Regional Activity to Promote Integration Through Dialogue and Policy Implementation (RAPID)

RAPID

FINANCE & INVESTMENT SUB-STRATEGY

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CHAPTER 1: THE FINANCE & INVESTMENT SECTOR WITHIN SADC

1.1 Establishment of FISCU

The Southern African Development Co-ordination Conference [SADCC] was formed in 1980 by nine so-called frontline states to reduce dependence on South Africa and counter the destabilisation of the apartheid regime within the southern African region. The founder members (Angola, Botswana, Lesotho, Malawi, Mozambique, Swaziland, Tanzania, Zambia and Zimbabwe) were later joined by Namibia when that country achieved independence in 1990. While the headquarters was established in Botswana, SADCC allocated various sectoral responsibilities to the different countries, which established institutional structures within their respective capitals to carry out these regional responsibilities.

Following the release from prison of Nelson Mandela and the democratisation of South Africa, the organisation was transformed in 1992 into a body that included South Africa (plus, in due course, three other new members: the Democratic Republic of the Congo, Mauritius and Seychelles, making 14 countries in all). The new organisation – the Southern African Development Community [SADC] – as the name implies has a more ambitious agenda than its predecessor, seeking not merely to co-ordinate development but to achieve progressively deeper forms of regional integration.

The most significant step that has been taken under SADC is the negotiation of the SADC Trade Protocol [STP] under which intra-regional trade will be liberalised over a 12 year period (2000-2012). Although the STP is criticised by those involved in trade issues for having rather modest goals and timetables[1], the impact within the region of having a tangible first step to the ultimate goal of becoming an economically integrated community is considerable. The successful negotiation of the STP provides momentum to efforts to intensify regional integration efforts in areas complementary to trade, including finance and investment.

With new members joining SADC, the range of sectoral responsibilities was broadened, with South Africa being allocated a newly created "finance and investment sector". To effectively discharge its regional responsibilities, the South African government set up a Finance & Investment Co-ordination Unit [FISCU], housed within the Department of Finance in Pretoria. The objectives of FISCU were as follows:

- to promote the development of sound investment policies of member states in order to establish an enabling environment for investment in the region;

- to provide a framework for regional co-operation in the area of finance in collaboration with central banks, other regulatory and supervisory authorities, banks and other financial intermediaries in order to mobilise resources for investment;

[1] See, for example, Flatters (2001) [Section 6 – section numbers in footnotes refer to the Annotated List of References in Annex 1].

- to encourage movement towards regional macroeconomic stability by, among other things, promoting prudent fiscal and monetary policies;

- to analyse and assess the impact of structural adjustment policies and programmes on the attainment of the sector's objectives.

Following the completion in 1997/98 of three major studies, FISCU developed a work agenda and established a number of sub-committees, involving officials from Ministries of Finance throughout the region, to take charge of specific aspects of the work. A complementary initiative was taken by the SADC Committee of Central Bank Governors [CCBG], who established a Secretariat, based in the Reserve Bank of South Africa, to co-ordinate the execution of a number of projects of regional significance.

1.2 SADC Restructuring into Directorates

The structure and activities of FISCU and the CCBG will be described in more detail in later sections. It is important to note at the outset, however, that with the decision by SADC Heads of State in August 2000 to centralise the work of the organisation in a greatly strengthened secretariat in Gaborone, FISCU has ceased to exist. The restructuring concept is that the member states will no longer host the sectoral co-ordinating offices, which instead will be restructured into four 'directorates', all based in Gaborone. The first of these, which was formally established in August 2001, is the Directorate of Trade, Industry, Finance and Investment. In practice, it will take probably until the end of 2002 for this and the other three directorates to be fully staffed and operational, and in the meantime it is important that the initiatives that were taken under FISCU's aegis continue to be executed by the relevant Committee of Senior Treasury Officials sub-committees and by the CCBG.

This sub-strategy for RCSA assistance to SADC's finance and investment integration efforts embraces both support to the existing operational structures and projects, as well as assistance to ensure the successful establishment of the new Directorate of Trade, Industry, Finance & Investment. It seeks first, however, to place the sub-strategy within the overall goals of SADC and RCSA and introduce some of the main issues in regional finance and investment. A conceptual framework is established to explain and support the design of the sub-strategy and to guide its implementation.

CHAPTER 2: USAID-RCSA's GOAL & STRATEGIC OBJECTIVES

2.1 RCSA Goal & Strategic Objectives

The United States has given considerable political support and practical assistance to the countries of Southern Africa in their efforts to achieve regional integration. The US Ambassador to Botswana is also the Secretary of State's Special Representative to SADC. The United States Agency for International Development established the Regional Centre for Southern Africa [USAID-RCSA] in 1995 in Gaborone so as to provide direct, practical assistance to SADC. The main thrust of RCSA is very much in line with SADC's:

> RCSA Goal:
>
> *to promote equitable, sustainable economic growth*
> *in a democratic Southern Africa.*

To contribute to this goal, RCSA is focussing on four complementary 'strategic objectives' [SOs]:

- SO1: *Increased regional capacity to influence democratic performance.*
- SO2: *A more integrated regional market.*
- SO12: *Increased regional co-operation in the management of natural resources.*
- SO13: *Expanded commercial markets for agricultural technologies and commodities in the SADC region.*

2.2 Intermediate Results

The building blocks for the attainment of the strategic objectives are a number of 'intermediate results' [IRs] for each SO. The intermediate results already identified by RCSA for SO2 are:

- IR2.1: *reduced barriers to broadened participation in the regional market*
- IR2.2: *more efficient provision of infrastructure*
- IR2.3: *advocacy for sustained regional integration strengthened.*

The potential contribution of finance and investment to the achievement of the overall RCSA goal of equitable, sustainable economic growth in a democratic Southern Africa requires careful analysis. The main point to be made is that high levels of **investment** are a fundamental and essential requirement for raising the pace of economic growth within the region. An adequate financial environment is one of the building blocks needed to establish a suitable environment for investment and hence growth, but is a necessary and not a sufficient condition in itself. Although other factors, such as the provision of infrastructure (IR2.2), are also important, increasing investment in the region is fundamental.

For the resulting growth to be *equitable*, regional integration efforts (*inter alia* in the finance and investment area) must ensure that the growth potential of all the member countries is achieved. For growth to be *sustainable*, in the sense of self-generating, investment must be predominantly domestic in origin. Cross-border and extra-regional investment can play a crucial role of providing necessary momentum to growth at certain junctures, but over the longer-term, sustainable economic growth must be based on domestic investment. The '*democratic*' element in the RCSA goal (supported by SO1 activities) is also relevant to investment and growth, as the recent experience of Zimbabwe amply testifies.

Although investment is centrally relevant to the overall RCSA goal, formally investment, together with trade and finance, fall under SO2. The way SO2 is specified – aiming to achieve 'a more integrated regional market' – places particular emphasis within RCSA's approach on **intra-regional** trade, finance and investment. The second tier of intermediate results following from IR2.1 (reduced barriers to broadened participation in the regional market) are:

- IR2.1.1: *trade barriers reduced.*
- IR2.1.2: *investment barriers reduced.*
- IR2.1.3: *use of financial services increased.*

IR2.1.1 is being handled in the trade sub-strategy. The means to achieve IR2.1.2 and IR2.1.3, in relation to the five other sub-strategies being concurrently developed (in trade, customs, telecommunications, transport and accounting & auditing standards) are examined in detail later in this report.

CHAPTER 3: THE ROLE OF FINANCE & INVESTMENT IN REGIONAL INTEGRATION

3.1 Investment & Growth

As was emphasised in the previous chapter, investment is fundamental to growth and development in each SADC country, with financial widening and deepening being one of the necessary prerequisites for strong production, trade, investment and growth performance. Moving from the country-specific level, the issue to be addressed from the RCSA sub-strategy perspective is how best to promote finance and investment at the **regional** level. This question was initially addressed for SADC through the three major studies mentioned in Chapter 1. These were commissioned by FISCU in 1997-1998 and covered the areas of "Investment", "Macro-economic Convergence & Adjustment" and "Development Finance"[2].

