LESOTHO

FOREIGN INVESTMENT PROMOTION STRATEGY

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EXECUTIVE SUMMARY

1. Lesotho is a land locked country geographically located within the Republic of South Africa (RSA). About 70% of the labor force of 750,000 is employed in the informal and agricultural sectors, most of them in the rural area. About 20% is migrant workers in the RSA (most of them employed in mining). The formal sector employs the remaining 10% of the labor force. The manufacturing sector employ about 9,500 workers. The employment in the formal sector is expected to grow in the next decade at a rate of 3.3% per annum (or 2,000 workers a year). The country offers limited opportunities in commercial agriculture due to difficult climatic conditions (the high risk of drought), a small arable land base (only 12% of the total land area of the country is cultivable) and the traditional land tenure system. The country has very limited natural resources except building materials. Therefore most of the future employment opportunities will have to be created in the manufacturing, construction and service sectors. The four post-independence development plans of the Government of Lesotho (GOL) progressively established the manufacturing sector as the main engine of growth and employment. Since the small domestic market cannot hope to absorb the scale of production necessary for efficient industries, the output of labor intensive industries must be aimed at export markets. The local private sector is small and has limited experience in production for exports. Therefore Lesotho must look for foreign investors for its export oriented investment drive.

2. Most of the exceptional annual growth of 18% in manufacturing over the last 20 years was due to foreign investment in labor intensive export oriented sectors. In 1986, foreign and joint venture firms accounted for 70% of the employment in manufacturing and 90% of manufactured goods exports. The emerging structural pattern of manufacturing was recently being questioned in three areas. First, most of the Foreign Direct Investment (FDI) came from the RSA and the Newly Industrialized Countries (NIC's) and is thought to be motivated by temporary political considerations (avoiding sanctions) or economic ones (avoiding trade quota limitations). Second, there is concern over the pace of development of the indigenous owned enterprises and the foreign domination of the manufacturing sector. Finally, there is growing awareness of the need for industrial deepening by promoting backward and forward linkages to the existing FDI and resource based activities.

3. Lesotho was actively engaged in foreign investment promotion from 1979 to 1982. During that period the Investment Promotion Unit of LNDC was actively promoting labor intensive foreign investment using image building, investment generating and investor services techniques. It had a good promotion strategy, was well funded and received technical assistance from the experienced Industrial Development Authority of Ireland. Though constrained by staffing problems, the effort appears to have resulted in a modest flow of FDI mainly from the RSA and NIC's. It was aborted by a change in investment policy in 1983 that followed a foreign policy change of active involvement in the RSA conflict. The change in promotion policy at that time was rational because the foreign policy stand increased the risk of instability to investors and engagement in any massive promotion

activities did not make sense.

4. Since 1983 the foreign investment promotion function in Lesotho has been carried out by the Projects staff of the Appraisal Subdivision, the Market Support Unit and the Public Relations Manager of the LNDC. The policy has been based on the strategy of promoting resource based projects (most of them prepared " in house "), joint ventures with local investors and an attempt to diversify away from the traditional RSA source of FDI. Investment promotion activities have been constrained by the very limited resources allocated to the promotion function.

5. The previous promotion efforts were only partially successful because of the following reasons:

-- the first promotion effort (1979 - 1982) had a slow start-up due to recruitment problems. Half the period of four years was used to recruit and train the necessary staff. When the operation became functional it was partially effective because of poor investor's targeting. The promotion staff had no project appraisal training and therefore the pre-screening of firms prior to making presentations was very weak. It resulted in a low ratio of site visits and implemented projects. The effort was aborted too soon for effective measurement of results. Because of the long decision and implementation period for a foreign investment initiative, the two years operational period is too short to measure the effectiveness of the promotion efforts. Nevertheless, the effort still resulted in a stream of labor intensive FDI mainly from the targeted RSA.

-- the promotion effort since then has been based on the promotion of resource based capital intensive projects with local majority ownership preference. The projects have been generated by LNDC. There have been limited investors outreach effort and limited services are provided to investors in labor intensive activities that do not need LNDC services.

6. Based on our perception of the desires of the GOL and the promotion strategy which appears desirable, we recommend the re-introduction of an active promotion effort in Lesotho. To be successfully engaged in a foreign investment promotion program the GOL needs to improve the investment environment and the investment policy instruments, to develop a well coordinated promotion strategy and to establish the Investment Promotion Center (IPC).

ENVIRONMENT AND POLICY

(i) The most important recommended changes in the environment are:

- improve the provision of **industrial infrastructure** by:

- easy, unrestricted and long term access to land and industrial buildings.

- a well coordinated and funded effort to provide: electricity, roads, telecommunications, water and sewage to industrial sites.

- improving the land and air transportation services available to investors.

- adopt a **wage policy** (minimum wage) that is highly sensitive to the competitive position of Lesotho compared to other countries in the region.

- deregulate industrial and export trade activities by easing **licensing** and permit requirements.

- automatic availability of **work permits** (certificate of employment) to key personnel in foreign invested enterprises.

- abolish the **local ownership requirement** in resource based projects.

(ii) Improve the investment policy instruments by :

- abolishing Pioneer Industry status, and elimination of the Pioneer Industries Board and the tax holidays and tax allowances it can grant.

- reduction of the manufacturing corporate income tax rate to 15%.

- streamlined and well publicized access to the use of the Financial Rand by foreign investors.

- improvement of the training grants system.

STRATEGY

The proposed promotion strategy includes:

- the promotion of foreign investment in a <u>diversified</u> list of labor intensive manufacturing sectors for exports to the RSA, Europe and the U.S.

- the targeting of RSA foreign investors for direct promotion efforts, and the NIC's, Europe and the U.S. for image building efforts (mainly missions and seminars) with the help of the home governments where feasible.

- building first an investor services capacity in Lesotho and followed by than investment-generating activities in the RSA, and image building activities in the NIC's, Europe and the

U.S..

- targeting quality (financially appraised) investors experienced in international trade and with a minimum size of 50 employees for RSA firms and 250 employees elsewhere.

- developing a new set of promotional materials that will reflect the change in FDI policy and the new institutional setup.

INSTITUTIONAL STRUCTURE

The proposed institutional arrangement include:

(i) Establishing the Investment Promotion Center (IPC) as an independent unit within LNDC (directly under the Managing Director). A special Sub-Committee of the Board of Directors of LNDC will be responsible for its work program, approve its budget and supervise its performance. The committee will be chaired by the P.S. Trade and Industry and its members will be the Honorary President of the LCCI, P.S. Finance, P.S. Planning, and the Director of the IPC.

(ii) The IPC main functions will be the promotion of foreign investment through :

- assisting the GOL in evaluating the investment environment and investment policy and in proposing the necessary changes.

- identification of potential investors.

- provision of information.

- expediting the processing of applications and permits

- representing investors within the public and private service and providing key introductions.

- identifying and working to eliminate specific problems encountered by investors (e.g. lack of infrastructure).

(iii) New IPC staff will need training in project evaluation and investment promotion techniques in Lesotho and abroad.

(iv) External funding (on a five year basis) will be needed for the following elements of the program :

- investment in furniture and equipment
- training of personnel
- technical assistance from foreign experts
- the direct marketing in the RSA
- the image building activities in the NIC's, Europe and the U.S.
- the production of promotional materials
- the use of public relation experts

(v) The total current budget of IPC is estimated at M 635,000 per annum and the initial investment at M 177,000.

PERFORMANCE

(i) The IPC should have targets for employment created by its activities and for the number of quality new implemented projects. It is proposed that the targets for IPC's second year of operation will be 550 jobs created (6 projects) rising to 700 jobs (7 projects) in the third year, and 1000(10 projects) in the fifth year and on.

(ii) Its staff should have targets for:

- the number of investors assisted
- the number of presentations made
- the number of site visits to Lesotho
- the number of approved projects
- the number of jobs created

INTRODUCTION

The Government of Lesotho (GOL) through its Ministry of Trade and Industry has requested FIAS assistance in " developing an investment promotion strategy and an active investment promotion effort ". In response to this request, the present report focuses on each of the investment promotion elements, i.e. the promotional strategy, the institutional setup to carry out this strategy and the methods to be used to evaluate its effectiveness. A short review is made of past promotion efforts in Lesotho and its lessons, and an effort is made to evaluate the likely results of future efforts based on certain assumptions. One of these assumptions is that the changes in the investment policy environment suggested by the previous FIAS report "Diagnostic Report on Foreign Direct Investment" are in fact made by the GOL.

The report draws on numerous studies of Lesotho's industrial strategy and comparative advantage in manufacturing and agro-industry and work done by World Bank experts in the December 1989 Investment Promotion Project pre appraisal mission. It includes the analysis and conclusions made in the studies of " The Industrial Development in Lesotho " and " The Lesotho Past Experience in Investment Promotion " prepared by local consultants Messrs. F. Baffoe and R. Kirk of Coopers and Lybrand .

In the preparation of the report, we have drawn on FIAS knowledge of the investment strategies of foreign firms in various countries and industries and a global research exercise done on " Promotion as a Tool For Attracting Foreign Investment ". Last but not least, this report draws heavily on the personal experience in managing an investment promotion agency of Mr. Benvenisti, the former FIAS staff member who led this exercise.

Background

Lesotho is a land locked country geographically located within the Republic of South Africa (RSA). About 70% of the labor force of 750,000 is employed in the informal and agricultural sectors, most of them in the rural area. About 20% is migrant workers in the RSA (most of them employed in mining). The formal sector employs the remaining 10% of the labor force. The manufacturing sector employs about 9,500 workers. The employment in the formal sector is expected to grow in the next decade at a rate of 3.3% per annum (or 2,000 workers a year). The country offers limited opportunities in commercial agriculture due to difficult climatic conditions (the high risk of drought), a small arable land base (only 12% of the total land area of the country is cultivable) and the traditional land tenure system. The country has very limited natural resources except building materials. Therefore most of the future employment opportunities will have to be created in the manufacturing, construction and service sectors.

The four post-independence development plans of the GOL progressively established the industrial sector as the main engine of the country's growth and employment. Since 1977, this strategy expressed itself in a foreign investment policy that promotes new labor intensive export oriented enterprises. Most of the exceptional annual growth of 18 percent in manufacturing over the last 20 years was due to foreign investment in these sectors. In 1986, foreign and joint-venture firms accounted for more than 70 percent of the employment in the formal industrial sector, and probably more than 90 percent of manufacturing exports.

The emerging structural pattern of manufacturing and its underlying foreign investment drive in Lesotho was however recently being questioned in three areas :

First, it introduced a high degree of fragility into the industrial sector because the major part of the attracted foreign investment was based on temporary political and economic factors. Nearly all foreign investors came from the RSA (about 70%) and the NIC's, and there has been a high concentration of investment in the clothing and footwear sectors for export (more than 40% of the employment in 1986, and 80% of manufacturing exports in 1988). These investors are considered highly sensitive to changing political conditions like the sanctions against the RSA, and their concentration in these sectors is driven by trade agreements that may be proved temporary in the long run. As an indication of this concern it is mentioned that of the 100 firms that were granted Pioneer Industries status until the end of 1988, 40 had subsequently closed.

