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AN EMPIRICAL ANALYSIS OF FOREIGN DIRECT INVESTMENT IN LIBYA: LOCATIONAL DETERMINANTS AND LOCAL BACKWARD LINKAGES

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A thesis Submitted to the University of Huddersfield

in partial fulfillment of the requirements for

the degree of Doctor of Philosophy

The University of Huddersfield

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Abstract

The role of foreign direct investment (FDI) has been increasingly important as a mean of transferring technology and innovation from developed countries to developing ones. It has made a significant contribution to development and economic growth in host countries by allocating resources from wealthy countries to be transferred to those experiencing scarcity, allowing host countries to invest in activities beyond their domestic saving capabilities. Understanding the relationships of foreign investment with domestic suppliers, and what determines investment location choices, can help dictate the consequences of implementing passive, as opposed to active, FDI policies by host country governments, as well as providing the tools for FDI agencies to formulate their strategies. The main focus of this research is to determine the factors that most encourage and discourage FDI in Libya, to identify the different requirements of each type of FDI by applying different characteristics, like nationality, industry type, and ownership, and to examine the relationship between the foreign companies and the domestic suppliers. To capture these relationships in sufficient depth, the host countries' locational determinants were analysed, these influenced the choice of FDI. These locational determinants, such as economic and investment policy, market conditions, facility and utility, financial and legal and institutions were developed based on an extensive review of the relevant theoretical and empirical literature.

Primary data were collected by means of a survey questionnaire from 74 foreign-owned and joint-venture companies and 20 face-to-face interviews with senior managers of these companies, and Libyan government senior officials, in order to gain a more in-depth understanding of their responses and to investigate the difficulties and challenges facing government bodies tasked to improve the Libyan business environment. Principal Component Analysis (PCA) with Varimax rotation was used for unidimensionality conditions. Multivariate analysis of variance (MANOVA), chi-square and cross-tabulation tools, then, were applied as statistic tools, while a thematic technique was employed to conduct an interpretative analysis of the interviews.

The research found that in the sample, six out of eleven determinant factors were considered as encouraging incentives (economic situation, market conditions, natural resources, tax exemptions, skilled labour and semi-skilled labour), these are needed for FDI in Libya, in line with the literature. The remaining five factors (government regulation, domestic infrastructure, and research development as well as financial, legal and judiciary systems), were found to be discouraging factors. When applying moderators to the model, the result reported that factors encouraging/discouraging FDI were different in all groups. Results also showed that there are many challenges facing Libyan policy-makers aiming to reform the business environment in order to make it more attractive for FDI. In general, foreign companies have developed limited backward linkages with domestic suppliers which need to be improved and made more competitive in order to be of real benefit to local companies. The policy implication of this finding is that for Libya to be a more attractive market for future FDI, urgent and decisive reforms are needed in the issues which inhibited FDI inflows, and the incentives provided should be restricted to and designed for targeted specific FDI only, in order to gain desirable benefits and promote the spillover.

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Dedication

I dedicate this work to:

The memory of my father;

My mother, brothers and my daughters,

then to all those interested in issues of investment and economic development.

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Statement of Originality

I hereby certify that all of the work described within this thesis is the original work of the author. Any published (or unpublished) ideas and/or techniques from the work of others are fully acknowledged in accordance with the standard referencing practices.

Chapter 1

Introduction

1.1 Background to the Study

It is important to understand the reasons and background of foreign direct investment (FDI) decisions, in order to be able to determine how the host country attracts foreign investors through economic policy measures. It is also essential to understand the expectations of foreign investors and how they view investment in Libya. The increased interest in FDI began after the international debt crisis of the early 1980s particularly affected developing countries, leaving some, like those of Latin America, unable to repay their foreign debts to their international creditors (World Bank and IMF). The accumulation of these debts coupled with their high interest rates led to an ever-increasing negative financial gap, with mounting government expenditure on debt and decreasing revenues from private investment and savings, together with greater imports than exports, creating a deficit in the balance of payments for these countries (Siddiqui, 1996). Finding alternative sources of international funds became an urgent necessity for these indebted countries needing to fill this deficit. Private foreign investment was viewed as the preferred choice, due to its advantages for balance of payment over other types of loans; equity investment requires payment only when it earns a profit whereas debt requires payment irrespective of the State economy. Moreover, host countries can control the terms of this payment whereas those for servicing debts are set by the international market. Earnings from foreign investment are frequently reinvested and only partly repatriated, whereas debts accumulate interest. In addition, in the case of foreign investment, the exchange rate and commercial risks are passed on to the investors rather than being borne by the host government (Moran, 2006). Furthermore, FDI is generally considered to be desirable for host countries, especially in emerging markets. The Asian debt crisis of 1997 provided a good example of FDI being a more stable source of capital

compared to other types, such as loans and portfolio investment (Lipsey, 2001). The importance of FDI increased following the establishment of the World Trade Organisation (WTO) in 1995, which came as a result of increasing global production and the growing importance of Trans-National Corporation roles as catalysts for economic growth and internationalization.

Nowadays, FDI has become one of the most important sources of capital for both developed and developing countries. This has made significant contributions to development and economic growth in many host countries by re-allocating resources from wealthy countries to those experiencing scarcity, allowing host countries to invest in activities beyond their domestic saving capabilities (Lipsey, 2001; Dimelis and Louri, 2002; Chang, 2010; Balasubramanyam *et al,* 1996; Romer, 2010); Wu and Zhang, 2010).

Furthermore, FDI not only supplies developing countries with the required capital but also provides support for an improved economic growth rate for the host country (Jones, 2006), development of human capital through transferring modern technology, skills, know-how and enhancing the efficiency of management methods which raises the efficiency of production and the subsequent increase of exports and a decline in imports. This leads to an increase in the reserves of foreign exchange in the host countries and improves the balance of payments (Meyer and Sinani, 2009; Blomström and Sjöholm 1999; Javorcik and Spatareanu 2008). FDI is also considered as one of the most important means of integrating the global economy (World Bank, 2012). In addition, FDI may involve competition between domestic and foreign firms, and helps the former to gain access to various global networks including foreign market sales and procurement networks (Jordaan, 2008; 2011; Belderbos, *et al.* 2001) Moreover, FDI activities and transactions play an important role in increasing employment opportunities for host country workforces (Lall 2000 and Moran *et al.* 2005).

As a result, since the 1980s, FDI has been welcomed, and many host countries' governments have amended their regulations and designed new frameworks. In particular, developing countries have opened up their economies globally, liberalised

their financial markets and offered tax incentives and other inducements, in order to persuade foreign investors to invest their money and knowledge in their countries. These countries aim to gain better access to the international market and to technological know-how, increase employment opportunities, and enhance their balance of payments; in short, they aim to benefit from all the potential positive effects of FDI (Lall, 2000).

Creating a suitable environment for FDI has become essential in an increasingly competitive environment, especially for developing countries that need to re-examine their policies toward FDI in order to capture the potential benefits to be gained from this in terms of productivity, employment and improving labour skills through technology transfer. This has led policy-makers to search for ways to attract foreign investors, using instruments at both the macro and microeconomic levels. Consequently, in order to encourage FDI, policy-makers have increasingly focused on the factors that could be improved in order to encourage this investment as a possible method for achieving sustainable economic development (UNCTAD, 2008).

Consequently, inward FDI across the world has risen sharply over the last three decades. Responses to host countries policies reforms, particularly the maintenance of policies for investment, removing barriers to international trade and the promotion of investment by host countries have all made positive contributions to the movement of investment capital across world. Supported by international economic growth in developing countries and developed countries, this has been among the fastest growing economic activity around the globe (Blomstrom et al, 2000).Inward FDI has risen from an annual average of US$ 142 billion for the period 1985-1990 to more than US$ 385 billion by 1996, reaching US$ 2.1 trillion in 2007. Affected by the global financial crisis during 2008, FDI decreased in 2010 to US$ 1.3 trillion but then began to rise again, reaching US$ 1.6 trillion in 2011 (UNCTAD, 2013). Developing countries are no exception to this increase. The annual share of the total world FDI inflows in developing countries has increased dramatically from 16.86% in 1990 to 18%, 45%, and then 52% in 2000, 2010, and 2012

respectively, while the share for the Middle Eastern and North African (MENA) countries was 0.61%, 0.42%, 4.97% and 2.67% respectively in the same period (UNCTAD, 2013).

These rapid and significant changes in the size of FDI inflows and the structure of FDI recipient countries raise a number of questions; for example what are the determinant factors for these changes?; what could host countries do differently in order to attract FDI?; and what policies should be adopted to promote FDI inflow? A part of the answer to these questions is to be found in the fact that many developed and developing countries have offered various investment incentives in order to create a suitable environment for FDI. Thus, it is essential for host countries to recognise the locational determinants of FDI, so that the incentives provided are effectively matched with the foreign firm's requirements (Asiedu, 2011).

Understanding what determines investment location choices can help host country governments to be more aware of the consequences of implementing passive as opposed to active FDI policies as well as providing tools for the FDI agency to help formulate their strategies. Since FDI is a rather complex economic category, depending on and relating to a range of factors, it is likely that as the global environment changes, factors affecting FDI will also change (UNCTAD, 2009).

In view of the economic benefits of FDI, at the beginning of 1990s Libya began to implement wide-ranging reforms in order to integrate its economy with the global economy, using various types of capital to diversify its sources of income and to attract FDI. Libya achieved this by encouraging the development of the private sector via deregulation, privatisation, and economic openness. Libyan policy-makers realised that attracting FDI had become critically important in order to reduce the country's dependence on oil revenues, since sustainable growth must involve the upgrading of technology and production scales, and the creation of linkages to an increasingly integrated globalised production system, chiefly through the participation of Multinational Corporations (MNCs). In this context, the Libyan government has given top priority to FDI as a future development strategy by amending investment legislation

to stimulate foreign investment such as investment law No. 5 of 1997, law No. 7 of 2003 and law No. 9 of 2010 in order to encourage foreign investors to invest in Libya and creating a competitive environment for investment (PIB, Investment Report, 2010).

As a result, FDI inflow to Libya has risen over the period 2003-2010 from a relatively low level of about US$ 143 million in 2003 to about US$ 4 billion in 2007. In 2010, FDI inflows decreased to about US$ 2 billion as a result of the world financial crisis. FDI continued to decrease and accounted for US$ 1.4 billion in 2012, having been affected by the conflict in 2011 (UNCTAD, 2013). Libya only received an average of 4% of the total FDI inflows into African countries in the last decade (UNCTAD, 2010). Despite all the Libyan government's efforts, the contribution of FDI to Gross Domestic Product (GDP) accounted for only 2.6% in 2010 (Central Bank of Libya, Annual Report, 2013). The non-oil sectors contributed some 40% of the Libyan GDP whilst employing about 97% of the official workforce in 2010. Moreover, most of the foreign investment inflows to Libya are still attracted by the gas and oil sectors (Porter and Yergin, 2006, p. 5; Political Risk Yearbook: Libya Country Report, 2009).

Given these problems, there is a broad agreement amongst Libyan policy-makers that the future economic stability of the country will depend on its ability to attract FDI to non-oil sectors in order to strengthen the private sector though technology transfer, create jobs for Libyan workers, and diversify the economy by reducing the country's dependence on oil and gas (Younes *et al.*, 2013, p. 19).

1.2 Research Rational, Motivation and Significance

Since the early 1990s, the international economic situation has changed substantially and many countries have tried to improve their situation by attracting more FDI. Research has shown that policy-makers in many countries focused their attention on attracting FDI, having realised the importance of this form of investment. Therefore, this research is situated at the confluence of two major areas of inquiry: increasing economic globalization and transformation in the economic and political environment in Libya.

Since attracting foreign investors has become a priority among Libyan policy makers, it may be useful to reassess the policies and regulations of inward investment as a means of developing linkages with the local economy. Whilst it is clear that more FDI is needed to diversify and sustain Libya's economic growth, it is not clear how this is to be achieved. One essential step is to determine the factors that serve to increase/decrease FDI inflows into the country, and to establish what Libya needs to do differently in order to renew its policies by learning from other developing countries in a similar situation and adapting these findings to its own local environment. It is necessary also for a host country to recognise the locational determinants of FDI, so that the incentives provided effectively match the requirements of attracting FDI and enabling rapid and significant changes to take place.

To date there have been limited studies in the Libyan context on those host country factors which attract FDI; therefore more research is needed in this area in order to highlight the most important factors that are likely to encourage or discourage the inflow of foreign capital into Libya, particularly given that FDI has been identified as a potentially important source of economic development and sustainability.

In the field of FDI studies there are several theories which are commonly used to examine the effect of external and internal factors on the movement of capital, such as international trade theory, the firm-specific ownership advantages theory, firm-based theory, new growth theory, product life cycle theory and eclectic theory. However, the latter is assumed to be the most appropriate for examining the fit between location factors and inflows of FDI in addition to specifically determining the fit between location factors and investment decisions.

Although several location factors have been adopted in examining the relationship between the host country's business environment and FDI, a number of these factors were considered to be more common variables such as economic and market size, human capital, and political factors (Asiedu, 2006). Therefore, many researchers have suggested

that further comprehensive efforts are required in this field, in particular to investigate the influence of infrastructure and institutional factors on FDI inflows, using an eclectic theory model (Asiedu, 2006; Moosa, 2007; Rogman and Ebbers, 2013; Quazi *et al.*, 2014).

Most FDI empirical studies were cross-sectional evidence use a set of different countries, such as studies by (Rogman and Ebbers, 2013; Anyanwu, 2012; Ho and Rashid, 2011; Vijayakumar *et al.* 2010; Moosa, 2007), while a number of studies shows that the determinants of FDI might be country specific (Arratibel, et al 2011; Oladipo, 2010; Chen, 1996). In addition, the relationship between FDI and location factors could be positive (Oladipo, 2010; Johnson, 2006), negative (Del Sol and Kogan, 2007), or insignificant (Vijayakumar *et al.* 2010 and Moosa and Cardak, 2006), depending on specific factors in the host country such as economic stability, market size, investment policy, labour force and infrastructure conditions. This emphasises the necessity for country-specific studies such as this one relating to Libya since it is a country with a wealth of natural resources which might produce fresh insights on this issue.

When comparing the results of existing empirical studies (De Mellor, 1997; Vijayakumar *et al.*, 2010) on the determinants of FDI, there appears to be a lack of agreement about some of the determinant factors, which emphasises the need to gain a better understanding of how host countries may attract and benefit from this form of investment. Therefore, the above authors posited that this difference might be related to the diversity of countries characterised but also, between each type and form of FDI. Moreover, they suggested that further studies should take into account the effect of different characteristics of FDI.

In recent decades, many studies (e.g. Li and Liu, 2005 and Sukar et al, 2007) have studied the direct impacts of FDI on economic development, such as growth and employment. Limited studies have focused on the indirect impacts, particularly on investigating the relationship between FDI and domestic suppliers. Kiyota *et al.*, (2008),

and then Jordaan (2011) conducted empirical studies to examine the influence of foreign firms on domestic firms in terms of technology transfer and improvement of production methods.

As this review will demonstrate, the majority of these studies investigated the relationship between location factors and investment decisions and the link between foreign firms and domestic suppliers in developing countries. Most of the earliest studies on the determinants of FDI are cross sectional, conducted either in developed countries or developing countries in different regions, while there are limited studies conducted particularly in the North African region. Therefore, this study aims to fill the gap of the lack of a single country study of Libya.

Moreover, there is still a lack of studies which have applied the characteristics of FDI to developing countries, especially those of North Africa, and specifically to Libya. Therefore this study seeks to fill this gap by studying the differences between various FDI characteristics such as foreign company nationality, industrial sector and ownership, with the aim of determining the influence of these FDI characteristics on investment decisions within foreign companies operating in Libya. If the study results show each type of FDI viewing the location determinants differently, than the study results could be useful for policy and decision makers in Libya as well as to those countries who have similar economic characteristics to target specific FDI. Also, the majority of the previous studies of FDI determinants and their impacts have used either secondary data for their analysis, while there is a lack of studies that adopted other methods such as a triangulation of questionnaire and interviews for collects the primary data which may produce different results.

There is very little research conducted on the location determinants of FDI in the case of Libya as a host country. There also appears to be a lack of comprehensive empirical studies, especially concerning FDI in the non-oil sectors, regarding the locational determinants of Libya as a host country (see Chapter Three). Moreover, this study is

considered to be the first study to identify the significance of various FDI characteristics such as foreign company nationality, industrial sector and ownership. There is also a lack of research in the area concerning the linkages between FDI and domestic suppliers, which was the major goal sought by the Libyan government. This research therefore represents the first study to investigate the linkages between foreign companies investing in Libya and domestic suppliers, and to assess the ability of domestic suppliers to supply these foreign companies with good quality and competitively priced inputs.

This study also responds to the recommendations of other researchers such as (Ben Taher, 2008 and Abdulla, 2010) whom examined the determinants of FDI on the local economy. In their studies, they explicitly recommended that further studies in this field should pay more attention to determining the effect of FDI companies operating in the Libya on the domestic firms.

The significance of this study is to make further progress in discovering the FDI determinant factors in Libya in order to broaden our theoretical understanding of these. It also aims to provide policy-makers with an objective assessment of the forces affecting FDI flows to Libya. More specifically, this research provides information concerning the effects of nationality, industry type, and ownership on the locational determinant factors of FDI. Determining those factors will help to provide policy-makers with a useful tool for planning, shaping, and adjusting existing scenarios or policies in order to ensure that these act as incentives to attract the preferred kinds of FDI and gain the highest benefits. Thus, the study also assesses the possible linkage between FDI and Libyan suppliers. This empirical study, therefore, will add to the literature concerning FDI determinants in Libya as well as contributing towards assisting other MENA and developing countries to use their resources to formulate policies which will play a greater role in attracting foreign capital and technology.

Based on the argument above, conducting this study presents a great opportunity to overcome the limitations of previous studies in this area and to provide a clear insight into the influence of location factors in relation to FDI decisions, as well as investigating

whether the foreign firms that operate in Libya have an effective effect on domestic firms.

1.3 Aim and Objectives of Study

The main aim of this thesis is to explore the determinants, obstacles and nature of the linkage of FDI to the rapidly developing economy of Libya over the last decade and in particular to establish whether these determinants, obstacles and linkages vary according to the characteristics of FDI.

This research aims to determine which factors are most likely to encourage and discourage FDI in Libya, and to identify the different requirements for each type of FDI by applying characteristics like nationality, industry type, and ownership, in order to provide more in-depth information to policy-makers. It is hoped that this empirical study will reach some useful conclusions regarding policy implications relating to the formulation of future policy in order to increase capital inflows into Libya so that the incentives provided by the Libyan government match what is actually required. This is especially important when Libya is actively targeting specific types of FDI. In addition, the study will examine the possible effect of FDI on the local economy by investigating the relationship between foreign companies and domestic suppliers. This study, then, has a number of objectives as follows:

- To identify those factors which are most likely to encourage or discourage FDI when used as determinants for considering locations for new investment abroad.
- To identify differences in locational determinant factors applied by various types of FDI in terms of nationality (Western or MENA), industry type (manufacturing or services), and ownership (fully foreign-owned or joint venture).
- To assess the effects of FDI on the local economy through the linkages between FDI and domestic suppliers.
- To provide guidelines for Libyan decision-makers concerning which incentives should be provided to attract specific FDI.