The analysis and many of the conclusions and recommendations in those three studies remain valid, and since that time there have been a number of other studies and papers prepared for SADC, as well as a growing body of non-SADC specific academic material (particularly analyses arising from the 1997 Asian financial crisis and its aftermath)[3]. It would not be appropriate here to provide a summary of this entire corpus[4]. What is instead provided in this chapter (supplemented by the annotated bibliography in Annex 1) is to give a brief overview of current global and regional best practices, trends and issues, highlighting key points which are particularly relevant to the RCSA finance and investment sub-strategy proposed in Chapter 6.

The starting point for considering strategies to increase investment in SADC is to analyse the components which together constitute the "investment environment" in the region from the viewpoint of different types of investor (differing by origin – domestic, cross-border, foreign – and by type of investment – natural resource-based, export-oriented manufacture, infrastructure providers, service providers). Even without considering the complexity of different categories of investors having different orientations and perspectives, the notion of the investment environment is inherently multi-dimensional in character, with in addition enormous differences between SADC member countries. Indeed, the FISCU Investment Study had a series of matrices documenting the status of each country with respect to six different sets of factors of importance to potential investors[5]:

- political, governance and security framework (covering political stability; freedom of speech and independence of the media; government capacity, transparency, and consistency; levels of political interference and corruption; crime, safety and security; market orientation and privatisation stance; levels of restrictions on foreign investment and employment of expatriates);

[2] The full details of the three studies and the summary volume are given in Section 1 of Annex 1.
[3] Section 8 of Annex 1.
[4] Three papers of particular breadth and interest are Bisignano (2001), Hawkins (1999) and Ndulo (2001) [Section 8].
[5] Robinson (1998), Chapter 5 [Section 1]. Recent analyses of the investment climate in SADC and more generally in Africa are available in Mbekeani (1999) and Isimbabi (2000) [Section 8].

- legal climate (adherence to the rule of law particularly in the enforcement of contracts and property rights; adequacy of business legislation) and international agreements (in respect of investment guarantees, double taxation and preferential trade);

- policy environment (macro-economic and general policy issues affecting domestic business; degree of currency convertibility or existence of exchange controls; degree and reliability of trade liberalisation); structures and procedures for exporting – including customs arrangements for imported inputs and financing availability; and financial sector (financial sector sophistication; foreign investor access to local loans);

- fiscal environment (particularly corporate and dividend taxation) and explicit incentives (for investment and for exports, both inside and outside any export processing zones, which exist at the moment in Malawi, Mauritius, Namibia, Tanzania and Zimbabwe);

- infrastructure (availability, reliability and costs of electricity, water, telecommunications, roads, rail, air and sea transport);

- labour (legislation, policies and institutions; literacy rate and education; skills, wage levels and productivity; strength of trade unions; ease of hiring and firing; HIV/AIDS and health sector).

A final matrix in the report compared the investment promotion agencies [IPAs] which have been set up in most SADC countries with the primary intention of attracting and insisting foreign investors. The IPAs are not so much part of the investment environment as its marketing and public relations arm. With IPAs being nationally based, one of the objectives that SADC seeks to achieve is to prevent harmful competition taking place between the IPAs of member states, or more fundamentally within the investment environments.

Working in the finance and investment sphere, how can the complex, multi-faceted investment environment within the SADC region best be improved? There are five main areas which are identified:

(1) Political factors

The ‘contagion effect’ of the recent self-inflicted crisis in Zimbabwe has dramatically illustrated the fundamental role of political perceptions for a regional investment climate. The views of international investors are quite clear on this – the following example is drawn from a paper presented to the Global Mining Congress held in Cape Town in February 2001:

> *The good policies of South Africa, Botswana, Mozambique and Namibia will count for little in the global competition for capital if global investors regard Zimbabwe as a proxy for Africa’s future. The fact that Zimbabwe was once perceived as having a better level of infrastructure and human capital than other African countries also makes her current crisis all the more damaging*[6].

[6] Hale (2001), page 6 [Section 7].

The immediate costs of Zimbabwe's muddying of the SADC waters could well be dwarfed by the longer-term impact, particularly in respect of foreign investment. The painstaking re-building of confidence, requiring unambiguous improvements in macro-economic performance and many other factors, is likely to take years to have an effect, as in the minds of outside investors "bad reputation tends to linger on, way after changes have occurred. The signal is as important as the information content"[7].

Within the RCSA programme and those of several bilateral USAID missions there are activities under SO1 (which seeks to increase regional capacity to influence democratic performance) that will be important in strengthening the political aspect of the regional investment climate. At moments of crisis, however, macro-political issues such as those evident in contemporary Zimbabwe are not amenable to technocratic, donor-led interventions. SADC itself has shown its awareness of the regional implications of political irresponsibility and has demonstrated that it has an important role to play in resolving the Zimbabwe situation. This commitment was evident in the SADC Heads of Government meeting held in Harare in the second week of September, this meeting being attended by the SADC Executive Secretary.

(2) Macro-economic convergence

In the economic sphere, simultaneous achievement of stable macro-economies, as evidenced by convergence of key parameters on an agreed set or band of target indicators, would be the defining step in achieving the economic integration to which SADC aspires. In its full expression, macro-economic convergence would allow the 14 fragmented member states to overcome the disadvantages of small size and relative isolation and turn instead into a region with the capability to be a player in the global economy, attracting portfolio and direct capital flows, expanding intra-regional and overseas trade, and achieving high rates of investment and growth.

At this stage, the SADC countries can be classified into markedly diverse categories of macro-economic performers, ranging from 'relatively stable' economies, to 'economies in civil war' which have rampant inflation, large fiscal deficits, negative growth and high exchange rate variability[8]. For those countries attempting to move towards greater stability, having regional macro-economic benchmarks and a public commitment to emulating the best performers in the region, should enhance policy credibility and help to 'lock in' economic reform. Thus, although SADC appears to be far behind other regional groupings which have achieved a high degree of macro-economic convergence (such as the European Union), the experience of other regions does indicate that the process itself should be cumulative once there is a firm commitment to the convergence goal.

(3) Harmonisation of investment provisions

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[7] Ndulu (2001), page 9. This observation applies *a fortiori* to portfolio flows where "investment in emerging markets' assets is likely to be highly sensitive to rumours and relatively unresponsive to 'fundamentals'" - Calvo & Vegh (1999), page 56 [both references in Section 8].

[8] Nathan Associates (2001), page 16 [Section 2].

Giving primacy, through macro-economic convergence, to the fundamentals of the regional investment environment is the best way to provide a sound and sustainable basis for regional development. Systems of controls and incentives sometimes appear attractive as a means of securing some particular investment project, but these measures contain the seeds of their own destruction in the national economy and are potentially very damaging in the regional context.

Tax incentives, for example, tend to undermine fiscal targets, leading to weak macro-economic performance and much greater losses of investment as the expectations of the whole spectrum of investors are downgraded. It is thus clearly in SADC's best interests to harmonise tax regimes and other types of investment provisions. This is needed not just to reduce the potential for harmful competition but also to ensure consistency between investment promotion objectives and the more fundamental issue of macro-economic stability as the basis for high growth.

(4) Harmonisation of legal & regulatory frameworks

Countries in a regional grouping which commit themselves to macro-economic convergence and harmonisation of explicit investment provisions must also logically seek to achieve harmonisation over the full range of sectoral issues which have a direct bearing on the investment climate. This would include harmonisation of labour laws and practices and convergence in respect of wages and productivity, thereby permitting in due course free movement of labour across national borders. Another example would be in the infrastructure sphere, where most SADC countries are encouraging private sector participation and are thus attempting to establish regulatory bodies which should ideally be professional and free of political pressures. In this regard, it would be beneficial for the regulatory bodies to be established in each SADC country on a similar legal basis and to operate according to a common set of 'best practice' principles.