Second, the growth and size of the newly developed foreign dominated manufacturing sector has resulted in a great concern over the pace of development of the indigenous entrepreneurial class and the growth of the local small to medium size firms. The latter employ only 20% of the total work force in manufacturing and are growing at a much slower pace than the foreign owned firms.

Finally, there is a growing awareness in Lesotho of the need for industrial deepening by promoting backward and forward linkages to the existing foreign owned firms and to the Highland Water Project and the development of domestic resource based industries in the building materials and agro-based sectors.

Some of the concern over the fragility of the manufacturing sector structure can be attributed to the political situation in Lesotho, the investment incentive policy of the GOL and the investment promotion practices in the early 1980's. In the early to mid 1980's there was growing tension between the GOL and the RSA. The crisis ended with a coup in Lesotho in 1986. Most of the closures of foreign firms occurred in the years 1983-1986. Of the 16 firms approved by the LNDC Board which started operations over the period 1980-1990 13 closed in 1983-1986. The current tax holiday system can promote the departure of foreign firms once the tax holiday period ends. The clothing and footwear labor intensive operations can easily change location to a more favorable tax location. In addition, an evaluation of the previous investment promotion practices reveals that there was minimal pre screening of the promoted foreign firms. This practice ended up with the establishment of fragile operations (with no established financial and marketing track record) that collapsed after a short period of operation. Furthermore, the fragility of the sector has been over estimated through an assumption that most of its output is exported to the U.S. and European markets using existing trade agreements and by avoiding sanctions. In fact some 60% of manufacturing exports are destined to the RSA which means that foreign investors are using the Lesotho location to penetrate or increase their share in this big regional market for labor intensive products.

Investment Promotion

Active investment promotion is only one of several tools available to countries eager to increase their entrepreneurial pool and the level of investment activity. Promotion efforts usually start with attempts to create a favorable investment environment in which political and economic policies are conducive to investment. Most of these policies have equal effects on local and foreign investors and therefore are not unique to foreign investment promotion. However, to some of them, like the availability of foreign exchange or the employment of expatriates, foreign investors are more sensitive. Investment promotion **activities** consist of providing information and services to potential investors. With foreign investment other activities are added -- the creation of an image of the country as a place to invest, outreach to attract investors and efforts at home to identify and build-up local partners.

In recent years there has been growing interest in developing countries in foreign investment as a result of growing foreign debt, budgetary constraints and a desire to involve the private sector in the development process. To this end many developing countries have either recently started active investment promotion programs, or are moving to enhance the effectiveness of existing agencies. Competition among countries to attract foreign investment is growing at a time when the total flow to developing countries is declining. The competition is especially keen over export oriented foreign investment. Many countries design export promotion policies and introduce investment incentives specifically designed to attract investors seeking a low cost environment and a production site to avoid quota limitations placed on them in their home countries.

It is for this reason that many governments attempt to strengthen their investment promotion programs by evaluating its three basic components:

a) **strategy** -- what sectors, countries and investors to target; and what investment promotion techniques and approaches to use to attract them most cost effectively.

b) **structure** -- what type of organization would be most effective in the investment promotion function and how should it relate to other interested organizations.

c) **performance** -- how to motivate the investment promotion staff and measure their effectiveness.

The **sectoral component** of the investment promotion <u>**strategy**</u> should be derived from the industrial strategy of the country. Countries choose priority sectors for two reasons. First, to deploy limited staff (including policy makers) and other resources to promote new investments (both local and foreign) in a priority manner. Second, to develop a special sector policy in cases where there are discrepancies between attractive economic rates of return in projects (strong comparative advantage and low resource cost ratios) , and less attractive financial rates of return. Sectoral policy is then needed to define the level and nature of the support which might reasonably be made available to bridge the gap.

For investment promotion strategy the **priority** sectors identified by the government provide a starting point in determining the **targeted** sectors for FDI promotion. Sectoral priority lists should not be used automatically for targeting foreign investment as in some cases they include sectors that are reserved to domestic investors. They should not be seen as exclusive lists (positive lists) that will preclude investors from investing in financially sound projects in other sectors. Policy makers are not considered the best decision makers when it comes to picking the "winners" (the future successful projects).

Sectoral targeting and related FDI promotion is sometimes confused with project promotion. The difference between the two is the definition of what is being promoted. Project promotion is usually done by project sponsors (private investors or public financial institutions) that are trying to package together the various elements that go into a foreign investment. Investment promotion agencies around the world usually are not involved in this form of investment promotion because of the technical skills and specialization needed to successfully perform this function.

The choice of countries from which to promote investment (**country targeting**) is determined by: the level of foreign investment activity of the home country; the traditional or historical links with the host country; the trade partners of the host country; and the trade agreements the host country has that are of interest to certain groups of investors. The most active Foreign Direct Investment (FDI) countries in the world are : Japan, U.S., Germany, U.K. and France. In recent years the Newly Industrialized Countries in the Far East (NIC's) - Taiwan, South Korea, Hong Kong and Singapore - became active in FDI as a result of rising labor costs and balance of payments surpluses in their home countries and export quota limitations. In some areas or countries there are specific cases of other large sources of FDI as a result of historical factors or a dominant neighboring economy. Such is the case of the Dutch investment in Indonesia, the U.S. investment in Mexico and the large RSA investment in the SACU countries. Targeting home countries for investment promotion should also take into account the political interest these countries have in certain regions or continents and the pattern of investors' behavior. Thus U.S. investors are less interested in Africa for historical reasons and Japanese investors regard investment in Africa as too risky and prefer to invest in Far Eastern low labor cost countries. Another example is the interest of the Scandinavian countries and Germany in the Southern African countries for political reasons. An additional factor in country targeting is the kind and amount of support the host country can expect from the home country. Since image building and investor targeting are costly activities for a poor developing country, it needs the financial support of the home country governments for these activities.

The last element of investment promotion strategy is the choice of **investment promotion**

techniques to be used to generate FDI flows. The country can focus on creating awareness of its existence and its strength and improve its image within the investment community as a favorable investment location. Or, it can start direct "sales" efforts by targeting and approaching specific investors and convincing them to locate their future investment in the country. Or, it can provide incoming (and existing) investors with services that will facilitate the investment process. Investment promotion strategy always involves a mix of these activities. The problem facing the policy makers is what is the proper mix considering the available resources and what is the correct sequencing of their use. Experience in other countries shows that the provision of services is the most cost effective promotion activity. It involves mostly local costs and can generate immediate results from investors coming to the country without any promotion efforts. The next technique -- image building -- is extremely important for small countries that investors are not aware of and/or which are located in a conflict region. This activity however can require large amounts of money and it needs a long term commitment. It is in this area that a poor developing country needs most of the support it can get from home country governments and where technical assistance is needed. The proper sequencing of the use of the various techniques is determined by how ready the system is for the use of this technique. If for example the environment is not ready because of a defensive attitude towards foreign investors (stiff local ownership rules), there is no point in trying to build a positive FDI image. If on the other hand the country is active in image building and targeting investors in their home countries and has not developed the capacity to provide services to investors, these efforts will be defeated by the reality of frustrated investors trying to implement their projects.

The central issue that a government faces in **structuring** its investment promotion efforts seems to be the appropriate mix of private and public involvement in them. There are various reasons why the private sector has difficulties in establishing and funding such operations. First, investment promotion can not be a profit making activity. It needs long term efforts and the benefits arising from these efforts are also long term because of the lengthy investment decision and implementation period. Second, to provide effective investor services there is a need for close interaction with government institutions that provide permits and incentives. An organization that is considered part of the system will probably be more effective in obtaining these approvals. Third, investors do not feel comfortable revealing their project details to people with business interests because of fear of competition or disclosure. They sometime prefer to deal with government officials that are expected to be objective (or are monitored) and who are without business interests. On the other hand, the skills and level of expertise needed to perform the investment promotion function are usually found in the private sector. Promoters and good marketing people are scarce in developing countries and therefore are hard to keep on the pay scale of governments. It is therefore no wonder that some countries have undertaken the middle road and created a " quasi-governmental " organization. This involves a parastatal that has a board of directors that includes all the interested parties in the government and is usually dominated by representatives of the private sector. It is funded by the government but the salaries may be similar to those of a parastatal. The institution needs to be separated from government ministries and public financial institutions to create an image of an independent organization that is dedicated to the interests of investors.

Performance evaluation is of utmost importance to the efficient functioning of the investment promotion organization. However, it is considered the most difficult task to design and monitor. The biggest difficulty is in establishing goals for the organization. Some countries set the goal as the volume of FDI flows, others the total investment and/or exports generated or the jobs created. It is essential that the government will set realistic targets for the institution that will be part of its national plan. Additional targets need to be designed to motivate the promotion staff and monitor their performance. Separate performance evaluation techniques exist for the evaluation of image building efforts.

CHAPTER I

THE RATIONAL FOR INVESTMENT PROMOTION IN LESOTHO

The promotion programmes of governments are based on two suppositions: first that FDI can make an important contribution to economic development of the country; and second that adequate flows of such investments will not occur without assistance of governments because of market failure and the competitive market environment for FDI. Changes of existing promotion programmes can thus be justified if evidence can be provided that the change will result in increase in the benefits of the inflow of FDI and/or increase in its volume; and that the additional government assistance will address certain distortion, newly identified market failure or an increase in competition for FDI.

From the marketing aspect of promotion the effectiveness of the efforts can be enhanced by the manipulation of the basic three variables of the country overall promotion (marketing) program:

- The product, or in terms of countries, the intrinsic advantages and disadvantages of the investment site;

- the price, or in terms of countries, the cost to investors of locating within this investment site. For governments , this usually means tax incentives, grants, tariff protection,etc. and

- promotion, or activities that disseminate information about , or attempt to create an image of, in terms of countries, the investment site, and provide services for the prospective investors.

Thus governments can disseminate positive information on the country to balance some negative aspects in the environment, or it can provide better services to investors to overcome a slightly inferior incentive package.

Research has shown that promotion efforts has strong effect on export-oriented FDI. Interviewed investors mentioned investment promotion efforts as having significant influence on their investment decisions. These findings can be explained by market failure in information and the influence of non rational elements (like perceptions and biases) in the investment decision process. An analysis of FDI trends in developing countries revealed a statistically significant relationship between promotion and inflow of FDI. Promotion was the most significant variable explaining FDI trends. Another test for the effectiveness of promotion is to analyze the additional costs of the promotional effort and compare it to the additional benefits resulting from this efforts.

The short analysis of the Lesotho economy established the need for FDI and its contribution to growth and employment. The size of the country, its location within a much bigger and developed economy, its narrow resource base, its early stage of industrial development and its weak entrepreneurial class establish the need for labor-intensive export- oriented FDI.

