Briefing Note: FDI that supports development priorities - Measuring the "quality" of foreign direct Investment

Like other developing countries, South Africa aims to attract foreign direct investment (FDI). Coming into The Presidency, President Cyril Ramaphosa prioritised increased investment – foreign and domestic – setting a five-year US$100 billion (over R1 trillion) target for new investment. This intensified drive to increase investment raises the question of "quality" of FDI into South Africa. That in turn points to the importance of developing tools or mechanisms to assess FDI, with the aim of maximising its benefits towards achieving inclusive industrialisation. It is important to understand the extent to which projects contribute to South Africa's development priorities – at a granular level, essentially being able to measure their value-add against developmental priorities.

Empirical studies have shown mixed results on the link between FDI and economic development. Benefits include raising productivity and tax revenues, while the positive spill-over effects include bringing in new technology and technical knowledge, upgrading skills and creating employment. However, increasing investment in itself, is not as important for sustainable growth as the quality, type and composition of investment. Different types of investment and objectives for investing generate varying benefits. For example, greenfield investments are likely to have greater gains for the host country than a company investing for market share through a merger or acquisition.

While there are variances in the definition of "quality FDI", there are some common characteristics in descriptions of the concept. The UNCTAD 2006 World Investment Report describes "quality FDI" as "the kind that would significantly increase employment, enhance skills and boost the competitiveness of local enterprises". The importance of technology transfers and upgrading and enabling domestic companies to access global markets is often highlighted as well. So is the importance of maintaining social and environmental standards. The emphasis is that FDI should be judged on its nature and qualities rather than quantitative measures on their own.

There are examples of tools or guidelines for measuring quality FDI. The Organisation for Economic Cooperation and Development has undertaken a project, the "FDI qualities project", that in part aims to provide governments with relevant instruments for this purpose. They identify five "FDI qualities indicators", namely productivity-innovation, skills, job quality, gender and carbon footprint. These were selected on the basis of an assessment of how FDI can contribute to specific sustainable development goals.

South Africa has the foundations from which to develop quality FDI outcomes and indicators such as local content agreements, social and labour plans in mining, and local community development requirements for renewable energy projects, among others. The development objectives set out in policy and plans are a good basis for developing criteria or indicators against which the quality of FDI can be assessed or measured. Different industries have different needs, necessitating the need for criteria to be tailored for specific industry needs.

While FDI is important, it should not be pursued or accepted without being interrogated, or questioned for its appropriateness for South Africa's needs. Having a mechanism to evaluate the quality of FDI projects could help indicate to both industry and government, in as clear terms as possible, how far FDI is going in contributing to development objectives, beyond the quantitative measures on inflows and outflows.