In the context of a regional finance and investment sub-strategy, harmonisation of legal and regulatory frameworks is particularly relevant to the financial sectors of member states, these going beyond banking to embrace money and stock markets, investment services, insurance and retirement funds. Efficient financial services, in which investors have a high degree of confidence, are crucial if long-term savings are to be mobilised to achieve adequate levels of growth in the region (the necessary dominance of domestic savings and investment in growth is discussed in Section 3.2). Properly regulated financial institutions also provide households and firms with reliable means to manage various forms of risk. By establishing and adhering to common norms and standards which imply familiarity and confidence, there will be higher levels of cross-border investment and hence a greater degree of integration within the regional market[9].

(5) Exchange control removal as a pre-cursor to monetary union

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[9] Several of the references have comprehensive analyses of these points, including Fox (2000) [Section 10] and Duesenberry & McPherson [Section 8].

The single greatest factor inhibiting cross-border investment at the present time is the lack of currency convertibility. This constraint would certainly disappear if the long-term vision for the region of moving beyond macro-economic convergence (with stable relationships between regional currencies) to a monetary union comes to fruition. Ultimately, a common SADC currency could be adopted. There would undoubtedly be large economic benefits from monetary union (lower transaction costs, greater transparency, higher levels of trade and investment), but this would require countries to be prepared to relinquish a degree of sovereignty, giving up national monetary policy in favour of a regional central bank[10].

This is certainly a long-term goal, well beyond the time horizon of the proposed finance and investment sub-strategy, but a more immediate objective would be to work towards reducing the incidence and impact of exchange controls between SADC countries. Much like the move in the regional trade sphere from a free trade area to a customs union with a common external tariff, the removal of intra-regional exchange controls would be a suitable pre-cursor to adopting a common currency for use within the region and in its relations with the outside world.

Although some linkages with other sectors have been included, the above five factors focus mainly on finance and investment actions. The regional investment climate can also be improved through activities in other sectors, particularly in respect of expanding trade and strengthening infrastructure. Some of the major points of intersection between finance and investment and various other RCSA sub-strategies are discussed in Section 5.2 below.

3.2 Other Points of Particular Relevance to the Sub-Strategy

Common objectives at the national level in SADC are to secure high and sustainable rates of growth and to achieve a more equitable pattern of growth that expands employment and reduces poverty. Coming together in SADC is not seen as an end in itself so much as a means to capture the dynamic as well as static efficiency benefits of a larger market and freer movement of goods. However, the extreme diversity of the membership of SADC makes it impossible for all countries to advance equally at all times. If the pace of the slowest were to determine the overall speed of the region, very little would be achieved and important opportunities for mutual benefit between sub-sets of members would be lost. The recommendation for countries to proceed at different speeds consistent with their capacities and levels of preparedness has been dubbed **'variable geometry'**[11].

This concept is a useful one in contextualising the necessary interplay between policies and programmes which have a domestic focus and participation by countries in regional activities. In any grouping in the early stages of deepening regional co-operation and integration, the primary focus of governments must necessarily remain on the national agenda. This observation is also very relevant when assessing the **importance of domestic investment** in relation to investment emanating from outside

[10] See the 1997 report of the Exchange Control Sub-Committee [Section 3].
[11] African Development Bank (1993) [Section 6].

national borders. In all fast-growing economies, domestic investment far outweighs foreign investment, yet in many SADC countries there has been a skewed emphasis on catering for foreign investors rather than domestic investors.

The finding that the level and dynamism of domestic investment is one of the major issues which tends to be assessed by foreign investors provides strong motivation for a change of emphasis. Instead of biasing the investment climate against domestic investors in order, supposedly, to attract foreign investors, the 'first best' approach is to work on a climate which is favourable and even handed to all investors. This approach must start with macro-economic conditions and financial institutions which generate high levels of domestic savings and channel resources efficiently into domestic investment projects. Booming domestic investment will contribute to growing foreign investor confidence, while foreign projects, particularly if they are in catalytic sectors which, for example, provide access to new technologies and have strong backward and forward linkages in the domestic economy, will add considerably to the momentum of growth.

As this last point illustrates, the shift of emphasis to domestic investment is not in any way intended to encourage an inward-looking development strategy. On the contrary, it is intended instead as a means of increasing foreign investment, thereby creating a dynamic region where domestic, cross-border and foreign investment complement and enhance one another. Within SADC, even South Africa is far too small an economy to 'go it alone'. As a region, all SADC strategies must seek to maximise opportunities for **'open regionalism'**; that is, forms of co-operation which do not preclude benefiting from the much greater growth opportunities that participation in the global trade, finance and investment system offers.

In many of the SADC states, one of the crucial constraints on investment is poor **infrastructure**. The possibility of emulating the world-wide trend of drawing in private sector capital and expertise into sectors previously monopolised by the state brings together a number of key inter-related investment and inter-sectoral issues. An important finding that was highlighted in the FISCU Investment Study is the likelihood of privatisation acting as a catalyst for additional domestic and private investment, over and above the flows directly related to privatisation project[12]. The International Finance Corporation has estimated that a properly managed privatisation process can give rise to a privatisation follow-on investment multiplier of around 3[13]. Since the FISCU studies were completed, there has been little private infrastructural investment or privatisation in other sectors (other than Zambia's copper privatisation), and this potential remains to be exploited[14]. Different components of RCSA support to SADC which feed into this process need to keep the overall picture in view.

Development finance institutions also have an important role to play in financing infrastructure directly or indirectly through various risk reduction mechanism or complementary financing possibilities to support private investors. One of the main questions addressed in the FISCU DFI study was whether a sub-regional SADC-wide development finance institution should be created, and if so whether this should be based on expanding the scope and resources of the Development Bank for Southern Africa [DBSA], based in South Africa. The report did not find a compelling case for a SADC DFI, and instead recommended that national DFI's be assisted to develop sub-

[12] Robinson (1998), Chapter 3 [Section 1].
[13] Bouton & Sumlinski (1996) [Section 8].
[14] BusinessMap (2000) [Section 7].

regional capabilities by networking with each other and applying a combination of co-operative as well as competitive strategies. To facilitate this networking, it was recommended that a Development Finance Resources Centre be set up and consideration be given to the establishment of a SADC Development Fund.

It is now appropriate to turn from general principles to the specific initiatives which have been taken since FISCU was established. The next chapter describes the existing SADC finance and investment institutions, activities, and donor support.

CHAPTER 4: EXISTING INSTITUTIONS, ACTIVITIES & DONOR SUPPORT

4.1 Institutional Structure & Activities to Date[15]

The structure of SADC was outlined in Chapter 1. Despite FISCU's recent reorganisation from a sector into part of a larger directorate, the underlying activities of its committees and subcommittees remain unchanged.

The SADC Finance and Investment Sector has two main committees: the Committee of Senior Treasury Officials and the Committee of Central Bank Governors.

The Committee of Senior Treasury Officials has 5 subcommittees:

- Macroeconomic Subcommittee
- Tax Subcommittee
- Committee of Insurance, Securities and Non-banking financial Authorities [CISNA]
- Investment Subcommittee
- Subcommittee of Development Finance Institutions

The Committee of Central Bank Governors has 5 on-going projects, some of which are directed by temporary steering committees:

- Payments Systems Project
- Legal and Operational Frameworks
- Exchange Control Subcommittee
- Training and Development Forum
- IT Forum

There are also 2 autonomous committees which report to the SADC Ministers for Finance and Investment through the Committee of Central Bank Governors:

- SADC Committee of Stock Exchanges
- SADC Banking Council

In view of the overlap between aspects of the work of CISNA and that of the SADC Committee of Stock Exchanges, CISNA has recommended that both committees should report through the Committee of Treasury Officials. This proposal has yet to be adopted.

[15] For references, see Sections 1-3 of Annex 1.