In the case of Lesotho market failure in information can be assumed for certain investors (NIC's, Europe and the U.S.A) because of its size and location. Wrong perceptions can also justify promotion efforts. Since the country is situated in the middle of a politically unstable region it needs to isolate itself from the conflict to reduce the investors' perception of risk. This can be done by image building campaign and inducing investors to visit the country (site visits).

The competition of Lesotho for export oriented FDI should be analyses in two sets. Its competition within the BLS countries for export oriented FDI based on trade preference agreements with the major world markets, and its competition with the Homelands and the BLS over RSA investors and investment oriented towards the SACU market. The competition among the SACU countries is in the broader aspect of promotion -- the product, the price and promotion. Lesotho does not have an advantage in labor cost in the BLS (although it had one before the 1989 increase in minimum wages), and does not present a superior investment environment (attitude and incentives to FDI). Therefore, investment promotion should be part of its marketing package in its efforts to increase FDI from the NIC's, Europe and the U.S.A. In its competition over investors from the RSA the need for promotion is increased because of its competitive position vis-a-vis the Homelands. The different incentives package offered in these two locations, Lesotho trade preference agreements, its better quality of labor, its stable political environment and the issue of trade sanctions on exports from the Homelands to the major world markets, make a compelling argument for promotion by Lesotho. The need for promotion arises from the complex set of information that should be presented to the RSA investors to affect his investment decision. Market failure and biases are the rational for promotion. Small and medium size RSA firms can not be expected to be aware of the details of all the trade agreements Lesotho has and its investment environment.

The next step in the analysis is to evaluate the existing investment promotion efforts and ways to increase their benefits and effectiveness.
(see Annex I)

The weakness of the current promotion efforts performed by LNDC, on behalf of the country, are in three areas: corporate policy towards promotion; the organization of the promotion function; and the quality of the promotion efforts.

The order of priority in promotion is: first, to promote projects initiated by LNDC and investors who come to the country on their own initiative and request LNDC assistance; second, to give services to promotion efforts initiated by overseas institutions; and third, to initiate targeted promotion when the project pipeline is low compared to corporate planning needs. The weakness of this policy is its passive approach to investors who are interested in locating in Lesotho in sectors and projects that were not initiated by LNDC. In addition, the quality of services offered to investors depends on the involvement of LNDC in the projects. For obvious reasons, better services are offered to projects in which LNDC stands to benefit most. In general the policy is to subordinate the promotion efforts to LNDC needs and capacity to provide its own services.

The promotion function is provided by the same people that negotiate and appraise projects. Their approach to investors is not as providers of services but as negotiators that attempt to maximize their corporate or country benefits from the investment. This conflict of interest can harm the investment promotion effort and result in lost opportunities. In addition, the skills and training of the appraisers and promoters are different. The promoters need marketing skills and training in marketing techniques. The planning and execution of promotion efforts cannot be subordinated to the capacity of the people in the unit and the work load of project evaluation and negotiation.

The promotion techniques used can be upgraded significantly by applying additional measures like image building and by training and specializing in the investment generating and investor services functions.

An attempt was made to learn the lessons from previous active promotion efforts attempted in 1979 - 1982. It had a slow start-up due to recruitment problems. Half the period of four years was used to recruit and train the necessary staff. When the operation became functional it was partially effective because of poor investor's targeting. The promotion staff had no project appraisal training and therefore the pre-screening of firms prior to making presentations was very weak. It resulted in a low ratio of site visits and implemented projects. The effort was aborted too soon for effective measurement of results. Because of the long decision and implementation period for a foreign investment initiative, the two years operational period is too short to measure the effectiveness of the promotion efforts. Nevertheless, the effort still resulted in a stream of site visits mainly from the targeted RSA.

In addition to the institutional weaknesses of the current promotion efforts FIAS identified some structural problems in the manufacturing sector that can be altered by a change of the investment promotion strategy. The high concentration of investors in the clothing and footwear sectors can be changed by a targeted promotion effort in other labor intensive industries like toys, hand tools,etc. The closure rate experienced in 1985-1986 can be reduced by better targeting of investors through pre-screening of targeted firms and training of the promotion staff in project evaluation. The benefits from FDI can be increased by promoting backward and forward linkages to the existing foreign owned firms and to the Lesotho Highland Water project.

Another measurement of the effectiveness of the proposed promotion effort is to compare it to another promotion operation that is using the same techniques. The Costa Rica Promotion Agency called CINDE is a private sector controlled institution funded by the USAID. It has attracted 5000 jobs per year at an operational cost of about US dollar 440 per job. If the conservative assumption for the Lesotho IPC will be met the 3550 jobs attracted to Lesotho over the five year operation period will cost US dollars 290 per job.

An attempt was made to calculate the cost of promotion and compare it to the direct employment benefits of the investment. It is assumed that the economic benefits of the additional job created is the stream of income (discounted value over the life of the project) that will result from the difference between the price the firm pay for labor and the shadow price of labor in Lesotho. Due to the high unemployment (and underemployment) in Lesotho the shadow price of labor was assumed at 70 % of its market price. Labor rate is taken as the minimum wage -- M 190 per month, and the rate of exchange as M 2.50 per US dollar. The annual difference is US dollars 273. The benefits to the economy is clearly demonstrated when the accumulated benefits to the economy is greater than the cost in the second year of operation of the promotion function.

CHAPTER II

PROMOTION STRATEGY

SECTOR TARGETING

Lesotho Government Policy

The four post-independence development plans of the Government have progressively established the industrial sector as the main engine of the country's growth and employment generation. At various times, as for example in the fourth plan, the main routes to industrialization have been referred to and these provides a broad but still loose guide to the articulation of sectoral priorities. The broad industrialization goals have been:

- import rationalization / substitution
- encouraging the development of labor intensive and export - oriented industry
- increased utilization of local raw materials

From about 1977 onwards, these broad policy guidelines were interpreted by the LNDC, by then the major single agent of official policy, as a policy of emphasizing new labor intensive manufacturing products. This manifested itself in a listing of priority sectors for promotion which was published in 1979 and was as follows:

TABLE 1: **LNDC Priority List of Sectors in 1979**

- Agro-Industry - cereals, dairy, vegetable and meat processing
- Textile and clothing manufactures
- Footwear and leather goods
- Assembly and testing of electrical goods and components
- Building materials
- Mixing and packaging of chemicals

- Manufacture of small consumer goods such as toys.

This broad list was subsequently elaborated as a much larger list of detailed product items in 1980. However, when the promotion functions of the LNDC were transferred from the separate promotion unit to the project staff in 1983,a somewhat different priority list emerged in the form of the three operational sector groupings within LNDC which still function there today, namely:

- Food, Agro - industries, Health care, Plastics and Chemicals
- Textiles, Clothing, Wood and Furniture, Miscellaneous Consumer Goods
- Engineering, Electrical/Electronics and Building Materials

The balance between these three groups was somewhat altered by events shortly thereafter, in that the increasing concern in the RSA about sanctions in the mid-1980's, gave rise to a largely unpromoted burst of new investment which was disproportional in the second of the three categories listed above, and especially in Textiles and Clothing.

It is this "success" which has given rise relatively recently to a re-thinking of sectoral priorities both in the LNDC and in the Ministry of Trade and Industry. Both organizations have now articulated the idea that some of the labor - intensive, and especially the clothing sector activities are highly "footloose", generate limited domestic value - added, rely mainly on imported raw materials and have little potential for linkage to other sectors. This does not mean that the "cut, make and trim" textile operations have been ruled out as an element of industrial strategy but that a broad range of sectors, not all of them labor - intensive, are now being talked about for possible priority status. In particular, the Ministry of Trade and Industry is now giving increased emphasis to domestic resource - based industries many of which would be relatively capital intensive as well as technically quite complex. It can be seen from the priority list issued by the MTI that almost half of the items involve strong dependence on local agriculture or natural resources. The Agro-Industrial items are meat processing, milk products, high-value fruits and sugar processing. The Mineral Processing items are bricks, sandstone slabs and aggregates from basalt and dolorites. A further item to which LNDC has attached high priority is ceramic tiles based on Lesotho clays. Overall, LNDC now has 25 of the 42 projects in the pipeline in the two sectors of agro-industrial, and engineering and building materials including transport.

TABLE 2: **Ministry of Trade and Industry - Priority List**

- Ranching and meat processing
- Milk and milk products
- High value fruits and vegetables (strawberries, peaches, garlic)

- Sugar processing (sugar beets)
- Expansion of bricks production
- Sandstone slabs and blocks
- Aggregates from basalt and dolorites
- Cement plant based on imported clinker
- Maintenance and equipment leasing workshops
- Depot of automobile spare parts
- Regional drug and pharmaceutical industry
- Integrated textile industries
- Commercial airport
- Components for electronic industry
- Galvanized steel wire and light structural products

The Proposed Targeted Sectors

It is clear from this brief historical review that the recent past has seen a sharp shift in announced policy relative to the formerly strong emphasis on labor intensive industries. Some confusion has also been introduced in the sense that both the MTI priority list and the LNDC pipeline relate more to aspirations of a structural nature than to viable projects which can attract appropriate foreign partners and be implemented on an acceptable financial basis. Any new targeted investment promotion effort in Lesotho therefore faces the difficult dilemma of choice between labor - intensive projects which are demonstrably viable in the country, and the "more desirable" natural-resource based projects which are far more difficult, may need longer term subsidies, and have not established any real track record. This confusion needs to be resolved if the efforts of the proposed new Investment Promotion Center (IPC) are not to be excessively diffused. The next few paragraphs sketch the framework for how this might be done.

The starting point in determining future strategy should be to enumerate the major factors which presently underpin Lesotho's comparative advantage in those sectors which enjoy such an advantage. In our view these are:

(i) A plentiful supply of relatively cheap and good quality unskilled labor (a long term advantage).

(ii) Almost unqualified free - trade access to the two major African trading blocks, namely SACU and the PTA (a long term factor).

(iii) Duty-free access of most Lesotho products to the European Common Market in accordance with the terms of the Lome - convention, and preferential access of goods under the Generalized System of Preferences (GSP) into eighteen industrial countries (a long term factor).

(iv) The intersection of (ii) and (iii) which in an era of sanctions against the RSA gives Lesotho a unique opportunity to attract export-oriented investment from the RSA to serve both the RSA market and world and regional markets. In an era of textile quotas against successful NIC's such as Taiwan, Korea and Hong Kong, that same intersection makes Lesotho an unusually attractive location for certain investment from these countries (a short or medium term factor).