1.4 Key Research Questions

This study addresses the following key research questions:

1. What are the main determinants and the main obstacles for inflows of FDI into Libya?
2. Which factors encourage/discourage FDI from companies that differ in terms of their nationality (i.e. Western or MENA)? If these factors differ, to what extent do they vary and why?
3. Which factors encourage/discourage FDI from companies in different types of incorporated industries (i.e. manufacturing vs. services)? If these factors differ, to what extent do they vary and why?
4. Which factors encourage/discourage FDI from companies that differ in terms of their ownership (i.e. fully foreign-owned or joint venture)? If these factors differ, to what extent do they vary and why?
5. Is there any significant backwards linkage between foreign companies and Libyan domestic suppliers?
6. Which strategies can be used to improve the Libyan business environment?

1.5 Theoretical Considerations

This research uses an extensive literature review to construct the basis for this study by providing a theoretical framework for the study of the determinants of FDI and its possible effect on the domestic economy through linkages with local suppliers. In the field of FDI studies there are several theories which are commonly used to investigate the determinants of FDI, and to examine its effect on economic development, including international trade theory, the firm-specific ownership advantages theory, firm-based theory, new growth theory, product life cycle theory and eclectic theory. However, the latter is assumed to be the most appropriate for investigating the relationship between location factors and investment decisions. Building on previous literature (see chapter

two) and using the locational advantages element of the eclectic paradigm, this study will investigate the flow of FDI as a function of Libyan location factors.

A number of reasons can be advanced to explain this use of the eclectic paradigm. Firstly, the eclectic paradigm is not a theory; rather it should be considered a framework that can be modified to fit the study's purpose. The purpose of this research is not to validate or test the eclectic paradigm itself but specifically to explore its relevance to the Libyan case.

Secondly, the strength of the eclectic paradigm comes from its compatibility with any FDI theory because it includes and covers the entire range of variables used in other theories. The eclectic paradigm can be used to investigate FDI flow both from the perspective of a firm and from that of a host country (Dunning 2002).

Thirdly, the literature review, specifically work on Dunning's (1993) eclectic paradigm, reveals that most studies focus on MNCs, aiming to determine how these MNCs make decisions about FDI. Choosing the eclectic paradigm enables this study to explore the relationship between the host country's locational determinants and the inflow of FDI.

Fourthly, this framework has been designed to allow FDI to be studied from two perspectives. The first perspective is that of the international firm, investigating which companies have the ability and desire to become an FDI entity. In this instance, the firm-related ownership advantages need to be known. If the firm has ownership advantages, then it may choose to internalize those advantages by becoming an FDI entity. Accordingly, it will choose the country that has the locational advantages that bring the benefits of such an investment to the company. The second perspective involves that of the host country, which wants to know what locational advantages it can offer to attract FDI. From the host country's perspective it cannot do anything about the firm's ownership advantages except knowing which factors it would consider in order to make the decision regarding internalization. Furthermore, the use of the sub-paradigm of

locational advantages from the perspective of the host country has been widely used in the literature.

1.6 Data Scope, Sources and Methodology of the Study

The study focuses on analysing the economic reforms since the beginning of the 1990s and the policies concerning FDI, particularly since 1997 when the Libyan government began to promote foreign investment and, consequently, received a significant amount of the share of FDI up to 2010. The reason for selecting this period to study the behaviour and trends in FDI inflows is because of the growing share of foreign investment in developing countries which took place in this period. Also, the start date of the study was chosen to reflect the beginning of the change in Libyan economic policies regarding the presence of foreign investors in the economy.

The study draws on information from various sources: (1) international agencies' reports including those of the Organization for Economic Cooperation and Development (OECD), the International Monetary Fund (IMF), the World Economic Forum, the World Banks, the African Development Bank, the Arab Investment Guarantee Corporation, and the United Nations Conference on Trade and Development (UNCTAD); (2) Official government publications; Central Bank of Libya, Ministry of Economy General Planning Council, National Board of Information and Documentation, and the Libyan Foreign Investment Board Company; (3) other sources such as books, periodicals, articles and bulletins relating to the topic of this study will be used; and (4) personal testimony arising from questionnaires and interviews for primary data collection.

The research methodology used in this study is comprised of both quantitative and qualitative analysis (see Chapter five), and is based on two modes of data collection: questionnaire and semi-structured interviews. The study was divided into three phases. The first of these involved the selection of the research philosophy, approach, strategy, and data collection methods. The research philosophy, which reflects the way knowledge is developed, was derived from a positivistic paradigm. Adopting a positivistic context

implies measuring the characteristics of the social world using quantifiable observations that can be analysed statistically. The research adopted a deductive approach, employing a cross-sectional survey strategy, which employed a questionnaire as the main data collection instrument. This questionnaire survey was followed by 20 semi-structured interviews used as supplementary data to support the questionnaire findings.

In the second phase the empirical study was conducted during field study in Libya during the period of July to November 2012 using self-administered questionnaires for the purposes of quantitative data collection. The population of this research was dependent on the official list obtained from the Register Office of the Libyan Privatisation and Investment Board (PIB) containing 263 joint venture and fully foreign-owned companies.

A questionnaire was used for the purpose of this research for quantitative data collection. In addition, 13 semi-structured interviews were conducted after administering the questionnaires with thirteen respondents from thirteen companies in the same sample. A further seven face-to-face interviews targeted Libyan officials with responsibility for dealing with FDI in various domestic institutions including the PIB, the Ministry of Economics and Trade, and the General Planning Council (GPC). These were intended (1) to provide a better understanding of the mechanisms used by local authorities to attract foreign investors; (2) to identify the obstacles facing foreign companies operating in Libya, and (3) to reflect official attitudes towards foreign investor impact on the local economy. The interviews were used to probe answers and support the questionnaire findings serving as the ideal method to verify, build on and add depth to the results of the questionnaire survey (Cooper and Schindler, 2011, p. 183).

Before carrying out the empirical work, the questionnaire was piloted. Several drafts were produced and distributed among professional personnel for the purpose of correcting possible mistakes and providing further insight into the questionnaire contents. The questionnaire was reviewed by members of academic staff at the University of Huddersfield who have practical and academic experience related to the research topic. The questionnaire was then sent to ten foreign companies selected from the same study

sample as part of the piloting stage, in order to ensure the practicality of the questionnaire and its ability to collect the required data and achieve the research objectives and its expected outcomes.

The third phase of the study methodology involved analysing the data and presenting the findings. At this stage, the statistical software SPSS Version 2.0, which is commonly used by social sciences researchers, was used to present and analyse the quantitative data from the questionnaire. External and internal validity were established and reliability was tested. In addition, descriptive statistics such as frequency and means were used to meet the descriptive goal. Factor analysis and the MANOVA test were used to test the research hypotheses, which will be explained in chapter five. In addition, the qualitative data obtained by the semi-structured interviews were presented and analysed using a thematic approach.

1.7 Outline of the Thesis

The thesis is organized into eight chapters. Chapters Two and Three present a literature review in which theoretical and empirical studies on locational choices and backward linkages are surveyed, the relevant explanatory variables to be used in the thesis are extracted and discussed, and research gaps are identified. Chapter four provides an overview of Libyan economic history and relevant policy discussions relating to FDI. This chapter also provides an overview of FDI experiences in Libya in terms of industrial distribution of FDI, sources, mode of entry and value added. Chapter Five outlines the research methodology, describing the design and method, variable measurements, and data sources. Chapter Six presents the data collected and descriptive statistics results whilst Chapter Seven discusses the findings of the study. Chapter Eight summarizes the contents of the thesis and presents the policy implications of the findings.

Chapter 2

Theoretical Overview of FDI

2.1 Introduction

A large body of theoretical and empirical studies of FDI exists, reflecting the interest that there is in understanding its determinants, location and impact (Moran, 2006). Many researchers have sought to explain these factors from different perspectives, with early contributions in this field essentially tracking developments in international trade. Later, different perspectives and conceptualizations of FDI were adopted, with their theoretical foundations lying in literature from a range of areas including institutional and industrial economics. Empirically-based research has sought to test these different theories and to analyses the location of FDI, using data for countries that include both developed and developing countries as discussed in the next chapter.

The main purpose of this chapter is to review the relevant literature on the determinants of FDI from a theoretical perspective, in order to provide the rationale for the subsequent empirical work that examines FDI location determinants. This chapter starts by considering definitions of FDI, and these various interpretations will be examined in Libyan context relating these to the definition which has been adopted in Libya. It then proceeds to describe the evolution of the determinants and effects of FDI from a range of theoretical perspectives, and end by drawing conclusions from the material reviewed.

2.2 Towards a Definition of FDI

As previously noted, FDI has been studied widely by academic researchers, international trade theorists and international economists since the 1950s. It is not an easy task, therefore, to provide one single clear-cut definition of FDI, given the differing opinions of the many theorists who have studied this concept and the similarity and overlap between FDI and other economic phenomena such as expect of capital movements and portfolio investments. It is also clear from the literature that although some definitions

have been more widely adopted there is no universally accepted definition of FDI. What is agreed, however, is that FDI involves much more than financial investment transactions that intend to make a profit.

According to the World Bank (1997) the term FDI conventionally refers to a form of international inter-firm cooperation that involves a significant equity stake in, or effective management decision power in, or ownership control of, foreign enterprises. However, this basic definition does not capture the whole meaning of FDI because it can also include other forms of cooperation such as non-equity forms of international enterprises. Foreign firms can provide tangible and intangible assets to host country companies without foreign control being involved. These international enterprises encompass most types of investment, including leasing, licensing, franchising, start-up and international production sharing agreements (De Mello, 1997).

The most commonly used definitions of FDI are those of the International Monetary Fund (IMF, 1993) and the Organization for Economic Co-operation and Development (OECD, 1999) which identify core elements of FDI. They define FDI as the category of international investment that reflects the objective of a resident entity in one economy (referred to as a 'direct investor' or 'parent enterprise') obtaining a "lasting interest" and control in an enterprise resident in another economy (referred to as a 'direct investment enterprise'). This definition highlights some other important aspects of FDI which distinguish it from a portfolio investment, since the definition of FDI points to a long-term relationship between a company/companies in the home or source country (the investor) and another company in the recipient or host country (country of investment). This relationship can also imply that a company in one country (the foreign investor) possesses assets in another country or owns a production unit that belongs to a country other than its origin country (UNCTAD, 2008:17).

In this context Brewer (1987, p.117) uses the percentage of ownership of an enterprise as a criterion for distinguishing FDI from a portfolio investment, setting 10% as the threshold "*below which investments are treated as portfolio investments and above which*

they are treated as direct investments". This illustrates that to reach a usable definition requires that a distinction is drawn between FDI and other economic phenomena. In Libya, there are very few projects had less than 10% foreign ownership, so that for practical purposes the definitions are the same.

The Arab Investment and Export Credit Guarantee Corporation (1987:14) defines FDI as the flow of capital in the form of financial assets or production assets, material or otherwise coming from outside into the host country, which features in independent or joint investment projects for business purposes.

From these definitions, it is apparent that FDI is a category of investment that reflects the objective of establishing a lasting interest by a resident enterprise in one economy (direct investor) in a firm (direct investment firm) that is resident in an economy other than that of the direct investor.

2.3 The Theoretical Determinants of FDI

Academic interest in FDI, as well as the development of theoretical and empirical models studies used to understand it, began to emerge in the years following the Second World War, between 1945 and 1960, a period when FDI flows started to gain prominence in the global economy. However, these early models (and consequently the empirical studies also) lacked a distinctive theoretical underpinning, as FDI was treated on the same basis as trade theories, and so did not have a separate conceptualization. This economic phenomenon gained ever-increasing attention from the late 1960s onwards, during a period which global FDI flows increase dramatically, from USD 13 billion in 1970 to USD 1.3 trillion in 2012. At the same time, FDI began to emerge as a concept in its own right, and one which crossed a number of disciplinary boundaries, comprising economics, politics relations and Management.

The FDI theories attempt to answer the next questions: First, why do firms choose to transfer their operations from their home country to the host country? Second, why do

they choose to do this instead of exporting or licensing? Finally, why do they choose to locate in a particular area? The following sections of this chapter is discussed development of these theories in the.

2.3.1 International Trade Theory

International Trade Theory and its associated models were initially more focused on explaining international trade in terms of foreign trade using the Heckscher-Ohlin (H-O) model of neoclassical theory developed in 1933. This is based on the framework so-called 2 x 2 x 2 models which take into account that there are two countries trading i.e. the foreign country and the home country. These two countries would require two commodities of production, namely, capital and labor. The land would also be used (Feenstra, 2003). This model, however, assumes that the two countries have the same technological capabilities and production, and that commodity markets are perfectly competitive. The H-O model was able to generate analysis for the first time while incorporating the fundamental factors of the local market into international trade theory. It did not, however, allow for differences in the factor intensity of constant-return-to-scale production functions or the factor endowments of the two countries (Lancaster, 1957, p. 19).

According to H-O model, every country is likely to produce and specialize in the product or products that would consume much of its raw material and in which it has a locally abundant factor of production. Thus, a country is likely to opt for capital intensive production if it has more capital in comparison to other countries. Higher salaries and wages would be expected if human resources and labour is scarce. In order to attain maximum return on their investment, companies are likely to seek low labor costs which are highly indicative of the reason why FDI occurs in the first instance (Lancaster, 1957). However, the H-O model neglected the cost factor relating to transportation between the two countries, which is impossible (Rugman, 1981).

The initial model suggested that countries have different factors of production which would ultimately determine the price but this was revised to incorporate suggestions from Samuelson (1953), creating the Heckscher-Ohlin-Samuelson (HOS) model (Baltagi *et al.,* 2003). Samuelson's model assumed that a country must possess specific advantages such as labour, capital or resources as a condition for trade between two locations. The revised model accepted that regardless of the difference in factor endowments, over time the factor prices are likely to equalize between the two countries going for the trade, if processes take place under free trade conditions. Another variant of this model was devised by Vanek (1968) who came up with the Heckscher-Ohlin Vanek (HOV) version of the mode which expanded the model to include the possibility of multiple countries, multi-factors and different commodities and goods options.

Kojima (1978) attempted to further enhance and develop the HOS model by studying Japanese FDI in the United States and American FDI in Japan to examine the links between trade and FDI. He concluded that a relationship between FDI and trade can be developed by encouraging trade using the macroeconomic approach instead of opposing this and placing obstacles in the way of those companies engaging in this.

When Kojima (1982) adopted the HOS model for his study, he realized that it was important to discard one of its core suppositions, namely that the function of production between the two countries is identical. According to Kojima's approach, the investment should flow from the foreign country's deprived sector to the host country's relatively growing sector (Feenstra, 2003). Thus, his study indicated that FDI was complementary to trade. On the other hand, Kojima's work contradicts that of Mundell (1957) who considered FDI to be a substitute for trade. This confusion has weakened the reliance on International Trade Theory to explain the FDI movement (Kohlhagen, 1977). In short, Kojima's model focuses on the source country of FDI and how the source economy can change the relationship between FDI and international trade.

One school of thought criticized Kojima's work, on the grounds that his findings were somewhat biased in nature due the fact that the major gap in the nature of FDI, in relation

to technology, institutional environment, financial capabilities and economic size, was more related to the difference in composition of the two countries he selected. Critics argued that a study that addressed the source country of FDI and how this source economy might impact on the relationship between international trade and FDI would have been improved if two countries with a similar composition had been used in the study. Kojima's findings were therefore largely dismissed by critics on the grounds they could not be generalized (Schroath *et al.,* 1993; Encarnation, 1999). Although Kojima's model and his findings did explain the inequality in the resource bases of national economies which can result from foreign investment, Dunning (1988, 1994) disregarded his work claiming has offered no clear explanation and understanding of FDI in theoretical terms, suffering from the simplicity of its own frame of reference.

According to the Heckscher-Ohlin model, countries with cheap labour attract the flow of capital from capital intensive countries as (Baltagi *et al.,* 2003). Those who reject this model claim that it only holds good for countries that possess identical production functions and goods, and it would be quite unrealistic for any two countries around the globe to have almost identical systems. Findings suggest that the same model cannot be generally applied to all the countries in the world. Also, the insistence in the Heckscher-Ohlin model on the necessity of removing all the differences between the countries except for factor endowment, also provoked criticism, to the extent that economists were forced to draw the conclusion that alternative approaches to the model needed to be explored (Kierzkowski, 1987).

2.3.2 The Theory of Firm-Specific Ownership Advantages (Industrial Organization)

Hymer (1960) is amongst the first authors to criticize the neoclassical approach for its limited ability to explain FDI flows, and to suggest that FDI was not just one element in a broader International Trade Theory, introducing FDI as an independent theory in its own right (Barrios *et al.,* 2005). As an economist, Hymer (1960) specified different characteristics of the investment firm and how the structure of the market tends to explain

FDI. He focused his observations on industrial economics and how these can breach international barriers to production. He pointed out that a firm may be in difficulty if an international firm does not possess specific ownership advantages (such as a monopolistic advantage). These are intangible assets such as patents, marketing experience or new technologies not available to the local companies in the host country for FDI.

Hymer's theory demarcates between FDI and portfolio investment, contrary to the earlier traditional practice in international trade theories. He believed that it would be an unjustified theoretical explanation of FDI to attribute portfolio investment to the interest differential between countries (Denisia, 2010). This is because it fails to address the concept of control and ownership benefits. According to Hymer, one of the reasons why capital movement occurs is because the interest rates in the host country are set to gain higher returns. The other reason is to gain firm control over the company in order to improve its profitability and reap the benefits of this ownership. Therefore, it could be easily deduced that when a company enjoys a certain level of ownership advantage over its competitors in the industry, this may result in that company entering the market internationally and FDI is likely to take place (Denisia, 2010).

Early efforts were made to develop and extend the theory put forward by Kindleberger (1969). He argued that the acquisition of intangible assets provide the required firm-specific benefits whilst his argument regarding flaws in the market indicated the non-availability of rivals in the host country. This theory was further refined to provide an explanation for the intentions of companies intending to do business abroad and gaining control of local resources was the reason given for FDI (Denisia, 2010). In this context FDI can be understood as companies seeking to expand their monopolistic economic rent in order to penetrate other foreign markets. Thus, FDI was considered to be a mode of international investment which is distinct from the standard theories based on international trade (Caves, 1971; 1974).

It can be argued that Hymer's work has changed the whole thinking process behind theories related to FDI. Although Hymer emphasised government laws and rules, country

specific benefits, customer aptitudes and preferences and even the level of economic development, he omitted costs that would be incurred by having to deal with differences in language, legal systems and cultural values especially with respect to manufacturing businesses and trades (Mossa, 2002). However, four key shortcomings of his work have been singled out.

Firstly, it failed to clearly identify the differences between environment and conditions that was supposed to be the mandatory requirement for FDI from that needed for trade. For example; FDI requires ownership specific advantages while trade activates do not.

Secondly, the penetrative costs incurred within foreign markets for transferring asset advantages was ignored in concentrated market structures. In reality, of course, there are many other sources of cost that are not related to market structures. Also, Hymer did not explore the internal cost of the firms, which occur as a result of international expansion, but instead put more emphasis on traditional costs such as those referring to financial and capital costs and his theory ignored the costs of working in a foreign environment which firms must bear when they operate in a different culture, language and legal system. However, these costs and implications of the foreign environment must be recognized (Denisia, 2010).