Each of the Committee of Senior Treasury Officials subcommittees has its own organizational unit, or secretariat, as does the Committee of Central Bank Governors, the Committee of Stock Exchanges, and the SADC Banking Council. The overall formal objective of each subcommittee is to develop one or more Memoranda of Understanding, which can be combined into a framework of principles and ultimately a SADC Finance and Investment Protocol. However, the work of the sub-committees is not restricted to MOU and protocol formulation, and the substance of their activities is far more directly related to meeting overall sector goals and objectives.

The work of most of the subcommittees and their secretariats should not in principle be affected by the re-organization of the sector co-ordinating units and their centralization in Gaborone, provided the funding which previously was channelled through FISCU is not disrupted. As explained below, this should be achieved through the Project Management Unit being established by the European Union. There will also be continued technical support from the USAID full-time technical expert, Dr Senaoana.

The achievements to date and present agenda of the various subcommittees are summarised below:

- **Macroeconomic Subcommittee:** presented a draft Memorandum of Understanding and a comprehensive report on macroeconomic convergence to the SADC Ministers of Finance and Investment on 31 July 2001. The draft MOU envisages the establishment of a regional surveillance unit to monitor key economic indicators reported by each member state.

- **Tax Subcommittee:** has produced a draft Memorandum of Understanding on tax co-ordination which envisages, among others, information sharing on taxes through a database of tax information, and capacity-building through exchanges of personnel, training and the establishment of a Southern African Tax Institute.

- **Committee of Insurance, Securities and Non-banking financial Authorities [CISNA]:** has agreed on harmonisation by each member state of its regulatory standards with those of the International Organisation of Securities Commissions and the International Association of Insurance Supervisors; has produced a draft Memorandum of Understanding; and proposes further activities in capacity building, assessments, training, and the establishment and funding of a permanent secretariat.

- **Investment Subcommittee:** membership consists of representatives of the Investment Promotion Agencies of member countries; work has focused on the sharing of information among the IPAs and harmonisation of investment incentives. The subcommittee produced a draft Memorandum of Understanding some time ago which has not yet been endorsed; also, the subcommittee's terms of reference were amended to include investment in industrial capacity as well as investment promotion which also has not been endorsed.

- **Subcommittee of Development Finance Institutions:** has agreed on the need for a Development Finance Resource Centre [DFRC] for the SADC region. A company registered under the South African Companies' Act has been formed and a Board of Trustees appointed. The first organisational meeting was held on 26-27 August 2001. A business plan and 3-year budget were presented and approved.

The DFRC will be located within the Development Bank of South Africa, which will also provide some support for its activities. The DFRC will need additional operational support, as well as sponsorship of a number of specific activities and studies which have been identified. The subcommittee is also studying the need for a SADC Development Fund.

The Committee of Central Bank Governors has one secretariat, housed in the South African Reserve Bank, organizing all its activities, which are described below:

- **Payments Systems Project:** member states are making progress towards standardizing their domestic payments systems as a precursor to developing a SADC-wide payment and clearing system; a Memorandum of Understanding is being developed as part of the Finance and Investment protocol process. Initial support provided by the World Bank.

- **Legal and Operational Frameworks:** studying the legal and operational frameworks of SADC central banks with a view to achieving greater comparability and compatibility among them; has drafted a Model Central Bank Act which is expected to be finalised in January 2002. The Danish Agency for International Development provided funding for the most recent workshop.

- **Exchange Control Subcommittee:** developed guidelines for use by member states in liberalisation of exchange controls; tracks progress made towards such liberalisation; and assists member states to develop ways to capture balance of payments information formerly captured through exchange control regimes.

- **Training and Development Forum:** co-ordinates the training of central bank officials across the SADC region; has assessed training needs and developed courses which are now being offered; is developing courses to improve human resources management at central banks.

- **IT Forum:** builds capacity within central banks to improve and harmonise the standards of their information technology personnel and functions. The World Bank has provided a grant to support the IT Forum.

In addition to the above on-going projects, the CCBG has completed the following projects:

- **Monetary and financial statistical database:** has been established and a standard methodology for calculating the data has been agreed; data is collected biannually and posted on the SADC Central Bankers website.

- **Information bank on policies and structures of SADC central banks:** has been established; data is collected annually and posted on the SADC Central Bankers website.

- **Assessment of procedures for repatriation of banknotes and coins among SADC countries:** agreed and implemented.

All of the above subcommittees deal with government or quasi-government functions. In addition, there are two private sector subcommittees, which operate autonomously but report to the SADC Ministers for Finance and Investment through the Committee of Central Bank Governors. They are:

- **SADC Committee of Stock Exchanges[16]:** has adopted harmonised listing standards for all SADC member states with stock exchanges. These standards are based on the listing standards of the Johannesburg Stock Exchange [JSE]. As the JSE has recently decided to alter its listing standards to harmonise them with the listing standards of the London Stock Exchange, it is likely that over time the other SADC stock exchanges will follow suit. RCSA recently received a study commissioned from the US Securities and Exchange Commission on the feasibility of setting up a common SADC platform for the clearing and settlement of securities, which concluded that such a system was both feasible and advantageous to participating countries. As an alternative, the JSE has offered all SADC stock exchanges the use of its electronic clearing system at cost.

- **SADC Banking Council:** is working on three projects which it expects to complete over the next 3-5 years: develop norms of good banking practice; build capacity to evaluate public-private partnerships for private-sector infrastructure finance; and reduce crime, with particular reference to reducing money laundering. The Canadian International Development Agency has provided C$4,000,000 over 5 years to support building capacity to evaluate public-private partnerships for private-sector infrastructure finance.

4.2 Donor Assistance[17]

The principal donor to the FISCU secretariat and subcommittees is the European Union. Donor assistance typically takes the form of assistance with training and capacity-building, and funding participation in workshops.

Several donors and subcommittees expressed the view that donor assistance to SADC is not well co-ordinated, and suggested that RCSA could usefully take the lead to improve donor co-ordination. This could be done by developing capacity within the new directorate, as the structure calls for donor funding to be channeled through the directorate.

The EU has two main projects related to finance and investment:

- **a Project Management Unit for FISCU:** this unit, which consists of a project manager, a project assistant, and a secretary, will assist the FISCU subcommittees to prepare MOUs which then combine to form the SADC Finance and Investment protocol. The EU expects the PMU to commence work in January 2002. The PMU will based at the SADC Secretariat in Gaborone. It has a budget of 1.9 million Euros ($1.7 million) and an expected life of 2 years. This project is an extension of previous EU assistance to the FISCU protocol development process.

- **EU/SADC Investment Promotion Programme [ESIPP]:** will provide capacity building and training to investment intermediaries in both the public and private sector, and will organize business-to-business forums for co-operation between firms inside SADC and between firms in SADC and the EU. ESIPP will be

[16] See Section 5 of Annex 1.
[17] See Section 9 of Annex 1.

managed by a Project Management Unit, which is expected to commence work in January 2002. The PMU will be based at the SADC Secretariat in Gaborone. It has a budget of 18 million Euros ($16 million) and an expected life of 5 years.

The EU also has a project related to capacity building of the Secretariat generally:

- **SADC Capacity Building Project:** this will fund up to 13 Technical Advisors in the following areas:

    - Protocol and Policy Adviser
    - Regional Integration Specialist
    - Technical Adviser to the Regional Authorising Officer
    - Database Manager
    - Regional Network Manager
    - Regional Transport Integration Adviser
    - Customs and Trade Facilitation Expert
    - Regional Project Manager Price and Economic Statistics
    - Long Term Expert Macro and Price Statistics

    The project has a budget of 15 million Euros ($12.5 million) and an expected life of 4 years.

Other donor agency projects at the Secretariat level are:

- **Belgian Development Co-operation:** has received a proposal from the Secretariat for assistance to determine whether regional economic partnership agreements between SADC and the EU should be negotiated by SADC or by the member states individually; proposal is not yet agreed. Funding of $300,000 is available for this project.

