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COMPARATIVE STUDY OF NATIONAL STRATEGIES AND POLICIES WITH REGARD TO FOREIGN DIRECT INVESTMENT IN THE ESCWA REGION

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ABBREVIATIONS

AFTA	Arab Free Trade Area
BOT	build-operate-transfer
EU	European Union
FDI	foreign direct investment
FIPA	Foreign Investment Promotion Agency
GCC	Gulf Cooperation Council
GDP	gross domestic product
ICRG	International Country Risk Guide
IDAL	Investment Development Authority of Lebanon
IMF	International Monetary Fund
IPRs	intellectual property rights
JD	Jordanian dinar
MENA	Middle East and North Africa
MERCOSUR	Southern Cone Market (Argentina, Brazil, Paraguay and Uruguay)
NAFTA	North American Free Trade Agreement
OECD	Organisation for Economic Cooperation and Development
PPI	private participation in infrastructure
QIZ	Qualifying Industrial Zone
TNC	transnational corporation
TRIPs	Trade-Related Aspects of Intellectual Property Rights
UNCTAD	United Nations Conference on Trade and Development
WIPO	World Intellectual Property Organization
WTO	World Trade Organization

EXECUTIVE SUMMARY

The purpose of the present study is to examine how ESCWA member countries have fared in attracting foreign direct investment (FDI). The study reviews those policies that have been the most successful in attracting inflows of FDI. The review focuses on case-studies of selected ESCWA member countries, namely Bahrain, Jordan and Lebanon. The analysis in the study is based on the findings of a survey of a sample of FDI enterprises in the selected ESCWA member countries and, for purposes of comparison, refers to the cases of Egypt, Morocco and Tunisia whenever relevant. The survey itself reflects the views of FDI enterprises with regard to the business environment, factors affecting investment decisions, and impediments faced in the host country.

In general, FDI is defined as those investments in which foreigners (in the sense of non-residents) own 10 per cent or more of the shares or voting power of an incorporated entity, and have the ability to exert a significant degree of influence, if not control, on the management of the enterprise. With regard to the above three ESCWA member countries covered herein, the present study shows that FDI has grown faster than either trade or income. Between 1985 and 1997, worldwide nominal GDP increased at a rate of 7.2 per cent per year and worldwide imports at 9.2 per cent, while FDI flows increased at an annual average of 18 per cent. The 1990s witnessed the emergence of a trend characterized by increased FDI flows to developing countries; however, these FDI flows decreased significantly in 1998-1999, mainly because of the crises in Asia and the Russian Federation.

The survey revealed differences in the reasons why foreign companies invest in the three countries selected for this study. The reasons included the size of the domestic market, access to regional and world markets, availability of local skills, low-cost labour, favourable incentive systems, and the existence of an entrepreneurial culture and competent local partners. Each of these reasons had a different impact on the final decision to invest in the three countries. For example, Bahrain has attracted investments in heavy industry and finance, Jordan has attracted investors in phosphates and potash, and recently in the garment sector, telecommunications and cement. With respect to Lebanon, and for the early 1990s, the majority of foreign investments were in mobile telephony, postal service, food service, clothing and the beauty industry.

Regarding the legal and institutional environment for FDI in the region, the study shows that most ESCWA member countries offer incentives in one form or another to encourage FDI, and in particular, fiscal incentives including tax holidays. In Jordan and Lebanon, the findings of the study indicate that the incentive system is not as important as in Bahrain. Other variables besides tax incentives played a more important role, and they included infrastructure development, size and growth rate of the market, the legal system and the FDI regulatory framework, macroeconomic and political stability, wage rates and levels of human capital development.

The findings of the study also indicate that foreign companies did not, in general, complain about discriminatory treatment in the countries under review. Securing land and real estate has become easier, as regulations governing land and real estate ownership have been relaxed for foreigners. A one-stop-shop for foreign investors has been established with the aim of facilitating administrative procedures for registration and establishment of their companies.

The survey for the study showed, however, that customs procedures and customs duties still constituted the two major barriers to trade, and that complex administrative procedures were the major problem faced by foreign companies when starting up activities in the selected countries. Other constraints included unexpected changes in economic policies, inappropriate judiciary systems, a lack of transparency in the tax system, and the relative absence of technical skills in the labour force.

Privatization is one of the most effective policies that Governments can use to attract FDI. The vast majority of FDI—over 90 per cent—in developing countries has come from privatization transactions, in particular private participation in infrastructure. The share of FDI in privatization programmes in the region increased dramatically in the 1990s. The privatization of the telecommunications, electricity and transport infrastructure has been the most effective means to interest foreign investors. Privatization can therefore be a

very powerful policy instrument to attract FDI, particularly when Governments establish the appropriate legal and regulatory environment for FDI and for private participation in infrastructure.

Although the ESCWA member countries have been active in concluding bilateral investment treaties, those countries that have succeeded in signing the greatest number of agreements have not necessarily been those that received the highest FDI inflows. There is, therefore, a need to continue to improve these countries' bilateral relations with their main trading and investment partners, notably the European Union (EU) and neighbouring Arab countries.

In addition, member countries should implement and enforce the Arab Free Trade Area (AFTA) as rapidly as possible and should introduce their own investment framework, standards, and rules of origin. They should also remove intraregional restrictions that may divert FDI to other regions. Fast-track negotiations among Arab countries are warranted to ensure that the overall interests of each AFTA member are respected and protected.

Cross-border mergers and acquisitions have increased significantly in the last decade; they have been concentrated primarily in the developed world. There are very few enterprises in the ESCWA region that are potential targets for such mergers and acquisitions. Firms in the region are often small in size, overburdened with a surplus of labour, and do not meet international standards for good corporate governance (including transparency, incentives for managers, oversight of managers and rights of minority shareholders). Exceptions to this are the utilities and telecommunication companies, as well as other infrastructure projects. Given the relatively small size of the economies in ESCWA member countries, any mergers and acquisitions could have a significant impact on the host economy.

Based on the findings of the survey and the deliberations of the participants in the above-mentioned Regional Seminar held to discuss the results of the survey, this study recommends that ESCWA member countries should introduce privatization programmes geared to inject FDI into infrastructure development. Such programmes could include telecommunications, electricity, roads and water. This study also recommends that the ESCWA member countries should develop the private sector within a framework of regional cooperation in order to attract more FDI. The modernization of national legal and institutional frameworks for investment, by introducing international norms and standards, would inevitably lead to the harmonization of laws and regulations among the countries of the region. Such development would greatly contribute to the emergence of an integrated market for investors, both domestic and foreign.

Investment promotion agencies in the various countries in the region also need to identify and disseminate information on investment opportunities, and foster strategic alliances between local firms and foreign companies through subcontracting, joint ventures and other forms of cooperative arrangements. The ESCWA members can work on establishing an environment conducive to cooperative arrangements with transnational corporations (TNCs) and, by doing so, assist firms in their own countries in capturing global markets.

The basic challenge for the authorities in ESCWA member countries will be to establish a clear, reliable and predictable legal framework for investment by TNCs. The proper enforcement of intellectual property rights (IPRs) is crucial for the development of FDI in the information and communication sectors, in the pharmaceutical industry, in the media and entertainment industries, in education, and in many other growth sectors where some of the world's largest TNCs operate.

Finally, the ESCWA member countries need to liberalize trade at bilateral, regional, and multilateral levels and to conclude various investment treaties and double taxation avoidance treaties. Although bilateral agreements are important, the greatest economic potential can only be achieved through deeper Arab trade integration (the Greater Arab Free Trade Area), combined with Euro-Mediterranean integration and multilateral integration within the context of the World Trade Organization (WTO).

I. OVERVIEW

One of the most powerful forces of globalization is the increasing volume and spread of foreign direct investment (FDI). The flow of capital across borders, of which FDI is part, leads to deeper and greater international economic integration. For good or bad, countries compete to attract FDI. To decision makers, FDI represents not just access to more capital but the promise of improved management skills and technology transfer. It also represents the promise of an improved position in the global trade system and of greater exports.

The purpose of the present study is to examine how ESCWA member countries have fared in attracting FDI. To that end, the study targets a select number of countries for which data were readily available: Bahrain, Jordan and Lebanon. For purposes of comparison, whenever relevant, the study also refers to the cases of Egypt, Morocco and Tunisia. The study focuses on those policies that have been most successful in attracting FDI inflows.

FDI flows in the world have been increasing at record levels and were expected to surpass the US$ 1,100 billion mark in 2000.[1] They have doubled in 3 years, and have more than quintupled in 10 years. Developed countries continue to be the main players, as most of the FDI flows between them. However, the share of FDI inflows to the developing world—most notably Latin America, the Caribbean, South-East Asia, and China—increased in the 1990s, only to decrease slightly in the latter part of the decade.

Unfortunately, FDI inflows to the ESCWA region cannot be characterized as part of a positive trend. The region's share in world FDI inflows remained below the 2 per cent mark in 2000. Most of the West Asian inflows were originally invested, in the past two decades, in the rich Gulf States and in oil-related projects (resource-based FDI). More recently, some improvements were noted: in Egypt, and in the two North African countries of Tunisia and Morocco. This improvement was partly due to the increased pace of privatization.

The FDI experience in the ESCWA region differs from country to another. There are country-specific obstacles, as well as cross-country obstacles, that are hindering the growth of FDI inflows. The former include a weak macroeconomic environment and an antiquated legal environment. The latter include barriers to trade as well as capital controls. The major obstacle to FDI inflows is the performance of the region's economy over the past few years. Policy-induced obstacles to FDI can be grouped into three categories: economic, institutional, and political.

Economic policy obstacles to FDI include an onerous tax regime, restrictions on foreign ownership, restrictions on freedom of exchange and remittance of profits, small economy and/or lack of regional trade integration, a scarcity of skilled labour, and inadequate infrastructure (telecommunications, transport and energy).

Institutional obstacles include lack of transparency concerning the rules and regulations governing investments, a weak legal system that does not deliver justice in a fair and timely manner, rigid labour laws and practices, high levels of red tape, bureaucracy and corruption, and inadequate protection of property rights (commercial and intellectual).

Political obstacles to FDI include political instability, arbitrary interventions in economic activity, and the risk of expropriation. Violence, recurring labour strikes, and other forms of tension can deter a foreign investor from venturing into an unstable country unless the return on that investment is high enough to compensate for the additional risk that is presented by the instability.

Although there is an overwhelming tendency in most developing countries to promote FDI, there are wide variations in the policies and strategies applied. It should first be noted, however, that only a few

[1] United Nations Conference on Trade and Development, *World Investment Report 2000: Cross-border Mergers and Acquisitions and Development* (United Nations publication, Sales No. E.00.II.D.20).

countries have a clear and consistent FDI strategy. Furthermore, many countries have problems with the application of their strategies.

These problems, in the context of the ESCWA region, arise primarily because there is a shortage of the skills needed to secure FDI inflows. Recently, a number of Arab countries established investment promotion agencies to promote foreign and domestic investments. Such agencies, however, are not a substitute for an FDI strategy but an integral part of it.

To develop the full potential of FDI, the ESCWA member countries would have to address several interrelated issues: (a) domestic political and social stability; (b) legal reform and the creation of a pro-business environment; (c) institutional (administrative) reform in both the public and private sectors; and (d) privatization and private sector development.

This study concentrates on the last three of the above issues. They clearly constitute economic policy parameters. An FDI strategy is a comprehensive arsenal of policies that goes far beyond the simple issue of taxation and subsidies. International experience shows that fiscal incentives, though welcome, do not constitute a sufficient determinant of FDI. The role of the State in attracting foreign investment is manifold and may include the following: (a) fiscal incentives, subsidies and other forms of State aid; (b) new legislation to create an enabling environment for the private sector to take a leading role; (c) competition and anti-trust legislation; (d) development of new financial instruments (such as leasing) and capital markets; (e) education and training of the labour force; (f) flexible labour legislation and cost-effective social security; (g) government procurement procedures; and (h) zoning regulations and environmental standards.

The ESCWA member countries need to establish a plan of action that takes into account market forces and the economy's comparative advantage. They need also to remove all distortions imposed on economic transactions. Privatization, regional integration, and cross-border mergers and acquisitions have been the most effective instruments in attracting FDI in other regions. The impact of these instruments on ESCWA member countries is reviewed in this study, in addition to other important factors such as foreign perceptions, protection of intellectual property rights, and political stability.

In reviewing the ESCWA region, the study examines thoroughly a selected number of countries, namely Bahrain, Jordan and Lebanon. The study includes the findings of a survey of a sample of foreign direct investment enterprises that was carried out in these countries. The survey also examines the views of FDI enterprises with regard to the business environment, factors affecting investment decisions, and impediments faced in the host country. Reference also has been made in the study, when relevant, to the experiences of Egypt, Morocco and Tunisia.

The study was enriched by the feedback received by the participants in the Regional Seminar on FDI National Strategies and Policies in the ESCWA Region, which was held in Beirut on 12 and 13 June 2001. The purpose of the Seminar was to discuss the main findings of the present study, including the findings of the above-mentioned survey. The recommendations adopted in the Seminar with regard to ways and means of improving the investment climate and attracting more FDI into the ESCWA region have been taken into consideration in the final version of this study.

Chapter II of this study revises the basic concepts and definitions of FDI and reviews the risk of negative implications of FDI on the host economy. Chapter III reviews the FDI performance of selected countries in the ESCWA region and identifies potential investors who may be interested in doing business in the region. The chapter also identifies the sectors that are most likely to attract FDI. Chapter IV reviews the legal and institutional environment in the region. Chapter V reviews major policies that are likely to promote FDI, notably the impact of privatization on FDI flows, international agreements as a determinant of FDI, and the importance of FDI through mergers and acquisitions. Chapter VI presents the main conclusions and recommendations of the study. The characteristics of the sample selected for the survey are contained in annex I to the study. Annex II to the study includes the questionnaire forms used for the survey.

II. INTRODUCTION TO FOREIGN DIRECT INVESTMENT: DEFINITIONS AND IMPLICATIONS

A. DEFINITION OF FOREIGN DIRECT INVESTMENT

Foreign direct investment (FDI) refers, in general, to investments in which foreigners (in the sense of non-residents) own 10 per cent or more of the shares or voting power of an incorporated entity. Both the International Monetary Fund (IMF) and the Organisation for Economic Cooperation and Development (OECD) use this definition of FDI. The 10 per cent threshold is indicative of the ability to exert a significant degree of influence, if not control, on the management of the enterprise.[2] The UNCTAD definition, which is based on the IMF/OECD definition, considers foreign direct investment as

> "an investment involving a long-term relationship and reflecting a lasting interest and control of a resident entity in one economy (foreign direct investor) in an enterprise resident in an economy other than that of the foreign direct investor...FDI implies that the investor exerts a significant degree of influence on the management of the enterprise resident in the other economy."[3]

Investments in which non-residents own less than 10 per cent of an entity are referred to as portfolio investments. Portfolio investors buy and sell on a short-term basis, and often have a passive interest in earnings potential.

FDI has three components:

(a) Equity capital, which is the foreign direct investor's purchase of shares;
(b) Reinvested earnings;
(c) Intra-company loans or debt transactions.

FDI stock is the value of the share of their capital and reserves (including retained profits) attributable to the parent corporation, plus the net indebtedness of affiliates to the parent enterprise. For many countries, FDI stocks are estimated by either accumulating FDI flows over a period of time or adding flows to an FDI stock that has been obtained for a particular year from national official sources or the IMF.

Investment undertaken by multinational corporations is often confused with FDI. FDI is not always equivalent to new investments made by foreign firms, since much of FDI never becomes investment in the real sense, but is simply a transfer of ownership of existing assets from local to foreign firms through mergers and acquisitions. Foreign investments can exceed, in real terms, the level of FDI when these investments are financed through borrowing on domestic capital markets. This study does not differentiate between FDI and real investments since the available data, especially for developing countries, are in aggregate format. Chapter V, however, addresses the subject of mergers and acquisitions in more detail.

The FDI regime is the legal framework within which FDI is admitted and regulated in the host economy. The legal context could include, among other things, constitutional provisions, laws, regulations, and policies. The FDI regime is supplemented by international agreements (such as avoidance of double taxation) that offer special rights or impose certain requirements on signatory countries.

There are five basic issues of concern for potential investors and these are: (a) admission; (b) treatment; (c) expropriation; (d) dispute resolution; and (e) exit. The FDI regime is evaluated according to its ability to address these five issues successfully. Admission is the procedure for legal establishment of FDI. Treatment refers to the manner in which FDI is received and treated, which is reflected in provisions for national treatment, repatriation of earnings, and freedom of activity. Expropriation refers to the institutions

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[2] Organisation for Economic Cooperation and Development (OECD), *OECD Benchmark Definition of Foreign Direct Investment*, third edition (OECD, Paris, 1996).

[3] UNCTAD, *World Investment Report 1999: Foreign Direct Investment and the Challenge of Development* (Geneva and New York, 1999), p. 465.

and practice of property rights and respect thereof. Dispute resolution refers to the local judicial and administrative system of the host country for settling disputes between investors and others, including the State, as well as among investors, unless there is explicit reference otherwise (for example, to international arbitration). Finally, exit refers to the mechanisms with which investors can liquidate their investments and repatriate their capital.

There are two principle types of FDI regimes: open investment regimes, and authorization—or approval—regimes. The former regime contains no special restrictions or special constraints beyond minimal conditions concerning public order and safety. The authorization regime, however, requires all or much of the FDI to be subject to specific approval prior to entry. Consequently, if public officials are not subjected to clearly defined criteria (such as time), the system could be inconsistent and unpredictable and it could open the way to high levels of corruption and other forms of abuse of authority. A limited discretion regime, with specific criteria guiding officials in screening proposed investments, limits the exercise of discretion of public officials in administrating investment regimes and may help to overcome many of the administrative hurdles associated with authorization regimes (such as Egypt since 1997). However, even a limited discretion authorization regime cannot match open investment regimes in terms of attracting investors.

B. TYPES OF FOREIGN DIRECT INVESTMENT

FDI has been categorized either by cause or by its structure, more specifically its relationship with the parent company if one exists.

With regard to causes or drivers, there are three main types of FDI:

(a) Natural resource-seeking, whereby foreign investment is a precondition for the production of primary products for foreign markets and generates exports of natural resources;

(b) Market-seeking, whereby foreign investment is an extension of the export strategy and FDI is used to penetrate heavily protected markets;

(c) Efficiency-seeking, whereby the investor is interested in realizing efficiency gains and FDI is used to produce more efficiently and therefore to expand export opportunities.

FDI has also been categorized according to whether it is horizontal or vertical FDI—another method of classification. Horizontal FDI replaces exports with local production to circumvent trade barriers and thus substitute for cross-border trade. In contrast, vertical FDI breaks down the vertical chain of production and relocates part of this chain to low-cost or higher efficiency locations. Vertical FDI is trade-creating given that products—and at different stages of the production process—are shipped between plant locations, often in different countries.

Economists have long argued about the main drivers of each type of FDI. It has been argued that FDI seeks to replace exports to markets where the costs of market access are high because of tariffs and non-tariff barriers, or where the costs of setting up a local plant are low. Similarly, the larger the market, the more likely it is that FDI would replace exports. With a larger market, the marginal fixed cost is reduced and the production cost is lowered.

Multinationals also shift their production process to low-cost locations. Theoretically, it is profitable to take advantage of countries where inputs are abundant and relatively inexpensive. This inequality in factor rewards (wages and rent) drives multinationals to undertake vertical FDI.

Multinational activity is overwhelmingly "horizontal," involving production for sale to the host market.[4] However, in developing countries, a greater share of multinationals' activity is "vertical," and it

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[4] Howard J. Shatz and Anthony J. Venables, "The geography of international investment," *The Oxford Handbook of Economic Geography*, G.L. Clark, M. Feldman, and M.S. Gertler, eds. (Oxford [United Kingdom], Oxford University Press, 2000).

involves manufacturing at intermediate stages of production. This explains why the largest share of FDI flows is between the United States and the EU member countries, with the United States accounting for the bulk of FDI inflows, followed by the United Kingdom of Great Britain and Northern Ireland.

C. Implications of foreign direct investment

In the 1980s, the disappearance of non-equity sources of foreign capital created a resurgence of interest in FDI. The need for alternative sources of capital led many developing countries to liberalize their FDI regimes and remove restrictions previously imposed on incoming foreign investment. Apart from employment creation and capital inflows, FDI is believed to favour technology and knowledge transfer to domestic firms. However, FDI is not a panacea and there is no justification for giving it any unfair advantage over local investment.[5]

Recent literature has raised some questions as to the positive spillover effects of FDI. First, there is mixed evidence on the role of foreign investment in causing technology transfer to domestic firms. A number of studies have shown that FDI may end up, in some cases, creating islands of technologically advanced industries with few linkages to the rest of the economy. Several plant-level studies have failed to find positive spillover from FDI to domestic firms competing directly with subsidiaries of multinational corporations. Subsidiaries of multinational corporations have been found to be more productive than their local counterparts.[6] Whether or not technology transfer will take place depends on a number of factors, the most crucial of which is the ability of a society to adapt new technologies and levels of investment in human capital (through education and training).

A second concern has been that productivity across domestic plants tends to fall when foreign investment increases and that foreign plants outperform domestic plants, creating a two-speed economy. A study by Aitken and Harrison[7] finds that there is a strong relationship between increased foreign equity participation and plant performance, suggesting that FDI benefits domestic firms. However, the evidence produced by the study also suggests that FDI has been associated with a drop in productivity among domestic firms. This drop in productivity may be attributed to the fact that foreign firms (FDI) can steal demand from domestic firms given the existence of imperfectly competitive markets. The drop in demand for local production causes domestic firms to cut production. Moreover, the performance differential between domestic and foreign firms can be attributed to a slow transfer of technology. The present study concludes that there is no positive spillover impact on domestic firms. This finding is supported by a study of the Czech economy that concludes that there was a negative spillover effect of FDI on the local economy.[8]

A third concern is that FDI is believed to crowd out domestic investments. Crowding out (or replacing) can take place both in the financial and the product markets. When multinational corporations borrow on the local market, the increased demand for capital will drive interest rates higher and thus cause a decline in the overall investment level. This impact affects the local economy regardless of the industry hosting the multinational corporation. Similarly, competition between local and foreign firms in the same product market can also create a crowding out effect if the multinational corporation is competing directly with the local enterprise.

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[5] Gordon H. Hanson, *Should Countries Promote Foreign Direct Investment?*, Paper No 9, G-24 Discussion Paper Series, United Nations and the Center for International Development, Harvard University (UNCTAD, 2001).

[6] Kamal Saggi, *Trade, Foreign Direct Investment, and International Technology Transfer: A Survey* Policy Research Working Paper 2349 (Washington, D.C., World Bank, 2000).

[7] Brian Aitken and Ann Harrison, *Do Domestic Firms Benefit from Foreign Direct Investment? Evidence from Panel Data*, Policy Research Working Paper 1248 (Washington, D.C., World Bank, 1994); and Brian Aitken and Ann Harrison, "Do domestic firms benefit from direct foreign investment? Evidence from Venezuela" in *American Economic Review* 89(3), June 1999, pp. 605-618.

[8] S. Djankov and B. Hoekman, "Foreign investment and productivity growth in Czech enterprises," *World Bank Economic Review* (Forthcoming).

In contrast, when multinational corporations introduce new products to the economy, FDI crowds in (creates new) domestic investment by creating business opportunities for the local entrepreneurs who will supply the multinational corporations (opportunities better known as linkages). This was the case in Costa Rica when Intel decided to build a large microprocessor plant, a line of production new to the local economy. Local firms did, however, complain about one form of crowding out, and that was in the labour market where Intel was "accused" of absorbing all the skilled programmers.[9]

Agosin and Mayer empirically examined the potential crowding in or out effect of FDI.[10] They found that in Asian countries—less so in Africa—there has been a crowding in of domestic investment by FDI. In contrast, a strong crowding out has been witnessed in Latin America. In Morocco and Tunisia, FDI was judged to have a neutral impact on domestic investment, and it was not empirically established that there was either a crowding in or a crowding out. At any rate, these results raise the question of whether and how government policies can encourage a crowding in rather than a crowding out of investments.

Agosin and Mayer argue that if FDI enters the economy where there are competing domestic firms, the very act of foreign investment may take away investment opportunities that were open to domestic entrepreneurs. The opposing hypothesis is that the entry of multinationals in new activities may pre-empt investments by domestic firms with some governmental assistance, as was, to a certain extent, the case in the Republic of Korea and Taiwan Province of China. It can also be argued that foreign investment drives incumbent domestic firms to increase their investment in order to become more competitive. Whatever the theoretical explanation, the data fail to uphold the hypothesis assuming a positive impact of FDI on domestic investment.

TABLE 1. EFFECT OF FOREIGN DIRECT INVESTMENT ON INVESTMENT IN DEVELOPING COUNTRIES

Crowding in	Neutral effect	Crowding out
Republic of Korea	Morocco	Nigeria
Thailand	Tunisia	Central African Republic
Pakistan	China	Zimbabwe
Ghana	Indonesia	Sierra Leone
Senegal	Malaysia	Jamaica
Côte d'Ivoire	Sri Lanka	Guatemala
	Philippines	Bolivia
	Argentina	Dominican Republic
	Brazil	Chile
	Mexico	
	Peru	
	Colombia	
	Costa Rica	
	Ecuador	

Source: Manuel R. Agosin Ricardo Mayer, *Foreign Investment in Developing Countries: Does it Crowd in Domestic Investment?* (UNCTAD/OSG/DP/146), UNCTAD Discussion Paper No. 146, February 2000.

Note: This table covers the period 1970-1996.

[9] UNCTAD, World Investment Report 1999: Foreign Direct Investment and the Challenge of Development.

