

# Revealing the Perceived Legal barriers Affecting China-Africa Investment Relationship

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## I. Overview

The investment relationship between China and Africa is significantly growing within the past three decades. The 2013 World Investment Report launched in Tanzania reveals that China is the third partner investing in Africa after United States of America and Japan<sup>2</sup>. This means that African states should be prepared to welcome these blessings by preparing good investment environment to attract Chinese foreign investor especially by reviewing their legal regimes regulating investments in order to remove the barriers that might affect the growing China investment in the Continent.

Among of the common legal challenges that are perceived to affect Investment between China and Africa includes ; Security of Investment from expropriation by the host countries , multiplicity of investment laws, Discrimination between foreign investors and domestic companies , Settlement of disputes between foreign investors and the citizens of the host country, existence of double taxation regimes , Cumbersome procedural requirements in registering companies and obtaining necessary business licences , Strict restrictions in environmental issues , Rights and Obligations of foreign investors to the host country and existence of too much incentives to foreign investors . This paper will address these challenges in detail and examine their implications to the future of China-Africa Investment friendship.

There are several questions to be considered in discussing the above issues, among of the questions are; what are the basic laws governing foreign direct investments in Africa? How are these laws prepared? For what purpose are they prepared? What is the nature of these laws? How far can these laws facilitate the growing development of foreign direct investments between China and Africa? What are the key legal challenges that affect investment growth between China and Africa? What should be done to these laws to promote good investment climate between the two partners? The important thing is to have the laws with balance of interests of investors to gain profit from their capital invested and the host countries desires to realize development from the foreign investors.

## II. China- Africa relationship a brief History

The relationship between China and Africa has a long history; this history dates about five hundred years ago but the recent influx if Chines investment in Africa begins in 2000 when China formally announced its intention to “go global.” The concept of ‘Going global’ involved both opening its doors to foreign investors and looking outward for opportunities to invest its vast foreign currency reserves. Following this policy decision, Chinese investment in Africa boomed<sup>3</sup>.

Around 1960’s at the time of Independence, most of African States had negative attitude towards foreign investors with the fear that it will extend neo colonialism. At this time African states maintained very rigid laws which discourages private investors and some states went even to the level of nationalization of private properties.<sup>4</sup> These changes were necessary in order to stabilize the economy of the newly independent states and restore the hope of the Africans who had been marginalized by the colonialist for decades

In early 1980’s , the World Bank and International Monetary Fund ( IMF) made a significant contribution to this growing investment relationship between China and Africa through the Structural Adjustment Policy which among other things required African states to open their market to foreign investors and privatize some public sectors for private investment. With this wing of economic reforms, foreign inventors started to massively invest in Africa so did the Chinese too.

However, the old history of China’s relationship with Africa predated the 2000 announcement. According to historians, the historical evidence shows that, economic and political relationships between China and Africa has existed as far back as five hundred years ago, scholars generally divide China’s commercial contact with Africa into three phases, beginning in 1850<sup>5</sup>. The last phase is the most relevant for the purposes of

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<sup>2</sup> The World Investment Report for 2013

<sup>3</sup> Brook Sulton , *A Bad Good Deal; The Challenges of China Foreign Direct Investments in Africa* available at <http://jurisafrika.org/html/pdf> retrieved on 28/October/2013

<sup>4</sup> C.P. Maina & S.J Mwakaje, *Investments in Tanzania; Some Comments-Some Issues* , Friedrich Ebert Stiftung, Dar es Salaam, 2004 pg 13

<sup>5</sup> Ibid

this paper it began in 1990 throughout 2000 up to present and has been especially noticeable in the past 10 years. The last phase characterized by the movement of Chinese companies into African countries mainly in the areas of construction, mining, and oil extraction. This last phase has been successful following the China's policy of non-interference in domestic affairs of the host countries unlike the American and U.E investors.<sup>6</sup>

The history reveals that, China is committed to invest in Africa basing on the fact that Africa is a continent blessed with so many opportunities that can attract foreign investors from big economy states. An important question to ask is 'does African States have a sound legal regime that will guarantee win-win investment relationship between China and Africa?' This paper will therefore study few areas which presents legal challenge toward a bright future of China-Africa investment relationship. It will also give few comments on the prospect of a way forward.