If these are indeed the main "selling points" which Lesotho has to offer, it would be wrong for a sectoral promotion strategy to ignore the fact. Even though item (iv) above could prove to be only short - lived, the other three sources of the comparative- advantage of export-oriented labor intensive industries will not be. Hence the first entry in the sectoral priority list of the new IPC ought to be a sub-set of such industries. A useful starting point for identifying these would be the LNDC priority list of 1980, refined by identifying those sub-sectoral items from the list in which some success in investment promotion has already been achieved. The revised list might then be as follows:

TABLE 3: **Priority list of labor intensive and export-oriented industries**

- Textile and clothing manufacture (including sportswear, shirts and pajamas, infant and children's clothing, and gloves)

- Leather and footwear (including handbags, belts and straps, travel goods)
- Electrical equipment and components assembly

- Other simple manufactures (such as farm and garden tools, toys, jewelry and cattery)

A second component of the sectoral priority list could be established through a careful scrutiny of agro-industrial projects where there is some a priori reason to expect that financially sound projects can be identified. A useful starting point here is the detailed work on Lesotho's comparative advantage in agriculture and agro-industry recently undertaken for the Government and the World

Bank. This has revealed several agro-industrial sectors where there is evidence of a favorable domestic resource cost and others where there is a possibility of this. The items which might therefore be added to the preliminary version of the sectoral priority list are as follows:

<u>TABLE 4: **Possible agricultural and agro-industrial priority list**</u> (preliminary list only)

- Wool and mohair (including local sewing)

- Beef ex feedlot (and possibly meat products)

- Milk

- Vegetable canning (based on results from asparagus)

- Peaches, tomatoes and green beans

- Oil- seed production (to support oil-seed processing)

In several of these cases, the justification for priority status is built on very favorable economic rates of return and is in spite of apparently poor financial performance (see World Bank reports on Lesotho). Thus production in these cases has to rely on concessional capital (mainly at the experimental stage) as well as direct Government support to bridge the gap between the financial and the economic rates of return (during the early years of the projects). It is because there is a reasonable expectation that such support will be forthcoming for well-conceived projects, that items such as those shown in Table 4, can be included in the sectoral priority list.

A third and final component of the sectoral priority list ought to be assigned to those project and sub-sectoral areas that could derive financial and economic viability from the substantial direct and indirect demand associated with the Lesotho Highlands Water Project (LHWP). Two main lists of possible investments have so far emerged in this connection. The first is one generated by project officers from LNDC and the second (substantially overlapping) is one shown in the Coopers and Lybrand Economic Impact Study. More work is needed to turn this lengthy list into a shorter list of high priority activities. However, preliminary indications are that the list would have the following main components:

<u>TABLE 5: **Priority projects linked to the LHWP**</u>
(preliminary list only)

- Construction Materials (and especially Bricks and Aggregates)

- Construction services

- Food items and catering
- Transport services and haulage contracting
- Tourism - related activities
- Specialized clothing projects (e.g. protective clothing)

It is stressed that not all of these items would necessarily need foreign investment partners. Some will be done on a relatively small scale using only Basotho resources. The refining of the list into a realistic set of target investments will be one of the functions of the new Business Advisory and Promotion service (BAPS) which is proposed by the World Bank Investment Promotion Project. It's work would be closely coordinated with that of IPC whenever there was a suggestion of the need for support of a foreign technical partner.

COUNTRY TARGETING

The decision to invest in a certain country is mainly affected by strategic considerations and the perceptions of risk and returns. The main strategic considerations include : access to markets and natural resources, and to a low cost production base for export. Access to markets refers to the domestic market, regional common markets, and markets with which the host country has preferential trade agreements. The perception of risks includes the political risk in the country of location and the risk in the destination market. The political risk can create push and pull effects which induce investors to move away from one country as a result of a clouded future, political unrest and economic sanctions, to countries from which the previous markets can easily be served.

The small domestic market of Lesotho offers limited opportunities to foreign investors. In the near future, most of the existing opportunities will be gradually exploited (probably by local investors with foreign technical partners or investors). Only minimal foreign investment promotion efforts will be required since projects will be small (due to the market size) and will produce simple products (due to the low income level). Some new opportunities will emerge in connection with the Highlands Water Project due to the demand for goods and services during the construction period. To materialize these opportunities some foreign investment promotion will be needed. However, most of this will be project oriented and will be done by the HWA, LNDC and (the proposed BAPS). Additional opportunities will be created by identifying possible forward and backward linkages to existing and future manufacturing and agro-industry projects.

The area for major foreign investment promotion effort is export oriented FDI. To evaluate the group of investors that are the potential market for investment promotion efforts one has to identify the potential export markets and the origin of the investors that would likely be attracted to Lesotho to serve these markets. The major potential markets for Lesotho's export promotion efforts were identified in the following order : The Republic of South Africa (and/or the SACU area), Europe (under Lome convention) and the U.S (under the GSP agreement).

The major sources of investors are the RSA, the NIC's, Europe and the U.S.

A key conclusion emerging from an analysis of the past experience of Lesotho and other SACU countries' is the importance of the political risk factor in determining the flow of FDI. The interest of foreign investors in Lesotho is affected by the political situation in RSA and the relationships between the two countries. In periods of instability in the RSA there is growing interest in Lesotho by RSA investors (which overrides the more generous incentives given in the Homelands), and less interest by other investors (except NIC investors who seem less affected by the political situation). In the mid 1980's, the Lesotho government increased the risk to investors by being more involved in the RSA conflict and the FDI flows were sharply reduced. During the same period investment promotion efforts were reduced and stronger demands were voiced to increase employment of indigenous people and local ownership in resource based projects. All of this increased the perception of risk by investors and they responded accordingly.

Table.... **Inflows of FDI to Africa and Selected Southeren African Countries**
(million US Dollars)

Region/Country	1980	1981	1982	1983	1984	1985	1986	1987	1988
Africa	312	1550	1411	1207	1379	2571	1751	2227	2853
Oil Exporters	459	1133	1012	1186	1144	2237	1571	1759	2370
Other	771	417	399	21	235	333	180	468	483
Botswana	112	88	21	24	62	54	70	114	40
Swaziland	26	39	-9	1	4	11	20	51	43
Lesotho	N.A.	N.A.	N.A.	N.A.	3	5	8	10	12
Zimbabwe	2	4	-1	-2	-3	3	8	-31	4
Zambia	61	-39	39	26	17	52	32	32	32
Mauritius	1	1	2	2	5	8	7	17	24
Seychelles	10	10	10	9	10	12	14	19	21

Source:IMF

Another example of the effect of this political instability and the perception of risk is provided by the Swasi experience with FDI. In spite of a pragmatic foreign policy and a generous incentives package, the country experienced in the mid 1980's the exit of investors to the Homelands as a result of a period of stability in RSA. It seems that he " foot-loose " investors in the region are influenced by the strong perception of instability and risk resulting from the RSA conflict as well as by the benefits and incentives offered by the SACU countries.

The RSA is the dominant market in the region. With a high GDP and a large protected industrial sector it creates vast opportunities as a source of investors and a target for FDI. However, this market suffers severe economic problems due to unstable internal and external political conditions. This has resulted in a trend of increasing pressures of sanctions and divestment. European and American investors are pulling out from this market and Japanese investors avoid entering it. There is evidence from recent FDI experience in the Lesotho, Swaziland, and Botswana's that this market is still of interest to investors and can attract FDI to SACU member countries. The influx of investors from the Far East NIC's since the early 1980's seems to be the result of less concern with the political situation in the region and their readiness to move in when the traditional FDI countries are pulling out.

The first group of investors are the **RSA** investors. For them Lesotho is just another location in SACU. Their alternatives for production to serve the SACU market are the Homelands and the BLS countries (Botswana, Lesotho and Swaziland).

At the end of the 1970's, the push effect of the political instability in the RSA and the pull effect of incentives and much lower labor rates were jointly affecting the flow of FDI to the other SACU countries. In the early to the mid 1980's the political situation in RSA stabilized and incentives in the Homelands increased with the resulting withdrawal of investors from the other SACU countries. Since 1984 RSA entered a period of instability and increased pressure of economic sanctions. There were no basic changes in the incentives offered in the Homelands and labor rates in the Homelands increased more than in the other SACU countries. The result was a new wave of RSA FDI to the latter countries.

The above analysis indicates that the economic sanctions offer only a partial explanation of the wave of RSA FDI to Lesotho and other SACU countries. Future potential for FDI should be evaluated against the political stability in RSA, the level of incentives offered in the Homelands and the comparative labor rates.

The political scenarios for RSA includes the possibility of continued periods of political instability with short periods of stability resulting from pragmatic moves by the Government. During the instability periods Lesotho can expect waves of RSA investors seeking a reduced risk environment and an opportunity to move capital out of their home country. Targeting the inefficient highly protected labor intensive industries in RSA can result in a handsome reward for promotion efforts in RSA. Furthermore, a recent evaluation of the Homelands incentive system in RSA predicted that it is highly unlikely that the existing system will be expanded because of its high budgetary cost and doubts about its effectiveness. There was even some speculation that the system will be rationalized and trimmed.

Based on this analysis it can be predicted that Lesotho's competitive situation vis a vis the Homelands will not be worse than the situation in the 1980's when it successfully attracted RSA investors. The economic sanctions factor will probably play either a direct or indirect roll in RSA investors' decisions in the 1990's. Even if sanctions are eased, RSA investors will find it easier to export from Lesotho to markets where Lesotho enjoys trade preference and customers are sensitive to the unstable situation in RSA.

Investors Choices Between SACU Locations

All SACU locations are near the major production and consumption areas in the RSA and are well connected with proper infrastructure. Obviously there are small differences in distance and quality of infrastructure but they do not seem large enough to tip the balance in favor of one location or the other. The major point in favor of the BLS is the possibility of using them as an entrance to the European and the U.S. markets using their trade preference agreements (and by avoiding sanctions). If the situation changes in RSA and the sanctions will be lifted the BLS will still enjoy the trade preference edge over the Homelands. If a settlement will be reached in RSA and the new regime will negotiate trade agreements with the developed countries the BLS will lose their advantage. However , this last possibility seems remote given the stage of negotiations in the RSA and the need to negotiate trade agreements with the EEC and the U.S. from a starting position of income per capita of U.S.$ 1800 (although with a huge income disparity).

The next major consideration is labor costs. The **BLS** has an advantage over the Homelands in both the price and quality of their labor. The strengthening of the power of labor unions in the Homelands with rising negotiated minimum wages has moved the official labor costs (this is not to say that un official rates can not be lower) above the rates in the BLS.

Minimum Wages in SACU
(per month)

Lesotho	M 189
Swaziland	M 192-200
Botswana	M 198

RSA	
Kwa Zulu	M 196
Qwa Qwa	M 280
Ciskei	M 264

Source: Coopers & Lybrand

The most important difference between the BLS and the Homelands is in the incentive packages and the corporate income tax systems. The regular corporate tax rates vary from zero in Ciskei to 50% in the RSA. In addition Botswana has a capital gains tax of 40%. The tax incentive packages also vary considerably from 6 years (average) in Lesotho to none in the Homelands. In addition there is a large array of other tax incentives and subsidies that makes an accurate comparison (even for a sophisticated investor) very difficult. The following tables try to bring together the most important of these tax regime and incentives elements.

