4 Openness to foreign investment and recent liberalisation reforms

This chapter provides an overview of the main regulatory restrictions to foreign investment in the MENA focus economies, drawing on the OECD FDI Regulatory Restrictiveness Index (the Index). The Index gauges the level of restrictiveness of an economy's statutory measures on FDI in over 70 countries worldwide and in 22 sectors. Despite important reforms, MENA economies are on average more restrictive than other regions, potentially limiting FDI inflows and economy-wide productivity gains. This can have implications for MENA economies' stated objectives of economic diversification and participation in global value chains.

Summary and policy considerations

The attractiveness of MENA economies to foreign investors depend on myriad factors, including market size, geography, and crucially, the policies and institutions that support a coherent and predictable investment environment. As other chapters of this report explore in detail, the legal framework for investment (Chapter 3), the quality of infrastructure (Chapter 9), and policies to promote FDI (Chapter 6) and link foreign and domestic investors (Chapter 8) are all areas governments can influence not only to attract more FDI, but to enhance its positive benefits to society. For foreign investors, another important policy area concerns the rules governing their entry and operations in the host country. All governments impose some legal or regulatory restrictions on FDI, often in an effort to protect domestic industries or safeguard national security interests. But FDI restrictions involve economic costs, which can in turn lead to lower competition, forgone government revenues, and reduced opportunities for productivity spillovers.

The MENA economies covered in this report (MENA focus economies) vary substantially in their level of openness to foreign investors. Based on statutory FDI restrictions (those explicit in regulations or laws) as of year-end 2019, Egypt and Morocco are as liberal as OECD countries, while Libya and the Palestinian Authority impose wide-ranging *de jure* restrictions. On average, the eight MENA focus economies tend to be more restrictive than OECD and many non-OECD countries. However, several MENA governments have undertaken significant liberalisation reforms recently, recognising the role of FDI in creating jobs, enabling economic diversification and supporting participation in global value chains. For example, Jordan in 2016 revoked a minimum capital requirement imposed on foreign investors, expanded the sectors open to full foreign ownership and, in 2019, further eased restrictions in some service sectors. Tunisia in 2016 removed a requirement that foreign investors receive approval for equity stakes exceeding 50% of a firm's capital. In 2020, Algeria ended its most substantial restriction, a cap on foreign equity of 49% in all sectors.

Remaining statutory restrictions may nonetheless inhibit greater volumes of FDI as well as productivity gains from competition – crucial for a resilient recovery from the Covid-19 crisis. Like most countries, the MENA focus economies impose more restrictions in service sectors than in manufacturing. These sectoral restrictions are more severe and widespread than in peer countries, however, including in Southeast Asia and Latin America. Several MENA countries restrict foreign ownership in business, financial, distribution and transport services, all of which are key inputs for other sectors. Limiting foreign investment in such backbone services hinders competition and productivity in these sectors and the industries that rely on them, including manufacturing, in turn holding back potential productivity gains throughout the economy.

Even in instances where MENA governments have removed statutory limits on FDI, *de facto* restrictions may be prevalent. While not covered in this chapter, these include informal or institutional barriers to investment (such as excessive bureaucracy or corruption), state ownership, or inconsistent enforcement of statutory rules. In some MENA countries these *de facto* barriers have disproportionately benefited a small number of politically-connected firms (Diwan, Keefer and Schiffbauer, 2015[1]). When restrictions are used as a tool for crony practices, they inhibit competition between foreign and domestic investors, as well as among domestic firms. A more competition-friendly environment would allow for a better allocation of resources towards higher-productivity firms and enable new entrants to bring in new ideas and innovate.

Policy considerations

- Consider reassessing remaining regulatory restrictions to foreign investment, notably horizontal restrictions and those in service sectors, against their public policy objectives and, where relevant, streamline or remove them. Restrictions should also be reviewed against MENA governments' national development objectives (e.g. objectives of economic diversification or participation in global value chains). Where such policies are deemed necessary, ensure that they are not more restrictive than needed to address identified risks and concerns.
- Consider improving the legibility and transparency of the legal framework for foreign investors. Often details on discriminatory measures are not available in English or involve lengthy and frequently updated lists of open sectors, making it difficult for investors to understand prevalent rules. A negative list approach, where restricted sectors are clearly outlined (as in Jordan), could improve clarity.
- Ensure effective and clear implementation of the regulations governing the entry and operations of foreign investors. Fewer discretionary regulations on foreign firms' market entry, both *de jure* and *de facto*, would reduce undesirable practices, such as corruption and cronyism, and foster a more dynamic private sector.

FDI restrictions can inhibit investment and its economic benefits

An open and non-discriminatory international investment environment has long-term benefits. Investment is critical to spur economic growth and sustainable development. It expands the productive capacity of an economy and drives job creation and income growth. International investment can provide further advantages. Beyond bringing additional capital to a host economy, FDI can help improve resource allocation, production capabilities, and access to international markets. It can also act as a conduit for local diffusion of technological and managerial expertise (see Chapter 2 on FDI trends and benefits in the MENA region for empirical evidence on the how FDI contributes to sustainable development outcomes).