### III. Conceptual Overview of the Study Problem

International Investment as any other component of international trade has laws regulating it. These laws define the nature of the prelateship between the foreign investors and the host countries<sup>7</sup>. However, these regulatory regimes are designed to facilitate investment but not to discourage it. This paper is designed to answer the question as to what extent do the legal framework regulating foreign direct investments between China and Africa discourage investment relationship between the two partners ? And ultimately recommend the way forward to strengthen the investment regulatory regimes to promote the development of China-Africa Investment relationship.

It is important to make this analysis because foreign investor makes investment decision after considering the risks involved in investing in a particular country ranging from security issues to sustainability of the particular investment project to bring the benefits intended.<sup>8</sup> This is basically done by looking at the nature of investment laws of the particular host country if they are friendly to the foreign investors or not.<sup>9</sup>

The main problem comes from the fact that, investment laws have the tendency of having competing interest where by the host countries are interested in tightening their investment laws to protect domestic companies and their development interests while the investors are looking for flexibility of the laws to allow maximum profit realization from the capital invested. If there is no balance between the two competing interests, the investors will not be attracted to invest in the particular country and the host country will lose revenue expected from the foreign investors.

This paper examines the common legal challenges that affect development of China-Africa investment relationship and at the end it contains recommendations to reduce or eliminate the legal barriers in order to have laws which facilitate win-win investment between Africa and China.

### IV. Scholarly Observation on the Legal Challenges facing China-Africa Investment Friendship

This study is not a new study, since other authors have already written on this subject. However, there is a need of revisiting what they wrote in order to note their significant contributions and point out few lacunas in their ideals so as to justify that this article will bring some new insights to add from where previous authors have ended especially in the areas of legal perspectives with the view of promoting the growing China –Africa investment relationship to next the level of development.

**Simon Lester** has written about *Policy Analysis; Liberalization or litigation? Time to Rethink the International Investment Regime*<sup>10</sup>. In one of the areas of his discussion he examines international investment regimes pointing out that, most of the international investment laws seem to have too much protection of foreign investors from bad treatment in the host countries despite of the fact that the current political climate in Africa has significantly changed into democratic states with no more expropriation policies. However, he poses a question as to whether these laws which protect foreign investors from expropriation regimes are relevant in contemporary world were rogue governments who treats foreign badly has fallen considerably?

This paper will examine the nature of the current investment regimes and answer this question as to; whether there is a need of having investment laws which provides more protection to foreign investors to assure them that there will be no more expropriation by the host countries regimes. I think now there is a need of having the laws which focuses on balancing the rights and obligation of foreign investors and host countries against one another in order to promote win-win investment environment.

Another though comes from **Brook Sulton** who has written about *A Bad Good Deal; The Challenges of China*

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<sup>6</sup> Ibid

<sup>7</sup> C.P. Maina & S,J Mwakaje, *Investments in Tanzania; Some Comments-Some Issues* , Friedrich Ebert Stiftung, Dar es Salaam, 2004

<sup>8</sup> Ibid, pg 29

<sup>9</sup> Ibid

<sup>10</sup> <http://www.cato.org/publications/policy-analysis> retrieved on 29/October/2013

*Foreign Direct Investments in Africa.*<sup>11</sup> This author writes about the general challenges revolving around Chinese Investments in Africa. He points out weak investment regulatory frameworks as one of the main challenge. According to his observation, most of the African investment laws lacks uniform/common standards of treating investors (investors are treated differently in the same investment laws) something which results into conflicting decision in enforcing the laws against investors in the host country. Another problem with the African investment laws is that, they tend to give too much discretionary powers to the political leaders to decide on investment issues these results into mixing political issues and serious investment decision. However, the author leaves a vacuum by not proposing the way forward to curb the situation so as to promote good investment relationship between the chine's investors and the African states.