Corporate Withholding Tax on:

	Dividends Tax	Interest	Tax to Non Residents
Lesotho (Proposed) (15%)	37.5%	15%	10%
Botswana	40%	15%	15%
Swaziland	37.5%	15%	10%
Zimbabwe	50%	20%	n.a
Mauritius	15%	n.a.	n.a.
South Africa	50%	15%	nil
Home Lands			
Bophuthatswana	40%	15%	10%
Ciskei	nil	15%	10%

Transkei	35%	15%	10%

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n.a.-- Not Available

Source: Coopers & Lybrand Ass.

Corporate Tax Incentives

Lesotho --For Pioneer Industries - Tax Holiday 5-10 years.(most frequent 6 years). Various tax allowances.

Botswana -- For approved enterprises- effective corporate tax rates:

year	1	2	3	4	5
rate	nil	nil	10%	20%	30%

In remote areas a 10 year tax holiday period is granted.

Swaziland -- For approved enterprises-- Tax Holiday 5 years. Applied to net profits minus total wage bill for local workers, and not exceeding 150% of the initial investment.

Other Incentives

Botswana -- Cash grant of M 1000 per worker not exceeding 40% of the investment in fixed assets (in the easily accessible areas, rising to 65% in rural areas). The cash grant is given instead of the reduced effective tax rate.

Homelands-- A tax free Employment Incentive for seven years as a percentage of salary and wage bill (80%-95%) subject to a maximum amount per worker R/month (R 25-R 130).Due to rising labor costs in the Homelands the effective subsidy has been reduced in recent years.

In addition to the above incentives each country offers a wide array of other incentives : subsidized loans, training grants, additional income tax allowances, reduced rental rates of industrial buildings, transport rebates etc.. A full comparison of the incentives granted goes beyond the scope of this analysis. However, judging from the major incentives granted it is possible to predict that the various packages end up with the same (except, may be, for the top Homelands package) effect on the "bottom line" of projects located in comparable locations. Thus the RSA investor ends up with the option of receiving higher incentives in the Homelands or locating in a more stable environment with access to the major export markets and employing a more adaptable and trainable labor force. Among the BLS countries the differences are less important and therefore investment promotion activities can make the difference in the investment location decision.

The typical considerations of the **NIC's** investors should be evaluated in a different context. As production costs within Hong Kong, Taiwan and South Korea rise, their manufacturing communities are aggressively seeking out lower-cost production sites and countries with trade preference agreements with their main world markets (the U.S. and Europe).

This need of NIC producers to maintain their competitiveness is the major driving force in their appearance as investors in the Homelands and the BLS countries. Their production strategies center around the sewn products industries (clothing and footwear). In these products there are two distinct groups, the high-and low-end markets. The high-end products demand fine quality and quick turn-around and the share of labor costs in the product value is low. Thus, the European and U.S. producers maintain domestic production for these products. However, for the lower-end products the U.S. and European producers or marketers (under general label or private label) will continue to establish direct sourcing arrangements in lower-cost areas throughout the world. The NIC producers, who have long established relations with them, will continue to search for lower-cost production sites to serve them. This trend does not necessarily cover only the sewn products group but also other labor intensive products like: toys, giftware, lower-end hand tools, lower-end electronic products etc..

The SACU countries have an additional appeal to these investors -- the lucrative RSA market. The RSA market of 38 million population (which is expected to rise to 50 million in the year 2000) with income per capita of U.S. dollar 1800 offers the NIC investors a strong motivation. The textile market alone is estimated at more than U.S. $ 2.5 billion. This market is expected to grow, especially in the lower-end products, with the expected change in income distribution in the RSA. Exploitation of the situation of many inefficient labor intensive industries that developed in RSA behind high protection barriers and the comparative advantage of Lesotho in labor intensive industries can generate many opportunities for these investors.

In addition to economic reasons the Hong Kong investors are also motivated by political considerations. With the expected change in the political status in 1997 Hong Kong residents are looking for a safe haven in other countries. Some of them may consider the RSA and BLS countries as their place of residence and/or business. In locating in one or the other locations in the SACU region the NIC investors behave like the RSA investors who will probably prefer political stability and a better quality lower cost labor force to a marginally better incentive package. As stated above for the RSA investors, with proper promotion efforts this group can be persuaded to locate in Lesotho.

The last group of investors are the **European and U.S.** Their prime motivation for locating in the SACU market will be the RSA market. Some are still operating in the RSA despite the sanctions and may consider moving to the BLS countries to reduce the risk of the expected difficult political transition period. For the others the prospects of change and lift of sanction may prompt a renewed interest in locating in the SACU countries. However, this group will be hard to approach since they may adopt a policy of wait and see until the situation will clear in the RSA.

Lesotho can expect to attract more investors from NIC's in periods of internal RSA instability since these investors seem to follow the behavior of the RSA investors. It is more difficult to evaluate the potential of U.S., European and Japanese investors. The RSA market is probably of interest to them but they are strongly affected by the political situation. However, if Lesotho (with possibly other SACU countries) can isolate itself from being active in the RSA conflict through public relations campaigns and supported by the U.S. and European Governments, it is possible that investors from these countries would consider penetrating the SACU market through Lesotho (or other SACU countries). The alternative can be investors missions and seminars (in Lesotho and abroad) organized by the home countries' governments that will show support for the political situation of Lesotho. In any case, the investment promotion task is politically complex and will need a sustained and long term effort. It is therefore not assumed that these countries will yield many FDI projects. It is recommended that they be the target for separate promotion of technology transfer, access to markets, capital and management expertise.

INVESTORS TARGETING

After selection of sectors and countries for targeted promotion, promoters have to select the type of investors that are most likely to be affected by their promotion efforts. The decision who will be the target investors is not only important for direct " sales " efforts but also for image building. Different groups of investors have different needs for their decision making process. Thus, small investors are more concerned with infrastructure because they do not have their own logistics capabilities like the big multinationals. Also when success stories are published care should be taken that the selection of companies reflects the types of investors that are targeted. Investor targeting is an essential element in direct marketing. This investment promotion technique involves tailored presentations to identified clients, reference selling and typical cost profiles which are relevant to the target investor.

The general audience of the promoters can be basically divided into two groups -- the decision makers and those that can have an input in the process. The typical decision maker is a corporate executive. In the other group there are all those that provide services to the decision maker like legal, accounting, financial, marketing, technical, public relations and other services. **A good investment promotion operation always keeps the decision makers at the center of their attention**. The other group is important in the process of identifying the decision makers and in image building campaigns.

Other criteria for selection of investors are: the **company size** and its **experience in international trade**. The size is a factor in determining management capability in handling a foreign operation. A small company cannot be expected to manage effectively a foreign subsidiary. The size can vary with distance. It is easier to control an across-the-border operation than an overseas one. For the **RSA** market the size can be **50** employees, and for a **U.S** company it can be **250** employees. The international trade and investment experience of the firm is useful in identifying export oriented foreign investment potential. Another important factor in investor targeting is the **quality of the investor**. It is extremely important to avoid investors that have troubled operations elsewhere. With proper use of company information sources that specialize in up to date financial and other information this trap can be avoided.

PROMOTION TECHNIQUES

An important component of promotion strategy is the choice of techniques to be used to attract investors. There are three broad categories of promotion techniques that are defined by the objectives they are designed to achieve:

- improve a county's image within the investment community as a favorable location for investment **(image - building activities**)

- directly generate investment (**investment - generating activities**); and

- provide services to prospective and current investors (**investor services**)

There are many detailed promotional techniques that are used to achieve these three broad objectives:

Image Building :

- Public relations campaigns including solicited stories in the media; the use of heads of states and top political figures to deliver the investment message to potential investors, etc.

- Advertising in the general financial media.

- Preparation of promotional informational material like: brochures, audio - visual presentations, etc.

- Conducting general investment missions from home country to host country or from host country to home country.

- Conducting general information seminars on investment in home and host countries.

Investment Generating :

- Advertising in sector specific publications.

- Preparation of sector specific publications, typical investment and operating cost profiles, etc..

- Conducting sector specific seminars and missions.

- Engaging in sector specific direct mailing and / or telemarketing.

- Engaging in firm - specific research followed by "sales" presentations.

- Initiating firm (and executive) specific site missions to the host country.

Investor Services :

- Providing investment counselling services.

- Expediting the processing of applications and permits.

- Providing post investment services.

The mix of the investment promotion techniques used by the promotion unit is determined by: the government's foreign investment policy cycle; its readiness to invest in promotion activities; and how ready the unit is to use the specific technique. When there is a change in policy towards encouraging foreign investment an image building campaign is needed. If there is no functioning investor services unit, resources invested in image building will be wasted. If offices abroad are not in the right places and staffed with trained people, investment generating techniques will be wasted.

In the case of Lesotho it is recommended to start the first year with investor services and preparation of new promotional materials that will include the new promotion policy. During the first year preparation should be made for an image building campaign in the RSA. In preparing the campaign it is recommended to hire a public relations company from RSA. During the first year promotion officers for RSA should be recruited. Direct promotional efforts in RSA should start in the second year and increase later on.

CHAPTER III

THE INVESTMENT PROMOTION CENTER (IPC)

Investment promotion has certain characteristics of tasks typically carried out by the government, but other characteristics that are normally associated with tasks usually located in the private sector. Activities of this type are often financed by a government because they generate social profits that are greater than the private profits they could provide. Where this condition exists, a government must either finance the activity or risk that it will be unprovided.

Governments can adopt two polar positions in their attempts to carry out non-traditional government activity of investment promotion. A government could carry out investment promotion itself, but this approach has the disadvantage that the government organization may be unable to acquire skills required to manage the activity properly. The required skills may reside in the private sector and be difficult to attract to the public sector, especially with the salary constrains typical of civil services. Accordingly, if the government decides to manage the activity it may also, through various methods, have to take steps to obtain the appropriate skills from the private sector.

An alternative approach is for the government to delegate the management of investment promotion activities to the private sector. This approach often has the disadvantage that the private sector will not handle well the attributes of the task that are more like traditional government tasks, such as servicing investors by acquiring permits and approvals from the other government departments. Indeed, neither the wholly public or wholly private approach to the management of investment promotion is ideal. Regardless of the approach that is chosen there will be management issues with respect to how the inherent disadvantages of either approach are to be overcome. In an attempt to overcome these disadvantages governments may search for organizational approaches that combine, most effectively, the skills and resources of both the public and the private sectors.

The FIAS study on investment promotion referred to earlier observes that many governments avoid these two extreme approaches and, instead, choose an intermediate approach. They conduct investment promotion through a quasi-governmental organization. These organizations, while reporting to the government, are not enmeshed within the conventional government and civil-service structure. This separation from the conventional apparatus of government gives these organizations certain inherent advantages vis-a-vis government in carrying out the investment promotion function. At the same time these quasi-government organizations have an advantage over private organizations in conducting the tasks of investment promotion that require close contact with the government since they are, in fact, a part of the government.