The potential benefits of FDI are mostly accepted across governments, and attracting FDI has become an important policy tool to finance development in many countries. Nonetheless, nearly all governments impose some legal or regulatory limits on foreign investors' entry and operations, often to shield domestic investors from foreign competition for purely economic reasons. FDI restrictions are also commonly motivated by concerns over the loss of national sovereignty to protect essential security interests. Governments often justify FDI restrictions to secure the proper functioning of the economy against threats of denial or disruption of the supply of critical goods and services to the economy (Moran, 2009[2]). National security is a legitimate concern, but should not be a cover for protectionist policies (see Box 4.1 for an overview of OECD guidelines regarding restrictions based on national security) (OECD, 2008[3]) (OECD, 2020[4]).

FDI restrictions should be used narrowly, and only as a measure of last resort, if other non-discriminatory measures cannot adequately mitigate the identified risks or concerns. Moreover, as described below, discriminatory policies may not always be optimal for tackling identified risks or concerns. Restrictions on foreign investment involve economic costs that can in turn lead to lower competition and productivity, forgone government revenues, and reduced opportunities for spillovers.

The FDI restrictions analysed in this chapter are discriminatory measures explicit in regulations or laws. There are, however, other *de facto* restrictions on foreign investors. These include institutional or informal barriers to investment (such as excessive bureaucracy or corruption), inconsistent enforcement of statutory rules, as well as distortions caused by state ownership of key sectors, and special regulatory treatment received by certain firms. In the MENA region, state-owned enterprises (SOEs) (either civil or military) dominate many sectors, and often receive preferential regulatory treatment, which if abused, can crowd out private sector activity (World Bank, 2018[5]) (OECD, 2019[6]).

Fair competition is also hindered when private firms with influential political connections benefit from formal or informal preferential treatment, creating barriers to foreign and domestic firm entry.[1] For example, there is evidence that politically-connected firms in Egypt were protected from competition through non-tariff import barriers, such as exclusive license requirements, prior to 2011 (Diwan, Keefer and Schiffbauer, 2015[1]). Other benefits received by politically-connected firms in several countries in the region include preferential access to land or government contracts, favourable tax treatment, or non-uniform application of doing business procedures (World Bank, 2015[7]) (Atiyas, Diwan and Malik, 2019[8]). Though not covered in this chapter, these other restrictions, and crucially the enforcement of statutory restrictions, play a key role in the overall investment climate (Kalinova, Palerm and Thomsen, 2010[9]).

Box 4.1. OECD Investment Policy Principles and Guidelines for Recipient Country Investment Policies Relating to National Security

The OECD Investment Committee has been a forum for intergovernmental dialogue on how governments can reconcile the need to preserve and expand an open international investment environment with their duty to safeguard the essential security interests of their people. As the custodian of key international investment instruments – the *Code of Liberalisation of Capital Movements* and the *Declaration on International Investment and Multinational Enterprises* – the Organisation has overseen progress in liberalisation for more than 40 years.

Three principles underpin these instruments: transparency, liberalisation and non-discrimination. The non-discrimination principle sets out that all investors in like circumstances are treated equally, irrespective of their ownership. **National treatment** requires that a government treat foreign-owned or -controlled enterprises no less favourably than domestic enterprises in like situations.

OECD members and other participating governments have developed additional guidance for the one exception to non-discriminatory investment policies provided for in these instruments – that governments may take measures they “consider necessary to protect essential security interests” and to maintain “public order or the protection of public health, morals and safety”. Investment policy measures addressing essential security interest should follow three principals:

1. Transparency and predictability: Information on restrictions on foreign investment should be comprehensive and accessible to everyone. While it is in investors’ and governments’ interests to maintain confidentiality of sensitive information, regulatory objectives and practices should be made as transparent as possible so as to increase the predictability of outcomes.
2. Proportionality: Restrictions on investment, or conditions on transaction, should not be greater than needed to protect national security and they should be avoided when other existing measures are adequate and appropriate to address a national security concern.
3. Accountability: Procedures for parliamentary oversight, judicial review, periodic regulatory impact assessments, and requirements that decisions to block an investment should be taken at high government levels should be considered to ensure accountability of the implementing authorities.

Source: (OECD, 2008[3])

Common statutory FDI restrictions and their economic costs

In most countries foreign equity limits, usually in specific sectors, are the most prevalent form of FDI restriction. This is the case among the MENA focus economies, with the exception of a few countries that apply wider restrictions across all or most sectors (Algeria, Libya and the Palestinian Authority, detailed below). The rational for equity limits, beyond national security concerns, is usually to protect domestic investors from foreign competition, or to push domestic investors to upgrade by forcing linkages between foreign investors and the host economy. The benefits of FDI to host economies are indeed partly associated with their spillovers to domestic firms, particularly knowledge transfers. Governments expect foreign equity limitations or joint venture requirements to facilitate such spillovers by strengthening interactions between domestic and foreign firms (see chapter 8 for other policies to promote linkages).