[10] Manuel R. Agosin and Ricardo Mayer, *Foreign Investment in Developing Countries: Does it Crowd in Domestic Investment?* (UNCTAD/OSG/DP/146), UNCTAD Discussion Paper No. 146, February 2000.

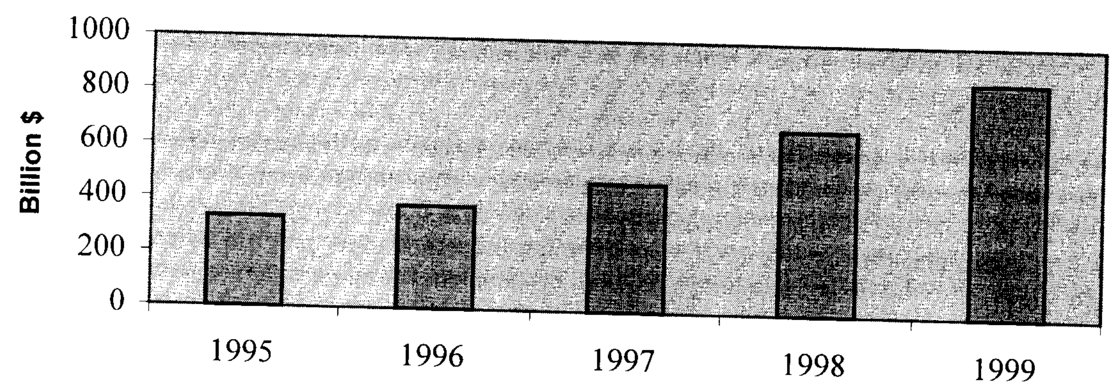
III. INFLOWS OF FOREIGN DIRECT INVESTMENT TO THE ESCWA REGION: TRENDS AND PERFORMANCE

The extent to which a country can attract FDI has been considered to be an accurate measure of the ability to generate growth and prosperity for its residents. A more accurate measure of that, however, would be measures of the growth of competitiveness and the current competitiveness of economies.[11] None the less, FDI inflows are a good indicator of the health of a developing economy.

A. GLOBAL TRENDS

Foreign direct investment has grown faster than either trade or income. Between 1985 and 1997, worldwide nominal GDP increased at a rate of 7.2 per cent per year and worldwide imports at 9.2 per cent, while FDI flows increased at an annual average of 18 per cent. The developed countries constitute the predominant source of supply (89.9 per cent of FDI stock in 1997); similarly, 71.5 per cent of FDI was destined to industrially advanced countries in the period between 1985 and 1997.[12]

Chart 1. Worldwide inflows of foreign direct investment



Source: UNCTAD, *World Investment Report 2000: Cross-Border Mergers and Acquisitions and Development* (New York and Geneva, 2000).

At a parallel level, a trend emerged in the 1990s, characterized by an increase in FDI flows towards developing countries. Between 1993 and 1997, the inflow rate to developing countries and countries with economies in transition more than doubled, to 1.91 per cent of GDP, while for developed countries it decreased by 0.87 per cent of GDP. A review of the distribution of FDI flows among developing countries shows that only 10 countries accounted for more that two thirds of all FDI flows during the period 1993-1997, with China alone receiving an annual average of 30.6 per cent of the total. Other large recipients of FDI are: Argentina, Brazil, Chile, Mexico, Poland, Hungary, Singapore, Malaysia and Indonesia.

At the regional level, Latin America (including Caribbean countries) received the largest level of inflows per capita. The West Asian[13] per capita level, though small, increased and approached the level of the South-East Asian countries. The explanation for the convergence is attributed to an increase in the inflow level for West Asia coupled with an increase in the population rate for the other region. The Asian crisis was

[11] World Economic Forum, *The Global Competitiveness Report 2000* (New York and Oxford [United Kingdom], Oxford University Press, 2000).

[12] Venables and Shatz, op. cit.

[13] The West Asia region includes, according to the UNCTAD *World Investment Report*, the ESCWA member countries in addition to three other countries in Western Asia (Cyprus, the Islamic Republic of Iran, and Turkey).

also a factor behind the decline in the FDI share for the South-East Asian region, from 22.1 per cent in 1996 to 12 per cent in 1998.

TABLE 2. INFLOWS OF FOREIGN DIRECT INVESTMENT PER CAPITA
(*US dollars*)

	1995	1996	1997	1998
World	580	624	796	1 089
Developed	2 386	2 403	3 093	5 183
Developing	238	298	374	354
Latin America	697	962	1 401	14 480
West Asia	-20	28	207	200
South-East Asia	222	260	283	246

Source: UNCTAD, *World Investment Report 1999: Foreign Direct Investment and the Challenge of Development* (New York and Geneva, 1999).

B. FLOWS OF RETAINED AND REPATRIATED EARNINGS

Before examining further FDI flows in the region and the world, it is important to determine how earnings of multinational corporations (retained and repatriated) are moving across the developing countries and the world. This analysis sheds some light on the direction followed by a foreign investor. A high level of repatriation, for instance, could signal a disinterest in the existing investment project or simply that there is little need to retain profits since capital can be easily raised and at more favourable real rates on the domestic market. The opposite may be true if the level of retained earnings is high.

Multinational corporations finance their affiliates with both internal and external capital. Internal capital originates from the parent company (retained earnings and intra-company transfers) whereas external capital (such as loans) can be raised from international as well as domestic capital markets. In other words, a multinational corporation can borrow money from domestic sources, and that amount will be considered a part of the FDI inflows (from a balance-of-payments perspective).

In 1994, American multinational corporations raised more capital from the domestic markets of developed countries where capital markets are advanced, resources are available, and borrowing rates compared favourably with United States rates (see table 3). When operating in developing countries (such as Mexico and Brazil), American multinational corporations relied more on retained earnings and other transfers from the parent company (intra-company transfers) to finance business activity. Retained earnings constituted 30 per cent of the needed capital for American multinational corporations to operate in Mexico, compared with just 8 per cent when they operate in Germany.

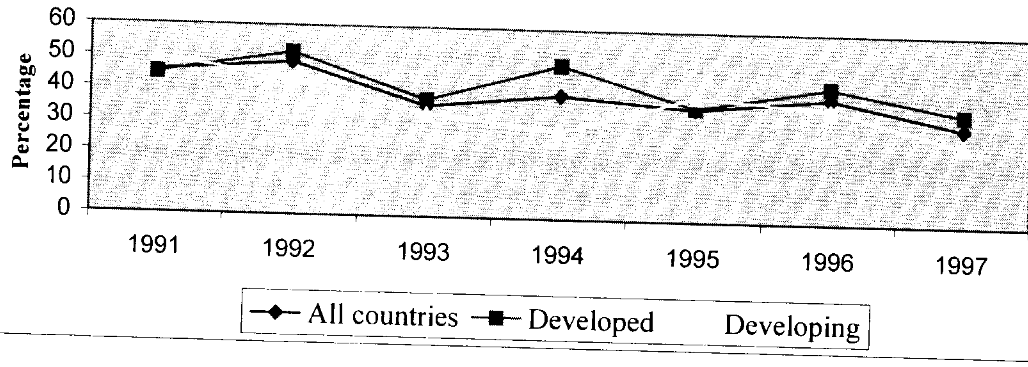
TABLE 3. SOURCES OF FINANCING OF FOREIGN AFFILIATES OF AMERICAN MULTINATIONAL CORPORATIONS, 1994
(*Percentage*)

Source	All countries	Brazil	Mexico	Germany
External to host countries	58	64	70	46
Parent companies	24	34	32	21
Retained earning	13	24	30	8
Non-FDI financing	21	6	8	17
Internal to host countries	42	36	30	54
Total	100	100	100	100

Source: UNCTAD, *World Investment Report 1999: Foreign Direct Investment and the Challenge of Development* (New York and Geneva, 2000), based on data from the United States Department of Commerce.

Profit not reinvested is repatriated to the home country. The repatriation constitutes a financial outflow. The repatriation of earnings leads to the question of balance-of-payment effects of FDI. If the ratio of repatriated profits to inflows is small, then net capital inflows are increasing and the net effect of FDI on the balance of payments is positive. With the exception of Africa, where repatriated earnings made up on average 75 per cent of new FDI inflows between 1991 and 1997, that ratio for all developing countries has been decreasing, from 50 per cent in 1991 to 25 per cent in 1997.

Chart 2. Repatriated earnings with regard to FDI inflows



Source: UNCTAD, *World Investment Report 1999: Foreign Direct Investment and the Challenge of Development* (New York and Geneva, 1999).

Chart 2 shows that the repatriation to inflows ratio is often higher in the developed world. This could be attributed to the fact that multinational corporations operating in advanced economies rely more on raising capital locally than on retained earnings and thus repatriating more of their profits back to their home country, and that developing economies tend to have more restrictions on capital accounts. As far as the developing countries are concerned, the ratio of repatriation to inflows is improving. This trend is not necessarily a symptom of economic strength. It could reflect more interest and trust in the local economy, but it could just as well reflect the inability of multinational corporations to raise funds locally (hence the need to reinvest earnings). Governments wishing to reduce the level of repatriation without imposing restrictions on the transfer of capital (which will have the counterproductive effect of scaring away FDI) can resort to a number of measures such as eliminating or reducing the marginal tax rate on capital gains and removing restrictions on the expansion of foreign investment projects.

C. CROSS-REGIONAL COMPARISON

The World Investment Report (2000) shows a decline in the share of developing countries out of the total level of world inflows. The peak level of inflows was reached in 1996/97, later to be followed by a significant drop in 1998 and 1999. The Asian and Russian crises are probably the main contributing factors to the drop in FDI inflows to developing countries.[14]

[14] The share of inflows to South Asia, East Asia and South-East Asia dropped from 22.1 per cent in 1996 to 12 per cent in 1998.

Box 1. Statistics on foreign direct investment

Two definitions and sources

There are two main definitions of FDI: the International Monetary Fund's *Balance of Payments Manual* (the main source for the UNCTAD *World Investment Reports*); and the Organisation for Economic Cooperation and Development's Benchmark Definition. In comparison with the IMF definition of foreign direct investment, the OECD definition is more inclusive. However, recent revisions of the OECD definition are now more consistent with the IMF definition; nevertheless, discrepancies in calculating level of inflows and FDI stocks persist.

UNCTAD estimates FDI stocks by either cumulating FDI flows over a period of time or by adding flows to an FDI stock that has been obtained for a particular year from national authorities or from the IMF. The definition of FDI stock is actually the value of the share of capital and reserves (including retained profits) attributable to the parent corporation, plus the net indebtedness of affiliates to the parent enterprise. The OECD recommends, however, that short-term loans and trade credit should be included, as there is no clear distinction between short-term and long-term finance. Differences also exist in calculating flows between the OECD and the IMF, mainly because there are differences as to what constitutes FDI.

UNCTAD collects published and unpublished national official data directly from Central Banks and other national authorities. These data are complemented with figures obtained primarily from the IMF, and, when needed, UNCTAD relies on the World Bank and the OECD. In certain cases, such as in Latin America, OECD data on FDI outflow to developing countries are used to estimate the level of inflows for the respective recipient countries.

It should be noted that a number of agencies and organizations also calculate FDI, among them J.P. Morgan and the Institute of International Finance, in addition to the World Bank, the IMF and OECD.

Data reliability

A number of countries have failed to report one or more components of FDI (such as reinvested earnings, intra-company loans, or equity investment) to the IMF. The reporting is also inconsistent from year to year. For instance, Bahrain did not submit data on intra-company loans for the period from 1989 to 1998, nor did Bahrain report the amount of equity investment for the period from 1982 to 1989.

There is a lack of comparability of the FDI data of different countries. There are discrepancies between total inflows and total outflows on the one hand, and between total inward stocks and total outward stocks on the other hand. For example, the inflows to Lebanon from France--as reported by the Lebanese authorities—may not equal the outflows from France into Lebanon, as reported by the French authorities.

Countries also differ in their definitions of FDI when most of them partially rely on either benchmark definition (of the IMF or the OECD). The UNCTAD World Investment Directory for West Asia lists the various definitions of FDI as viewed by each country in the region. In addition, Governments calculate flows according to different methods; each one draws selectively from the IMF standardized methodology. Corporate accounting practices and valuation methods differ as well between countries.

National authorities rarely report the three components of FDI. Instead, they rely exclusively on foreign exchange records of the Central Bank that account only for the capital that crosses a country's borders, and not reinvested earnings. In fact, most countries in the Middle East and North Africa (MENA) do not provide detailed data on their FDI flows since they do not abide by either benchmark definition. Developed countries such as Canada and the United States supplement their exchange records data with periodic company surveys and censuses covering all aspects of FDI.

The valuation of FDI stock often does not account for inflation or movements in the exchange rates. Adding inflows to a past FDI stock, measured in what were then current prices, does not yield the real value of the stock. Moreover, if data on FDI flows are collected from exchange records, and FDI stock data from company surveys, the cumulative FDI flows do not generally equal stocks.

Box 1 *(continued)*

FDI flow data are calculated on the basis of the immediate host country and immediate home or investing country. This leads to an overstatement of flows since it is the ultimate host and destination that need to be considered. The overstatement is attributed to a high turnover rate, similar to the velocity effect of money creation. The German model made inroads in reducing the effects of FDI turnover by differentiating between primary and secondary FDI. The rest of the world needs to follow suit, but also to make further improvements to the German system.

FDI data often overlook flows attributed to the takeover of firms. A change of ownership between two foreign countries is not always recorded when it should be calculated as a dis-investment and then a direct investment. Furthermore, a gradual acquisition deal is treated as a portfolio investment (if less than 10 per cent of shares are initially acquired) and is not later added on as FDI when the acquisition is completed (that is, greater than 10 per cent ownership).

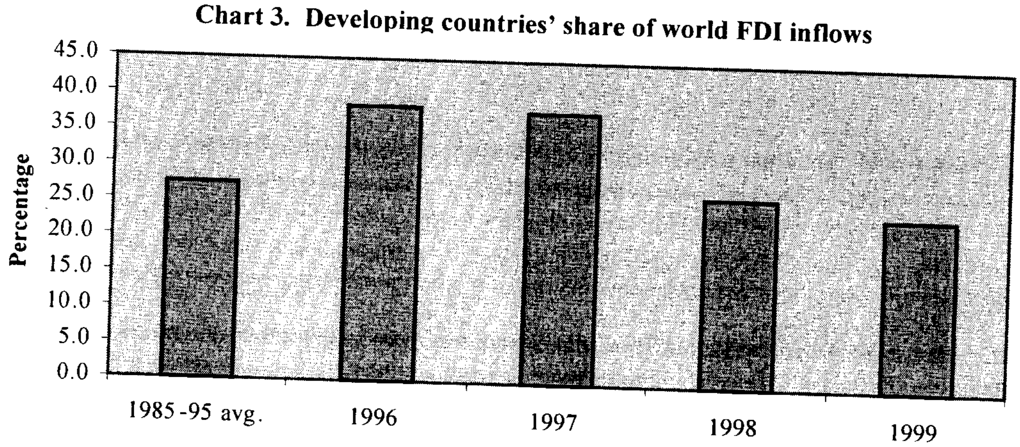
The measurement of FDI in the finance sector also creates over- or underestimation of flows. FDI data often mistakenly include deposits made by a parent bank in its foreign affiliates, considering them intra-company flows. These deposits may simply be driven by interest rate differentials or political uncertainty in a given country. Lebanon has to be especially careful to avoid this miscalculation, given its open financial sector.

To sum up, the ESCWA member countries need to move closer to a benchmark definition of FDI, preferably the narrow IMF/UNCTAD definition. Calculating data ought to move beyond cross-border capital flows to include the results from standardized and periodic corporate surveys. Countries have to provide data for the three FDI components, on a regular and consistent basis. Figures need to take into account price fluctuations (including inflation and exchange rates) and flows attributed to takeovers, but discount intra-company deposit transfers. Most important, the data have to avoid double and triple counting of flows by considering only the ultimate source and destination of investments, thus not including flows going through intermediate companies and countries. These recommendations are difficult to implement even for developed countries. However, unifying the basic concept of what constitutes FDI is a necessity, and a good starting point for ESCWA member countries in their effort to produce an accurate, and comprehensive FDI data set.

The list of important indicators needed for the ESCWA region includes: (a) FDI components; (b) payments of royalties and licence fees by affiliates firms and countries (intra-firm); (c) (better) data on the sectoral and industrial distribution of FDI inflows; (d) detailed intraregional FDI activity (flows, firms, capital, employment); (e) listing of multinationals in the region (size, market, profits); (f) regular and updated data on FDI origins; (g) sources of financing of multinationals operating in the MENA region; (h) value-added of foreign affiliates (across sectors and aggregate levels); (i) employment creation by foreign affiliates; (j) export, import, and output activities made by foreign affiliates; (k) balance sheets of foreign affiliates; and (l) estimates of fiscal revenues (and loss) attributed to FDI promotion.

Source: UNCTAD, *World Investment Reports*, *World Investment Directory 1996, volume VI, West Asia* and the *OECD Benchmark Definition of Foreign Direct Investment*, third edition.

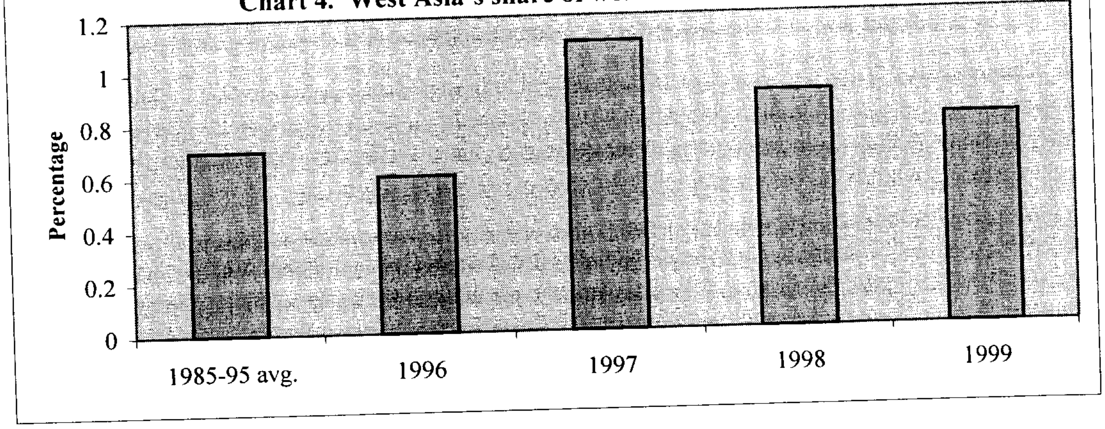
Chart 3. Developing countries' share of world FDI inflows



Source: UNCTAD, *World Investment Report 2000: Cross-border Mergers and Acquisitions and Development* (New York and Geneva, 2000).

A similar downward trend is observed for the West Asian region. The year 1997 was the peak year for this group of countries. The large increase is attributed to common factors shared by most developing countries as well as region-specific factors such as the peace treaty between Jordan and Israel. West Asia was affected—to a lesser degree—by the Asian crisis, but it is the increasing instability in the region and the lack of security following the deadlock in the peace process that had a larger role in the decline of FDI inflows during the latter part of the 1990s. However, the 1999 level of inflows remained greater than both the 1985-1995 annual average and the 1996 level.

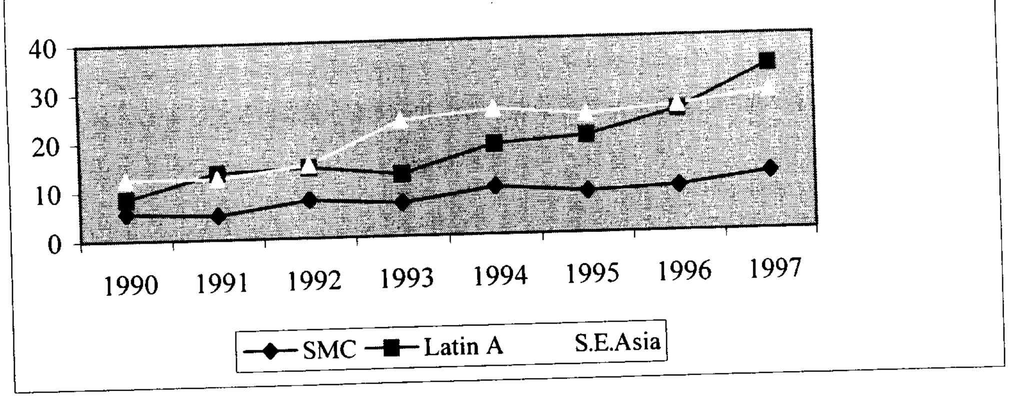
Chart 4. West Asia's share of world FDI inflows



Source: UNCTAD, *World Investment Report 2000*.

The southern Mediterranean region lags far behind Latin America and South-East Asia in terms of capital inflows (chart 5). The comparison factors in the size of economies (inflows per US$ 1,000 GDP), attempting to neutralize the size effect; nevertheless, Latin America continues to receive the largest amount, followed by the Asian region. This data series does not include the time period of the Asian crisis during which there was a drop in most forms of investment, including portfolio as well as foreign direct investments. The crisis had a much larger impact on Asian countries than on Mediterranean or Latin American countries.

Chart 5. FDI Inflows in per US$ 1,000 of GDP



Source: S. Alessandrini, "FDI in the MENA region," paper prepared for the third Mediterranean Development Forum, Cairo, 5-8 March 2000.

Note: SMC stands for southern Mediterranean countries and includes Algeria, Morocco, Tunisia, Egypt, Jordan, Lebanon, the Syrian Arab Republic, Malta, Cyprus, Israel and Turkey. Latin America includes the Caribbean, and S.E. Asia includes South, East and South-East Asia.

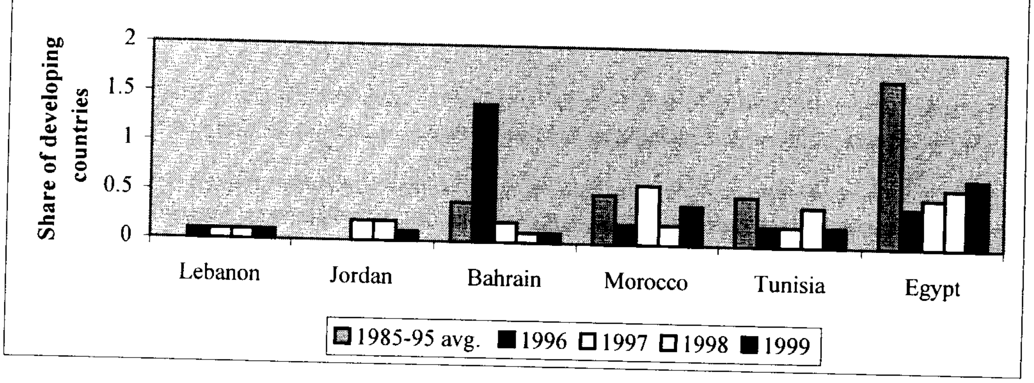
D. FDI INFLOWS: ESCWA AND THE ARAB REGION

1. *Share of selected countries in FDI inflows to developing countries*

A review of the three countries selected for this study finds that their share of FDI inflows, out of the developing countries' total, is insignificant. With the exception of one year for Bahrain (a statistical outlier), all three countries (Bahrain, Jordan and Lebanon) received less than 0.5 per cent of the developing countries' total throughout most of the past two decades. The absolute amount of FDI may have fluctuated from year to year, but the relative FDI "attractiveness" of the selected countries vis-à-vis other developing countries remains unsatisfactory. The annual average share of Bahrain for the period 1985-1995 was higher than the shares of Lebanon and Jordan, mainly because Bahrain, a Gulf country, was receiving resource-seeking FDI during that period and prior to the Gulf war.

The other three countries considered in the study (Egypt, Morocco and Tunisia) performed relatively better, with a share of FDI inflows of around 0.5 per cent. Egypt's share was as high as 1.7 per cent (annual average) during the period 1985-1995, compared with only 0.7 per cent in 1999.