In contrast to government organizations, quasi-government organizations tend to be created for the purpose of marketing a country as an investment site and not with the primary objectives of screening investment or negotiating with investors. These agencies have the flexibility to attract personnel with the marketing expertise that successful investment promotion requires. In addition, they are able to obtain sufficient autonomy to design and implement promotion strategies, and to develop an integrated management control system that ties the activities of marketers to particular investments. These management control system provide sufficient and timely information so that agencies can simultaneously control, evaluate, and motivate marketing representatives. The quasi-government agencies also tend to have their overseas offices staffed by full-time promoters who are directly controlled by, and accountable to them. These advantages are particularly important when the agency is involved heavily in investment-generating activities.

On the other hand, in contrast to private organizations, the quasi-governmental agencies do not face the problems a private agency is likely to face in conducting the investment promotion tasks that are more like typical government tasks, such as servicing investors, and cooperating with the government. The research findings, therefore, build a strong case for the location of a government's promotion program in an independent quasi-governmental organization(or within a quasi-governmental organization).

ORGANIZATION AND MANAGEMENT

Lesotho was actively engaged in foreign investment promotion from 1979 to 1983 through the Investment Promotion Unit of LNDC. Though constrained by staffing problems, this Unit actively promoted labor intensive foreign investment using image building, investment generating and investor services techniques. At the outset the Unit benefited from technical assistance from the experienced Industrial Development Authority of Ireland. The effort raised awarness of Lesotho as a potential investment site and resulted in a flow of site visits and FDI mainly from the RSA and NIC investors. It was aborted by a change in investment policy in 1983 that followed a foreign policy change of active involvement in the RSA conflict. The change in promotion policy at that time was rational because the foreign policy stand increased the risk of instability to investors and engagement in any massive promotion activity did not make sense.

The investment promotion function is still being performed by LNDC. It is considered to be an integral part of the corporation's marketing efforts but since 1983 has been carried on more as a project promotion activity for the institution than as a promotion activity for the country. Under LNDC's existing organizational structure the unit responsible for promotion is the Planing and Promotion Sub-Division under the Director Planing, Programming,and Operation Division. In practice the promotion function is performed by the Appraisal Subdivision which is responsible for preparing projects for the Investment Committee decision. The decision to establish the Promotion Section was made in 1988 but the unit was not staffed until the time of the mission visit. The Planning and Promotion Subdivision is currently involved in: corporate planning; donors relations including management of the use of funds allocated to LNDC by bilateral and multilateral organizations; market information for project preparation; the supply of data on the Project Pipeline for the corporate Management Information System; and the representation of LNDC (and its investors) in the Pioneer Industries Board.

Investment promotion by the Appraisal Subdivision is done on an ad hoc basis. Whenever a certain sector Section head is confronted by a small pipeline of projects he submits a promotion campaign plan in relation to the RSA. When approved, the campaign typically takes 5 days and is based on targeting firms from the RSA Yellow Pages (usually of Johannesburg) and company data from an RSA database. The campaign is followed by attempts to initiate a site visit in Lesotho. There are no periodic reports on these promotion efforts and their results. In 1989 there were two or three campaigns of that sort. In addition, the unit is promoting project profiles prepared by LNDC. The Planning and Promotion Subdivision is contacting organizations in Europe and the U.S.(like: OPIC,and CDI) in an effort to recruit a technical partner for the project. After initial contact is made the Appraisal Subdivision is doing the follow-up. In addition The Planning and Promotion Unit is hosting missions initiated by home government organizations like OPIC, DEG etc. The Planning and Promotion Subdivision employs 6 professionals (including the Director) and the Appraisal Subdivision 11 professionals.

The weakness of the current promotion efforts are in three areas: corporate policy towards promotion; the organization of the promotion function; and the quality of the promotion efforts.

The order of priority in promotion is: first, to promote projects initiated by LNDC and investors who come to the country on their own initiative and request LNDC assistance; second, to give services to promotion efforts initiated by overseas institutions; and third, to initiate targeted promotion when the project pipeline is low compared to corporate planning needs. The weakness of this policy is its passive approach to investors who are interested in locating in Lesotho in sectors and projects that were not initiated by LNDC. In addition, the quality of services offered to investors depends on the involvement of LNDC in the projects. For obvious reasons, better services are offered to projects in which LNDC stands to benefit most. In general the policy is to subordinate the promotion efforts to LNDC needs and capacity to provide its own services.

The promotion function is provided by the same people that negotiate and appraise projects. Their approach to investors is not as providers of services but as negotiators that attempt to maximize their corporate or country benefits from the investment. This conflict of interest can harm the investment promotion effort and result in lost opportunities. In addition, the skills and training of the appraisers and promoters are different. The promoters need marketing skills and training in marketing techniques. The planning and execution of promotion efforts cannot be subordinated to the capacity of the people in the unit and the work load of project evaluation and negotiation.

The promotion techniques used can be upgraded significantly by applying additional measures like image building and by training and specializing in the investment generating and investor services functions.

For the above reasons it is proposed that an independent promotion unit be established in LNDC, and called the Investment Promotion Center (IPC). The unit will be directly under the Managing Director of LNDC. A special sub committee of the Board of directors will be responsible for its work program, will approve its budget and will receive periodic reports on its performance. The committee will be chaired by the P.S. Trade and Industry and its members will be: the Honorary President of the LCCI, P.S. Finance, P.S. Planning, and the Director of the IPC.

The broad responsibilities of the IPC will be:

To achieve specific targets in respect of investment commitments by promoters.

The achievement of these targets involves many specific tasks that broadly are divided into three components: investor services, and investment-generating and image-building activities. Since investor out-reach is not recomended initially beyond the RSA, the first two components can be merged into one unit.

The IPC will have four sections:

- Promotion and Services
- Public Relations
- Research
- Corporate Planning and Donor Relations

The **Promotion and Services Section** will be responsible for investment generating activities and investor services. The specific tasks of this unit will be:

- Identification of potential investors by means of local advertising, public relations and market research;
- Direct contact with key decision makers in target companies and with their close advisors to persuade them to commit investment in Lesotho;
- Direct mail, missions, seminars , receptions and visits by Ministers or Chief Executives to targeted companies;
- Managing site visits (in Lesotho);
- Information guidance on location choice and introduction to national regulations, customs

and business practices, industrial services and utilities;

- Expediting the processing of applications and permits;

- Representing foreign investors within the public and private service and providing key introductions; and

- Identifying and working to eliminate specific problems encountered by industrialists in the wider environment (e.g. the lack of infrastructure)

To effectively perform these duties the unit should adopt a "project office" approach. This involves assigning to an individual staff member (" **project officer** ") the responsibility to provide a defined range of assistance to a portfolio of investors from specific locations on a continuing basis. The advantage of this system is that the efforts of the individual project officers and their manager can be monitored by reference to their output.

The staff of this section will be assigned territorial responsibilities on regions in the RSA, Europe, The Newly Industrialized Countries (NIC's) and the U.S.. The section will: be engaged in firm specific research followed by "sales" presentations in the RSA; initiate firm specific site visits; help the Appraisal Subdivision to identify technical partners for its projects; provide investment counseling services;expedite the processing of applications and permits; provide post investment services; work on the initiation of linkages between the promoted foreign firms and local suppliers; and participation in the small scale industries "patron" program . The Section will have 4 professionals.

The **Public Relations Section** will be responsible for image building activities. The image building task is an activity that needs a substantial input from support staff and outside specialists. It involves writing, editing, and managing the production of brochures, briefing materials, speeches, press releases, and other communications. In addition this unit will handle all the general promotion missions and seminars in Lesotho and abroad. It is recommended that this unit will develop good press relations with local as well with foreign journalists and employ local PR specialists in the RSA. The unit will have two professionals.

The **Research Section** will help the Promotion unit with firm search and research; will maintain a data base on the Lesotho market and economy; and prepare policy papers on effects of policy changes on the investment environment. The unit will have one professional.

The **Corporate Planning and Donor Relations Section** will continue its function as corporate planner and coordinator of the available resources from bilateral and multilateral aid organizations. It will have two professional.

With the establishment of the IPC the Planning and Promotion Subdivision of LNDC will be dissolved. The Marketing Research, Public Relations and Donors Relations Sections will move to the Center.

STAFFING, STAFF TRAINING AND TECHNICAL ASSISTANCE

The staffing of the new unit will be from the existing Planning and Promotion Subdivision of LNDC and form new recruitment. The unit will be managed by the current Director of the Subdivision. His knowledge of the Lesotho economy and Government, experience in investment promotion and previous training by the Irish IDA makes him a natural candidate for this position. The Section Heads of: Research, Public Relations and Corporate planning and Donor Relations will be existing staff.

The new recruitment will be three professionals for the Promotion and Services Section (including one senior person as Head of the Section),and one junior staff member for the Public Relations Section. The skills required of a " project officer " may include the ability to speak effectively in public, to write persuasively, to carry out market research, to organize functions efficiently and economically yet to high standards, and to negotiate effectively with clients and providers of services and permits. Some of these skills can be acquired but some are personality traits like being a good communicator, readiness to perform service functions and ability to generate trust. <u>The investment promotion function is " a people business ". The assets the organization deploys are people and their skills and commitment are the keys to its success</u>. One of the reasons for the slow start of the LNDC Investment Promotion Unit in 1980 was its recruitment problems. The recruitment of officers to IPC will probably encounter the same problems as in 1980. LNDC should make an effort to recruit the new staff from Basotho experienced in international trade (either from within the government or from the private sector). The skills of the public relations staff (image-building people) are similar to those required in the PR industry and Journalism. It is therefore recommended to recruit persons with experience in these professions.

All the staff of the Center will be trained by the Irish IDA in Ireland and Lesotho. The new recruitment will attend the course in Investment Promotion in Ireland. The Director and Section Heads will go for one month of special training in their respective fields in Ireland. The Director will spend two weeks in Mauritius to study the experience of MEDIA. The rest of the staff will be trained by the Technical Adviser assigned to Lesotho by the IDA.

Technical assistance to the Center will be provided in the following manner:

(i) The Irish IDA will assign a staff member to be appointed as Deputy Director of the Center for a period of one year. He will be responsible for assisting in the setting up of the Center; the designing of its strategies; building up its working procedures; and training of its staff.

(ii) In the second year of operation the IDA will assign a staff member that will be involved in consulting and monitoring of the progress of the Center on a quarterly basis. From the third year onwards this assistance will be given on a twice a year basis.

BUDGET AND FINANCING

The proposed budget was built on the basic assumption that LNDC will continue to finance the current staff salaries and part of the public relations expenditure. The project will cover the additional staff costs, the operating costs of the promotion function, part of the costs of public relations, the costs of the changes of the premises of the Center and additional equipment and furniture needed for the smooth operation of the unit.