**Honest Posper Ngowi**, a Tanzanian author conducted research on *Foreign Direct Investments (FDIs) Roles in Economic Transformation for Poverty Reduction: What Does it Take in a Tanzanian-type Economy?*<sup>12</sup> in this report the researcher presented few issues affecting investment performance in Tanzania and one of the issue he raised is poor investment policy and laws. According to his findings, most of the African states (Tanzania inclusive) have investment laws which seem to concentrate much in attracting foreign investors at the expense of host country's development. In his observation he insists that host countries needs to have regulatory frameworks that will attract foreign investment at the same time facilitating the FDIs Contribution into the host countries development process. However, like other authors, he too does not examine the way forward towards the best investment laws that will cure the problem and strengthen the investment regimes but he poses a question for further research.

All these authors examine the general investment challenges without paying special attention to legal regime which is the subject matter of this study. They also leave a vacuum of way forward to solve the challenges. This study will underscore the perceived legal challenges and their implications to the China-Africa Investment relationship and propose the way forward to improve the investment climate to have a balanced legal regime which quenches the thirsty of both foreign investors to realize investment benefits and of the host country to realize the benefits of foreign investments in national development.

#### **V. Leading Questions in the Discussion**

The guiding question in preparing this study surrounds the followed key issues

- a. The Current Investment Laws in Africa are not relevant to accommodate the growing Investment relationship between Africa and China since these laws have many legal challenges because they were made with the view of protecting domestic investment interests from neo-colonialism threats
- b. There is a need of reviewing the Current African Investment laws to remove the inherent legal challenges in order to facilitate win-win investment relationship between china and Africa. This is also important to harmonize conflict of interests between foreign investors, host countries governments and citizens of the host country in investment relationship between the two partners.
- c. There is a need of having Regional framework which provides for uniform investment principles to be adhered by investors and member states (host countries) in preparing and enforcing investment laws in order to harmonize domestic laws in Africa host countries . Eg embody principles of respect for host countries sovereignty, Sustainable Utilization of Natural resources, Impartiality in dealing with investment disputes, Non discrimination between domestic investors and FDIs, The duty to transform investment benefits to the community development in the host countries. etc

#### **VI. Basic Laws governing International Investments in Africa**

International investments are governed by two types of regimes, the bilateral investment Agreements concluded between the foreign investors and the particular host countries or those prepared by the Multinational Investment Agencies like the International Centre for Settlement of Investment Disputes and Multilateral Investment Guarantee Agency (MIGA) and on the other hand the domestic investment laws of the particular host country (the laws of the country in which investments are done. In this discussion a case study of domestic investment laws will be based on Tanzania for the fact that Tanzania is also a key investment target for chine's investors.

##### **a. Convention Establishing Multilateral Investment Guarantee Agency**

This is an agreement prepared by World Bank to establish Multilateral Investments Guarantee Agency in order to provide guarantee to investors wishing to advance investment loan from the World Bank and provide for the terms and conditions of the MIGA guarantee to FDI seeking the Agency cover. For example this agreement contains provision which requires MIG to provide guarantee to investments against expropriation of investment projects by the host countries, unforeseen fluctuation in currency transfer, breach of contract by the host country which have the effect of depriving a particular investor to recover compensation from the breach of the said

<sup>11</sup> <http://jurisafrika.org/htm/pdf> retrieved on 29/October/2013

<sup>12</sup> <http://www.repoa.or.tz/documents/s3b.pdf> retrieved on 29/October/2013

contract and protection from civil wars in the host country.<sup>13</sup>

This Convention is an important law because majority of the host countries are obliged to sign in order to guarantee FDI of their protection from investment risks like expropriation. Tanzania for example assures foreign investors of their protection by making a police statement that it has signed MIGA Convention which guarantees foreign investor of their protection through the MIGA guarantee.