Thirdly, Hymer also failed to address vertical FDI which was neither dealt with nor accounted for in industrial organization, especially manufacturing Vertical FDI which is generally put into place to provide for the input to the parent company at home.

Finally, Hymer's study focused only on the USA as the sole source of FDI in his study, meaning it would not be generally applicable to all countries (Aizenman and Marion, 2004).

2.3.3 Firm-Based Theories of FDI

Firm-Based Theory is considered to be one of the theories that shifted away from traditional economic theoretical perspectives on FDI, and instead began to carry out research concentrating on the behavioural theory of FDI that is firm-based. The earliest

attempt to explain the behavioural theory was introduced by Simon (1958). His work was originally carried out to provide a decision-making model in intra-organizational settings. This model revolved around the influences that may impact on individuals working in a particular organization and how they may respond to this (Aharoni, 1966). Further additions were made to the original formulation of the model of behavioural theory and decision-making processes (Morgan and Katsikeas, 1997). This helped to clarify the impact on development, formulation and implementation of expectations and major decision-making on the structure and practices being adopted and implemented within an organization. Organizational goals, organizational expectations, organizational choice and organizational control were identified as the four major steps in the decision-making process (Cyert and March, 1963).

This model was further developed by other researchers such as Dunning (1974) to analyses the decision-making process of FDI by those MNCs working within the borders of the USA. The focus again was on the decision-making process and associated issues and commitments. In addition, the economic and environmental factors, individual characteristics and relationships were addressed. There was a strong belief that economic profits were not the only thing to be considered when seeking direct investment. This new approach identified four decision-making investment stages when implementing FDI. These four stages include (1) the initial decision to target the foreign market, (2) the investigation process, (3) the reviewing process, and finally (4) the foreign investment process (Cyert and March, 1963).

The “internalization theory” of FDI (Buckley and Casson, 1976) highlights the contrast between the trades and transactions that a firm conducts. They also attempt to fully understand the reason why a company is better off performing intra-company rather than intercompany transactions (Rugman, 1986). It was argued that some firms opt to set up overseas rather than applying for a license and exporting their product via other channels (Buckley and Casson, 1976). To a certain extent this Buckley and Casson suggests that the theory of internalization theory is an extension of the firm-specific theory of Hymer.

They emphasize that it is not only the firm-specific theories are important for foreign investment perspective, but also improves the decision-making probability of internalizing the crucially required firm-specific benefits. This was of key significance especially for the MNCs (Rugman, 1986). This is particularly due to the fact that this decision relevant for foreign firms, as markets of intermediate goods, which include marketing practices, production methods and managerial skills are characterized via high-risk costs, so that such markets are involved as in the case of internalized (Buckley and Casson, 1976). Buckley and Casson also argued that any market imperfections distorting market prices including government regulation, tariffs and taxes, non-existent future markets, controls and asymmetric information between buyer and seller provided an incentive to internalise production.

In brief, it can be say that although it may seem a lucrative option for a company to enter other countries they are likely to encounter various business limitations in place. These limitations tend to increase the cost of investment, making the product less competitive in terms of price. As companies tend to gain firm-specific benefits and knowledge, they enhance their local marketing abilities, utilizing their technological and management abilities to manage their resources for efficiency and economy in the scale of production, making themselves more competitive than their competitors. The companies tend to internalise ownership to safeguard their benefits from competitors. This helps companies to expand across borders and to exploit foreign international markets.

2.3.4 Product Life Cycle Theories

The product life cycle model was proposed in response to the growing criticism of the neoclassical comparative advantage models. The functions of economies of scale and the role of innovation were also incorporated into this model for explaining FDI (Malhotra *et al.,* 2003). As a result, Vernon (1966) devised a new product life cycle model which revolved around two concepts while explaining FDI. These were the nature of the product and the developmental stage of the country. Three stages of product development were identified: new product, mature product and standardized product. Since research and

technology is required to develop a new product, the first stage of the product life cycle usually occurs in those countries that are already developed and in a position to spend time on innovation with assistance from skilled labour, and advanced technology. At the second stage, as there is less product development and more standardization in place; the product is less reliant on being close to the home economy. Finally, as the final or standardization stage approaches the emphasis shifts to increasing production and economies of scale (Malhotra *et al.,* 2003). At this stage the investor is likely to move to underdeveloped countries to tap into the ready supply of cheap labour on offer there.

Krugman (1979) further developed this product life cycle model by applying the concepts of innovation circles and technological gaps and coming up with an equilibrium model of the product cycle trade. The model focuses on the function of this innovation gap, with the product in its developmental stage originating in the North from the developed countries and ending up in the South where underdeveloped countries help in the economy of scale production at a very low labour cost. Soon the South begins exporting goods to the North and in the meantime the North continues to spend on innovation and developing new products. This results in a constant technology gap between the countries of the North and South.

The Uppsala School theory of FDI, developed by Johanson and Wiedersheim (1975), and Williamson (1973; 1985) has also been linked to the product life cycle theory and incorporated into the theory of FDI (Lu and Beamish, 2001). This concept is based on the idea that companies generally tend to improve gradually over the course of four small stages. In the initial stage they are not exporting their products; then they start exporting via foreign agent; next, they establish a subsidiary and finally, they began to export their production facilities to the foreign market, resulting in FDI.

Johanson and Vahlne (1977) built on this work, suggesting that the more a company becomes involved in FDI, the better it becomes at using and applying foreign market intelligence. The end result is that the parent company gains the confidence to invest abroad in producing its products. A company's confidence is gained from the knowledge

and experience of the working environment that it acquires while working abroad. There is a significant reduction in the cultural gap and cultural distance between the host country and the other country which helps them to undertake effective production and operations. The difference and similarities between the original product life cycle model and the one developed with the improvement and changes consist of the stress placed on the incremental commitment to international investment in the exporting countries at different stages and over a period of time.

2.3.5 The Eclectic Paradigm (OLI)

There is a further school of thought by Dunning (1979) who posits that although the ownership specific advantages and internalization theories are capable of justifying the reason for FDI to a certain extent, they still cannot justify it completely (Dunning, 2001). Dunning's eclectic model (1979) was developed as a result of his thoughts concerning the weaknesses within the existing theories (ownership specific advantages and internalization theories) used to explain the international production, and the lack of a formal model relating to either trade or other modes of resource transfer. In addition, Lall (1980, p. 120) observes that "*any study of international involvement which leaves one or other of these aspects out of account may be rather unrealistic*". Hence it may be concluded that when addressing international trade there can never be a single framework that can comprehensively explain cross-border trade and transactions for different products and services (Dunning, 2001; p176).

It has been argued that the flow of FDI cannot be merely defined as a specific area of economics. Rather, it was suggested that it needs to be examined using many different theories combined to produce a complete picture and understanding of the logical explanation to the relevant steps of the process (Dunning, 1977, 1979, 1981, 1988). The concept of the eclectic paradigm was put forward since this encompasses all the different aspects of FDI rather than addressing only its economic aspects (Dunning, 2001). Combining International Trade Theory and industrial organization theory with other economic theories produced a more complete explanation of FDI or eclectic paradigm of

FDI which is also known as the Ownership Location Internalization (OLI) theory. Ownership, location and internalization benefits were deemed to be a necessary requirement for any MNC intending to invest abroad.

For the exporting company, ownership benefits (O) may include competitive edge over the foreign competitors including new technologies, patents, managerial knowledge, and brand reputation which provide the firm with an advantage in the sector (as discussed in Hymer's Industrial Organization Theory1960). Therefore, companies would tend to produce and sell the same product by themselves overseas rather than selling this off to third parties or exporting it under license. On the other hand, the internalization method (I) and its benefits presume it to be a dangerous decision to deal with external companies (as discussed earlier by Buckley and Casson, 1976). This is because operating with these companies may serve to reveal ownership-specific benefits in other countries and thus those contracting companies may, in time, become the unexpected competitors. Therefore, it is of key significance to internalize the company's key advantages. This is because company hierarchy is the best plan for organizing business dealings.

The element which complements ownership and internalization theories is the location specific advantage (L) that a company reaps. It is suggested that it would be important to locate in a foreign country where the company is willing to invest to gain further business transactions. Thus the OLI paradigm, covering all the three aspects of ownership, location and internalization, advances the concept of FDI as a means of providing benefit for the investing companies (Dunning, 2001).

The OLI model by Dunning (1988; 1994 and 2000) was further expanded to incorporate specific variables like country, industry and company characteristics. Therefore, if the home country has particular benefits such as cheap labour or raw material, skilled labour, a large market or resources and innovative government policies prompting companies to invest in the R&D, then the country-specific advantage will come into play and define the outcome and nature of the ownership, location and internalization advantages of the company (Guisinger, 2001). Thus those companies operating in a technologically sound

country are likely to have the edge when it comes to their product being innovative in nature.

Contrary to the ownership advantages, location benefits are generally immobile and stagnant in nature since they cannot be transferred easily, but these are established according to the properties and characteristics of both the home and host country. Assessing the characteristics of the country plays a very important role in the choice of location. This may be related to cultural distance or economic differences between the two countries where transactions are being carried out. If the political relations between the host and home country are close with good cultural and economic ties between the two; then in the longer run a good relationship will develop between the two countries and make the business environment attractive for the investors. In this context, the chance of FDI is markedly improved when low political risks are involved (Dunning, 1993).

Policies implemented by the country, both in terms of trade and taxation can play a significant role from the investor's point of view when approaching a foreign country to invest. Tariff barriers and higher taxes may result in an investor shying away from investing (Nicoletti *et al.,* 2003). Also, the policies of countries governments and proximity between countries are crucial to the location of MNCs. Industry factors and variables are also vital for the companies investing. Transportation costs, fuel costs, cost barriers, tax barriers, finished and intermediary product cost and subsidies provided by the government can all affect the choice of location for the investor bringing in the FDI and also the availability of skills labour and infrastructure could affect the foreign company's decision. Similarly, the nature of already existing competition and the size of already existing companies within the same sector at the location are also important factors for the investor (Nicoletti *et al.,* 2003).

When a company opts for ownership advantage by using its location, internalization advantages tend to occur. Different countries implement different set of rules and regulations when it comes to business in relation to transfer pricing, mergers, acquisitions or resource transfer (Nicoletti *et al.,* 2003). A company is likely to invest in the host

country where the government policies subsidizes internalization transaction costs (transfer pricing) (Lu and Beamish, 2001). Controlling the source of inputs is of key significance at industry level. This way a local firm may have the edge over the foreign companies when it comes to internalization. Similarly, organizational and control processes are also not streamlined between the companies. These may differ in reference to subcontracting, franchising, technical assistance and licensing agreements (Lu and Beamish, 2001).

According to Dunning (2002), ownership and internalization advantages explain the ability of firms to invest in a foreign country. In other words, the location advantages answer the question concerning where FDI should invest, while the other advantages answer which firm should be an international investor and why they should invest internationally. The locational advantages result from differences in factor transport costs and distance, non-natural barriers, infrastructure and incentives present in different foreign locations. Examples of location advantages or determinants making a firm choose to locate in a particular country over others, including its own home country are low-cost skilled labor, availability of natural resource, and good infrastructure (Dunning 2002).

Many authors, including Dunning himself, see the eclectic paradigm as being the most complete model and framework to explain FDI in all respects. It determines the degree and outline of both the foreign and local-aided production of the product and service in international arena Dunning (1993). Moreover, it provides a basis for the comparison of different theories on the same topic by establishing the common ground and links between them. Also, different theories have been addressed, clarifying the relations between different levels of analysis (Cantwell and Narula, 2001, p. 156).

2.3.6 Traditional Location Factors of FDI

The eclectic paradigm framework examines the location dimension of FDI in depth by reflecting on investor motivation for carrying out FDI in relation to ownership benefits to invest in overseas markets (Dunning, 1993). These motives are categorized as; Resource-

seeking, market-seeking, efficiency-seeking and strategic asset-seeking. These motives enable the characterization of the motives for the location chosen by the FDI. This characterization of FDI location can be considered as follows.

In market-seeking motivation, investors opt for the relocation of the business activities in other countries to sell their products and services by taking advantage of the foreign market to increase their market share. Market-seeking motivation for FDI would involve targeting any country or market which is suitable for fast-growing industry and the host country will promote the foreign firms to expand their activities in this industry. On the other hand, resource-seeking investors are those which are looking for cheap labour, resources and raw material to decrease the cost of investment, as a means of increasing their profit margin, reducing the cost of production and becoming extremely competitive in price wars within the industry (Dunning, 1993).

Factors including endowments, economic and public policies and government incentives are likely to attract efficiency-seeking foreign investors to a country. These aspects will tend to reduce costs, making it more favorable for them to invest in other countries. The efficiency of the company is improved and there is concurrent reduction in cost for the companies if they invest in a limited number of companies only. All of these aspects would attract an efficiency-seeking investor. Finally, those investors who would opt for FDI as a means of maximizing their ownership advantages and weakening the significance of their competitor's advantages are grouped together as strategic asset-seeking investors.

These investor motives are also based on specific decisions collectively known as the classical location factors. These factors are wages and salaries for resource-seeking FDI; market size and market growth for market-seeking FDI; managerial experience and expertise for strategic asset-seeking FDI; and finally transport costs for efficiency-seeking FDI (Dunning, 2000). It has been generally observed that in the recent past there has been a significant decline in resource-seeking and market-seeking FDI and a

concurrent rise in strategic asset-seeking FDI. At the same time, alliances have increased (Hollenstein, 2005).

2.3.7 The New Growth Theories

Inflows of capital to developing economies have a significant exogenous component. Such capital could be a significant amount when compared to the size of the domestic financial sectors of recipient countries. Furthermore, such inflows can have a large macroeconomic impact on the economy of many developing countries.

The 1980s witnessed the emergence of a set of new theories which either built on Solow's (1956) neoclassical growth model or challenged this, including New Growth Theory, which attributed the sustained increase in growth rates to technological change. This new economic growth literature stressed the function of companies investing abroad and the significance of agglomeration economies. Martin (1999) indicated that Solow's (1956) neoclassical growth model addressed the interactions between the traditional factors of input and technology and their impact on long-term rate growth. It highlighted the role of technology as an exogenous factor providing steadiness in the driving force of the growth rate.

The endogenous growth theory was developed in the 1980's by Romer (1983, 1986, 1990; 2010), and challenged Solow's (1956) existing model of neoclassical growth. It was an attempt to explain the long-term rate of growth as the outcome of the interactions between the conventional factors of production inputs and technology, while attributing the continued improvement in growth rate to technological change. This new knowledge was treated as an endogenous factor in the new model. Those companies opting for profit maximization would employ innovative techniques and invest in R&D while coming up with new products and continuing to invest in foreign countries and direct knowledge transfer to local economies. Thus, FDI plays a key role in transferring ideas and knowledge globally and improving the endogenous growth of the host country as well (Romer 1990). Other minor contributory factors were later added to the theory which

initially focused on technology as the reason for economic growth (Lucas 1988). Martin's (1999) critique noted that this theory only focused on human resources and local technological processes, the underlying focus of economic activity being focused on inter-regional transfers.

The new growth theory was largely dependent on how FDI would affect the economic growth. The role of FDI was recognized with particular reference to the transfer of advanced technology to developing countries via both direct and spill-over channels as a result of linkages between foreign companies and domestic suppliers and customers (Lim, 2001). Other theories such as that devised by Krugman (1991a, b) try to address spatial issues that had previously been ignored. Krugman's general equilibrium model was developed to further describe the spatial aspect of economic development. The model largely based its assumptions on three factors, namely, transport costs, demand for manufacturing goods and increasing returns. In those places where there was increased demand, the low cost of transportation and substantial returns are likely to encourage companies to invest and concentrate if there is a concurrent supply of intermediary products at attractive prices and ample supply. For FDI location, these models are of key significance in the theoretical analysis.

However, a number of studies have argued that it is more difficult for host countries to gain benefits from FDI than to attract this because they require a minimum level of development in certain areas, such as education, infrastructure, and, more generally technological capabilities in order to reap valuable benefits from inward FDI (Fagerberg and Godinho, 2005; Dyker and Radošević, 2001; Archibugi and Filippetti, 2011). Previous studies have investigated the direct and indirect relationships between inward FDI and economic development from both macro and micro perspectives, including Romer (1983, 1986, 1990, 2010); Wernerfelt (1984); Blomström and Kokko (1998); Rodriguez-Clare (1996) and Bhagwati (1978). From the macro perspective, previous studies such as Romer have explored the direct and indirect relationships between inward FDI and poverty reduction. In these studies, it was found that host country economic

growth mediates this relationship while, from the micro perspective, previous studies such as Blomström and Kokko (1998) and Bhagwati (1978) have focused mainly on the indirect effect of FDI inflows on host country economy. These studies found that the level of development and technology gap and technological capability of the host countries mediates this relationship.

The indirect effect of FDI on the local economy is also explained by the concept of spill-over effects, which refers to direct as well as indirect effects. Indirect spill-overs result from the effects such as labour turnover and enhanced competition (Giroud and Scott-Kennel, 2009). As a result, these effects influence local firm behaviour and performance. On the other hand, direct spill-overs result from linkages that MNEs create with their local affiliates. A broader definition of linkages includes both business and non-business relationships. Giroud and Scott-Kennel (2009) categorized the concept of linkage into three forms: supply chain linkages with suppliers, collaborative linkages with other firms such as alliance partners, or institutional linkages with the private sector or governments. The micro perspective which can be divided into two forms: productivity spill-over and market access spill-overs.

The productivity spill-over effects occur when the efficiency of domestic companies improves as a result of FDI, or when domestic firms acquire benefits from an MNE's superior knowledge without incurring a high cost while the market access spill-overs take place when MNEs enable domestic firms to access distribution networks, marketing outlets, and information about consumer preferences and regulatory standards in order to facilitate the market access barriers which is common for domestic firms in most developing countries.

In addition, FDI has indirect effects on the inflow of foreign exchange, through increased productivity and the subsequent increase of exports and a decline in imports. It can also lead to an increase in the volume of foreign exchange in host countries and an improvement in the balance of payments (Blomström and Kokko, 1998). Further theoretical contributions regarding the relationship between FDI and linkages came from

Markusen and Venables (1999) who argue that the entry of international firms in the host economy can create two different effects: a competition effect and a linkage effect.

In this context the early theoretical attempt to explain FDI linkages was introduced by Hirschman (1985). The author argued that the establishment of new industries in the host country would lead to expanding the market in terms of its primary inputs, even if the inputs were supplied from abroad in the initial stage. He argued that foreign firms would make attempts to supply inputs needed for their activity using domestic production. Hence, further development stimuli are more likely to emanate from activities that have higher backward linkage effects. He further argued that the lack of interdependence and linkages is one of the most typical characteristic of underdeveloped economies.

Hirschman also highlighted the way in which the backward linkages in a developing economy may work towards improving industrial development. Underdeveloped countries often set up with less industry of advanced countries in terms of both input and output flow. These industries are initially linkage-free in that materials are imported from abroad, some value is added to them through mixing, assembling, and packaging, and the finished product is sold to final consumers. This type of venture is particularly attractive to foreign capital, particularly in China, where many branch plants owned by foreign corporations assemble final products for export using largely imported materials. Hirschman argued that these industries are conducive to backward linkages of practically infinite range and depth. In most cases, imported goods are gradually replaced by domestic production, which is produced because of the presence of a large and stable market. This process describes what has occurred in many rapidly developing and underdeveloped countries, where backward linkages from the final stage has stimulated the production of domestic intermediate goods and basic industrial materials, or even agricultural production.

