference between the two regions appears to be twofold: 1) the *quality* of investment (as measured by the student/teacher ratio) is significantly lower in the SAR region; and 2) the average age of school-leaving is much lower in SAR countries than in the "Asian 8." As an important indicator of educational quality, the percentage difference in student/teacher ratios between East Asia and SAR countries widened significantly from 16% in 1965 to over 45% by 1992, according to most recent UNESCO data. The SAR region averaged roughly 42 students per teacher in 1992, versus a 24:1 ratio in East Asia. Furthermore, a much lower percentage of SAR students continue to the 4th grade level as compared to their East Asian counterparts (77% versus 100%). Thus, they are ill-equipped to make productive contributions to economic growth.

Education is both a goal of development and a major contributor to sustained growth. The interaction works both ways in a virtuous cycle of mutually reinforcing incentives. An expanding economy offers incentives and opportunities for educated people and thus increases the demand by the population for education and the effort exerted to increase education levels. But higher education levels also have a highly positive impact in generating further economic growth through better productivity.

Table 7

EDUCATION SUMMARY TABLE	SAR Average	HPE Average
% of Cohorts Persisting to Grade 4 (Female/Male) 1970	81/81	97/97
1988	78/77	99.7/99.5
Educational Expenditure as % of GDP: 1960	2.03	2.5
1992	6.15	4.4
% of Education Budget Spent on: Primary	42.6	41.3
Secondary	29.2	33.6
% of Adults Literate	60	92
% Enrolled in First Grade	90	96
% Completing Primary Level	62	96
Student to Teacher Ratios: 1965	50:1	44:1
1992	42:1	24:1

Source: World Development Report, World Bank, 1994.

3. Rapid Productivity Growth

The third critical factor found to correlate highly with strong economic growth in Asia was rapid improvement in productivity. Productivity is a measure of overall efficiency. The interesting characteristic of the "Asian 8" is that as the total amount of capital being employed in these economies grew, the efficiency with which that capital was utilized also improved. This is in contrast to much of the conventional wisdom which assumes diminishing returns.

Total factor productivity is the increase in productivity that cannot be accounted for by increases in inputs. Total factor productivity, thus, is a complex phenomenon dealing with intangible elements such as economic organization, innovation, absorption of technology, and the interaction among ideas, technologies and business strategies. Data on total factor productivity are difficult to acquire. However, as pointed out above, the apparent productivity of investment in the SAR countries lags that of the HPEs. What is not clear from this information is how much of the gap is attributable to input accumulation, technology, human capital or intangible factors. Clearly, apartheid, civil war and socialist policies distorted investment funds and created an unfriendly climate for foreign investment. Furthermore, labor in the region is not as well prepared as in Asia in terms of technical and managerial skills. The region has a large segment of the economy operating in the informal sector which also has an impact on investment decisions and overall productivity. General lack of openness and continued obstacles to foreign investment may also indirectly influence total factor productivity levels in SAR countries.

Rapid productivity growth is evident in the figures on per capita GDP (average of 5.5 percent in East Asia). Per capita growth depends primarily on rising output per worker. Some of this increase is due to increases in physical capital and some is the result of increased human capital. In the "Asian 8," about two-thirds of sustained economic growth is attributable to the rapid increase in physical and human capital inputs. The remaining one-third is attributable to increased efficiency. Increased efficiency is the result of better technology, better organization, gains from specialization, openness to market forces and innovation.

III. THE IMPORTANCE OF SOUND POLICY

The most critical determinants of savings, private investment and productivity are related to government policy. Specifically, the most important policy determinants of the high levels in the above-mentioned categories, as demonstrated by the East Asian experience, are the following:

Restrained government budget deficits
Low to moderate inflation
Controlled external debt
Stable, market-driven exchange rates
Quick and market-led responses to external macroeconomic shocks
Open economies with an emphasis on an export-push strategy
Effective and secure financial systems
Low price distortions
Facilitation of entry and absorption of foreign technology
Bias against agriculture avoided

These policies led to a stable and predictable environment for investment, universal primary and secondary education, sound and solvent financial institutions, and secure property rights. Public investment created infrastructure complementary to private investment. Tax policies favored savings and investment. High tariffs were avoided on imported capital goods. Taxes were used as a development tool and incentive. Fiscal deficits were managed and a low debt to

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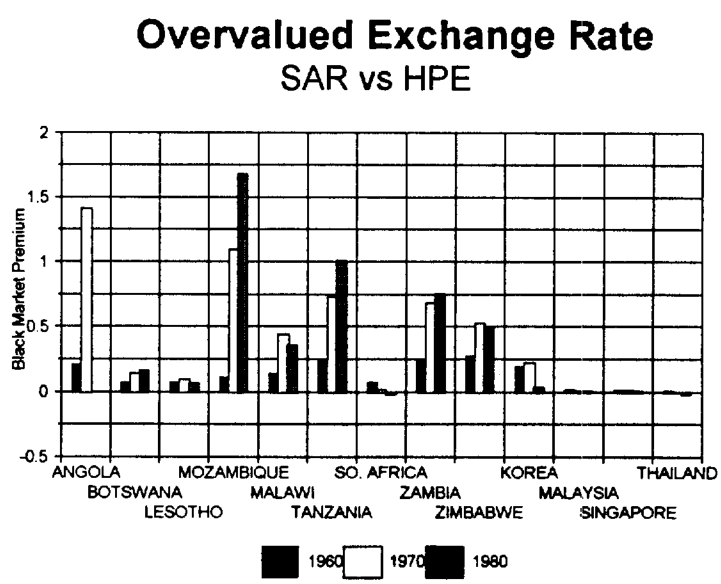
export ratio was maintained. Additionally, competitive real exchange rates were maintained and normally reflected market conditions. The economy was supervised by a technocratic elite which received political support. When external shocks hit, such as the oil crisis, quick adjustments occurred.

The authors of the World Bank report on the Asian economies found that three major policy areas were most important in explaining the rapid rate of growth.

The first of these was stable, market-based exchange rates. The graph below provides available data on the "black market premium" exchange rate in SAR countries. It is obvious that most SAR countries have had a strong tendency over the last three decades to maintain overvalued exchange rates, especially when compared to the Asian countries. An overvalued exchange rate hinders exports, making them more expensive in foreign currency terms, and encourages imports by making them less expensive than they would be otherwise, often at the expense of domestically produced goods.

The second policy area which is highlighted by the World Bank study involves the development of the financial sector. Well-functioning financial markets are extremely important if the incentives which encourage savings and provide investment financing are to be transmitted throughout the economy. As mentioned above, savings and investment were critical to fostering the rapid economic growth experienced by the Asian economies.

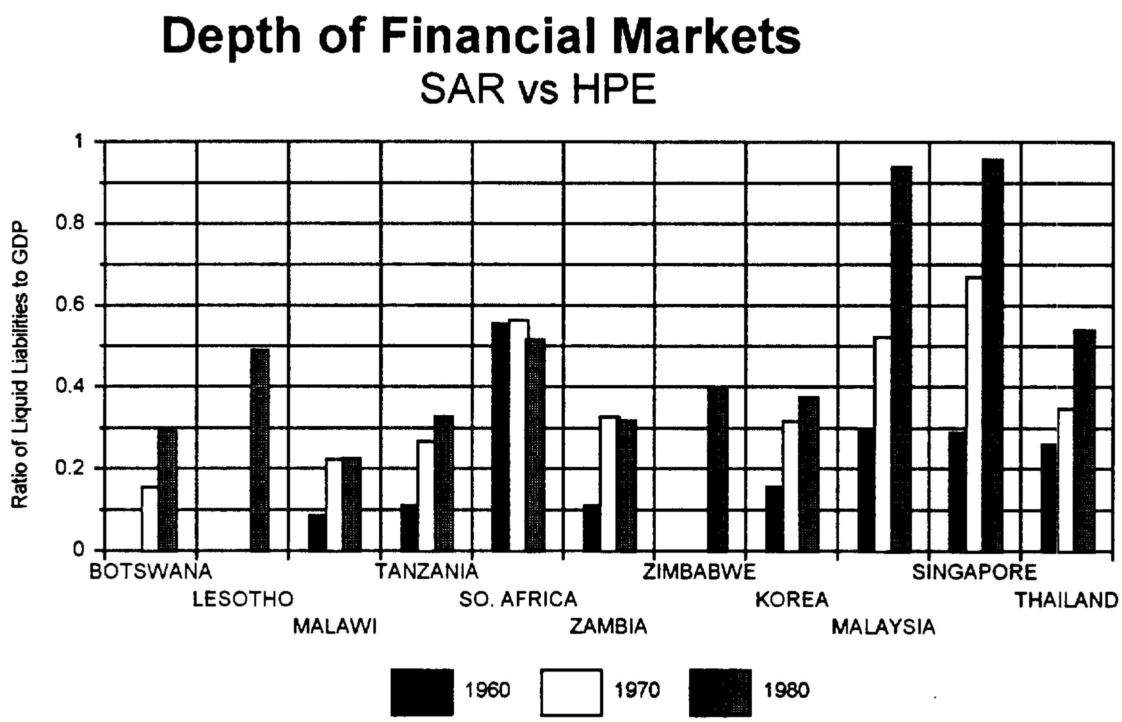
Table 8



Financial markets not only mobilize savings and allocate funds to competing investments, but they also monitor performance. If firms are forced to rely on retained earnings for investment because financial intermediation does not function due to financial market failures, economic growth will be significantly reduced. The Asian economies had policies which promoted savings and investment. As these economies matured, bond and equity markets were created and improved. Most of the Asian countries also had development banks to ease the constraints of long-term capital markets and to provide financing to agriculture. The governments of many Asian economies also designed a number of mechanisms to increase the attractiveness of private foreign investment.

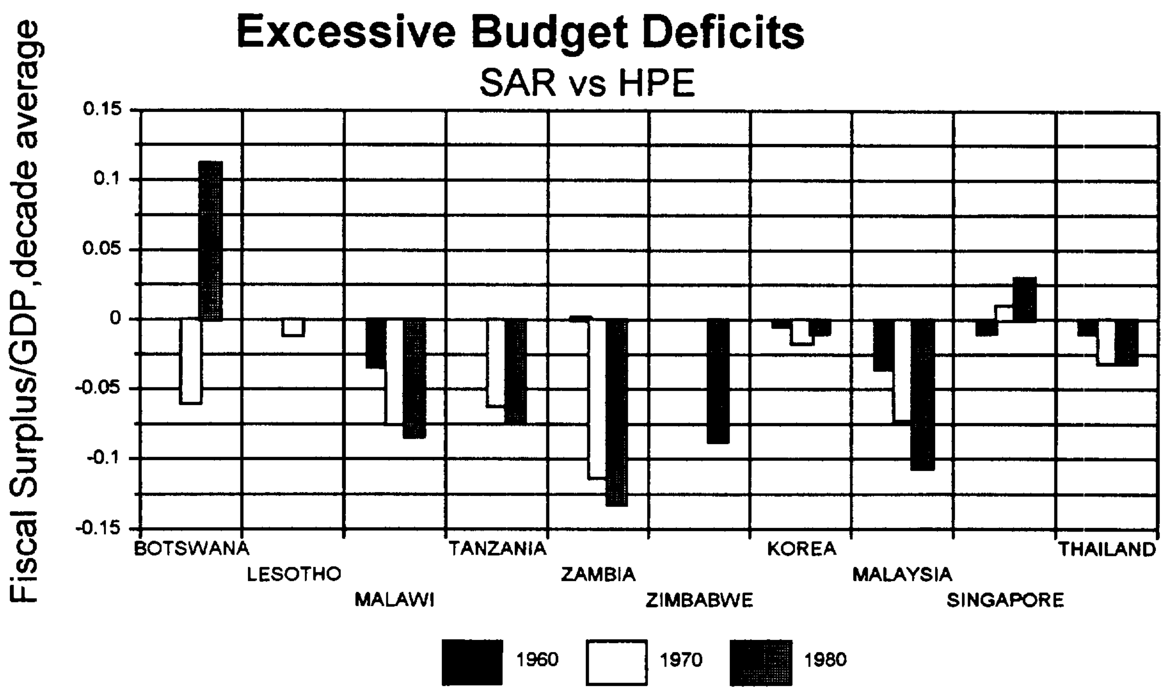
Real interest rates for most countries of the SAR region have tended to be negative over the last 20 years, providing incentives to invest outside the region. Many of the countries also maintained monetary policies which promoted high rates of inflation. Average inflation rates ranged from 12 percent in Botswana to 42 percent in Mozambique. In Asia, only Korea experienced double digit inflation. Both interest and inflation rates impact financial markets. Real interest rates must be attractive in order to encourage savings. Additional analysis of the financial sector is provided in **Annex V.**

Table 9



The third critical macroeconomic policy failing is an excessive government budget deficit. The graph on the following page provides data on the fiscal surplus in relation to GDP for the SAR and Asian economies over the last three decades. Here, the difference between the African and Asian economies is not so clear. Most of the Asian countries were sustaining deficits during the period covered by the data. The main difference is that the economies of these countries were sufficiently large so as to absorb such deficits without detracting from economic growth. Deficit spending on the part of the government is certainly one of the major factors fueling inflation. High rates of inflation, in turn, impact on financial markets and levels of investment. High rates of inflation increase the cost and risk of business activity and thus serve as a strong disincentive to private investment, both domestic and foreign.

Table 10



V. IMPLICATIONS FOR USAID/RCSA STRATEGY

Comparing the SAR with the high-performing Asian economies clearly demonstrates that a gap as measured by per capita GDP has significantly widened over the last thirty years. This analysis also clearly highlights the critical importance of sound economic policy for providing the basis for the performance in Asia. The above analysis provides benchmark data for a number of critical variables at various levels of concern: country level, strategy level and activity level, based on the SAR data and with reference to the high performance targets achieved by high-growth countries.

The analysis also demonstrates that policy is an important constraint, perhaps the most important constraint, to rapid and sustained economic growth and should thus play a central role in any strategy seeking to alleviate the principal constraints to private sector development in Southern Africa. It has also provided an overall conceptual model for private enterprise development in the context of overall development strategy.

It is important to note that the lessons of East Asia must be applied with caution. Economic development models which prove successful in one region cannot be adopted blindly in another without appropriate modification to suit local conditions. East Asia's rise cannot be understood apart from the political, historical and sociocultural context in which economic development occurred. Thus, prescriptions for growth in SAR countries based on findings from other regions must be tailored to the unique circumstances in which SAR private and public sector actors operate. This is critical for the sustainability of donor interventions.

ANNEX III-B:
COMPARATIVE POLICY ANALYSIS

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INTRODUCTION AND EXECUTIVE SUMMARY

This Comparative Policy Analysis is designed to assist the USAID Regional Center for Southern Africa (RCSA) in developing a strategy for promoting private enterprise in the southern Africa region. It can also be used as a contribution by USAID to stakeholders in the region who share the USAID goal of helping the countries of the region to achieve rapid, sustained, broad-based economic growth.

The methodology used in this study incorporates categories similar to those presented in the policy matrix developed by Dr. James Austin in the late 1980s. It was chosen from among many existing methodologies because it is comprehensive and easy to follow.

After reviewing the policy analysis work of many sources, two complementary approaches for assessing the overall policy environment in southern Africa were chosen: 1) the Growth With Equity Model; and 2) the Heritage Foundation Index of Economic Freedom. The Growth With Equity Model (GEM) is a comparative policy tool devised by J.E. Austin Associates based upon a recent World Bank study on the high-performing East Asian economies. These high-performing economies demonstrated that economic growth can be congruent with an equitable distribution of income. Economic growth, fueled by the private sector, has also contributed to an improvement in various non-economic measures of development in these countries over the last decade, including higher life expectancy, reduced infant mortality, better health and sanitation, and increased educational attainment (especially for women). The Growth With Equity Model provides useful non-economic benchmarks for evaluating growth. Removal of specific constraints to private enterprise will promote overall economic growth which, in turn, will lead to gradual improvement in broader, non-economic objectives.

Although controversial because of its conservative reputation, the Heritage Foundation Index of Economic Freedom is the only current comparative policy tool which is both comprehensive and updated annually. Thus, it serves as a useful complement to the Growth With Equity Model for the purpose of this MAPS exercise.

The analysis in this Annex shows that countries in the region still have policies poorly suited to the goal of stimulating private sector growth. If the region were one country, it would rank in only the 29th percentile (101 of 142 countries for which the methodology has been applied). Intriguingly, the GDP of the region is about 25% of the world average - an interesting correlation. Thus, there is a much room for progress. Interviews in the region corroborated that government policies were the single largest impediment to private sector growth. In the absence of a commodity boom, the region is unlikely to achieve high rates of growth in income per capita unless significant policy changes are made.

However, the team analyzed findings from two separate reports done two years apart. The analysis showed improvement in policy reform. The policy environment in the southern Africa region ranks slightly higher than sub-Saharan Africa in general and is improving at a slightly faster pace.

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Among 10 policy areas which were rated, the region scored worse in the area of trade policy. The region continues to live within a protective cocoon. On the other hand, investment policies were shown to be much more favorable. This review was confirmed by interviews, which revealed greater eagerness for liberalizing investment regimes than trade regimes.

Botswana has the most pro-private enterprise policies while Angola and Mozambique, with legacies of civil war and Marxist control, were still the most anti-free enterprise. However, Mozambique made the most year-to-year progress since 1990. Zimbabwe has one of the least attractive sets of policies. Some counter-intuitive results are noted. Countries such as Zambia, rank higher than other countries which have stronger historical commercial development, such as Zimbabwe. Zambia recently reformed its statist economy while Zimbabwe continues to protect certain industries and maintain significant state influence.

After presenting the objectives, methodology and key findings, a detailed examination of the policy situation in each country is presented, along with a bibliography of information sources utilized. It is hoped that this study can contribute to dialogue and to the search for initiatives which can result in sustained and participatory economic growth.

I. OBJECTIVE

This study is one component of the MAPS exercise conducted by J.E. Austin Associates for the U.S. Agency for International Development Regional Center of Southern Africa (USAID/RCSA). The general objective of this analytical study is to assess and compare the investment and business policy environment within the eleven member countries of the Southern African Development Community (SADC) - Angola, Botswana, Malawi, Mozambique, Lesotho, Namibia, South Africa, Swaziland, Tanzania, Zambia, and Zimbabwe.[1]

The specific objectives are:

1. To analyze policy constraints to private sector development in the Southern Africa region;

2. To provide USAID with baseline data for a bench marking system to assess policy trends based on sources which will be updated in the future;

3. To stimulate dialogue among stakeholders;

4. To contribute to the development of private sector action strategies;

5. To make a useful contribution by USAID/ RCSA to stakeholders in the region.

In addition, it also offers an evaluation of appropriate methodologies which can again be used to help the Center's staff to develop their own practical, easy-to-follow methodology for tracking commercial policy development.

Mauritius became a member of SADC after this study was commissioned.

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II. Overview of Methodology

The team surveyed available primary and secondary material on policies of the region. The team then reviewed methodologies for analyzing and ranking policy reform and evolution. Information and analytical methodologies were reviewed from an extensive set of studies collected by the team. These included: 1) the Multilateral Investment Guarantee Agency-sponsored IPA*net* (via the Internet); 2) Economist Intelligence Unit country reports for the third and fourth quarters of 1995; 3) the 1995 and 1996 Index of Economic Freedom published by the Heritage Foundation ; 4) Ernst & Young Country Investment Profiles (via the Internet); 5) a report by SRI International entitled "Commercial Policy Model Application: Southern Africa"; 6) the 1994 Encyclopedia Book of the Year; 7) selected articles from the September-October 1995 edition of "The Courier: Africa-Caribbean-Pacific-European Union" magazine; 8) the World Bank Cross Border Initiative; and 9) material provided by embassies.

The first methodology used in this Annex is the Policy Impact Matrix developed by Dr. James E. Austin and presented in Managing in Developing Countries. This methodology shows not only which policies affect the private sector, but also where in the company they make their impact. It is presented below to show the impact points between government policy and the day-to-day operations of private firms. However, it was not deemed appropriate to try to use this as the principle analytical tool because the Policy Impact Matrix has not been applied to all countries of the region, nor is it guaranteed that such an exercise would be repeated regularly as a source of benchmark data for the mission.

Business Environment Policy Impact Points

		Company Impact Points[b]			
Category	Instrument	Finances	Marketing	Production	Organization
Monetary	interest rates (A)[a]	x			
	loans (O)	x			
Fiscal	tax rates (L)	x			
	investment credits (L)	x		x	
	govt. sales (O)			x	
	govt. purchases (O)		x		
Incomes	price controls (A)		x		
	wage controls (A)	x			x
Trade	tariffs (A)	x	x		
	import quotas (A)		x	x	
	export incentives (L)	x	x		
	exchange rates (A)	x	x		
Foreign investment	ownership requirements (L)	x			x
	repatriation limits (L)	x			
	personnel regulations (A)				x
Sectoral	technology licensing (A)	x		x	x
	production licensing (A)			x	x
	SOE operations (O)	x	x	x	x

a Types of policy instruments: L = Legal; A = Administrative; O = Direct Market Operations
b Management control aspects of each of the four functional areas could also be affected.
Source: Austin, James E., Managing in Developing Countries: Strategic Analysis and Operating Techniques, 1990.