Salaries

Position	Salary
Director	M 35,000--
Secretary	M 13,000--
Typist	M 7,000--
Promotion 3 positions	M 65,000
Research 1 position	M 20,000--
Donor Relations 2 positions	M 40,000--
Public Relations 2 positions	M 20,000
Total	M 135,000

Other Operating Costs

Communications	M 150,000
Travel	M 120,000
Public Relations	M 105,000
Office Supplies	M 20,000
Total	M 395,000

Initial Investment Budget

3 cars	M 105,000
PBX	M 8,000
Small Copy Machine	M 13,000
Fax	M 3,000
Lap Top Computer	M 13,000
Furniture	M 10,000
Redesign of premises	M 25,000
Total	M 177,000

Total Operating Costs

Budget Item	LNDC	The Project

Salaries	M 135,000	M 80,000
Other	M 25,000	M 395,000
Total	M 160,000	M 475,000

Total Project Costs

	LNDC	The Project
operating costs 5 years	M 800,000	M 2,375,000
Initial Investment		M 177,000
Total (U.S. $)	M 800,000 ($ 320,000)	M 2,552,000 ($1,021,000)

The proposed budget was built on the assumption that the unit will operate for five years with LNDC and the World Bank contributing their share of respective financing. To sustain the operation beyond the five year period it is important to introduce an automatic source of income to fund the operation.

PERFORMANCE TARGETS AND CONDITIONS FOR SUCCESS

Based on the past experience of LNDC's Investment Promotion Department, the RSA market can yield one site visit to Lesotho for each five presentations in RSA. For each 15 site visits there was one implemented project. Assuming a better investment climate, promotion strategy and infrastructure situation the ratio can be scaled down to 10 visits to a project. The ratio of presentation to an implemented project will then be 50 to one. Assuming 20 presentations a week it will take 12.5 man weeks to generate 5 new RSA projects with 500 employees per year in Lesotho. If the new Investment Promotion Authority will have three executives that divide the major metropolitan area in RSA (Pretoria-Witwatersrand-Vereening[PWV], Durban, Cape Town, and Port Elizabeth-Uitenhage) among themselves it is feasible to meet this target.

It is estimated that the NIC's, Europe and the U.S. will generate about 100 site visits a year and generate about 3 projects with 150 employees per year. These markets will not need targeted promotion efforts by the IPC but will need a major input in the form of provision of information and services to investors. There will be a need to assist the home countries in the image building and missions effort.

The IPC will have the following employment generating targets:

Year	Employment	Projects
1	400	5
2	550	6
3	700	7
4	900	9
5	1000	10

The Promotion Section staff should have targets for:

-- the number of assisted investors

-- the number of presentations made

-- the number of site visits to Lesotho

-- the number of implemented projects

- the number of jobs created

The proposed investment promotion strategy is based on our perception of: a pragmatic foreign policy that is similar to the policies adopted by Swaziland and Botswana; a foreign investment policy that is based more on economic criteria than on political and social needs; a return to the more traditional approach to the promotion of labor intensive industries (with all their weaknesses of lack of linkages and the risk of them being " foot loose "); readiness to accept the dominant position of the RSA economy and its implications for the source and orientation of FDI; and the need to have a balanced approach in the promotion of local and foreign investment and of the separate componeants of foreign involvement in projects (capital technology, knowhow and marketing) at the same time.

Essential conditions for success of the IPC includes:

-- adoption of the investment promotion policy conditions of the World Bank's " Industrial and Agro-industries Development " Project; and - adoption of the recommended strategy, structure , and operating procedures for the IPC by LNDC.

ANNEX I

PAST EXPERIENCE WITH INVESTMENT PROMOTION IN LESOTHO (1977-1989)

The First Period (1977-1983)

In 1977, the LNDC began to reemphasize the importance of promoting new labor intensive manufacturing projects. The loss making subsidiaries and associated companies were to be restructured and where necessary sold. The stress on promoting foreign investment resulted in an appraisal of the existing strategy of investment promotion. The review was carried out by the Managing Director, who observed that to date the LNDC had been operating without a coordinated investment programme. Prior to 1977 Investment Promotion consisted of:

- Distribution of brochures by LNDC

- Conferences organized largely at the Government level.

- Irregular advertisements in papers and magazines.

- Preparation of Project Profiles.

All of these activities were carried out intermittently usually in response to a directive from Government. The outcome was a series of uncoordinated initiatives with minimal follow up. Indeed the event, such as for example the 10th Anniversary of Independence was frequently viewed as the final objective.

The analysis of the LNDC's record of investment promotion concluded that a clear strategy should be developed with dedicated staff members. This policy was adopted by the Board in October 1977. The objective was to formulate a coordinated investment promotion programme. It was explicitly agreed that the LNDC would take full responsibility for coordinating the programme. The Corporation was to begin reviewing the incentive package, to identify the more attractive sectors for inward investment, to develop detailed project profiles, and to identify potential investors. A series of overseas investment promotion missions were to follow from the above.

During the following year (1978) a number of Investment Conferences were organized. One meeting held in Durban resulted in contacts being made with twenty companies three of whom agreed to establish manufacturing projects. The evident success of the new policy provided a stimulus for the establishment of a specialized Investment Promotion Unit within LNDC in January 1979.

The Investment Promotion Unit was initially staffed by an Expatriate on secondment from the Irish Industrial Development Authority. A Mosotho counterpart was recruited in April. Despite provision for an Investment Promotion Officer no one was recruited - with the exception of a University Student on a vacation job - during the first nine months. The Mosotho counterpart attended a course on Investment Promotion in Ireland. Consequently, during the first year of operation the Investment Promotion Unit consisted primarily of one individual. In order to compensate for the staff shortage the Managing Director allowed staff from other divisions to be seconded on an ad hoc basis to implement the investment promotion.

Within four months of the Investment Promotion Unit being established a programme of action was formulated. The targets for the new unit were: market research to identify 100 companies per month; contacts 25 of the companies; 10-12 presentations; and 4 site visits. The LNDC programme identified four principal areas for the new unit.

- Market Research

- Direct Contact with target companies

- Organization of Promotional functions

- Preparation and dissemination of publicity on LNDC and Lesotho.

The major activity of investment promotion was defined as direct contact with a potential investor. All the other areas were viewed as essential to achieving the direct contact. Although the on market research and identification of appropriate areas for investment were cosidered to be important, the manager of Investment Promotion Unit was constrained by manpower shortages from implementing these tasks.

The new commitment of LNDC to attracting foreign investors through promotion was carried out by a series of 'high profile' one day conferences that took place on a monthly basis in the RSA during 1979. The Corporation began its promotion outside South Africa in 1979 with a visit to the USA in August. During the following year missions were made to Europe, the Far East and the USA. The stated objective was to expand the overseas activities without lessening contact with South Africa.

During 1980 there was a complete turnover of staff in the Unit with the original local counterpart leaving and being replaced by a transport economist. Two Investment Promotion Officers were appointed from new graduate recruits to the Corporation. During 1980 the expatriate left and the Mosotho counterpart was appointed as Manager. In the same year all three staff attended a three month course on Investment Promotion organized by the IDA. The Unit retained the same personnel until it was restructured in 1983.

With the recruitment of additional staff during 1980 the promotion Unit began to develop its market research capacity. Contact had been made with the South African Foreign Trade Organization (SAFTO) which was employed as consultant for two major Investment Conferences in Johannesburg in June and a mission to Germany in May 1981. The research was carried out using Business Directories (Braby's), the JSE Handbook and MacGregors Who Owns Whom. For overseas marketing, Kompass and Standard & Poors Directories were obtained. The background research consisted of identifying the names of companies in particular product sectors from the Trade Directories.

There appears to have been an informal 'rule' that only foreign owned companies employing a minimum of 250 persons would be contacted. There was no emphasis on turnover nor on the amount of capital to be invested. Further, the 'employment rule' was never enforced since the Unit trawled through the Directories by Product category and every entry was either mailed or contacted by telephone. The former head of the unit estimated that 50% of all presentations were arranged with the Corporation having no prior information on the company.

The absence of pre-screening prior to making a presentation was compounded by the emphasis within the Corporation on quantitative targets. In 1980 and 1981 the Unit's targets for presentations were 400 and 900 respectively. Perhaps it is unsurprising that there was a very low rate of conversion from presentation to site visits. The Unit was responsible for organizing the site visit, although during the visit the investor would meet the Director of Projects to discuss the preparation of a proposal. Only at this stage would the technical and financial details be discussed. During this period, none of the Investment Promotion Staff were trained in project analysis or appraisal.

Promotional material consisted of a Quarterly Newsletter which began in 1979. This featured articles on New Projects and the expansion of existing projects. The Investment Guide which outlined the procedures involved in investing in Lesotho, described the incentive package and the existing industrial structure. This was first prepared in 1981.The objective of the Investment Guide was stated clearly at the outset to provide the basic information needed by a potential investor in Lesotho. The potential investor was assumed to be foreign and producing for export. The guide has been updated periodically, however, the first major rewrite was in the 1989 edition. An audiovisual slide presentation was prepared during 1979.

During 1979 the LNDC had a series of promotional functions in South Africa. A number of observations may be made on the promotions in South Africa:

- Three of the functions took the form of speeches at regular monthly meetings. Only two were specific conferences organized by LNDC with delegates attending with the sole intention of obtaining information on investment in Lesotho.

- The campaign was led by Government Ministers with LNDC staff in attendance.

- The LNDC Conferences were greeted with considerable interest both by the businessmen attending - with a significant number of site visits resulting - and by the South African media.

- The Conference approach succeeded in providing Lesotho with high profile business publicity in South Africa.

During the first six months of 1979 the following site visits took place. From fourteen site visits thirteen were South African companies, however, a small number had overseas links to a parent company in Europe. Out of these particular site visits no investment resulted.

In addition to the main market of South Africa which, on average, accounted for 64% of all presentations from 1979-83, attempts were made to promote in the Far East, Europe and the United States of America. Table 1 indicates the geographical spread of promotional activity. It is clear that within Europe the focus was on West Germany. The LNDC employed SAFTO as consultants for the series of Investment Seminars in Germany during May 1981. The visit to Austria during the same mission was primarily to meet with UNIDO. The Unit followed up the contacts with a presentation to all companies who were still interested 12 months later. Since 1983 there has been no systematic follow up. Two site visits resulted; however, no projects proceeded even to the negotiation stage.

The LNDC first visited the Far East in 1980 and followed up with an official mission in May 1981 led by the Minister of Trade & Industry. One industrialist from Hong Kong seeking to avoid quota restrictions on clothing imports to Europe subsequently invested in Lesotho. In Taiwan the Government encouraged the private sector to consider investing in Lesotho. The Chinese National Federation of Industries sent an 11 person mission to Lesotho (June 1981) to investigate investment possibilities. Investment proposals were forthcoming although before they could be implemented the GOL withdrew diplomatic recognition from Taiwan and recognized the People's Republic of China. This effectively halted any further direct contact with Taiwan. There was little interest shown in South Korea.

The investment promotion in Israel was made as part of the round trip to Germany. The two brief visits to Tel Aviv were not systematically followed up. The approach to the USA market was made through consultants who failed to generate even one site visit. They were employed on a retainer basis and were not renewed at the end of their contract.