**b. *Convention on the Settlement of Investment Disputes between States and Nationals of Other States***

This convention establishes ICSID as an International Centre responsible for Settlement of Investment disputes between the foreign investors and the government of the host countries and provides for various methods and procedures that can be followed by foreign investors and host countries to settle investment disputes between the host countries and the respective investors. For example this convention provides for the need of having conciliation, negotiations and arbitration as methods for settlement of investment disputes arising between the foreign investors and the host countries than taking unilateral measures.

This Convention is important because it gives guarantee of justice to the investors in settlement of disputes with the host countries. There are moments in which investors falls into disputes with the host countries and they need an impartial organ to decide the dispute. This becomes easy if the parties agreed to submit their disputes before the ICSID which is an impartial organ that can guarantee justice to both parties involved in the dispute. Therefore most of the states signs this convention in order to guide them in the event of disputes with the host country.

**c. *Bilateral Investment Treaties***

These are the agreements concluded between the host countries and the particular investor stating the terms and conditions of the investment relationship. This is the main source of international investment laws because majority of the investment issues are governed by the BITs. For example these agreements may state the rights and obligation of the parties to one another, the scope of the investment, issues relating to institution and methods to be used in settlement of disputes and the basic principles to be observed by the parties as guidelines for their investment relationship. Recently China has been making a lot of these treaties with African States. For example in October 2013 China signed about 7 BITs with the Tanzanian government

The World Trade Organization did not prepare a uniform International Agreement for international investment recognizing that international investment is a fragile component of international trade and each state has its own preferences in making investment decision. Therefore this part of law was left to the hands of the particular states and the respective investor to negotiate.

**d. *Host Country's Investment Laws***

These are multiple investment policy and laws prepare by the host countries to regulate investment matters at national level. Most of these laws relates to the , the national Investment Policy , National Investment regulatory framework (The National Investment Acts), The national laws governing acquisition of business licences for investment, the labour laws , the land laws, the mining laws , the tax laws and the national environmental laws.

Tanzania as the case study for this study has a list of investment laws mentioned in the National Investment Guide of 2007. These laws include;

- Tanzania Investment Act No 26 of 1997
- The Business Activities Registration Act of 2007
- The Employment and Labour Relations Act No 6 of 2004
- The Immigration Act of 1995
- The Income Tax Act of 2004
- The Value Added Tax Act of 1997
- The Land Act of 1999
- The Companies Act of 2002
- The Environmental Management Act No. 20 of 2004
- The Mining Act of 2010
- The Foreign Exchange Act of 1992

NB; Other countries almost have similar investment laws for most of the African states legal system has the tendency of having closely related laws depending on the former colonial background. If they were colonized by the same master they adopt a uniform legal system. For example all the former British colonies uses common law legal system which consists of closely related systems of courts and laws.

## **VII. The legal Challenges affecting African-China Investment Relationship**

This part is the main area of the study. Legal challenges referred here means, the obstacles inherent in the legal

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<sup>13</sup> Article 11 of MIGA Convention

framework governing investment relationship between China and Africa. In international trade language, these are also referred to as non tariff barriers to international trade. States started to adopt these measures when the tariff barriers were removed by the WTO Agreements like the General Agreement on Trade and Tariff (GATT).

*a) Too many incentives to investor than their obligations to the host countries economy*

Most of the African states investment laws provide many incentives to foreign investors than their obligation to the development of the host countries economy. For example the laws grants the investors with unconditional tax holidays, gives them the red carpet treatment in obtaining bank loans, gives them tax incentives and first priority in investing to some important natural resources like mining at the expenses of the local miners. All these treatments are intended to attract foreign investors and assure them of their protection from expropriation of their properties with very little obligations to contribute to the development of the host countries. Prof. Maina Peter from Tanzania perceives this as investors investing nothing but taking everything away<sup>14</sup>.