Such foreign equity conditions may not necessarily achieve their intended purpose. The exercise of control over foreign operations is one key underlying characteristics of foreign investment by multinational firms. Ownership restrictions limit investors' ability to exercise this control, possibly affecting their decision to invest in the first place. Foreign equity restrictions can also limit the potential financial and economic gains of a project. Foreign investors may be reluctant to enter into a joint venture with local investors, including because it may be difficult to find suitable local partners with the required capacity and skills. Investors might not want to share new technology and production techniques with these local partners, thereby limiting spillovers (Moran, Graham and Blomström, 2005[10]).

Screening and approval mechanisms are another common means to regulate the entry and behaviour of foreign investors, though their use has declined substantially in the past three decades (Mistura and Thomsen, 2017[11]). Discriminatory screening involves approval requirements for foreign investors beyond licensing or permit rules for domestic investors. Some countries screen FDI projects horizontally across all sectors, such as Tunisia before reforms in 2016; others screen only specific strategic sectors, or large projects (above a certain investment threshold). Governments that impose screening measures argue that they help to keep out potentially harmful projects to consumers or the environment, and ensure that projects generate the maximum potential benefit for the local economy, in terms of employment, R&D, or technology or managerial spillovers. What distinguishes screening from other licensing and authorisation processes is its discriminatory nature against foreign-owned investments. For this reason, screening based on economic criteria is listed as an exception to national treatment in international agreements and under the OECD Declaration and Decisions on International Investment and Multinational Enterprises, as well as a reservation under the OECD Code of Liberalisation of Capital Movements. Screening which is exclusively for considerations of national security is listed for transparency purposes under the Declaration (Box 4.1).

Screening requirements can dissuade foreign investors, however, as they create unpredictable and costly barriers to entry. Criteria for approving investors, such as national interest, are often vague or left undefined. Conditions imposed can be arbitrary, inconsistent and non-transparent, creating restrictions that are discretionary and sometimes fairly stringent, such as limitations on foreign shareholding, forced technology transfer and asset divestment. Approval mechanisms also impose administrative costs to the government and investors.

Other barriers to FDI, including restrictions on employment of foreign key personnel, land acquisition by foreigners, or limits on the repatriation of profit and capital, also affect the profitability or structure of the business activity. As such, even when governments justify these restrictions by policy concerns, they raise transaction costs for foreign-owned firms relative to competing locations, and may negatively influence firms' investment decisions (Mistura and Roulet, 2019[12]). Alternative policy instruments may be better suited to achieve certain goals.

By potentially dissuading foreign investors, FDI restrictions also reduce competition, thereby inhibiting sectoral and even economy-wide productivity gains. In the MENA region, weak private sector competition, marked by the prevalence of a few dominant firms, is one the main impediments to more dynamic job and firm growth.[2] FDI restrictions can limit domestic as well as foreign firm entry and further entrench market power of select businesses. Under the pre-2011 government in Tunisia for example, firms connected to the government were more prevalent in sectors restricted to foreign investors under the previous 1993 Investment Code. There is evidence that these firms performed better than peers, in terms of market share and profit, largely because of these entry regulations, effectively crowding out competitors (Rijkers, Freund and Nucifora, 2017[13]).

Beyond the types of restrictions in place, the legibility and transparency of laws and regulations on FDI also affect investors' entry (See chapter 3 for more details on the importance of a coherent investment policy framework). In the MENA region, details on discriminatory measures often involve lengthy and frequently updated lists of un-restricted sectors, making it difficult for investors, particularly smaller firms with fewer resources, to understand prevalent rules. A more transparent and predictable approach involves a "negative list", whereby all foreign investment projects are authorised without any discriminatory conditions, except specific sectors or sub-sectors clearly outlined in the negative list. Among the MENA focus economies, Jordan has a negative list, and Tunisia and Algeria are in the process of adopting this approach. When a negative list is used, however, it is important that the list is publically available, with sufficient detail on the sectors involved, and easy to understand. A long delay between the publication of legislation authorising a negative list and the details of the list, as occurred in Tunisia, can confuse and hold up investors, adding an additional hurdle on top of the restriction itself.

MENA economies tend to be more restrictive than their peers

Despite the economic costs of these measures, nearly all governments impose some restrictions on foreign investors. The OECD *FDI Regulatory Restrictiveness Index* allows for a comparative assessment of statutory FDI restrictions in over 70 countries across four main types of FDI restrictions (Box 4.2). In the MENA region, Egypt, Jordan, Morocco and Tunisia are adherents to the OECD *Declaration on International Investment and Multinational Enterprises*. As such, they commit to accord national treatment – to treat foreign-owned or -controlled enterprises operating on their territory no less favourably than domestic enterprises – subject to a list of exceptions. These countries' scores on the *Index* reflect their reported list of exceptions to national treatment under the OECD National Treatment Instrument, updated yearly.[3] Scores for Algeria, Lebanon, Libya and the Palestinian Authority reflect the results of a questionnaire completed by relevant authorities, supplemented by a comprehensive legal review of the relevant legislations of each economy by the OECD secretariat.