The development of local intermediate goods market is an effective strategy to provide the required quality of local materials so that foreign-invested enterprises do not have to supply these materials from abroad. Hirschman argued that those industries that use

imported materials are often hostile to the establishment of local industries, because, for example, the domestic inputs may not be as good as the imports in term of quality. In this context Rodriguez-Clare (1996) has produced a theoretical model to support Hirschman's explanation.

International trade is another vital means of knowledge transfer as indicated by the new growth theory. Domestic firms may benefit from exports through more efficient use of resources and greater capacity utilization, thus benefitting from the gains in scale effects associated with large international markets (Bhagwati, 1978). To obtain low-cost products, with better-quality from main exporters, foreign purchasers may spread tacit and occasionally proprietary knowledge (World Bank, 1993). Moreover, taking part in exports allows firms access to international best practice and learning, and acquaintance with the availability and absorption of advanced technologies (World Bank, 1997). International competition provides companies with the motivation to adopt and foster advanced technologies (Hejazi and Safarian, 1999). Both FDI and international trade together with other international activities such as technological collaboration and scientific exchange allow developing countries to exploit the technological opportunities presented by the most advanced countries (Archibugi and Filippetti, 2011; Perez and Soete, 1988).

Initially, FDI can increase the demand for local output and generate complementarities that can be beneficial for domestic final-good producers. Furthermore, Ping and Saggi (2007) show that FDI impacts on domestic development by increasing the number of domestic suppliers that interact with multinational companies.

In short, in the field of FDI studies there are several theories which are commonly used to investigate either the determinants of FDI or to examine its impact on economic development, including international trade theory, the firm-specific ownership advantages theory, firm-based theory, new growth theory, product life cycle theory and eclectic theory as discussed above.

From the discussion above it is important to recognize that FDIs are becoming increasingly flexible and fluid, and much less static in nature and composition. Furthermore, there is a trend away from hierarchical and vertically integrated MNEs that are wholly controlled from the centre, and towards looser organizational structures, or extended organizational forms that tend to resemble markets linked by various forms of contract, and not just by equity ownership. The recent shift towards greater international outsourcing is one example of this trend. The implication for Libyan policy makers is that there are potentially more opportunities to benefit from this change in FDI behaviour and structure, and as the various parts of production are sliced and diced into finer and finer elements, the opportunity to become a specialised participant should increase. But, at the same time, they should aware that there is greater competition between countries to attract these smaller parcels of investment.

As a result, the theoretical model could be drawn as presented in Figure 3.1, based on the above theoretical literature review of FDI determinants. According to Dunning (1979, 1980, 1988), FDI can occur when three conditions are met; i.e. "O" ownership/firm specific advantages, "I" internalization specific advantages, and "L" locational country specific advantages. The "O" and "I" factors are purely dependent on the firms, and cannot be managed by others. On the other hand, the "L" factor is manageable by a host country. A country is able to choose which kinds of FDI they would like to attract, by providing factors that suit the needs of such foreign investors. At the same time, the country should be well aware of the costs and benefits received from the attracted FDI, for the overall highest benefit.

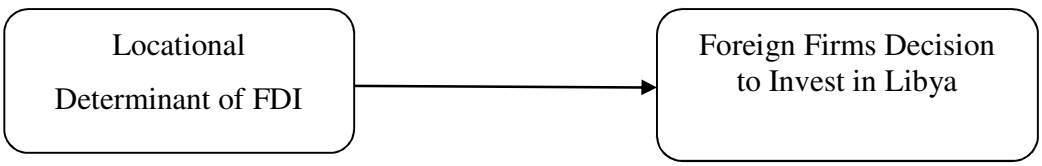


Figure 2-1: Theoretical Model

Among countries in the same region, Libya is known as one of the most attractive locations for foreign investment. However, with severe competition in the region, it is imperative for the government to provide what is really needed by the investors. Hence, this research focused on identifying locational determinant factors which encouraged foreign investors to invest in Libya. Therefore, the eclectic theory is assumed to be the most appropriate for investigating the relationship between location factors and investment decisions. Building on previous literature and using the locational advantages element of the eclectic paradigm, this study will investigate the flow of FDI as a function of Libyan location factors. A number of reasons can be advanced to explain this use of the eclectic paradigm.

Firstly, the eclectic paradigm is not a theory; rather it should be considered as a framework that can be modified to fit the study's purpose. The purpose of this research is not to validate or test the eclectic paradigm itself but specifically to explore its relevance to the Libyan case. Secondly, the strength of the eclectic paradigm comes from its compatibility with any FDI theory because it includes and covers the entire range of variables used in other theories. The eclectic paradigm can be used to investigate FDI flow both from the perspective of a firm and from that of the host country (Dunning 2002).

Thirdly, choosing the eclectic paradigm enables this study to explore the relationship between the host country's locational determinants and the inflow of FDI. Furthermore, the use of the sub-paradigm of locational advantages from the perspective of the host country has been widely used in the literature.

2.4 Conclusion

To conclude, this chapter has reviewed the theoretical literature on the determinants of FDI and backward linkages of FDI. In the period before 1960, the pattern of trade was discussed in terms of comparative advantage, and it was argued that it was the pattern of

specialization between countries that promoted movement of capital. The Heckscher-Ohlin theory was an initial explanation of FDI based on the concept of comparative advantage. However, this theory failed to recognise the unique nature of FDI. The cornerstone to a new theory first emerged in the 1960s, when Hymer introduced his own theoretical insights on the theory of international investment. Since then, the literature has taken many new directions in an attempt to understand and describe the pattern of FDI flows.

One new direction was the consideration of transaction costs, representing an extension to Hymer's theory, although it still left something of a gap in understanding. Latte on, this has been filled by Dunning's so-called eclectic paradigm, incorporating ownership, location and internalization (OLI) advantages into a single strand of FDI theory. While this framework is widely accepted for its comprehensiveness, recent insights have acknowledged the need to add further elements. With these developments, the Dunning framework has proved its flexibility, although it remains something of a collection of ideas within a single framework, which has yet to be fully unified. Nevertheless, it draws attention to the main features, including location, for which new theoretical developments attempt to explain the spatial concentration of FDI activity.

The location of FDI has played an increasingly vital role in the theoretical literature of FDI, and has been extended by the modern theories of economic growth, trade theory and new economic geography. These theories provided a rich framework to develop the reasons behind why, how and where firms engage in FDI.

Next chapter provided details of the empirical literature review of FDI determinants and its linkage with domestic suppliers based on the theoretical background.

Table 2-1: Summary of the Literature Review of Theories of FDI

Theory	Author	Contribution
International Trade Theory	Heckscher and Ohlin (1933)	Their universal equilibrium model determines a country's reasonable advantage, assuming that there are two countries (host and home) and two commodities requiring two factors of production (capital and labour), in addition to the use of land. It further assumes identical production technologies between the two countries and perfectly competitive commodity markets, but differences in the factor intensity of constant-returns-to-scale production functions and differences in the factor endowments of the two countries.
Heckscher-Ohlin-Samuelson (HOS) Model	Samuelson (1953)	The basic logic of the HOS model is that under free trade, factor prices will be equalized across countries regardless of the difference in factor endowments.
Heckscher-Ohlin-Vanek (HOV) Model	Vanek (1968)	This generalizes the Heckscher-Ohlin model to a multi-factor, multi-good and multi-country model and reveals the patterns of trade between countries.
Theory of Firm-Specific Ownership Advantages	Hymer (1960)	Hymer states that in order for a firm to overcome international barriers to production it must possess firm-specific ownership advantages.
Product Life Cycle Theories	Vernon (1966)	Vernon develops the product life cycle model to clarify FDI, conceptualizing it in the relationship between two factors: the nature of the product; and the level of development of the country. He envisages three stages of a product life cycle: new product, mature product and standardized product stages.
The new economic theory	Krugman (1991)	Krugman devises a general equilibrium model of product cycle trade highlighting the importance of technological gaps and innovation circles to explain their role in the trade between countries and regions in the industrialized North and those in the less developed South.
Uppsala School Theory of FDI	Johanson and Wiedersheim (1975) Johanson and Vahlne (1977)	They focus on the gradual development by small incremental change in firm behaviour in the multinational dimension, which they divided into four phases: not exporting; exporting via foreign agents; establishing a subsidiary; and transferring production to an external market. Johanson and Vahlne added farther developing by asserting that firms should take steps to use foreign market intelligence that serves to encourage their level of commitment to investing in a foreign country.

Behavioural Theory of FDI	Aharoni (1966)	Aharoni identifies four stages through which the foreign investment decision is made: decision to target the external market; investigation process; reviewing process; and foreign investment process.
Internalization Theory	Buckley and Casson (1976)	This is an extension of Hymer's firm-specific theory but emphasizes that the investment decision depends on internalizing the firm-specific advantage within the firm.
The Eclectic Paradigm (OLI)	Dunning (1977, 1979, 1981, 1988)	Dunning utilizes International Trade Theory with other relevant economic theories to generate a comprehensive explanation of FDI, known as the eclectic paradigm of FDI or the Ownership-Location-Internalization (OLI) theory.
Classical Location Factors	Dunning (1993, 2006)	This gives an insight into the location dimension of FDI by reflecting on MNC motivations for utilizing their ownership advantages to invest in foreign markets. These motives are categorized as: market-seeking, resource-seeking, efficiency-seeking and strategic-asset-seeking.
The New Growth Theory	Romer (1983, 1986, 1990)	Romer attributes the sustained increase in growth rates to technological change. Profit maximizing firms engage in costly R&D activities in order to produce innovative products, which will allow them to undertake investments in foreign markets efficiently, and thus, will lead to knowledge transfer to local economies.
The New Economic Geography	Krugman (1991)	Krugman develops a general equilibrium model to clarify the spatial concentration of economic activities by focusing on three factors: increasing returns, transport costs and demand for manufacturing goods
Commercial policy theory and trade theory	Bhagwati (1978). Romer (2010)	This provides an understanding of the nature of the relationship between multinational and domestic firms and how the latter could benefit from exports by more efficient use of resources and greater capacity utilization, thus making gains of scale effects associated with large international markets.
Method for the Developing Economy	Hirschman (1985)	In his model, he explains another way in which host countries benefit from multinational firms through the backward linkage.
New trade models	Rodriguez-Clare (1996); Markusen and Venables (1999)	In his model, the beneficial impact of a multinational firm in the host economy depends on its relative propensity to generate backward linkages compared to domestic firms. The author defines the backward linkage coefficient of a firm (domestic or foreign) as the ratio of employment generated in upstream industries (i.e., suppliers of specialized inputs) to the labour directly employed by the firm.

Chapter 3

Empirical Literature Concerning FDI

3.1 Introduction

In line with the development of theoretical literature of FDI, there has also been a substantial increase in the number of empirical studies that examining the determinants of FDI. There are a large number of studies that have empirically examined the determinants of FDI. These studies are different in, for example, research methodology used, and selected countries and years. The aim of this chapter is to reviewing the empirical studies on the determinants of FDI, and also, shed light on the studies investigate the linkage between FDI and domestic suppliers in the light of the models discussed. Moreover, another purpose of this chapter is to find answers in what are the most important location factors for FDI?

Despite the large number of FDI studies, researchers have varied opinions on the factors that determine FDI (Dunning 2002). However, there is general agreement on a number of important factors which include: the host country policies that adoption to promote and facilitate investment and the characteristics of host country economies. The relative importance of different location-specific FDI determinants depends on the motive and type of investment, the industry in question, and the strategy of the investor (UNCTAD, 2008).

3.2 Empirical Determinants of FDI

This section presents a detailed analysis of the empirical research pertaining to FDI, identifying those factors that also support the theories discussed in Chapter Two. The rise in the number of studies evaluating FDI is an indication of its growing interest in FDI theory and many economists have taken up the task of empirically evaluating the determinants of FDI by studying the variables that influence and are influenced by FDI. (Blonigen 2005: 383).

3.2.1 International Trade Theory

Initially, most of the researchers who worked on the Heckscher-Ohlin theory used multiple factors of production from a sample chosen from at least two countries. One of the earliest studies was conducted by Tharakan (1978) using a sample chosen from several European countries i.e. Germany, France and the Benelux states (i.e. Belgium, the Netherlands and Luxembourg) drawing on products from Multi-National Corporations (MNCs). The datasets were as follows: Germany: 34 manufacturing products for one year (1972); France: 15 products for two years (1970-1972) and Benelux countries: 18 products for a single year (1968). Capital intensity, product differentiation and applicable tariff rates were studied. In this context, capital intensity implies the physical capital consumed by a product whilst product differentiation accounted for the differentiating factors and standard production rules in practice. Advertising expenditure was studied as a component of standardization procedures. The results were consistent with the Heckscher-Ohlin theory, identifying capital intensity as the major factor influencing FDI whilst imports were found to be positively influenced by tariff rates. Moreover, production standards appeared to have a greater impact than advertising expenditure.

Another perspective focuses on evaluating factors of production other than the ones typically used i.e. capital and labour force. This approach was adopted in the research undertaken by Clifton and Marxsen (1984) who argue that using only traditional capital and labor is unreliable in terms of determining a country's factor abundance. They adopted an entirely different approach towards determining a country's abundance factor by taking into consideration GDP per person. Thus, in countries where GDP per worker exceeds world GDP per worker, capital abundance is said to be present. From their total data sample of nine countries on several continents, seven countries (Australia, New Zealand, Japan, the United Kingdom, Ireland, USA and Israel) exhibited capital abundance whereas the remaining two (Korea and Kenya) exhibited labour abundance. With the exception of three countries (Israel, Kenya and the UK), the trade structure of all the countries in the sample were consistent with the theory.

Another relevant study is that performed by Wood (1994) which examines capital as a non-static entity. From Wood's perspective, it is a theoretical error to consider capital as a non-static entity when studying international trade but as a static entity in other contexts. He argues that the previous studies considered capital as an immobile factor when, in reality, it is internationally mobile, and this can lead to inaccurate estimates. Wood's research sample included countries representing the industrial North and the developing countries in South. His results were more concerned with trade patterns rather than FDI flows and showed that the North possessed skilled labour and hence traded goods that required skill, i.e. skill-intensive products whilst the South possessed a non-skilled labour force and therefore traded goods that were not skill-intensive.

3.2.2 The Theory of Firm- Specific Ownership

Hymer theory of monopolistic advantage is one of the most prominent in this category and researchers who advocate his theory argue that firms should invest to gain ownership advantage. This allows them to deal with the costs incurred while shifting production into other countries. Lall's (1980) aim was to identify the determinants of successfully expanding MNCs and his research explored transferrable and non-transferrable factors in 25 US-based manufacturing firms. The former included overseas production units, while the latter referred to export. Lall chose explanatory variables and analysed them using the Ordinary Least Squares method. His results showed that the higher the technological intensity within an industrial segment, the higher its productions exports and tendency to expand operations beyond borders. A similar relationship was witnessed in case of two other factors i.e. production skills and scale economies. Moreover, those products that rate high on differentiation factor also support overseas expansion. Firms that maximize the benefits from these factors are bound to have a successful overseas expansion.

Later on, study undertaken by Lall and Siddharthan (1982) studied investments made by US-based firms with the aim of determining the reasons for high levels of FDI inflow there. Data was collected from1974 using a sample of companies representing 45 US industries. The analysis was explanatory in nature and studied multiple variables

including (1) Product differentiation (reflected in the amount invested in R&D and advertisement);(2) Skill level (reflected in industry wage rates for workers in different skill categories); (3) Entrepreneurial advantages (the level of entrepreneurial tendency in each industry was measured by determining the number of employees in non-production posts in comparison to all other employees in a given industry); (4) Multi-plant operations (5) Scale economies, and (6) Trade barriers (tariffs and non-tariff barriers). They concluded that the first three variables did not provide sufficient evidence regarding US investment flows. However, a strong positive relationship was observed in those industries where multi-plant operation was a norm but they reasoned that this might be attributable to the information availability. The second variable that exhibited a strong positive relationship was the trade barriers: the higher the trade barriers within an industry, the higher the overseas expansion supported by FDI.

Studies have also been conducted on samples from other countries to determine the factors influencing FDI. Thus, Saunders (1982) analyses the impact of intangible assets on the foreign ownerships held by Canadian manufacturing firms using a sample of 84 companies. His analysis was based on explanatory variables similar to those used by Lall and Siddharthan (1982). The results confirmed the positive influence of intangible assets on the degree of foreign ownership held by Canadian firms. Anastassopoulos' (2003) study focused on a sample of Greek food companies using data collected from 1988 to 1992. His findings supported the theory of ownership advantage since the factors under consideration (i.e. marketing, knowledge and skill intensiveness) exhibited a strong link with a firm's tendency to expand within the industry.

Studies have also analysed whether the ownership advantage theory is valid in the case of samples chosen from developing countries. A study by Love and Lage-Hidalgo (1999), based on data gathered for the period 1989 to 1992, considered the factors influencing US FDI in Mexico. A sector-wise analysis of several industries was performed. The factors under consideration were R&D, capital expenditure and employee remuneration and they reflected knowledge intensity, capital intensity and ownership advantage. The results

confirmed the existence of ownership advantages within a developing country such as Mexico as well.

3.2.3 Product Life Cycle Theories of FDI

Life cycle theories in particular the Product Life Cycle (PLC) Theory put forward by Vernon (1966, 1979) provide useful empirical evidence regarding FDI patterns. Although there are relatively few publications in this area, the theory still offers some substantial findings about FDI. Hirsch and Bijaoui (1985) conducted research on a large sample of 111 manufacturing-sector companies. Their findings shed light on the role of PLC on the level of company exports, showing that companies investing heavily in R&D eventually have larger exports than those which invest less in this area. Another correlation analysis, carried out by Mullor-Sebastian (1983), found a significant link between growth rates and trade patterns in a sample of three industrial groups. These results supported the PLC theory by demonstrating that industrial groups with higher growth rates exhibited superior performance. Similar research was conducted by Lutz and Green (1983) to evaluate the applicability of PLC on US-based firms using a dataset for the period 1963 to 1974. A simple comparative analysis involving the US, UK, Japan and West Germany showed that the export pattern of the latter did not support the PLC theory.

Turning now to the Uppsala School theory of Johanson and Wiedersheim (1975), this posits a systematic approach towards the expansion of firms into international markets. Davidson (1980) conducted a study using data collected in 1975 from 180 US-based MNCs firms to evaluate this theory. At that moment in time, these MNCs were working on 13,000 FDI projects. Results showed that those countries where the MNCs had a good corporate experience had a higher chance of receiving more future investment.

Knowledge of the target country culture has also been identified as a key factor influencing FDI patterns. This is supported by Erramilli's (1991) study which analysed the internationalization patterns of a sample of 151 US-based firms from the service industry. The results showed that those firms with extensive experience of FDI were

more confident about investing in entirely different cultures than those lacking experience. Another study, along similar lines, was conducted by Kogut and Singh (1988) using a data sample for the period 1974 to 1980 collected from 228 firms that had entered the US market. The results reinforced the earlier findings that knowledge and experience serve to lower the impact of cultural differences on investment decisions.