In absence of balance between foreign investors interests and host countries interests, investors will avoid their corporate social responsibilities to the investment surrounding communities hence provoke them to take laws into their own hands because they don't see the benefit of having investors. In absence of obligations, investors are considered as neo colonialists who aim at exploiting hence they lack cooperation from the local communities.

*b) Inadequate procedures regulating settlement of disputes between the citizens of the host country and the foreign investors*

Most of the investment laws address the procedures of settlement of disputes between the investors and the host government however there are other disputes which involve the ordinary citizens surrounding the investment project and the particular foreign investor. It becomes difficulty to address these problems because there are no open procedures which the ordinary community members can follow to deal with a foreign investor directly. This lacuna forces some citizens to take law into their own hands and threaten the investors and / or destroy the investor's properties

*c) Cumbersome Procedures of Obtaining Business Licence*

This is one of the biggest legal challenges of African investment laws. In most countries, the investment laws require a person to go through some long processes and prepare so many attachments in order to obtain investment licences. These procedures may sometime be as barriers for people to invest in a particular country and make investors give up and shift their capital to some other destinations were the laws are flexible. For example, there are laws which requires quires an investor who is applying for investment licence to make a procurement plan which guarantees that they will procure goods or services available in local markets<sup>15</sup>. This is unnecessary because some of the local services or goods are not in the customs of the investors and may not be available from local sources.

*d) Multiplicity of Investment Laws*

Multiplicity of investment laws refers to existence of several pieces of laws regulating investors. This is a problem because sometimes investors overlooks some of the laws and falls into a trap of legal actions by the host countries. It is very hard for the investors to remember every piece of law affecting their investment venture because they are too many. Host countries are trying their best to harmonize the functions of institutions dealing with investors to have a one stop centre but very little efforts are being done to harmonization of investment laws. For example, Tanzania has the following laws affecting investors at a go; Tanzania Investment Act No 26 of 1997, The Business Activities Registration Act of 2007, The Employment and Labour Relations Act No 6 of 2004, The Immigration Act of 1995, The Income Tax Act of 2004, The Value Added Tax Act of 1997, The Land Act of 1999, The Companies Act of 2002, The Environmental Management Act No. 20 of 2004, The Mining Act of 2010, The Foreign Exchange Act of 1992

*e) Existence of discretionary powers in the hands of politicians to determine investment matters*

Investment laws grand too much powers in the hands of political officers like ministers to determine some serious investment matters like tax rates, tax incentives and termination of investment licences if some discrepancies are discovered. This tendency creates rooms for corruption. These politicians use their powers illegally to harass some investors who go against their personal interests or refuse to offer bribery. For example the Tanzania Income Tax Act<sup>16</sup> empowers the minister to vary or exempt a person from paying tax on his own opinion. This invites corruption to some investors who might be interested with the exemptions. The laws must have a base line of examining tax exemption applications by the ministers.

*f) Frequent Change of tax laws without consultations*

This is the problem attached with annual changes of government tax laws reviewing the tax rates to the extent of making the investment climate uncertain to the foreign investors. The host countries make changes to upgrade

<sup>14</sup> C.P. Maina & S,J Mwakaje, supra, pg 29

<sup>15</sup> Section 28(3)(e) of the Tanzania Mining Act No 14 of 2013

<sup>16</sup> Section 10 of the Tanzania Income Tax Act

taxes rates almost every year. This problem makes the investors unable to predict the anticipated returns from their investments following frequent review of tax laws without even consulting the stake holders like the respective investors to be affected. For example the minister for finance in Tanzania makes review to the tax laws almost every year that he submits the new budget to the house. For example in 2013 he made changes to the telecom services which requires every customer to pay sim card tax of Tsh 1000 per month something which raised concern to the telecom service operators.