FDI restrictiveness varies greatly across countries and regions (Figure 4.1). OECD economies are among the least restrictive, while large countries, resource-rich economies and countries in the Asia-Pacific region tend to be more restrictive. The eight MENA focus economies are on average more restrictive than most countries covered by the *Index*, but there is considerable variation among them. Morocco and Egypt impose foreign investment restrictions that are close to the average level of restrictions in OECD countries. Algeria, Libya and the Palestinian Authority, however, have the highest levels of restrictions of all economies covered by the *Index*. Jordan also imposes restrictions that are on the upper end of the spectrum, while Tunisia and Lebanon's restrictions are close to the average for non-OECD economies covered by the *Index*.

The high scores of the most restrictive MENA economies are largely driven by horizontal restrictions applied across various sectors to all or most foreign investors. Among the most stringent measures is Palestinian Authority's prohibition of majority foreign ownership across sectors with few exceptions (e.g. manufacturing, banking, hotels and restaurants). Until recently, Algeria restricted foreign ownership to less than 50% of the firm's equity in all sectors, but the government lifted this restriction in 2020. Libya prohibits foreign investment in a relatively long list of sectors. It also restricts entry by requiring foreign investors to carry out business through joint-ventures with minority foreign shareholding or wholly-owned greenfield specific investment vehicles, subject to government approval and discriminatory minimum capital requirements. Except for Libya, none of the MENA focus economies apply economy-wide screening measures to regulate the entry of foreign investors, though some governments impose discriminatory approvals or criteria for admitting foreign investment in certain sectors, or in some cases both.

Box 4.2. The OECD FDI Regulatory Restrictiveness Index

The OECD *FDI Regulatory Restrictiveness Index* gauges the restrictiveness of an economy's FDI rules. The FDI *Index* is currently available for more than 70 economies, including all OECD and G20 members, allowing comparison of FDI policies and identification of potential areas for reform. It is commonly used on a stand-alone basis to assess the restrictiveness of FDI policies when reviewing candidates for OECD accession and in OECD Investment Policy Reviews, including reviews of new adherent countries to the OECD *Declaration on International Investment and Multinational Enterprises*.

The *Index* does not provide a full measure of an economy's investment climate as it does not score the actual implementation of formal restrictions and does not take into account other aspects of the investment regulatory framework, such as the extent of state ownership and other institutional and informal restrictions that may also affect the FDI climate. Nonetheless, FDI rules are a critical determinant of an economy's attractiveness to foreign investors; the index, used in combination with other indicators measuring the various aspects of the FDI climate, may help to explain variations among economies in attracting FDI.

The FDI Index covers 22 sectors, including agriculture, mining, electricity, manufacturing and main services (transports, construction, distribution, communications, real estate, financial and professional services). For each sector, the scoring is based on the following elements:

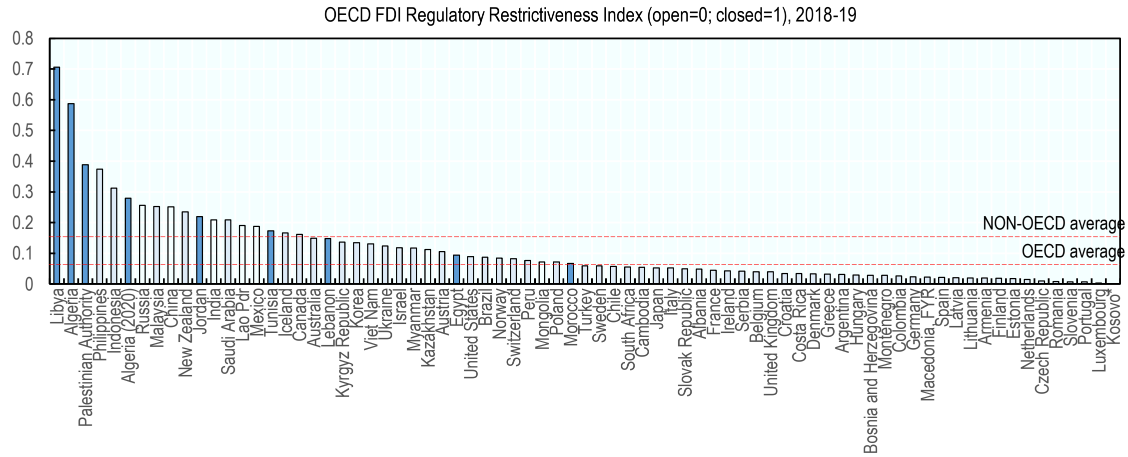
- the level of foreign equity ownership permitted
- the screening and approval procedures applied to inward foreign direct investment
- restrictions on key foreign personnel (e.g. CEO, technical expert)
- other operational restrictions (e.g. land ownership, branching, profit repatriation).