Noting that previous studies had investigated the role of experience in specifying the entry mode, Eriksson *et al.* (1997) took a new approach to the effect of cultural distance on FDI by taking into account investor perceptions about the cost involved. Their study analysed a sample of 362 firms based in the US service industry and found that lack of cultural knowledge translates into an exaggerated perception of cost. When making FDI decisions, the costs being considered involved collection, encoding/decoding and transmission of information. In addition, costs were entailed in customising organizational resources to suit cultural requirements. Collectively, these costs influence FDI decisions.

Although PLC theory was useful in identifying many of the determinants of FDI in earlier years, it still lacks the depth necessary to explain more contemporary patterns of FDI (Moosa, 2002). This is evident in the fact that PLC is unable to explain the reasons for the simultaneous launch of new products in multiple markets, when markets occupy a different position on the lifecycle curve.

3.2.4 Firm-based theories of FDI

This section discusses the findings of empirical research performed in the area of internationalization theory which has been one of the most successful and has also generated most interest in terms of practice. The theory outlines a systematic process for expanding operations into foreign markets. It provides options such as exporting, subsidiary, licensing and FDI for entering international markets. Advocates of this theory prefer to choose FDI when it is a cost-effective means of gaining access to certain resources in international markets as compared to internalizing these resources.

Initial research in this area did not produce much support for internationalization theory. Rugman (1981) took a sample of 35 firms consisting of foreign subsidiaries and firms based in Canada. The results showed that subsidiaries exhibited lower investment in R&D, whereas their Canadian counterparts invested higher amounts in R&D. The prime reason for the low investment in research was to internalise the technological resources of the company. This theory was also applied to a sample of Japanese firms which had invested in the US manufacturing sector in a study performed by Pugel *et al* (1996). This found that high technological assets (measured by R&D) and marketing assets (measured by level of advertising) have a higher positive effect on Japanese FDI which could able these firms to internalize ownership in the US manufacturing sector.

3.2.5 The Eclectic Paradigm

Dunning's Eclectic Paradigm provided the theoretical base for many empirical studies aimed at determining the factors influencing FDI. This theory combines multiple schools of thought and has therefore generated a great deal of FDI-related research concerning the contemporary scenario and also covering firms operating in foreign markets.

One of the earliest studies in this category was conducted by Dunning and McQueen (1981) who analysed inward FDI patterns and internationalization activity in the hotel industry. A large sample consisting of 81 MNCs from 22 countries oownership of 1025 international hotels was selected. The fact that the MNCs were based in 22 countries added more depth to the analysis. The results supported the theory, showing that ownership advantage ultimately translates into higher FDI and lower management costs. Propriety rights such as trademarks, knowledge and experience were found to be factors contributing to ownership advantage.

Galán and Benito (2001) analysed the key determinants of FDI inflows into Spain by taking into account multiple potential factors such as ownership, location and resource withholding, etc. The findings revealed that a firm's intangible resources, including

experience, management skills and innovation, played the most important role in determining FDI.

The Eclectic Paradigm provided theoretical support for a study by König (2003) which focused on the Swiss context. By applying logit and probit methodology, the research showed that FDI was affected by ownership, R&D and new product launches. In addition to these intangible factors, firm size also proved to be significant in determining overseas expansion.

Driffield (2002) studied FDI inflows into UK using a data sample collected from manufacturing firms during the period 1984 to 1992. The independent variables studied came under multiple categories including ownership, trade pattern, location etc. The result showed that: (1) FDI was positively influenced by ownership advantage factors such as R&D expenditure, advertising and capital intensiveness; (2) FDI was influenced by location factors such as concentration of operations and an earlier investment record for the location; (3) FDI was influenced by export and import, but a lesser extent than location factors; and (4) lastly, FDI was positively influenced by the degree of profitability and market size.

The Eclectic Paradigm was applied by Tatoglu and Glaister (1998) to study foreign investment in Turkey by foreign MNCs. The sample included 98 Western subsidiaries operating in Turkey in the manufacturing and service industry, using data collected for the years 1954 to 1994. A logit regression analysis of the data sample revealed that ownership advantage, in the form of managerial expertise, technological skills or scale economies, had a positive impact on the investment pattern. The study also found that service firms have a lesser tendency to internalise the ownership advantages whereas manufacturing firms tend to internalise their ownership advantages due to the nature of the higher transaction costs in this sector compared to those in the services sector. Moreover, investment by service firms is more susceptible to location advantage because the entire service industry thrives on the host country's infrastructure, policy framework concerning foreign investment and labour policies.

Lastly, Pheng and Hongbin (2006) provided empirical evidence of the Eclectic Paradigm using a sample of data for 2001 collected from 31 Chinese construction sector companies. Their results showed that Chinese firms invest more when offered ownership advantages such as good reputation and readily available resources. The decision of Chinese MNCs to enter a market is influenced by the concentration of other Chinese firms already there. Internalization advantage becomes a significant variable only when it leads to performance enhancement due to a decrease in transaction costs.

Having reviewed the empirical studies pertaining to determinants of FDI, it is evident that ownership advantage is a significant variable encompassing managerial knowledge, the technological skill set, corporate experience and proprietary rights (i.e. trademark). Apart from ownership advantage, location advantage is another major factor effecting FDI.

3.3 Location Determinants of FDI

This section will highlight the existing literature that has focused on identifying specific factors relating to specific national economies and facilities and utilities that may serve to promote FDI in host countries. Many empirical studies on the locational determinants of FDI are focused on either the host or the home country (Moose, 2007). These studies are guided by theoretical frameworks, but have utilized different analytical approaches including cross-section, time series, panel data, and survey, and have used a variety of explanatory variables. The studies have mainly focused on MNCs from the developed countries as either home or host country, and fall into two groups. The first explains the characteristics of investment that flows from one home country to one or several host countries, whilst the second explains the flow from several home countries to one host country. This section reviews empirical studies for both developed and developing countries across different geographical regions, focusing on a range of factors that are discussed in the theoretical literature.

Various studies have focused mainly on factors which may influence foreign investment decisions or locational choices for FDI based on evidence from a range of different

countries and regions. The focus here is mainly on the following factors: economic and market conditions, policies toward FDI (including government regulations and tax incentives), and utilities and facilities (such as domestic infrastructure, human capital, natural resources, research development, and financial and legal institutions). However, it should be noted that the locational factors of FDI have taken various forms of measurement in the existing literature as researchers have made use of several different proxies to measure the factors that can be used to explain the dependent variables, the amount or probability of attracting FDI within a particular region. For example, the market size variable usually takes one of several different proxies, namely, GDP, GNP, lagged GDP or per capita GNP. In the rich literature of empirical studies on this topic, most of these variables have been tested.

3.3.1 Country-Specific and Risk Factors

3.3.1.1 Macroeconomic stability

The host country's macroeconomic stability is often considered by investors as a key factor in their location decisions. Many studies, such as those by Bellak *et al.* (2009); Arratibel, et al (2011), and Rogman and Ebbers (2013), have highlighted the role of economic growth, inflation rate, exchange rate (which is representative of the comparative stability of Libyan currency), and the extent of government intervention in economic activities and privatization process. All of these are indicators of macroeconomic policies and conditions of economic liberalization in the host countries, which seem to be one of the most important determinants for inflow of capital aimed to serve domestic regional and international markets. Market-seeking FDI uses market size as a benchmark of potential demand for output. Macroeconomic stability stimulates the inflow of FDI to a country and vice versa (Zhang, 2001).

As described below, previous studies have found a significant positive correlation between economic stability and FDI (Buckley *et al.,* 2007; Alavinsab, 2013). Various economic indicators have been used in such research including economic growth which is

necessary for attracting FDI (Moosa, 2007). Empirical evidence showed that the countries with the fastest growing economies are the biggest FDI host countries (UNCTAD, 1998). Some researchers have replaced economic growth by GNP or its growth rate, GDP or its growth rate, per capita GNP or its growth rate (Grosse and Trevino 1996; Thomas and Grosse, 2001; Bevan and Estrin 2004; Bellak *et al.,* 2009; Frenkel *et al.,* 2004; Oladipo, 2010; Rogman and Ebbers 2013). Some others have applied actual growth rates for GDP or for per capita income (Oladipo, 2010; Friedman *et al.,* 1992; Bhavan *et al.,* 2011; Dunning 1994).

Using a gravity model on a dataset for the period 1995 to 2004, Bellak *et al.* (2009) analysed bilateral FDI outflows from seven countries to eight Central and Eastern European Countries (CEECs) hosts, the result showing that the GDP growth per capita of the host country has a positive impact on FDI. Oladipo (2010) used a different method of data analysis, employing time-series data from 1970 to 2005, to examine the factors influencing FDI inflows into Nigeria, but obtained similar results with GDP and also overall macroeconomic stability being positively related to FDI inflows.

Another study by Kolstad and Villanger (2008) showed that a higher amount of FDI is attracted to host countries with higher GDP per capita. However, from a different perspective, Xing (2006) examined the determinants of Japanese FDI for nine Chinese manufacturing sectors from 1981 to 2002. He argued that the real exchange rate is one of the significant factors affecting Japanese FDI inflow in China and other variables such as rising GDP growth rate are also significant, but less important, particularly in short-term FDI inflows. The study indicated that the real growth of each sector also contributed to the surge of outward Japanese FDI to China. Alavinsab (2013) used the least squares technique to investigate the economic determinants of inward FDI in Iran for the period 1991-2009. He also found that the rate of growth for GDP has a significant and positive relationship with FDI inflows in Iran.

Varied results have been found on the influence of exchange rate (measured in units of foreign currency per domestic currency) on FDI inflows: A case study on Ghana by Kyereboah-Coleman and Agyire-Tettey (2008) on the volatility of real exchange rate shows that the volatility of the real exchange rate has a negative influence on FDI inflow while empirical investigation of firm level data on the US FDI to Korea (Jeon and Rhee, 2008) shows that FDI inflows have significant association with real exchange rate and expected exchange rate changes just as the results of Ramiraz (2006) and Cushman (1985) arm the same. However, Brahmasrene and Jiranyakul (2001) and Dewenter (1995), fond insignificant relationship between the level of the exchange rate and FDI inflows, also studies such as (Graham and Krugman, 1995; Thomas and Grosse, 2001; Naude and Krugell, 2007 and Arratibel, et al 2011) provided more evidence in this context.

In his study, Russ (2007) used the endogeneity of the exchange rate as a determinant of FDI and found that the variance of the exchange rate has an impact on the multinational company's decision to enter a particular market. Similarly, Erdal and Tatoglu (2003) also claimed that in the case of Turkey the highly volatile exchange rates of the currency had a negative relationship with FDI inflows, discouraging foreign investments.

Higher inflation rates are normally used as an indicator of macroeconomic instability reflecting the presence of internal economic tension and of the inability of the government and central bank to balance the budget and restrict money supply (Schneider and Frey, 1985). When Woodward and Rolfe (1993) examined the relationship between inflation rate and FDI inflow to the Caribbean countries, they found this variable statistically significant and negative. Another study conducted by Addison and Heshmati (2003) used the rate of inflation as determinant of FDI inflow to 207 countries, concluding that inflation has a negative effect on FDI inflow for Central Asia, Europe, and MENA regions while it has positive effects for Latin American countries They explained that this positive relation might refer to the fact that a high return promotes FDI and consequently the growth in the prices of products the investor has invested in, should

be positively associated with FDI. Various other studies such as Buckley *et al.,* (2007) have used inflation rate as a proxy for macroeconomic instability, finding that a low rate of inflation attracts more FDI. Also Ho and Rashid (2011) confirmed that low inflation rates have a positive impact on FDI inflow in South ASEAN countries, particularly Thailand. The study concluded that there was enough evidence to indicate that a reduction in inflation rate could lead to a rise in FDI inflow in a developed market. The same results were reported by Asiedu (2002) who examined the determinants of FDI in sub-Saharan African countries and found that low inflation rates promote and stimulate FDI within the region.

Openness policies can take different forms from a simple bilateral trade agreement to a more elaborate open economy with no trade restrictions such as Singapore. This can also entail a low level of government intervention in economic activity or increased privatization, which helps to provide a greater role for the private sector to lead the economy. These market forces play a leading role in the resource mobilization. The immediate outcome of such openness policies is a free-market that serves to connect a country to the rest of the world. It acts to direct capital and technological flows to and from a country. Establishment of an open economy requires the reduction of trade barriers to encourage exports and ultimately leads to inflow of FDI. There are numerous other benefits of openness policies. They can stimulate economic activity and open up new avenues for companies to exhibit their products and services. One driver of FDI flows is the market liberalization of the host country, as is financial liberalization, permitting capital to flow without any restrictions across the globe (UNDP, 2005). Moran *et al.,* (2008) highlighted that host countries with an open economy and business environment are more able of improving on other related areas. This produces enhanced production processes and the overall lifestyles of the people. Moreover, Mina (2007) found that the influence of trade openness is positive and statistically significant in explaining changes in FDI in the Gulf Cooperation Council (GCC) countries. Erdal and

Tatoglu (2003) also indicated that the degree of openness in the host countries has a significant relationship with FDI inflows.

3.3.1.2 Market Conditions

The situation of the host country market is one of the most important determinants of FDI consisting of trends in the local market and its size which is usually measured by per capita GDP income levels as a sign of increases in the market size and purchasing power. Other measures include competition in the local market; existence of distribution channels, and the availability and reliability of market information. FDI flow usually associated with countries that have expanding markets and where purchasing power is higher or investors expect higher return on their investment (Jordaan, 2008). Foreign firms targeting a local market are attracted to countries with high growth rates in their market since this indicates a larger potential demand for their products. The market-seeking FDI aims to penetrate the local markets of host countries and is usually connected with market size potential and growth, per capita income, access to regional and global markets, and structure of the domestic market and the level of competition with in the economy(UNCTAD, 1998).

Market size represents the level of demand for goods and services in the host country, and it is usually proxied by a measure of either GDP or GNP. Most of this literature identifies market size as an important determinant of FDI (Garcia-Fuentes *et al.,* 2013). China has been the largest recipient of FDI among the developing countries since 1992, and has been the second largest FDI recipient in the world since 1993 (UNCTAD, 2013).

The literature about US FDI in Latin American countries has also indicated positive and significant effects of market size on US FDI. Investigating the determinants of US FDI in Mexico for the period 1967 to 1994, Love and Lage-Hidalgo (2000) found per capita GDP had a significant positive effect on US FDI. Lall, Norman and Featherstone (2003) examined the determinants of US FDI for a group of Latin American countries over the

period 1983 to 1994. They found GDP, GDP squared and GDP growth to have significant and positive effects on FDI.

Many empirical researchers found a positive significant link between market size and host country potential which is usually measured by GDP or its growth rate and FDI including (Kolstad and Villanger, 2008; Chidlow, *et al.* 2009; Mina, 2007; Havrylchyk and Poncet, 2007; Bellak *et al.* (2009); Kimino *et al.,* 2007; Bhavan *et al.* (2011); Ledyaeva, 2009; Arratibel, et al (2011); Rogman and Ebbers, 2013; Oladipo, 2010).

Kolstad and Villanger (2008) found that different measures of market size are significantly related to FDI inflows in the finance sector. In similar results, Erdal and Tatoglu (2003) found that the size of the domestic market of the host country is positively related to FDI inflows. As domestic market size increases, the number of customers and opportunities for foreign investors will increase. According to Chidlow *et al.* (2009), when tested, market size was found to be related to FDI inflows in Poland, indicating that market-seeking foreign investors are influenced by these when establishing their business or investments outside the parent country. Oladipo (2010) also found a positive correlation between inward FDI and potential market size (proxied by the growth rate of real GDP and real GDP per capita) in the case of Nigeria. Jadhav (2012) also found a significant positive relationship between inward FDI and market size in the cases of Brazil, Russia, India, China, and South Africa.

3.3.1.3 Policy Framework and Regulations relating to FDI

Other factors influencing location decisions include continuity of government policy, levels of government bureaucracy or red tape, and roles and regulation for foreign nationals and companies entailing ownership of land and property. Flexibility of regulation for investors and transparency may be critical in investment decisions, as well as the extent of corruption, tax exemptions and government subsidies, including reductions in import duty on machinery, components, and materials; and tax rates on income and dividends.

Taxation policy affects the location decisions of foreign firms because it is related to investors' strategic objective which is maximization of profit. Developing countries usually use fiscal incentives, such as reductions in the base rate of corporate income tax, and import-duty exemptions, to attract FDI (Oman, 2000). It was presumed that tax concessions tax holiday would have a positive relationship with FDI, as taxes have a direct effect on profit, and are therefore believed to significantly affect FDI decisions. However, this effect is not straightforward, depending upon the tax instrument used, the characteristics of FDI, and the relationships between the tax systems in the home and host countries (Morisset and Pirnia, 2001).

Studies relating to taxation on FDI decisions produced various results. Some found that State and local taxes acted as a strong deterrent to FDI Bustos (2011), while others discovered a weak relationship between tax and FDI (Coughlin *et al.,* 1991; Gorg *et al.,* 2008). One study on Japanese FDI in the US reported varied results: state unitary taxes appeared to act as a significant deterrent, while corporate tax had no impact (Woodward, 1993). Evidence of the significant negative influences of corporate tax rates were also reported in previous studies (Gastanaga *et al.,* 1998; Wei, 2000).

With regard to import duties, the effect of tariffs differs for different types of FDI expansion, whether this is horizontal or vertical. A typical vertical FDI can be characterized by individual affiliates specializing in different stages of production of the output. Horizontal expansion, on the other hand, involves each affiliate engaging in similar types of production as the parent company. Vertical FDI may be encouraged to invest in a country with relatively low tariff barriers due to the lower cost of their imported intermediate products and the greater reliability of supply and increased efficacy in reducing cost and price of production. Therefore, the import duty variable is negative in this case. In contrast, high tariff barriers induce firms to engage in horizontal FDI, and thus, replace exports with production abroad by foreign affiliates (Culem, 1988).

Corruption and bureaucratic red tape is another key determinant of FDI which could be expected to affect FDI, since a high rate of corruption increases costs of production (World Bank, 2013). Three common measures of corruption were used in most empirical studies as corruption is not easily quantified. One of these measures was based on surveys conducted by Business International and used in work by Wei (2000). In another study, Wei (2000) made use of a second measure identified by the International Country Risk Guide. The final measure was the Corruption Perceptions Index (CPI), compiled by Transparency International, used by Smarzynka and Wei (2000). The occurrence of corruption usually correlated with dimensions of government quality such as the level of bureaucracy and red tape (Urata and Kawai, 2000).

Opinions on the impact of corruption on FDI are divided, and previous studies on this issue fall into three groups. The first group, which comprises the majority of the studies, suggests that corruption affects FDI negatively; thus Wei (1997) found that corruption has a large and significant effect on FDI, supported by Asiedu (2006) who found that FDI grew more rapidly in less corrupt countries. Corruption decreases the rate of return by creating higher costs for doing business which discourages FDI. FDI needs consistency and transparency in policy-making by host countries and is averse to gratuitous bureaucracy and red tape which are often associated with corruption (UNIDO, 2005).

The second group of studies focusing on corruption proposes that corruption could have a positive impact on economies with low levels of protection and property rights (Quazi *et al.,* 2014). Quazi analysed the impact of corruption on FDI inflows in 53 African countries over the period 1995 to 2012 using the Generalized Method of Moments (GMM) and found that corruption facilitates FDI inflows to African countries. Results from the third group indicated that either the relationship between corruption and FDI is insignificant or that the results are not decisive. Helmy (2013) used data from 21 MENA countries over the period 2003 to 2009 employing panel data estimators in order to assess the link between corruption and FDI flows to the region. Helmy's empirical results suggested that corruption in MENA does not discourage FDI inflows to these countries.