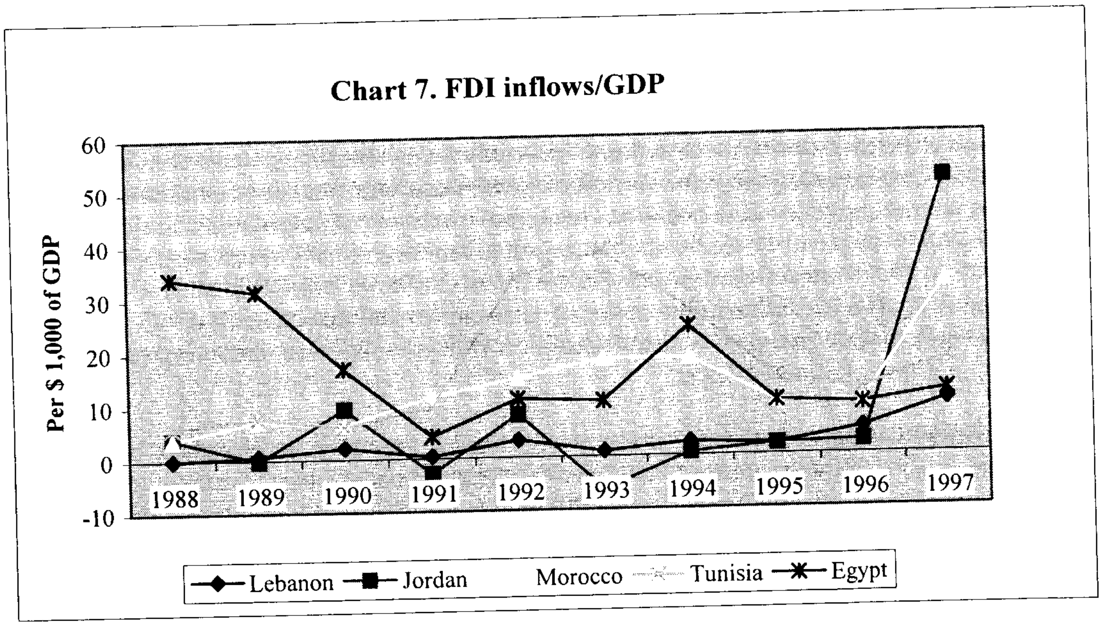
Chart 6. Share of selected countries in FDI inflows to developing countries



Source: UNCTAD, *World Investment Report 2000.*

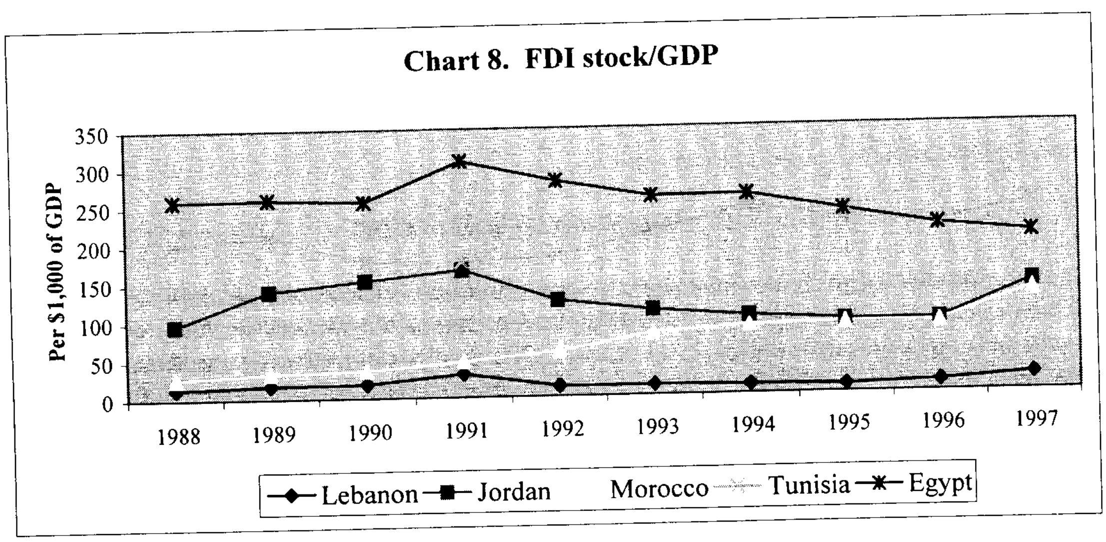
2. *Contribution of FDI to GDP*

Lebanon and Morocco have experienced the smallest fluctuations in FDI inflows since 1988, especially when the FDI/GDP ratio is considered. In the case of Lebanon, the level of FDI measured by whatever indicator (inflows, inflows/GDP, or stock/GDP) is small but steadily increasing. Egypt, Tunisia, and Jordan have unstable FDI paths. The Jordanian case is the most pertinent since not only are the fluctuations large, but the absolute amount of FDI is small and sometimes negative. This is not the case for Tunisia and Egypt, where inflows remained large and positive. The increase in inflows for Jordan between 1996 and 1997 is an exception to the path followed since 1988. This large and unexpected jump in inflows is mainly attributed to the peace treaty signed with Israel. Since 1999, Jordan has received larger FDI inflows as a result of privatization and trade liberalization with the United States.



Source: S. Alessandrini, "FDI in the MENA region," paper presented at the third Mediterranean Development Forum, Cairo, 5-8 March 2000.

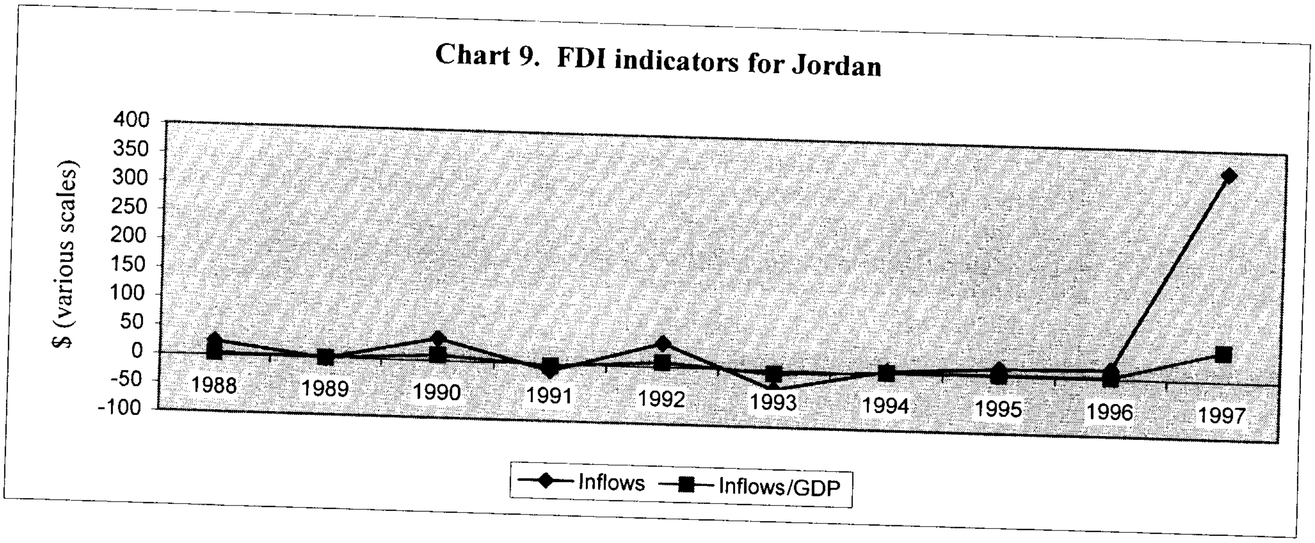
Compared with the late 1980s, Egypt's FDI indicators have followed a negative trend. In less than a decade, the inflow to GDP ratio has decreased significantly, reaching amounts comparable to the Lebanese ratio and scoring well below Morocco and Tunisia. In terms of FDI stock per GDP, Egypt is now behind Tunisia after a continuous decline that started in the early 1990s. If this trend continues, the Egyptian path will soon converge with that of Jordan and Morocco.



Source: S. Alessandrini, "FDI in the MENA region," paper presented at the third Mediterranean Development Forum, Cairo, 5-8 March 2000.

It should be noted that the choice of indicators is important, as each one reflects the status of FDI—and the economy for that matter—but from a different perspective. In the case of Jordan, the country that witnessed the largest fluctuations, when comparing the total inflows to the inflow to GDP ratio, the two paths follow a parallel trend when the scales are normalized. The larger fluctuation for the FDI inflow variable is attributed to a scaling differential, where inflows are measured in millions of United States dollars, whereas the two other ratios are per $1,000.

To compare FDI inflows between countries where the economies vary greatly in size, it is preferable to consider the inflows/GDP ratio as a leading indicator.



Source: S. Alessandrini, "FDI in the MENA region," paper presented at the third Mediterranean Development Forum, Cairo, 5-8 March 2000.

Note: Inflows are in millions of US dollars; inflows/GDP are per US$ 1,000.

3. *Contribution of FDI to gross investment*

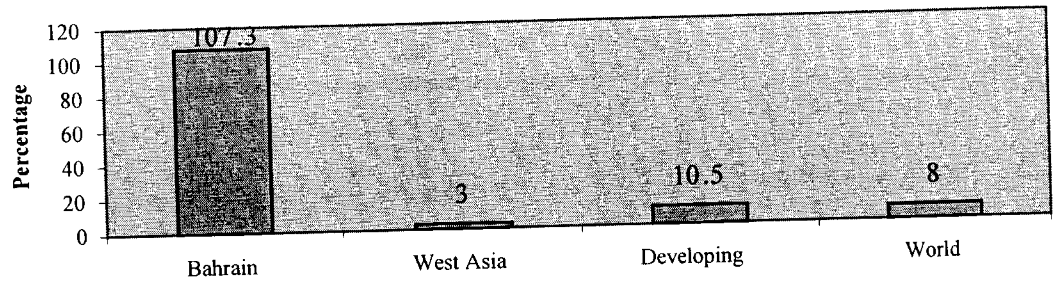
The share of FDI inflows in gross investment or gross fixed capital formation could reflect the level of "investment dependence" of an economy on foreign investors, or may also reflect the level of "attractiveness." Thus, if a low level for the FDI/gross investment ratio is observed, it can inferred that either the country is self-reliant or that the economy is not attractive to foreign investors. Similarly, a high ratio, as is the case for some North African countries, could reflect an attractive but also a totally dependent economy. The same can be said for Bahrain, where there is no domestic capital formation with a ratio exceeding100 per cent.

FDI flows into developing countries, and mostly the smallest or poorest countries, constitute a large share of gross fixed capital formation.[15] Compared with the world average of about 8 per cent, and the developed countries' average of less than 7 per cent, the Latin American average is about 13 per cent. The extreme ratio of 107 per cent for Bahrain (1996-1998 average) can be the result of a low level of overall investment or a relatively large level of FDI inflows, or both. In all cases, the FDI component is dominant, whether *a priori* or *ex post*. There is no clear-cut evidence that there is a positive relation between a high FDI share (as a percentage of total capital formation) and a crowding out effect (see table 4).

Policy makers have to bear in mind that, in some extreme cases and unless the environment for domestic as well as foreign investment is improved, FDI may crowd out domestic investments. This risk, however, is mitigated if the overall climate for investments, whether local or foreign, is improved and no preferential treatment is given to foreign investments.

[15] UNCTAD, *World Investment Report 2000*.

Chart 10. FDI Inflows as percentage of gross capital formation, 1996-1998 average



Source: UNCTAD, *World Investment Report 2000.*

TABLE 4. FDI/GROSS FIXED CAPITAL FORMATION

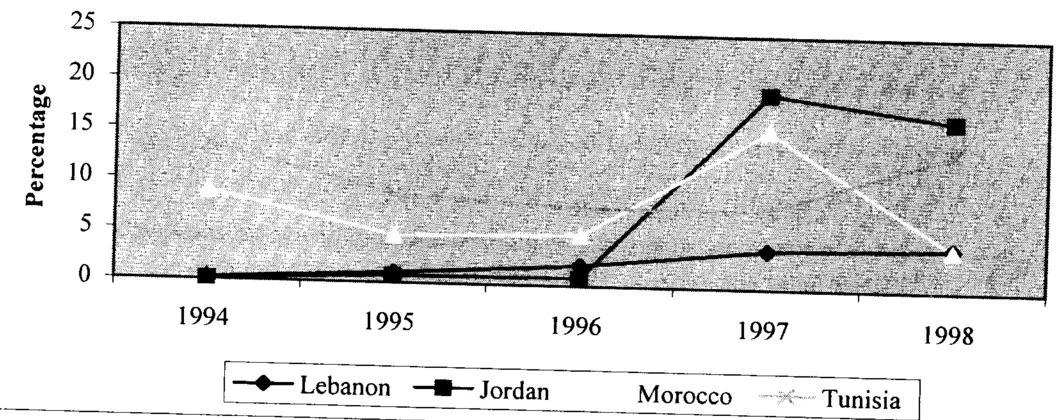
Country	1996-1998 simple average (percentage)	1988-1993 annual average (percentage)	Impact on domestic investment
Bolivia	48	11	
Chile	26	13	
Jamaica*	13	11	
Guatemala*	9	10	
Dominican Republic*	11	8	Negative
Sierra Leone	20	8	
Central African Republic*	8	-3	
Nigeria	24	30	
Zimbabwe	17	0	
Costa Rica	25	14	
Argentina	13	8	
Mexico	15	7	
Ecuador	18	9	
Colombia	20	8	
Peru	16	2	
Brazil*	12	2	Neutral
Tunisia	10	9	
Morocco*	8	5	
Malaysia	15	21	
Philippines	9	8	
Sri Lanka*	7	4	
Indonesia*	5	3	
China	14	6	
Côte d'Ivoire	23	8	
Ghana*	6	4	
Senegal*	10	3	Positive
Thailand	12	5	
Republic of Korea*	3	1	
Pakistan*	7	4	

Sources UNCTAD, *World Investment Report 2000;* and Manuel R. Agosin and Ricardo Mayer, *Foreign Investment in Developing Countries: Does It Crowd in Domestic Investment?* (UNCTAD/OSG/DP/146), UNCTAD Discussion Paper No. 146, February 2000, for the column in the table covering "impact on direct investment."

Note: * = the ratio is not among the 20 largest in the country's own region.

In a cross-country comparison, Lebanon has an extremely low ratio of FDI inflows (with respect to gross capital formation) which is, however. increasing at a slow and steady rate. The increase coincides with the launching of large projects such as the two mobile phone operators. In Jordan, the ratio increased in 1997 as a result of a major increase in the amount of inflows. The figures for Jordan—including 1990-1994 data—are volatile, agreeing with other indicators in describing the instability in the Jordanian FDI patterns. The North African countries in the sample showed a relatively high but moderate ratio, close to the average for developing countries. Chart 11 excludes Bahrain because the figures for the Gulf country are disproportionate to the rest of the selected countries, as shown above, and would skew the patterns hiding relevant data.

Chart 11. FDI inflows as a percent of capital formation in selected countries



Source: UNCTAD, *World Investment Report 2000.*

TABLE 5. FDI INFLOWS AS A PERCENTAGE OF CAPITAL FORMATION

Country	1994	1995	1996	1997	1998
Lebanon	0.2	1	2	3.8	4.2
Jordan	0.1	0.7	0.8	19.3	16.8
Morocco	8.8	4.7	5	15.6	4.1
Tunisia	13.4	8.7	7.7	7.8	13.6

Source: UNCTAD, *World Investment Report 2000.*

E. FACTORS AFFECTING FDI PERFORMANCE IN THE SELECTED MEMBER COUNTRIES

FDI performance has varied within ESCWA member countries. The variation is due not only to differences in strategy but also to different economic conditions.

TABLE 6. FDI INFLOWS TO SELECTED COUNTRIES
(*Millions of US dollars*)

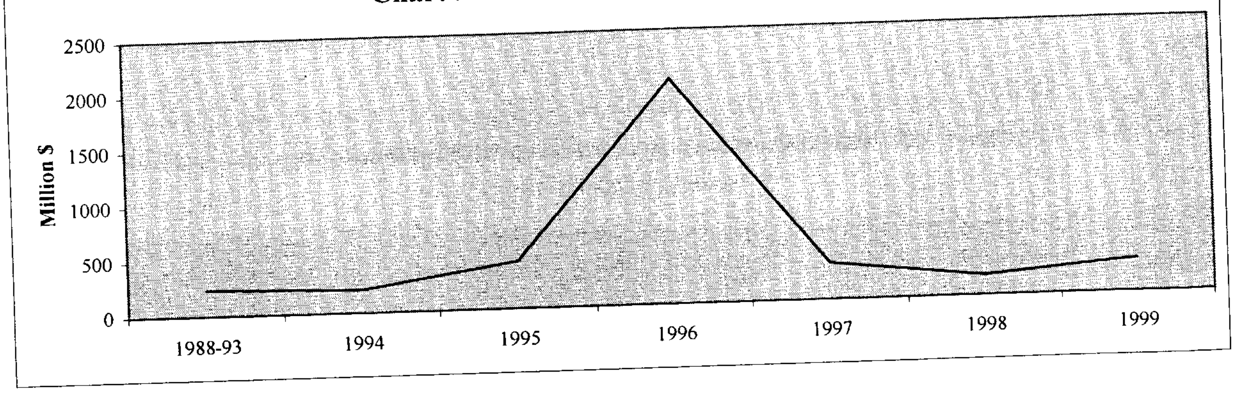
Country	1991	1992	1993	1994	1995	1996	1997	1998	1999
Lebanon	2	18	7	7	35	80	150	200	250
Jordan	-12	41	-34	3	13	16	361	310	151
Morocco	320	423	491	551	335	357	1079	329	847
Tunisia	125	526	562	566	378	351	366	670	368
Bahrain			239*	208	431	2048	329	181	300

Source: UNCTAD, *World Investment Report 2000.*

* This figure is the annual average for the period 1988-1993.

FDI inflows to Bahrain dropped in the early 1990s, and then began to increase in 1994. They peaked in 1996 after a fivefold increase, only to drop again in 1997 below 1995 levels. After 1998, inflows increased by almost 100 per cent, reaching US$ 300 million. The major drop in the early 1990s was, by and large, due to the Gulf war.

Chart 12. FDI Inflows in Bahrain



Source: UNCTAD, *World Investment Report 2000*.

Note: 1988-1993 figure is the annual average.

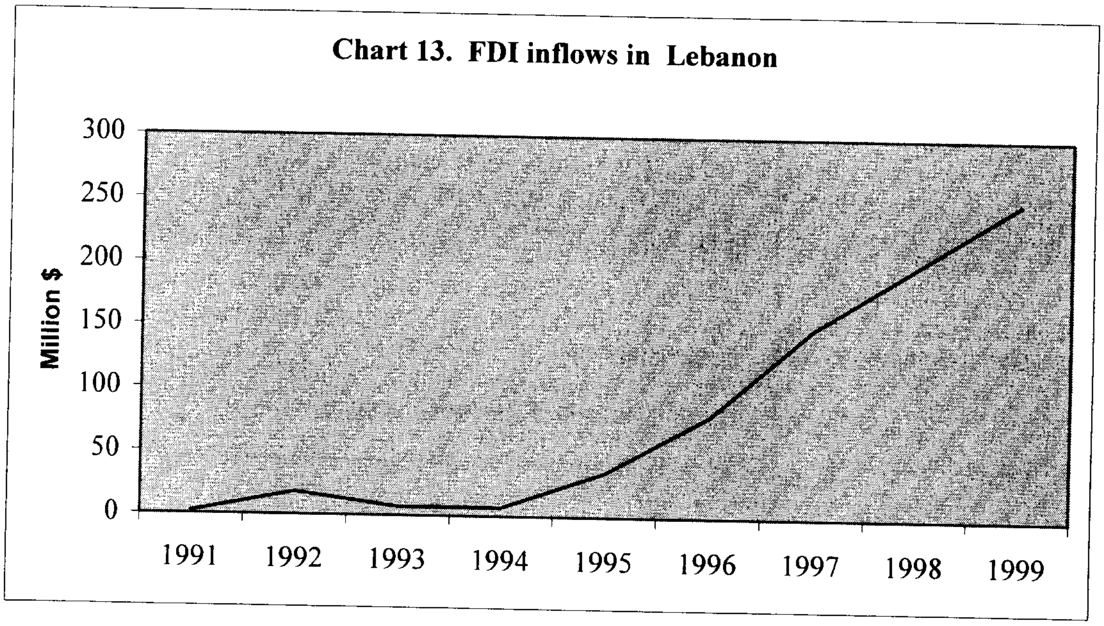
The table below looks into factors that might have played a role in influencing the level of FDI inflows. In some cases, the direct causality or simple correlation between FDI performance and the associated factors cannot be proven. This is the case for the copyright law: it cannot be determined whether this law, effective since 1993, had any lagged impact in the FDI increase of 1995-1996.

TABLE 7. BAHRAIN: FDI ENVIRONMENT

Period	Inflows	Associated factors
1990-1994	Decrease	• 1990/91 Gulf war • Copyright law (1993)
1994-1995	Stable to increasing	• Patent & Trademark Law (1995) • Joined WIPO (1995) • Post-war recovery • Bahrain Marketing Promotion Agency (1993) • (1993 • (1993) (1993) – promotion agency
1995-1996	Large Increase	• Member of WTO (1995)
1996-1998	Large drop	• GDP nominal growth of -2.6% • Drop in oil prices • Drop in oil-related exports • Outflow of portfolio investments
1998-1999	Increase	• Increase in oil prices

The factors possibly determining the path of FDI flows into Lebanon, Jordan, Morocco and Tunisia are listed in the tables below. The Lebanese case witnessed no major fluctuations compared with the inflows of Jordan, and most especially Morocco and Tunisia. Without underrating the importance of other variables, it is plausible to state that three major factors had a strong impact on the level of inflows, and they were: privatization, the Euro-Mediterranean Agreements between the EU members and some Middle Eastern countries, and peace with Israel (for Jordan). However, the available data do not shed light on the degree of importance of free zones and one-stop-shops (except for Tunisia) in attracting foreign investment into the selected countries.

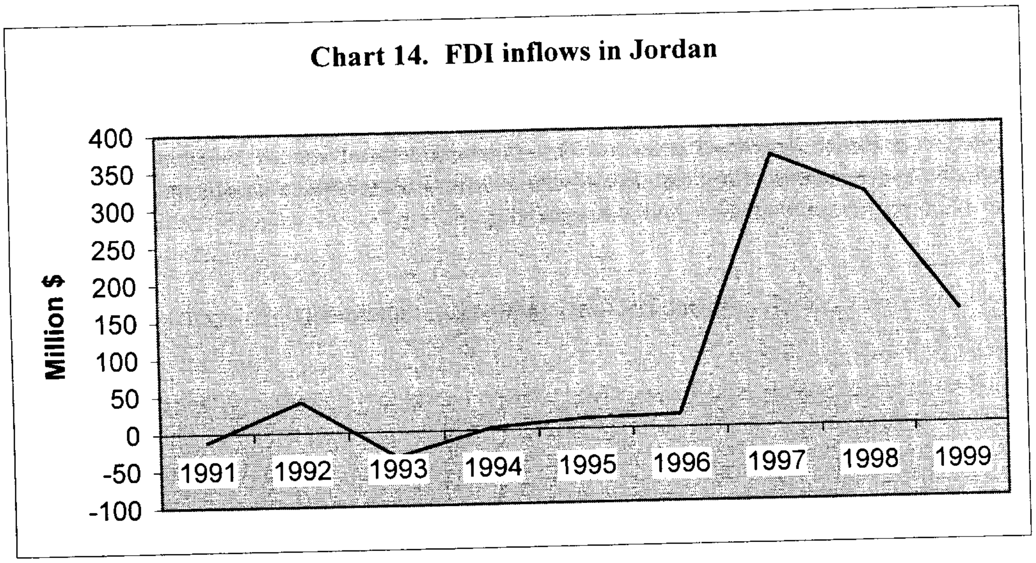
It is important to note that the date of the signature of a treaty or a free trade agreement is as important as the date of its entry into force. The actual signature serves as a signal for entrepreneurs interested in long-term investments. An additional observation in this regard concerns data. Major discrepancies in figures were observed between the 1999 and the 2000 UNCTAD *World Investment Report*, especially for Tunisia and Bahrain and, to a lesser degree, Lebanon. Moreover, the most recent numbers are always subject to revision, especially for countries that fail to adhere to a standardized accounting methodology or whose private firms are not transparent in their annual reporting.



Source: UNCTAD, *World Investment Report 2000*.

TABLE 8. LEBANON: FDI ENVIRONMENT

Period	Inflows	Associated factors
1991-93	Stable to increasing	• Post war recovery • GDP growth rates
1993-94	Stable	• Inflation reduced from 500% • Horizon 2000 Government reconstruction programme launched • IDAL established
1995-99	Large increase	• Inflation down to single digits • Privatization (Liban Poste) • Tax reduction in 1995 • Negotiations with the EU, the WTO • Establishment of mobile phone companies (joint venture with major foreign investors)

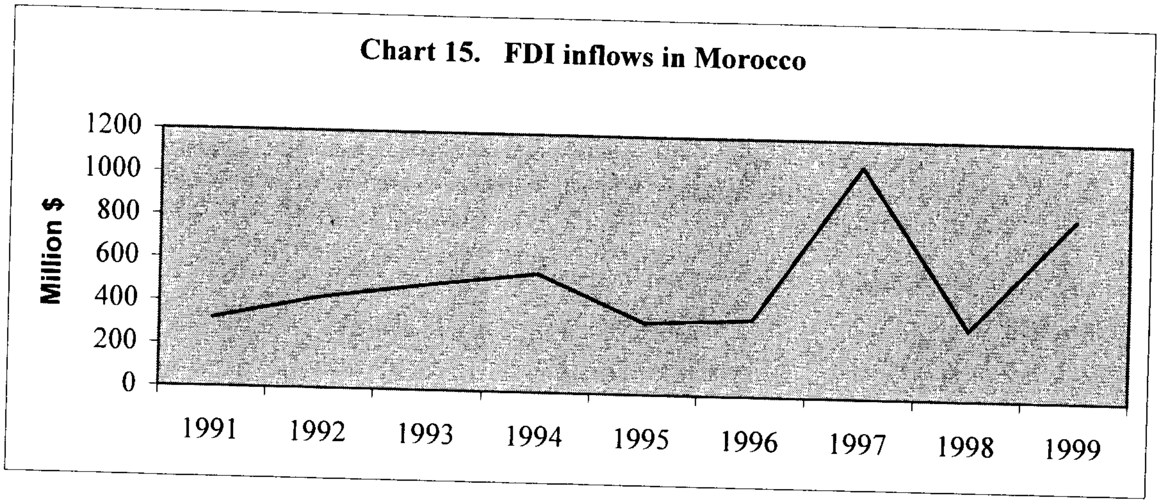


Source: UNCTAD, *World Investment Report 2000*.

TABLE 9. JORDAN: FDI ENVIRONMENT

Period	Inflows	Associated factors
1991-1992	Increase	• Investment by Jordanian returnees (Gulf war)
1992-1993	Decrease	• Post-Gulf war (Jordan isolated)
1993-1994	Increase	• Reintegration (post-isolation)
1994-1996	Stable to increase	• 1995 Investment Law (fiscal incentives, fast service) • 1995 Income Tax Law (pro-FDI) • Privatization (Jordan Holiday Co., \$11.3million) • Investment Promotion Corporation (1995)
1996-1997	Increase	• 1997 Investment Promotion Regulation (accords National Treatment) • The 1995 Tax Law effective 1996 • Peace treaty with Israel • 1997 Al Hussain Industrial Park (qualifying industrial zone)
1997	Peak	• Bilateral investment treaties with USA • Privatization (Arab Potash co., \$32.7million) • Euro-Mediterranean Agreement (1997)*
1997-1999	Large decrease	• Privatization (only \$5.1million) • Cessation of the peace process

Note: * = Date of signature.