*g) Existence of Discrimination between Foreign Investors and Domestic Companies*

This results from the tendency of host countries providing some law which grants first priority treatment to domestic investors or nationals of the host country at the expense of foreign companies<sup>17</sup>. This tendency results into double standard in implementing the laws and they also cause unfair competition to the foreign investors. It is perceived that not all domestic companies cannot meet international competition against FDIs but it is just the fear of unfair competition from the developed countries investors. It is high time for the African states to rethink about this practice and revisit their decision in order to allow free competition in international investment that will guarantee close partnership between the local and foreign investors and ultimately result into technology transfer. For example The Tanzania Mining Act contains a provision which reads that “A mining licence for mining gemstones shall only be granted to applicants who are Tanzanians.”<sup>18</sup> The same provision appear in the Ghana Investment Promotion Centre Act which states that “investment specified in the First Schedule ( hair dressing saloon, barbershop, retail shops and tax service) cannot be done by a non citizen”<sup>19</sup> These provisions may not be necessary in the new China-Africa relationship which requires investment be done with the view of promoting rule of law or equality between people from china and the local people in the host countries.

*h) Immigration restrictions*

The investment laws in most of the developing countries tend to have limited immigration quotes which restricts movement of personnel to supervise the investment projects. It is very awkward to restrict qualified personnel while at the same time we need many experts to transfer technology to local citizens. For example the investment laws of many states provides for Immigration quote of up to five persons during start-up of the project<sup>20</sup>. This fixed number cannot save in big projects which require huge number of qualified staffs. For Chinese investors, this approach is not relevant because they insists on investment that links people and not states i.e they want investment relationship which goes down to connect people and not states.

## VIII. Conclusion

The above challenges discussed reflects that, despite of the efforts of liberalizing international trade and investments, non tariff barriers (legal obstacles) are still maintained in domestic investment laws of the investors host countries in Africa and in the Bilateral Investment treaties. These barriers are maintained with the view of controlling foreign investors in conducting their investment business in the host countries and protecting the home economy of the host countries.

The technical legal barriers maintained by some developing country states is the source of underperformance of investment in some of the developing countries economies do to investor’s tendency of avoiding those barriers and opting to shift their capital to other countries where the investment laws are flexible enough to attract foreign investors.

The current developing countries investment laws were prepared with the view of attracting foreign investors and protecting them from the fears of expropriation by the host countries but that age is long gone and the African states should rethink of having the laws which concentrates in balancing the interests of the foreign investors and the home countries so as to enable the investments done in the country to promote development of domestic countries economy. For example by reviewing the rights and obligation of foreign investors to the home country

## IX. Recommendations

The legal barriers available in African states investment laws can be avoided through the following ways

- a) Review of the current investment laws to accommodate the challenges of the rapid growing relationship between China and African states, Example revisit the rights and obligations of the China’s investors to the host countries economies
- b) Having a regional framework which stipulates the basic principles to be observed by the host countries in preparing their domestic investment laws, this will ensure certainty of investment laws in the region. Eg principle of respect for human rights in the host country, sustainable utilization of natural resources, non discrimination between the domestic companies and the foreign companies, principles of respect to

<sup>17</sup> Section 2 (2) of the Tanzania Investment Act of 1997

<sup>18</sup> Section 8(3) of the Tanzania Mining Act of 2010

<sup>19</sup> Section 18 of the Ghana Investment Centre Act

<sup>20</sup> Section 30 of the Ghana Investment Promotion Centre Act and 24 of the Tanzania Investment Act No 26 of 1977

- the sovereignty of the host country, principle of impartial justice in host countries courts etc
- c) Having a participatory and transparent approach of making investment laws which reflects the interests of the host country's government, the foreign investors and the ordinary citizens of the particular state

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