- **Deutsche Gesellschaft fur Teknische Zusammenarbeit [GTZ]:** has proposed providing assistance to SADC in restructuring and change management by means of a long term consultant to be attached to the office of the SADC Executive Secretary.

- **Norwegian Agency for Development Co-operation:** has a program funded with $1.5 million until 2002 to assist the SADC Secretariat with re-structuring. The Secretariat can request assistance in: recruitment of staff for the new Trade, Finance, Industry and Investment Directorate; training of Secretariat staff in policy analysis and research; and an audit of all physical assets belonging to SADC.

- **UK Department For International Development [DFID]:** discussing with the SADC Secretariat assistance with institutional development and restructuring, probably in the form of assistance in developing a human resources policy and strategic plan.

It should be noted that these projects focus on assistance at the Directorate or Secretariat level, and do not provide direct assistance to specific subcommittee projects.

Other donor support is focused on specific projects or subcommittees:

- **Belgian Development Co-operation:** provides legal assistance to review draft MOU's and ensure they are in accordance with international law. The project has a budget of 25,000 Euros ($22,500).

- **Canadian International Development Agency [CIDA]:** has provided C$4,000,000 over 5 years to the SADC Banking Council to support building capacity to evaluate public-private partnerships for private-sector infrastructure finance.

- **Danish Agency for International Development [DANIDA]:** provided assistance in the initial establishment of the subcommittees; provided funding for the most recent workshop held by the Legal and Operational Frameworks project of the CCBG.

- **Swedish International Development Agency [SIDA]:** provided initial support for Dr. Senaoana's work; funded the publication of an investment profile review prepared by FISCU.

- **World Bank/International Finance Corporation [IFC]:** provided initial support for the Payments Systems Project of the CCBG; provides assistance to various investment promotion agencies through the Foreign Investment Advisory Service; provides assistance to the IT Forum.

- **Foreign Investment Advisory Service** (FIAS, part of the IFC): has not directly assisted SADC as a region, but has in recent years worked with nine SADC states on diagnostic studies of their investment climates and procedures (administrative barriers), formulation of investment policies, codes and promotion strategies; in 2000, FIAS outlined the issues and challenges for regional investment promotion at a COMESA workshop, which was attended by many SADC members.

4.3 USAID Bilateral Missions

Any strategy for support by RCSA to SADC at a regional level must also consider the activities of the USAID Bilateral Missions to SADC member countries. RCSA support should optimally enhance Bilateral Mission activities, and at a minimum not work against them.

Trade and Investment contacts were identified at 11 Bilateral Missions in the SADC region:

- Angola
- Lesotho
- Malawi
- Mauritius
- Mozambique
- Namibia
- South Africa
- Tanzania
- Swaziland
- Zambia

- Zimbabwe

All Missions except for Angola were successfully contacted with a request for information on any country level activities which should be considered in the design of the sub-strategy.

Responses were received from 5 Missions (Mozambique, South Africa, Swaziland, Zambia, Zimbabwe). In addition, Program Summaries were downloaded from the USAID website for 8 Missions (Angola, Malawi, Mozambique, Namibia, South Africa, Tanzania, Zambia, Zimbabwe).

Broadly speaking, Bilateral Mission activities with relevance to RCSA's finance and investment sub-strategy consist of capacity-building assistance to government departments. Such assistance is being provided by 4 Bilateral Missions:

- **Angola:** USAID Program no. 654-008 More Market-Oriented Economic Analysis Used in Decision-Making Process, which will provide technical assistance and training to improve the capacity of the government to produce, analyse, and use economic statistics and reports. This program is being undertaken in co-operation with other donor agency capacity building programs.

- **Mozambique:** USAID has programs which support the reform of direct taxation, reform of the legal system, and private sector initiatives to work with government to reduce barriers to trade and investment.

- **South Africa:** USAID has programs which improve capacity to undertake sound economic analysis through funding graduate-level training of economists to work in government departments (Mandela Scholars); work by the US Treasury Department with the South African National Treasury and South African Revenue Service on tax policy and implementation; and work by the US Department of Justice and Federal Trade Commission to assist in the establishment of a South African Competition Commission. The Mission also funded a study on the feasibility of a common currency for the SADC region and several workshops on various topics.

- **Zambia:** USAID funds the Zambia Trade and Investment Enhancement Activity, which supports the Zambia Investment Centre.

In addition, most of the Bilateral Missions have programs which support the development of private sector economic activity (particularly micro-finance), and democracy and good governance, which, as was pointed out in Chapters 2 and 3, are key to the promotion of regional market integration.

CHAPTER 5: CRITERIA FOR RCSA SUPPORT

5.1 Identification of Criteria

The design of the finance and investment sub-strategy, which is presented in the next section, is based on applying the following criteria for RCSA support of specific interventions:

(1) activities which most directly contribute to fulfilment of the RCSA goal, strategic objectives and intermediate results at the regional level;

(2) activities which are complementary to other RCSA regional sub-strategies;

(3) activities in which RCSA has a comparative advantage;

(4) activities consistent with USAID's overall policies with respect to finance and investment;

(5) activities which are not already financed by SADC governments and central banks or supported by other donors.

RCSA should not be directly involved in the chosen activities, but needs to find **partner institutions** operating at the regional level which will take responsibility for the detailed design, implementation, monitoring and reporting of activities. Criteria similar to those given above are to be applied in the choice of regional finance and investment partner institutions. The possibility of helping establish new institutions should also be kept in view. In general, however, RCSA should not directly pay for the establishment or the general running costs of such institutions, but should provide sufficient support to ensure that the activities (which directly contribute to the overall goal and strategic objectives) can be effectively implemented.

5.2 Analysis of Criteria

The above criteria merit more detailed discussion. The *first* (see Section 2) relates to the hierarchy of the RCSA goal of promoting equitable, sustainable economic growth in a democratic Southern Africa, in part through achieving a more integrated regional market (SO2), through reduced barriers to broadened participation in the regional market (IS2.1), involving in turn reducing trade and investment barriers (IR2.1.1 and IR2.1.2) and increasing the use of financial services (IR2.1.3). Application of this criterion to prioritising potential areas of support requires value-for-money considerations to be invoked – which activities will contribute most to the achievement of the goals and objectives per dollar of scarce resources allocated to them?

The *second* relates to the complementarity of other RCSA sub-strategies. In that regard, there are a range of activities which could be justified on the grounds of their positive impact on regional finance and/or investment, but which fall under other RCSA sub-strategies :

- **Trade** and investment are clearly closely related in that reduction in trade barriers will provide new incentives for investors to locate in smaller SADC countries in order to produce for the regional market. Reduced trade barriers will also encourage upstream investment in production that is spread over more than one country, where the final product is to be sold within the region or exported abroad (in principle, rules of original and duty drawback systems should prevent intra-regional tariffs being a problem at all, but in practice this may be the case or be perceived to be the case by potential investors);

- **Customs** harmonisation and increased efficiency at border posts, particularly if electronic documentation and clearance were to become the norm in the region, would clearly contribute to increased trade, encouraging higher levels of investment. Improved customs performance would also have important positive effects in the financial sphere (higher tariff revenues, better budget planning and more effective budget execution). Collaboration by SADC customs authorities would also make it possible to identify and eliminate transfer pricing, and other types of fraudulent activity and corruption, with additional fiscal benefits for the countries involved.

- **Accounting & auditing** harmonisation will bring an immediate improvement to the investment environment of countries hitherto using unconventional standards and hence to the overall attractiveness of investment in the SADC region. In particular, eliminating differences between approaches and standards in the anglophone and lusophone members of SADC will lower one of important perceived barriers to cross-border investment that exists at the present time.