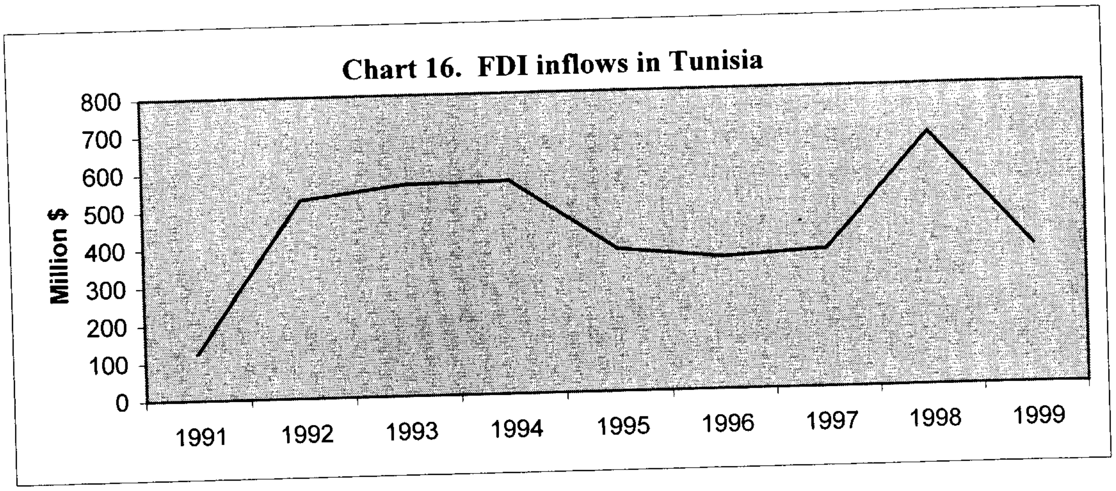


Source: UNCTAD, *World Investment Report 2000*.

TABLE 10. MOROCCO: FDI ENVIRONMENT

Period	Inflows	Associated factors
1991-1994	Increase	• 1990 Privatization Law • 992 Investment Law (liberalization) • Privatization of 48 out of 112 SOEs[a/] (1993 to 95)
1994-1995	Decrease	• Privatization process slows down
1995-1996	Stable	• Investment Charter Law (tax incentives) • 1995 Privatization Law • Euro-Mediterranean Agreement (1996)* • Trade agreement with United States • Member WTO (1995)
1996-1997 1997	Large increase Peak	• Euro-Mediterranean Agreement (1996)* • Move to privatize telecommunications • Large privatization programmes (in amount)
1997-1998	Large decrease	• 1998 privatization revenues relatively much smaller than the exceptional year of 1997, with relative decrease in inflow
1998-1999	Large Increase	• Privatization • Euro-Mediterranean Agreement entry in 2000 • 1999 Competition Law

Source: UNCTAD, *World Investment Report 2000*.
Note: * = Date of signature and date of entry into force set for the year 2000.
a/ State-operated enterprise.



Source: UNCTAD, *World Investment Report 2000.*

TABLE 11. TUNISIA: FDI ENVIRONMENT

Period	Inflows	Possible factors
1991-1992	Large increase	• 1991 Competition Law • Transparency ensured (competition law) • Some privatization (small in amount) • Some privatization of SOEs[a/]
1992-1994	Stable to increase	• 1993 Investment Incentive Law (fiscal measures)
1994-1995	Large decrease	• No privatization sale in 1994 • One privatized SOE[a/] sold to foreigners
1995-1996	Stable to decrease	• The Euro-Mediterranean Agreement (1995/96)* • Member WTO (1995) • Competition Law amended (1995) • Follow international accounting standards (1996) • FIPA[b/] establishment 1995 (promotion agency) • Effective one-stop-shop and promotional offices worldwide
1996-1998	Major increase	• Large privatization (in amounts) • 1998 was an exception, 1999 figures are comparable to 1997
1998-1999	Major decrease	• Questionable data, 1999 figures are estimates to be revised in 2001

Note: * = Signature date was in 1995 and the actual implementation started in 1996.

a/ State-operated enterprise.

b/ Foreign Investment Promotion Agency.

F. FACTORS AFFECTING INVESTMENT DECISIONS IN THE SELECTED MEMBER COUNTRIES AS VIEWED BY FOREIGN INVESTORS

A survey conducted on a sample of foreign direct investment (FDI) enterprises in three selected ESCWA member countries—Bahrain, Jordan and Lebanon—revealed the major reasons that incited foreign companies to invest in one of these countries. The sample consists of 50 enterprises in Jordan, 50 enterprises in Lebanon, and 35 enterprises in Bahrain. The sample was selected randomly from a list of FDI enterprises provided by concerned government agencies and investment promotion offices in the three countries. In the selection of the sample, however, due consideration was given to the three following criteria: (a) companies representing various sectors of the economy; (b) companies of different sizes; and (c) companies established at different periods: before 1990, from 1990 to 1995, and after 1996 (see annexes I and II to the present study). In this connection, it is important to note that the results of the survey cannot be fully extrapolated to the whole FDI sector; these results are more representative of trends than an accurate state of the sector.

The major reasons of interest indicated by foreign companies to invest in the host country vary among the three countries. Foreign companies seem to be interested to different degrees in: the domestic market; access to regional and world markets; the availability of local skill; low-cost labour; the favourable incentive system; the existence of an entrepreneurial culture; and a competent local partner.

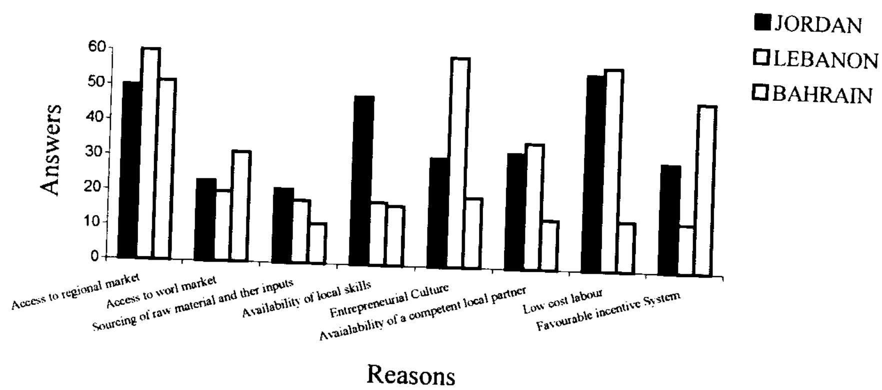
Table 12 shows the percentage of companies in the sample that indicated their major reasons for investing in Bahrain, Jordan and Lebanon.

TABLE 12. MAJOR REASONS FOR THE FOREIGN PARTNER TO INVEST IN BAHRAIN, JORDAN AND LEBANON
(*Percentage*)

Major reasons	Jordan	Lebanon	Bahrain
Size of domestic market	42	28	22.9
Access to regional market	50	60	51.4
Access to world market	23	20	31.4
Sourcing of raw materials and other inputs	21	18	11.4
Availability of local skills	48	18	17.1
Low-cost labour	56	58	14.3
Existence of a technological base	35	22	17.1
Favourable incentive system (tariffs and taxes)	31	14	48.6
Existence of an entrepreneurial culture	31	60	20
Availability of a competent local partner	33	36	14.3
Other	42	30	17.1

Source: Results of the ESCWA survey conducted for this study.

Chart 17. Major reasons for a foreign partner to invest in Bahrain, Jordan and Lebanon



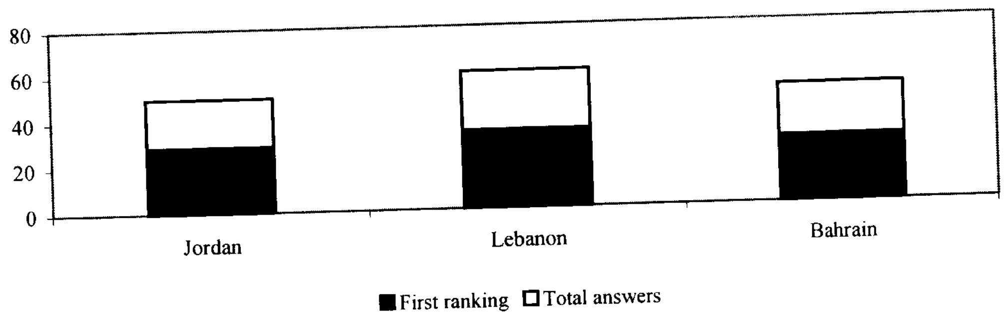
1. *Access to regional market*

Access to the regional market is considered one of the most important reasons for the inflow of FDI in Bahrain, Jordan and Lebanon. Sixty per cent of the sample in Lebanon, and half of the sample in both Jordan and Bahrain, have cited this factor as the major reason to invest.

> The percentage of interviewed enterprises that considers access to the regional market as one of the major reasons for investing in the host country varies in each of the three countries as follows:
>
> 50 per cent in Jordan
> 60 per cent in Lebanon
> 51.4 per cent in Bahrain.

Many companies have established branches in Jordan to cater to the needs of the Iraqi market, though exports to Iraq have dropped since the imposition of the economic sanctions. Jordan is attracting FDI in service activities, mainly tourism and hotels. Some foreign companies indicated their preference for Lebanon rather than for any other countries in the region, as Lebanon is considered the most "adequate" country to live and operate in at the regional level. Many foreign companies stated their intention to establish a regional office in Lebanon, especially if a free zone is created in the Levant area. Foreign investors consider Bahrain as a gateway to the Gulf Cooperation Council (GCC) market, and in particular to Saudi Arabia. Bahrain's geographical location makes it possible to access the GCC (particularly the Saudi Arabian market) and the Middle East market. In this connection, it should be noted that the Government of Bahrain encourages FDI, especially in export-oriented activities, and in those that do not compete with national enterprises. It is also important to note that more than half of the companies that selected "access to the regional market" as one of the most important reasons for investing placed this reason in the first- ranking category.

Chart 18. Access to the regional market
(Percentage of the sample)



2. *Labour cost*

Low-labour cost is cited by foreign companies as the most important reason for investing in Jordan, as skilled and unskilled labour in Jordan have relatively low wages in comparison with Bahrain and other ESCWA member countries. While Lebanese labour is relatively expensive, foreign investors are attracted by the availability of low-wage labour from the Syrian Arab Republic in Lebanon, particularly in construction and contracting work. In Bahrain, since labour costs are high, the factor of low-cost labour is cited by only 14 per cent of the sample.

> The percentage of interviewed enterprises that considers low-labour costs as one of the major reasons for investing in the host country varies in each of the three countries as follows:
>
> 56 per cent in Jordan
> 58 per cent in Lebanon
> 14.3 per cent in Bahrain.

3. *Availability of local skills*

The availability of local skills is a major reason for foreign companies to invest in Jordan, but it is considered of secondary importance in both Bahrain and Lebanon, though the skills are available in Lebanon. Jordan has a high rate of unemployment, and enjoys the availability of skilled labour (including engineers and specialists in information technology). The educated workforce in Jordan constitutes one of the major factors in attracting FDI, though enhancing training and re-education in promising sectors (such as information technology, vocational training and management) is needed if Jordan is to improve its competitive advantage vis-à-vis other countries in the region.

The percentage of interviewed enterprises that considers the availability of local skills as one of the major reasons for investing in the host country varies in each of the three countries as follows:

48 per cent in Jordan
18 per cent in Lebanon
17 per cent in Bahrain.

4. *Size of the domestic market*

Foreign companies seem more interested by the size of the domestic market in Jordan than in Bahrain or Lebanon. Although the size of the market in Jordan is small, in the 1990s Jordan had the potential for market growth in import-substitution goods and services. In this connection, it should be noted that with trade liberalization and the reduction in the effective protection of the country's domestic production, foreign companies would be reluctant to invest in Jordan to produce for the local market. Trade and production under licensing agreements and franchises will thus replace inflows of foreign investment.

The percentage of interviewed enterprises that considers the size of the domestic market as one of the major reasons for investing in the host country varies in each of the three countries as follows:

42 per cent in Jordan
28 per cent in Lebanon
23 per cent in Bahrain.

5. *Access to the world market and sourcing of raw materials*

Access to the world market and sources of raw materials and other inputs has not been cited as a major reason for investment, though this is factor is more pronounced in Bahrain than in Lebanon and Jordan.

The smallness of the sample does not make it possible to capture the impact of a few large companies that are operating in major sectors in Bahrain and Jordan, and that contribute significantly to total country exports. In Jordan, the mining sector and the Qualifying Industrial Zones have attracted major TNCs. Sourcing constitutes a major factor that is attracting FDI, particularly since foreign investors can now have ownership of 100 per cent of the capital in the mining sector. Joint ventures are being established with United States, Japanese and Indian companies to produce chemicals and fertilizers to exploit the Dead Sea minerals. The creation of the Qualifying Industrial Zones in Jordan constitutes an important reason for several foreign companies to establish themselves in this zone with the aim of taking advantage of the free access to the United States market.

In Bahrain, several foreign companies have entered into joint ventures in the aluminium-based industries and in the garment sector to take advantage of the free quota the Bahraini garment sector enjoys in the United States market.

Lebanon has very few natural resources, and sourcing of raw materials and other inputs by foreign companies is very limited. Nevertheless, raw materials and other inputs are sometimes available in the Lebanese market through imports that are facilitated from neighbouring countries.

The percentage of interviewed enterprises that considers sourcing of raw materials and other inputs as one of the major reasons for investing in the host country varies in each of the three countries as follows:

21 per cent in Jordan
18 per cent in Lebanon
11.4 per cent in Bahrain

---

23 per cent in Jordan
20 per cent in Lebanon
and 31.4 per cent in Bahrain:

consider that the access to the world market is one of the main reasons to invest in the host country.

6. *Favourable incentive system*

Around half of the sample in Bahrain indicated that the favourable incentive system is a major reason for investing in this country. In Jordan and Lebanon, the incentive system was not as important to the foreign investors as it was in Bahrain.

The percentage of interviewed enterprises that considers the favourable incentive system as one of the major reasons for investing in the host country varies in each of the three countries as follows:

31 per cent in Jordan
14 per cent in Lebanon
48.6 per cent in Bahrain.

7. *Existence of an entrepreneurial culture and of a competent local partner*

Unlike Jordan and Bahrain, Lebanon enjoys the existence of an entrepreneurial culture, which has been considered among the most important reasons attracting foreign investment. This is coupled with the existence of competent local partners, who have better communication skills than in other countries. Several foreign companies have successful experiences with their local partners. Many local partners are Lebanese expatriates who encouraged investment in Lebanon and formed partnerships with foreign investors.

The percentage of interviewed enterprises that considers the existence of an entrepreneurial culture and the availability of a competent local partner as major reasons for investing in the host country varies in each of the three countries as follows:

Entrepreneurial culture	Competent local partner
31 per cent in Jordan	33 per cent in Jordan
60 per cent in Lebanon	36 per cent in Lebanon
20 per cent in Bahrain	14.3 per cent in Bahrain

In Jordan, Jordanian entrepreneurs are generally reluctant to enter into joint ventures with foreign investors, since this would entail providing information on their performance, and sharing ownership authority.

8. *Other reasons of interest to foreign investors*

Other less important reasons are the availability of a technological base, the absence of discrimination against foreigners, and the fact that Jordan and Bahrain in particular are considered stable countries and safe for investment.

> The percentage of interviewed enterprises that consider the existence of a technological base as one of the major reasons for investing in the host country varies in each of the three countries as follows:
>
> 35 per cent in Jordan
> 22 per cent in Lebanon
> 17.1 per cent in Bahrain.

G. CONCENTRATION OF FDI IN SELECTED ESCWA MEMBER COUNTRIES

Data on FDI listed by company and sector of operation are very poor. Few Governments have up-to-date lists of foreign investors. International sources, such as the most recent World Investment Directory for West Asia (1996), suffer from the same problems. In spite of all its shortcomings, this information is still useful to the extent that investment relations between countries, most notably FDI patterns, do not drastically change from year to year. This information can also be cross-checked against what is already identified as a country's comparative advantage.

Bahrain has developed as a financial centre in the Gulf region and has also attracted investments in heavy industry that rely on cheap sources of energy. The vast majority of foreign companies investing in Bahrain are based in Saudi Arabia, Bahrain's closest trading partner. Foreign investment is concentrated in metals and finance. As the Gulf economies diversify away from energy, Bahrain's foreign investor roster is also likely to become more diversified.

TABLE 13. LARGEST FOREIGN AFFILIATES IN BAHRAIN, 1993

Company	Home economy	Industry
Arab Aluminum Bahrain (ALBA)	Saudi Arabia	Metals
Arab Shipbuilding & Repairs Yard	Saudi Arabia, United Arab Emirates, Kuwait, Qatar, Libyan Arab Jamahiriya	Other manufacturing
Midal Cables	Saudi Arabia	Metals
Bahrain National Gas	United States	Petroleum
Mitsui and co.	Japan	Distributive trade
Bahrain telecommunications	United Kingdom	Communication
Bahrain Maritime & Mercantile Int'l	United States	Transport
Arab Banking Corporation	Kuwait, United Arab Emirates, Libyan Arab Jamahiriya	Finance
Gulf International Bank	Gulf Cooperation Council	Finance
Bank of Bahrain and Kuwait	Kuwait	Finance
Faysal Islamic Bank of Bahrain	Saudi Arabia	Finance
Bahrain Middle East Bank	Kuwait	Finance
Investcorp Bank EC	Gulf Cooperation Council (ex. Bahrain)	Finance
Arab Asian Bank EC	Luxembourg	Finance
Arab Insurance Group	Kuwait, United Arab Emirates, Libyan Arab Jamahiriya	Insurance

Source: UNCTAD. *World Investment Directory for West Asia, volume VI*, 1996.

Jordan's FDI is harder to characterize. Jordan is a resource-poor country, except for phosphates and potash, two industries in which Arab investors are present. It also has a burgeoning banking sector that has already attracted foreign investors. More recently (in 1999-2000), however, Jordan has been able to diversify its list of foreign investors, with France leading the way after Lafarge's acquisition of Jordan

Cement Factories and France Telecom's acquisition of a controlling share in the Jordan Telecommunication Company.

TABLE 14. LARGEST FOREIGN AFFILIATES IN JORDAN, 1993

Company	Home economy	Industry
Jordan Petroleum Refinery	Saudi Arabia	Petroleum
Jordan Phosphate Mines	Kuwait	Mining
Arab Potash	Iraq, Libyan Arab Jamahiriya, Saudi Arabia, Kuwait	Mining
Sendan Equipment & Steel Works	Cyprus	Other manufacturing
Amman Marriott Hotel	United States	Other services
Consolidated Engineering	Lebanon	Construction
Foxboro Intercontinental	United States	Other services
Housing Bank	Kuwait, Qatar and Oman	Finance
Jordan National Bank	Lebanon and Kuwait	Finance
Jordan Kuwait Bank	Kuwait	Finance
Arab Jordan Investment Bank	Saudi Arabia	Finance
ANZ Grindlays Bank	United Kingdom	Finance

Source: *World Investment Directory for West Asia, volume VI*, 1996.

More recent data on foreign investors in Jordan show the rapid increase of privatization-related FDI. The Government of Jordan sold 40 per cent of the shares of the Jordan Telecommunication Company to a consortium made up of France Telecom and the Arab Bank. The sale generated US$ 504 million in revenues for the Government. Other major privatization projects that have attracted FDI are the above-mentioned sale of the Jordan Cement Factories, and the Aqaba Rail Corporation BOT contract that was awarded to a consortium headed by Raytheon (United States). Jordan is undergoing a major restructuring programme of its State-owned enterprises, including Royal Jordanian Airlines, the electricity sector and other major enterprises, most of which have already been incorporated (including the Public Transport Corporation and the Aqaba Railway Corporation), and shares have been partially sold on the Amman Stock Market. It is noteworthy that, of all the companies in Jordan with significant foreign investments, only one is from an Arab country and the vast majority are from Europe (table 15).

TABLE 15. FOREIGN AFFILIATES IN JORDAN ESTABLISHED AFTER THE MID-1990S

Company name	Nationality	Year of entry
Ibrahim Abunia Sons	Saudi Arabia	1996
Ata for Engineering & Commerce	Turkey	1996
Schneider Electric A	France	1996
SES for Hotels	Denmark	1997
Alestom for Electric Capacity Co.	Germany	1997
Di Nepou Construction	Japan	1997
Motorola Anco	United States	1997
Meridian Hotels	France	1998
Hyundai	Republic of Korea	1998
Atela Dogan for construction	Turkey	1999
Crandi Lavori Venco Seet	Italy	1999
Sumitomo Construction company	Japan	1999

Source: Ministry of Industry and Trade, Jordan.

With respect to Lebanon, and for the early 1990s, the majority of foreign investments originated in Europe, most notably France. More recent data show, however, that a number of Kuwaiti firms entered the Lebanese food service sector in the mid-to-late 1990s (including Americana and El-Chayeh), introducing food and coffee chains as well as clothing and beauty stores (such as Starbucks, Kentucky Fried Chicken, Mothercare and Bodyshop).

The largest foreign investments to date undoubtedly took place in mobile telephony, with two Lebanese-European consortias (Finland and France) setting up two networks for cellular phones. A Canadian consortium also ventured into the postal service and became the first foreign enterprise that entered the Lebanese market as a result of a privatization project. Moreover and immediately following the enactment of a law protecting intellectual property in 1999, Microsoft Corporation opened its regional office in Lebanon, becoming the first computer giant to enter the local market.

TABLE 16. LARGEST FOREIGN AFFILIATES IN LEBANON, 1993

Company	Home economy	Industry
Liban Cables	France	Electrical equipment
Steel & Aluminium Construction	France and Germany	Metal
Spinney's Lebanon	United Kingdom	Distributive trade
Al Hamra Engineering	Kuwait	Construction
AT&T	United States	Distributive trade
Triad Condas International	Luxembourg	Construction
Banque Libano-Française	France	Finance
Société Générale Libano-Européene de Banque	France	Finance
Fransabank	France	Finance
Byblos Bank	Luxembourg	Finance
Syrian Lebanese Commercial Bank	Syrian Arab Republic	Finance
Beirut Riyad Bank	Saudi Arabia	Finance
Banque Misr Liban	Egypt	Finance

Source: *World Investment Directory for West Asia, volume VI*, 1996.

H. POTENTIAL FOREIGN INVESTORS

It is important to identify who the potential investors in the ESCWA region might be. This exercise is useful for two reasons. The first is to examine whether the efforts to attract FDI will be fruitful. The second is to fine-tune the investment promotion strategy in order to give priority to those investors who are most likely to invest in the region.

1. *Multinational corporations in the ESCWA region*

Over 500,000 foreign affiliates are in operation worldwide, established by about 60,000 parent companies. Foreign affiliates are by no means corporate giants, the type that might not be interested in investing in the relatively small West Asian market. In fact, the number of new small and medium-size multinationals is significant. In 1996, about four fifths of Swedish multinational corporations were small and medium-size enterprises, while in Italy small and medium-size enterprises accounted for three fifths of all multinationals.[16]

The number of parent companies based in Oman, Saudi Arabia, and Turkey—countries with available data—is relatively small, with a share of 5 per cent of the developing countries' total. As for the number of foreign affiliates located in these three countries, they do not exceed 1 per cent of the developing countries' total.[17] The United Arab Emirates, Turkey and Saudi Arabia can be considered among the most attractive hosts for multinational corporations in the region. Turkey is ranked 40th in growth competitiveness by the World Economic Forum (2000), ahead of China, Egypt and Mexico. Saudi Arabia's International Country Risk Guide (ICRG)[18] rating in 1998 was 73, compared with 70 for the MENA average.[19] Saudi Arabia is

[16] *World Investment Report 2000*.

[17] Ibid.

[18] The higher the ICRG index, the lower the risk in the country. The index is a composite of 24 components grouped into three main categories: political, financial, and economic. Each component has a scale that varies from 0 to 6, and in some cases the range is smaller.

[19] World Economic Forum (2000), Global Competitiveness Reports for 1995-2000 (WEF web site).

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also a country rich in natural resources, including oil and gold. The relatively weak performance of FDI in the most attractive economies in the region (the United Arab Emirates, Saudi Arabia and Turkey) raises questions about the possibility of multinational corporations locating in the less attractive economies of the region.

The insignificant presence of multinational corporations in West Asia makes it harder for countries such as Bahrain, Jordan and Lebanon to enjoy a spillover or an expansion effect from the multinationals operating in the region. The problem thus does not lie in specific countries but in the region at large, a harsh fact that calls for a cross-national action plan that would render the area more attractive to foreign investors.

TABLE 17. MULTINATIONAL CORPORATIONS OPERATING IN THE DEVELOPING WORLD

Region/country	Year	Parent corporations based in economy	Foreign affiliates located in economy
West Asia*		449	1 948
Oman	1995	92	351
Saudi Arabia	1989	N/A	1 461
Turkey	1995	357	136
Developing		9 246	238 906
Africa		43	429
Latin America		2 594	26 577
Developed		49 806	94 623
World		59 902	509 239

Source: UNCTAD, *World Investment Report 1999.*

* In this table, "West Asia" refers only to the three countries listed in the table: Oman, Saudi Arabia and Turkey.