After attending the Bulawayo Trade Fair in April 1982, the LNDC decided to mount an investment promotion drive in Zimbabwe. In November 1982, two members of the Investment Promotion Unit travelled to Zimbabwe and met 79 companies, out of which 16 expressed an interest in visiting Lesotho. In March of the following year the Corporation employed a consultant, on a one year contract, however, they were not satisfied with his performance. He was paid a commission on a company making a site visit. It appears that a number of site visits were made by companies wishing to increase their trade with Lesotho. His contract was not renewed and once again the LNDC began to directly promote in Zimbabwe. During 1984, the Zimbabwe government complained to the GOL that disinvestment was being encouraged. This effectively ended active investment promotion in Zimbabwe.

In the case of the overseas conferences LNDC personnel would return with a list of 'interested' businesses and hand over responsibility to the Investment Promotion Officers to follow up by letters. The Investment Promotion Officers were not invited to the original overseas conferences; consequently there was a break in continuity.

The number of presentations consistently exceeded 500 per year during the period 1980-83 while the number of site visits averaged 60 per annum. The breakdown of presentations and site visits during the period from the establishment of the Unit to its demise in October 1983 are shown in the Table.

LNDC Investment Promotion Unit 1979-83

	Presentations			Site Visits		
Year	RSA	Other	Total	RSA	Other	Total
1979	232	87	317	81	3	84
1980	338	242	580	59	10	69
1981	343	176	519	41	23	64
1982	329	212	541	36	12	48
1983	221	115	336	18	20	38

Source: LNDC

Although the RSA accounted for only 64% of the total number of presentations over the whole period, 78% of the site visits were made by South African companies. Overall, the Promotion unit made 7.6 presentations to achieve one site visit. When the analysis is restricted to South Africa the ratio declines to 6.2 presentations. The immediate results from the investment promotion programme were rather modest with 7 manufacturing companies beginning operations during the three financial years ending 31st March 1982.

By 1982, the initial commitment by the GOL to investment promotion was in doubt. The LNDC did not receive a subvention for 1983. During 1983, the LNDC experienced severe difficulties in conducting investment promotion in South Africa. The poor diplomatic relations between the two countries resulted in a decline in interest from the South African business community. The LNDC employed the services of a Public Relations Agency, although, this was terminated after a trial period when the agency concerned stated that it was very difficult to portray Lesotho in a positive light for investment given the prevailing political situation.

A detailed series of steps were laid down for arranging a face to face meeting with investors. This included collecting background information on the quantitative number of contacts per month. The number of companies visited included many where the only information available in advance was the product classification in Braby's Directory , the address and the name of the managing director. This resulted in contacts being made with a number of small and financially weak companies.

The Second Period (1983-1989)

In October 1983 the Investment Promotion Unit was disbanded. In its place a Market Support Unit was established. The Manager of the Unit and one Investment Promotion Officer - the other having been transferred within LNDC - were to be responsible for overseeing market research and conducting promotion outside of Africa. Investment contacts within South Africa were to be carried out by Project staff within the New Industries Division. The project staff were to be responsible for making the initial contact with the investor, the negotiation, appraisal and implementation of the project. The Market Support Unit was to liaise closely with the Public Relations Manager and to be responsible for the preparation of all promotional material.

It was the perceived absence of quality in the Investment Promotion targeting that encouraged the transfer of its responsibilities for promotion in Africa to the project officers within the New Industries Division. The project staff were now to be organized on clear product lines and to be responsible for their own promotion. **This structure still prevails**. The specialization by product area was aimed at staff developing a detailed knowledge of the economic/financial conditions prevailing in the various sectors. The Corporation began subscribing to a range of specialist trade journals and subscribed to the services offered by the Bureau of Market Research of UNISA (University of South Africa). UNISA maintains a database of all manufacturing companies registered in South Africa and provided printouts by product, employment, size, and address. The Corporation also subscribed to Dun and Bradstreet and SVP which provided credit references and general market information respectively. Promotion by project staff was also expected to address the problem of promotion being carried out by personnel who were not conversant with the technical issues of project appraisal. It was believed that promotion would become more 'business minded'.

The fundamental weakness of the current approach is the link between investment promotion and project appraisal. The project staff operated with quantitative employment targets from 1983 - 87. There was the potential for a conflict of interest in staff promoting to an investor and then appraising the project.

The three project areas (sectors groups) were defined as :

- (A) Food, Agro-Industries, Healthcare, Plastics and Chemicals

- (B) Textiles, Clothing, Wood & Furniture, Miscellaneous Consumer goods

- (C) Engineering, Electrical Electronics and Building Materials

LNDC Presentations and Site Visits

(October 1983 - August 1987)

	Presentations				Site Visits			
	sectors				sectors			
Year	A	B	C	Total	A	B	C	Total
10/83-3/84	4	2	22	28	2	3	3	8
FY1985	64	106	70	240	17	19	39	75
FY1986	12	0	45	57	22	26	14	62
FY1987	0	45	21	66	23	25	31	79
4/87-8/87	8	23	3	34	15	27	32	74

Source: LNDC Monthly Reports

The record of presentations and site visits from October 1983 - August 1987 is shown above in Table 3. The data was compiled from monthly divisional progress reports which stopped listing promotional activities after August 1987. Although detailed reports of investor contacts and site visits are still maintained by the project sections.

The reorganization of investment promotion resulted in an immediate decline in the number of promotion activities. More emphasis was put on identifying potential companies and improving the presentation skills of project staff. During 1984 all the project sections went on extensive promotion missions which resulted in a positive response measured by the number of site visits. The textile and clothing section received such a large number of serious enquiries following from the presentations that a moratorium had to be put on presentations during FY1986 as project staff were preoccupied with project appraisal.

After 1985 the ratio between presentations and site visits changed markedly as Investors began to visit Lesotho without a prior presentation. The majority of these companies were in the clothing sector with a factory in South Africa producing for export markets. They were concerned that the threat of sanctions would restrict their access to foreign markets. Companies in this sector account for a significant proportion of the rapid growth of the manufacturing sector from 1986. During FY 1987, eight out of the nine new manufacturing projects produced clothing. The same projects constituted the bulk of the demand for factory shells. A considerable proportion of project officers' time was focussed on processing projects requiring a factory shell with less and less time spent on a pro-active investment programme. In 1987, it was estimated that approximately one third of a project officer's time was spent on promotional activities. This would appear to be an upper bound estimate,with the proportion declining over the past two years.

The growing threat of sanctions was regarded as generating 'free' investment promotion. During 1986 the Investment Promotion Manager left and has not been replaced. The absence of a pro-active investment promotion strategy was noted by the Industrial Sector Study in 1987. It recommended an immediate expansion with the opening of offices in the Far East, USA and Europe. A total staff of 12 was recommended.

The signing of the Highlands Water Treaty in October 1986 presented the LNDC with additional opportunities for industrial growth. At the outset it was envisaged that considerable potential existed for the development of industries to supply inputs to the Highlands Project. The LNDC allocated a senior staff member to work with an expatriate engineer to develop project profiles. They identified 40 possible investment opportunities related to the LHWP. The Economic Impact Study (Coopers and Lybrand: Lesotho Highlands Water Project: Phase IA Economic Impact Study, April 1989) identified 70 business opportunities, and observed that the majority were suitable for small scale enterprises as it would be unsound to develop projects on a scale which could only be viable if the LHWP purchases only, or even mainly from them. Thus although there are many business opportunities relating to the LHWP, the promotion of large scale joint ventures premised on the supply of inputs to the LHWP, is unlikely to yield significant returns.The challenge for the LNDC is to promote local business involvement. The wider opportunities from the LHWP relating to investment promotion are the prestige that it brings to Lesotho. The management of the project enhances the image of Lesotho as a low risk, stable environment - a good place to do business. The existence of the LHWP could be emphasized in all promotional campaigns aimed at attracting investment unrelated to the project.

The LNDC revised its organization structure in January 1988 and recreated the post of Investment Promotion Manager. To date this position has remained vacant with the Corporation continuing its reactive approach. Consequently, de-facto the situation now prevailing is unchanged since October 1983.

The Lessons of The Past Experience

The evaluation of the effectiveness of Lesotho's investment promotion strategy is problematic because data is not available on the additional investment generated. Even if data were available it is possible that a company may invest several years after the date of first contact. In view of these problems, information will be presented on the cost of investment promotion and the possible results in terms of new manufacturing projects implemented, to help draw out the implications of the earlier strategy.

Investment promotion expenses are listed separately in the LNDC's Head Office accounts for the period FY1980-FY1984. For the period FY 1985-FY1987, the cost of investment promotion has been estimated to be approximately half of total travelling expenses. This rough approximation is premised upon the doubling of travelling expenses after the dissolution of the Investment Promotion Unit. It is not possible to carry this estimate beyond FY1987 because there has been a large increase in foreign travel to negotiate projects. The decline in expenditure on investment promotion is shown in Table 4. It is quite striking when presented in constant 1980 prices.

Table 4: **LNDC Expenditure on Investment Promotion**
(000s Maloti)

Year	Current Prices	Constant (1980) Prices
1980	108	108
1981	309	272
1982	277	222
1983	71	50
1984	20	13
1985	85	48
1986	83	42
1987	64	29

NB: Year ending March 31st

The number of projects implemented was very low during the first half of the decade, excluding the cancellations which did not result in any inward investment. During the period 1980-83 there were a large number of cancellations reflecting a weak appraisal process. There would therefore appear to be a weak correlation between the level of investment promotion and the rate of inward investment. However, it would be fallacious to draw the conclusion that an active investment promotion programme would not yield increased results for the following reasons:

- the experience of the LNDC from 1979-85 would dictate a different strategy today.

- foreign investment since 1985 has been primarily in one sector - clothing - seeking a safe haven and avoidance of sanctions. In periods of comparative stability in RSA and reduced risk of sanctions, the level of new projects and jobs created can be much lower.

The experience of the LNDC in investment promotion may be summarized under the following heads:

- Organization and Funding

- Sector and country targeting

- Promotion techniques

- Investment environment

Organization and Funding

The Investment Promotion Unit should be independent and adequately staffed with personnel experienced in promotion techniques, project appraisal and negotiation skills in order to promote only screened investors. Promotion must be separated from appraisals for incentives and the provision of loans and/or equity. The organization requires security of funds to ensure the continuity of an agreed programme.

Sector and country targeting

It is important to have clear guidelines on the type of industry and the quality of investor that are being targeted. The emphasis must be on quality. Having agreed the guidelines it is necessary to undertake thorough market research, and maintain an up to date data base in order to ensure regular follow up.

Promotion techniques

The Conference/Workshop approach is more appropriate for raising general awareness regarding investment in Lesotho. The key to successful promotion is to arrange direct contact with the key decision makers in the key source country for FDI -- the RSA.

Investment Environment

A stable political environment is essential for the promotion of inward investment. The LNDC experienced a rapid decline in interest when Lesotho's diplomatic relations deteriorated with South Africa.