- Effective **telecommunications** and **transport** systems**,** together with other infrastructure, are essential if investment is to be increased in the region. Adequate telecommunications are particularly crucial for investment in banking and related financial services, which are now heavily dependent on information technology. In order to achieve the requisite levels of efficiency and capacity expansion within SADC, an adequate environment needs to be created to attract private sector involvement in infrastructure while having professional, autonomous regulation in place to properly balance the interests of consumers and investors. RCSA support for the establishment of such regulators within the region could readily be justified in terms of its impact on infrastructural investment and hence, through the 'follow-on' effect identified in Section 3.2, on overall investment. However, this area of support is part of the telecommunications and transport sub-strategies, and, more generally of activities related to IR2.2 (more efficient provision of infrastructure).

The *third* criterion requires RCSA's comparative advantage in the regional context to be identified. In the area of finance and investment, RCSA has the immense resources and experience of USAID to draw upon. The regional focus, however, implies that activities must be at one or two stages removed from the 'coalface'. For example, in pursuing IR2.1.3 – use of financial services increased – a bilateral USAID mission might contribute to enhancing the capital base or operational capacity of particular financial institutions (micro-finance, venture capital etc), while for the region the appropriate level of intervention would be to help establish legal and regulatory systems for the financial sector which are harmonised across the region.

The *fourth* criterion requires consistency with USAID's overall policies with respect to finance and investment. These are clearly spelt out as being that "USAID should promote a system of financial markets that is integrated and relatively undistorted, one that relies heavily on competitive financial institutions, and on policies to facilitate competition"[18]. The emphasis is thus on USAID support policies and institutional mechanisms that ensure effective competition, rather than on capitalising financial entities. This emphasis applies *a fortiori* in the investment sphere, where achieving an attractive investment environment through appropriate policies, legal and regulatory frameworks is a readily justifiable strategy, whereas support to specific investment incentives or strategies would be much more problematic.

A recent USAID Program and Operations Assessment Report comes to very clear conclusions about how USAID can best support the development of "efficient capital markets"[19]: (1) Government oversight is needed to prevent a lack of competitiveness undermining the benefits of developing capital markets in developing countries; (2) donor support should aim primarily at strengthening governmental regulatory frameworks; (3) macro-economic stability is needed for capital market projects to achieve their real potential; (4) in the longer term, the creation of debt markets is essential to reduce the risk of financial crises, such as the recent Asian experience. Extended to the regional level, these conclusions are highly relevant for SADC.

The *fifth* criterion is included to ensure that RCSA support will not displace SADC's own funding and ownership of the finance and investment programme and that RCSA will complement rather than compete with the funding of other donors. In this regard, it is to be noted within the finance and investment sphere that the SADC Central Banks are in a much stronger position in terms of human and financial resources to finance the activities they propose than the activities that fall under the Committee of Treasury Officials. As identified in Chapter 4, the main donor in the SADC finance and investment sector is the European Union. The proposals for RCSA made in the next section take the EU intentions fully into account, and recommend co-ordination with other donors as the need arises.

As was pointed out by several of the people interviewed in connection with compiling this sub-strategy, donor co-ordination has not in the past been a strong point in SADC. Under the new structure, it is suggested that the Deputy Executive Secretary take charge of donor co-ordination. In the transitional phase, it would be useful if this function could be supported by donor technical assistance. RCSA may wish to consider providing such assistance itself, in the form of capacity-building within the Secretariat, or it may wish to encourage the provision of such assistance by another donor. Such support would not be part of the sub-strategy, but is included in the final recommendations (in Chapter 7).

[18] USAID Policy Paper: Financial Markets Development (1998), page i [Section 10].
[19] Fox (2000) [Section 10].

CHAPTER 6: FINANCE & INVESTMENT SUB-STRATEGY

6.1 Overview

The sub-strategy for RCSA support to SADC in finance and investment presented below is intended to cover the period October 2001 – December 2003. The recommended components of the sub-strategy arise from applying the criteria presented in Chapter 5 to the theoretical considerations of how best to give support in this area (developed in Chapter 3) and to the realities of the existing institutions and activities in SADC (discussed in Chapter 4). With SADC's 14 member states at very different stages of development, diverse economic structures and varying levels of economic stability, there is no unique set of interventions which can be unambiguously prioritised to ensure the achievement of the goal and strategic objectives presented in Chapter 2.

The approach, rather, is to recognise that a number of different interventions need to be simultaneously pursued – these will be more important for some countries than others but together will move SADC forward towards finance and investment objectives which in any event can only be fully realised over a long-term horizon. It is in this context of complexity and the need for 'variable geometry' that the criteria for RCSA support (Chapter 5) are important to make consistent choices and arrive at a coherent sub-strategy.

To aid in the presentation of the sub-strategy, two schemas are presented, Figure 1 illustrating the institutional structure and Figure 2 giving a conceptual framework.

6.2 Institutional Channels of Support

As was described in Chapter 4, the activities in the finance and investment sector of SADC have been initiated and managed the Committee of Senior Treasury Officials [CTO] and the Committee of Central Bank Governors [CCBG], with FISCU acting as co-ordinator and providing secretariat functions. Much has been achieved in the sector, with the various activities generally being well managed and usefully contributing to the achievement of the objectives of SADC and its supporting partners (including RCSA). It is recommended that RCSA support in future should continue to be channelled principally through the sub-committees of the Committee of Senior Treasury Officials and the Committee of Central Bank Governors. The support may be in the form of responding to specific project-related requests (prioritised in Section 6.4), but could also focus on a major capacity-building initiative, which is outlined in Section 6.5.

In addition to identifying areas for support by the sub-strategy, it is also relevant to identify areas which should not be supported. In this regard, it should not be part of the sub-strategy to give direct support to the day-to-day expenses of the sub-committees or related structures (such as the SADC Banking Council or the Committee of SADC Stock Exchanges). At this juncture, however, special attention needs to be paid to the restructuring that is proceeding within the SADC Secretariat.

As is illustrated in Figure 1, the co-ordinating link between CTO and CCBG, which used to be FISCU, in future is to be the Directorate of Trade, Industry, Finance and Investment [TIFI]. With the rather lengthy processes that are necessarily involved in the establishment of the new Directorates within SADC, there is a danger that the important and useful finance and investment initiatives that have been taken under the aegis of the Committee of Treasury Officials and the Committee of Central Bank Governors could be jeopardised over the up-coming months.

RCSA, through its Technical Expert, Dr Senaoana, has a critical role to play in ensuring instead that the work of those committees continues in the period while the TIFI Directorate is being established. The Finance & Investment Project Management Unit [PMU] being established with European Union support will also be important in this regard. This PMU will have a technical manager plus two support personnel. It is expected that the PMU administrative staff will *de facto* assume the logistical back-up role that was previously supplied by FISCU and which will in future become the responsibility of the TIFI Directorate. This should mean that the USAID expert will not be requested to take on administrative duties and will enable him to continue to give technical support to the CTO and CCBG sub-committees and projects.

6.3 Schema for Finance & Investment Sub-Strategy Support

The schema in Figure 2 serves to highlight that the key means of attaining finance and investment regional objectives is to strengthen the **regional investment climate.** There are two main aspects:

- **Stable macro-economies:** The efforts SADC has already made towards achieving improved fiscal systems and macro-economic convergence constitute a significant start in this area. If there is a hierarchy of importance, macro-economic stability has to be based on fiscal probity, but to work only on tax issues, expenditure rationalisation and effective budget management would be inadequate. The macro-economic convergence targets which SADC has established go beyond budget deficit and public debt to include inflation and the balance in the external account, thus requiring fiscal policy to be co-ordinated with monetary policy, exchange rate management and the broad panoply of measures needed to ensure international competitiveness of exporters in each country[20]. Over the longer term, convergence should lead not just the abandonment of exchange controls which presently inhibit intra-regional trade and investment flows, but to full liberalisation of current and capital accounts and the ultimate adoption of a common currency.