2. *Origin of FDI*

None of the 100 top multinational corporations in the world considers the Middle East or Northern Africa as its home economy. For this reason, policy makers in this region should not rely on, or expect, significant intraregional FDI. In 1998, and according to the 1999 UNCTAD World Investment Report, only 8 out of the 100 largest multinational corporations originated outside the European Union, North America, and Japan. Countries such as France, the United Kingdom and the United States. are, by and large, the main hosts of multinational corporations. These countries are also the region's major source of FDI and are its primary trading partners.

TABLE 18. WORLD'S LARGEST NON-FINANCIAL MULTINATIONAL CORPORATIONS RANKED BY FOREIGN ASSETS, 1997

Rank	Corporation	Country	Industry
1	General Electric	United States	Electronics
2	Ford Motor Company	United States	Automotive
3	Royal Dutch/Shell Group	United Kingdom/Netherlands	Petroleum
9	Nestle	Switzerland	Food and beverages
15	Bayer	Germany	Chemicals
16	Elf Aquitaine	France	Petroleum
19	Siemens	Germany	Electronics
26	Alcatel Alsthom	France	Electronics
34	Cable and Wireless	United Kingdom	Telecommunication

Source: UNCTAD, *World Investment Report 1999.*

Table 18 selects a number of the largest multinational corporations operating worldwide. Out of the top 100, the European Union had, in 1997, a share of 45 entries, the United States 27, and Japan 17. For the same year, the leading sector was chemicals and pharmaceuticals (21 per cent) followed by electronics and electrical equipment (18 per cent), automotive (14 per cent), and petroleum refining (13 per cent). With the exception of the automotive sector, these sectors are relatively active in Bahrain, Jordan and Lebanon. Therefore, with a proper investment environment, more FDI can be expected to flow into the respective sectors.

TABLE 19. VARIOUS SECTORAL INDICATORS: LEBANON AND JORDAN, 1998

Activity in:	Lebanon	Jordan
	43 new industries	
Chemicals	$87 million[a/]	
Pharmaceuticals	$40 million[a/]	$143 million[b/]
Petroleum refining	A	3,237 tons[c/]
Electronics/electrical equipment	$74 million[d/]	B

Source: for Jordan, the Central Bank of Jordan; for Lebanon, Banque Audi and the Administration Centrale de la Statistique.

a/ 1998 exports, 12 per cent of total exports (chemicals), 6 per cent for pharmaceuticals.
b/ 1998 exports of pharmaceutical products that made up 10 per cent of total exports.
c/ 1998 output of petroleum products, second largest product in the nation.
d/ 1998 exports of electrical products, 10 per cent of total exports.

Notes: A = There are two major Lebanese refineries with pipelines from the Gulf.
B = See table 15 on foreign affiliates in Jordan.

The ESCWA region's strategy for attracting FDI must rest on a thorough knowledge of the strengths and weaknesses of the region. The main weakness is that the region has not attracted much interest from multinational corporations. On the positive side of the ledger, however, the region has very close trading ties with the host countries of the largest number of multinational corporations (the United States and European countries) and is therefore "on the radar screen" of multinational investors. The presence of some multinational corporations already in the region could also be used as part of a strategy for promoting FDI. Multinational corporations tend to develop a greater comfort level with a particular country the greater the pre-existing level of foreign investment. To use a concrete example, if French companies are already present in strength on the Lebanese market, it will be easier to attract additional French companies to Lebanon, assuming that the overall experience of the existing multinational corporations is positive. Investment promotion agencies will also get a bigger return on their investment if they focus on those countries with which there is a high level of trade. The biggest challenge, however, is to attract the "floating investor," the investor who is not yet committed to investing in the ESCWA region and who has not yet made an effort to invest in it. In either case, investors will first assess the environment for doing business before they make a decision as to whether or not to invest.

Box 2. FDI and international practices of small economies: Ireland, Mauritius and Bolivia

Government policies in 1999 confirmed and strengthened the trend towards liberalization and promotion of FDI. Restrictions on ownership of land and real estate, employment of foreigners, and foreign exchange controls were reduced or removed in a large number of countries. Legal guarantees and the protection of intellectual property rights were also strengthened. In addition, numerous fiscal incentives were initiated to promote investment. According to UNCTAD, the main types of changes in FDI laws for 1999 were:

(a) Liberal entry and operational conditions (performance requirements);
(b) Sectoral liberalization;
(c) General and sectoral promotion including incentives and free zone regulations.

The following three countries are examples of successful promotion of FDI.

1. *Ireland*

Ireland's economic performance was exceptional for most of the 1990s, when real GDP growth averaged over 9 per cent per year between 1996 and 2000. No other OECD country has been able to match that record. The structural factors behind this growth include a young and highly educated population. About 40 per cent of the 3.7 million Irish people are under 25 years old, and 60 per cent of school-leavers go on to tertiary education. In addition, Ireland's labour costs are among the lowest in developed countries. Ireland, as a result of its FDI strategy, was able to increase the level of inflows from US$ 787 million (1988-1993 annual average) to US$ 18,322 million in 1999, an increase of about 2,200 per cent.

Box 2 *(continued)*

The FDI strategy initiated in the 1980s had three components:

(a) Selecting leading, high value-added industry such as electronics, computer software, and financial services;
(b) Creating specialized industrial clusters in designated locations;
(c) Promoting links to domestic firms.

The Industrial Development Agency of Ireland played a central role in coordinating efforts between local and national authorities and in developing incentives and other promotional measures. Among the fiscal incentives, grants were offered for the establishment of R and D facilities and for financing new machinery and equipment. In order to generate clusters of new activity, the Agency introduced special industrial zones. The Agency also approached and attracted firms that were leaders in their sectors to invest in Ireland, a policy aimed at persuading other firms to follow suit.

Ireland was also committed to increasing the level of education. The Government offered employment and training grants but also worked on an overall plan to revamp the country's education sector, a strategic choice that proved very successful.

2. *Mauritius*

Mauritius is one of Africa's most dynamic economies. FDI inflows peaked in the early 1990s and investments were attracted to labour-intensive manufacturing industries, especially garments and textiles. The success was the result of the following:

(a) The establishment of an export-processing zone;
(b) Implementation of an export-oriented development strategy;
(c) Preferential access to EU and United States markets;
(d) Skilled and low-cost labour force;
(e) Efficient physical infrastructure;
(f) Sound legal system for dispute of settlements.

Mauritius had to address three main challenges: rising labour costs (relative to other African economies); limited technological infrastructure; and the threat of losing preferential access to Western countries. In response, Mauritius redirected its FDI regime and promotion strategy to focus on the following measures:

(a) Initiation of a skills development programme;
(b) Reprioritizing of education and skill-building policies;
(c) Establishment of a National Productivity and Competitiveness Council;
(d) Various technological upgrading initiatives;
(e) Fast-track approval procedure system;
(f) Multi-entry visas for foreign investors;
(g) Other steps to reduce delays.

Mauritius was successful in increasing FDI inflows from the US$ 25 million annual average for 1988-1993 to US$ 55 million in 1997 and US$ 49 million in 1999. As a percentage of GDP, inflows increased from 6.2 per cent in 1990 to 8.5 per cent in 1998.

3. *Bolivia*

Bolivia, a nation of 8 million people, is one of the poorest countries in Latin America with a GDP estimated at $8.1 billion for 1999. The country is, however, well endowed with mineral and hydrocarbon resources, an attraction to natural resource FDI-seekers.

After the 1985 stabilization and adjustment programme which yielded modest growth rates in the early 1990s, Bolivia launched a number of structural reform policies that encompassed the financial sector, public enterprise, trade and registration procedures, regulatory and legal systems, and public financial and economic management. Among the important reform measures that ultimately had a positive impact on FDI flows, the Government of Bolivia initiated the following:

Box 2 (*continued*)

(a) Comprehensive privatization law (1992)—not including State mining and hydrocarbon enterprises—60 State-owned enterprises sold or liquidated by 1995;

(b) Establishment in 1995 of a fund to restructure and capitalize banks;

(c) Attraction of strategic partners after the 1994 Framework Law;

(d) The establishment of a broad regulatory framework with the 1994 System of Sectoral Regulation Law;

(e) Enactment of several sectoral regulatory laws;

(f) Amendment in 1994 of the tax system that provided a uniform and stable tax environment;

(g) Administrative decentralization following the Popular Participation Law (1994) and the Decentralization Law (1995);

(h) Elimination of sugar import licensing requirement in 1992;

(i) Abolishment of all quantitative restrictions on imports;

(j) Keeping tariff levels low and fairly uniform.

In the 1990s, Bolivia witnessed a surge in its FDI inflows from US$ 130 million in 1994 to $1.016 billion in 1999. Similarly, inflows per GDP increased from 23.3 per cent in 1995 to 44.6 per cent in 1998.

Sources: For Ireland: UNCTAD, *World Investment Report 1998: Trends and Determinants; World Investment Report 2000: Cross-border Mergers and Acquisitions and Development;* and the Industrial Development Agency of Ireland (www.idaireland.com); for Mauritius: UNCTAD, *World Investment Report,* 1998 and 2000; and for Bolivia: World Bank, *World Development Indicators,* and UNCTAD, *World Investment Report 2000.*

IV. THE LEGAL AND INSTITUTIONAL ENVIRONMENT FOR FOREIGN DIRECT INVESTMENT

A. INVESTMENT LAWS AND TREATMENT OF FDI IN THE SELECTED MEMBER COUNTRIES

1. *Incentive policy*

Most ESCWA member countries offer one form or another of incentives to encourage FDI in the region. Many of them offer fiscal incentives including tax holidays. For example, Egypt offers foreign investors a five-year corporate tax holiday that could be extended to another five years under most circumstances. An additional two years are granted if over 60 per cent local machinery is used. Projects located in the new industrial zones, new urban communities and remote areas have a 10-year tax holiday subject to five-year extension.

Foreign projects operating in Jordan are offered reductions in income taxes ranging from 25 to 75 per cent based on their location, provided the projects are carried out in the following sectors: industry, agriculture, hotels, leisure and recreational compounds, hospitals, maritime transport, and railways. Fixed assets are exempted from customs duties. The business community in Jordan considers, however, that the incentive system is complicated and cumbersome to access.[20] It is not known, however, to what extent the varying incentives are determinant factors in attracting FDI in Jordan.

In Lebanon, the new Law for the Promotion of Investments (August 2001) provides specific incentives for projects established in the industrial, agriculture, tourism and information technology sectors. The incentives are mainly in the form of tax reductions and exemptions, the extent of which depends on the geographical area in which the project is established. Lebanon is divided, for the purposes of the investment law, into three areas. The investment law also gives greater flexibility for the employment of foreign labour. In Bahrain also, except for the income tax imposed on oil companies, no taxes are levied on corporate income. Imports of capital equipment, machinery and raw materials are also exempted from customs duties.

Surveys of the effects of incentives on foreign investors confirm that incentives play only a limited role in the decisions of transnational corporations as to where to locate their operations.[21] The ESCWA survey on a sample of foreign enterprises showed that, in Jordan and Lebanon, the incentive system is not as important to foreign investors as it is in Bahrain. Around half of the sample in Bahrain indicated that the favourable incentive system was a major reason for investing in the country; the percentages were 31 per cent in Jordan and 14 per cent in Lebanon.

In this respect, other variables besides tax incentives play a more important role. Among these variables are infrastructure development, size and growth rate of the market, the legal system and the FDI regulatory framework, macroeconomic and political stability, wage rates, and levels of human capital development. The studies also made clear that when fiscal and financial incentives were used to compensate for problems on these other dimensions, the response of FDI to increased incentives might be minimal, although the costs of these incentives may be high. The studies also revealed that fiscal and financial incentives have very limited effects, particularly on FDI oriented towards the domestic market. It becomes obvious that there is a need for some cooperative efforts at the regional level to avoid the use of excessive incentives. The ESCWA member countries would be well advised to take a pro-active approach in this area and to place limits on incentives, on a multilateral basis, in order to prevent distortions in the allocation of resources as well as a transfer of tax revenues from host country to transnational corporations and their home countries.[22]

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[20] Euro-Jordanian Business Service Team, "Jordan – Foreign Direct Investment: Opportunities and Constraints," draft report, Amman, January 2001.

[21] See UNCTAD, *Tax Incentives and Foreign Direct Investment. A Global Survey* (New York and Geneva, 2000).

[22] Antoine Basile, "Transnational corporations strategies and State policies in the ESCWA region," paper presented at the Regional Seminar on FDI National Strategies and Policies in the ESCWA Region, held in Beirut on 6 and 7 June 2001.

2. *Limitation on the activity of foreign enterprises*

The ESCWA member countries have recently relaxed restrictions on the activities of foreign enterprises. In the case of Lebanon, restrictions are few and no preliminary authorization is required. There are no performance requirements imposed as a condition on foreign investors, nor are there any requirements regarding geographical location, amount of local content, or export substitution. The Moroccan case is not very different from that of Lebanon. According to the 1995 Moroccan Investment Law, the advantages offered to foreign investors are granted automatically. Tunisia, however, screens foreign investors to protect domestic competitors, and the Government has a negative list that discourages FDI in some priority sectors.

TABLE 20. LIMITATIONS ON THE ACTIVITY OF FOREIGN ENTERPRISES

Country	Authorization	Limitation on foreign workers	Performance requirement	Deregulation
Lebanon	No	Preliminary authorization	No	High
Jordan	Yes	Yes	No	Average
Bahrain	Licence needed	Yes[a/]	No	Average
Morocco	Automatic after 60 days	No	If defined as objective	High
Tunisia	Yes[b/]	Yes	Yes in some sectors	High

a/ Foreigners are often under the management or sponsorship of a Bahraini citizen.

b/ A simple declaration is needed for manufacturing industries, agriculture, food industry, and public works. The remaining sectors require prior authorization, especially if foreign ownership exceeds 50 per cent.

In Bahrain, a licence is required to set up an industrial enterprise, which can be obtained after submitting an application to the Directorate of Industry. Licences are granted to Bahraini nationals and companies incorporated in Bahrain. No performance requirement is asked of foreign enterprises. Some restrictions, however, are placed on foreign investment. For example, the Ministry of Development and Industry rarely approves projects that are energy-intensive, consume large quantities of water and use excessive land. Usually, the Government of Bahrain does not license companies that would compete with existing Government-owned companies.

3. *Employment of foreign labour*

In Lebanon, foreign workers must obtain a work permit from the Ministry of Labour and a residency permit from the relevant authorities, procedures that can be time-consuming and cumbersome. Tunisian law limits the number of expatriate employees allowed and requires lengthy renewal procedures for annual work and residence permits. In Jordan, the Ministry of Labour approves, with limits, the hiring of foreign workers by private businesses under the umbrella of the 1996 Labour Code, which protects the local workforce.

Some companies in Lebanon had difficulties in obtaining work permits for their foreign management staff. Moreover, work permits are considered expensive. The new law on investment in Lebanon, the August 2001 Law for the Promotion of Investments, however, gives authority to IDAL to facilitate the issuance of work permits for foreign labour.

Despite the fact that Bahrain offers a well-educated and skilled indigenous workforce, foreign companies have to rely, to a large extent, on imported labour, in particular labour from Asia, which is not readily available. There are still, however, restrictions on the employment of foreign labour, as a percentage of the total employees of a company must be Bahraini nationals; this percentage varies with the nature of the project. The ESCWA survey shows that more than 55 per cent of the companies interviewed that considered "human resources" as their most important problem also ranked it as the most important constraint. The Economic Development Board is now working on the removal of labour restrictions so that the demand for employment will be market-driven.

4. *Foreign ownership*

Morocco was the first country in the Arab region to liberalize access to foreign capital with its 1983 law. Egypt followed in 1989. In 1993, Tunisia introduced FDI legislation seeking maximum liberalization and deregulation, and abolishing quantitative restrictions on ownership (except agricultural land). In 1995, Morocco adopted an innovative approach abolishing quantitative restrictions on ownership while maintaining exclusions in "strategic" sectors. In 1995, Jordan approved a law that, for the first two years, placed limitations on foreign ownership, restrictions that were abolished in 1997.

TABLE 21. LEGISLATIVE MEASURES PROMOTING FDI

Country	Investment Law	Competition Law
Lebanon	New Investment Law (voted on 14 August 2001)	N/A
Bahrain	No specific law	N/A
Jordan	No. 16, Investment Promotion Law (1995/96)	Under consideration
Morocco	No. 18, Investment Chart (1995)	1999
Tunisia	No. 120, Investment Incentives Code (1993)	1991

Note: N/A = no competition law as yet.

With regard to ensuring competitive practices, Algeria and Tunisia (1991) were the first countries in the region to pass a competition law. Morocco followed in 1999. Jordan has been debating a draft competition law since 1997, but no law has been adopted yet.

Tunisia does not impose quantitative restrictions, but excludes a number of sectors from earning special incentives, and these are: restaurants, real estate, and general retail. Finally, Bahrain imposes no major restrictions on foreign investors and has attempted in recent years to open up fully to international competition. The Economic Development Board recently removed some of the restrictions on FDI. Foreign ownership of companies, up to 100 per cent of the capital, is now permitted in all economic sectors, except in the oil sector.

Foreign companies do not generally complain about discriminatory treatment in Bahrain, Jordan and Lebanon. The results of the ESCWA survey conducted for this study confirm that there is little discrimination in Jordan against foreign investors. The same treatment is provided by the Investment Promotion Law (Law No. 16 of 1995) to national and foreign investment, with few exceptions. The share of foreign ownership in total investment was clarified in Regulation No. 39 of 1997 and its subsequent amendment in 1999. This regulation allowed non-Jordanian investors to own the full project, except in the following sectors where foreign ownership is limited to 50 per cent: the construction and contracting sector; the commercial and commercial services sector; and the mining sector. Recently (2001), the Jordanian Government allowed foreign investors to own 100 per cent of the capital in the mining sector, with the exception of phosphate extraction, which is closed, for the time being, to foreign ownership. Israeli investors, in particular, felt there was discriminatory treatment by business associations and others in Jordan.

5. *Protection of intellectual property rights*

With regard to the protection of intellectual property rights, Jordan recently enacted comprehensive legislation to match international standards. It was not until 1999 that Jordan signed the 1971 Berne Convention for the Protection of Literary and Artistic Works. As for Morocco and Tunisia, they are members of the World Intellectual Property Organization (WIPO). Tunisia, however, has not adopted the UNCTAD Agreement on the protection of trademarks and patents. Lebanon has also been a member of WIPO since 1986 and in 1999 revised its 1924 Intellectual Property Law. The protection of intellectual property rights in Bahrain is judged to be effective and strong, given that the country is a member of WIPO and joined the World Trade Organization in 1995. Bahrain thus has to adhere to all relevant laws and standards imposed by both international bodies.

TABLE 22. CONDITIONS OF ACTIVITY OF FOREIGN ENTERPRISES

Country	Multilateral agreements	Intellectual Property Rights	Property right protection
Lebanon	WIPO (1986), Paris Convention	1999 revised law, problems with enforcement	High
Jordan	WIPO (1972) Euro-Mediterranean Agreement (1997)	Copyright law 1999 Seven years, protection for patents and trademarks, Problems with enforcement	Low
Bahrain	WTO (1995), WIPO (1995) GCC (1981)	Yes, Patent and Trademark Law (1995)	High
Morocco	WIPO (1971), WTO (1995), Madrid Protocol (1989), Paris Convention, Euro-Mediterranean Agreement (1995/96)	Yes (including TRIPs) Problems with enforcement	High
Tunisia	WIPO (1975), WTO (1995), Euro-Mediterranean Agreement (1995) Paris Convention	Yes (including TRIPs)	High

6. *Securing land or real estate*

Securing land and real estate is considered to be more of a problem in Lebanon than in Bahrain or Jordan. In Lebanon, however, a recent amendment to the law has relaxed the rules governing land and real estate ownership by foreigners. In Bahrain, foreign ownership of real estate has recently been authorized, but in specific locations of the country. In Bahrain, there are 10 industrial estates with adequate infrastructure and services for investment projects (power supply, water and telecommunications). Land is leased at reduced prices in these sites for establishing industrial projects. The ESCWA survey showed that the percentage of enterprises interviewed that had difficulties in securing land or real estate was: 25 per cent in Jordan; 38 per cent in Lebanon; and 22.9 per cent in Bahrain.

7. *One-stop-shop*

Jordan, Lebanon and, recently, Bahrain have established a one-stop-shop for foreign investors with the aim of facilitating administrative procedures for the registration and establishment of the foreign company. The Investment and Development Authority of Lebanon (IDAL) is playing an increasing role in facilitating procedures. Almost all those interviewed for the ESCWA survey who had experience with the Lebanese one-stop-shop were satisfied with the services provided. In addition, IDAL supports investors in establishing a company and a representative office, and in obtaining the approvals required by various ministries, in addition to securing the required work permits and visas.

Investors in Bahrain have to deal with different parties, and in some cases two licences have to be secured: one from the Ministry of Industry and the second from the Ministry of Commerce.[23] The Government of Bahrain recently established the Economic Development Board, whose role is to design laws, regulations and policies with the aim of creating an environment conducive to national and foreign investment. The Marketing Promotion Board, which was responsible for the promotion of foreign direct investment, is now part of the Economic Development Board. In order to reduce administrative barriers, the Economic Development Board recently established a one-stop-shop for investors.

In countries where a one-stop-shop has been established, the experience is relatively recent, and very little data are available to test whether the one-stop-shop has attracted any additional investments that would not have taken place otherwise. It is probably the case that the one-stop-shop is receiving many applications and is shepherding them through the cumbersome maze of the region's bureaucracy. Undoubtedly, this work is saving investors time and money. However, the one-stop-shop cannot be a substitute for more radical policy, legal and institutional reform.

[23] The Bahrain Ministry of Industry and Ministry of Commerce were merged shortly after this study was written.

B. TRADE AND FISCAL POLICIES AFFECTING FDI IN THE SELECTED MEMBER COUNTRIES

1. *Trade barriers*

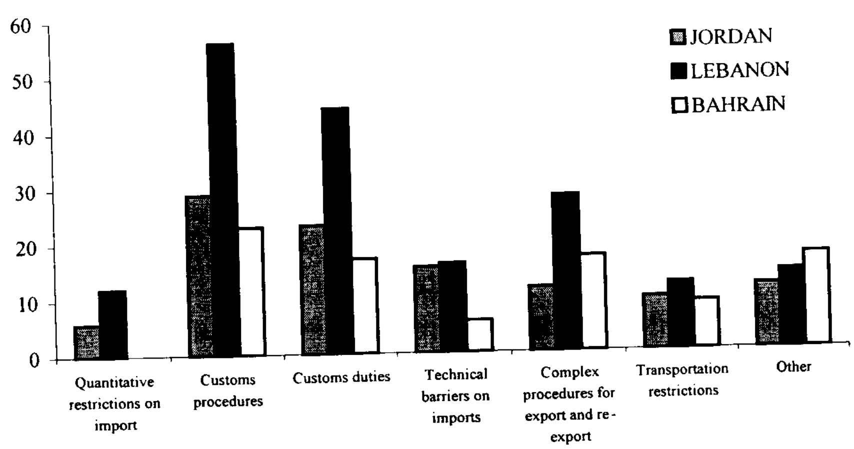
Customs procedures and customs duties are considered, in varying degrees, the greatest trade barriers in Bahrain, Jordan and Lebanon. These customs procedures and duties are more pronounced in Lebanon than in the other two countries. The level of customs duties constitutes one of the major trade barriers hindering the operation of the foreign companies in Jordan. Few companies considered the customs duties on raw materials and intermediate goods as low or very low; most of them characterized these duties as either medium or high. Another related barrier was cited by some companies, which stated that the customs department employees were incompetent.

TABLE 23. MAJOR TRADE BARRIERS HINDERING THE OPERATION OF THE COMPANIES
(*Percentage of the sample*)

Major trade barriers	Jordan	Lebanon	Bahrain
Quantitative restrictions on import	5.8	12	0
Customs procedures	28.8	56	22.9
Customs duties	23.1	44	17
Technical barriers on imports	15.4	16	5.7
Complex procedures for export and re-export	11.5	28	17
Transportation restrictions	9.5	12	8.6
Other	11.5	14	17

Source: Results of the ESCWA survey conducted for this study.

Chart 19. Major barriers



Foreign investors usually complain about the procedures to clear goods from the customs, which are slow and very costly. The process of sorting products and defining them in the customs is another major problem for foreign investors.

> The percentage of interviewed enterprises that view customs procedures in the country as the first major trade barrier that hinders the operation of their company varies as follows:
>
> 29 per cent in Jordan
> 56 per cent in Lebanon
> 23 per cent in Bahrain.

In Bahrain, foreign investors face technical barriers (standards) when exporting to Saudi Arabia and Kuwait. In fact, the flow of goods to Saudi Arabia and Kuwait is protected by various standard organizations, thus posing a problem for suppliers in Bahrain. Bahrain does not have such strict standards.

When asked to rank each major trade barrier by order of importance, almost all companies ranked as first these two major trade barriers: customs procedures and customs duties.