Also, other types of government legislation are important for inflows of FDI as less transparent property rights and economic policies led to increases in the cost of investment as result of lack of information provided by government department (Bangoa *et al.,* 2003). The general quality of governance in host countries can play a crucial role in either attracting or deterring FDI. Government regulation was found to significantly affect FDI inflows into African countries (Quazi *et al.,* 2014).

3.3.2 Facilities and Utilities Factors

Facilities and utilities factors refer to human capital resources, natural and physical resources, and financial and legal institutions, and R&D.

3.3.2.1 Human Capital Resources

Another perspective was put forward by OECD (2003:20) in their study which focused on issues such as training and development of human capital. Training sessions directed towards enhancing a technical skill set in the workforce attract foreign investors interested in technology-intensive projects. This is because training implies availability of skilled yet still cost-effective human capital in the host country. Many studies attempt to investigate the impact of labour force on FDI including both the costs and quality of labour where rates of pay act as a proxy for labour costs while labour quality is measured by the availability of a semi-skilled and skilled labour force (Onyeiwu, 2003). In general, workforce quality is an important determinant of the marginal value of investment, as higher quality labour implies higher profitability or higher quality products, and thus, enhances competitive advantage for FDI (Lucas, 1988).

Since cost minimization is a prime motivation for foreign investors establishing a plant abroad, labour costs have been widely tested as an influence on the locational choices of FDI. Low labour costs are supposedly an attraction for FDI, and conversely high labour costs are thought to deter FDI entry. It is predicted that foreign firms would prefer lower waged locations in order to minimize production costs. This research, however, yielded mixed results. A positive relationship was highlighted by a number of studies such as

those by Cassidy and Andreosso-O'Callagan (2006); Chidlow *et al.* (2009); Alam and Shah (2013); Oladipo (2010); Bellak *et al.* (2008); and Bavan *et al.* (2011). A negative relationship between labours cost and FDI was found in studies by Havrylchyk and Poncet (2007) and Barrell and pain (1996) whilst other research indicated an insignificant relationship (Kimino *et al.,* 2007; Chen, 1996). Labour skill is more significant for those host countries where more capital and technology-intensive investment projects are concentrated.

These mixed results may be caused by the fact that in some countries, wages already reflect levels of labour productivity or quality. High wages, in this case, mean high labour quality and thus, would attract more FDI (Li *et al.,* 2008; Onyeiwu, 2003). In other cases, the significance of labour cost may be outweighed by other production and transaction costs, such as political stability (Grosse and Trevino, 1996). Low labour cost is considered a more important determinant for small than for medium to large firms, as the former are more cost sensitive (Kinoshita, 2003).

From the perspective of the foreign investor, the importance of labour costs has been highlighted and confirmed by number of studies which used the wage rate as a proxy for labour costs including Cassidy and Andreosso-O'Callagan (2006); Chidlow *et al.* (2009); Bitzenis *et al.* (2009); Alam and Shah (2013) and Oladipo (2010). Cassidy and Andreosso-O'Callagan (2006) found that labour costs were generally a critical determinant of FDI. Their study shows that disparities in the cost of labour within and between countries are apparent in market economies. Chidlow *et al.* (2009) suggested that low labour costs and productivity costs as well as the availability of labour are positively significant in explaining FDI inflows in Poland. Bitzenis *et al.* (2009) found that labour market structure tends to be one of the primary barriers to FDI inflows in the case of Greece. Alam and Shah (2013) indicate that labour costs affected investor decisions, as host countries with low labour costs were preferred by investors wishing to reduce the costs of their business and products. The same results were reached in the case of FDI inflows to Nigeria (Oladipo, 2010). However, Dunning (1980) found a positive

relationship between the two, arguing that wage rates could be treated as a proxy for labour quality. Nevertheless, a negative relationship between labour costs and FDI is expected when labour costs are adjusted for productivity.

3.3.2.2 Natural and Physical Resources

This category includes the supply of raw materials which can be measured in terms of availability, cost and quality. Raw material supply is anticipated to have a positive relationship with FDI, especially for the resource-seeking FDI (Dunning, 1993; UNCTAD, 1998).

The availability of natural resources of the required quality and standard as a major factor in attracting FDI and promoting economic development has been established by a number of studies. Buckley *et al.* (2007) emphasise that most Chinese foreign investment targets natural resources. Dunning (1979) argues that companies usually target natural resources which are available in huge quantities abroad while maintaining production in their home countries. This argument is corroborated by Anwar (2008) who states that most multinational companies in the fledgling markets are state-owned and seeking natural resources to meet increasing local demand for these resources which are cost prohibitive in the home country. South Korea is a case in point where the government encourages local companies to intensify the search for natural resources abroad in order to secure cheap and sustainable inputs for the Korean economy (Han and Brewer, 1987). Likewise Chinese government-owned MNCs look for foreign natural resources in order to provide the local economy with cheap inputs (UNCTAD, 2005).

Acheampong and Qsei (2014) used a time-series annual dataset from 1980-2010 to identify the determinants of FDI in Ghana by employing an econometric methodology. Their findings indicate that the inflows of FDI into Ghana mainly depend on natural resources in the short-run. Anyanwu (2012) examined the relationship between the availability of natural resources and inward FDI, employing cross-country regressions for the period 1996-2008 using data from African countries. His results indicate that the

availability of natural resources has a strong positive impact on FDI inflows. Koka *et al.,* (2012) found the same result in the case of Nigeria where natural resources were critical factors for inward FDI and the remaining locational factors were less important.

3.3.2.3 Availability and Quality of Infrastructure

The availability of quality of host country infrastructure can be a critical determinant of FDI and is believed to have a decisive effect on foreign investor decisions. Infrastructure covers a broad range of components including cost and quality of energy and utility supplies; cost of transportation systems; cost and quality of communication systems as indicator of infrastructure levels which can increase productivity and boost the locational advantages of a host country (Quazi *et al.,* 2014). Poor infrastructure increases the cost of business by creating unreliability which reduces the rate of return on investment and vice versa (Moosa and Cardak, 2006). This factor has been frequently examined and various measures of infrastructure levels, including their quality, have been identified as having a positive relationship with FDI. The infrastructure includes many facilities that can provide an efficient environment for foreign investors to do business. The transportation system is one of the most important elements, since a location with convenient access to various transportation systems can save producers both transportation costs and time. Hence highways, railways, and ports are considered important variables that influence the locational choices of FDI. Previous studies have tested these variables (Majocchi and Strange, 2007; Bavan *et al.,* 2011; Soumia and Abderrezzak, 2013; Moosa, 2007; Havrylchyk; Alfaro, 2010; and Poncet, 2007).

Empirical studies also show that those countries with more developed infrastructure have a tendency to attract FDI. This helps to explain the concentration of FDI areas with extensive high technology infrastructure in external markets. Mina's (2007) study indicates that infrastructure developments tend to be an important determinant of FDI and are positively significant in explaining changes in FDI inflows. Acheampong and Qsei (2014) reached the same conclusion in the case of Ghana particularly in the case of long-term FDI. Erdal and Tatoglu (2003) noted that investors prefer to invest in a country with

established infrastructure. Their study showed that infrastructure development is positively significant in explaining FDI movement. A well-developed transportation system reduces production costs by decreasing the costs of importing components and machinery, and exporting outputs.

In terms of telecommunication industry development, a study by Gholami, et al (2003) found that telecommunication advances are important in permitting information exchange to develop as a valuable commodity. Countries that are equipped with better and more sophisticated telecommunication technologies and systems have been rapidly transformed into post-industrial, growth-oriented information-based economies. The study also concluded that technical progress in telecommunication services was one the factors that facilitated the rapid expansion of world FDI. Alam and Shah (2013) employed the Granger causality test to investigate the relationship between FDI and infrastructure in OECD member countries over the period 1985 to 2009. Their findings indicate that infrastructure has a positive relation to FDI.

It has been maintained that the infrastructure services constitute an important determinant for attracting FDI. In this context, Kamaly (2004) surveyed 23 developed and developing countries to identify the determinants of investment and other factors influencing investment activities with the aim of applying these to the Egyptian context to enable it to benefit from the successful experiences of other countries. He concluded that the main determinant of FDI was good infrastructure. Another study by Alavinsab (2013) concluded that the same factor was one of the most important determinants of FDI for Iran.

3.3.2.4 Research Development and Training System Factor

This factor includes the availability of industrial research and training support in the home country. The efficiency-seeking FDI is motivated by creating new sources of competitiveness for the firm; thus, there is more focus on the host country's investment in industrial training and R&D (UNCTAD, 1998).

An alternative view of local research ability could be that a stronger local research orientation may reduce the comparative advantage of foreign investors, which could make them less enthusiastic about locating in a region. Chen (1996), for example, argued that domestic firms that are more technologically progressive can out-compete foreign investors. Thus, foreign firms may prefer to locate away from the seedbeds of domestic technological innovation. It is also possible that foreign investors who have advanced technology may be cautious about technological spillovers to domestic firms, and may choose a location where domestic R&D is too weak to benefit from any spillovers. Most researchers point out that this depends on the characteristics of foreign investors. Indeed, mixed results have been found regarding the influence of R&D capacity on FDI locational choices. In China, R&D capability was found to have a negative relationship by Chen (1996), but a positive by Zhao and Zhu (1998).

Oakland (2003) revealed that the training and development of the labour force has become a significant part of human resource management since the 1980s. Major changes took place in many organisations as a result of the introduction of new technology and a wider range of tasks, all of which require necessary training provision. Kanji and Asher (1996) indicated that the availability and quality of training centres are key factors in improving total productivity.

Kogut and Chang (1991) investigated Japanese FDI across 297 manufacturing industries in the USA and found that more Japanese outward FDI occurred in those industries that had greater R&D expenditure. Another study conducted in 18 MENA countries by Moosa (2007) indicated that FDI flows more to those countries that have better R&D expenditures.

3.3.2.5 Financial Development

Financial development includes access to local sources of fund; cost of capital; availability of financial systems; accounting and auditing standard. Empirical studies

found a significant negative relationship between the cost of capital and FDI (Love and Hidalgo, 2000).

Many countries offer financial incentives to attract foreign investors as these are a good means of appealing to investors when they are linked to factors that benefit the recipient country, for example, linking financial incentives to human capital development or technology advancement which is brought in with the incoming investment.

In Israel, MNCs that introduce new products into the market are given special grants for R&D. This is not simply a one-way flow of capital as the investor receives returns in the form of royalty fees. Finland offers grants to those MNCs which play a role in improving capacity management, an approach which enables the companies to compete better in the global business landscape (Centre for Information and Decision Support, 2004b).

Another type of grants exists for reaping long-term benefits. These grants are development oriented and serve to incentivize capacity enhancement, and eventually leads to the creation of skilled human capital and advanced technology. Such grants are location and project-dependent. Ireland and Hungary, for example, offer financial incentives to foreign companies in return for job creation. A foreign entrant in these markets receives a grant if it generates the specified level of job openings within three operational years. This is just one example of the type of requirements that make one eligible for this grant. Another example is of a minimum investment level and the technology deployed (OECD, 2003, p.17).

3.3.2.6 Legal Factors

In the context of investment, a legislative framework provides a useful support to investors and all concerned parties. An ideal legislative framework offers protection for investor rights and ensures fair competition amongst market participants. Controls to restrict growth of monopolies and unhealthy competition are managed within the jurisdiction of a well-laid economic legislation. Research emphasizes the supremacy of a single and transparent law over multiple laws. Transparent laws are deemed more stable

by investors and play a better role in managing investor concerns. Such laws can deal with the menace of corruption, which is one of the most costly aspects of investing in another country. Therefore, legislation is conducive to promoting business interests and reduces costs for investors (El-Fergani, 2002:24).

Examples of legislative reforms can be found all across the globe. The economic reforms introduced in Mexico, after the 1980s debt crisis, were aimed at bringing economic stability into the economy. The country also undertook extensive measures such as privatization and renewal of State policies to stimulate economic growth. Similar changes were introduced in Brazil to open up the country to foreign investment, with privatization and legislative reforms forming the major part of the reforms. The actions proved fruitful as the country began receiving higher foreign investment in later years (Biglaiser at el, 2006).

In order to maximise the potential benefits by protecting the rights of all parties involved, economic activity should take place under an umbrella of appropriate legislation. However, this legislation should encourage free competition, prohibit monopolies, and protect investment by providing the necessary guarantees for investors. In this context, the multiplicity of laws in relation to investment should be replaced by a single stable law, integral and transparent law. This will make the law more reliable for investors as it facilitates the legal environment for investment. Moreover, effective legislation should be introduced to combat corruption in official circles, as this would also lower costs for potential investors. Moreover, the Steadiness and timely procedures of laws in a legal system is a crucial factor in stimulating FDI flows to the host country (Soumia and Abderrezzak, 2013). In addition, OECD (1994) stated that the frequency of changes in a country's legal policies and bureaucratic/administrative barriers can decisively influence investment choices (OECD 1994).

Another study conducted by Mina (2007) found that institutional quality also positively influenced FDI inflows, as expected, reflecting the importance of this determinant in attracting FDI flows to the GCC countries. Similar results were obtained by Cassidy and

Andreosso-O'Callagan (2006) who concluded that institutional quality proved to be significant and positively related to FDI. Their study recommended that a high quality legal system is an extremely significant determinant of inward FDI in China. These findings were supported by Jadhav (2012) who concluded that the rule of law proved to be significantly and positively related to FDI inflows in the case of Brazil, Russia, India, China, and South Africa.

3.3.3 Determinants of FDI in MENA Countries

Finally, given the nature of the focus of this thesis, it is useful to consider those studies which are related to the determinants of FDI in the MENA countries. There have been a limited number of empirical studies which have considered various aspects of the determinants of FDI flows into these countries but Moosa (2007) argues that there is no widely accepted set of explanatory variables that can be regarded as the exact determinants of FDI in the MENA countries. Earliest study in the region conducted was by Onyeiwu (2003) who tried to identify the key factors, and considered whether they differ from the determinants in the other developing countries. His study covers 51 developing countries, 10 of which are from the MENA region using data over the period 1975 to 1999. Using a fixed-effects regression with panel data to control for country and time-specific factors, the results indicate that some of the determinants in the developing countries appear not to be important in the MENA countries. These include the rate of return on investment, infrastructure and economic fundamentals, such as the real growth rate in GDP, the inflation rate, tax rate and external debt. The significant determinants that explain the relatively low levels of FDI to the MENA are corruption/bureaucracy and the lack of openness to trade.

Chan *et al.* (2004) studied the pattern of FDI in 19 countries in the MENA region and the role of risk, using both fixed and random effects dynamic panel models. They conclude that the degree of instability associated with investment risk is the most important contributory factor to the low level of FDI flows in the MENA region. The location drivers of FDI inflows to the MENA region are also investigated by Hisarciklilar *et al.*

(2006), who use a panel data for 18 countries over the period 1980 to 2001. Applying a fixed-effect model and Maximum Likelihood estimation, they found that FDI in the MENA region is driven by the market size of the host country and the ability to export to other MENA countries, which may give some explanation of the role of risk.

Moosa (2007) used cross-section analysis to examine the determinants of FDI inflows to 18 MENA countries. He applied extreme bounds analysis to test a number of explanatory variables that included the real level and growth rate of GDP, real GDP per capita, exports, telephone lines per 1000 inhabitants (measuring economic development), commercial energy use per capita, R&D expenditure, students in tertiary education (measuring human capital), country risk and domestic gross fixed capital formation. The results are perhaps unsurprising, and indicate that FDI flows more to countries that have growing economies, better education and research, better infrastructure, low risk and a higher return on capital.

Rogman and Ebbers (2013) employed multiple ordinary least squared models to analyse a United Nation Conference on Trade and Development (UNCTAD) dataset of 16 MENA countries for the years 1987 to 2008. They ran FDI flows on a set of variables such as market attractiveness (measured by GDP per capita), openness to trade (measured by exports as a percentage of GDP), political risk (measured by environmental risk comparable with other countries), natural resources (measured by total oil and gas reserves) and oil prices (measured by world oil price at the start of the year). They find that oil prices and openness are positively associated with FDI, while the country's oil and gas reserves were negatively associated with FDI. The other two variables (GDP per capita and political risk) were not found to be significantly associated with FDI performance.

Within the Arab Maghreb Union (AMU) region there are a small number of researches regarding the determinants of FDI. Soumia and Abderrezzak (2013) examined the factors determining FDI inflows in the Arab Maghreb Union (AMU) countries from 1980 to 2010 using a dynamic panel system GMM estimator. Their findings revealed that

political stability is an important determinant of FDI in AMU countries. Policies improving the legal framework, infrastructure, good governance and judicial system are found to be economically less important determinants of FDI inflows in AMU countries.

Ben Taher (2010) investigated the determinants of FDI inflows in the AMU countries including Libya over the period of 1970-2006. After applying quantitative data analysis to the independent variables that include market size, economic openness, wage rates and country risk, the study concluded that the level of GDP appears to have a significant positive effect on FDI flows, while international trade has a negative effect. In terms of the country risk, the results show, like other studies for the MENA region, that it has a significant negative effect on the overall flow of FDI.

The only research paper regarding the determinants of FDI in Libya is by Abdulla (2010) who investigated the determinants of FDI inflows in Libya over the period of 2003-2009. By applying a descriptive analysis and statistical analyses such as frequency, chi-square goodness of fit and cross-tabulation tools to the independent variables that included market size (GDP), "openness", bureaucracy, wage rates and country infrastructure, El Fergani was able to evaluate the success of the Libyan business environment at attracting FDI. This study concludes that despite the success of government policy at attracting FDI, there are still difficulties associated with the Libyan business environment. The level of GDP and wage rates appears to have a significant positive effect on FDI flows, while bureaucracy has a negative effect. In terms of the country's infrastructure, the results show that a poor infrastructure has a significant negative effect on the overall flow of FDI. The research, however, did not mention anything about the differences between each type of FDI's requirements or the effect of foreign companies on Libyan domestic suppliers, which were the major goals of the Libyan government.

This chapter has presented the empirical evidence on the theoretical determinants of FDI. Overall, it is clear that the main focus of the empirical work is on FDI flowing between developed countries, but researchers initially sought to explain this in terms of differences in the characteristics of countries. This was not wholly successful, and it was only after

Hymer's theory that the focus of the empirical work shifted to the characteristics of the MNCs themselves. Subsequently, empirical work has largely been based on the widely accepted Eclectic Paradigm framework, examining the determinants of FDI in developed and developing countries. This paradigm draws attention to the locational determinants of FDI, and research has been conducted for many different countries and regions, including the MENA countries. From the vast literature, which can sometimes produce contradictory results, it is possible to conclude that some of the main determinants of FDI flows include a whole array of factors, such as economic and market condition, labour costs, human resources, government policies, infrastructure, and the quality of institutions including financial and legal institutions. These potentially provide support for many of the discussed theories.

3.4 Empirical Impact of FDI on Host Economy

FDI plays an important role in the economies of both developed and developing countries alike. In spite of the controversies surrounding the benefits and costs of FDI, several studies have investigated the relationship between economic growth and FDI (World Bank, 2010). Some studies are concerned with measuring the impact of FDI on the rate of economic growth in general, while others concentrate on specific economic or political variables and their impact upon growth. For example, some studies focus on the impact of FDI on production, while others assess the impact on economic aspects such as foreign trade, various manufacturing strategies and what these mean for growth and local investment, other research gauges this impact by evaluating the linkage between FDI and domestic firms. Many countries have managed to achieve extremely positive effects from foreign investments.