- **Sound financial systems:** this involves the establishment of adequate legal and regulatory frameworks to ensure that investors can have confidence in the banking and financial services which are available in each country, and that, for the deepening of regional integration within SADC, the standards and regulatory systems are harmonised between the member countries. The importance of this was most recently emphasised at the August 2001 meeting of the Association of African Central Banks by an official from the Bank of International Settlements: “a recurrent problem in many developing countries has been the retarded evolution of the prudential regulatory and supervisory function” this applying both to banks and especially to non-bank financial intermediaries. Experience of a “number of developing and emerging market countries, in Central Europe for example, has shown that domestic savings can be encouraged and private foreign capital stimulated where countries take serious steps to improve their legal, informational, and financial infrastructures. And as Western Europe has shown,

[20] Nathan Associates (2001) [Section 2].

sometimes major institutional reform in the monetary and financial spheres is best accomplished where countries group together with a common objective and programme"[21].

Figure 2 portrays graphically that stable macro-economies and sound financial systems lead to high levels of domestic savings and investment, the emphasis on domestic investment being important for sustainability and for encouraging external investment (as discussed in Section 3.2). High levels of domestic investment should foster higher levels of cross-border investment within SADC and larger inflows of foreign portfolio and direct investment from outside the region. High overall levels of investment will lead to higher levels of growth. As has been demonstrated within the region by Botswana and Mauritius, high rates of growth make it easier to sustain stable macro-economic conditions and sound financial systems. Positive feedback of this kind should lead to self-sustained growth being progressively achieved in the region.

The process is not merely technical, however, and political expediency can certainly intervene to disrupt the painstaking achievements at the levels of intervention amenable to RCSA support. As stressed in Section 3.1, however, one of the expectations which are pinned on the concept of regional macro-economic convergence is that this will give some degree of leverage to 'lock in' macro-economic achievements, making political disruptions somewhat less likely in future.

In terms of the RCSA strategic objectives and intermediate results, achievement of a stable macro-economy is fundamental to the reduction of investment barriers within the region (IR2.1.2), while a sound financial system is a pre-requisite for financial systems to expand and use of financial services to increase within the region (IR2.1.3). The complementarity of sub-strategies in Accounting & Audit, Trade and Customs (relating to IR2.1.1), Telecommunications, Trade and other infrastructure (IR2.2) was presented and discussed in Section 5.2 above. The strengthening of regional capacity to influence democratic performance (SO1) is crucial to ensuring adherence to principles (such as the rule of law) which are fundamental to the regional investment climate. Similarly, advocacy for sustained regional integration (IR2.3) is important to ensure that economic agents and ordinary citizens understand and support the move to greater integration in the region. Once people understand why seemingly disparate concepts, such as the rule of law and stable macro-economic conditions, are necessary for improving the economic welfare of ordinary people, the political space for irresponsible political and economic policies to be imposed on the electorate will narrow.

A final element illustrated in Figure 2 is that of investment promotion. This is deliberately shown as an 'outside' activity to emphasise that investment as such cannot be promoted. The best the investment promotion agencies [IPAs] can do is to try to package whatever investment climate is available to them to 'sell' to potential investors. It is important therefore to make clear that the key element identified in Section 3.1 of harmonisation of investment provisions relates primarily to issues of harmonisation of fundamentals which constitute the investment environment, and only secondarily to harmonisation of IPA strategies for promoting SADC countries individually and collectively as an investment destination.

[21] Bisignano (2001), pages 14 & 18 [Section 8].

This distinction serves to explain the difficulties that have been encountered by the Investment Sub-committee and why it has been criticised for being ineffective. Being in direct contact with investors, IPAs do have an important role in identifying investment climate issues which require attention, but the actual detailed work is then more effectively carried out by other sub-committees with specialised skills than by IPA 'generalists'. Tax harmonisation with the aim of eliminating wasteful competition, which is being addressed by the Taxation Sub-committee, provides a good example.

6.4 Prioritisation of Specific Areas of Support

The unfinished agenda of FISCU is to move towards agreement on a comprehensive SADC Finance & Investment Protocol through an agreed process of working through Memoranda of Understanding in various areas to formal agreements, which will later be annexed to the Protocol. Having the Protocol as an endpoint provides a useful unifying framework for a number of rather disparate activities, but in practical terms it is the activities themselves which contribute to achieving the overall goals and objectives. It is the substance rather than the form which should be looked at to determine priorities and to fine-tune the RCSA sub-strategy during implementation. It is fortunate that RCSA has a high degree of flexibility to do this, because the formal agenda of achieving the agreement and ratification of the Protocol has been adopted and generously supported by the European Union.

The priority list of CTO sub-committees recommended for support from the RCSA sub-strategy are as follows:

- **Macro-economic Sub-committee:** particularly its activities directed at achieving macro-economic convergence, but also work on the impact of HIV/AIDS and debt management.

- **Taxation Committee:** activities such as the proposed tax database[22], research on the impact of tax incentives and harmonisation, work on mining taxation and negotiation with multinational mining houses, eliminating indirect tax barriers to intra-SADC trade, tax treaties.

- **CISNA:** wide range of activities aimed at creating a harmonised regional capital market, investment and insurance services and retirement funds across the region.

Activities of the Investment and Development Finance Sub-committees can be regarded as having lower priority, both in terms of the support schema presented in Section 6.3 and due to the support of other funding agencies. In the case of the Investment Sub-committee, the EU, through its Europe-SADC Investment Promotion Programme, will be providing a high level of support. The SADC Secretariat has nonetheless requested that Dr Senaoana's terms of reference be extended to enable

[22] RCSA has already been approached to provide seed financing for the tax database, which would be compiled for and disseminated to potential investors in the region. Without any assurance of sustainability, RCSA was understandably reluctant to do this. An alternative suggestion to be considered would be to encourage one or more of the accountancy majors to undertake to maintain the database (after the start-up phase) and distribute the results, the *quid pro quo* being access to the official SADC logo and cross-references from SADC and CCBG websites.

him to work with the Investment Sub-committee. Given that Dr Senaoana, through at the same time being fully involved in the work of the Macro-economic and Taxation Sub-committees will be in a position to play a uniquely useful co-ordinating role, it is suggested that this request should be acceded to, while at the same time noting the inherent limitations on the role and effectiveness of the Investment Sub-committee (see previous section). As regards the Development Finance Sub-committee, this is adequately funded by the participating institutions together with special purpose support from other donors.

As noted previously, the CCBG activities are generally fairly well resourced by the Central Banks themselves. RCSA has been supporting some of the work of the **SADC Committee of Stock Exchanges**, and it is recommended that that support be continued. In particular, the RCSA-funded project to consider the establishment of a Centralised Securities Depository, Clearing and Settlement System in Botswana, Malawi, Zambia and Zimbabwe should be brought to fruition[23].

Two new areas where RCSA support could provide useful seed financing are as follows:

- **central analytic unit for macro-economic convergence monitoring** – such a unit has been proposed by the Macroeconomic Sub-committee as part of the recommendations to advance the agenda of macro-economic convergence. Ultimately, this unit might be housed within the TIFI Directorate in the SADC Secretariat, but an alternative, more in line with the philosophy of keeping the Secretariat as lean and streamlined as possible, would be to put out this function to tender over, say, a two year period. A tender to execute the functions of a central analytic unit for monitoring macro-economic convergence could attract bids from government agencies (Ministries of Finance, central banks, statistical offices etc), SADC universities, NGOs (such as MEFMI) and private consulting firms. Award of the tender to a SADC-based institution could be linked to capacity-building within the region (see Section 6.5 below).

- **regional co-operation in banking sector regulation** – while it is gratifying that SADC, through CISNA, is grappling with issues of regulation of non-bank financial institutions[24], it may also be important to initiate activities within SADC to ensure that the highest standards of bank supervision, harmonised across the region, are set and applied by member states. This issue is presently being investigated by CCBG, with specific proposals to be made at the meeting of Central Bank Governors scheduled for April 2002. The RCSA sub-strategy should make provision to support any well-formulated proposals which might be put forward in this area.