An effort was made to identify a methodology which had the analytical rigor of the Policy Impact Matrix, was applied to all countries of the region, and would be repeated on a regular basis. To respond to USAID's request to identify sources for future benchmarking, the team incorporated J.E. Austin's Growth With Equity Model and the Heritage Foundation's Index of Economic Freedom, which appear suitable to the aims of this exercise. Both approaches are outlined separately in this Annex.

The team realizes that the Index of Economic Freedom is controversial and that the sponsor is identified with particular political and economic viewpoints. Nonetheless, the Index can be used as an initial measuring tool without the user having to adopt all of the positions of the sponsoring institutions. For example, the team modified the categories with less strident terminology. This analytical tool was deemed more suitable than other surveys reviewed for the following reasons:

- as the Index reviews 142 countries worldwide, it is quite comprehensive[2] ;
- the Index is relatively up-to-date, having been finished in November, 1995, and is updated every year;
- the Index's methodology was comparatively easy to understand and follow, which fit with the team's goal of providing a practical and easy to comprehend analysis;
- the methodology covers 10 policy categories yet lends itself to the addition of further categories of analysis which can be developed by regional stakeholders to influence policy debate.

In addition, extensive research with the other materials mentioned above was conducted to cross-check the findings of the Heritage Foundation Index. Where more recent information was identified, it was substituted. Where subjective analysis from consultant visits to the region's countries and discussions with private and public sector representatives intimated different findings than shown in the Index findings, the report reflects those differences.

The thirty-two countries included in the Sub-Sahara Africa analysis include: Angola, Benin, Botswana, Burkina Faso, Cameroon, Cape Verde, Congo, Ethiopia, Gabon, Ghana, Guinea, Ivory Coast, Kenya, Lesotho, Madagascar, Malawi, Mali, Mauritania, Mozambique, Niger, Nigeria, Senegal, Sierra Leone, Somalia, South Africa, Sudan, Swaziland, Tanzania, Uganda, Zaire, Zambia, and Zimbabwe. The eighteen countries included in the Asia analysis include: Bangladesh, China, Hong Kong, India, Indonesia, Japan, Laos, North Korea, Singapore, South Korea, Taiwan, Thailand, Malaysia, Myanmar, Pakistan, Philippines, Sri Lanka, and Vietnam. The eighteen countries included in the Latin America analysis included: Argentina, Belize, Bolivia, Brazil, Chile, Columbia, Costa Rica, Ecuador, El Salvador, Guatemala, Guyana, Honduras, Nicaragua, Panama, Paraguay, Peru, Uruguay, and Venezuela.

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The team sought to provide a snapshot of current policy and a ranking of countries. It also sought to compare the region with Sub-Saharan Africa and with other regions. Furthermore, since two such studies have been done over time, the team sought to analyze change over time. Analysis of those policies which ranked highest and lowest in the region was also conducted based on the data from the two studies which were conducted at one-year intervals. The team also looked at the region in a global context and provided a composite ranking as if the region were a country.

Reliance on any one source for an area such as policy is risky. Also, things are changing quickly in the region. Therefore, this analysis should be used as a point of departure and not as the definitive indicator of policy efforts or progress. Policy evolution is a complex phenomenon that is difficult to reduce to a number. Readers are encouraged to review the findings of this report with the caveat that they use this analysis as the beginning of their research and not as the sole basis for decision.

Private Enterprise Policy Analysis and Grading Scale

Categories of analysis used by the Index of Economic Freedom included: Trade Policy, Taxation, Government Consumption of Economic Output, Monetary Policy, Capital Flows and Foreign Investments, Banking, Wage and Price Controls, Property Rights, Regulation, and Parallel Market activity.

The grading scale for each policy area assessed runs from 1 to 5, 1 signifying pro-free enterprise policy and pro-private sector commerce policies, and 5 denoting a restrictive environment and anti-free enterprise and anti-private sector commercial policies. Following each score is a "+", "-", or "stable" mark which signifies the direction in which the country's policies are moving - improving, declining, or remaining steady. Countries receiving a score of 1.99 or less are considered to have policies that are definitely pro-free enterprise and economies that are for the most part open to international trade. Countries with scores of 2.00 to 2.99 are considered to have policies that are moderately pro-free enterprise and economies that are relatively open. Countries with scores of 3.00 to 3.99 are considered to have policies that are primarily anti-free enterprise and economies that are comparatively closed. Countries with scores of over 4.00 are considered to have policies that are definitely anti-free enterprise and economies that are closed. The category titles used by Heritage Foundation are somewhat more polemical: "free, mostly free, mostly unfree, and repressed." We have taken the liberty of making these slight changes in category titles. Also, we have referred to "parallel market" rather than their terminology of "black market."

The Index's grading scale was utilized to assess 142 countries, developed and developing. Most of the developing countries, including those in Africa, scored in the high two's, three's, and above. These scores, static as they are, offer only a snapshot of the development of these countries politically and economically, and as a result do not necessarily reflect the significant improvement in the commercial policies in some of these countries since 1990.

Below, the key factors and methodologies presented in the Index are summarized.

Factor #1: Trade Policy

A country's trade policy (i.e., how high its tariffs are and how many artificial trade barriers are permitted) is a key factor in measuring a county's commitment to free enterprise. Trade policy is also a key factor in industrialization of developing economies as it allows for the free transfer of needed technology, services, and products. In light of this, the degree to which a government hinders the free flow of international commerce has a direct bearing on economic growth. International trade also enables a country's industries to maximize production by allowing them to import raw materials and foreign goods and services that are cheaper than those produced at home. In a reverse sense, open trade policy can also offer a country greater access to the world market via reciprocal trade agreements.

Methodology: The average tariff rate is used to score a country's trade policy. A score of 1 through 5 is given based on a country's tariff rate - the higher the tariff rate, the worse the score. References from which to determine the average tariff were derived from reports issued by the International Monetary Fund and General Agreement on Tariffs and Trade. When the average tariff rate was not available in these sources, the Heritage Foundation authors determined the average rate by calculating the revenue raised from tariffs and duties as a percentage of total imports. With additional research undertaken for this report, most of the average tariff rates are valid for at least 1994, and in some cases 1995. Notwithstanding best efforts, however, in some instances, adequate tariff figures did not exist. Additionally, the Index authors used publications from the U.S. Trade Representative's office, the U.S. Department of Commerce Department, and the State Department to supplement their research. In this area, non-tariff barriers such as overly strict licensing, trade quotas, or import inspections are also examined. If such barriers were sufficient in quantity, a country's score based solely on tariff rates was moved one point higher on the scale, representing decreased private sector opportunity and free enterprise-fostering policies.

Grading Scale:

Score	Levels of Protectionism	Criteria
1	Very low	Average tariff rates less than 4 percent and/or very low non-tariff barriers.
2	Low	Average tariff rate 5 percent to 9 percent and/or low non-tariff barriers.
3	Moderate	Average tariff rate 10 percent to 14 percent and/or moderate non-tariff barriers.
4	High	Average tariff rate 15 percent to 19 percent and/or high non-tariff barriers.
5	Very high	Average tariff rate 20 percent and higher and/or very high non-tariff barriers that virtually close the market to imports.

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Factor #2: Taxation

A country's tax rate is a key factor in assessing its government's commitment to free enterprise. While every country taxes economic activity to pay for public health, national defense, and other vital government services, too much taxation stifles the business environment, international trade, and entrepreneurship. A tax can be viewed as a government-imposed disincentive to perform the activity being taxed. For this reason, the higher the tax the greater the disincentive and the greater the barrier to economic growth. When analyzing this factor, taxes on corporate profits, income, and other significant activities are measured.

Methodology: Two types of taxation are scored: corporate taxes and income taxes. Each country was first scored based on these two major types of taxation, which many economists agree have the most negative economic impact on individuals. These scores were then averaged to get a single taxation score. Then, other taxes such as state and local taxes, sales taxes, and value-added taxes also were examined. If these taxes existed in sufficient quantity, a country's taxation score was moved one-half point higher on the scale, representing a decrease in the country's commitment to free enterprise. This one half-point increase represents the relative impact of these other taxes on private sector development.

1) Income Taxes

To discover the average income tax rate, a country's total gross domestic product was divided by total population. This per capita income figure was then used to determine which rate applies to the average income level. Once this was done, easy country was scored on 1, top tax rate, and 2, the tax rate that applies to average income.

Income Tax Grading Scale

This scale lists a score from 1 through 5. The higher the score indicated, the higher the tax. The highest level for which a country qualifies is the score that the country receives.

Score	Tax Rates	Criteria
1	Very low taxes	No taxes on income; flat tax rate on income of 10 % or less.
2	Low taxes	A top tax rate of 25 percent or flat income tax of 10-20% percent. A top rate of 40 percent or below, but average tax below 10%.
3	Moderate taxes	A top tax rate of 35% or below; or average tax below 15%.
4	High taxes	A top income tax rate of 36%-50% and an average level of 15-20%.
5	Very high taxes	A top rate above 50% and average income tax of between 20 -25%. A tax rate on average income of 25% or above regardless of the top rate.

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2) Corporate Taxes

The second type of tax analyzed is the corporate tax. Each country is scored according to a sliding scale based on corporate tax rates.

Corporate Tax Grading Scale

Score	Tax Rates	Criteria
1	Very low taxes	Considered a tax haven. Limited or no taxes are imposed on corporate profits.
2	Low taxes	Flat corporate tax less than 25 percent or a progressive top tax of less than 25 percent.
3	Moderate taxes	A progressive corporate tax system with top rate between 26 percent and 35 percent, or a flat tax system with levels above 25 percent.
4	High taxes	A progressive corporate tax system with a top rate between 36 percent and 45 percent.
5	Very high taxes	A cumbersome progressive tax system with top corporate tax rates above 46 percent.

Factor #3: Government Consumption of Economic Output

The greater degree to which the government is involved in the economy, the fewer actors in the private sector are free to engage in commercial activity. By taking government consumption as a percentage of gross domestic product, the level of government consumption of economic output can be determined. The higher the rate of the government consumption as a percentage of gross domestic product, the higher the Index score, and hence the lower the country's policy commitment to free enterprise.

Methodology: Measuring a country's government consumption as a percentage of GDP approximates the government's role in the economy. The government consumption figure includes resources allocated for servicing government budget deficits and transfer payments, through funding of health care and other public services. However, government consumption figures for most less developed countries, including most of those in the southern Africa region, do not include funds spent on servicing the budget deficit and transfer payments. While using government consumption figures probably understates the total government intervention in the economy, it is a useful tool and starting point for gauging the degree of government intervention in the economy.

Grading Scale

Score	Level of Government Consumption of Economic Output	Criteria
1	Very low	Less than 10 percent of GDP
2	Low	11 percent to 25 percent of GDP
3	Moderate	26 percent to 35 percent of GDP
4	High	36 percent to 45 percent of GDP
5	Very high	46 percent or above of GDP

Factor #4: Monetary Policy

Throughout the world, the value of a country's currency is based significantly on that government's monetary policy. If a government maintains a tight monetary policy, meaning the supply of currency does not exceed demand, individuals have an economic incentive to engage in productive and profitable economic activities. If the government maintains a "loose" monetary policy, meaning it supplies more money than demand requires, money loses its value and individuals are discouraged from engaging in productive and profitable economic activities. The best way to measure monetary policy is to analyze a country's inflation rate over a period of time. The inflation rate is directly linked to the government's ability to manage the supply of money in the economy.

Methodology: The average inflation rate was the main criteria for this factor. The inflation rate is the best measure of how a country manages its money supply. Countries with high inflation rates have a loose monetary policy and are graded higher because they have a less conducive environment to private sector enterprise than countries with lower inflation rates. Countries with a low inflation rate have a tight monetary and are graded lower because they have a more disciplined and conducive environment from a monetary policy standpoint.

Grading Scale

Score	Inflation Rate	Criteria
1	Very low	Below 6 percent
2	Low	Between 7 percent and 13 percent
3	Moderate	Between 14 percent and 20 percent
4	High	Between 21 percent and 30 percent
5	Very high	Over 30 percent

Factor # 5: Capital Flows and Foreign Investment Policy

Globally, attracting foreign investment is a critical component to stimulating a country's economic expansion. Investors from abroad supply capital, technology and know-how to domestic partners who then start or expand their businesses. Restrictions on foreign investment hamper economic freedom and thus limit the inflow of foreign capital. By contrast, few or no restrictions on foreign investment enhances a country's commercial attractiveness and helps increase the flow investments. For this category, the more restrictions a country imposes on foreign investment, the higher the score, and hence the lower the country's commitment to free enterprise and private sector development .

Methodology: A country's foreign investment policies were reviewed and analyzed in order to assess the overall investment climate. Questions asked included the following: Are there foreign ownership limits placed on domestic industries? Does the government encourage foreign investment by providing tax holidays or other incentives? Is there an existing foreign investment code that defines the country's investment laws and procedures? Are foreign corporations treated under the law the same as domestic corporations? Are specific industries closed to foreign investment? The answers to these questions helped the Index authors develop an overall description of the investment climate of the country being examined. Each country was graded based on its investment climate.

Grading Scale

Score	Barriers to Foreign Investment	Criteria
1	None	Investors are encouraged to invest through tax holidays and other incentives and allowed to invest in almost any industry.
2	Low	Restrictions on investments like utilities, companies vital to national security and natural resources.
3	Moderate	Restrictions on many investments, but government policy conforms to established foreign investment code.
4	High	Investments permitted on a case-by-case basis.
5	Very high	Government actively seeks to prevent foreign investment.

Factor #6: Banking

Access to capital and private financial institutions are catalysts of economic growth in most countries. Banks in particular are important as they lend money to start businesses, provide services such as real estate, insurance, and securities investments, and furnish a safe place for individuals to store their earnings. The more governments control banks, the less these institutions are able to engage in these useful activities. Heavy regulation of banks restricts economic opportunity and stunts commercial growth. Thus, the more a government restricts its banking sector, the higher the Index score it received.

Methodology: This factor is measured by determining the openness of a country's banking system. The questions asked in assessing this policy area included: Are foreign banks able to operate freely? How difficult is it to open domestic banks? How heavily regulated is the banking system? Are banks free to provide customers with insurance, sell real estate, and invest in securities? The answers to these questions were used to develop a description of the country's banking climate. The Index represents a sliding scale that measures the relative openness of a country's banking system.

Grading Scale

Score	Restrictions on Banks	Criteria
1	Very low	Very few restrictions on foreign banks. Banks can engage in all types of financial services Government controls few, if any commercial banks. No government deposit insurance.
2	Low	Few limits on foreign banks. The country may maintain some limits on financial services and have interstate banking restrictions and deposit insurance. Domestic bank formation may face some barriers.
3	Moderate	Barriers to new bank formation. Heavy influence on banks by government. Government owns or operates some banks. Strict government control of credit. Domestic bank formation may face significant barriers.
4	High	Banks tightly controlled by government. Corruption may be present. Domestic bank formation is virtually nonexistent.
5	Very High	Financial institutions in chaos. Corruption is rampant.

Factor #7: Wage and Price Controls

A government which promotes free enterprise and encourages international investment is one that allows private sector players to set not only the prices on the goods and services they sell, but also the wages they pay to the workers they employ. However, many governments mandate wage and price controls. By doing so, they restrict economic activity, and thus curtail commercial activity. Indeed, the more a government intervenes and controls prices and wages, the higher the Index score and the lower the government's commitment to economic growth via private sector development.

Methodology: This factor is measured by how much a country lets the market or the government set wages and prices. Among specific questions asked: Are there any products whose prices are set by the government? If so, which products? Does the government affect prices by controlling such things as utilities? Does the government have a minimum wage policy? Are other wages set by the government? A sliding scale is developed to measure the relative degree of government control over wages and prices. A 1 or "very low" score represents wages and prices being set completely by the market, whereas at the other end of the scale, a "very high" score of 5 means that wages and prices are set completely by the government.

Grading Scale

Score	Wage and Price Controls	Criteria
1	Very low	Wages and prices determined by the market. No minimum wage.
2	Low	Most prices determined by supply and demand. Some prices are determined by the government or monopolies such as utilities. May or may not have minimum wage laws.
3	Moderate	Mixture of market forces and government determined wages and prices or heavy government control of either prices and wages.
4	High	Rationing, wage and price controls on most jobs and items.
5	Very high	Wages and prices completely controlled by the government.

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Factor #8: Property Rights

In a country which supports free enterprise and encourages capitalism, the accumulation of private property is one of the main motivating forces in the economy. This factor examines the extent to which private property is protected by the government and how safe it is from expropriation. The less protection private property receives, the higher the score, and hence the lower the country's commitment to free enterprise.

Methodology: The degree to which private property is a guaranteed right is measured. So, too, is the extent to which the government protects and enforces laws to protect private property. The probability that the state will expropriate private property also is examined. The less legal protection of private property, the higher the score. The higher the chance of government expropriation of private property, the higher the score.

Grading Scale:

Score	Protection of Private Property	Criteria
1	Very high	Private property guaranteed by the government, and efficient court system enforces contracts. Adequate justice system to punish those who unlawfully confiscate private property. Expropriation not likely.
2	High	Private property guaranteed by the government, but enforcement is lax. Expropriation is unlikely.
3	Moderate	Government recognizes some private property rights, such as land, but property can be nationalized. Expropriation possible.
4	Low	Property ownership is limited to personal items with legal protection. Communal property is the rule. Expropriation likely, and the government does not adequately protect private property.
5	Nonexistent	Private property is outlawed. Everything belongs to the people or the state. Expropriation is certain, or the country is so corrupt and chaotic that property protection is nonexistent.

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Factor #9: Regulation

In many less developed economies, obtaining a business license to sell a good or service is very difficult. With many bureaucratic obstacles for the entrepreneur to overcome, it is very difficult to create new businesses. In some cases, government officials frown upon private sector initiative and it may even be illegal. While there are many regulations that hinder business, the most important ones are those associated with licensing new companies and businesses. Often, once a business is open, that is not necessarily the end of government regulation. In some cases, it is just the beginning. Some countries apply their regulations in an inconsistent manner. Business owners become confused over which regulations must be obeyed. Moreover, the existence of many regulations can cause corruption as confused and harassed business owners try to work around the red tape.

Methodology: The purpose is to measure how easy or difficult it is to open a business. The more regulations on business, the harder it is to open. In addition, the degree of corruption was examined, as whether the regulations are applied uniformly to all businesses. Another factor was whether the country has any state planning agencies that set production limits and quotas. The scale was established by listing a set of conditions for each of the five possible scores. These conditions include such items as the extent of government corruption, the uniformity of regulatory applications, and the extent to which the regulations pose a burden on business. At one end of the scale is the 1 score of very low levels of regulation, where corruption is nonexistent and regulations are minimal and uniformly applied. At the other end of the scale is the "very high" score of 5, where corruption is rampant, regulations are applied randomly, and the general regulation level is high.

Grading Scale

Score	Levels of Regulation	Criteria
1	Very low	Corruption-free. Existing regulations are straightforward and applied uniformly to all businesses. Regulations are not much of a burden to business.
2	Low	Simple licensing procedure. No bribes. Existing regulations are relatively straightforward and applied uniformly most of the time. However, regulations prove to be a burden to business in some instances.
3	Moderate	Existing regulations may be applied haphazardly and in some instances are not even published by the government. Complicated licensing procedures. Regulations are a substantial burden to business. A significant state-owner sector exists. However, bribes are not customary.
4	High	Government-set production quotas and state planning. Major barriers to opening a business. Complicated licensing process, very high fees, bribes sometimes necessary. Regulations a great burden to business.
5	Very high	Government discourages new business creation. Bribes mandatory. Regulations applied randomly.

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Factor #10: Parallel Market

Parallel markets are often a direct result of too much government intervention in the market. Parallel market activities are those which a government has outlawed or made prohibitively difficult to engage in. The larger the parallel market is in a country, the lower the business community's confidence in that government's policies relating to the formal market. The smaller the parallel market, the higher the support and confidence in the government's economic policies. This factor considers the size of a country's parallel market as a percentage of GDP. The higher the percentage, the higher the score and the lower the country's commitment to free enterprise.

Methodology: Information available on the size of parallel markets in less developed countries is extremely scarce. Nevertheless, estimates can be made on the size of parallel market activities by answering several questions. For example, does the country have a large smuggling market? If so, this could be an indication that the parallel market to buy such items as televisions and video-cassette recorders? If so, this could be an indication that these products cannot be bought in stores legally or that their prices are too high because of very high tariffs. Are there large numbers of workers who work illegally? If so, this could be an indication that the economy is overly regulated and that labor must be supplied by the parallel market.

The existence or absence of these and other activities was used to estimate the size of the parallel market as a percentage or gross domestic product. In cases where parallel market information exists for specific countries, it is noted. At one end of the scale is the score of 1, where the parallel market constitutes less than 10 percent of GDP. At the other end is the score of 5, where the parallel market makes up 30 percent or more of GDP.

Grading Scale

Score	Parallel Market Activity	Criteria
1	Very low	Parallel market makes up less than 10 percent of GDP. Economies with this ratings are free markets with parallel markets in such things as drugs, weapons and prostitution.
2	Low	Parallel market makes up between 11 percent and 15 percent of GDP.
3	Moderate	Parallel market makes up between 16 percent and 20 percent of GDP.
4	High	Parallel market makes up between 21 percent and 30 percent of GDP.
5	Very high	Parallel market is equal to more than 30 percent of GDP.

III. KEY FINDINGS

Taking two years of comparable data, the team highlighted the relevant 11 countries, analyzed each one, compiled a composite score for the region, measured change over time, and also analyzed rankings for types of policies on a regional basis. The team also created composite scores for not only the SAR region but also (for comparative purposes) Sub-Saharan Africa, Latin America, and Asia.
The following are the results of these analyses.