Chart 20. Customs procedures
(Percentage of the sample)

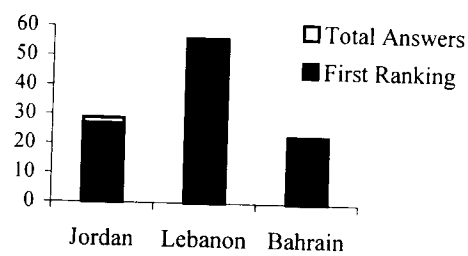
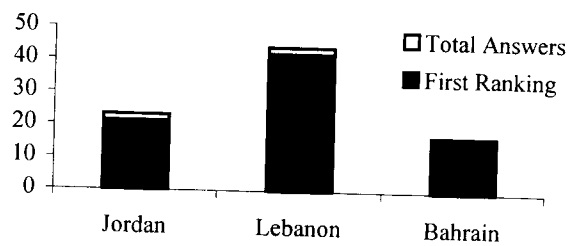


Chart 21. Customs duties
(Percentage of the sample)



2. *Fiscal system*

Lebanon reduced its income and corporate taxes in 1994 and then increased them in 1999. Similarly, a new draft customs law, eliminating several non-tariff barriers, was approved by the Council of Ministers in November 2000. Concurrently, the Government of Lebanon drastically reduced tariff rates. The new investment law offers fiscal incentives to investment in certain regions of Lebanon that are relatively less developed. The Government proposal to impose taxes on the annual turnover of the companies, instead of taxes on the profits, led many foreign parties to declare their intentions to withdraw from Lebanon and to move to another area or country, such as Dubai in the United Arab Emirates, or Cyprus. In Lebanon, even though the capital gains tax and the corporate tax rates are not considered high but rather medium, especially if compared with those in Western countries, the ambiguity and instability of the tax system is a disadvantage.

Morocco and Tunisia are also in the process of revising their tax and trade codes as part of their accession to the Euro-Mediterranean free trade area. In fact, and ahead of the scheduled date, the European-Mediterranean Agreement of Tunisia entered into force in 1996. Bahrain is a tax-free country where fiscal considerations do not constitute a hindrance to FDI.

In Jordan, the corporate tax rate is considered by the majority of companies as high, although around one third of the sample indicated that they considered the rate to be average. The interviewees did not give high ratings to the tax system in terms of transparency and stability. When asked about the practices related to tax assessment collection, a number of companies complained that the tax collectors were unprofessional and incompetent, and usually based their tax assessments on personal views rather than on a systematic and objective method.

TABLE 24. FDI FISCAL AND FINANCIAL INSTRUMENTS

Country	Transfer of profit and capital	Import duties (percentage)	VAT or consumption tax (percentage)	Income tax percentage	Corporate tax percentage
Lebanon	Yes	15%	N/A	Up to 20%	15%
Jordan	Yes	Up to 45%	10%	5%-35%[a]	15%-35%
Bahrain	Yes	Negligible	0%	0%	0%
Morocco	Yes	Up to 35%[b]	0%-20% (VAT)	14%-46%	35%[c]
Tunisia	Yes	10%-287%, 10%-43%[d]	10%-29% (VAT)	35%	35%

a/ Income for foreigners working for foreign companies is tax-free.

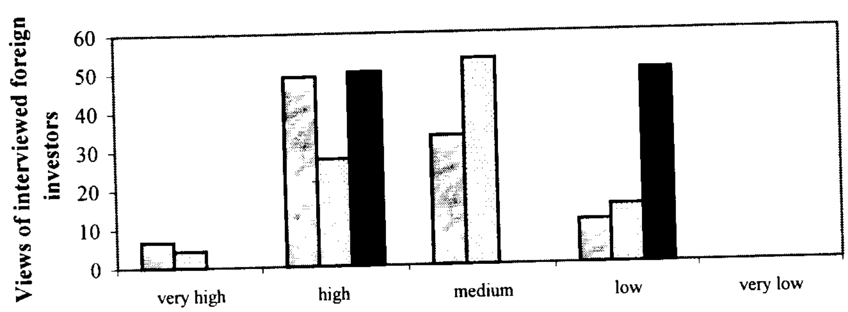
b/ Of the c.i.f. (cost, insurance, freight) value of imports.

c/ Add 15 per cent withholding tax applicable only on foreigners (effective rate is 44.75 per cent).

d/ Tariff rate ranges add to that up to 30 per cent in temporary duty.

In Jordan also, foreign companies that are of small and medium size complain that the sales tax is high, the import licence fees (including university taxes, social services taxes) are high, and the municipality tax is high. These companies also complained about the restrictions imposed by the law on the minimum of capital to be invested by foreigners (50,000 Jordanian dinars [JD]), which increases other government fees such as professional licence fees and chamber of commerce fees.

Chart 22. Corporate tax rate



C. OBSTACLES TO FDI IN THE SELECTED MEMBER COUNTRIES

1. *FDI entry and admission*

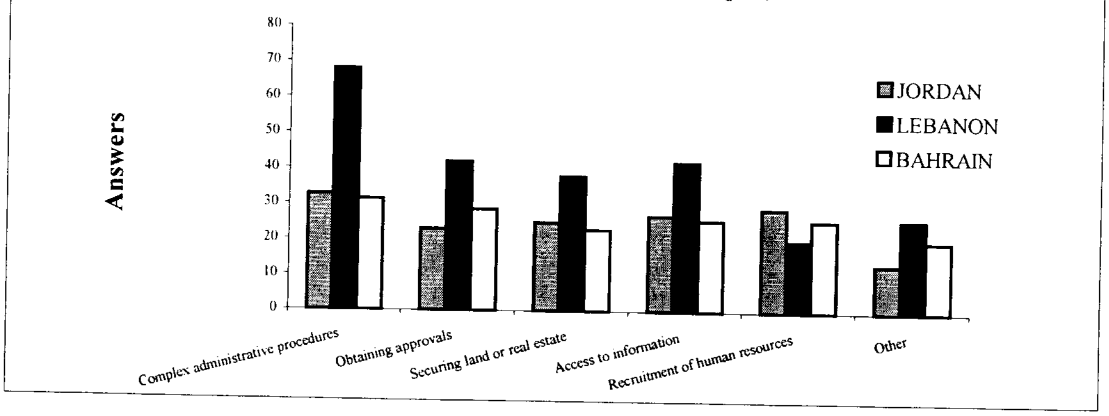
The complex administrative procedures involved in obtaining approvals for registration of the company and access to information are, to varying degrees, the major problem faced by foreign companies when starting up activities in the three countries selected for the survey.

TABLE 25. MAJOR PROBLEMS FACED IN THE START-UP PHASE
(*Percentage of the sample*)

Major problems	Jordan	Lebanon	Bahrain
Complex administrative procedures	32.7	68	31.4
Obtaining approvals	23	42	28.6
Securing land or real estate	25	38	22.9
Access to information	27	42	25.7
Recruitment of human resources	29	20	25.7
Other	13.4	26	20

Source: Results of the ESCWA survey conducted for this study.

Chart 23. Major problems faced in starting up activities in three countries
(Percentage of the sample)

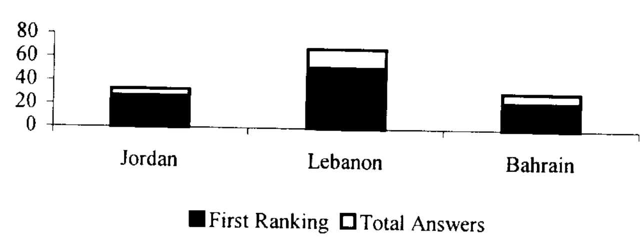


(a) *Complex administrative procedures and obtaining approvals*

As noted above, complex administrative and bureaucratic procedures constitute the most important common problem faced by foreign investors in starting up activities in the three countries under review. Foreign companies complain about the behaviour of government employees who are given excessive authority. They also complain about the lack of effective coordination between the government agencies concerned to facilitate the course of procedures. In Lebanon, as noted above, the one-stop-shop at IDAL is facilitating administrative procedures for foreign companies wishing to set up new activities in Lebanon.

More than two thirds of the sample in Lebanon and one third of the sample in both Bahrain and Jordan complained about these procedures. The majority of those enterprises that considered this the most important problem have also ranked it as the most important constraint.

Chart 24. Complex administrative procedures in starting up activities
(Percentage of the sample)



The majority of the sample (52.9 per cent) in Lebanon considers the delay for FDI admission too long, against 19.2 per cent in Jordan and 12.5 per cent in Bahrain. In Lebanon, foreign investors complain about the very long delays to get a permit to start a business; the time needed to process an approval exceeds, in many cases, one year. In Jordan, very few companies believe that the procedures to approve a foreign investment are very complex. A significant number (42.3 per cent) in Jordan considered this an easy process, against 16.7 per cent in Lebanon, and 29.4 per cent in Bahrain.

Chart 25. Complexity of FDI approval process

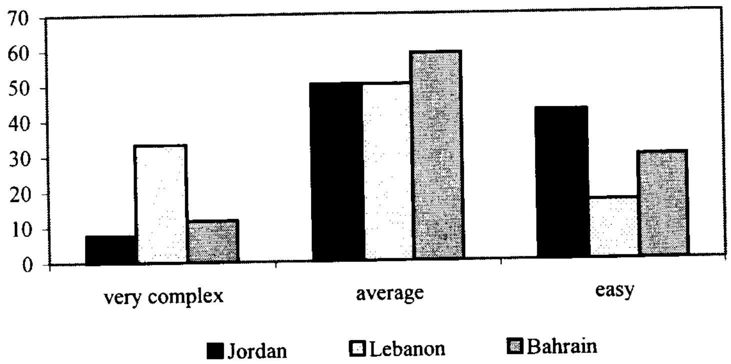
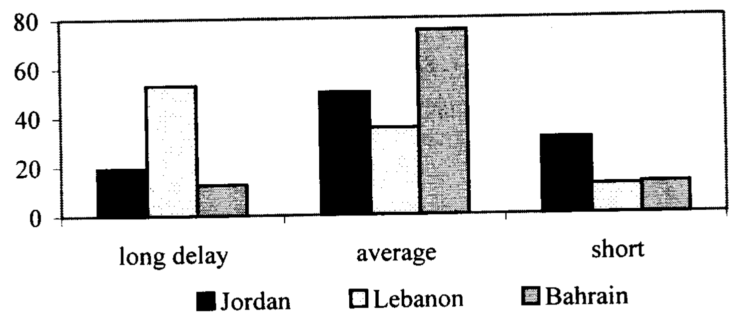


Chart 26. Length of FDI approval process



In Jordan, significant improvements have been achieved in the past three years with regard to reducing administrative barriers. In addition, the administrative procedures necessary to register a company are becoming less cumbersome. The Jordan Investment Board has simplified its procedures, while economic policies have been increasingly liberalized.

> The percentage of interviewed enterprises that faces complex administrative procedures in the start-up phase varies in each of the three countries as follows:
>
> 32.7 per cent in Jordan
> 68 per cent in Lebanon
> 31.4 per cent in Bahrain.

(b) *Access to information*

Access to legal and business information is a common problem faced by foreign investors, though this problem is more acute in Lebanon than in Bahrain or Jordan. Little information or advice is available for the foreign investor with regard to opportunities and possible investment projects. There is also a lack of data on FDI in these three countries.

Data on FDI enterprises in the three countries are unreliable. Foreign companies are not required by law to declare the actual amount of investments made. Data on FDI enterprises are scattered among different government agencies. In Jordan, various agencies deal with FDI, including the Jordan Investment Board (responsible only for the sectors that enjoy special treatment and incentives); the Ministry of Industry and Trade; the Free Zones; and the Special Economic Zone of Aqaba. In Bahrain and Lebanon, sources of information are dispersed among various agencies, including the Ministry of Industry, the Ministry of

Commerce and the Central Bank. In these two countries, there is as yet no unified investment law that regulates foreign investment. Therefore, foreign investors have to gather the necessary information from different sources.

In Bahrain, foreign investors lack information on the markets of neighbouring countries (such as Saudi Arabia and the Islamic Republic of Iran), as many foreign companies want to use Bahrain as a gateway to a regional market.

> The percentage of interviewed enterprises that has difficulties in having access to information is:
>
> 27 per cent in Jordan
> 42 per cent in Lebanon
> 25.7 per cent in Bahrain.

Around half of the enterprises in Jordan and Bahrain that considered "access to information" a major difficulty ranked it first among the most important difficulties faced.

2. *Impediments faced in operating in the country*

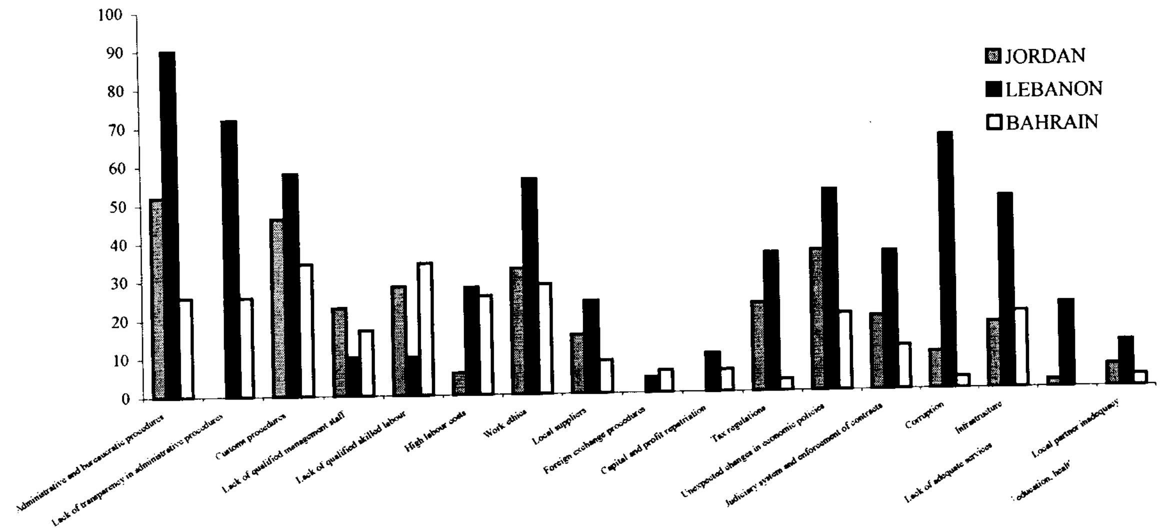
Foreign companies stated they faced a number of constraints in their operations: administrative and customs procedures, contradictions in some of the regulations, inappropriate judiciary systems, a lack of transparency in the tax system, and a relative absence of technical skills among the labour force.

TABLE 26. DIFFICULTIES FACED BY COMPANIES IN OPERATING IN THE COUNTRY
(*Percentage of the sample*)

Difficulties	Jordan	Lebanon	Bahrain
Administrative and bureaucratic procedures	51.9	90	25.7
Lack of transparency in administrative procedures		72	25.7
Customs procedures	46.1	58	34.3
Lack of qualified management staff	22.9	10	17.1
Lack of qualified skilled labour	28.3	10	34.3
High labour costs	5.7	28	25.7
Work ethics	32.7	56	28.6
Local suppliers	15.3	24	8.6
Foreign exchange procedures		4	5.7
Capital and profit repatriation		10	5.7
Tax regulations	22.9	36	2.9
Unexpected changes in economic policies	36.5	52	20
Judiciary system and enforcement of contracts	19.2	36	11.4
Corruption	9.6	66	2.9
Infrastructure	17.2	50	20
Lack of adequate services: education, health	1.9	22	0
Local partner inadequacy	5.7	12	2.9

Source: Results of the ESCWA survey conducted for this study.

Chart 27. Difficulties faced by companies in operating in the country
(Percentage of the sample)

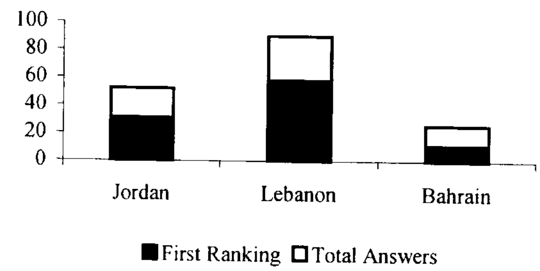


(a) *Administrative and customs procedures*

The percentage of interviewed enterprises that faces administrative and bureaucratic procedures in operating in the country varies as follows: 51.9 per cent in Jordan 90 per cent in Lebanon 25.7 per cent in Bahrain.

The administrative and bureaucratic procedures, in particular the lack of transparency in the procedures, and the customs procedures are the greatest difficulties faced by foreign investors operating in the three countries under review, though these difficulties are less pronounced in Bahrain. Foreign investors consider the administrative and bureaucratic procedural problems in Lebanon and Jordan to be more acute during the operational phase of the company than during the start-up phase. This may be explained by the fact that in the start-up phase, IDAL and the Jordan Investment Board contribute to alleviating the difficulties faced by foreign investors getting established in the host country. In Lebanon, there is almost a consensus among foreign investors (90 per cent of the sample) regarding the difficulties they faced with regard to administrative procedures. This problem was ranked as the most significant obstacle by more than 60 per cent of the companies that cited this impediment in Lebanon and Jordan, and by around 45 per cent of those companies that cited this problem in Bahrain.

Chart 28. Administrative and bureaucratic procedures
(Faced in the operational phase [Percentage of the sample])



The majority of the sample interviewed in Lebanon complained about corruption, customs procedures and lack of transparency in the administrative procedures. Around two thirds of the companies interviewed considered corruption as the most important problem faced, and almost all these companies ranked this problem as the first priority.

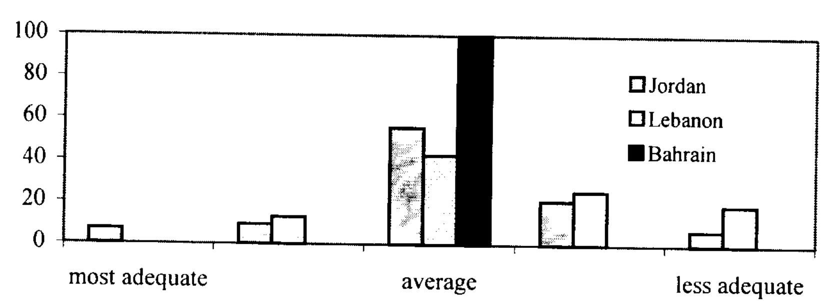
> Sixty-six per cent of the interviewees in Lebanon believe that corruption is the major barrier hindering the operation of the company against only 9.6 per cent in Jordan and 2.9 per cent in Bahrain.

In Jordan, though administrative procedures recently became less cumbersome in the start-up phase, foreign firms continue to face bureaucratic barriers in their operation, as half of the sample complained about these barriers. The sample interviewed stated that they face the hurdles of customs officials, tax collectors, and labour and health authorities. Lack of transparency in administrative procedures was a difficulty cited by 72 per cent of the sample in Lebanon and 25.7 per cent in Bahrain.

(b) *Unexpected changes in economic policies*

Half of the sample in Lebanon and more than the third of the sample in Jordan consider the unexpected changes in economic policies to be one of the major impediments to operating in the country. Foreign investors in Bahrain do not consider this issue a major problem. Bahrain has a stable business environment, a stable market, stable currency and minimum government interference.

Chart 29. Stability of the tax system



Economic instability reduces the trust and confidence of foreign investors; it is reflected in Lebanon in the constantly changing tax regulations, which negatively affect businesses. Companies cannot predict their forecasts in a reliable manner, and have difficulties in completing a proper business plan. The unpredictability of the regulatory system is risking the viability of businesses. However, in spite of the latest reduction in the customs tariff rate, the instability in that respect, reflected in the many successive amendments since 1994, is creating a source of worry for investors, making them reluctant to invest in Lebanon. Moreover, foreign investors are affected negatively by the changes that occurred in the various

government administrations of the country. The two successive changes of the Cabinet in 1998 and in 2000 led to a lack of continuity in government policy.

> The percentage of interviewed enterprises that believes that unexpected changes in economic policies in the country is a difficulty in operating in the host country varies as follows:
>
> 36.5 per cent in Jordan
> 52 per cent in Lebanon
> 20 per cent in Bahrain.

(c) *Judiciary system and enforcement of contracts*

More than one third of the sample in Lebanon complained about the judiciary system and the fact that contracts were not enforced. Only a few companies in Bahrain and Jordan considered this a constraint in operating in those countries. However, it has been frequently stated by foreign companies in Lebanon that the judicial system is not an independent system. Thus, foreigners often have recourse to foreign arbitration overseas.

> The percentage of interviewed enterprises that believe that the judiciary system and enforcement of contracts is a difficulty in operating in the host country varies as follows:
>
> 19.2 per cent in Jordan
> 36 per cent in Lebanon
> 11 per cent in Bahrain.

(d) *Infrastructure conditions and cost*

With the exception of Lebanon, where half of the sample stated that they suffered from the infrastructural conditions, foreign companies in Jordan and Bahrain in general considered the infrastructural conditions to be adequate.

In Jordan, around half of the sample rated infrastructural conditions as most adequate. Infrastructural costs are considered average, except for electricity, with 39 per cent of the sample indicating that electricity was very expensive. It is hoped that, with the privatization of the newly formed Central Electricity Generating Company and the Electric Distribution Company, electricity costs will drop. Telecommunications are not yet considered cheap by most of the sample, despite the privatization of the Jordan Telecommunication Company, in which France Telecom acquired 40 per cent of the shares.

In Lebanon, foreign companies considered infrastructural conditions to be adequate, except for road conditions and electricity. Electricity services are considered very bad and expensive. However, with regard to Beirut International Airport, clear efforts have been made since the beginning of the 1990s and the result is very satisfactory to foreign investors. Costs of production, labour, transport, utilities and energy are high.

V. MAJOR POLICIES TO ATTRACT FOREIGN DIRECT INVESTMENT

A. FDI AND PRIVATIZATION: COUNTRY ANALYSIS

Privatization is one of the most effective policies that Governments can use to attract FDI. Properly designed and implemented, privatization can have great economic benefits as well as a direct impact on the quality of goods, services and infrastructure available. Privatization has been strongly associated with FDI. The vast majority of FDI—over 90 per cent—in developing countries has come from privatization transactions, especially private participation in infrastructure. A comparison between slow privatizers (countries where privatization sales were less than 1 per cent of GDP over the recorded period) and fast privatizers (countries where privatization sales exceeded 3 per cent of GDP) shows that fast privatizers accumulated twice as much FDI over the same period. These trends are also associated with a much more rapid development of capital markets.

Privatization is effective in structural adjustment programmes when Governments need to restore a healthy balance in both their fiscal and external accounts (balance of payments). The positive impact of privatization is, however, greater if the State-owned enterprises are sold to foreign enterprises. Privatization proceeds are often used to reduce fiscal imbalances, but they also bring an influx of capital, improved technologies and management know-how. Privatization often leads to increases in productivity through its positive impact on efficiency.

The impact of privatization on FDI can be classified into the following categories:

(a) Direct impact: privatization attracts foreign investors who not only acquire the State-owned enterprise, the right to develop a new infrastructure (such as a power plant or toll road), or the right to deliver infrastructural services (such as telecommunications or electricity). This brings new investments, and these investments increase the stock of FDI;

(b) Indirect impact: privatization, especially when accompanied by measures to liberalize the market and open it up to competition, creates new opportunities for foreign investments. Privatization often leads to the development of financial markets, which will create a better environment for FDI;

(c) Induced impact: privatization is most often an integral part of a series of economic reforms that improve the country's economic performance. Improved economic performance will raise the per capita income and make profitable foreign investments that were previously not profitable;

(d) Catalytic impact: privatization first puts the developing country on the investors' "radar screen" and generates interest in it. Furthermore, the commitment to privatization and liberalization provides firm evidence to investors that the political and regulatory risks (of expropriation, restrictions on capital accounts, and repatriation of profits) are being reduced. Finally, the "demonstration effect" of a successful privatization can convince other foreign investors to follow suit and participate in subsequent privatization transactions.

Privatization can be implemented using a variety of methods, from the trade sale to the initial public offering. An initial public offering takes place when an enterprise goes (or becomes) public and for the first time offers shares for sale on the stock market. When a State-owned asset is privatized, it is often incorporated, paving the way for an initial public offering. Some privatization methods that preclude foreign investors in the initial stages of privatization, such as voucher privatization or management buy-outs, have had a bad track record. The method of privatization has to be tailored to the needs of the enterprise or the sector being privatized, and to local and international market conditions. For example, enterprises that lack good management and a solid financial track record may not be ripe for an initial public offering. Furthermore, an initial public offering requires capital markets to be sufficiently developed in order to succeed. It is obvious that, for privatization to attract FDI, restrictions on foreign investments have to be eliminated.

1. *The status of privatization in the MENA region*[*]

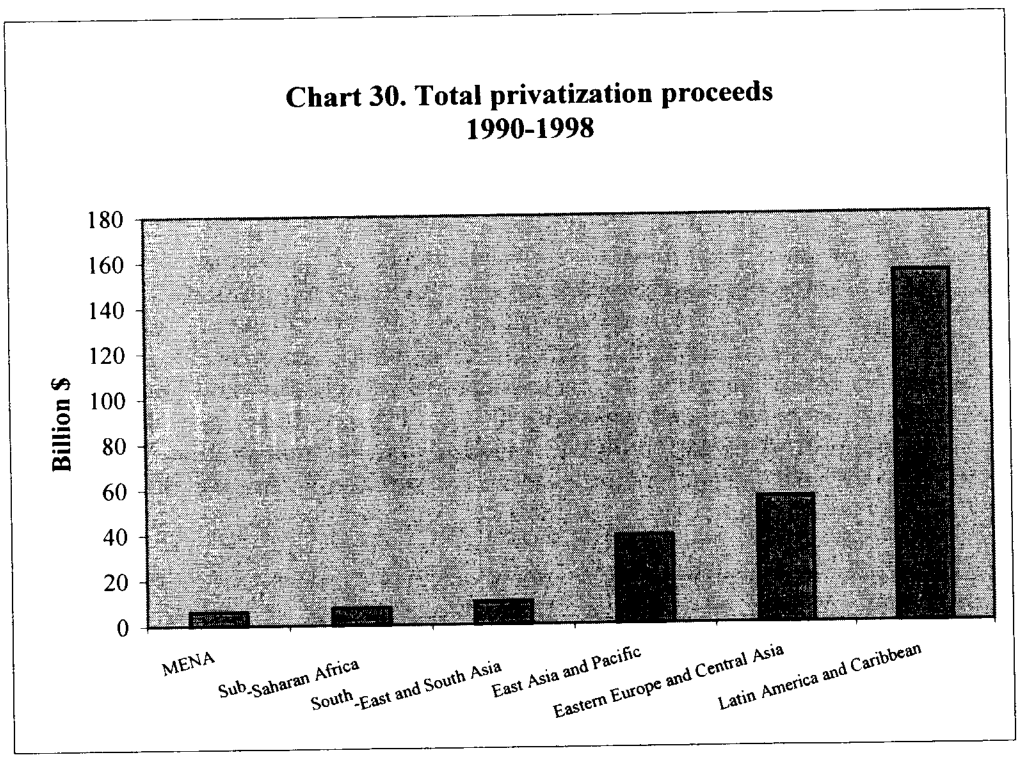
Privatization has been slow in the Middle East and North African countries, with proceeds averaging only 3 per cent of the worldwide total over the period 1991-1998. Global privatization revenues increased from US$ 25 billion in 1990 to US$ 159 billion in 1999. The MENA region is doing better in terms of privatization, but not as well as the rest of the world.