Restrictions are evaluated on a 0 (open) to 1 (closed) scale. The overall restrictiveness index is the average of the 22 individual sectoral scores. The discriminatory nature of measures, i.e. when they only apply to foreign investors, is the central criterion for scoring a measure. State ownership and state monopolies, to the extent they are not discriminatory towards foreigners, are not scored. For OECD and non-OECD country adherents to the OECD *Declaration on International Investment and Multinational Enterprises*, the measures taken into account by the Index are limited to statutory regulatory restrictions on FDI, as reflected in their list of exceptions to national treatment and measures notified for transparency under OECD instruments, without assessing their actual enforcement.

For non-OECD economies, information is collected through Investment Policy Reviews or, when not in the review process, through a dedicated questionnaire. Regulatory information is updated on a yearly basis following the monitoring of investment measures carried in the context of OECD Freedom of Investment Forum for participating economies, and on the basis of ad hoc monitoring for the remaining ones.

Source: (Kalinova, Palerm and Thomsen, 2010[9])

Figure 4.1. OECD FDI Regulatory Restrictiveness Index (MENA 2019)



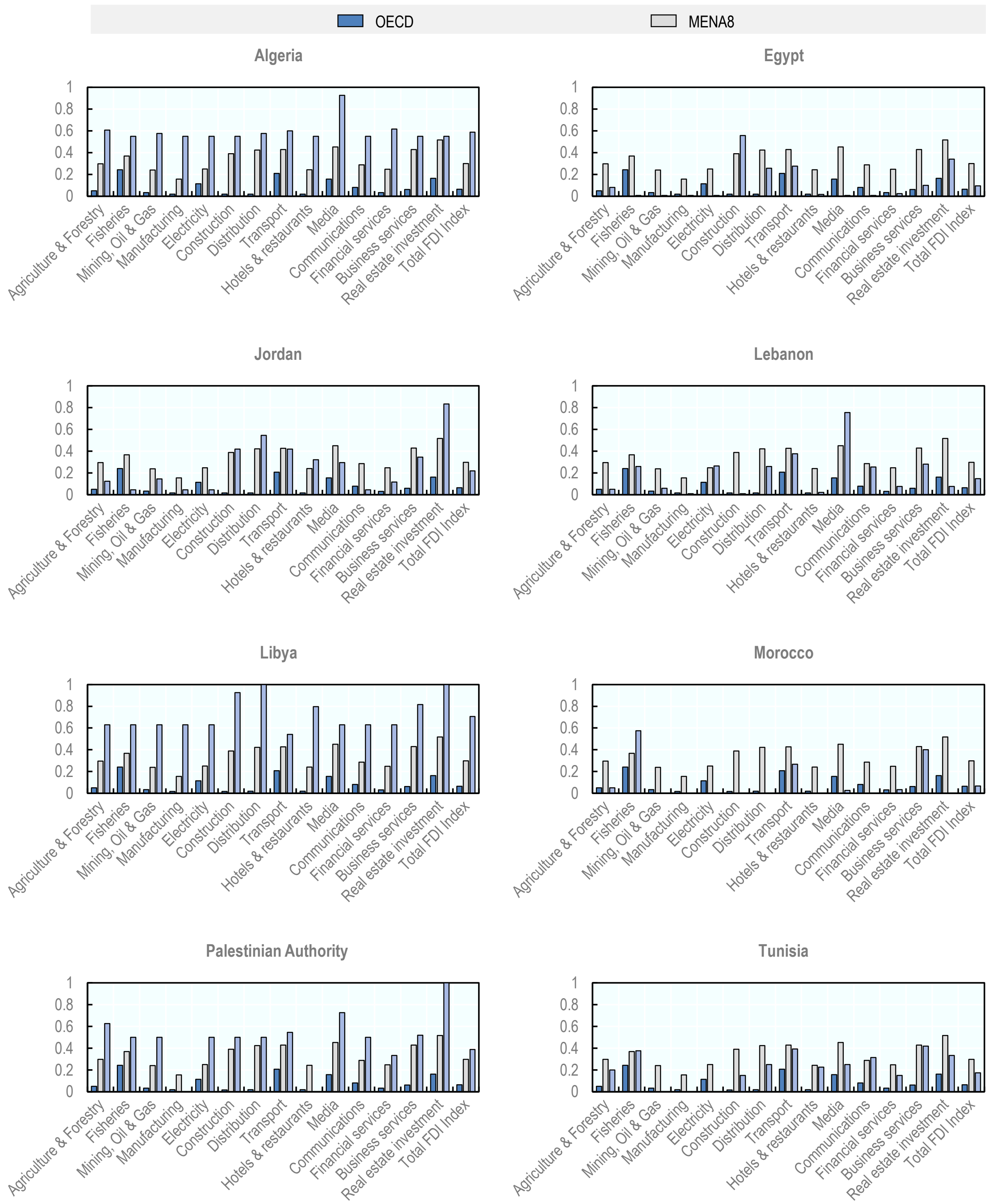
Note: The OECD FDI Regulatory Restrictiveness Index only covers statutory measures discriminating against foreign investors. The implementation of regulations, restrictions related to national security, state monopolies, preferential treatment for export-oriented investors and special economic zone regimes are not considered. Data reflect regulatory restrictions as of December 2019 for the MENA8 countries and 2018 for all others.
Source: OECD FDI Regulatory Restrictiveness Index (database), www.oecd.org/investment/fdiindex.htm.