If the SAR region were a country, it would rank 101 out of 142 entries, scoring only in the 29th percentile relative to the rest of the world. The region is well below average in terms of its policy environment. Coincidentally, the economic performance as shown in a companion study to this presentation showed the region performing at about 25% of the world average. While this is probably coincidental, poor policy undoubtedly causes poor results. This is confirmed by the constraints analysis which summarized 200 studies and 100 interviews in the region and also pointed to policy obstacles as the leading constraint to private sector growth.

Among SAR countries, Botswana performed best (47th overall) and Angola worst (133rd out of 142). Botswana also had the best ranked policies for all of Sub-Saharan Africa. It has also been the top economic performer in the region over the last 30 years. Angola and Mozambique scored lowest in part because of their legacy of war and Marxist-based socialism. After these two special cases, Zimbabwe scored lowest in terms of having a pro-free enterprise economy.

The SAR region improved its overall ranking slightly from 1994 to 1995. In 1995, the composite score showed improvement in the policy environment. Mozambique showed the greatest improvement, followed by Botswana which already scored well the year before. Most countries in the SADC region either saw their scores remain stable or improve. Only Zimbabwe lost ground. Despite its relatively advanced industrialization, it has had problems controlling inflation. Bigger companies in Zimbabwe also appear to be opposed to efforts to open the country's markets and reform its economy.

Zambia scored relatively well (2.95) in the survey, in light of recent major policy reforms. Yet, unemployment is exceptionally high in Zambia, and the country's structural adjustment program has neither created a high growth economy nor a favorable investment environment. Tanzania had a worse score (3.45) although the team found entrepreneurial activity to be flourishing and local businesspeople are positive about the economy. Progress may be occurring in spite of the policy environment. Entrepreneurship itself may push the policies forward. The findings demonstrate the difference between entrepreneurial policy and entrepreneurial culture. There are inevitable lag times between policy reform and results.

SAR countries scored best in the area of Wage and Price Controls (2.9) and scored relatively well in the areas of Government Consumption (3.0) and Property Rights (3.0). Nonetheless, our visits to the region indicated that the tradition of communal land holding limited clear title to real estate property, further limiting access to credit for entrepreneurers who lack such land for collateral.

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SAR countries scored worst in the area of openness to Trade (4.4). The region still lives within a protective cocoon, sheltering itself from innovation and competition and depriving consumers of the best goods at the most competitive prices.

The highest score within the group in any category was 2.0, with Botswana and Zambia having four 2.0s (Monetary Policy, Banking, Property Rights and Parallel Markets for Botswana, and Government Consumption, Foreign Investment, Banking, and Wage and Prices for Zambia). Swaziland gained three 2.0s (Government Consumption, Monetary Policy, and Property Rights) as did South Africa (Foreign Investment, Wage and Prices, and Regulation), and Namibia one 2.0 (Monetary Policy).

SAR is improving slightly faster than Sub-Saharan Africa as a whole. In comparison to Sub-Saharan Africa overall (including the SADC countries), the SAR region tied the continent's score for 1995 and did better than its 1996 score, indicating a slightly faster movement toward open markets and free enterprise in Southern Africa than elsewhere on the continent. Sub-Saharan Africa as a set remained stable in 1996.

Mozambique registered the biggest improvement in its policy environment between the 1995 and 1996 surveys for the Index (1995-4.40: 1996-4.05; + 0.35). Continued improvement in the political and economic situations in Mozambique and Angola will help prospects for the region improve significantly, as these are the only two countries in the region which had overall scores in the 4.00+ range.

Compared to Asian and Latin American countries, the countries of the SADC region compared most favorably in the area of Wages and Prices (2.9:2.4:2.9, respectively). Overall, the SADC countries scored closest to those in the Asian region, registering identical or similar scores in the following areas: Taxation (SADC 3.6: Asia 3.7); Foreign Investment (SADC 3.1: Asia 3.0); Banking (SADC 3.1: Asia 3.1); and Regulation (SADC 3.6: Asia 3.8). Compared with the Latin American region , the SADC countries scored better in the area of Monetary Policy (SADC 3.5: LA 3.8) and close to the region in the area of Property Rights (SADC 3.0 : LA 2.7); Regulation (SADC 3.6: LA 3.3); and Parallel Markets (SADC 3.8: LA 3.7). Government Consumption was significantly lower in the former regions in comparison to the SADC countries (1.7:2.5:3.1, respectively).

The charts below present the scores of the countries of the region as assembled by the team from the Index data for two years. They also indicate the trend year-to-year. A composite score is given for the SAR region for each of the 10 policy areas showing which are most pro-free enterprise and which are most anti-free enterprise in the region. After this, a series of 10 charts provide greater detail for all countries in each of the 10 policy areas. Finally, the team ranked the composite scores of the individual countries. A commentary for each chart is provided.

Chart 1: FREE ENTERPRISE POLICY RANKINGS

Scale 1-5: (1) Pro-Free Enterprise - Anti-Free Enterprise (5)
[0-1.99 Pro-Free Enterprise, 2-2.99 Mostly Pro-Free Enterprise
3-3.99 Mostly Not Pro-Free Enterprise, 4-5.00 Anti-Free Enterprise]

Rank Country	Trade	Taxation	Govt.. Consum-ption	Mone-ary Policy	Foreign Invest-ment	Banking	Wage\ Prices	Property Rights	Regul-ation	Parallel Market	1995	1996	Trend
#47 Botswana	4	3	4	2	3	2	3	2	3	2	3.05	2.80	+ 0.25
#57 Swazi-land	4	3	2	2	3	3	3	2	3	4	2.90	2.90	Stable
#62 Zambia	3	3.5	2	5	2	2	2	3	4	3	3.05	2.95	+ 0.1
#66 South Africa	5	4	3	3	2	3	2	3	2	3	3.00	3.00	Stable
N/A Namibia	4	3.5	3	2	2.5	3	3	3	3	4	N/A	3.10	N/A
#90 Malawi	4	4	3	3	3	3	3	3	4	4	3.40	3.40	Stable
#94 Tanzania	5	3.5	3	4	3	3	2	3	4	4	3.5	3.45	+ 0.05
#110 Lesotho	4	4.5	3	3	3	4	4	3	4	4	N/A	3.65	N/A
#112 Zimbabwe	5	4	3	4	4	3	3	3	4	4	3.50	3.70	- 0.20
#127 Mozam-bique	5	3.5	3	5	4	4	3	4	4	5	4.40	4.05	+ 0.35
#133 Angola	5	3.5	4	5	4	4	4	4	5	5	4.35	4.35	Stable
SADC Average	**4.4**	**3.6**	**3.0**	**3.5**	**3.1**	**3.1**	**2.9**	**3.0**	**3.6**	**3.8**	**3.50**	**3.40**	**+ 0.10**
Sub-Saharan Africa	**4.5**	**4.0**	**3.1**	**2.9**	**3.1**	**3.5**	**3.1**	**3.2**	**3.8**	**4.1**	**3.50**	**3.53**	**- 0.03**
Asia	3.6	3.7	2.5	2.4	3.0	3.1	2.9	2.7	3.8	3.4	2.80	3.11	- 0.31
Latin America	3.7	3.1	1.7	3.8	2.2	2.5	2.4	2.7	3.3	3.7	3.32	2.91	+ 0. 41
#1 Hong Kong	1	1.5	1	2	1	1	2	1	1	1	1.25	1.25	Stable
#7 U.S.	2	4	2	1	2	2	2	1	2	1	1.90	1.90	Stable
#15 Japan	2	4.5	1	1	3	3	2	1	2	1	1.95	2.05	- 0.10

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The chart below ranks the ten policy areas from "most pro-free enterprise" to "anti-free enterprise." The results of this SADC ranking demonstrates that the most "anti-free enterprise" policy area is that of trade (4.4). The region continues to operate within protective borders, sheltering its producers from competition and its consumers from better products at lower prices. It is this area in which the SADC region is revealed to be most behind.

However, there is a more liberal policy when it comes to investment (3.1), and this dichotomy is mirrored in the interviews with South African policy makers who continue to prefer a liberalized investment regime in SADC prior to a liberalized trade regime.

SADC Policy Ranking

Rank	Policy Area	Score
#1.	Wage/Prices	2.90
#2.	Government Consumption	3.00
	Property Rights	3.00
#4.	Banking	3.10
	Foreign Investment	3.10
#6.	Monetary Policy	3.50
#7.	Regulation	3.60
	Taxation	3.60
#9.	Parallel Market	3.80
#10.	Trade	4.40

IV. POLICY SUMMARIES

TRADE POLICY SUMMARY

Rank	Country	Score	Assessment
1.	Zambia	3 +	Moderate level of protectionism
2.	Botswana	4 Stable	High level of protectionism
2.	Lesotho	4 Stable	High level of protectionism
2.	Malawi	4 Stable	High level of protectionism
2.	Namibia	4 Stable	High level of protectionism
2.	Swaziland	4 Stable	High level of protectionism
3.	Tanzania	5 Stable	Very high level of protectionism
4.	Angola	5 +	Very high level of protectionism
4.	Mozambique	5 +	Very high level of protectionism
4.	South Africa	5 +	Very high level of protectionism
4.	Zimbabwe	5 +	Very high level of protectionism

Commentary: Zambia is now rated as having the least protectionist policy in the southern Africa region. Angola, Mozambique, South Africa and Zimbabwe are still rated as highly protectionist. However, all of the countries are either stable or moving in a positive direction.

TAXATION SUMMARY

Rank	Country	Score	Assessment
1.	Swaziland	3 Stable	Moderate tax rates
2.	Botswana	3 +	Moderate tax rate
3.	Angola	3.5 Stable	High tax rates
3.	Mozambique	3.5 Stable	High tax rates
3.	Namibia	3.5 Stable	High tax rates
3.	Tanzania	3.5 Stable	High tax rates
3.	Zambia	3.5 Stable	High tax rates
4.	Malawi	4 Stable	High tax rates
4.	South Africa	4	High tax rates
5.	Zimbabwe	4 +	High tax rates
6.	Lesotho	4.5	Very high taxes

Commentary: The highest marginal tax rates are moderate to high in most countries but effective rates are often quite different. The formal sector often ends up having a disproportionate tax burden because of ease of collection. For this reason, trade-related taxes (import/export travel taxes) were also historically important.

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GOVERNMENT CONSUMPTION OF ECONOMIC OUTPUT SUMMARY

Rank	Country	Score	Assessment
1.	Swaziland	2 Stable	Low level of government consumption
2.	Zambia	2 +	Moderate level of government consumption
3.	Lesotho	3 Stable	Moderate level of government consumption
3.	Malawi	3 Stable	Moderate level of government consumption
3.	Namibia	3 Stable	Moderate level of government consumption
3.	South Africa	3 Stable	Moderate level of government consumption
3.	Tanzania	3 Stable	Moderate level of government consumption
4.	Mozambique	3 +	Moderate level of government consumption
4.	Zimbabwe	3 +	Moderate level of government consumption
5.	Angola	4 Stable	High level of government consumption
5.	Botswana	4 Stable	High level of government consumption

Commentary: Government consumption as a % of GDP is relatively moderate, except in Angola, which continues to face the costs of war, and Botswana, which enjoys the luxury of diamond revenues.

MONETARY POLICY SUMMARY

Rank	Country	Score	Assessment
1.	Swaziland	2 Stable	Low level of inflation
2.	Botswana	2 +	Low level of inflation
3.	Lesotho	3 Stable	Moderate level of inflation
3.	Malawi	3 Stable	Moderate level of inflation
4.	Namibia	3 +	Moderate level of inflation
4.	South Africa	3 +	Moderate level of inflation
5.	Tanzania	4	High level of inflation
5.	Zimbabwe	4	High level of inflation
6.	Mozambique	5 Stable	Very high level of inflation
7.	Angola	5 +	Very high level of inflation
7.	Zambia	5 +	Very high level of inflation

Commentary: Monetary policy varies greatly in the region, but the trend is positive. Swaziland and Botswana have low inflation while Angola, Mozambique and Zambia have the highest inflation levels.

CAPITAL FLOWS AND FOREIGN INVESTMENT POLICY SUMMARY

Rank	Country	Score	Assessment
1.	South Africa	2 Stable	Low barriers to foreign investment
2.	Zambia	2 +	Low barriers to foreign investment
3.	Namibia	2.5	Moderate barriers to foreign investment
4.	Lesotho	3 Stable	Moderate barriers to foreign investment
4.	Malawi	3 Stable	Moderate barriers to foreign investment
4.	Swaziland	3 Stable	Moderate barriers to foreign investment
4.	Tanzania	3 Stable	Moderate barriers to foreign investment
5.	Botswana	3 +	Moderate barriers to foreign investment
6.	Angola	4 Stable	High barriers to foreign investment
7.	Zimbabwe	4 +	High barriers to foreign investment
7.	Mozambique	4 +	High barriers to foreign investment

Commentary: The region has low to moderate barriers to foreign investment. South Africa and Zambia now have the lowest barriers to foreign investment, while Angola, Zimbabwe and Mozambique have the highest. Most foreign investment continues to be directed toward South Africa. However, Angola's impediments have not stopped major petroleum companies from investing in the country, nor discouraged new South African investment in the country.

BANKING SUMMARY

Rank	Country	Score	Assessment
1.	Botswana	2 +	Low restrictions on banking
1.	Zambia	2 +	Low restrictions on banking
2.	Namibia	3 Stable	Moderate restrictions on banking
2.	South Africa	3 Stable	Moderate restrictions on banking
2.	Swaziland	3 Stable	Moderate restrictions on banking
3.	Zimbabwe	3 +	Moderate restrictions on banking
3.	Malawi	3 +	Moderate restrictions on banking
3.	Tanzania	3 +	Moderate restrictions on banking
4.	Angola	4 Stable	High restrictions on banking
4.	Lesotho	4 Stable	High restrictions on banking
5.	Mozambique	4 +	High restrictions on banking

Commentary: Botswana and Zambia have the lowest restrictions on banking. However, in several countries, high restrictions are still in place, including Lesotho.

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WAGE AND PRICE CONTROLS SUMMARY

Rank	Country	Score		Assessment
1.	South Africa	2	Stable	Low level of wage and price controls
1.	Tanzania	2	Stable	Low level of wage and price controls
2.	Zambia	2 +		Low level of wage and price controls
3.	Malawi	3	Stable	Moderate level of wage and price controls
3.	Namibia	3	Stable	Low level of wage and price controls
3.	Swaziland	3	Stable	Moderate level of wage and price controls
4.	Botswana	3 +		Moderate level of wage and price controls
4.	Mozambique	3 +		Moderate level of wage and price controls
4.	Zimbabwe	3 +		Moderate level of wage and price controls
5.	Lesotho	4	Stable	High level of wage and price controls
6.	Angola	4 +		High level of wage and price controls

Commentary: A high incidence of wage and price controls still exists in Angola and Lesotho. South Africa, Tanzania and Zimbabwe all have low levels of wage and price intervention, although South Africa, which has a strong union movement, is not regarded as having competitively priced labor.

PROPERTY RIGHTS SUMMARY

Rank	Country	Score		Assessment
1.	Botswana	2	Stable	High level of protection of private property
1.	Swaziland	2	Stable	High level of protection of private property
2.	South Africa	3		Moderate level of protection of private property
3.	Lesotho	3	Stable	Moderate level of protection of private property
3.	Namibia	3	Stable	Moderate level of protection of private property
3.	Tanzania	3	Stable	Moderate level of protection of private property
3.	Zimbabwe	3	Stable	Moderate level of protection of private property
4.	Malawi	3 +		Moderate level of protection of private property
4.	Zambia	3 +		Moderate level of protection of property rights
5.	Angola	4 +		Low level of protection of private property
5.	Mozambique	4 +		Low level of protection of private property

Commentary: Property rights protection scored highest in Botswana and low in Zambia and Malawi. Angola and Mozambique scored worst but, although offering the least protection of property rights, showed indications of positive movement.

REGULATION SUMMARY

Rank	Country	Score		Assessment
1.	South Africa	2	Stable	Low level of regulation
2.	Botswana	3	Stable	Moderate level of regulation
3.	Lesotho	3	Stable	Moderate level of regulation
3.	Swaziland	3	Stable	Moderate level of regulation
4.	Namibia	4		High level of regulation
5.	Malawi	4	Stable	High level of regulation
5.	Mozambique	4	Stable	High level of regulation
5.	Tanzania	4	Stable	High level of regulation
5.	Zambia	4	Stable	High level of regulation
6.	Zimbabwe	4 +		High level of regulation
7.	Angola	5 +		Very high level of regulation

Commentary: The Southern Africa region tends to be very highly regulated, per the definition given earlier. Zimbabwe and Zambia continue to be highly regulated indicating that Zambian reform has been partial.

PARALLEL MARKET SUMMARY

Rank	Country	Score		Assessment
1.	Botswana	2 +		Low level of parallel market activity
2.	Namibia	3	Stable	Moderate level of parallel market activity
2.	South Africa	3	Stable	Moderate level of parallel market activity
3.	Zambia	3 +		Moderate level of parallel market activity
4.	Lesotho	4	Stable	High level of parallel market activity
4.	Malawi	4	Stable	High level of parallel market activity
4.	Swaziland	4	Stable	High level of parallel market activity
4.	Tanzania	4	Stable	High level of parallel market activity
4.	Zimbabwe	4	Stable	High level of parallel market activity
5.	Mozambique	5		Very high level of parallel market activity
6.	Angola	5 +		Very high level of parallel market activity

Commentary: Parallel markets still affect the business environment in most countries of the region with only Botswana scoring "low."

SUMMARY OF OVERALL SCORES

Rank	Country	Score	Assessment
1.	Botswana	2.8	Primarily committed to free enterprise
2.	Swaziland	2.9	Primarily committed to free enterprise
3.	Zambia	2.95	Primarily committed to free enterprise
4.	South Africa	3	Moderately committed to free enterprise
5.	Namibia	3.2	Moderately committed to free enterprise
6.	Malawi	3.4	Moderately committed to free enterprise
7.	Tanzania	3.45	Moderately committed to free enterprise
8.	Lesotho	3.65	Moderately committed to free enterprise
9.	Zimbabwe	3.7	Moderately committed to free enterprise
10.	Mozambique	4.05	Not committed to free enterprise
11.	Angola	4.35	Not committed to free enterprise

Commentary: Overall, Botswana, Swaziland, Zambia and South Africa had the most conducive policies for private enterprise. Angola and Mozambique still have the least conducive policies for private enterprise. Nonetheless, field interviews revealed strong investor interest in both Angola and Mozambique, indicating perceptions that things are changing.

Free enterprise policy should not be confused with an entrepreneurial culture. Among non-war torn countries, Zimbabwe was shown to have policies reflecting the least commitment to private enterprise, although the country does have a significant entrepreneurial base. Zambia scored well, thanks to recent policy changes, but has yet to develop a strong cadre of private enterprises.

V. COUNTRY BY COUNTRY POLICY ANALYSIS

This section assesses the economic, commercial and investment policy environment of the eleven SADC countries. The country reports are summaries of those found in the Heritage Foundation Index for Economic Freedom. However, the team has added some updated additional information reflecting recent changes brought to its attention during the visits to embassies and to the region. The format closely follows the Index report, but some sections, such as political climate and economic overview, have been added by the team.

Since this is intended to be a stand-alone document, the sources used for the country information are presented at the end of each country report in addition to their inclusion in the larger bibliography provided to USAID/RCSA as part of this study.

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		1995	1996	Trends
1. Angola	**Overall Score:**	**4.35**	**4.35**	**Stable**

Political Climate: Granted its independence from Portugal in 1975, after a fourteen year war, Angola has been war-torn throughout its existence. The Popular Movement for the Liberation of Angola (MPLA) assumed power after liberation in 1975 and has remained the ruling power. However, this authority has been hotly contested by the rebel organization turned political party, National Union for the Total Independence of Angola (UNITA), which has waged guerrilla warfare with the MPLA throughout the country's existence. UNITA, which was once funded by South Africa (the MPLA was assisted by Cuba and Russia), had been a conduit for South African aggression and destabilisation efforts during its attempts to sustain and expand apartheid throughout the region (until 1988). In 1988, the United Nations, with U.S. assistance, was able to broker a cease fire and the withdrawal of Cuban forces. The United Nations Angola Verification Mission (UNAVEM I) went into effect in 1988, and along with forcing the withdrawal of Cuba, mandated an end to South Africa's support for UNITA. However, the conflict between the MPLA and UNITA continued through a second cease fire in 1991 (UNAVEM II) and a third in 1993. However, hopes were high that a multi-party government would ascend in Angola following the agreement in 1993 by UNITA to become a political party and participate in elections. However, after closely losing the Presidential election in 1994, Jonas Savimbi, the head of UNITA, renewed his war against the MPLA-led government of Angola. To date, although a third U.N. observation, UNAVEM III, has been authorized under an agreement made in November of 1994, and negotiations have taken place between SAVIMBI and Angolan President Jose Eduardo Dos Santos, Savimbi has not agreed to accept the position of Vice-President offered to him. Thus, Angola's version of South Africa's current government of reconciliation remains off track. UNAVEM II's mandate has been extended until February of 1996, but skirmishes between the two parties continue. However, UNITA is much weaker than it has been in the past, and the government much stronger. The conflict has caused increasing economic hardship in the country and raised the political temperament in the capital of Luanda. Additionally, a parallel war in Cabinda instigated by *Frente de Libertacao do Enclave de Cabinda-Renovada* (FLEC-Renovada), fighting for independence in an oil rich region where production levels accounts for two-thirds of Angola's export earnings and state revenues.