3.4.1 The Impact of FDI on Economic Growth

Developing countries often face the problem of unemployment since despite the availability of the workforce, there are limited job opportunities. Given this scenario, FDI often in the form of huge projects, can provide much-needed job openings and financial

support to host country residents. Projects that require forward and backward integration are even better at solving the unemployment issue. Therefore, FDI serves to provide direct as well as indirect benefit to the employees in the host country Ramirez (2006). Ramirez conducted a study designed to determine the employment implications of FDI. The sample consisted of economy level data for the years 1960 to 2001. The findings revealed that worker productivity rises as the figure for FDI per worker increases.

Esquivel and Rodríguez-López (2003) carried out another study along similar lines, studying the effect of FDI on Mexico with reference to the North Atlantic Free Trade Agreement (NAFTA). A comparative analysis was carried out using data from 1988-1994 and from 1994-2000. The study found that trade liberalization brought in through NAFTA did not serve to lower the wage gap immediately, mainly because the Mexican workforce did not have the skill set to match the technological requirements for investment projects. Thus, initially, at least, NAFTA produced a small impact on the Mexican workforce.

There is a difference in perspective when examining the implications of foreign investment. Feenstra and Hanson (1997) conducted a study on investment in Mexico by the USA, finding that the Mexicans viewed the incoming investment as skilled and semi-skilled labor intensive. On the other hand, the US firms viewed this as outsourcing of unskilled but labor intensive tasks.

Lastly, a study by Haddad and Harrison (1993) showed that foreign investment causes improvement in administrative procedures. The investment allows companies to conduct training and development, which is bound to improve working conditions in the host country. FDI introduces advanced business administration methods which ultimately improve business performance.

Bengoa *et al.* (2003) carried out a study of Latin American firms, collecting panel data for the years 1970 to 1999. The results reinforced the previous empirical research that FDI has a positive effect on the recipient country's economic health. However, the more

advanced the human resources, and the greater the degree of economic stability and liberalization within a country, the more pronounced is the impact of FDI. Another study on the same sample was carried out by Bengoa and Sanchez Robles (2005) to evaluate how the state of the economy interacts with the effects of FDI and concluded that countries with economies in transition can still experience the impact of FDI.

Chowdhury and Mavrotas (2006) used the Granger Causality model with the LA-VAR technique in their study to test the causality between FDI and economic growth on the cases of Chile, Malaysia and Thailand. The findings stated that no causality was seen in the case of Chile whereas the other two countries showed bidirectional causality. A more advanced analysis was carried out by Ali-Irani and Al-Shamsi (2007) who employed the Granger Causality model with the LA-VAR technique on member countries of the Gulf Co-operation Council (GCC). The study concluded that bidirectional causality was present between FDI and economic growth in Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and UAE.

Bengoa and Sanchez-Robles (2005) conducted another study on Latin American firms to determine the impact of another variable, namely policy measures. Their results demonstrated that liberalization stimulated by policy measures also adds to the positive effect of FDI on the GDP per capita of the recipient country. The access to technology is another contributory variable in this relationship.

Del Sol and Kogan (2007) studied the case of Chilean FDI. They made similar findings to Bengoa and Sanchez-Robles (2005) but observed a difference between access to technology and actual flow of technology. The main aim of the research was to establish the basis for the competitive advantage of the sample firms. The study concluded that competitive advantages arise as a result of business knowledge gained over the years of host government policy of economic liberalization.

Single and simultaneous equation techniques were utilized in a study by Li and Liu (2005) to analyse FDI patterns and economic growth. The study arrived at two main

findings. Firstly, FDI and economic growth exhibit a strong relationship. Secondly, FDI indirectly influences economic activity by first improving the human resources of a developing country.

Other studies have established a relation between FDI and economic growth, but with conditional factors, including the initial level of development (De Mello, 1999; Zhang 2001; Sukar *et al.* 2007). Using a time-series and panel data sample from both developed and developing countries over the period 1970-1990, De Mello (1999) found that FDI inflows increase growth by means of technological progress and knowledge spillovers only under certain condition, and concludes that FDI is growth-enhancing only for countries in which local and foreign investments are complement each other. Zhang (2001) investigated the causality between FDI stock and economic growth using data from 11 developing countries in East Asia and Latin America. Employing cointegration and Granger causality tests, Zhang found that economic growth is enhanced by FDI but the effect of FDI on economic growth also depends on host country conditions such as trade regime, human capital, and macroeconomic stability. Sukar *et al.* (2007) employed panel data to investigate the effect of FDI on economic growth in the Sub-Sahara African countries. They note that although the correlation between FDI and economic growth is positive, the effect of FDI has only a marginal effect on economic growth, and host economic characteristics such as macroeconomic, local investment, and openness also play a positive role in influencing economic growth.

3.4.2 FDI and Backward Linkages with Local Supplier

Clearly, foreign companies do not work alone and may prefer joint-venture or collaboration with domestic firms in order to reduce their risk and gain other advantages in the host country, since there are also local private and public companies, and there is a causal mutual relationship between foreign and local investors. Local firms competing with the foreign companies can experience both positive and negative effects (UNCTAD, 2001). On the positive side, the arrival of foreign competition from MNCs can force local firms to become more efficient, and may provide spillovers in skills, management

techniques or technical knowledge (Managi and Bwalya, 2010). In addition, the entry of MNCs disturbs the existing equilibrium in the market, and forces local firms to take action to protect their market shares and profits. Both these effects are likely to cause various types of spillover that may lead to productivity increases in local firms (Blomström and Kokko, 1998).

According to Carnoy (1985), it is often believed that foreign firms are in a better position than local firms to choose those industries that are more in line with the comparative advantages of the host country. Moreover, the presence of foreign firms will promote a more efficient use of resources in the host country and increase the output and export of manufactured goods in the host country.

Through competition with local firms, MNCs may force them to search for more efficient technology, or at least to copy some of the technology used by MNCs operating in the local market. For example, Langdon (1981) reported that the entry of MNCs into Kenyan industry forced local firms that used to sell handmade soap to introduce mechanised techniques in order to stay in business. On the negative side, of course, this entry can force local firms out of business. However, these effects depend on government support for domestic entrepreneurs, the supply of venture capital and the strength of indigenous business culture. MNCs may not use local sources for legitimate reasons because the locally supplied inputs are less competitive than those available from abroad or they may be of poorer quality or higher price.

The literature on these issues contains multiple views concerning the relationship between FDI and local investment since empirical studies carried out in different countries have yielded different results in this regard. At times FDI was found to act as a substitute for local investment whereas at times FDI and local investment were present simultaneously. A study by Bayoumi and Lipworth (1997) analysed this relationship in Japan and their results showed that both these sources of capital were present together in the Japanese economy. Moreover, poor performing sectors improved on the arrival of FDI. However, contradictory findings were reported by De Mello (1997) study was based

on data collected for 1970-1992 from a sample of OECD states. De Mello concluded that while FDI gave a boost to the local economy, it could also serve as a substitute for local investment.

As mentioned previously, FDI brings in business knowledge to the host country. Technological advancement can be difficult given the fact that much of the technology has proprietary rights and is patented. FDI facilitates technology transfer by upholding the copyright laws and other laws pertaining to protection of intellectual property to assist with the adoption of the latest technology (UNCTAD, 2001). This helps to improve production processes in host country firms. MNCs have advanced production management procedures in place which enable them to reduce resource wastage and manufacturing costs. It also deals with issues such as poorly utilized production capacity and ineffective resource deployment. Eventually, the improvement in production processes helps to create an edge over competitors.

Investment from foreign countries also impacts on the economy of the host country by improving the productivity and skill set of the recipient country's workforce. It is a generally accepted concept that the more skilled the workforce the higher the growth rate of an economy. A study by Blomstrom and Kokko (1998) evaluated the impact of foreign investment on economic factors using data collected from a sample of Venezuelan firms for the period 1976-1989. The results supported the notion that FDI translated into better productivity measures. However, these results were applicable only to those firms where the productivity was previously low and foreign investment was high. Aitken and Harrison (1999) findings suggested exactly the opposite in their study of Venezuelan manufacturing firms. The study was based on a data sample extracted from Venezuelan Industrial Surveys dated 1976-1989. Their results showed that greater foreign ownership in these firms led to lower industrial output and this inverse relationship was found to be highly significant.

Bwalya (2005) analysed the effects of investment on Zambian manufacturing firms using three years of data (1993-1995) taken from the World Bank Regional Programme on

Enterprise Development Survey. The results showed that within different industries, foreign investment led to higher output whereas within the same industry the relationship was the opposite. Moreover, sectors with lesser productivity experience improved more compared to those sectors with high productivity benefits from received FDI. Jordaan (2008) studied the impact of the effects of FDI on the Mexican manufacturing industry. The results verified the indirect positive impact of FDI. Additionally, the impact was found to be focused on a particular region and exhibited variations as well. Given the empirical evidence of the benefits of FDI, authorities in developing countries are attempting to improve on their policy structure to make it more attractive to foreign investors.

Applied economics studies focusing on the linkages between FDI and local suppliers or its static and dynamic impacts on local firms commonly distinguishe between direct and indirect effects (Dunning, 1993; Potter, *et al.* 2002). The level of use of suppliers by an FDI firm can be considered to be a static impact of FDI, producing an effect on the host country economy (Jordaan, 2011). Several studies which examined the static impact of FDI in developing countries were reviewed by Dunning (1993), who concluded that the degree of use of local suppliers can differ substantially between countries.

Later studies employed the FDI characteristics to explain how this static impact may influence the direct effects. In this context Belderbos *et al.* (2001) used a sample of Japanese FDI firms in a large number of host economies to conduct multivariate analysis to explain the level of use of suppliers. Their results indicated that firms that produce for international markets use less domestic suppliers compared to those producing for host economy markets (Giroud and Mirza, 2006). Kiyota *et al.* (2008) argue that the age of the FDI firm is another important factor that may explain the linkages of FDI with domestic supplier, as it takes time to identify suitable suppliers. Furthermore, Muhkerji and Mukheri (2009) argued that it takes time for foreign companies to become embedded into their host economy, depending on the degree to which personal relationships are important to creating sustainable linkages with domestic suppliers, while Giroud and

Scott-Kennel (2009) argued that the role of the foreign firm in the multinational enterprise to which it belongs can be also another important factor, as affiliate firms do not always have control over sourcing decisions. Other factors, such as the size of the foreign firm, its mode of establishment, and the type and nature of its production processes can be also important (UNCTAD, 2008).

Recently, further emphasis has been placed on the indirect impact (dynamic) from FDI backward linkages. This impact relates to the idea that backward linkages are a good conduit for knowledge and technology flows between FDI companies and their suppliers (UNCTAD, 2001). Input and output linkages can act as another channel which usually involves frequent contacts between buying and supplying parties, resulting in exchanges of information, knowledge, and skills (Giroud and Scott-Kennel, 2009). Additionally, FDI multinationals in developing countries in particular usually have an interest in improving their local suppliers, which may result in a variety of types of support provided by foreign-owned firms. Lall (1980) presented a case study with detailed information on the variety of types of support provided by a foreign-owned truck manufacturer in India, which comprised assistance with the creation of new suppliers, technological upgrading of suppliers' production processes, and assistance with sourcing. In his survey of manufacturing firms in Mexico, Jordaan (2011) also found that FDI firms provide a variety of support, including assistance with production processes and quality.

The above discussion concerning the effect of the entry of FDI on domestic firms leads to a more specific point, which is related to the capability of the host countries domestic companies whether they are private or public. A foreign company can create a local network with the domestic firms who can work together with this as partners (joint ventures), suppliers, distributors, or advertisers. However, that can only happen if the local company has the capacity to provide the production input required by the foreign company. Furthermore, the FDI characteristics of the company including; size, age, mode of establishment of the foreign firm as well as the type and nature of its production processes appear to be critical factors to create backward linkage with domestic firms.

3.5 Limitations of Previous Studies

From the above empirical literature review, the gap in previous studies, which the current research is aimed to bridge, is identified as follows: Most of the studies on the determinants of FDI are conducted in developed countries, while there are limited studies conducted in developing countries particularly in the North African region and specifically in Libya. Furthermore, most FDI studies were across sectional evidence, (Rogman and Ebbers, 2013; Anyanwu, 2012; Ho and Rashid, 2011; Vijayakumar *et al.* 2010; Moosa, 2007) compared different countries, and several studies showed that the determinants of FDI might be country specific (Arratibel, et al 2011; Oladipo, 2010; Chen, 1996) and the relationship between FDI and location factors could be positive (Oladipo, 2010; Johnson, 2006), negative, or insignificant (Vijayakumar *et al.* 2010; Del Sol and Kogan, 2007; Moosa and Cardak, 2006), depending on specific factors in the host country such as the economy, the market, investment policy, labour force, or infrastructure conditions. This emphasises the necessity for country-specific studies such as this one relating to Libya, since it is a wealthy country of natural resources and in a transition stage, might produce fresh insights on this issue.

Moreover, the lack of agreement among the results of existing empirical studies on the determinants of FDI emphasises the need to gain a better understanding of how host countries may attract and benefit from this form of investment, and also to understand how FDI affects economic development by means of the linkages between foreign companies and domestic firms. Since the previous studies in developing countries were descriptive, this study aims to provide information about the determinants of FDI, without further analysis, to find out the factors that influence (facilitate or hinder) each type of FDI in these countries. While studies such as Li and Liu (2005) and Ramirez (2006) have investigated the impact of FDI on a local economy, they have relied on the direct impacts of FDI.

In terms of the data used in the previous studies most of the studies of FDI determinants (Moosa, 2007; Vijayakumar *et al.* 2010; Ho and Rashid, 2011; Anyanwu, 2012 and

Rogman and Ebbers, 2013) have used published secondary data, while there is a lack of studies that have gained their data through a triangulation of methods of data collection such as questionnaires and interviews, which may lead to a more in depth understanding of FDI issues. Therefore, this study adopted mixed methods of data collection to see how this affected the outcome.

In the case of Libya there is very little research conducted on the location determinants of FDI as a host country. There appears to be a lack of comprehensive empirical studies, especially concerning FDI in the non-oil sectors. Also, this study is considered to be the first study to identify the significance of various FDI characteristics such as foreign company nationality, industrial sector and ownership. There is also a lack of research on the area concerning the linkages between FDI and domestic suppliers, which was the major goal sought by the Libyan government. This research therefore represents the first study to investigate the linkages between foreign companies investing in Libya and domestic suppliers, and to assess the ability of domestic suppliers to supply these foreign companies with good quality and competitively priced inputs.

3.6 Conclusions

This chapter has reviewed and discussed the empirical literature relating to the locational determinants of FDI and its impact. It has highlighted the factors that explain the pattern of FDI flows and found that these appear to be related to aspects such as the economy, market, policy, utilities and facilities, and financial and legal spheres, meaning that many different factors potentially impinge on the decision to invest and locate internationally. Moreover, the lack of agreement among the results of existing empirical studies on the determinants of FDI emphasises the need to gain a better understanding of how host countries may attract and benefit from this form of investment, and also to understand how FDI affects economic development by means of the linkages between foreign companies and domestic firms. Although most FDI studies are across sectional compare different countries there is considerable evidence to suggest that the determinants and role of FDI appear to be country specific, and could be positive, negative or insignificant,

depending on specific factors in the host country such as the economy, the market, investment policy, labour force, or infrastructure conditions. This emphasises the necessity for country-specific studies such as this one relating to Libya since it is a wealthy country of natural resources which might produce fresh insights on this issue.

This chapter concluded that FDI is particularly important in helping developing countries to achieve a rate of rapid economic growth and the economic transformation of their industrial sector. In addition, very few FDI studies have focused on the MENA countries (including Libya) and those studies which have been conducted have failed to reach agreement on many of the issues investigated. Moreover, the backward linkages of MNCs with domestic firms are a central issue in the literature on interdependence and are key components in the process of linking MNCs with the GNP (Dunning, 1993; Sun and Du, 2011; Williams *et al.,* 2008). For these reasons, this study will investigate and analyse the determinants of FDI in Libya, focusing in particular on evaluating FDI effects on the local economy which in some respects can be considered to be even more important than attracting FDI. To the best of our knowledge, this is the first study that attempts to investigate these local linkages between foreign companies and domestic suppliers within the Libyan context.

Chapter 4

The Libyan Economy and Legal framework for FDI

4.1 Introduction

The main purpose of this chapter is to place this study in context by providing background information about the main indicators used to describe the development of the Libyan economy since it gained independence in 1951, and to discuss the nature of the country's economic policy system to place this study in context. The chapter focuses on three main issues. It begins by considering the Libyan economy, using the main indicators to describe its development and performance during the period pre-1990 when this was centrally planned. An outline is provided of the economic, financial, administrative and legislative conditions which affected the flow of FDI into the country as well as a description of the Libyan economy during more recent times. The chapter then proceeds to trace the evolution of recent changes in economic policy and to examine investment guarantees, focusing on the legal framework for these which were provided to foreign investors under Libyan investment law. Finally, global trends of FDI from 1990-2012 are considered, with particular emphasis on developments, trends, and sources of foreign investment together with the role played by FDI in the Libyan economy. A summary of the key points in the chapter is presented in the conclusion.

4.2 The Profile of the Libya

Before discussing Libya's most important economic indicators and reforms, it is useful to provide a brief overview of Libya's geographical location and its economic development and indicators. Libya covers a vast area, extending from the center of the Southern Mediterranean coast in North Africa (with a coastline of some 1990 km) to the Northern highlands of central Africa. According to Terterov and Wallace (2002) it occupies some 1,775,000 square kilometers (or seven times the size of the United Kingdom), making it the fourth largest state on the African continent. Libya also occupies a strategically

important geographical location, lying at the center of the North African region. From an historical point of view, Libya's distinctive location has made it a bridge, linking Arab and African cultures. Its territory extends nearly 2000 km into the African continent and for centuries, Libya has been linked to the Sudan in the South East and West Africa by a number of caravan routes which played a major role in transport and trade activities between the Mediterranean region and Sub-Saharan Africa. Moreover, it has played a major role in the economic and political developments that have taken place in this region which has witnessed the flourishing of a number of ancient civilizations. In addition, Libya has acted as an important link between the eastern and western regions of the Arab world which share similar languages, and a cultural, religious and historical legacy (GPC, 2005).

In order to better understand Libyan economic life, it is necessary to know something about the development of Libya's political and economic system, which has continuously changed its philosophical aims and principles, together with other aspects associated with the organization of investment and economic activities. These developments are discussed in more detail in the following sections, beginning with the evolution of political development in the Libyan context in order to describe the government machinery and the decision-making mechanisms responsible for those decisions that influence people's lives in general, and the economy in particular.

4.2.1 Overview of the Libyan Political Context

When the United Nations set the date for Libyan independence it became evident that Libya's long-held dream would finally become reality. It was decided that the Constituent Assembly would draft the constitution to be enforced in the country and that the independence date would not go beyond the first week of 1952 (Cavendish, 2001). Under the terms of the Constitution, the new federal State comprising of three regions: Fezzan, Tripolitania and Cyrenaica, will be known as the United Kingdom of Libya. Following a significant amendment to the Constitution in 1963 with the approval of King Idriss, the

federal system was replaced and the three regions were unified to become the Kingdom of Libya (Otman and Karlberg, 2007).