Other horizontal restrictions among the MENA focus economies include limits on foreign land ownership – Lebanon and Jordan require approvals for land purchases for business use by foreigners – and preference to domestic firms in government procurement – applied in Algeria, Jordan and the Palestinian Authority. Algeria also maintains conditions for the repatriation of profits by foreigner investors, guaranteeing free transfer of capital only to those investments above a minimum threshold.

Aside from these horizontal restrictions, sector-specific limits on foreign equity ownership are the most prevalent forms of discrimination against foreign investors among the MENA focus economies (Figure **4**.2). This is also the most common restriction in most countries covered by the *Index*. Also like most countries, the MENA focus economies impose more restrictions in service sectors than in manufacturing, which is for the most part open to foreign investors (except when horizontal restrictions are in place). Sectoral restrictions are more severe and widespread than in peer countries, however, including in Southeast Asia and Latin America. Limiting foreign access to certain sectors holds back potential economy-wide productivity gains.

By hindering competition in service sectors, for instance, restrictions consequently raise costs of service inputs, such as financing and logistics, for other economic sectors. Empirical studies demonstrate the negative relationship between manufacturing productivity levels and barriers to competition or foreign participation in services sectors (OECD, 2015[14]) (OECD, 2018[15]). Market access reform allow for more competition in service sectors, and consequently, higher productivity. This in turn allows downstream manufacturers to benefit from higher quality or low cost services inputs, key to moving manufacturing up the value chain (see Chapter 8 on enabling SME linkages with foreign firms in global value chains). Among the MENA focus economies, restrictions on business, financial, distribution and transport services – all key inputs for all other sectors – are common. These sectors tend to be mostly open to foreign investors in OECD and many Latin American countries, with the exception of some limited restrictions in transport. The restrictions on foreign investment in these services in the MENA region are also higher than in other emerging markets, including ASEAN countries, particularly in distribution and business services, though there is wide variation in restrictions among ASEAN members (OECD, 2020[16]).

Figure 4.2. OECD FDI Regulatory Restrictiveness Index by sector (MENA 2019)



Note: see Figure 4.1 note.

Source: OECD FDI Regulatory Restrictiveness Index (database), www.oecd.org/investment/fdiindex.htm.

Sectoral foreign equity restrictions among the MENA economies include:

- Business & financial services: Foreign ownership in legal services is restricted in Lebanon and Tunisia. Tunisia and Jordan place some restrictions on engineering, and Jordan limits foreign control of scientific and technical consulting firms. Foreign ownership in architectural, accounting and auditing services is limited in Morocco. Algeria, Lebanon, Jordan and Tunisia restrict foreign equity in some financial services.
- Distribution: Wholesale trade and retail is open only to domestic firms in Egypt, Libya and the Palestinian Authority. Jordan and Lebanon restrict foreign equity ownership in distribution services to under 50%. Majority ownership by foreigners in distribution enterprises in Tunisia is subject to prior government authorisation
- Transport: Algeria, Egypt, Jordan, Lebanon, Morocco and Tunisia place limits on foreign ownership in air and maritime transport. Jordan also restricts foreign equity control to less than 50% in rail and road transport, and Lebanon limits foreign ownership in land cargo transport. Libya prohibits foreign investment in road transport and auxiliary transport services in ports.
- Agriculture: Algeria and Palestinian Authority prohibit foreign ownership of most agricultural land (although the Palestinian Authority allows long-term leases). Algeria also prohibits foreign investment in the production, use, transport, import and export of certain agricultural products. While Morocco allows foreign investors to lease agricultural land, outright ownership is prohibited, though a proposed law may revise this restriction.
- Real estate: real estate investments by foreigners are in many cases prohibited in Jordan, Libya and the Palestinian Authority.
- Construction: foreign equity in construction is limited to under 50% in Egypt and Jordan. In Tunisia, foreign majority investments are subject to prior government authorisation.
- Fisheries: foreign investments in fisheries prohibited in Morocco and limited to minority interest in Lebanon.

Some MENA countries also place restrictions on key personnel and other operations. For example, Lebanon requires that nationals make up the majority of boards of directors of joint-stock companies, and joint-stock companies are mandatory in several service sectors, including insurance, banking and finance. Business services, including auditing, accounting and insurance, are subject to personnel requirements or reciprocity agreements in several MENA economics, including in Algeria, Tunisia and the Palestinian Authority.