Economic Overview: In the climate of armed conflict which has beset Angola for over 20 years, the country's economy has been devastated. Although the Angolan government has pursued economic liberalization efforts launched since 1991, they have had modest impact. Considerable opposition to economic liberalization exists inside the government, and the government has had to put down strikes and threats of strikes on numerous occasions. Subsistence farming provides the main livelihood for 80 - 90 % of the population, but accounts for less than 60 % of the GDP. Oil production is vital to the economy, contributing about 60 % to GDP. Yet, Angola has vast reserves of other mineral resources such as gold, diamonds and significant tracts of arable land. Angola's primary export partners are the U.S., Germany, Belgium-Luxembourg, Spain, Brazil and The Netherlands. The country's primary suppliers are Portugal, the U.S., France, South Africa, Japan and Brazil.

Factor #1: Trade Policy
Score 5+ (Very high level of protectionism)
Angola is virtually a closed market and politically well-connected firms continue to dominate trade. While figures on Angola's tariff rates are virtually non-existent, its market is highly protected behind a wall of trade quotas and import licenses, which are required for all imports. Corruption in the customs services hampers foreign imports. The government's promise to remove formal and informal barriers to foreign trade has been honored only slightly.

Factor #2: Taxation
Score - Income taxation: 2 - Stable (Low tax rates)
Score - Corporate taxation: 4-Stable (High tax rates)
Final Taxation Score: 3.5 - Stable (High tax rates)
Angola currently maintains a top marginal income tax rate of 40 percent. The rate that applies to the average income level is 4 percent. Angola has a top corporate tax rate of 40 percent, a 40 percent capital gains tax, and a 7 percent social contributions tax.

Factor #3: Government Consumption of Economic Output
Score: 4 - Stable (High level of government consumption)
Government consumption as a percentage of GDP is 37.1 percent. Progress with privatization has been minimal, and the government continues to control most of the modern sectors. Following a September 1995 meeting of donors in Brussels, over $1 billion was pledged to assist the government in an effort to undertake a rehabilitation program. This is likely to increase the level of government consumption and intervention in the economy.

Factor #4: Monetary Policy
Score: 5 - Stable (Very high level of inflation)
Inflation in Angola has reached astronomical levels. The annual inflation through August of 1995 was 2,041 with the government exercising no fiscal discipline. Angola has plans to lop off three zeros from newly designed currency notes. Angola's average annual rate of inflation from 1990 through 1994 was over 500 percent.

Factor #5: Capital Flows and Foreign Investment
Score: 3 + Stable (Moderate barriers to foreign investment)
The economic and political crisis in Angola serves as the major deterrent to foreign investment. Notwithstanding recent efforts to attract foreign investors, Angola is effectively closed to most foreign investment. Today, still, foreign investment in several sectors is prohibited. There is considerable red tape and corruption in the investment approval bureaucracy. While there has been some easing of investment restrictions, a number of proposed projects are languishing because of government roadblocks.

Factor #6: Banking
Score: 4-Stable (High restrictions on banking)
Banks are controlled by the government. Recent attempts have been made to allow foreign investment in banks, but little progress has been made.

Factor #7: Wage and Price Controls
Score: 4+ (High wage and price controls)
While price controls have been lifted on many items, they still exist for many goods and services. The Ministry of Labor and Social Security sets wages and benefits. Petroleum price subsidies recently were eliminated; gas no longer is 12 cents per gallon. Large subsidies remain, however, on a wide array of services, including transportation and telecommunications.

Factor #8: Property Rights
Score: 4 - Stable (Low level of protection of private property)
The Angolan government has few means to protect private property. Corruption and bureaucratic inefficiency leave property at risk of criminals and state confiscation. The protection of property rights should improve given the climate of cease fire and the growing military strength of the government.

Factor #9: Regulation
Score: 5+ (Very high level of regulation)
Government regulations are overbearing and a severe hindrance to business. Labor regulations are particularly onerous. Corruption and bureaucratic red tape have created an environment where legal businesses find it nearly impossible to operate.

Factor #10: Parallel Market
Score: 5+ (Very high level of parallel market activity)
The civil war has boosted parallel market activity. A significant share of Angola's economic output is in the parallel market. The government has been cracking down on these parallel economic activities. Medicine and food are sold on the parallel market. There is considerable smuggling of goods. An illegal diamond and gold trade exists.

Summary

Overall Ratings		**Overall Score**	**4.35**
Trade	5	Banking	4
Taxation	3.5	Wage and Prices	4
Government Consumption	4	Property Rights	4
Monetary Policy	5	Regulation	5
Foreign Investment	4	Parallel Market	5

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			1995	1996	Trend
2.	Botswana	Overall Score:	3.05	2.80	+0.25

Political Overview: Botswana was granted independence from England in 1966. Sparsely populated, Botswana is one of the few African countries to experience continuous civilian rule since independence. The country has historically played an important role in galvanizing the "Front Line States" in opposition to apartheid South Africa, and has served as the headquarters for SADC since its inception as the Southern African Development Coordination Committee. Currently, the country is exploring term limits on the office of the President, although elections are not to be held until 1999. The main political parties in Botswana are the Botswana Democratic Party, the ruling party, headed by President Ketumile Masire Botswana, the Botswana National Front and the Botswana People's Party.

Economic Overview: Historically, Botswana's economy has been based on cattle rearing and agriculture. 73% of the population live in rural areas and agriculture provides a livelihood for more than 80% of the population. Yet, only 50% of Botswana's food needs can be met by local production. From the 1970s through the 1980s, the mining sector, particularly the diamond industry, has gone from generating 25 % of GDP to more than 37.4 % in 1994. Agriculture in Botswana has been plagued by erratic rainfalls and poor soils. Unemployment is yet a problem, although, compared to other countries on the continent, it is relatively low, rate of 25%. Yet, the government has launched a number of initiatives to stimulate entrepreneurship. After determining that there was no longer a need for the country to be self-sufficient in power and that sufficient supply was available for import in the region, the Botswana Power Corporation lowered electricity prices by 10%, effective in October 1995. Further, the minister of commerce and industry launched a program to help business students at the University of Botswana assist entrepreneurs in business planning and development. In a move that was welcomed by many living in government owned housing, the Botswana Housing Corporation decided to lower its rental rates to keep pace with changes in the private sector. Botswana has made significant progress in cutting its taxes, reforming its banking sector, and diminishing its parallel market. In light of these factors and other positive changes in the government's economic policies, the Economist Intelligence Unit forecast that Botswana's GDP would continue to grow from its rate of 4.1 in 1994; 4.5 in 1995; 5.0 in 1996; and 5.5 in 1997. While its growth had slowed over the last few years, it must be noted that the Botswana economy remains one of the most vibrant in Africa. From a trade standpoint Botswana is highly dependent on neighboring South Africa. South Africa supplies about 85 percent of its imports and even administers the country's customs procedures. Other key trading partners are Zimbabwe and the European Community, for both imports and exports.

Factor #1: Trade Policy
Score: 4-Stable (High level of protectionism)
Botswana has moderately high tariffs but few, if any, non-tariff barriers. The average tariff rate is 19.4 percent. Botswana is in SACU with South Africa, Lesotho, Swaziland and Namibia.

Factor #2: Taxation
Score - Income taxation: 2 - Stable (Low tax rates)
Score - Corporate taxation: 3+ (Moderate tax rates)
Final Taxation Score: 3+ (Moderate tax rates)
Botswana recently cut taxes. It now has one of the lower tax burdens in Southern Africa. Botswana has a top marginal income tax rate of 35 percent. The rate that applies to the average income level is zero percent. Botswana has a corporate income tax of 35 percent. It also has a 35 percent capital gains tax and a 10 percent sales tax which recently was to cover a greater number of goods and services. There also is a 35 percent capital transfer tax which covers such transfers as inheritance. Botswana also offers two packages of financial assistance for medium scale projects: Automatic Financial Assistance for new manufacturing projects and Case-by-Case Financial Assistance for existing project expansions and selected other new projects.

Factor #3: Government Consumption of Economic Output
Score: 3 + (Moderate level of government consumption)
Botswana has a moderately high rate of government consumption in the economy. The government consumes 31.6 percent of the Botswana GDP. However, the state sector owns a sizable portion of the country's enterprises.

Factor #4: Monetary Policy
Score: 2+ (Low level of inflation)
The average annual inflation rate from 1985 to 1993 was 12.7 percent. The inflation rate was about 11 percent in 1994. In 1995, the inflation rate hovered around 10%.

Factor #5: Capital Flows and Foreign Investment
Score: 3+ (Moderate barriers to foreign investment)
Some sectors are closed to private investment, including most utilities. The requirement that licenses be obtained for expatriate employees is a deterrent to foreign investment. Investments are approved by the Ministry of Commerce and Industry. One hundred percent foreign equity is permitted. The foreign investment bureaucracy recently has improved its performance. There are some tax holidays for specific investments. The EIU reported (Fourth Quarter, 1995) that General Motors agreed to establish an assembly plant of light and medium Chevrolet cars for export to the SACU countries.

Factor #6: Banking
Score: 2+ (Low restrictions on banking)
Botswana has a competitive and advanced banking system compared to most African nations. Three new foreign-controlled commercial banks were established recently in Botswana. The state plays a significant regulatory role in the banking system, including limiting credit to foreign-owned companies. In September in response to lowered expectations of a rise in inflation the Bank of Botswana (the central Bank) lowered the bank interest rate to 13.05%.

Factor #7: Wage and Price Controls
Score: 3+ (Moderate level of wage and price controls)
Price controls have been eliminated. However, agriculture prices are established by negotiated agreements with the government. Moreover, since a large portion of the economy is owned by the government, both prices and wages are affected by government-determined wage and price policies. Botswana has a minimum wage.

Factor #8: Property Rights
Score: 2-Stable (High level of protection of private property)
Property is relatively safe in Botswana. There is little history of property expropriation. However, due to financial constraints, the court system does not always operate efficiently.

Factor #9: Regulation
Score: 3-Stable (Moderate level of regulation)
Government bureaucracy often poses a burden on businesses. A business license is relatively easy to obtain. However, the bureaucracy plays a significant role in running the economy. For example, the government regulates the length of the work week, maternity leave, and standards for hiring and firing. This is burdensome for businesses.

Factor #10: Parallel Market
Score: 2+ (Low level of parallel market activity)
By African standards, Botswana's parallel market is small. The elimination of price controls and exchange controls has diminished the parallel market.

Summary **Overall Score** **2.8**

Overall Ratings

Trade	4	Banking	2
Taxation	3	Wage and Prices	3
Government Consumption	4	Property Rights	2
Monetary Policy	2	Regulation	3
Foreign Investment	3	Parallel Market	2

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			1995	1996	Trend
3.	Lesotho	Overall Score:	N/A	3.65	N/A

Political Overview: Granted independence from Britain in 1966, the Kingdom of Lesotho, which is a small mountainous country encircled by South Africa, is a primarily agrarian country. A constitutional monarchy, over much of its history, Lesotho has had a turbulent government with on-going tension between, primarily, the military and the monarchy, most recently involving King Letsie III and his father King Moshoeshoe II. The more recent incidents began in 1988, when King Moshoeshoe II was deposed by General Justin Lekhanya (after the latter overthrew the single party government that ruled the country between 1970 and 1988) and was headed by Lebua Jonathan, under the Basutoland National Party. However, a year later disillusioned soldiers stripped General Lekhanya of his power and, in 1991, the government authorized the formation of opposition parties. Elections, though delayed, were held in 1993. The Basuto Congress Party (BCP) won with nearly 75% of the vote. Yet, in 1994, the Prime Minister , Ntsu Mokhele, was stripped of his power by King Letsie III who insisted that his father be reinstated. In January 1995, this occurred and the prime minister was asked to return. In September of 1995, a National Forum was convened by Prime Minister Mokhele, to forge a new, more democratic, political compact in Lesotho.

Economic Overview: During the 1970s and much of the 1980s, under one party rule, Lesotho adopted heavy restrictions on almost all economic activity. Lesotho's major natural resource is water and its economy is based primarily on agriculture, light manufacturing and remittances from workers employed in South Africa. In this country, which is almost 80% rural, most families gain their livelihood from subsistence farming and migrant labor. Manufacturing depends largely on farm products to support the canning, milling, leather and jute industries. The Highlands Water Project, a major multilateral bank funded project, also has been important in stimulating growth in the construction industry. Lesotho's main trade partners in terms of exports include the other countries of the Southern African Custom's Union, Canada and the United States, and the European Community. In terms of suppliers, the main trade partners are the SACU countries, Asia and the European Union.

Factor #1: Trade Policy
Score: 4-Stable (High level of protectionism)
Lesotho has a common average tariff rate of about 20 percent. It is likely, however, that new tariffs established by the South African Customs Union, comprised of South Africa, Botswana, Lesotho, Namibia and Swaziland, will help reduce this rate over time. Lesotho also has significant trade restrictions in the form of strict licensing requirements and import bans on some products..

Factor #2: Taxation
Score - Income taxation: 4 - Stable (High tax rates)
Score - Corporate taxation: 4-Stable (High tax rates)
Final Taxation Score: 4.5-Stable (Very high tax rates)
Lesotho has a top income tax rate of 40 percent. However, the average taxpayer is in the 15 percent bracket. It has a top marginal corporate tax rate of 40 percent. Lesotho maintains a 40 percent capital gains tax and a 10 percent general services tax.

Lesotho also has both a subsidiary and a branch tax (40%) and a 25% withholding tax on dividends paid to non-residents investors.

Factor #3: Government Consumption of Economic Output
Score: 3 - Stable (Moderate level of government consumption)
Lesotho's government consumes about 28.1 percent GDP. The state-owned sector contributes greatly to GDP.

Factor #4: Monetary Policy
Score: 3-Stable (Moderate level of inflation)
Lesotho had an average inflation rate of 14.6 percent from 1985 to 1993 but in 1994, according to the Economist Intelligence Unit, inflation dropped to 8.3 percent in 1994. From 1990-95, Lesotho averaged slightly more than 4 percent annual GDP growth.

Factor #5: Capital Flows and Foreign Investment
Score: 3 - Stable (Moderate barriers to foreign investment)
Lesotho maintains some informal restrictions on investments in areas competing with domestic local investment. It has an established investment code, but offers few incentives.

Factor #6: Banking
Score: 4 - Stable (High restrictions on banking)
The banking system in Lesotho is heavily regulated by the government. Moreover, the government owns one of the country's largest banks.

Factor #7: Wage and Price Controls
Score: 4-Stable (High level of wage and price controls)
Wages and prices in Lesotho are affected by the large state sector, which receives government subsidies. Lesotho continues to set some prices on some utilities, as well as on some agricultural goods.

Factor #8: Property Rights
Score: 3-Stable (Moderate level of protection of private property)
Private property is guaranteed in Lesotho and expropriation is unlikely. However, foreigners are not allowed to own land.

Factor #9: Regulation
Score: 3-Stable (Moderate level of regulation)
Establishing a business in Lesotho can be difficult if it competes directly with a state-owned company or government-sanctioned monopoly. Moreover, some corruption is present.

Factor #10: Parallel Market
Score: 4 - Stable (High level of parallel market activity)
There is a substantial parallel market is Lesotho, primarily in consumer goods.

Summary **Overall Score** **3.65**

Overall Ratings

Trade	4	Banking	4
Taxation	4.5	Wage and Prices	4
Government Consumption	3	Property Rights	3
Monetary Policy	3	Regulation	4
Foreign Investment	3	Parallel Market	4

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			1995	1996	Trend
4.	**Malawi**	**Overall Score:**	**3.40**	**3.40**	**Stable**

Political Climate: Granted independence from England in 1964, Malawi is a small country situated between Mozambique and Zambia. Historically a one-party state, in May 1994, Malawi held multi-party elections for the first time electing Bakili Muluzi President. Mr. Muluzi's party, the United Democratic Front are opposed by the declining Alliance for Democracy (AFORD) and the Malawi Congress Party, formerly the ruling party. And after years of dictatorial rule by Kamuzu Banda, Malawi citizens seem to welcome the enhanced oversight that multiple political parties puts upon the incumbent President and his government. Currently, the biggest challenge to UDF will be its ability to get control of the economy, particularly the inflation rate, which reached approximately 34.7 percent in 1994 and 50 percent in 1995.

Economic Overview: Malawi's biggest contributor to the GDP are earnings from tobacco sales. The economy is primarily agricultural and nearly 90 percent of the population live in rural areas. Agriculture accounts for over 30 percent of GDP and over 80% of the country's export earnings. Thus, in the 1980s when southern Africa was beset by long rainless periods, the regional drought brought significant hardship to Malawi. Furthermore, the country's economy was taxed by refugees from nearby Mozambique. These pressures caused Malawi's economy to sink into a deep recession. The government responded by restricting imports and raising government spending on social programs. This action caused the budget deficit to balloon and pushed the country further into a depression. As a result, Malawi's economy shrank nearly 8 percent and real per capita GDP dropped by 11 percent in 1992. Today, Malawi's economy depends significantly upon IMF and World Bank assistance. In 1994, real GDP growth slumped to negative 12 percent as the country waited upon the outcome of their first democratic elections. Following a June meeting with the IMF, Malawi signed into effect an enhanced Structural Adjustment Facility. Based upon the prospect of improved agricultural productivity, particularly relating to tobacco and corn, and efforts in place to reduce government expenditure and borrowing from commercial banks, the Ministry of Finance is optimistic about economic growth in 1996. The main trade partners for Malawi in terms of exports are the U.S., South Africa, Germany and Japan. Leading suppliers to Malawi include South Africa, Zimbabwe, England and Japan.

Factor #1: Trade Policy
Score: 4-Stable (High level of protectionism)
Malawi has an average tariff rate of 10.5 percent. It imposes non-tariffs barriers like strict import licenses on imports of eggs and poultry. In addition, Malawi still maintains import bans on such items as fresh meats and sugar.

Factor #2: Taxation
Score - Income taxation: 4 - Stable (High tax rates)
Score - Corporate taxation: 3-Stable (Moderate tax rates)
Final Taxation Score: 4-Stable (High tax rates)
Malawi has a top income tax rate of 35 percent. However, given a low salary level, the tax on the average income level is zero percent. Malawi's top corporate tax rate is 35 percent. Foreign branch offices in Malawi are taxed at 40%. Malawi also has municipal taxes, a border tax and capital gains tax.

Factor #3: Government Consumption of Economic Output
Score: 3 - Stable (Moderate level of government consumption)
Malawi's government consumption as a percent of GDP is 23 percent. In addition, Malawi has a large public sector. Specifically, it operates marketing boards for some agricultural products. These marketing boards allow the government to confiscate crops from farmers, pay lower than market value prices, and export them at higher prices, keeping the profits.

Factor #4: Monetary Policy
Score: 3-Stable (Moderate level of inflation)
Malawi has an average annual rate of inflation from 1985 to 1993 of 17.8 percent. It had an inflation rate of 34.7 percent in 1994.

Factor #5: Capital Flows and Foreign Investment
Score: 3 - Stable (Moderate barriers to foreign investment)
The government encourages foreign investment only in industries that produce goods for export. Thus, the government does not restrict foreign investments in the coffee, sugar, or tea industries. However, it does restrict foreign investments in the production of consumer goods for the domestic market. The government offers a number of tax related incentives for new investments, particularly, export oriented investments.

Factor #6: Banking
Score: 3+ - Stable (Moderate restrictions on banking)
Of the five major banks in Malawi, only one is totally free from government ownership. Although the government completely freed interest interests rates in 1992, it still exercises a great deal of control over the country's financial system. The government plans to allow two foreign banks to open operations in the near future.

Factor #7: Wage and Price Controls
Score: 3-Stable (Moderate level of wage and price controls)
Price controls have been lifted on almost all products, but they still remain on some food items and energy. Malawi maintains a minimum wage.

Factor #8: Property Rights
Score: 3+ (Moderate level of protection of private property)
Malawi has begun a huge privatization program aimed at selling its biggest state-owned enterprises. Nevertheless, despite plans to eliminate them, marketing boards still control the sale of agricultural products such as corn and fertilizer. The enforcement of laws protecting private property is lax.

Factor #9: Regulation
Score: 4-Stable (High level of regulation)
The government heavily regulates the sale of such agricultural products as corn and fertilizer. Health and safety regulations are enforced erratically, causing confusion among businesses. Moreover corruption is becoming more prevalent.

Factor #10: Parallel Market
Score: 4 - Stable (High level of parallel market activity)
The government strictly controls the importation of food. Thus, there is a huge parallel market is such items as eggs and poultry, which are often imported illegally.