While having a clear set of priorities, the RCSA finance and investment sub-strategy should be flexible enough to respond to *ad hoc* requests for assistance that fit into the overall schema proposed in Section 6.3. There should, in particular, be allowance for support to the execution of studies of particular issues, and related workshops, which may contribute to increasing levels of cross-border investment. An example would be a study of the benefits of regional non-financial companies accessing Botswana's

[23] See documents by Saverson in Sections 4 and 9.
[24] As Bisignano (2001) has emphasised, non-bank financial regulation is often grossly neglected in developing countries.

International Financial Services Centre as part of their strategies to expand their operations in the SADC region.

6.5 Capacity-building – a Major Thrust

If RCSA is careful to complement and not compete with other donors and avoids supporting areas that governments and central banks should themselves be funding, the contribution of the RCSA finance and investment sub-strategy would still be critical in the areas identified above, but the programme of support might itself be quite small. There is, however, an area that is not adequately covered at present, which it would be appropriate for RCSA to adopt as a major focus – that of capacity-building. If the proposal below is adopted, capacity-building would absorb a large proportion of the resources allocated to the finance and investment sub-strategy.

The recommendation is for RCSA to work with the CTO and CCBG to develop a comprehensive programme, drawing together the capacity-building initiatives of the key sub-committees, to develop a training model that has been articulated most clearly in relation to the Southern African Tax Institute[25]. The relevant sub-committee initiatives are as follows:

- the Macro-economic Sub-Committee training initiative;
- the Tax Sub-committee's proposal for a Southern African Tax Institute;
- the CISNA proposed clearing-house for the training of regulators;
- the central banks' SADC Training & Development Forum.

The justification for this recommendation lies in the failure at present to address a major aspect of the overall RCSA goal – that growth should be **equitable** as well as sustainable in a democratic southern Africa.Taking 'equitable growth' seriously may in future involve the sort of regionaldevelopment funds which, in the case of the EU, have been used to enhance rates of growth in more backward areas of Europe in order to advance the agenda of macro-economic convergence.

At this point in SADC, a more modest, but nonetheless crucially important issue in obtaining more equitable growth in the region is to reduce discrepancies between the countries in their capacity to formulate and implement sound economic policies. At present, weaknesses in some of the tax departments, ministries of finance, and central banks constitute a major impediment to SADC as a region moving rapidly towards regional macro-economic convergence and the establishment of stable, diverse financial systems.

RCSA is well placed to fund the comprehensive programme of capacity building which is needed to address this deficiency and thereby make a significant contribution to more rapid achievement of the finance and investment objectives, including the goal of more equitable growth within SADC. The programme that is being proposed will also have significant spill-over effects elsewhere in the SADC economies, enhancing the developmental value of USAID support within the region.

[25] See detailed proposal in Section 4.

Some of the principal aspects of the approach that is envisaged are as follows:

- start the process with audits of capacity on the demand side (in tax departments, ministries of finance, regulatory offices etc) and the supply side (regional universities, central bank and other types of training institutions) – such an exercise has already been carried out in some areas (e.g. central banks) and has been requested in others (e.g. Macro-economic Sub-committee)[26];

- to ensure relevance and ownership, have the content, style and duration of training modules agreed by the sub-committees;

- encourage as much synergy across different areas of specialisation as possible;

- support networks of local universities and other training institutions to develop the training materials and offer the courses; where needed, support back-up and train-the-trainer being provided from leading US institutions;

- give particular emphasis to short-release full-time residential courses complemented by distance-learning methods, as this will provide minimum disruption of the employee's contribution in the workplace while maximising the interplay between the work agenda and new perspectives and skills arising from the training;

- support research that feeds directly into the teaching activities;

- encourage relevant materials to be incorporated into under-graduate and post-graduate training so that new generations of economists will be better prepared for careers in ministries of finance and central banks, and also in the private banking and financial services sectors.

The last aspect is significant in countering the perennial Achilles' heel of capacity building for staff within the public sector of most African countries. That is that trained people use their enhanced skills as a means to move out of the public service jobs for which they were trained. Provided they remain active in finance and investment related activities, the countries will continue to derive benefits from their training, but there is still then the problem of replacing such personnel (and those now dying prematurely due to the HIV/AIDS pandemic) within public sector structures. Having courses in university curricula which directly prepare students to play useful roles within a country's Ministry of Finance or central bank, would certainly help to obviate this problem.

If the above proposals are adopted in full, the employment of a full-time expert to co-ordinate and manage the capacity-building component of the finance and investment sub-strategy would be warranted. Given the similarities in the approach to the African Economic Research Consortium joint masters programme, the detailed design of the programme and its subsequent management would benefit from interaction with the AERC.

[26] A formal proposal for such an audit has been drawn up [Section 4].

CHAPTER 7: SUMMARY & CONCLUSIONS

7.1 Sub-Strategy Summary

The sub-strategy which has been recommended for RCSA to adopt for its support to SADC in the areas of finance and investment over the next two years is based on improving the stability of the macro-economies of the region and establishing sound financial systems, thereby enhancing some of the most fundamental factors determining the region's investment climate. The institutional structure which SADC has established for the finance and investment sector, consisting of entities under the Committee of Senior Treasury Officials and the Committee of Central Bank Governors, has generally performed well over the last 3-4 years. The sub-strategy recommends that assistance continue to be given to these structures, with priority to the following sub-committees:

- Macro-economic Sub-committee
- Tax Sub-committee
- Committee of Insurance, Securities and Non-banking financial Authorities [CISNA]

With the re-organisation of SADC into Directorates based in the central Secretariat in Gaborone, the national sectoral responsibilities are being transferred. The Finance and Investment Co-ordination Unit, previously based in the Department of Finance in Pretoria, has already been disbanded. Its functions will in future be taken over by the Directorate of Trade, Industry, Finance and Investment, but in the meantime RCSA, through its technical expert, Dr Senaoana, and the EU-sponsored Project Management Unit which is shortly to be established in Gaborone, have a crucial role to play in ensuring that the work in the sector continues unhindered during the period of transition (it may only be towards the end of 2002 that the Directorate will be fully operational).

The contribution of RCSA to the work of the sub-committees and to maintaining the co-ordination and momentum of activities will be crucial, but a major additional thrust which is recommended in the sub-strategy concerns **capacity-building**. RCSA is well positioned to integrate and enhance synergies between capacity-building proposals which have been formulated by the various Ministry of Finance and Central Bank committees and, by promoting networks of local universities and training institutions to deliver the training that is required, can make a significant and lasting contribution to the region.

7.2 Requirements for Success

Although overall economic growth within SADC remains at a low level, there are clear signs of dynamism in the region, not least in the financial services sector. A number of local banks have opened branches in other SADC countries in recent years and major new initiatives, such as the International Financial Services Centre in Botswana, are attracting interest from both financial and non-financial companies. These developments are likely to be the pre-cursors of a significant increase in regional investment activity.

The role of the SADC Ministries of Finance and Central Banks is to facilitate and support private sector developments of this kind. Much has already been achieved since the finance and investment sector of SADC was created, but there is now a degree of uncertainty due to the change in the co-ordinating role from the nationally-based FISCU to the new Directorate to be based in the SADC Secretariat. It is important for SADC and the donors involved, particularly RCSA, to reassure the sub-committees of continued support and appreciation of the work they are doing.

At the level of the Secretariat as a whole, RCSA might offer assistance to the Deputy Executive Secretary in co-ordinating donor support to SADC, particularly during the transition to the directorate structure. A major outstanding issue is how the new structure is to be financed: RCSA could play a catalytic role here in bringing the Secretariat and the SADC Tax Committee together to ensure that the best solution for the region is achieved.

ANNEX 1: ANNOTATED LIST OF REFERENCES

The references consulted in this study cover a wide spectrum of documents, varying from bureaucratic reports to full-scale academic-style studies. For convenience, the references have been organised into the 10 categories listed below, with further sub-divisions, as necessary, within those categories. Key papers in each sub-category are identified by asterisks (**). In Sections 2 and 3, for example, the highlighted papers give the objectives and strategies being pursued by the various sub-committees. Otherwise, the papers highlighted are the ones most relevant to the sub-strategy.

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