Several MENA governments have removed important FDI restrictions

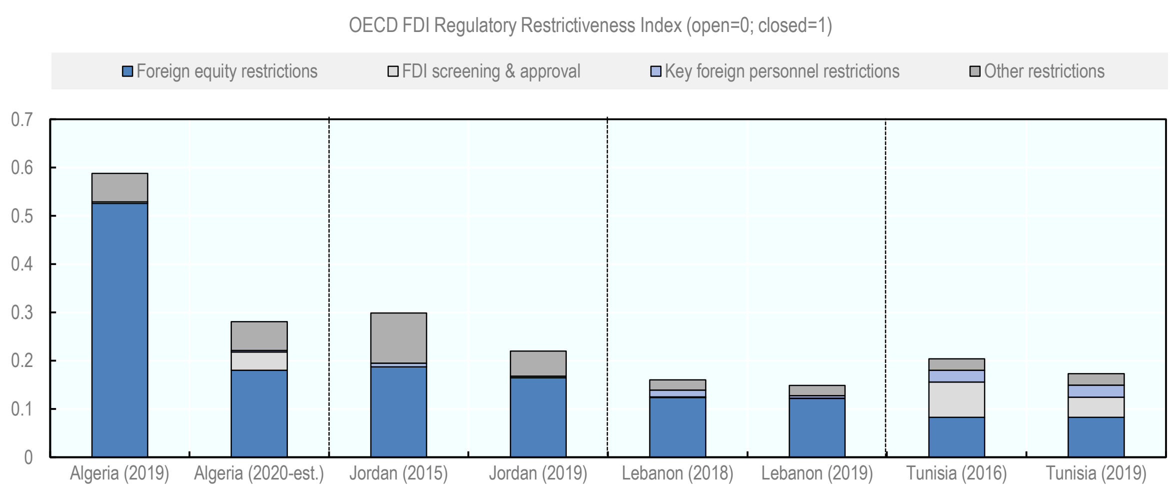
While FDI restrictions remain prevalent across the MENA focus economies, some governments have implemented important reforms in the past several years to ease discriminatory measures against foreign investment. As mentioned above, Algeria recently took steps to remove its most significant restriction, the cap on foreign ownership to 49% of a firm's equity in all sectors. The 2020 Finance Law provides that foreign equity restrictions apply only in sectors of national strategic interest and for distribution services. Strategic sectors listed in the law include: minerals, energy, military industries, airports, railroads, ports, and pharmaceuticals (Government of Algeria, 2020[17]).

Jordan has also eased some of its horizontal restrictions on FDI. In 2016 it removed the minimum capital requirement for foreign investors (Regulation No.77). The measure placed foreign investors at a disadvantage to Jordanian competitors in low-capital industries, such as knowledge-based sectors, and likely diminished Jordan's competitiveness compared to other countries where capital requirements are mostly non-existent or much less burdensome. The previous capital requirement was substantially greater than non-discriminatory capital requirements (applied to both domestic and foreign investors) in OECD countries and large emerging countries including China, Indonesia, India and Russia (OECD, 2018[18]). The 2016 reform also expanded the sectors open to full ownership by non-Jordanians. In 2019, Jordan further eased restrictions placed on foreign investors in certain services activities, including construction, distribution, transport and media (Regulation No. 80 of 2019).

Tunisia also removed a significant FDI restriction in its 2016 Investment Law. Previously, foreign investment required prior approval if foreign equity exceeded 50% of a firm's capital, except in the case of fully export-oriented activities, which were exempt from such requirement (OECD, 2012[19]). The 2016 law removed this requirement, guaranteeing national treatment for foreign investors with few exceptions, notably in sectors where foreign equity conditions apply and those subject to obtaining a foreign merchant card (Government of Tunisia, 2018[20]). Other recent reforms in the region include a 2019 amendment to Lebanon's Code of Commerce partly easing the restriction on foreign personnel on boards of directors of Lebanese Joint Stock Companies (Law No.126 of 29/03/2019).

These reforms are important steps towards a more open and predictable investment framework for foreign companies (see Chapter 3 on Legal Reforms for more examples of investment-related legislative reforms in the MENA region). Jordan and Tunisia's liberalisation measures have changed their positions on the *Index,* and are now closer to the non-OECD average. Algeria's position is likely to change in next year's *Index* (2020) as per simulated results below (Figure 4.3). However, barriers to FDI in the three continue to be greater than in the average OECD and non-OECD country. Algeria and Jordan remain among the most restrictive of the MENA focus economies. Even for MENA countries more open to foreign investment, the effects of remaining restrictions on both inward investment and economic development can be sizable.