Summary **Overall Score** **3.4**

Overall Ratings

Trade	4	Banking	3
Taxation	4	Wage and Prices	3
Government Consumption	3	Property Rights	3
Monetary Policy	3	Regulation	4
Foreign Investment	3	Parallel Market	4

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The Following Supplied by Embassy:

Investing in Malawi: A Smart Choice, Malawi Investment Promotion Agency

			1995	1996	Trend
5.	**Mozambique**	**Overall Score:**	**4.40**	**4.05**	**+0.35**

Political Climate: Granted independence from Portugal in 1975, Mozambique held its first democratic elections in 1994 under the observation of the United Nations. Like Angola, Mozambique has had a war torn political history and suffered economic devastation because of the conflict. As in Angola, there was a South Africa backed counter party which destabilized the country almost from its inception. *Frente de Libertacao de Mocambique* (FRELIMO), which fought Portugal for independence, was immediately confronted, upon independence, by opposition from the *Resistencia Nacional Mocambicana* (RENAMO). The conflict between the two groups lasted almost 16 years and had a disastrous effect on the country's economy. The war saw nearly a million Mozambicans killed, over 5 million displaced, and, financially, cost about $15 billion. In the late 1980s and early 1990s, as the Cold War ground to a close, and President De Klerk became South Africa's leader and exhibited much less enthusiasm to continue to support the war, both of the allies of the warring parties disappeared. Pressure from the donor community and exhaustion finally took a toll and in 1992 a peace agreement was signed. FRELIMO's candidate, Joaquim Alberto Chissano, was voted into office with 53% of the votes cast in the 1994 election. Today, RENAMO still poses a threat, but as a political party, not a military foe. The current agenda of FRELIMO is dealing with the economic legacy of the long war which left the country classified by the World Bank as the world's poorest.

Economic Overview: With tremendous agricultural, hydropower and transportation resources, Mozambique's economic future appears bright. However, major constraints exist, including 93% illiteracy and $5 billion in debt. On the other hand, Mozambique experienced GDP growth of 5.4% in 1994. In the short-term, while dealing with high inflation (70 percent in 1994) and high unemployment, the government is also faced with maintaining fiscal austerity, combating corruption, continuing to reform the tax and customs policies, and speeding up the privatization process. Mozambique's main export markets are Portugal, Spain, India and Japan. Its main suppliers include France, the U.S., Saudi Arabia and Zimbabwe. The main export product of Mozambique is shrimp.

Factor #1: Trade Policy
Score: 5+ (Very high level of protectionism)
Mozambique has tariff rates that range from 5 percent to 35 percent. There has been some trade liberalization, including a moderate lowering of tariffs and implication of licensing procedures. The customs service, however remains riddled with corruption and the government is considering privatization. There is a small number of prohibited imports, including used automobiles.

Factor #2: Taxation
Score - Income taxation: 2+ - Stable (Low tax rates)
Score - Corporate taxation: 4-Stable (High tax rates)
Final Taxation Score: 3.5-Stable (High tax rates)
Mozambique adjusted personal income in 1994. The highest bracket is now 35 percent. Mozambique has a top corporate income tax rate of 45 percent. Mozambique also has a 45 percent capital gains and a 5 percent to 150 percent consumption tax.

Factor #3: Government Consumption of Economic Output

Score: 3 + (Moderate level of government consumption)

Mozambique has a government consumption figure of 17 percent of GDP. Mozambique has progressed with privatization. Some 350 small enterprises have been privatized, including a beer brewery and cement factory that were sold to South African and Portuguese concerns. Plans for privatizations exist; in the meantime, public enterprises will continue to account for a considerable amount of formal sector economic output.

Factor #4: Monetary Policy

Score: 5 -Stable (Very high level of inflation)

Mozambique had an average inflation rate from 1985 to 1993 of 54.3. Inflation was 60 percent in 1994.

Factor #5: Capital Flows and Foreign Investment

Score: 4+ (High barriers to foreign investment)

A recent change in investment law has improved the climate for foreign investors. Mozambique has established a one-stop shop for foreign investment approval. The government may soon grant land concessions to South African farmers. However, Mozambique's corrupt bureaucracy and feasibility study requirements frustrate foreign investment, particularly by small-scale investors. Infrastructure and a few other areas are off limits to private investment. Free trade zones were established in 1993, through their terms are not comparatively attractive.

Factor #6: Banking

Score: 4 + (High restrictions on banking)

Banking in Mozambique is dominated by state banks, though the banking system is being liberalized. Three private banks now operate in Maputo. Interest rates were recently freed. The government plans to privatize the Commercial Bank of Mozambique, which accounts for some 70 percent of banking assets, and the Popular Development Bank, in 1996. Private banks will remain at a competitive disadvantage until this is done. Corruption exists in the state banks.

Factor #7: Wage and Price Controls

Score: 3+ (Moderate level of wage and price controls)

Price controls for several products were lifted in 1994. Remaining price controls apply to wheat, flour, bread, rents, fuels, utilities, newspapers, transportation and a few other services. Mozambique has a minimum wage.

Factor #8: Property Rights

Score: 4+ (Low level of protection of private property)

While some progress in bolstering property rights has been made lately, the land tenure and property rights regime remains fairly chaotic. Technically, all land still belongs to the state. The vast majority of housing is state owned, though some progress has been made with residential privatization. The government recently announced that it will not make restitution for pre-independence property claims. Mozambique's underdeveloped court system is unable to give private property adequate protection.

Factor #9: Regulation
Score: 4 - Stable (High level of regulation)
Mozambique's regulatory environment is characterized by increasing bureaucratic corruption. Registering a company is a cumbersome and secretive process. There is considerable red tape.

Factor #10: Parallel Market
Score: 5 - (Very high level of parallel market activity)
Mozambique is a center for drug trafficking and money laundering. International crime organizations use Mozambique as a clearinghouse for parallel market trade between Asia and Europe. An estimated 70 percent of consumer goods are smuggled into the country to escape high tariffs and customs corruption.

Summary **Overall Score** **4.05**

Overall Ratings

Trade	5	Banking	4
Taxation	3.5	Wage and Prices	3
Government Consumption	3	Property Rights	4
Monetary Policy	5	Regulation	4
Foreign Investment	4	Parallel Market	5

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			1995	1996	Trend
6.	**Namibia**	**Overall Score:**	**N/A**	**3.10**	**N/A**

Political Climate: The southern African nation of Namibia gained independence from South Africa in 1990. In the five years since independence, Namibia has attempted to integrate the former combatants of the South West Africa People's Organization (SWAPO), without significantly altering the economy or radically changing the ownership structure in terms of industry and land. The government has gone out its way to be viewed as a genuinely national and conciliatory government.

Economic Overview: Although the country's GDP is heavily dependent upon the mining sector (25 percent), 50 percent of Namibia's population depend upon subsistence agriculture for their livelihood. Namibia is the fourth largest exporter of non-fuel minerals in Africa and the world's fifth largest producer of uranium. Alluvial diamond deposits are among the richest in the world , making Namibia a primary source for gem-quality diamonds. Namibia also has large reserves of zinc, tin, lead, tungsten and silver. Namibia's economy, though small, has until recently been relatively stable. Over the last 18 months; however, in the midst of a significant drought which has affected the largely agrarian rural communities, increasing pressure on the government has emerged from unemployed former SWAPO members who feel as if the government has not done enough to help their cause. President Sam Numoja has taken on the task of trying to retrain his former colleagues while at the same time promoting the launching of a new much anticipated export processing zone. Further, the finance minister, Helmut Angula, has set out to put Namibia on a course to improve its fiscal health by decreasing the civil service, establishing a new public enterprise management system with more controls and working with labor activists to solicit their support for the EPZ project. Namibia's key trading partners in terms of exporting are the United Kingdom, South Africa, Japan and Spain. Namibia's key suppliers are South Africa (which also serves as a point of transshipment for products from other parts of the world), Germany, France and Japan.

Factor #1: Trade Policy
Score: 4-Stable (High level of protectionism)
Trade reforms have abolished import and export licenses. There are no prohibited imports. Nevertheless, high tariffs, import quotas, increasing corruption, and bureaucratic inertia hinder trade expansion.

Factor #2: Taxation
Score - Income taxation: 3 - Stable (Moderate tax rates)
Score - Corporate taxation: 3 -Stable (Moderate tax rates)
Final Taxation Score: 3.5-Stable (High tax rates)
The highest income tax rate is 30 percent. The corporate tax rate is 40 percent. Capital gains are taxed on a progressive basis to 30 percent, and a sales tax ranges up to 30 percent.

Factor #3: Government Consumption of Economic Output
Score: 3 - Stable (Moderate level of government consumption)
Government consumption as a percentage of GDP is 31 percent. While there is comparatively significant private activity in the fishing and mining sectors, state-owned enterprises continue to play a major role in the industrial sector.

Factor #4: Monetary Policy
Score: 3+ - (Moderate level of inflation)
Namibia's average annual rate of inflation from 1990 through 1994 was 12.2 percent. Inflation currently is estimated to be 11.5 percent, with projections for 12.5 percent for 1996 and 12.0 percent for 1997.

Factor #5: Capital Flows and Foreign Investment
Score: 2.5 (Moderate barriers to foreign investment)
Since 1990, Namibia has had an investment code and has developed a relatively favorable environment for foreign investment. Investment incentives exist, especially related to the development of the pending export processing zone.

Factor #6: Banking
Score: 3 - Stable (Moderate restrictions on banking)
Namibia boasts of significant private banking interests, primarily from South Africa. Namibia has a small but growing capital market and a significant insurance sector.

Factor #7: Wage and Price Controls
Score: 3 -Stable (Moderate level of wage and price controls)
Most price controls have been removed in Namibia. The pricing of agriculture products has been liberalized. Some wage controls are imposed indirectly by the government's via parastatal enterprises.

Factor #8: Property Rights
Score: 3-Stable (Moderate level of protection of private property)
There has been no nationalization of private enterprises in Namibia. There is, however, growing resentment against white owned businesses that still have few non-white managers.

Factor #9: Regulation
Score: 4 (High level of regulation)
Excessive regulations hinder the private sector. There is a significant effort underway to reduce government bureaucracy in starting and expanding private sector businesses. Gaining approval to hire expatriate employees is not very problematic.

Factor #10: Parallel Market
Score: 3 - Stable (Moderate level of parallel market activity)
Namibia's parallel market is relatively prominent. A relatively small, and closely held, formal economy has entered the parallel market to a certain degree.

Summary **Overall Score** **3.20**

Overall Ratings

Trade	4	Banking	3
Taxation	3.5	Wage and Prices	3
Government Consumption	3	Property Rights	3
Monetary Policy	3	Regulation	4
Foreign Investment	2.5	Parallel Market	3

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			1995	1996	Trend
7.	**South Africa**	**Overall Score:**	**3.00**	**3.00**	**Stable**

Political Climate: After years of apartheid and race-based rule in South Africa, in April 1994, the country held its first multiparty elections, with former African National Congress head, Nelson Mandela, handsomely winning the election. Since then, South Africa's transition from apartheid to a non-racial democracy has gone remarkably well. The country has adopted a federal system of government, held provincial elections and in the Fall 1995 held for the first time in its history multiracial local elections that bound black, white, Indian voters in redefined municipal jurisdictions. National reconciliation has been impressive and white South Africans have by and large been helpful to the new government in working to put the country's sordid past behind it. The primary political challenge of the government comes from former ANC representative turned instigator, Chief Mangosuthu Buthelezi, Minister of Home Affairs, head of the Inkatha Freedom Party and chief proponent of the delegation of more power to the provinces, in particular to the KwaZulu-Natal Province. A key to the country's future stability will be the revival of its long depressed economy and the ending of the bitter feud between Inkatha and the ANC.

Economic Overview: South Africa enjoys many economic assets, including a modern industrial sector, a well-developed infrastructure, and abundant natural resources. The government over the years has maintained a great deal of control over the economy. However, some badly needed economic liberalization has been undertaken recently. While fiscal discipline has been maintained, the government could easily be tempted to overspend on social programs and engage in other state interventions in an effort to improve the lives of previously disenfranchised non-white South Africans. After several dismal years, the South African economy is growing at a respectable pace, with GDP edging toward 4.0 percent in 1996. Gold exports, which are the country's primary export earner are picking up and foreign investment interest has been raised significantly. Manufacturing was up 8 percent by the most recent statistics, returning to 1990 levels. South Africa's primary trading partners in terms of exports are Japan, the U.S., Italy, Germany and the United Kingdom. Exports to SADC countries have jumped significantly over the past year. Key suppliers include Germany, the U.S., England, Japan and Italy.

Factor #1: Trade Policy
Score: 5+ (Very high level of protectionism)
For many years South Africa has maintained high tariffs and other import restrictions. This is gradually changing as the country liberalizes its trade policies. Tariff reductions agreed to under the GATT will be phased in over several years. In the meantime, South Africa remains a heavily protected market. There are no import quotas. Import permits are required for many goods. Used equipment imports are strictly regulated.

Factor #2: Taxation
Score - Income taxation: 4 - Stable (High tax rates)
Score - Corporate taxation: 3 -Stable (Moderate tax rates)
Final Taxation Score: 4 (High tax rates)
South Africa has a progressive tax system with the highest tax bracket being 43 percent. The corporate tax is 35 percent. It also has a value added tax of 14 percent, a financial services tax, and regional taxes.

Factor #3: Government Consumption of Economic Output
Score: 3 - Stable (Moderate level of government consumption)
The South African government's consumption as percentage of GDP is 21 percent. Six state owned companies rank among the 25 largest South African firms. State assets include the country's railways, national airline, broadcasting services, and electric utilities. The government is currently studying the "reconstruction" of state enterprises. There is unlikely to be significant privatization any time soon.

Factor #4: Monetary Policy
Score: 3+ (Moderate level of inflation)
South Africa's average annual rate of inflation from 1985 to 1993 was 13.8 percent. The current inflation rate is below 10 percent.

Factor #5: Capital Flows and Foreign Investment
Score: 2 - Stable (Low barriers to foreign investment)
There is no government approval required for foreign investment. Foreign investors are subject to the same laws as domestic investors. There are no requirements for South African participation in management. Foreign investors are free to acquire land and only a few areas of the economy are reserved for South Africans. Foreign-controlled firms are subject to domestic borrowing restrictions and foreign investment incentives are non-existent. High corporate taxes, political and criminal violence, and low labor productivity are harming South Africa's attempt to attract foreign investment. Concerns about the transition after Mandela and about protection of trademarks and patents also surfaced in a recent survey.

Factor #6: Banking
Score: 3 - Stable (Moderate restrictions on banking)
South Africa has a world-class financial sector. Legal restrictions that discriminate against foreign owned financial institutions have been eliminated. Over 30 foreign banks operate in South Africa. The banking and insurance industries nevertheless are tightly controlled by the Reserve Bank. Interest free reserve balances must be deposited with the Reserve Bank. Exchange controls preclude international investment by South African financial institutions. Licenses for new banks and insurance companies are not readily granted. The new government may pressure the banks into investing in its Reconstruction and Development Program, which is a government at tempt to uplift economically previously disenfranchised black South Africans.

Factor #7: Wage and Price Controls
Score: 2 -Stable (Low level of wage and price controls)
Price controls, once pervasive, now exist only on agricultural machinery, liquor, coal, fertilizers, steel products, meat, milk, gasoline, sugar and tires. No national minimum wage exists. However, labor legislation under consideration has the potential to impose de facto wage controls.

Factor #8: Property Rights

Score: 3 (Moderate level of protection of private property)

No private sector company, whether South African or foreign controlled, has ever been nationalized. The judiciary is professional and effective. However, there is a danger that the redistributionist policies of the government, including its land reform program, may weaken private property rights. Moreover, it is possible that the protection of private property, clause now part of the interim constitution will not be part of the new one. Squatters and crime are a problem and the state may assume control of tribal-controlled communal land. Courts failed to uphold the "McDonalds" international trademark and other international companies have had similar problems.

Factor #9: Regulation

Score: 2-Stable (Low level of regulation)

Regulation of economic activity is minimal in South Africa. It takes only four to ten day to incorporate a business, and most businesses can be started with a minimum of formalities. While licenses are required for certain activities, they can be obtained with relative ease. There has been a blossoming of once banned street vendors. There will be increasing political pressure to practice more affirmative action in hiring and firing of personnel, with an affirmative action directorate having been established in the Labor Ministry.

Factor #10: Parallel Market

Score: 3 - Stable (Moderate level of parallel market activity)

Legal restrictions which prevented black South Africans from owning businesses, obtaining skilled jobs, or living in major urban centers were lifted in 1991. This will reduce parallel market activity. Nevertheless, South Africa's continued high level of trade restrictions encourages smuggling of several goods, including textiles.

Summary **Overall Score** **3.0**

Overall Ratings

Trade	5	Banking	3
Taxation	4	Wage and Prices	2
Government Consumption	3	Property Rights	3
Monetary Policy	3	Regulation	2
Foreign Investment	2	Parallel Market	3

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			1995	1996	Trend
8.	**Swaziland**	**Overall Score:**	**2.90**	**2.90**	**Stable**

Political Climate: Granted independence from England in 1968, Swaziland is one of Africa's last monarchies. King Mswati III has proven to be a foe of full multi-party democracy, preferring the more traditional Tinkhundla system, involving a relatively complex voting procedure through which Swazi citizens elect representatives to the two houses of government. Candidates for each jurisdiction are nominated by electors (it only takes fifteen electors to be nominated). Primary elections are then held to choose a candidate for each jurisdiction. These are followed by secondary elections at the "Tinkhundle" level, where several jurisdictions are grouped together and representatives to the Lower Chamber are chosen. The King also has the right to nominate 10 of the 55 members of the lower house and 20 of the 30 Senators. Lastly, in this system, there are no opposition parties. Most recently this system has come under increasing attack and there is growing pressure in Swaziland for the adoption of a traditional system of multi-party governance. Swaziland has been increasingly singled out in Southern Africa for its lack of multiparty democracy and some traditional leaders who want the country to be buoyed by the region's economic rise realize that the longer reform is delayed the greater the likelihood that the international donor and investment communities will overlook Swaziland.

Economic Overview: Swaziland's population is sustained primarily by subsistence agriculture, which accounts for 25 percent of the country's GDP. As in other countries in the region a large part of the population lives in rural areas (67 percent). However, Swaziland also has a comparatively strong industrial base, and manufacturing, particularly in agroprocessing facilities, also accounts for 25 percent of GDP. The sugar industry is particularly notable. Mining, which once was a strong part of the economy, has declined as iron ore deposits have been depleted and health concerns have cut into the world market for asbestos. Today, exports of sugar and forestry products are the country's main earners of foreign currency. Swaziland's economy is heavily dependent upon South Africa, from which the country receives nearly 75 percent of its imports and sends about 50 percent of its products. Most recently, Swaziland's government, which has held a fairly steady reign on expenses, has been encouraged by the IMF to further reduce expenses, particularly in the public sector managerial level and in the parastatal sectors. Further, privatization, of at least the Post and Telecommunications Corporation is being discussed.

Factor #1: Trade Policy
Score: 4-Stable (High level of protectionism)
Swaziland has an average tariff rate of 13.5 percent. Non-tariff barriers include strict licensing requirements for some imports. These licenses can create delays in bringing foreign goods into the country. With the development of the new SACU agreement, however, these tariffs may drop in 1996.

Factor #2: Taxation
Score - Income taxation: 2 - Stable (Low tax rates)
Score - Corporate taxation: 4-Stable (Moderate tax rates)
Final Taxation Score: 3 -Stable (Moderate tax rates)
Swaziland has a top income tax rate of 39 percent. There are no taxes on the average income level. The top corporate tax rate is 37.5 percent.

Factor #3: Government Consumption of Economic Output
Score: 2 - Stable (Low level of government consumption)
The government consumes 26.4 percent of GDP.

Factor #4: Monetary Policy
Score: 2 -Stable (Low level of inflation)
Swaziland had an average annual inflation rate from 1985 to 1993 of 11.4 percent. It was about 11 percent in 1994.

Factor #5: Capital Flows and Foreign Investment
Score: 3 - Stable (Moderate barriers to foreign investment)
Foreign investment is generally encouraged, and the nationalization of foreign-owned property is prohibited by law. Foreign firms receive the same legal treatment as domestic firms. However, some investments are discouraged in areas that compete directly with local companies. For example, the government discourages foreign investment in some agriculture enterprises. There are a number of tax related incentives for investors in export industries and for investments which involve the training of Swazis.

Factor #6: Banking
Score: 3 - Stable (Moderate restrictions on banking)
Banks in Swaziland are relatively free of government control by African standards. Nevertheless, the government still controls the lending policies of banks, and there is strict government control of credit.

Factor #7: Wage and Price Controls
Score: 3 -Stable (Moderate level of wage and price controls)
Price controls remain on the sale of cotton, corn, milk, petroleum, energy, and tobacco products. Swaziland has a minimum wage.

Factor #8: Property Rights
Score: 2 -Stable (High level of protection of private property)
Property is legally protected against government expropriation. However, enforcement of property rights in the court system can be weak in some cases.

Factor #9: Regulation
Score: 3-Stable (Moderate level of regulation)
Swaziland has streamlined its regulatory system. The government encourages private companies to establish their own safety and health standards. However, some government regulations, mainly those dealing with safety conditions, are applied erratically, which can create uncertainty and confusion.

Factor #10: Parallel Market
Score: 4 - Stable (High level of parallel market activity)
A high level of parallel market activity exists in Swaziland, mainly in the supply of labor, transportation services, construction industry, and pirated computer software. In addition, high external tariffs create incentives for smuggling goods from developed countries.