TABLE 27. PROCEEDS FROM PRIVATIZATION IN THE MENA REGION, 1990-1997
(*Billions of US dollars*)

Country	Revenues
Turkey	3 600.0
Morocco	1 846.7
Egypt	1 510.2
Tunisia	150.2
Oman	60.1
Jordan	58.7

Source: World Bank, *World Development Indicators*, 1999.

In comparison with the rest of the developing world, the MENA countries have received the lowest amount of revenues from privatization, even when compared with the poorest region of sub-Saharan Africa. The 1990-1998 total of proceeds collected by all Middle East and North African countries does not exceed the total received by Colombia (US$ 6.2 billion) alone during the same period. The low figure is a reflection of the slow process of divestment in State enterprises.



Source: World Bank Privatization Database.

[*] This section refers to the MENA (Middle East and North Africa) region because the data available are about the MENA region. Most of the MENA region is considered part of the ESCWA region.

Box 3. Privatization and FDI in Jordan

- Management of the Greater Amman Water and Wastewater Networks was awarded to a French company, Suez Lyonnaise des Eaux.
- Aqaba Railways Corporation was awarded to a United States consortium to operate for 25 years conditional on an investment of US$ 154 million in the railway.
- Jordan Cement Factories was partially sold (33 per cent) to Lafarge Cement Group of France in October 1998 for US$ 102 million.
- Jordan Telecommunications Company sold 40 per cent of its shares to a consortium consisting of France Telecom, the National Bank of Kuwait, Saudi Arabia's National Bank, and the (local) Arab Bank. The sale was for US$ 508 million.
- A stake in Royal Jordanian airlines is for sale, with a number of foreign airlines expressing interest in the company.

Source: Economist Intelligence Unit, *EIU Country Profile 2000-01*.

2. *Privatization proceeds and FDI*

According to the World Bank database, privatization in the countries reviewed attracted the following foreign investments.

TABLE 28. FDI AND PRIVATIZATION: SELECTED COUNTRIES, 1988-1998
(*Millions of US dollars*)

Country	FDI from privatization
Egypt	2 144.5
Morocco	1 257.4
Tunisia	458.9
Jordan	49.1
Lebanon	122.0

Source: World Bank Privatization database (www.ipanet.net).

Note: The figures include investments made by foreigners and by various investors (including national joint ventures).

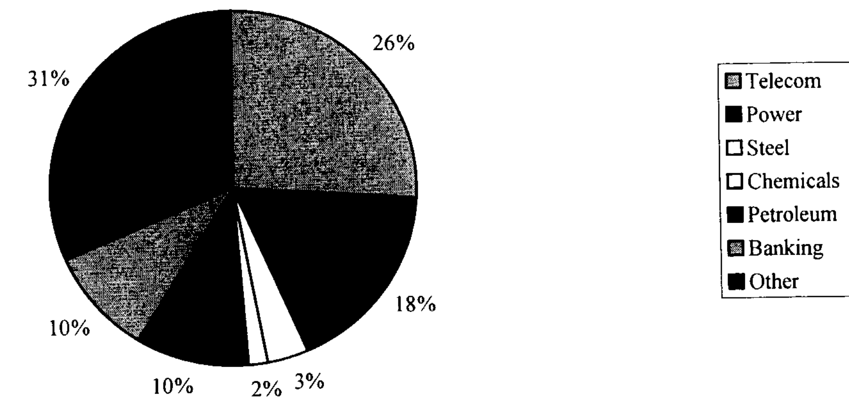
Morocco's privatization programme slowed considerably; it raised an estimated US$ 92 million in 1998 compared with US$ 716 million the previous year. Additional shares were sold to a foreign investor and to workers in two oil refineries: the Société Anonyme de l'Industrie de Raffinage (SAMIR) and the Société Cherifienne de Petrole (SCP), generating approximately US$ 40 million. Morocco also raised another US$ 37 million with the sale of Wafa Insurance, and more than US$ 12 million with the sale of hotels to local investors.[24]

Tunisia's privatization programme began in 1987 and accelerated in 1998, raising US$ 364 million. Key divestitures included the private sale of two cement companies, the Société des Ciments Jebel Ouest and the Société des Ciments d'Enfidha, to foreign investors raising US$ 361 million.

If the proceeds of global privatization are grouped by sector, infrastructure received above US$ 142 billion between 1990 and 1998, with the largest share for the telecommunications sector, which received 50 per cent, or about US$ 70 billion. The overwhelming majority of investors in the telecommunications sector were foreign.

[24] World Bank Privatization Link.

Chart 31. Percentage of proceeds from privatization in the World (1990-1998)

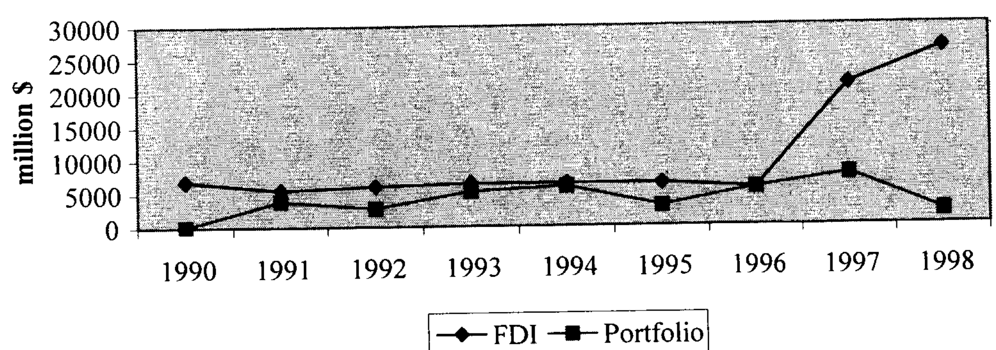


Source: World Bank Privatization Database.

3. *Investment flows: FDI and other forms of inflows*

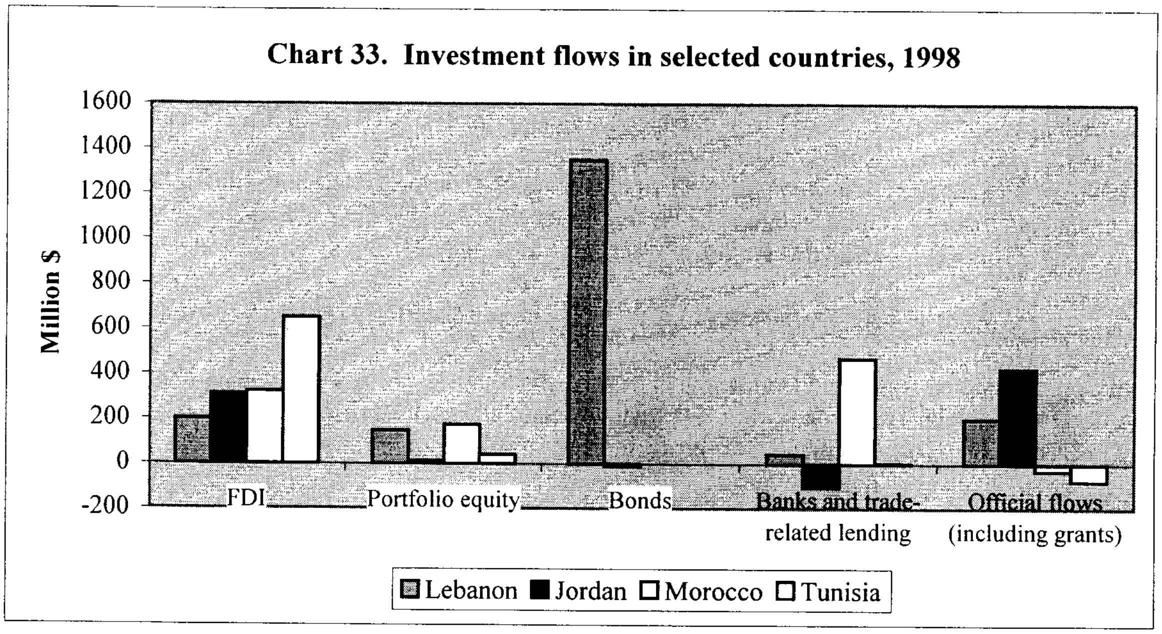
According to the World Bank, foreign investors (direct and portfolio investors) contributed to 58 per cent of total privatization proceeds in the developing world. In 1998, FDI was the main source of foreign revenues raised through privatization, accounting for 93 per cent of the total. Total portfolio equity flows to developing countries were almost cut in half, while total FDI flows increased between 1997 and 1998.

Chart 32. Foreign investments in privatization in the developing world



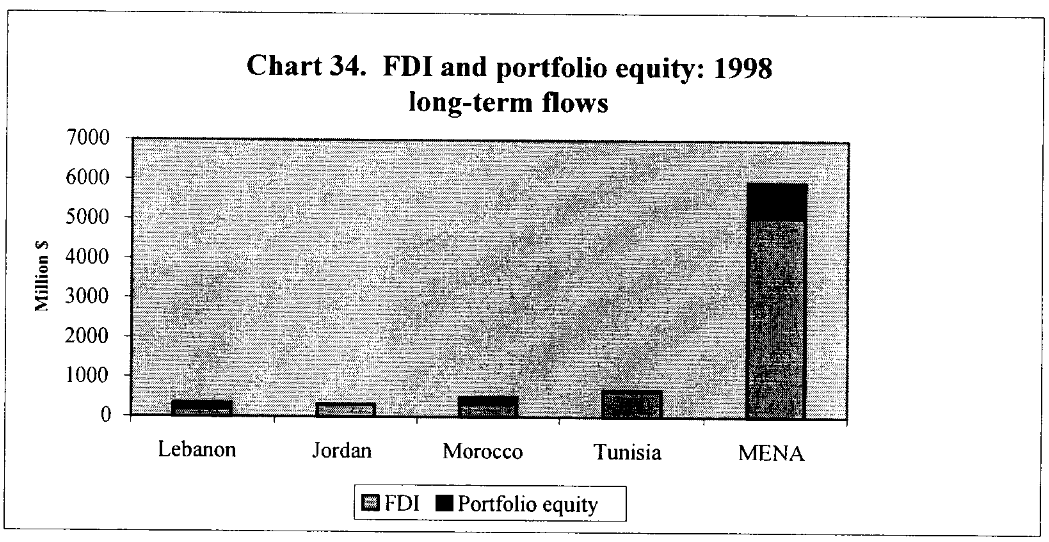
Source: World Bank Privatization Database.

The share of FDI in privatization programmes—in relation to portfolio foreign investment—increased dramatically after 1996, and this trend has continued ever since. The main cause behind the dichotomy in figures and trends is the privatization of telecommunications and banking sectors in Latin America and the Caribbean. The extent of foreign participation in privatization has varied across regions. Latin America, the Caribbean, Eastern Europe, and Central Asia attracted the largest share of foreign investment, with Brazil, Poland, Romania, and the Russian Federation being the main recipients.



Source: World Bank web site.

FDI inflows were the largest investment component of long-term investment flows for the region in 1998. Lebanon was an exception, since in 1998 the country issued bonds worth US$ 1.35 billion, whereas Tunisia and Morocco did not issue any capital debt. In terms of official investment flows, Jordan and Lebanon received substantial amounts, comparable to their respective FDI inflows.



Source: World Bank web site.

With the exception of Lebanon and Morocco, FDI exceeded the level of portfolio equity in the region in 1998. FDI inflows to Morocco decreased from US$ 514 million (1993-1997 annual average) to US$ 322 million (1998), with portfolio equity increasing from US$ 136 million to US$ 174 million. The case for Lebanon is different, as both FDI and portfolio flows increased at about four times the level of 1993-1997. FDI increased from US$ 56 million to US$ 200 million, and portfolio equity increased from US$ 49 million to US$ 147 million. The decline in Morocco's FDI may have been partially driven by the slowdown in the privatization programme in the country. FDI to Lebanon increased as a result of a proactive governmental policy to attract foreign investors. However, Lebanon remained a risk, and thus a magnet to short-term investors as reflected by the comparable increase (relative to FDI) in the level of portfolio investments.

4. *Conclusions*

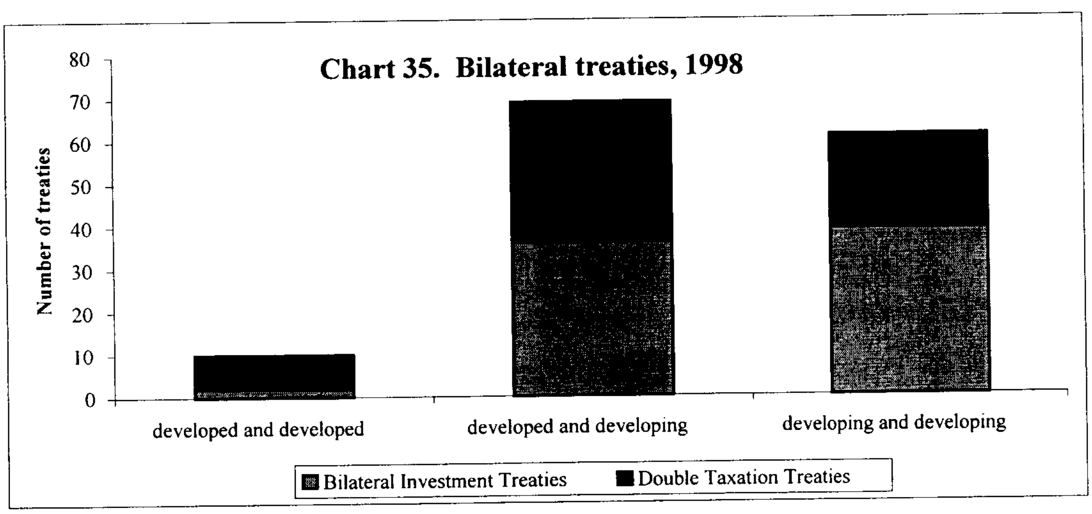
Privatization can be a very powerful policy instrument to attract FDI, especially when Governments establish the appropriate legal and regulatory environment for FDI and for private participation in infrastructure. The most effective means to interest foreign investors has proved to be Greenfield[25] PPI (private participation in infrastructure), as well as classic privatization of telecommunications, electricity and transport infrastructure. This also happens to be one area where the ESCWA member countries have lagged behind the rest of the world, and where a lot of catching up is needed.

B. TRADE AND INVESTMENT LIBERALIZATION AND FDI: COUNTRY ANALYSIS

The importance of trade and investment liberalization in the promotion of FDI cannot be understated. The elimination of barriers to trade and investments is critical to increasing the size of the market accessible from any one country. Governments can therefore promote FDI by eliminating these barriers.

1. *Investment agreements and FDI*

Bilateral investment treaties are believed to be positively correlated with FDI inflows. These treaties strengthen the standards of protection and treatment of foreign investors, facilitate entry into a host nation, and establish mechanisms for settling disputes. This explains why the number of bilateral investment treaties reached 1,726 by the end of 1998, 170 more than in 1997. Of these, 434 were concluded between developing countries, with 66 treaties concluded in 1998 alone. About 174 countries have signed bilateral investment treaties, thus signalling to multinational corporations that their countries are liberalizing their investment regimes and opening up to foreign investment. The more recent treaties are addressing non-traditional issues of concern to foreign investors, such as workers' rights and national treatment at the pre-establishment phase, thus including the more common fiscal and financial measures often seen in bilateral investment treaties. Bilateral treaties for the avoidance of double taxation, another FDI-friendly measure, have also increased; their number reached 1,871 at the end of 1998, with 39 signatory countries from the developing world, out of which 26 were Asian and six were African.[26] The treaties facilitate the integration of developing economies into the global market and reduce distortions and restrictions blocking FDI flows.



Source: UNCTAD, *World Investment Report 1999*.

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[25] Greenfield investment is an investment in new productive facilities, as opposed to mergers and acquisitions, where there is not necessarily an additional investment since a standard merger or acquisition does not necessitate the creation of assets and employment in the short term. Developing countries thus prefer a Greenfield project, given the direct and more immediate impact on the local economy (see box 4).

[26] *World Investment Report 1999*.

In spite of their proliferation, bilateral investment treaties remain weak determinants of FDI. Other determinants such as market size are more statistically important.[27]

As part of their efforts to increase FDI inflows, the ESCWA member countries have been actively engaged in negotiating and concluding bilateral investment treaties. However, the countries that have signed the highest number of bilateral investment treaties are not necessarily those receiving the largest FDI inflows. Saudi Arabia, the largest recipient of FDI in the region, has signed few agreements, while Oman, which has been more active in this respect, has received insignificant amounts of FDI. Western European countries—notably France, Germany and the United Kingdom—the largest investors in the region, have signed the greatest number of treaties with ESCWA member countries. Among the ESCWA member countries, the number of bilateral investment treaties signed between them is relatively small. However, the main reason for the success of bilateral investment treaties in most countries, including the ESCWA member countries, is that they usually provide for national treatment to foreign investors in the post-establishment phase only. Therefore, they neglect certain issues that are very delicate for the host countries but of major significance to transnational corporations, such as non-discriminatory treatment of these investors at the entry and establishment stages of investment.[28]

Table 29 lists a sample of the most important double taxation treaties and bilateral investment treaties signed by the selected ESCWA member countries. A large number of these agreements remain pending (notably in Lebanon), or their entry into force was further postponed. At any rate, the ESCWA member countries need to continue to improve their bilateral relations with their main trading and investment partners, in particular the EU and neighbouring Arab countries. In addition, they must revise outdated treaties and work on enforcing the existing ones. Syrian-Lebanese agreements, for instance, remain only partially implemented after both countries had rushed into signing them.

TABLE 29. MAJOR TREATIES: BILATERAL AND MULTILATERAL

Countries	Partner country	Date	Type of treaty
Lebanon	Egypt	1996	BIT, DTT
	Syrian Arab Republic	1997	BIT, DTT
	Spain	1996	BIT
	France	1996 (pending)	BIT
	Italy	1997 (pending)	BIT
Jordan	Euro-Mediterranean	1997	FTA
	Israel	1997	BIT
	United States	1997, 2000	BIT
	UK and Ireland	1979	BIT
	France	1985[a/]	DTT
	Egypt	1997[a/]	DTT
Bahrain	UK	1990	BIT
	France	1993	DTT
Morocco	Euro-Mediterranean	1995	FTA
	USA	1995	BIT[b/]
	France	1975, 1996[c/]	BIT
	Egypt	1978[a/]	BIT
	France	1989	DTT
	UK	1981	DTT

[27] UNCTAD, *Bilateral Investment Treaties in the Mid-1990s* (New York and Geneva, 1998).

[28] Basile, op. cit.

TABLE 29 (*continued*)

Countries	Partner country	Date	Type of treaty
Tunisia	Euro-Mediterranean	1997[a/]	FTA
	Turkey	1993	BIT
	Spain	1994	BIT
	Italy	1989	BIT
	France	1973	DTT
	UK	1982	DTT

Source: UNCTAD, *World Investment Directory 1996, West Asia*, author's compilations.

Notes: FTA = free trade area; DTT = double taxation treaty; BIT = bilateral investment treaty.

a/ Date of entry into force.
b/ Investment framework.
c/ Not entered into force.

In response to the large increase in FDI flows worldwide and the existence of multilateral agreements regulating international trade, developed countries are pushing for the establishment of a multilateral agreement on investment. The ESCWA member countries are thus faced with two basic strategic options. The first is to continue with the existing strategy, that is, to purse further liberalization of their FDI regimes through unilateral, bilateral, and regional agreements. The second option is for the ESCWA member countries to coordinate their efforts and start preparations for a multilateral agreement on investment that takes into account their priorities and objectives. While a multilateral agreement on investment is not a pressing issue, the ESCWA member countries can start building up their negotiating strategy in order to benefit from such an agreement.

2. *Trade agreements*

(a) *Regional integration and FDI*

With a view to a future global investment framework, countries have moved beyond cooperation at the bilateral level and have created regional blocs within which investment rules have been standardized and the restrictions facing intraregional FDI removed. Regional integration frameworks increase the geographical scope and size of effective markets. They increase the ease of access within member markets through the removal of trade and non-trade barriers, and they induce outside countries to increase their investments in member countries, since each host country now can offer the foreign investor access to the whole region. In 1995, for instance, 31 per cent of the sale of United States affiliates in the EU were geared to countries other than the host country.

TABLE 30. REGIONALISM AND FDI INFLOWS

Country/region	Time period	Note	FDI changes
EEC (established 1954)	1950	FDI from the United States	5.4%
	1957		6.6%
	1962		10.0%
	1972		17.1%
Ireland	1983-1992	Following accession to EEC	27.0%
Netherlands	1983-1992	Following accession to EEC	22.0%
Mexico	1992/1993	Before NAFTA	US$ 4 billion annually
	1994/1995	After NAFTA	US$ 10 billion annually
MERCOSUR (established 1995)	1995	Before	US$ 10 billion
	1996	After	US$ 17 billion

Source: UNCTAD, *World Investment Report 1998*.

Between 1957 and 1972, the outward FDI stock of the United States into the European Economic Community (EEC) increased from 7 to 17 per cent (after the establishment of the six-country bloc). That is after the establishment of the six-country bloc. Similarly, intra-EEC flows also witnessed a substantial increase. At the country level, Spain, Portugal, the Netherlands and Ireland benefited greatly from EEC membership, as they received record FDI flows in the years immediately before and after their accession. It should be noted that Portugal, the Netherlands, and Ireland are small in size, and that Spain and Portugal are considered the poorest Western European countries.

FDI flows into MERCOSUR (the Southern Cone Market) as a whole increased immediately before and after the establishment of MERCOSUR in 1995. This regional bloc (composed of Argentina, Brazil, Paraguay and Uruguay) provides access to a market of 200 million people in the MERCOSUR members. The economic integration of such a large market helped attract some US$ 10 billion in FDI inflows in 1995 and US$ 17 billion in 1996. Having said that, it is difficult to attribute the FDI gains to the MERCOSUR framework alone. The implementation of the privatization programmes, which had begun prior to the economic integration, had a lot to do with the increase of FDI. MERCOSUR, however, consolidated the macroeconomic reforms, standardized the rules, opened up the region to the world, and helped spread the privatization programme as well as other FDI-inducing programmes across the region.

Evidence from the North American Free Trade Agreement (NAFTA) shows that Mexico benefited greatly from the Agreement. The FDI inflows doubled to over US$ 4 billion annually in the years immediately before NAFTA and increased to over US$ 10 billion in 1994 just after the signature of the Agreement. The significant jump in FDI flows to Mexico is attributed to a number of factors (including market size, proximity to the United States and low-cost labour), but the establishment of a regional agreement remains a major contributing factor as it creates a framework within which investment is conducted, given agreed-upon rules of engagement. Neither the above-listed factors nor the NAFTA framework alone could have induced this amount of FDI if they had been operating separately. The size of the Mexican market was always large, and labour was always abundant and cheap, but FDI inflows increased only when NAFTA was signed.

Together with a number of other factors, regional integration frameworks have contributed positively to the growth of FDI into the recipient region, whether such frameworks grouped together developed or developing countries, or both. From the point of view of each member country, what attracts FDI to a specific market depends on the ability of the country to provide access to the regional market, which in turn depends on how well it is integrated into the regional bloc. To what extent that conclusion is applicable to the Arab countries remains to be seen. Further empirical analysis is warranted to test the impact and significance of these bilateral and multilateral agreements on FDI inflows.

The lesson of regionalism to Arab countries is clear. Arab countries have to implement and enforce the Arab Free Trade Area (AFTA) as rapidly as possible and introduce their own investment framework, standards and rules of origin, as well as remove intraregional restrictions that may divert FDI to other regions. Fast-track negotiations among Arab countries are warranted to ensure that the overall interests of each AFTA member are respected and protected.

(b) *Trade agreements with the European Union and the United States: the case of Jordan*

Unlike Lebanon and Bahrain, Jordan has entered into free trade agreements with both the European Union and the United States. Jordan signed the Euro-Mediterranean Agreement with the European Union. Although the Agreement will create new opportunities for Jordanian and foreign investors to export to the EU market without customs duties, the strict application of rules of origin by the EU is hindering exports to the European market. Jordan is benefiting more, however, from the Free Trade Agreement with the United States, as well as from the advantages granted by the United States to products originating in the Qualifying Industrial Zones.

(i) *Qualifying Industrial Zones*

In 1996, the United States gave Jordan and Egypt the opportunity to establish Qualifying Industrial Zones (QIZ), by which products manufactured in these zones enjoy duty free entry into the United States

market, provided that the requirements of certain rules of origin are met. Under United States law, an article is considered to be a product of a QIZ if it includes a minimum value added content of 35 per cent, of which 7-8 per cent should have Israeli input, and 11.7 per cent should be of Jordanian origin; the remaining 15-16 per cent can be of United States, Jordanian, Israeli or Palestinian origin.[29] In such cases, products manufactured in the QIZ enjoy duty free entry into the United States market.