Figure 4.3. Tracking FDI reforms in Algeria, Jordan, Lebanon and Tunisia

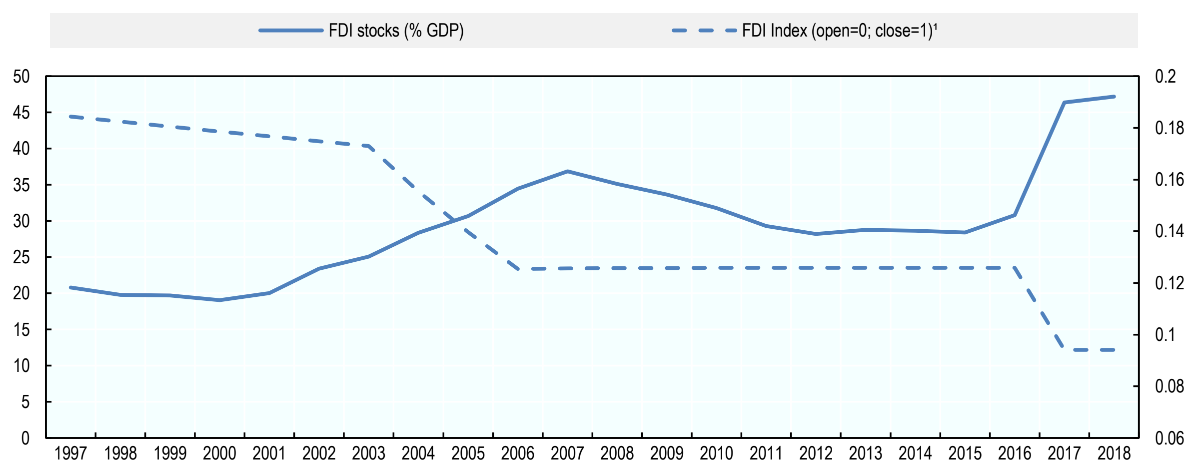


Note: The above results reflect regulatory changes introduced by mainly: (1) Algeria: Finance Law No. 20-07 of 2020; (2) Jordan: Regulation No. 77 of 2016 on non-Jordanian investors, and its revision by Regulation No. 80 of 2019; (3) Lebanon: Law No. 126 of 2019 modifying certain provisions of the Lebanese Code of Commerce (No. 304 of 1942); (4) Tunisia: Investment Law No. 2016-71 of 2016 and Government Decree No. 2018-407 of 2018 related to the issuance of the exclusive list of economic activities subject to licensing and the list of administrative licenses to complete a project and to control and simplify the relevant provisions and simplify them.
Source: OECD FDI Regulatory Restrictiveness Index (database), www.oecd.org/investment/fdiindex.htm.

Egypt's own experience seems to confirm that foreign investors respond favourably to regulatory reforms that level the playing field for all investors. Liberalisation reforms in the early 2000s corresponded with a significant rise in inward FDI, though global FDI flows also rose during this period (Figure 4.4).

Even partial restrictions to FDI can inhibit investment. Recent OECD research shows that liberalisation reforms can have a sizable and significant effect on FDI (Mistura and Roulet, 2019[12]). Reducing the level of FDI restrictiveness, as measured by the *Index*, by 10% could lead to 2.1% increase in bilateral FDI inward stocks on average, all else held equal. If this average effect were to apply equally across all countries, the more restrictive economies could expect FDI stocks to be between 7 and 95% higher if they were to ease FDI restrictions to the OECD average level. Egypt, for example, could expect its FDI stocks to be up to 37% higher (OECD, 2020[21]). The magnitude of the impact of liberalisation reforms on FDI would in practice vary between countries, but the estimation gives a sense of how restrictions act as barriers to investment. Foreign equity limitations appear to have the greatest effect on FDI, followed by screening policies (Mistura and Roulet, 2019[12]). The persistence of both forms of restrictions across the MENA focus economies suggests that there is substantial room for FDI growth if governments continue to advance liberalisation reforms.

Figure 4.4. Co-movement of liberalisation reforms and FDI stocks in Egypt



Note: Index scores linearly interpolated over missing periods
Source: (OECD, 2020[22])

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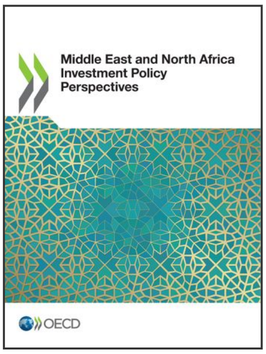
Notes

[1] Connections to the state can be formalised by current or former members of government on board, or involve more informal connections (such as family or other close personal relationships). For more details on privileged firms and their impact on economic growth see, (World Bank, 2015[7]), (Atiyas, Diwan and Malik, 2019[8]) (compilation of analysis on the region, Egypt, Morocco, Lebanon, Tunisia and Jordan); (Diwan, Keefer and Schiffbauer, 2015[1]) (Egypt); (Rijkers, Freund and Nucifora, 2017[13]) (Tunisia).

[2] See, among others: (OECD, 2020[21]), (World Bank, 2018[5]), (World Bank, 2015[7]), (Malik and Awadallah, 2013[23]).

[3] The National Treatment obliges adhering countries to notify their exceptions to National Treatment and establishes follow-up procedures to deal with such exceptions in the OECD.



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