Summary		**Overall Score**	**2.9**
Overall Ratings			
Trade	4	Banking	3
Taxation	3	Wage and Prices	3
Government Consumption	2	Property Rights	2
Monetary Policy	2	Regulation	3
Foreign Investment	3	Parallel Market	4

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			1995	1996	Trend
9.	**Tanzania**	**Overall Score:**	**3.50**	**3.45**	**+0.05**

Political Climate: Granted independence in 1961 from England, Tanzania is a united republic comprised of the former Tanganyika and the island of Zanzibar. The two became Tanzania in 1964. Historically, Tanzania has had a one party system of governance, and only recently has the government begun taking steps to establish multi-party democracy. In 1992, the government authorized the creation of political parties, after which 12 parties emerged. Since then, an independent press has emerged and an electoral commission been established. Earlier this year, the government set the country's first multi-party elections. In the run-up to the elections, some are questioning the union of Tanganyika and Zanzibar and increasingly religious and racial tensions are creating tension between the island and mainland communities.

Economic Overview: One of the poorer countries in the world, Tanzania depends significantly on agriculture for the country's GDP (almost 57 percent). Agriculture accounts for 85 percent of exports and employs roughly 90 % of the working population. Coffee and cotton are the main export products of the country. Despite receiving tens of billions of dollars in foreign aid from the West, Tanzania remained mired in economic doldrums until the late 1980s. At that time, the government of President Ail Hassan Mwinyi began to introduce limited market reforms. Since then, the government has made some progress liberalizing the economy. Dismayed by the slow move toward democratization and free enterprise, earlier in 1995, aid flows were suspended by the IMF in 1995. These are expected to resume in 1996. Tanzania's budget proposal was also approved by the IMF and international investors. Entrepreneurship is flourishing and Tanzania's less than two year old Tanzania Venture Capital Fund has done very well, turning a profit after its first full year in operation. Tanzania's main trade partners in terms of exports are Germany, India, Belgium, Japan and England. Tanzania's main suppliers are England, Saudi Arabia, Japan, Germany and India.

Factor #1: Trade Policy
Score: 5-Stable (Very high level of protectionism)
Trade reforms have abolished import and export licenses. There are no prohibited imports. Nevertheless, high tariffs, import quotas, increasing corruption, and bureaucratic inertia hinder trade expansion. Momentum for regional trade liberalization with Kenya and Uganda has stalled.

Factor #2: Taxation
Score - Income taxation: 3 - Stable (Moderate tax rates)
Score - Corporate taxation: 3 -Stable (Moderate tax rates)
Final Taxation Score: 3.5-Stable (High tax rates)
The highest income tax rate is 30 percent. The corporate tax rate in Tanzania is 40 percent for foreign firms and 35 percent for domestic firms. Capital gains are taxed on a progressive basis to 30 percent, and a sales tax ranges up to 30 percent.

Factor #3: Government Consumption of Economic Output
Score: 3 - Stable (Moderate level of government consumption)
Government consumption as a percentage of GDP is 11 percent. While some industries have been privatized, inefficient state-owned enterprises continue to play a major role in the industrial sector. Government monopolies in agriculture remain. The privatization program has been impeded by intensifying nationalistic rhetoric.

Factor #4: Monetary Policy
Score: 4- (High level of inflation)
Tanzania's average annual rate of inflation from 1985 through 1993 was 23.4 percent. Inflation currently is estimated to be 35 percent.

Factor #5: Capital Flows and Foreign Investment
Score: 3 - Stable (Moderate barriers to foreign investment)
Tanzania has a new investment code which will create a more favorable environment for foreign investment. A one-stop foreign investment approval office has been established. Majority government participation in mining projects is no longer required. Investment incentives exist. There is a free trade zone on the island of Zanzibar. However, bureaucratic impediments constrain foreign investment. These include the necessity of acquiring business licenses, company registrations, and other documentation from a variety of ministries. The prohibition against owning land also deters foreign investment.

Factor #6: Banking
Score: 3+ (Moderate restrictions on banking)
At least five foreign banks opened their doors in Tanzania over the last two years. A Tanzanian owned bank opened in 1995. These are the first private banks to take advantage of a 1991 law permitting private banking. The banking sector had been nationalized in 1967. Interest rates now are market determined. Despite reforms, financial services are still provided largely by inefficient and corrupt state banks.

Factor #7: Wage and Price Controls
Score: 2-Stable (Low level of wage and price controls)
Most price controls have been removed in Tanzania. The pricing of agriculture products has been liberalized. Wage controls are imposed indirectly by the government's extensive control of economic enterprise. Tanzania also has a minimum wage.

Factor #8: Property Rights
Score: 3-Stable (Moderate level of protection of private property)
There has been no nationalization of private enterprises in Tanzania since 1973. There is, however, a great deal of resentment against individuals, particularly Asians, who have acquired privatized properties. Moreover, the questionable independence of the judiciary leaves property rights insecure.

Factor #9: Regulation
Score: 4-Stable (High level of regulation)
Excessive regulations throttle the private sector. There is rampant corruption throughout the government bureaucracy. Titles, deeds, business licenses, work permits, and other documentation must be secured through several different departments. Gaining approval to hire expatriate employees is not as problematic as in some other African countries.

Factor #10: Parallel Market
Score: 4 - Stable (High level of parallel market activity)
Tanzania's parallel market is huge. High textile tariffs have produced a vibrant market in smuggled textiles. The free trade zone on Zanzibar has led to the smuggling of goods to the mainland.

Summary **Overall Score** **3.45**

Overall Ratings

Trade	5	Banking	3
Taxation	3.5	Wage and Prices	2
Government Consumption	3	Property Rights	3
Monetary Policy	4	Regulation	4
Foreign Investment	3	Parallel Market	4

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			1995	1996	Trend
10.	**Zambia**	**Overall Score:**	**3.05**	**2.95**	**+0.10**

Political Climate: Granted independence from England in 1964, Zambia has been undertaking a transition to multi-party democracy since 1992. It remained a one party socialist state until 1989, when political party opposition was legalized. In 1991, Frederick Chiluba won an overwhelming election victory over long time President Kenneth Kaunda. Chiluba ran on a platform of democracy and free enterprise. The former ruling party, the United National Independence Party, under the leadership of former President Kaunda is back, however, and poised to contest the 1996 presidential election against current President Chiluba. The critical difference between the two has been Mr. Chiluba's unswerving adherence to a IMF prescribed structural adjustment program and Mr. Kaunda's promise to create a government of national unity, reorganize the agriculture sector and to lead a government free of corruption.

Economic Overview: The economy in Zambia, which is based significantly on copper exports, has been in a downward spiral for more than ten years. Real GDP growth in 1994 was provisionally stated at -5.4 percent. Over the past decade, an annual 3 percent growth rate has also led to a 50 percent decline in per capita GDP. As a result of drought, a downward trend in world copper prices, and the government's commitment to withdraw from the economy, the country's population are likely to see a continued fall in their standard of living. Privatization efforts have been sluggish and the government has been tainted by charges of corruption. Zambia's primary trade partners in terms of exports are Japan, Thailand, France and Malaysia. The main import partners are South Africa, England, Zimbabwe and Japan.

Factor #1: Trade Policy
Score: 3 + Stable (Moderate level of protectionism)
Zambia's average tariff rate compared to other African countries is relatively low at 11.9 percent. Import restrictions have been eased. However, resentment against increasing South African imports is generating protectionist sentiment. Moreover, corruption in the Customs Bureau is a growing problem.

Factor #2: Taxation
Score - Income taxation: 3 - Stable (Moderate tax rates)
Score - Corporate taxation: 3 -Stable (Moderate tax rates)
Final Taxation Score: 3.5-Stable (High tax rates)
In 1993 income tax rates were cut for the poor and lower middle income groups. Zambia's top marginal rate is 35 percent. The average Zambian income tax payer is in the 15 percent bracket. In 1993 Zambia cut its corporate tax rate to 35 percent. Zambia also has a 23 percent sales tax and property transfer taxes.

Factor #3: Government Consumption of Economic Output
Score: 2+ (Low level of government consumption)
The Zambian government consumes 10 percent of GDP. During the Kaunda regime, state owned enterprises accounted for more than 50 percent of the GDP. The state sector still dominates the economy. The government, however, is considering selling off the state's massive copper concern.

Factor #4: Monetary Policy
Score: 5+ (Very high level of inflation)
Zambia's average annual rate of inflation from 1985 to 1993 was 89 percent. The inflation rate is currently running at approximately 55 percent.

Factor #5: Capital Flows and Foreign Investment
Score: 2+ (Low barriers to foreign investment)
The government has improved its foreign investment laws. Some investment incentives exist. There is no legal discrimination between foreign and domestic investors, and few investment opportunities are currently off limits, though it is uncertain whether all future privatizations will be open to foreign participation. Zambia is attracting commercial farmers from South Africa and Zimbabwe. Foreign investment must be screened by an investment board, but it operates quickly and efficiently. Difficulties in acquiring land and various licensing requirements deter foreign investment.

Factor #6: Banking
Score: 2+ (Low restrictions on banking)
Private international and domestic banks operate in Zambia. Interest rates for loans and deposits are set by the market. Merchant banking recently has been legalized. However, Zambia still has a few state-owned banks. The government recently took over the management of a failed major commercial bank.

Factor #7: Wage and Price Controls
Score: 2+ (Low level of wage and price controls)
Price controls have been removed and most subsidies have been eliminated. State subsidization of government-owned enterprises, however, distorts the pricing system in Zambia. There is a minimum wage.

Factor #8: Property Rights
Score: 3+ (Moderate level of protection of private property)
Kaunda's socialist regime left a legacy of nationalized property. Businesses were expropriated as recently as 1989. However, legislation enacted in 1993 provides for full compensation for newly nationalized property in convertible currency. Though the courts in Zambia are reasonably independent, property rights protection is weak. It is very difficult to gain title to land in Zambia

Factor #9: Regulation
Score: 4-Stable (High level of regulation)
There are complex procedures and delays for acquiring business licenses. An investment board screens domestic investment. Corruption is an increasing problem. Burdensome and expensive labor laws exist, including the requirement that employers provide housing to employees. Residence permits are difficult to acquire.

Factor #10: Parallel Market
Score: 3+ (Moderate level of parallel market activity)
There is widespread evasion of taxation and expensive labor laws. An illicit drug trade is growing in Zambia. An illegal gemstone trade thrives due to a government monopoly.

Summary **Overall Score** **2.95**

Overall Ratings

Trade	3	Banking	2
Taxation	3.5	Wage and Prices	2
Government Consumption	2	Property Rights	3
Monetary Policy	5	Regulation	4
Foreign Investment	2	Parallel Market	3

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			1995	1996	Trend
11.	**Zimbabwe**	**Overall Score:**	**3.50**	**3.70**	**-0.20**

Political Climate: Granted independence from England in 1980, Zimbabwe has a parliamentary democracy. Since independence, the country has had only one President, Robert Mugabe, of the Zimbabwe African National Union-Patriotic Front party (ZANU-PF). Although technically a democracy, Zimbabwe has been primarily a one party government, as only ZANU-PF receives government financing under constitutional rules. Growing unrest, however, is emerging because the country's economy has been faltering for the past five years and few of the promises made at independence about land redistribution have been followed. Currently, 4,000 white farmers own 11.2 million hectares of farm land compared with 1 million black families eking out a living on barely 16.3 million hectares.

Economic Overview: Although agriculture employs three-fourths of the labor force and supplies almost 40 % of exports (particularly tobacco), Zimbabwe has a comparatively strong manufacturing sector. Zimbabwe has a mixed economy in which the government exercises considerable control over economic activity. President Mugabe, however has begun to liberalize the economy somewhat. The manufacturing sector, based on agribusiness and mining, produces a variety of products and contributes 35% to GDP. Although mining accounts for only 5 percent of both employment and GDP, minerals and metals account for about 40 percent of exports. Despite a relatively sophisticated economic base, since independence in 1980, unemployment has quadrupled and today almost 45 percent of the population is out of work. The last five years have been particularly difficult and have been aggravated by drought, rising government debt and an inflation rate around 25 percent. The structural adjustment program which Zimbabwe has been following has not born fruit and citizens are growing weary of continued austerity.

Factor #1: Trade Policy
Score: 5+ (Very high level of protectionism)
Zimbabwe's average tariff rate is 30 percent. Customs procedures are complex. Concern over cheaper South African imports could lead to more protectionist measures. Some textile and clothing imports are banned. There has been some progress in reducing non-tariff trade barriers.

Factor #2: Taxation
Score - Income taxation: 4+ (High tax rates)
Score - Corporate taxation: 3+ (Moderate tax rates)
Final Taxation Score: 4+ (High tax rates)
Zimbabwe has a top income tax rate of 45 percent. The top corporate income tax rate is 40 percent. Branches of foreign companies are subject to an additional tax of 8.4 percent. Capital gains are taxed at a 30 percent rate. Zimbabwe also has a 10 percent to 20 percent sales tax.

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Factor #3: Government Consumption of Economic Output
Score: 3 + (Moderate level of government consumption)
Government consumption as a percentage of GDP is 23.7 percent. The government owns 40 enterprises, many of them requiring subsidies. Government-owned enterprises include postal, telecommunications, and broadcasting services, railroads and the national air service, all of which are closed to private investment. The government has refused to adopt a program of privatization, despite donor encouragement.

Factor #4: Monetary Policy
Score: 4 - (High level of inflation)
Zimbabwe's average annual rate of inflation from 1985 to 1993 was 20.5 percent. The inflation rate was approximately 23 percent in 1994.

Factor #5: Capital Flows and Foreign Investment
Score: 4+ (High barriers to foreign investment)
Foreign investment regulations have been liberalized substantially by a 1992 investment code. Investor incentives, including duty-free imports in some cases, recently have been introduced. The Zimbabwe Stock Exchange has been opened to foreign investment. However, prior government approval is still required for all foreign direct investment. In 1994, the government banned several sectors from foreign participation, including much of the agriculture, forestry, and transportation sectors. Foreign control of insurance companies is discouraged.

Factor #6: Banking
Score: 3+ (Moderate restrictions on banking)
Four of five commercial banks are foreign-owned, Interest rates have been recently freed. Foreign commercial and merchant banks are allowed majority shareholder status, though this is discouraged. Recent attempts by foreign banks to obtain operating licenses have failed. The government operates some financial institutions.

Factor #7: Wage and Price Controls
Score: 3+ (Moderate level of wage and price controls)
The government has succeeded in removing all but a few price controls. Some subsidies on food goods remain. The government sets a minimum wage by employment sector. Government marketing boards continue to control exports of traditional crops.

Factor #8: Property Rights
Score: 3-Stable (Moderate level of protection of private property)
No nationalization of private property has occurred since independence. However, in 1992 the legislature passed a sweeping land reform bill that enables the government to force the sale of nearly half of the remaining white-owned farmland. This land is to be used to establish state owned communal farms. This legislation denies landowners due process, and its implementation has been subject to corruption.

Factor #9: Regulation
Score: 4+ (High level of regulation)
Wages and employment are heavily regulated. Government permission is required not only to terminate an employee, for example, but to commence virtually any commercial activity. The private sector is under increasing pressure to hire and train more Zimbabweans. The use of foreign nationals is severely restricted. The bureaucracy lacks transparency and is highly arbitrary.

Factor #10: Parallel Market
Score: 4 - Stable (High level of parallel market activity)
Around 20 percent of Zimbabwe's GDP is in the parallel market. This is caused mainly by government monopolies in such areas as transportation services.

Summary **Overall Score** **3.7**

Overall Ratings

Trade	5	Banking	3
Taxation	4	Wage and Prices	3
Government Consumption	3	Property Rights	3
Monetary Policy	4	Regulation	4
Foreign Investment	4	Parallel Market	4

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ANNEX IV:
FINANCIAL SECTOR ANALYSIS

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SOUTHERN AFRICA REGION FINANCIAL SECTOR

The purpose of this Annex is to review the financial sector in the Southern Africa region. The importance of mobilizing savings and investment and of ensuring that scarce investment resources are allocated efficiently has been demonstrated in other parts of this study. It has also been shown that the region suffers from poor quality rather than quantity of investment (see Constraints Analysis in the main report and GEMS Analysis in Annex IV-A). It is the function of the financial sector to generate savings and channel it to the best uses, thus securing high quality investment.

A review of the financial sector reveals that although savings mobilization could be higher in the region, the major problem is not one of the quantity of capital and credit but rather the mechanisms by which this capital and credit can be made available to the private sector and especially the linkages between emerging small- and medium-size enterprise and the formal financial sector. Expanding these linkages should increase the overall quality of investment.

I. CURRENT FINANCIAL SECTOR SITUATION IN SOUTHERN AFRICA

Inflation rates have been high and real interest rates to depositors have actually been negative in the SAR financial systems. Although South Africa has recently begun to bring its inflation under control, Zambia and Mozambique experienced very high inflation in the 1990s. Even without the special case of Mozambique, the average unweighted rate of inflation for SAR countries in the 1990s has been above 15%. No country achieved an inflation rate below 10% for the period. Comparing inflation rates to deposit rates reveals that the latter have generally been negative in real terms, thus making it difficult for the financial system to mobilize savings. Furthermore, it is difficult to argue that lending rates were expensive -- in some countries, they too have been negative in real terms.

Table 1: Inflation, Lending and Deposit Rates

Country	Deposit Rate			Lending Rate			Inflation Rate (cpi)		
	1980	1985	1990-94	1980	1985	1990-94	1980	1985	1990-94
Botswana	5.0	9.0	10.8	8.5	11.5	12.5	13.3	8.1	13.2
Lesotho	n/a	10.4	10.6	11.0	19.7	17.8	15.4	13.2	14.0
Malawi	7.9	12.5	17.6	16.7	18.4	24.7	n/a	n/a	n/a
Namibia	n/a	n/a	10.7	n/a	n/a	19.7	*14.8	11.8	12.2
South Africa	5.5	17.0	14.5	9.5	21.5	18.4	13.8	16.1	12.0
Swaziland	4.5	10.2	8.8	9.5	17.0	15.0	18.3	20.3	12.5
Tanzania	4.0	4.5	n/a	11.5	12.3	35.0	31.7	33.0	*22.6
Zambia	7.0	15.3	37.1	9..5	18.6	67.7	14.3	36.4	*154.8
Zimbabwe	3.5	10.0	19.8	17.5	17.2	24.6	5.4	8.3	28.6
SAR Average	5.3	11.1	16.2	11.7	17.0	26.2	15.9	18.4	33.7

Source: IMF International Financial Statistics Yearbook 1995. Starred inflation data from different years: Namibia 1981, Tanzania 1990-1993, Zambia 1990-1993.

Savings mobilization varies markedly in the region but generally falls somewhat short of desired levels. Gross domestic savings (gross domestic income minus total consumption) has been quite high in Angola and Botswana, has been quite low in Lesotho, Mozambique and Malawi, and has fallen off sharply in Zambia, South Africa and Swaziland. Gross national savings shows a different picture because it also includes net factor income and net current transfers from abroad. When this is factored in, savings levels are much lower for Angola, and much higher for Lesotho. Table 2A-2B below present an overview of these two figures and unweighted regional averages.

Table 2A: Gross Domestic Savings

	Percentage of GDP						
Country	1980	1985	1990	1991	1992	1993	1994
Angola	n/a	28.0	29.7	28.1	28.2	30.0	32.3
Botswana	27.7	32.9	37.4	36.6	44.3	23.1	24.8
Lesotho	-59.7	-77.5	-46.1	-43.3	-30.2	-23.1	-13.7
Malawi	10.8	12.9	9.4	7.9	5.4	0.4	-0.9
Mozambique	0.5	3.8	-3.9	0.2	1.4	7.2	4.7
Namibia	38.6	21.9	13.1	6.8	11.0	8.5	16.9
South Africa	36.5	29.2	23.1	21.3	18.5	19.1	19.7
Swaziland	6.5	4.7	14.6	9.5	10.7	14.6	13.5
Tanzania	n/a	8.7	14.3	8.8	2.2	3.2	3.3
Zambia	19.3	14.1	17.8	14.5	6.4	9.2	3.5
Zimbabwe	15.8	21.0	24.9	20.6	12.4	16.8	n/a
SAR Average	10.67	9.06	12.21	10.09	10.03	9.91	10.41

Table 2B: Gross National Savings

	Percentage of GDP						
Country	1980	1985	1990	1991	1992	1993	1994
Angola	n/a	20.2	8.8	9.5	4.0	0.4	-8.1
Botswana	20.5	21.8	30.2	31.9	46.0	20.2	21.5
Lesotho	12.5	40.8	27.2	25.3	32.9	40.0	40.6
Malawi	3.8	9.2	8.2	8.1	6.6	0.9	-2.9
Mozambique	n/a	n/a	n/a	n/a	n/a	4.0	1.2
Namibia	27.2	0.7	16.0	11.8	14.0	11.9	19.5
South Africa	n/a	24.5	17.4	16.9	15.1	16.3	17.2
Swaziland	-1.1	15.3	15.5	11.8	12.8	12.6	10.9
Tanzania	n/a	9.8	22.5	14.6	9.9	12.9	13.5
Zambia	7.3	0.6	8.1	2.0	-4.8	1.5	-4.6
Zimbabwe	12.2	17.2	20.2	15.8	7.6	12.7	n/a
SAR Average	11.77	11.81	17.41	14.77	14.41	12.13	10.88

Source: African Development Indicators, World Bank, 1996.

Many countries suffer from a lack of long term financing instruments. Banks tend to focus on short-term commercial lending, and in most countries of the region it is harder to get longer term project financing. This is easy to understand when interest rates are negative. No one is willing to save via long term debt instruments.