Several QIZs have been established in Jordan, the most important being the one in Irbid in 1998. The QIZs have attracted Israeli, United States and Asian investors (China, Taiwan Province of China, and Pakistan), which have set up large plants to produce articles facing high import tariffs in the United States market. Foreign investment has been mainly in garments, including jeans, luggage and sportswear. The total approved investments for QIZ projects during the period 1996-1999 amounted to JD 50.8 million, while total planned employment amounted to 6,241 new jobs. According to the AMIR study, 71 per cent of all approved investments, and 77 per cent of the total planned employment have been realized.[30] The QIZs are becoming an increasing source of export revenues and employment generation for Jordan. In the year 2000, exports from the QIZs were estimated at US$ 40 million, and were projected to more than double in the next two years.[31] As most of the factories established in the QIZs are labour-intensive industries requiring little skill, they are creating increased sources of employment for remote areas in Jordan where the QIZs are established. In this connection, it is important to note the restrictions imposed by Jordan on the employment of foreign labour, as foreigners should not exceed 35 per cent of the labour force in the company.

(ii) *The Jordan-United States free trade area*

The Free Trade Agreement between Jordan and the United States was completed in 2001. Both countries will reduce gradually customs duties over a 10-year period. The United States products not covered by the Agreement include cigarettes, alcoholic beverages and cars. Foreign companies are expected to take advantage of the Agreement to invest in Jordan, and to invest, in particular, in products that face high import duties in the United States market. The Agreement imposes a 35 per cent value added content of Jordanian origin; this is much higher than the 11.7 per cent imposed in the QIZ model. Despite the Free Trade Agreement, the QIZ model will still attract foreign investors, particularly those who have difficulties in meeting the requirements of the rule of origin of the Free Trade Agreement. In the short term, projects in the QIZ model also have the advantage of entering the United States market duty free, while in the long run (10 years after the implementation of the Free Trade Agreement), both models will have equal advantages with regard to exemption from customs duties.

C. Mergers and acquisitions and FDI

1. *Definitions*

A firm can undertake FDI in a Greenfield investment, or by acquiring or merging with an existing local firm. Cross-border mergers and acquisitions can be functionally classified as horizontal, vertical, and conglomerate mergers and acquisitions. Horizontal transactions make up the largest share—in value and number of deals—and are conducted between firms competing in the same industry. Conglomerate mergers and acquisitions are between companies in unrelated activities, whereas deals that fall into the vertical category are between firms in client-supplier or buyer-seller relationships. Cross-border portfolio acquisitions are deals that result in an acquisition of less than 10 per cent of a firm's voting shares, and thus do not constitute FDI-related mergers and acquisitions.

[29] Riad Al-Khouri, "Qualifying Industrial Zones (QIZs) as a model for industrial development: the case of Jordan and its implication for the ESCWA region," paper presented at the Expert Group Meeting on Review of Industrial Policies Aimed at Increased Productivity and Competitiveness within the Global Context, held in Amman from 14 to 17 January 2001.

[30] Access to Microfinance and Improved Implementation of Policy Reform (AMIR Programme), "Investment realization analysis for the Jordan Investment Board," draft report, Amman, April 2000.

[31] Euro-Jordanian Business Service Team, "Jordan – Foreign Direct Investment: Opportunities and Constraints," Draft report, Amman, January 2001.

2. *Impact on developing countries*

Even though in principle there is no reason to distinguish between the two, there are notable differences between cross-border mergers and acquisitions and Greenfield or conventional FDI (in this section referred to as FDI), in terms of the benefits and implications they bring to a host country. An acquisition, for instance, does not necessarily lead to capital formation, at least in the short run, if the new owner only makes the purchase without risking any additional investment. For this obvious reason, developing countries prefer FDI that increases fixed capital formation and consequently affects development and growth at a faster pace. Greenfield FDI is, by definition, an investment in new productive facilities.

Nevertheless, developing countries can benefit from mergers and acquisitions even if they do not create new assets. Among the benefits, cross-border transactions increase the total available funds that can be invested. They serve as a positive signal to foreign investors, inducing them to execute a conventional FDI project. They could enhance the productivity level in the host country, and they ultimately offer access to technologies that local firms do not possess. However, mergers and acquisitions can also lead to capital formation, even in the initial stages when new owners have to make additional investments in order to make their business profitable.

3. *FDI versus mergers and acquisitions*

Estimating precisely what share of FDI flows account for cross-border mergers and acquisitions is a difficult task. For instance, the value of cross-border mergers and acquisitions includes funds raised in local (and international) financial markets, which FDI data do not take into account. An acquisition, for instance, can be fully funded at the domestic level and thus the transaction is not entered as FDI. In other words, a merger and acquisition may, or may not, be considered FDI.

Box 4. Cross-border mergers and acquisitions in comparison with "conventional" FDI

- FDI through mergers and acquisitions does not necessarily create new assets, or add to the productive capacity of host countries (at least in the short run).
- FDI through mergers and acquisitions can be funded (financed) locally as well as internationally, and more so when operating in developed countries
- FDI through mergers and acquisitions can bring in capital faster
- FDI through mergers and acquisitions is less likely to transfer new and better technologies or know-how in the short run, but this is not necessarily true in the long run.
- The tax base is likely to expand under Greenfield FDI, which creates new businesses and subsequently a larger tax base.
- No employment increase is expected in the short run but, depending on performance and market demand, new jobs could be created in the long run with mergers and acquisitions.
- Mergers and acquisitions could reduce global competition if the acquiring firm were a part of a small number of firms at the global level.
- Host countries sometimes have policy instruments (and laws) that differentiate between FDI and mergers and acquisitions even though the overall FDI policy is not explicitly discriminatory.
- There is no clear difference with respect to the crowding in or out of domestic firms.

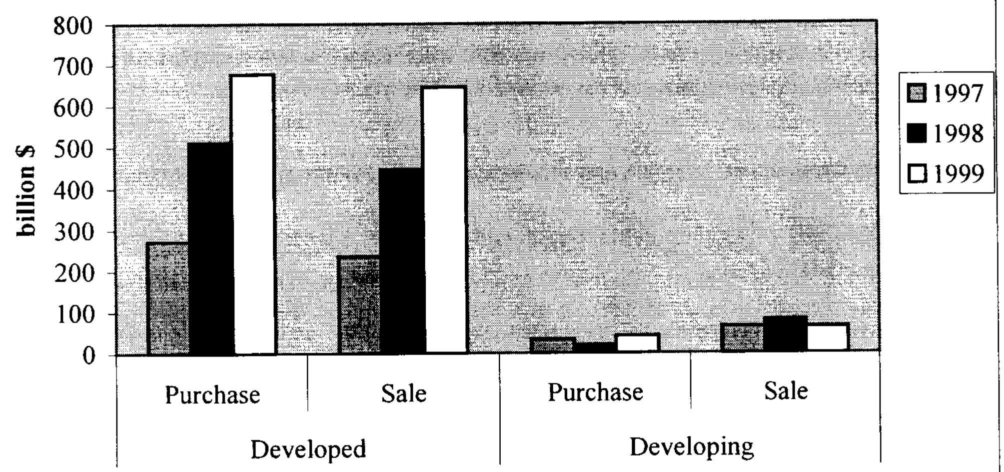
Source: UNCTAD, *World Investment Report*, 1998 and 2000.

4. *Global and regional trends*

Cross-border mergers and acquisitions—acquisitions more so than mergers—have increased significantly in the last decade, concentrating primarily in the developed world. For most of the 1990s, the share of cross-border mergers and acquisitions (in value and number of deals) out of the total mergers and acquisitions approached the 25 per cent mark. The absolute value of cross-border deals reached US$ 544 billion in 1998, a 60 per cent increase from the previous year. The growth rate is about 100 per cent for transactions resulting in the acquisition of a more than 50 per cent equity share.[32]

Developing countries provided only 11 of the 89 major deals struck in 1998, most of which were related to privatization. Among the top 50 mergers or acquisitions completed between 1987 and 1999, one Malaysian company acquired a German firm, and one United States company acquired an Argentinian firm. The remaining transactions were conducted among Japanese, North American, or West European countries. As with FDI flows, outward mergers and acquisitions (purchases - acquiring) for developed countries are larger than inward mergers and acquisitions (sale - being acquired), while the opposite is true for developing countries. In absolute terms, the trend is favourable to the developed countries, where the overwhelming majority of the transactions are taking place.

Chart 36. Mergers and acquisitions: global trends
(Developed and developing countries)



Source: UNCTAD, *World Investment Report 2000*.

Developing countries diverge from the path followed in developed countries, with conventional FDI in the developing countries increasing at a faster rate while mergers and acquisitions have either decreased or increased at a slow rate. The divergence is more significant for countries in developing Asia and Africa. Developing countries are attracting more conventional FDI than mergers and acquisitions because their regimes do not welcome foreign acquisitions. Even though the liberalization of FDI regimes often targets both FDI (directly) and mergers and acquisitions (indirectly), some developing countries have various "hindering" instruments that deal with mergers and acquisitions such as special authorizations. Cross-border mergers and acquisitions raise issues of competition policy.

5. *Determinants of mergers and acquisitions*

There are very few enterprises in the ESCWA region that are potential targets for mergers and acquisitions. Firms in the region are often small in size, overburdened with a labour surplus, and do not meet

[32] *World Investment Report 1999*.

international standards for good corporate governance (including transparency, incentives for managers, oversight of managers, and rights of minority shareholders). Exceptions to this are the utilities and telecommunication companies as well as other infrastructure projects. Privatization is in itself an acquisition transaction, and it is through this medium that developing countries get their share of revenues from worldwide mergers and acquisitions. Given the relatively small size of the economies of the ESCWA member countries, any merger and acquisition could have a significant impact on the host economy.

The promise of financial gain is the most important determinant of mergers and acquisitions, whereas economic and strategic reasons are much more influential in developed countries. Table 31 shows than even though non-financial gains are also important in developing countries, the gap between the two factors is smaller compared with the richer economies. In 1998, strategic motives were twice as important as financial motives in developing countries, while in developed countries strategic motives were 12 times as important as financial motives. In 1999, the gap was 7 in developing countries and 12 in developed countries.

The task facing developing countries is to make their economies strategically attractive and not be persuaded that mergers and acquisitions cannot be a tool to bring in foreign capital. Among the possible measures that can be taken, developing countries can join a regional bloc, restructure their enterprises and utilities, ensure long-term stability and continuity, and improve their overall investment climate.

TABLE 31. MOTIVATION BEHIND CROSS-BORDER MERGERS AND ACQUISITIONS, 1995-1999
(Billions of US dollars)

	Developed countries		Developing countries	
	Financial gains	Economic and strategic reasons	Financial gains	Economic and strategic reasons
1995	12.9	151.6	2.4	13.6
1996	19.6	169.1	7.1	27.6
1997	27.0	207.7	11.7	52.9
1998	33.1	412.1	25.9	54.9
1999	46.4	598.1	7.6	56.9

Source: UNCTAD, *World Investment Report 2000*.

6. *Conclusions: policy implications for the ESCWA region*

The data on the ESCWA member countries are, unfortunately, limited and very scattered. The Gulf countries, in particular the United Arab Emirates and Saudi Arabia, dominate the mergers and acquisitions market. Lebanon's mergers and acquisitions sales (inflows) amounted to US$ 168 million in 1997 and only US$ 11 million in 1998, compared with only US$ 150 million in FDI in 1997. The comparatively high level of mergers and acquisitions inflows registered in 1997 was due to one transaction, namely the Central Bank of Lebanon's divestiture of Crédit Libanais to a Saudi Arabian-led group. Jordan attracted only US$ 26 million in FDI in 1995 through mergers and acquisitions. As for Bahrain, the available data show that mergers and acquisitions accounted for US$ 4 million in 1993 and US$ 30 million in 1999.

The weak activity in mergers and acquisitions is due to a number of factors, namely the size and structure of firms in most of the ESCWA member countries. Another very important factor is the poor record in corporate governance (legislation and tradition), an area where the region could benefit a great deal from adopting international best practices. Finally, mergers and acquisitions activity often looks for an exit strategy, which is often the eventual listing on the stock exchange. In most countries in the region, the stock exchange is not well developed and suffers from poor capitalization and a shortage of liquidity.

TABLE 32. BEIRUT AND AMMAN STOCK MARKET OPERATIONS
(2000, second quarter)

	Lebanon	Jordan
Listed companies	13	161
Capitalization	US$ 1.7 billion	US$ 5.1 billion
Turnover rate of shares	66%	222%
Initial public offering	0	12

Source: Arab Monetary Fund, database on Arab securities markets, second quarter, 2000.

In many aspects, the Jordanian economy is not very different from most of the economies of the ESCWA region. The listed and traded companies are, by and large, small—at least by international standards (see table 33).

TABLE 33. SIZE INDICATORS FOR JORDANIAN FIRMS
(Millions of Jordanian dinars)

	1995	1996	1997	1998	1999
Capital of registered companies	460.1	768	206	191	138
Net profit of public companies (after tax)	192.5	226.4	207.1	240.2	171.5

Source: For registered companies, the Ministry of Industry and Trade; and for net profits, the *Amman Financial Market* and the *Jordanian Shareholding Guide* (www.cbj.gov.jo).

Note: US$ 1 = approximately JD 0.7.

What, if anything, can the ESCWA member countries do to promote mergers and acquisitions? First, there has to be a public awareness campaign on the importance of FDI—and, in particular, mergers and acquisitions FDI—to the economy in order to change the negative public perception of mergers and acquisitions, and of the "acquisition of the economy by foreigners." The Governments of the ESCWA member countries cannot have it both ways: on the one hand, bemoaning the country's poor economic performance and, on the other hand, refusing to embrace the full package of globalization. Secondly, as noted above, there is a need to review the legal and regulatory environment for doing business with a view to facilitating investments in general, and foreign investments in particular. Thirdly, the ESCWA member countries have to realize the importance of privatization as a key to FDI and to mergers and acquisitions FDI. Finally, the ESCWA member countries have to bring about a revolution in corporate governance in their domestic firms. Such a revolution is not only warranted to encourage mergers and acquisitions but is, in itself, the key to improved company performance.

VI. CONCLUSIONS AND RECOMMENDATIONS

1. The ESCWA member countries should consider strengthening the private sector and, where necessary, introduce privatization programmes geared to inject private capital into infrastructure development (telecommunications, electricity, roads and water). Those measures will also attract FDI and other forms of private investment, as privatization has been an important determinant of investment in emerging markets.

2. Developing the private sector within the framework of regional cooperation is increasingly seen as a means of drawing strength from the substantial investment and technology transfer offered by transnational corporations through FDI and non-equity forms of cooperation. Public-private sector partnerships could facilitate regular dialogue and sharing of experience, and could be effectively used in a number of cases to attract investment flows from transnational corporations, as well as other benefits.

3. The ESCWA member countries face, in addition to the deficiencies and shortcomings of the legal and institutional framework, particular challenges in attracting investment from transnational corporations and promoting business activities. One such challenge stems from the narrowness of these countries' respective domestic markets. The modernization of national legal and institutional frameworks for investment, through the introduction of international norms and standards, would inevitably lead to the harmonization of laws and regulations among the countries of the region. Such a development would greatly contribute to the emergence of an integrated market for investors, domestic and foreign. International and regional organizations should assist the member countries in harmonizing trade and investment policies at the regional level, modernizing national legal and institutional frameworks, and monitoring the enforcement of laws and regulations with regard to FDI.

4. One area in which the ESCWA member countries have not been very active, and which is extremely important to the promotion of FDI, is the promotion of the host country and the consequent development of a positive image of the country in international public opinion. The promotion of the host country in general should be addressed in tandem with the promotion of FDI. Investment promotion agencies need to identify and disseminate information on investment opportunities. These agencies should also improve the information provided to potential investors on the privatization programmes launched by the member countries in the ESCWA region.

5. International organizations are requested to assist investment promotion agencies in carrying out in-depth studies on ways and means to simplify administrative procedures for FDI entry and establishment and to introduce more transparency in the legal and institutional framework of investment.

6. There is a need to upgrade entrepreneurial skills of managers of national enterprises through capacity-building workshops and the setting up of networks of entrepreneurs. Strategic alliances between local firms and foreign companies should be fostered through subcontracting, joint ventures and other forms of cooperative arrangements.

7. Cross-border alliances and partnerships between transnational corporations, such as those involving FDI, are concentrated in particular industrial sectors, characterized by dynamic technology and information-intensive products and services.[33] This development is generally perceived as a negative one by countries whose domestic firms are not at the required level of technical sophistication. In fact, cross-border alliances and partnerships between transnational corporations create opportunities for these firms to upgrade their core competencies and become more competitive in world markets. In addition, strategic alliances cover a wide range of cooperative arrangements, from very specific technical services to subcontracting agreements. They also cover less formal, but still binding, modes of intercorporate cooperation. The ESCWA member countries can work on establishing an environment conducive to cooperative arrangements with transnational corporations, and by doing so assist their own firms in capturing global markets. They can also play a more proactive role in upgrading the wealth-creating capabilities of their enterprises and their competitiveness, bearing in mind that transnational corporations are seeking strategic assets. Experience shows that those

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[33] See J. Dunning, *International Enterprise and the Global Economy* (Wokingham [United Kingdom], 1993).

countries/areas where Governments have striven to provide the right environment for establishing cooperative arrangements (such as Japan, the Republic of Korea and Taiwan Province of China) are generally those that do the best in the global economy. There is a challenge here for the ESCWA member countries that has yet to be addressed.

8. The basic challenge for the authorities in the ESCWA member countries would be, in addition to the efforts aimed at improving infrastructures, to establish a clear, reliable and predictable legal framework for investment by transnational corporations, and other forms of their involvement, and to set up the necessary rules for competition, but then, as far as possible, to leave the private sector to its own devices. The role of the authorities would also include providing effective oversight and enforcement of the law, while avoiding unnecessary continuous and burdensome bureaucratic interference.

9. The Governments in the ESCWA region have gradually enforced protection of property rights and extended it to new spheres where it did not exist before, namely to the protection of intellectual property rights. Intellectual property rights and their proper enforcement are crucial for the development of FDI in the information and communication sectors, in the pharmaceutical industry, in the media and entertainment industries, in education, and in many other growth sectors where some of the world's largest multinational corporations operate. Intellectual property rights have become even more crucial in the "new economy" and in all activity related to the information and telecommunications sectors. For countries such as Egypt, Lebanon, and Jordan, effective enforcement of intellectual property rights is the key to the "new economy." The enforcement of intellectual property rights will also continue to constitute an important factor in decisions on FDI.

10. The ESCWA member countries need to liberalize trade on bilateral, regional, and multilateral levels and to conclude various investment treaties and double taxation avoidance treaties. While bilateral agreements are important, the greater economic potential can only be achieved through deeper Arab trade integration (the Greater Arab Free Trade Area), if that is ever faithfully implemented, combined with Euro-Mediterranean integration and multilateral integration within the context of the World Trade Organization.

Annex I

CHARACTERISTICS OF THE SAMPLE

(a) *Date of establishment*

More than two thirds of the sample in Jordan and Lebanon, and half of the sample in Bahrain, were established in the 1990s. The table below shows the distribution of the sample according to the period of establishment: before 1990, from 1990 to 1995 and after 1996.

DATE OF ESTABLISHMENT OF THE COMPANY
(In percentage of the sample)

	Jordan	Lebanon	Bahrain
Before 1990	23	20	50
1990-1995	23	20	32.4
1996-2000	54	60	17.6
Total	100	100	100

(b) *Share of foreign investment in total capital of the FDI enterprise*

More than three quarters of the companies selected in the sample in Jordan and Lebanon have more than 50% of foreign participation in total capital, against 57% in Bahrain, as indicated in the following table.

SHARE OF FOREIGN INVESTMENT IN TOTAL CAPITAL OF THE COMPANY
(In percentage of the sample)

Share (in per cent)	Jordan	Lebanon*	Bahrain
10-49	20	13.2	43
50	20	2.6	5.6
51-100	60	84.2	51.4
Total	100	100	100

* Only a total of 38 companies answered this question.

(c) *Nationality of the director of the company*

The directors of the companies of the sample are of foreign nationality in more than two thirds of the sample in both Jordan and Bahrain, and only one third in Lebanon.

NATIONALITY OF THE DIRECTOR OF THE FOREIGN COMPANY
(In percentage of the sample)

Nationality	Jordan	Lebanon	Bahrain
Foreigner	71.2	35	67.6
Local	28.8	65	32.4
Total	100	100	100

Annex II

QUESTIONNAIRE

Personal information of the interviewee

Name

Position

Period of stay in the country

General information on the company

Name

Tel
Fax
E-mail
URL

Date of establishment

Capital investment

Type of activity

Lifespan of venture
- □ 1 year
- □ 1-5 years
- □ More than 6 years

Information on foreign investment

Nationality of foreign investors

Share of foreign investment in capital

Management of the company

Director: foreign □ local □
Foreign staff in the management of the company:

Number:

Percentage in total management staff
Percentage of foreigners in total number of skilled workers

How difficult it is to get work permits for foreign staff? (1 being the most difficult)

1 2 3 4 5

Is having a local partner a legal requirement?

Yes No
□ □

Is there a local partner in this venture?

Yes No
□ □

Markets the company is serving, and share of each in total sales

	Share
□ Local market	...
□ Regional market	...
□ International market	...

Major reasons of interest of the foreign partner to invest in the country

Indicate the major reasons by order of importance (1 being the most important reason):

□ Size of the domestic market/size of purchasing power
□ Access to regional market
□ Access to world market
□ Sourcing of raw materials and other inputs
□ Availability of local skills
□ Low-cost labour
□ Existence of a technological base
□ Favourable incentive system (tariffs and taxes)
□ Existence of an entrepreneurial culture
□ Availability of a competent local partner
□ Other (specify)

Problems faced by the company in starting up activities in the country

Indicate problems (when it applied) by order of importance (1 being the most important)

□ Complex administrative procedures for registration of the company
□ Obtaining approvals to invest
□ Securing land or real estate
□ Access to information (legal, business and other)
□ Recruitment of human resources
□ Other (specify)

Indicate number of weeks required to get permit to start up activities

Indicate cost of permit

In case of the existence of a one-stop shop for registration of the company, indicate problems faced

Difficulties faced by the company in operating in the country

Indicate difficulties (when it applied) by order of importance (1 being the most important)

□ Administrative and bureaucratic procedures
□ Lack of transparency in administrative procedures

□ Customs procedures
□ Lack of qualified management staff
□ Lack of qualified skilled labour
□ High labour costs
□ Work ethic
□ Local suppliers (including poor quality of products and difficulties in dealing with suppliers)
□ Foreign exchange procedures
□ Capital and profit repatriation
□ Tax regulations
□ Unexpected changes in economic policies
□ Judiciary system and enforcement of contract
□ Infrastructure
□ Lack of adequate services: such as education and health
□ Difficulties arising from local partner inadequacy

Trade barriers

Indicate major trade barriers that hinder the operation of the company

□ Quantitative restrictions on imports
□ Customs procedures
□ Customs duties on imports
□ Technical barriers on imports
□ Complex procedures for export and re-export
□ Transportation restrictions
□ Other barriers (specify)

National treatment

Is there any discriminatory treatment vis-à-vis your company?

□ Ownership of land and property
□ Government procurement procedures
□ More delays for foreign investor to obtain necessary permits to start operations
□ Prior authorization for investment
□ Restrictions on activities that are confined to nationals only
□ Company law
□ Special treatment for multinational firms operating in ESCWA member countries
□ Other (specify)

Infrastructure

How do you consider infrastructure conditions in the country? (please rate from 1 to 5, 1 being the most adequate infrastructure)

Roads	1	2	3	4	5
Electricity	1	2	3	4	5
Airport	1	2	3	4	5
Seaport	1	2	3	4	5
Telecommunications	1	2	3	4	5
Internet services	1	2	3	4	5

How do you rate the cost of infrastructure services? (1 being the most expensive)

Electricity	1	2	3	4	5
Gas	1	2	3	4	5
Telecommunications	1	2	3	4	5
Land or real estate	1	2	3	4	5

Taxation and customs duties

How do you view the corporate tax rate?

Very high □ High □ Medium □ Low □ Very low □

How do you view the capital gains tax or any other pertinent tax?

Very high □ High □ Medium □ Low □ Very low □

How do you consider the customs tariff rate on raw materials and intermediate goods?

Very high □ High □ Medium □ Low □ Very low □

How do you consider the tax system in terms of clarity and transparency (please rate from 1 to 5, 1 being the most adequate)

1 2 3 4 5

How do you consider the tax system in terms of stability? (please rate from 1 to 5, 1 being the most adequate)

1 2 3 4 5

List only the other taxes that impose costs on foreign investors.

How do you see the practices related to tax assessment collection?

FDI admission/approval process

How complex are the procedures to approve the foreign investment?

Very complex □ Average □ Easy procedures □

How do you rate the flexibility (level of discretion) exercised by the bureaucrats in processing admission or approval of the foreign investment?

High □ Medium □ Low □

How do you assess the time period involved in processing admission/approval?

Long delay □ Average □ Short □

Country risks/Investment protection

List by order of importance (from 1 to 4, 1 being the most important) the following risk factors endangering your business:

□ Record of the host country in terms of expropriations and nationalizations
□ Legal safeguards against uncompensated services
□ Foreigners' rights to judicial review
□ Unpredictability (and corruption) of the judicial system
□ Availability of investment insurance against expropriation and political risks

Other investor concerns

Indicate one or more of the following concerns that may hinder your operations:

□ Protection of intellectual property rights
□ Anti-monopoly/competition laws
□ Labour laws and relations
□ Enforcement of contracts
□ Security and protection from crime and theft
□ Security from acts of violence (including terrorism and war)

General remarks

Compare the advantages this country offer with other countries where you had some experience.

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