Credit to the private sector has been expanding in recent years, but has grown at an erratic pace. Annual growth in credit to the private sector has been over 20% in recent years but has been far from stable. Credit to the private sector in Malawi, for example, declined by 12% in 1993 and then rose by 54% in 1994. Unsteadiness in such growth may indicate a lack of breadth and depth in financial markets, and makes it difficult for businesses to plan (see Table 3).

Table 3 Credit to the Private Sector

Country	Level	Percentage annual change						
	1980	1980	1986	1990	1991	1992	1993	1994
Botswana	93	10	20	52	43	36	12	12
Lesotho	21	-10	1	20	34	16	59	39
Malawi	184	8	11	35	28	34	-12	54
Namibia	n/a	n/a	n/a	n/a	17	30	30	31
South Africa	16115	29	6	16	n/a	n/a	11	18
Swaziland	98	15	4	39	40	3	9	22
Tanzania	1137	11	22	18	32	-12	40	13
Zambia	509	5	44	58	59	n/a	n/a	29
Zimbabwe	107	-9	12	28	70	42	44	29
SAR Average	---	7.4	15.0	33.3	40.4	21.3	24.1	27.4

Source: African Development Indicators, World Bank, 1996.

Some South African banks are moving into the rest of the region and while this may help the overall level of credit to neighboring countries, these banks will not likely be targeting small and medium-sized businesses.

Lack of access to credit and capital is a frequent complaint of those in micro, small and medium business. Surveys of businesspeople, interviews in the field, and focus groups revealed that small- and medium-size entrepreneurs believe that lack of access to credit and the cost of credit when available are significant constraints to the growth of their businesses.

However, the problem seems to be not so much lack of capital and credit in the system as the lack of mechanisms which link smaller users to the formal financial system. This acts as a constraint on small and emerging business and is particularly important for women and for ethnic groups which have not traditionally been prominent in the formal business sector.

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Non-traditional financial intermediaries are needed to provide the critical linkages between small business and the formal financial sector. South Africa, with its stokvels and community banking experience, has some interesting models to offer the region. However, non-traditional financial intermediaries are not as well developed in most of the other SAR countries as one might expect based on experience in other regions. Comprehensive data on credit unions, NGO micro-enterprise lending programs and other similar activities were not available for the region as a whole.

Possibilities exist for raising capital on the stock markets, but this will require a degree of regional harmonization on accounting standards, financial reporting requirements and listing regulations. A current USAID-funded study reveals that it is not necessary to set up a regional stock exchange to allow SADC countries to get access to equity capital. However, harmonization of standards regarding accounting standards, financial reporting, and listing requirements may lead to joint listings and cross listings, much as the Jamaica Stock Exchange provides an equity vehicle for various small Caribbean countries.

Having presented a brief review of some of the salient data and findings on the sector, the team looked at the possibilities for regional approaches to financial sector development.

II. FINANCIAL SECTOR DEVELOPMENT IN A REGIONAL CONTEXT

A. The Rationale for a Regional Approach

Regional economic co-operation has become a major theme in the global economy. The European Union (EU), the North American Free Trade Area (NAFTA), the Southern Cone of South America Common Market (MERCOSUR), and the Association of Southeast Asian Nations (ASEAN) are various regional groupings with differing degrees of economic co-operation, coordination and integration among member countries.

Economic regionalization is not new to the African continent. There have been various regional organizations established both prior to and since the independence movement in Africa. These organizations include the relatively successful Franc Zone of West and Central Africa, whose members, with the support of France, have had shared central banks (BCEAO for West Africa and BEAC for Central Africa), an integrated monetary policy, a common currency, low levels of inflation, relatively free convertibility of the currency and integrated regulatory and supervisory authorities for the banking and insurance industries. An example of one of the less successful African economic regional organizations is the original East African Economic Community.

As the USAID "Initiative for Southern Africa" policy documents point out, Southern Africa offers greater potential for economic growth than any other area of the continent. The predominance of English as a common language, English law as the basis of countries' legal systems, the relatively strong and sophisticated economies of Namibia, Zimbabwe, Botswana and South Africa, the

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abundance of essential minerals, fertile agriculture, and a regional population exceeding 125 million all position the region as an area with tremendous opportunity for entrepreneurial business activity and private sector development. At the same time, the recent worldwide recession and unfavorable terms of trade for raw materials and agricultural products, as well as the continued existence of inappropriate policies, low worker skills and productivity, narrow productive bases, corruption and high population growth rates have combined to generate poor overall economic performance for the region.

A consensus has emerged among development specialists that the way to solve many of the region's problems and take advantage of its enormous natural potential is through increased regional economic integration. Moreover, it is thought that generating rapid and sustained economic growth in the region would have salutary spillover effects on the rest of Africa in terms of trade, growth of service industries and through the power of successful example. Thus, the effort to further regional economic cooperation and eventual integration of Southern Africa is a major thrust of economic policy of the countries of the region. Recent inclusion of South Africa into SADC provides an increased impetus to the regionalization process.

B. Conditions for Financial Sector Regionalization

Global experience with economic regionalization point out two essential elements for regional financial sector cooperation: political will and stable and coordinated macroeconomic policies.

1. Political Will

Political will and active support from the political structures and governments of member nations are required for regional financial sector cooperation and eventual integration. Without the active support of the member countries in the effort, little forward progress will be made. In the specific case of regional financial sector integration, political will means that member governments at some point will have to come to terms with the fact that varying degrees of sovereignty may have to be handed over to regional regulatory, licensing and supervisory authorities.

A clear, shared vision of the goal of regionalization and a consensus that the efforts required for regionalization will result in medium- to long-term benefits outweighing short-term economic and political costs at the national level are required. Political will also requires that national governments be able to make convincing arguments for regionalization to their national stakeholders -- government bureaucracies, the private sector and labor -- as it is clear that the effects of regionalization may have negative short-term impacts on these groups. Maintaining political will to support regionalization will not be easy.

2. Macroeconomic Factors

Sound macroeconomic policies are a requirement for better regional financial cooperation. In particular, member countries must strive to reduce fiscal deficits and external debt, maintain effective monetary control, reduce government direct intervention in the financial sector, improve financial sector regulatory and supervisory functions and improve the general business climate for trade and investment.

III. THE SOUTHERN AFRICAN CONTEXT

A. Diversity of the Region

Southern African countries are highly heterogeneous, a factor that affects the region's financial sector. For example, countries differ widely in terms of population size and density, size and structure of member economies, levels of investment and savings ratios, inflation rates, structures of government finance, foreign exchange rates and availability, levels of government indebtedness, levels of real interest rates, per capita income and unemployment. This wide diversity of national macroeconomic factors will influence not only the countries' efforts toward regionalization, but also (and more importantly) their domestic development strategy efforts. Regionalization in southern Africa must be viewed as a long-term process which will inevitably suffer numerous setbacks as national priorities come into conflict with broader regional goals.

B. Unprecedented Opportunity for Regional Financial Sector Cooperation

Despite the diversity among SAR countries, this period represents an unusual and unprecedented opportunity for working towards increased regional cooperation, especially in the financial sector. All of the countries of the region are experiencing, albeit to varying degrees, many common problems -- macroeconomic instability, negative resource balances, weak relationships between investment and economic growth, narrow export base subject to commodity price swings, severe external indebtedness, extreme aid dependence, and weak financial systems. Furthermore, all of the countries are in the process of economic restructuring either through World Bank/IMF supported Enhanced Structural Adjustment Programs or voluntary restructuring. All countries are reviewing and reforming their financial sectors. The period of change offers the member countries an opportunity to coordinate their restructuring and reform programs towards the goal of regional harmonization.

C. Barriers to Increased Regional Financial Sector Cooperation

In spite of the opportunity that the present situation represents for increased regional financial sector cooperation, such cooperation will certainly not be easy. The heterogeneity and instability of member economies are only two of the factors which will make increased cooperation difficult. This is especially true with the recent entry of South Africa into SADC. Indeed, the economic diversity of the countries will produce short-term conflicts of interest which will hinder regional integration.

For regional cooperation to be successful in Southern Africa, national governments will have to ensure a convergence of macroeconomic policies. The critical macroeconomic policy elements include: 1) significant reductions of fiscal deficits and external debt; 2) increased effective monetary policy and control; and 3) improvement and harmonization of economic policies directly affecting business (trade, investment, industrial development, SME development, availability of foreign exchange, and continued reduction of government direct involvement and intervention in the financial sector). Efforts to address these requirements will be neither easy to undertake nor to maintain. It should, therefore, be understood that significant regional cooperation and integration will be a very long-term process requiring concerted effort and political will.

One critical issue is whether the region will seek to move quickly toward global competitiveness by reducing barriers more quickly and to a greater degree or whether they will pursue integration within the region while meeting only those targets minimally acceptable under the WTO. The key indicator of the region's direction in this area will be South Africa's policies.

IV. SHORT-TERM FINANCE ENVIRONMENT AND INSTITUTIONS

The financial sectors of the SAR countries range from highly developed (South Africa and Zimbabwe) to rudimentary (Mozambique). They also vary in terms of their openness, with South Africa and Zimbabwe historically closed, and thus having an excess of funds due to limitation on investment opportunities and controls on capital exports. Even in the countries with sufficient capital, however, financial systems have not become open to risk taking and support for new business ventures. Instead, as countries with underdeveloped financial sectors, there exist constraints which severely limit access to the system of all but the well established business community. These constraints include:

1. a lack of long-term capital;
2. underdeveloped public (listed) stock exchanges (which could provide liquidity for equity investment);
3. a focus on short-term trade and/or inventory finance;
4. a reliance on donor-supported external financing of capital goods;
5. excessive collateralization requirements (limiting financing to those with substantial assets outside their business venture);
6. higher perceived risks to lending for industrial or agro-industrial projects with longer repayment horizons;
7. a history of government subsidized finance programs which placed a premium on political influence to access capital;
8. higher perceived risk in lending to groups in the informal sector; and
9. lack of effective institutional mechanisms to reach smaller scale enterprises.

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To varying degrees these factors are found in all SAR countries. In this environment, the development of access to equity finance instruments for previously disenfranchised groups is very difficult. It is, however, improving. Governments are increasingly willing to accept fiscal and monetary discipline, and more liberal, independent financial institutions are emerging. Southern African governments, driven principally by Structural Adjustment Programs (SAPs), are in the process of implementing financial sector reform and restructuring programs to address some of these problems.

A. Depository Institutions

1. Commercial Banks

Commercial banks are by far the most numerous financial institutions in the region. **Exhibit 1** (at the end of this chapter) presents the thirty largest banks in the region. In 1994, seventeen of these banks were among the top one hundred banks on the African continent. Commercial banks are far from evenly distributed throughout the region, with eight of the top seventeen located in South Africa representing 98.9% of the assets as shown in Table 4 below.

Table 4: SAR Banks Among Top 100 in Africa and Their Asset Values

Country	Number of Banks	Assets (USD millions)	Assets % of Total
South Africa	8	$89,498	98.966
Malawi	2	399	0.004
Lesotho	1	222	0.002
Zambia	2	215	0.002
Zimbabwe	3	98	0.001
Swaziland	1	1	0.000

The commercial banking industry in the region can be loosely divided into two major categories - banking in countries with historically high levels of government involvement and those with relatively low levels of government involvement. Government involvement has been high in Angola, Mozambique, Tanzania, Malawi and Zambia, and low in Botswana, Lesotho, Mauritius, Namibia, South Africa, Swaziland and Zimbabwe.

Commercial banks operating in countries such as Angola and Mozambique where government involvement has been high have suffered from: 1) extensive overlending to the public sector; 2) extremely poor savings mobilization; 3) high levels of insolvency; 4) high levels of over-liquidity; and

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5) generally higher rates of return (ROA) on assets due to oligopolistic tendencies. In Malawi and Zambia, government involvement has been slightly less than other countries in this group. Banks operating in countries where there has been relatively less government involvement tend to be more financially sound, less liquid and, due to competition, have experienced lower ROA.

There is anecdotal evidence suggesting banks in the region have not provided adequate financial services to lower income populations or to SME sectors. Only over the last several years has there been a more concerted effort, prompted by governments like South Africa, to encourage banks to more actively serve the financial needs of smaller businesses and low-end wage earners. Some banks have been opening branches or using mobile banking services in these communities.

The banking industry has been seen as the primary mechanism to meet investment and credit needs because of the relatively unsophisticated, poorly diversified financial sector of the countries. This has been especially true in countries where there has been greater government intervention. Traditionally, commercial banks are principally effective at lending short and medium-term working capital to established medium and larger companies.

There is a trend towards deregulation and liberalization of the commercial banking sector. The goals of the reform process are to increase competition, resulting in improved services at more reasonable cost for the consumer; to reduce government claims on banking resources, so that these resources can be directed to more productive sectors of the economy; to reduce credit controls, so that there is a more rational use of credit within the economy; and to improve the regulatory and supervisory framework, thereby bolstering the credibility and financial viability of the banks. Implementation of these reforms has resulted in the closing of some banks, complete or partial government divestiture, and the opening of the sector to new banks.

2. Extra-Regional Banks

Historically, extra-regional banks have been major players in the region. Partly due to more sophisticated management techniques and defined strategies, banks like Standard Chartered and Barclays have generally experienced high levels of profitability.

Extra-regional banks have been in the process of repositioning their assets in the region despite their profitability, primarily by reducing their direct investment through the sale of their local operations. Much of the repositioning is in direct response to the re-entry of South Africa into the regional marketplace. In many cases, they are selling their operations to South African banking establishments. This should not be seen as the international banking community withdrawing from the region. These international banks generally have equity positions in the very South African banks that are taking over former operations. Instead, this movement is reflective of a strategy to use South African banks as the vehicles which will allow the extra-regional banks to continue to offer their international clients banking services in these countries. This can be achieved through correspondent banking relations without maintaining the same level of direct investment.

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The international financial community sees South Africa as the window to the region. While extra-regional banks generally have reduced their direct investment in most countries in the region, there has been an increase in the number of extra-regional banks established in South Africa.

3. The Role of South African Banks in the Region

Increased presence of South African banks in the other countries of the region will increase the regionalization of the banking sector. With the withdrawal of extra-regional banks from many countries in the region, the role and importance of South African banks in the region will grow. This is a phenomenon that will likely continue in the near-term. The trend will reverse only when one or more of the other economies of the region reach a level of business, trade and general economic activity that will warrant reinvestment by extra-regional banks.

4. Money Markets

There is little in the way of money markets (short-term funds traded primarily among banks and other financial institutions) outside South Africa. Greater attention should be paid to development of not only national money markets but a regional money market where financial institutions with short-term excess liquidity can lend funds to other institutions in need of capital. Free currency convertibility needs to be addressed. Establishment of a regional money market might provide the impetus and part of the solution to the problem. It should certainly be considered one of the first transactional steps needed to be taken towards financial sector regionalization.

5. Credit Unions

Formal Credit unions are surprisingly under-developed in the region. These institutions have been significantly more effective in dealing with low income populations and the lower end of SMEs than commercial banks and are major factors in other regions of the continent and developing countries around the world, particularly in Asia. Efforts to encourage credit union development and expansion in a number of countries are being undertaken with the support of donor organizations such as USAID. This is an area that warrants more investigation, intervention, and long-term support.

B. Non-Depository Financial Institutions

Non-depository financial institutions such as equipment leasing companies, factoring companies and discount houses are also very scarce in the financial sectors of the region, with the exception of South Africa, and to a lesser extent, Zimbabwe. Their absence is additional evidence of the lack of depth and breadth of the region's financial sector. Leasing and factoring companies can be of particular assistance in providing non-bank credit to well managed small and medium-sized businesses. The leasing companies offer access to new equipment so that these businesses do not have to purchase the equipment outright. Factoring companies allow businesses to sell off their accounts receivable at a discount, freeing up cash for ongoing operations. Discount houses buy the loans of other financial institutions, allowing those institutions to recycle the funds into new loans and other performing assets. As part of the effort to meet SME credit needs, there is a need for greater development and expansion of these institutions throughout the region.

C. The Informal Financial Sector

The informal financial sector is widespread throughout the region. In response to the lack of SME and lower income population access to formal financial services, the informal financial sector takes the form of savings groups such as the *stokvels* of South Africa, rotational savings and credit arrangements, and credit provided by family and friends. The benefits of the informal financial sector are that its services are appropriate to their client base, flexible, have relatively low transaction costs (although data on cost are generally unreliable), can better mobilize savings from lower income groups and have a high level of reciprocity.

The informal credit sector has both advantages and limitations. While the advantages of the informal sector providing credit to groups generally excluded from the formal financial institutions have been lauded, it should be remembered that the informal financial sector has its own set of limitations and problems. Credit provided by the informal financial sector is at relatively high interest rates which tend to skew lending to short-term commercial transactions. Longer term loans for capital investment are virtually nonexistent in the informal financial sector. In addition, the informal financial sector does not necessarily guarantee the best allocation of resources within the SME community, does not provide access to external financial services and resources and, depending on the amount of money circulating in the informal sector, may weaken the overall effectiveness of macroeconomic and monetary policy reforms.

There is a need for the development and establishment of appropriate structures and mechanisms to address the Southern African SME sector. Numerous studies have been undertaken analyzing the informal SME credit situation in SAR countries and a number of programs have been established in an effort to increase SME access to credit. Generally, these programs have been less than successful, primarily because most of these programs have been implemented either by commercial banks or by government agencies. These institutions are neither organized nor staffed with personnel who can deal with the informal SME sector effectively. NGOs tend to be more effective at getting credit to SMEs. However, their programs are rarely sustainable without continued donor assistance.

V. LONG-TERM FINANCE ENVIRONMENT AND INSTITUTIONS

For the private sector to develop and expand, medium and long-term debt and equity sources are also crucial.

A. Development Finance Institutions

Development banks have not been notably successful. These institutions, which played an important role in the "Asian Miracle," were established in all the countries of the region with the mandate of providing development capital to small and medium businesses. With rare exceptions, they have failed. Most of those development finance institutions which still exist are in financial distress. Development banks are politically-initiated institutions and tend to have a high degree of government involvement. This has resulted in more loans being directed to government-owned or -influenced medium and large scale projects. Any small scale lending undertaken is generally done as a social activity, reducing the likelihood of borrower repayment. As a result of this mismanagement, development banks presently have the highest concentration of non-performing loans of any type of financial institution in the region.

B. Insurance Companies

Insurance companies, especially life insurance companies, can be significant providers of longer term capital. In addition, insurance companies improve the business environment by providing property and casualty coverage, various trade-related coverage, and the development of pension fund products.

South Africa is by far the largest insurance market in the region. With the exception of South Africa, the insurance industry in the region is highly underdeveloped, although Zimbabwe, Botswana, Malawi and Madagascar have quite small but active sectors. Not surprisingly, Angola, Mozambique and Zambia have relatively moribund insurance industries, due either to nationalization or civil war. Exhibit 2 (at the end of this chapter) presents a brief snapshot of the insurance industries of South Africa and Zimbabwe.

Regional linkages already exist and are growing between South African insurance companies and firms operating in Botswana, Malawi and Zimbabwe. In fact, insurance firms in other countries of the region are often subsidiaries of South African firms. Where there is an active insurance sector, there appears to be a relatively competitive environment for small and medium business. There is significantly less competition in the large-scale business market. Reinsurance, a means of spreading risk, is undertaken principally between regionally-based firms and Western firms which results in high foreign exchange transaction costs. Relatively little reinsurance has occurred between firms within the region although this too is changing as more regional firms are exploring and engaging in reinsurance arrangements in the South African market. Insurance firms in the region need to engage in more "comparative shopping" for reinsurance products within and outside of the region in the future.

The medium term outlook for growth of the life insurance industry in the region is limited, principally due to the high incidence of HIV/AIDS. Not only will companies restrict the amount of life insurance underwriting undertaken, there will no doubt be increasing losses based upon increased claims. This is unfortunate as it is the life insurance sector which normally is a source of long-term funds for investment in productive activities.

C. Venture Capital Companies

It is still relatively early to measure the results of the venture capital firms operating in the region. Relative newcomers to the Southern Africa region, venture capital companies target start-ups and expanding formal SMEs for equity (and occasionally, medium/long-term debt) financing. It would be safe to say that venture capital firms will have only a limited impact in providing credit to the private sector and will have even less impact at the lower end of the SME market.

D. Capital Markets

Capital markets encompass both equity and long-term debt markets and there is a legitimate need for both. In the last five years or so, there has been significant discussion regarding the desirability of establishing capital markets in the region. Unfortunately, ths discussion has been limited to stock markets.

There is a virtual absence of medium and long-term debt market activity in the region. This includes both public and private debt financing. Even in South Africa, which possesses the most sophisticated financial market in the region, medium- and long-term debt market activity is quite limited. The lack of such activities in the region results in the absence of a market-determined yield curve which is essential for the effective and efficient operation of the financial sector.

In addition to the established stock markets of Johannesburg and Harare, several other countries in the region have founded their own local stock markets in large part based upon the perception that these markets will facilitate privatization efforts being undertaken. Certain linkages already exist in the form of technical assistance between South Africa and other stock exchanges in the region (i.e., Botswana, Zimbabwe) and are likely to grow. Exhibit 3 (at the end of this chapter) presents statistics on the stock markets of the region. These data point out the dominance of the South African market.

Over the last three to four years, there has been growing discussion regarding the creation of a regional stock exchange in the context of a regional financial center. South Africa and Mauritius have both been raised as possible sites of such a stock exchange, South Africa because of the sophistication of its financial sector and Mauritius because of its off-shore banking activities. Before deciding to support the establishment of a regional stock exchange, donors should ask the following questions: 1) will a regional stock exchange add to the total flow of savings and other resources available for investment in the region? 2) will a regional stock exchange be more efficient at resource allocation? 3) will liberal resource allocation throughout the region be politically and socially acceptable? 4) is there the infrastructure (principally, telecommunications) in place to support a regional stock exchange/financial center where all members will have equal and timely access? A recent USAID study by Price Waterhouse suggests that similar results are likely to be achieved through harmonization of accounting standards and cross-listings, allowing for more effective regional use of currently existing markets.

E. Investment Funds

A number of private investment funds targeting the region have been established. Responding to growing international interest in emerging market opportunities and the re-entry of South Africa into the global economy, the country or regional funds invest primarily through established stock market vehicles, although several do allow for direct equity investment on a limited basis. Where direct investment has taken place, the investment has been in major, large-scale businesses or privatizations. Presently, there is little access to these funds by the SME sectors although it is possible to imagine that bridging mechanisms will be created to tap into a very limited amount of these funds. In the near-term, these funds will not be a major source of resources for SMEs in the region.

Several donor sponsored investment funds have been created over the last few years, including USAID's Southern Africa Economic Development Fund (SAEDF), the IFC's Africa Enterprise Fund (AEF) and the ADB's Private Sector Development Unit (PSDU). Unlike private funds, these funds are targeted to provide equity and longer-term debt financing to the SME sector. The SAEDF has just begun to function (the Director of the SAEDF has only recently been appointed and is in the process of setting up offices and engaging staff), so it is difficult to predict how effective it will be at increasing SME access to equity finance throughout the region and operating profitably. Little lending or investment in the region has been done by the AEF or PSDU, thus far.

VI. REGIONAL APPROACHES TO FINANCIAL SECTOR ISSUES

A. Currency Convertibility

The lack of convertibility of national currencies represents the single most important obstacle to financial sector regionalization. As a result, most currencies (with the exception of the South African Rand) are thinly traded, exchange rates are relatively volatile, and high transaction costs abound. The lack of convertibility is largely the product of macroeconomic instability. No significant movement towards free convertibility will occur without national effort to control government spending and restore effective monetary control and discipline.

There has been some talk of the establishment of a regional exchange rate stabilization fund to "jump start" support for regional convertibility. Given the state of national government treasuries, it is highly likely that the financing of such a fund would have to be sourced by international donors. At this point, it is unclear how receptive donor agencies would be to such an idea. Certainly, establishment of such a fund will not occur in the immediate future. It is in the interest of national governments to proceed as quickly as possible with stabilization of their own domestic macroeconomic policies, as a starting point.

B. Harmonization of Financial Standards

As the chair of the SADC Finance Working Group, South Africa is presently undertaking analyses and discussions with other member nations regarding the harmonization of financial sector norms and standards, including, *inter alia*, commercial, accounting and financial regulations and supervision. This is an important effort that will likely move forward regardless of donor intervention as it will be supported by the South African banking community as it moves its operations further out into the region.

C. Telecommunications

The poor state of telecommunications in the region is the second most important constraint. Timely access and exchange of financial information is crucial to an effective regional financial sector. Although great strides have been made in upgrading the telecommunications sector, continued investment is essential. This issue is discussed further in the Constraints section (Part I).

D. The Role of South Africa

South Africa will play a dominant role in the ongoing development of the region's financial sector. It is clear that given the comparative size of its economy and the relative sophistication of its financial sector, that in addition to pursuing its efforts at harmonization of financial sector norms and standards, there are opportunities for South Africa to provide increased technical assistance to other SADC members. Finally, it is very likely that the South African Rand will eventually act as the anchor currency in the region, similar to the role played by the Deutsche Mark in the European Community and the Yen in Asia.

VII. CONCLUSIONS AND RECOMMENDATIONS

This review has shown that inflation has been prevalant in the region and that real interest rates have not encouraged strong savings mobilization. Nonetheless, growth in credit to the private sector has been substantial. Absolute scarcity of capital or credit is not the major constraint and hence simplistic solutions such as the channeling of more foreign aid in that form to the credit system are not warranted.

What is needed is the encouragement of sound policies which can lead to the broadening and deepening of the financial system and to the development of longer term instruments and mechanisms which can provide a needed interface between the formal financial sector and the emerging small and medium enterprises.

One is beginning to see a regionalization of financial markets as South African banks move into neighboring SADC countries and as SADC itself explores regional financial coordination. There are some regional approaches which could be useful in this regard. While a regional stock exchange is not necessary, the harmonization of accounting standards, financial reporting obligations and listing requirements could provide access to regional stock markets by companies from many countries of the region. In addition, the development of a money market to permit the short-term trading of excess liquidity among financial institutions would prove extremely useful.

Although there are very interesting models, especially the community banking experience in South Africa, none of the financial sectors of the countries have been particularly successful in addressing the credit needs of SMEs, as evidenced by "lack of access to credit" being one of the most frequent complaints from entrepreneurs. Unless there is some outside intervention, it is not likely that there will be a major change in this trend in the near future. New structures such as credit unions, *stokvels*, and savings associations, which not only provide credit but also other financial services at the grassroots level, are needed. The development of non-depository financial institutions could also help alleviate this problem. Development of such organizations requires a very long-term commitment, since significant and measurable impact normally is not forthcoming before at least a ten-year time horizon. Promotion of NGOs which provide credit to SMEs with sound commercial and business criteria and practices is also needed.

Exhibit 1: **TOP THIRTY BANKS IN SOUTHERN AFRICA**
(Ranked by Capital Strength)

Name (country of origin, date of figure)	Capital US$m	Assets US$m	Capital to Assets ratio (%)	Return on Assets (%)
Amalgamated Banks of South Africa (RSA, 03/91)	1,040	18,200	5.72	0.84
Stanbic (RSA, 12/90)	871	16,600	5.24	1.45
Nedcor (RSA, 09/91)	647	13,115	4.93	1.48
First National Bank of South Africa (RSA, 09/91)	589	12,403	4.75	1.81
Bankorp (RSA, 06/91)	450	8,860	5.08	0.33
NBS Holdings (RSA, 03/91)	138	2,733	5.05	1.12
Meridien International Bank (ZAM, 09/91)	93	1,650	5.64	--
National Bank of Commerce (TAN, 06/89)	67	1,646	4.10	1.80
Boland Bank (RSA, 03/91)	53	1,224	4.33	0.55
Investec Bank (RSA, 03/91)	48	1,055	4.56	--
Mauritius Commercial Bank (MAU, 06/90)	44	686	6.41	--
Standard Chartered Bank Zimbabwe (UK, 12/91)	41	378	10.91	--
Barclays Bank of Botswana Ltd (UK, 12/91)	40	447	8.90	3.55
Rand Merchant Bank (RSA, 06/91)	37	702	5.24	--
State Commercial Bank (MAU, 06/90)	34	396	8.69	1.33
Zimbabwe Banking Corporation (ZIM, 09/90)	34	601	5.72	1.27

Exhibit 1, page 2:

Name (country of origin, date of figure)	Capital US$m	Assets US$m	Capital to Assets Ratio (%)	Return on Assets (%)
Barclays Bank of Zimbabwe Ltd (UK, 12/91)	33	376	8.66	--
Standard Chartered Bank Botswana (UK, 12/90)	25	243	10.23	3.60
Zambia National Commercial Bank (ZAM, 03/91)	23	343	6.81	5.31
First Merchant Bank of Zimbabwe (ZIM, 12/90)	20	185	10.84	1.84
Lesotho Bank (LES, 12/90)	20	184	10.84	2.35
Lima Bank (ZAM, 03/89)	19	33	57.52	--
Standard Chartered Bank Zambia (ZAM, 12/91)	19	152	12.8	9.50
National Bank of Malawi (MAL, 12/90)	18	251	7.32	5.81
Tanzania Investment Bank (TAN, 06/91)	15	44	35.06	0.75
Merchant Bank of Central Africa (ZIM, 03/91)	14	80	17.51	1.71
ANZ Grindlays Bank (Zimbabwe) Ltd (UK, 09/91)	10	203	4.94	--
Barclays Bank of Swaziland Ltd (UK, 12/91)	8	143	5.48	--
Standard Chartered Bank Swaziland Ltd (UK, 12/91)	7	104	6.56	3.66
ANZ Grindlays Bank (Zambia) Ltd (UK, 12/91)	5	54	10.03	3.56

Notes: Primary source: *The Banker*, Issue No. 54, December 1991. Also used were figures for subsidiaries of Barclays Bank, Standard Chartered Bank and ANZ Grindlays taken from balance sheets and profit and loss accounts. Amalgamated Banks of SA and Bankorp merged in early 1992. Stanbic purchased ANZ Grindlays Africa in November 1992.

Exhibit 2:

THE PRIVATE INSURANCE MARKET IN EASTERN & SOUTHERN AFRICA

Data for 1989 (US$m)	Non-life Premiums (Percent all Premiums)		Life Premiums (Per cent all Premiums)		All Premiums Per Capita	All Premiums /GDP
South Africa	1,992	21.2%	7,396	78.8%	272.2	10.0%
Zimbabwe	115	35.3%	211	64.7%	35.7	5.5%
Kenya	156	81.3%	36	18.8%	7.7	2.4%
World Total	576,300	47.6%	633,700	52.4%	1,271.0	--

Source: Sigma *World Insurance Review*, 1988 and 1989.

Exhibit 3:

STOCK MARKETS IN SOUTHERN AFRICA, 1994

Country	Number of Companies Listed	Traded Value (US$M)	Market Capitalization (US$M)
Botswana	11	31	377
Mauritius	34	83	1,579
Namibia	9	16	196
South Africa	640	20,657	259,536
Swaziland	4	2	339
Zambia	8	N.A.	N.A.
Zimbabwe	65	188	1,810
TOTALS	**763**	**20,976**	**263,838**
South Africa's share	83.9%	98.5%	98.4%

Source: International Finance Corporation (IFC), 1996 statistics.

ANNEX V:
OVERVIEW OF BILATERAL AND MULTILATERAL INITIATIVES IN SOUTHERN AFRICA

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REVIEW OF BILATERAL AND MULTILATERAL DONOR INITIATIVES IN SOUTHERN AFRICA

I. USAID

In May 1996, USAID's Africa Bureau conducted an extensive review of its private sector programs in Southern Africa. This Results Review was designed to evaluate the effectiveness of these programs in addressing five primary constraints to private sector growth in the region: 1) unfavorable policy environment (legal, regulatory, institutional); 2) inadequate physical infrastructure; 3) underdeveloped financial markets and institutions; 4) lack of effective private sector organizations (i.e., chambers of commerce, business associations); and 5) impediments to micro-enterprise/informal sector expansion.

Overall, the review found that USAID programs in Sub-Saharan Africa have been reasonably effective in addressing key private sector growth constraints, especially in the areas of policy, micro-enterprise and financial market reform. Support for private sector organizations, while successful on a region-wide basis, has been slightly less effective on a bilateral level. USAID programs have also been somewhat less effective in addressing infrastructure constraints, although important new initiatives in this area are underway. Not surprisingly, USAID assistance has shown the most favorable progress in countries strongly committed to market-oriented, pro-private sector strategies.

In the area of trade and investment reform, USAID initiatives have resulted in substantial liberalization in Mali, Guinea-Bissau, Senegal, Ghana and Zimbabwe. Furthermore, Ghana, Guinea, Guinea-Bissau, Mali, Uganda and Zimbabwe have witnessed a strong increase in non-traditional exports over the last few years. Considerable progress has been made in privatizing state-owned enterprises in Zambia. Lessons learned from the Zambian privatization experience are being adopted in other countries.

In the area of financial market reform, USAID programs have positive results in Zimbabwe, South Africa, Kenya, Guinea and Uganda. In South Africa, USAID's Small Enterprise Foundation and Get Ahead Foundation made an estimated 50,432 loans to small and micro enterprises between 1994 and April 1996.

USAID micro-enterprise initiatives have created jobs and generated substantial income for small-scale farmers and entrepreneurs in Zimbabwe, Tanzania and Malawi.

With respect to private sector organizations, USAID's ability to bring government and business leaders together in a National Forum has helped introduce a number of reforms to promote business expansion and new investment in Uganda. Since 1993, real private investment has grown 35% per year.

Finally, USAID has allocated funds to improve the commercial and operational performance of the Southern Africa region's rail, road and telecommunications enterprises. In Ghana, improved feeder road systems are benefiting rural areas. USAID-assisted privatization of road construction and maintenance in Tanzania has resulted in a 20% decline in transport fares and freight charges.

Overall, the 1996 USAID Africa Bureau Results Review produced a number of important conclusions which will shape future USAID activity in Southern Africa. First, although USAID programs have shown positive results in addressing the five primary constraints to private sector growth in the region, greater impact in the field is needed. This can be achieved through more targeted bilateral strategic objectives (SOs) related to private sector programs, greater local input into project design and implementation, and the strengthening of regional private sector development initiatives such as the Southern Africa Enterprise Development Fund (SAEDF). Second, many challenges remain and USAID cannot realistically address all of the constraints to private sector growth in the region. In an era of declining resources, USAID assistance must be directed toward those areas which offer the greatest promise of sustained growth. These areas include: 1) capital market development; 2) removing barriers to increased cross-border trade and investment among African countries; 3) increasing African private sector access to international market information and business opportunities; and 4) promoting the expansion of the informal/micro-enterprise sector (i.e., facilitating the informal-formal sector transition).

While the Africa Bureau Results Review assessed the effectiveness of USAID bilateral assistance in the area of private sector development, the conclusions are applicable on a regional level. Regional programs which address constraints in the areas of government policy, infrastructure, financial markets, micro-enterprise and business associations must be strengthened where possible. Lessons learned on a bilateral level may form the basis for broader, region-wide initiatives.

The following chart illustrates USAID private sector programs in Sub-Saharan Africa. Programs are categorized according to the specific private sector growth constraints they address. In addition to the five primary constraints outlined by USAID's Africa Bureau Results Review assessment, two additional constraint categories have been added: 1) human resources; and 2) governance. Interventions in the Southern Africa region are listed at the top of the chart. Due to unavailable data, Angola, Lesotho and Mauritius are not included.

ANALYSIS OF USAID PORTFOLIO
INTERVENTIONS ADDRESSING KEY PRIVATE SECTOR CONSTRAINTS *

Countries of USAID Activity	Policy Environment	Underdeveloped Financial Markets	Human Resources	Inadequate Physical Infrastructure	Lack Of Effective Private Sector Organizations	Impediments To Micro Enterprise Expansion
BOTSWANA	✓					
MALAWI	✓	✓			✓	✓
MOZAMBIQUE	✓			✓		
NAMIBIA			✓			
SOUTH AFRICA	✓	✓	✓	✓		✓
SWAZILAND	✓	✓		✓		
TANZANIA	✓	✓	✓	✓		✓
ZAMBIA	✓		✓			✓
ZIMBABWE	✓	✓	✓	✓		✓
ETHIOPIA	✓	✓				
GAMBIA	✓				✓	
GHANA	✓			✓	✓	✓
GUINEA	✓	✓		✓	✓	✓
GUINEA-	✓				✓	✓
KENYA	✓				✓	✓
MADAGASCAR	✓	✓		✓		✓
MALI	✓				✓	✓
NIGER	✓	✓			✓	
SENEGAL	✓				✓	
UGANDA		✓			✓	✓
REDSO/ESA	✓	✓			✓	
REDSO/WCA	✓	✓			✓	

*Sources: USAID Africa Bureau Private Sector Development Results Review, May 1996; Research conducted by J.E. Austin Associates, June 1996;
NOTE: Angola, Lesotho and Mauritius not included.

II. World Bank

The World Bank is the most active donor agency in the SADC region in terms of total lending. In 1994 and 1995 combined, total World Bank lending to the region (excluding Mauritius) in the five key constraint areas outlined in this exercise amounted to over **$1.1 billion** (World Bank Annual Report 1994 and 1995).

Human resources and infrastructure constitute the largest areas of current World Bank lending to SADC countries **(Tables 1-2)**. Over the last two years, the World Bank has approved over $600 million in infrastructure projects and over $120 million in human resource-related projects (including health) in SADC countries (World Bank Annual Report 1994 and 1995). Furthermore, infrastructure and human resource-related projects with a projected total cost of over $2.7 billion and $750 million, respectively, are in the current pipeline for fiscal year 1996 (World Bank 1996 Projects Catalog).

III. European Union

European Union activity in SAR countries is undertaken in the context of the Lomé Convention. Since 1975, over 360 million ECU has been allocated in four Lomé disbursements. In addition, the Cross-Border Initiative (CBI) designed to facilitate intra-regional trade and investment currently receives 80 million ECU in financial support. The table below depicts total European Union commitments (in millions of ECU) to the region in all sectors (except CBI) over a twenty-year period:

EC COMMITMENTS TO SOUTHERN AFRICA: 1975-1995

	Lomé I (1975-80)	**Lomé II (1981-85)**	**Lomé III (1986-90)**	**Lomé IV (1991-95)**
Total Allocation	30	70	141	121
Infrastructure:	20	23.1	91	60
Railways	10	10.5	19	
Roads	10	10.5	24	45
Ports			48	
Airports		2.1		5
Other				10
Human Resources	8.8	13.8	14	21
Food, Agriculture, Natural Resources	0.8	23	27	18
Energy, Industry, Mines		1.8	5.5	12.5
Technical Assistance		3.9	1.5	7.1
Reintegration of Qualified Africans		2.2	2.0	2.4

Source: Southern Africa and the European Union, European Commission, July 1994.

Table 1

CURRENT WORLD BANK INITIATIVES IN SADC REGION ADDRESSING KEY CONSTRAINTS TO PRIVATE SECTOR GROWTH

Country	Policy (Trade, Investment)	Financial Sector	Human Resources	Physical Infrastructure	Access to Information, Contacts	Small and Disadvantaged Enterprise
Angola			x	x		
Botswana						
Lesotho	x		x	x		
Malawi		x	x	x		x
Mozambique	x	x		x		x
Namibia						
South Africa						
Swaziland				x		
Tanzania			x	x		
Zambia	x	x	x	x		x
Zimbabwe	x			x		x

Sources: World Bank Annual Report 1994; World Bank Annual Report 1995; World Bank Public Information Center, 1996 Projects Catalog.

Table 2

WORLD BANK PROJECTS IN SADC REGION ADDRESSING KEY CONSTRAINTS (1994-1996)

Country	Project Description	(US$m)	Year*
Angola	Labor Force Skills Development & Training	35	1996
Angola	Lobito Port Transport System	30	1996
Angola	Urban Water Supply and Sanitation	14	1996
Lesotho	Highlands Water Project	1,100	1996
Lesotho	Privatization & Private Sector Development	11.4	1996
Lesotho	Road Rehabilitation & Maintenance	129	1996
Malawi	Education Sector Credit III	300	1996
Malawi	Entrepreneurship Development	266	1996
Malawi	National Water Development	94.1	1996
Malawi	Power VI Project	90	1996
Malawi	Primary Education Project	0.2	1996
Malawi	National Water Development	79.2	1995
Malawi	Railways Restructuring Project	16.16	1995
Malawi	Entrepreneurship Development	4.6	1995
Malawi	Entrepreneurship Development	40	1995
Malawi	Civil Service Training	22.6	1994
Malawi	Entrepreneurship Development	4.3	1994
Mozambique	National Water Development	1	1996
Mozambique	Financial Sector	9	1994
Mozambique	Financial Sector	200	1994
Mozambique	Transport Sector Rehabilitation	188	1994
Swaziland	Urban Infrastructure Development	29	1995
Tanzania	Human Resource Development Project	22.5	1996
Tanzania	Urban Infrastructure Rehabilitation	178	1996
Tanzania	Transport Sector	170.2	1994
Zambia	Road Sector Project	500	1996
Zambia	Road Sector Investment Program	380	1996
Zambia	Urban Restructuring & Water Supply	33	1995
Zambia	Health Sector Support Project	38.7	1995
Zambia	Financial Sector	18	1994
Zambia	Financial Sector	10	1994
Zambia	Privatization	16.8	1994
Zambia	Trade Reform/Macroeconomic Policy	150	1994
Zimbabwe	Power Sector Project	200	1996
Zimbabwe	Hwange Power Station	90	1994
TOTAL:	**1994 and 1995 only ****	**1,119.56**	

* 1996 figures represent total projected costs and not the amount of World Bank lending.

**1996 projects not included as the exact amount of World Bank lending as % of total cost is not yet known.

Sources: World Bank Annual Report 1994 and 1995; Public Information Center, 1996 Projects Catalog.

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ANNEX VI:
LIST OF INTERVIEWEES AND CONTACTS

USAID/RCSA PRIVATE SECTOR ASSESSMENT
LIST OF INTERVIEWEES AND CONTACTS

From September to November 1995, a team of JAA consultants conducted over 100 interviews with private sector representatives in nine SADC countries (Botswana, Lesotho, Malawi, Namibia, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe). For Angola and Mozambique, recently conducted private sector strategy exercises were used in lieu of direct visits.

Local input into the policy-making process ensures magnified impact in the field. These interviews, therefore, were designed to ascertain local views on private sector development in Southern Africa and to obtain firsthand information on local private sector experiences. Thus, they constitute a critical body of evidence supporting our conclusions regarding constraints to private sector growth in the region.

The following is a list of interviewees and contacts by country. Detailed results of each interview are included in **Annex II** of this document.

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