Following a military coup on September 1st 1969, the Arab Republic of Libya came into existence and the newly drafted constitutional declaration was enforced, describing the new mode of government and legislature, the 1951 constitution being annulled by default and the country being led by what was known as the Revolution Command Council (RCC) (Vandewalle, 2006).

The country later became the Socialist People's Libyan Arab *Jamahiriya* following a declaration by the General People's Congress (GPC) in 1977 (Hajjar, 1980). Further, political change occurred in 1979 when the country moved into another political framework called socialism and as inspired by the Gaddafi green book (Alexander, 1981). Increasing power was vested in President Gaddafi, as a result of the GPC passing a resolution in 1989 instructing the GPC and Council of Ministers to adhere to his counsel. This also meant that all laws, policies and other issues of importance needed to be approved by the President before implementation. After that, it became the norm for any other important meeting to both seek the opinion, and gain the approval, of the President (Vandewalle, 1998).

Despite the political uncertainty and its effect on investment especially following the military coup in 1969, the political system in Libya was stable for over four decades (Zoubir, 2009). In February 2011 when conflict in Libya started, the National Transitional Council (NTC) controlled the country, endorsing a non-violent political shift which would normalise economic conditions, set out a general improvement agenda and builds a democratic government. In 2012 the NTC held its first elections after the fall of the previous government, aiming to encouraging political and economic change in the country and promote development (Chami, et al. 2012, pp. 1-28).

In terms of international relations for Libya it has always remained problematic and it suffered a great deal especially during the 1980s and 1990s. This was particularly true

with respect to the deteriorating relations between Libya and the United States following the political crisis in 1979. The situation was worsened affected by poor relations with other western countries and United Nation sanctions imposed from 1992, until 1999 following the Lockerbie bombing in 1988 (Aljbiri, 2013). Relations between Libya and the western countries improved once the United States and Libya began restoring their political and diplomatic relations in 2003 (Zoubir, 2009). The following year the United States inaugurated its American Interest Section in the Libyan capital which was converted into a communications office within four months.

It was a chain of events that propelled Libya closer to the west and international companies. Major renowned American oil groups such as Amerada Hess, Chevron and Occidental re-established their businesses on Libyan soil, prompted by the fact that the binding economic sanctions previously imposed on the country were removed by the United States in 2004. Its embassy started working again in the capital in 2006 (Blanchard, 2010). Libya was also removed from the list of terrorist countries by the United States. These factors positively affected their international credibility, reputation and importance and the United Nations soon inducted Libya, giving it a seat in the Security Council. This further improved Libya's international relations, in particular decreasing the tension with the West which resulted in countries with mutual interests proposing cooperation and businesses. All these political and international relations developments with respect to Libya propelled foreign investors to invest more in the country which they viewed as an attractive opportunity (Zoubir, 2009).

4.2.2 Libyan Economy Overview pre 1990s

As an underdeveloped country devastated by the Second World War, Libya's economy received a massive boost when oil was discovered there during the 1950s (Gurney, 1996). Although initially it had basic infrastructural facilities, the Libyan economy soon became wholly dependent on the oil exports that started in the early 1960s and the economy underwent a phenomenal transformation. The Government adopted more lenient policies and started to shift their focus towards economic development. In 1963, the first Five-

Year Developmental Plan was initiated. Foreign companies in the Libyan economy also increased. The government investment in the economy was increased along with the domestic investors and the job market in Libya in the 1960s was such that around 75% of the total labor force was employed in the private sector (Gurney, 1996).

Political changes in 1969 led to the enforcement of a system which was heavily influenced by the Arab Socialist Union and a Socialist outlook was adopted that promoted the idea of the ownership of different productive sectors by the Government or State. This continued until Libya climbed up to the next rung of the economic ladder in the late 1980s. These were a major shift in Libyan economic policies as the country started to change its economic strategies in line with socialist ideology from the early 1970s. In line with its Socialist ideology, the Libyan government embarked on a programme of State-sponsored and State-controlled economic development (Otman and Karlberg, 2007).The government also took control of most of the foreign investment especially in the non- oil sector and only allowed investment in the oil and gas sector. Moreover, the private sector was almost completely restricted, creating a closed economy (Alexander, 1981). In 1977, more changes were made in accordance with the ideology of Colonel Gaddafi's economic system, and these were later implemented throughout the country. This new approach trumpeted the idea of labourers working in partnership with business owners, instead of them simply receiving wages and salaries (Terterov and Wallace, 2002:19).

A series of laws were passed in the 1970s which resulted in the step-by-step change of ownership. The nationalisation of foreign shares in local banks was followed by another piece of legislation which resulted in government control of the insurance companies. Later foreign trade, imports and exports were also nationalized following government legislation passed in 1976 (Ministry of Economics and Planning Report, 1995:11).

As a result of the nationalization program over 86% of economic activities were managed by the public sector by the early 1980s (Vandewalle, 1998). Also, the adoption of three- and five-year plans by the government from the early 1970s until 1986 laid down the

rules and responsibilities for investing in the economy, detailing how investors were expected to keep the permanent investment in those industries and their distribution (Shernanna 2007).

The poor infrastructure and the disparity between the wages of the workers gave rise to poverty. The natural resources discovered in the country at the end of 1950s led to the change in the economic systems of Libya, giving way to more public control over businesses. The Libyan government started to take control by negotiating and dealing with foreign investors which resulted in increased holdings in the country's share in the oil-based sectors. This augmented national revenues and the collective effect of the increased interest rates and oil prices in the market further boosted the Libyan economy. Libya has increased foreign currency which prompts more projects and developmental plans for the public that would help boost its economy further (Gailani, 2007:6; Human Development Report, 2010:53).

The global economic recession in the early1980s, dropping prices and demand for oil coupled with the fact that non-OPEC countries started to increase their oil supply propelled a downturn in the 1980s and the prosperity previously seen in Libya could no longer be sustained. As a consequence, in 1982, Libya's daily production of two million barrels was reduced to only 60% of the original (Vandewalle, 1998). As Libya's economic structure was still being developed and thus vulnerable, it started to collapse especially since investment projects started failing, and inflation also increased due to the sudden increase in money supply whilst domestic demand resulted in increased public spending. This decline was also prompted by the fact that the Central Bank only had limited control over monetary policy and its implementation and the vicious cycle continued. Thus, the government proceeded with the introduction of deflationary policies in Libya. The effect of this was a very close monitoring of exchange rates. There was, now, a strict restriction, and checks and balances on the quantities of imports. In 1981, to ensure the monitoring of the balance of trade and imports licensing of the import goods was conducted (Vandewalle, 2011). Government passed a law to ban luxury items that

had seen previously imported to save the foreign exchange. New policies were drafted that strictly limited foreign tours and travel allocations, increased custom duties and even proposed the annual import budgets so that the goals set by the government to reduce imports could be achieved. New legislation was enforced for the people's market in 1982 which limited the trade which were under the public sector only (Shukri, 2003:2).

All these economic measures adopted as a corrective step, backfired to a certain degree as the black market began to thrive during the 1980s and 1990s. This was because the restrictions and limitations imposed by the government on imports resulted in shortages and the domestic producers were not up to the mark. The black market that was only LYD123.5 million in 1982 rose to LYD1, 132 million in 2000. This meant a rise of more than 8% in the non-oil GNP in eight years (Gailani, 2007).

However, the public sector did help Libya to achieve great success especially in developing the infrastructure. These projects included communication, telecommunication and transportation infrastructures such as roads, airports and even power stations. The public sector also helped to increase the public sector workers salaries and moblised the use of local resources, work force and gave some basic economic stability to Libya (Zoubir, 2009).

On the other hand, public revenues were spent unwisely when the power over the economic activities and business was more controlled by the government official and public sector in the absent of any monitoring body. There were a number of negatives that were associated with the public sector. They were unable to generate new revenues except for the oil industry to induct the work force and their quantitative and qualitative productivity was below par. Productivity ranged between zero and 36% of the expected productivity. Similarly, there was huge dependency on the import of machine tools and spare parts which led to reducing foreign exchange. The failure on the part of the public sector to improve productivity, come up with new products and services, and most importantly, enforce budgetary control may also be considered as their downfall. This could be explained by an example. In the case of oil production, the mainstay of the

Libyan economy was OPEC which determines the prices based on global supply and demand. Three-quarters of the labor market in the 1970s were employed by the public sector. All this together with the reduced productivity and concurrent lack of motivation pushed the economy towards an extra financial burden. In short, the public sector failed to achieve the economic goals and transfer the economy to an advanced stage (Manisia. 2002).

In short during the 1970s and early of 1980s, Libya economic policy was based on a centrally planned model adopted in the early 1970s. To achieve the objectives of this policy, a number of five-year plans were implemented which directed production, distribution and consumption in line with its Socialist philosophy. There was little role for the private sector to play in economic activity. Under the command economy, five-year plans were developed by the Council of Ministers which proposed development of particular branches of the country's economy (Wallace and Wilkinson, 2004). During the command economy, the government pursued a policy aimed at creating the foundation for an industrial sector using the financial and technical support of the government. External economic collaboration intensified, starting from 1970 when Libya signed Friendship, Mutual Assistance and Economic and Cultural Collaboration agreements with the number of regional countries, especially the industrialized nations, and including Italy. These agreements were aimed at fostering the development of Libyan's industrial and transportation sectors, intensifying geological exploration, establishing several mining enterprises and developing the oil sector, but most of the country's economic sectors faced difficulties in achieving these goals (Kridan and Goulding, 2006).

4.3 Libyan Economic Reforms Since 1990

To address economic difficulties associated with Libyan economic during the 1970s and 1980s, the government embarked on a reform agenda in 1990 in order to try to stabilize the economy and create a private sector-led open economy. The reform programme included: the liberalization of state controlled prices and tariffs, the privatization of state-owned properties, the liberalization of the trade and investment regime, a reformed

banking system, the adoption of a reasonable exchange rate, and the creation of a favorable legal environment for private sector development. Details of these reforms are discussed in the next section.

Table 4-1: Key Economic Indicators, 1970-2010

Year	Real GDP US$(m)	GDP Growth rate (%)	Exports US$(m)	Imports US$(m)	Inflation rate (%)	Unemployment rate (%)	Per capita income	Real exchange rate
1970	3979	-5.28	NA	NA	4.4	NA	1 605	0.35
1975	13649	4.03	NA	NA	10.4	NA	4775	0.29
1980	38186	-0.28	22084	12671	9.7	NA	1205	0.29
1985	29887	8.33	10416	7529	9.14	NA	7728	0.29
1990	31088	3.72	11486	8960	8.4	0.4	7366	0.26
1995	28292	-2.22	7513	5755	7.24	1.4	6013	0.42
2000	38471	3.7	12210	5024	-2.9	7.9	7477	0.54
2005	45451	10.29	29383	13523	2.6	20.7	8073	1.35
2010	80942	4.20	49345	30686	2.4	21.8	13319	1.25
2011	40587	-60.27	19100	15586	15.9	NA	6610	1.22
2012	95802	104.4	61178	32586	6.1	19.3	15472	1.26
2013	96878	11.00	NA	NA	2.6	NA	NA	1.27

Source: UNCTAD 2013, Annual Report of the Central Bank of Libya 2013.
Key: NA = No data available.

Despite the wider economic reform during the 1990s, the results were counterproductive and most of the economic indicators declined as a result of UN sanctions and oil prices decreased. From the beginning of the last decade, the Libyan economy witnessed significant improvements and most of the economic activities got back on track. GDP grew from 3.7% in 2000 to 10.2% by 2005, reaching 11% by 2013, mainly due to a recovery in the economic sectors including oil and service sectors as result of the initial economic reforms and supported by removal of UN sanctions as explained previously in subsection 4.2.1. In addition, inflation dropped from 8.4% in 1990 to about 2.4% in 2010. Also, per capita income rose from USD 7366 in 1990 to USD 13319, 15472 in the years 2010, and 2013 respectively (see Table 4.1). Economic growth slowed down between 1992 and 1999 due to external and internal circumstances, including UN sanctions. However, since 2002, the Libyan economy has been growing steadily, with GDP growth rate reaching 10% in the mid-2000s. This notable growth was largely brought about by the performance of oil and services, which grew by about 10% and 5% per annum

respectively (Central Bank of Libya Annual Report, 2010). However, the restructuring of the Libyan economy, and the negative outcome of privatization, particularly in education and the civil service, led to the loss of more than 100,000 jobs (National Council for Planning, 2008). The average annual inflation rate was 8% in 1990, which declined to -2.9% in 2000 and, then rose again in subsequent years to some 2.4% in 2010. This was largely due to a rise in the price of food products, as Libya is heavily dependent on food imports (Central Bank of Libya Annual Report, 2013).

However, the Libyan economy is small in terms of domestic market size: in 2010 the real GDP was US$ 80,942 billion (see Table 4.1). The Libyan market is expanding faster than the global economy between the years 2008-2010 of last decade the average growth rate in Libya was 6.2% compared to 4.3% for global growth in the last decade. In addition, the demand for goods and services as measured by per capita income increased from US$ 7,477 in 2000, to US$ 13,319 in 2010, reaching US$ 15, 472 in 2012 (UNCTAD 2013; Central Bank of Libya, 2010). This rapid growth can be explained by a number of factors, particularly the increase in oil prices which meant oil sector revenue grew from US$ 47.1 billion to US$ 59. 3 billion with a growth rate of 25.9% in 2010.

Most of Libya's international trade is conducted with European countries. In 2005, more than 60% of Libyan imports and exports came from and went to European countries accounting for LYD eight billion both ways. While Libya exported fuel in the shape of gas and oil, its major imports from the European market including transport, machinery, food and other commodities (Central Bank of Libya, 2010:43).

Furthermore, there was important growth in the non-oil sector from LYD 39.2 billion in 2009 to LYD 41.3 billion in 2010 with an annual growth rate of 5.4%. Also, in this context it is worth mentioning that the Libyan economy was not very affected by the international recession from 2008. Normally, inflation is driven by increases of public spending and the subsequent rise in wages, and the increasing cost of food. However, the inflation rate in Libya remained stable at 2.4% in the second half of the first decade of the new millennium. (Central Bank of Libya, Economic Bulletin, 2014).

Libya is classified by the different international and regional organisations as one of the oil-producing countries and oil revenues are still the main source of foreign currency, constituting 95.0% of its foreign currency (Central Bank of Libya, 2010). Moreover, the oil sector contributed 59.3% of GDP in 2010 while non-oil sectors contributing 40.7% (Central Bank of Libya, Economic Bulletin, 2012). This strong link between the Libyan economy and the oil sector is highlighted by the Human Development Report, which argues that a 10.0% change in oil prices affects national income by 3.0% (Human Development Report, 1999: 22).

Despite being the largest contributor to the country's GDP, the oil industry only employs about 3% of the total workforce in this regard Porter and Yergin (2006: 5) stated that "*the Libyan non-oil sectors contributed only 40% of the Libyan Gross Domestic Product (GDP) whilst employing about 97% of the formal staff*". Manufacturing, due to its capital intensity, employs just 4.4%, and the services sector, employs 65.7% of workforce in year 2010. Whilst contributions by the trade sector to employment rose from 5.7% in 2007 to 15.7% in 2010, construction sector employment has remained at 2.5% for the last three years of the last decade (General Authority for Information, 2012). The oil and gas industry is the mainstay of Libyan revenues and the largest contributors to the country's GDP as showed in table 4.2. The exports from this industry accounted for some 97% of total Libyan exports in 2010, an amount which is half of its foreign exchange earnings while machinery and transport equipment made up 49.6% of its total imports in 2010 (Central Bank of Libya, 2010). The oil and gas sector's continue led the Libyan economy by contributed an average of two third of Libyan GDP as shows in table 4.2.

Table 4-2: Sector contribution to GDP 2004-2012 (% share)

Sector/Years	2004	2005	2006	2007	2008	2009	2010	2011*	2012
Oil and Gas	60.6	66.1	68.2	67.2	69.6	54.6	59.3	44.8	65.5
Agriculture, Hunting and Forestry, Fishing	2.8	2.2	2.1	2.1	1.9	2.8	2.5	1.7	0.8
Mining and Quarrying	0.2	0.1	0.1	0.1	0.1	0.2	0.2	0.1	0.1
Manufacturing	5.1	4.7	4.6	4.3	4.2	6.3	5.7	2.0	3.2
Construction	4.5	4.0	4.0	4.5	5.1	8.8	7.9	2.8	1.3
Services**	26.8	22.9	21.0	21.8	19.1	27.3	24.4	49.5	29.1
TOTAL	100	100	100	100	100	100	100	100	100
Oil and Gas activities	60.6	66.1	68.2	67.2	69.6	54.6	59.3	44.8	65.5
Other Economic Activities	26.8	22.9	21.0	21.8	19.1	27.3	24.4	49.5	29.1

Source: Annual Report of the Central Bank of Libya (2013).
* Primary Data.
** Services include Education, Health, Wholesale and Retail Trade, Rental Real Estate Activities and others.

This rapid growth was largely due to the increase in international oil prices, which led to an increase in oil sector revenues. However, since 2004 the contribution of agriculture to GDP has declined from 2.8% to 0.8% in 2012. This appears to be largely due to the growth in the services sector which led to the creation of alternative employment opportunities as well as the fact that Libya's agricultural sector suffers from a lack of modern technology and is still highly dependent on rainfall which is inadequate (Ministry of Agriculture, 2010). The services sector was considered the second largest contributor to GDP with 17.7 % in 2010, and the largest source of employment in 2010 as mentioned previously. The contribution to GDP of the manufacturing sector decreased from 6.9% in 1990 to 5.2% in 2010 and further reduced to 3.0% in 2012 as shown in Table 4.2. This backwards step is due to the lack of development and mismanagement as consequences, of the failure of the public sector (Central Bank of Libya, Annual Report 2013).

Ensuring the constant supply and availability of human resources and their development is a focal point for any business activity and supply needs to be high in both quantitative

and qualitative terms in order to ensure the success and sustainability of any project. Similarly, growth in the national population makes it easier for business to expand, to recruit more manpower and execute better projects with better continuity in production.

Like other oil producing countries Libya still has a relatively low population, however, in comparative terms, its growth population rate is very high. Libya's population was around one million in 1954 and has raised six fold to some six million by 2010 (World Population Report, 2014). Needless to say, most of the population is comprised of young Libyans with the majority being teenagers or younger, some 68.8% of its total population being aged between 15 and 64 years in 2010 indicated that about two third of the Libyan population are still in working age (National Authority for Information, Statistic Book, 2012).

Natural factors and migration are considered to be the two main demographic reasons for the increase in the Libyan population. With regard to migration, many refugees left during the Italian occupation of the country and they mostly returned after conditions stabilized, particularly following the boom in the Libyan oil sector in 1963. There was a noticeable growth in the Libyan population during the two decades from 1964 to 1984 (Vandewalle, 1998). The Libyan growth rate for population was 1.8% and 4.5% for the periods 1973-84 and 1995-2006 respectively and 2.07% in 2013. It is perhaps not surprising that Libya was ranked 64th in the list of 186 countries in terms of rate of human development in 2012 by UNDP (2011).

Table 4-3: Human Development Indicators in Libya compared with other Regions (2012)

Human Development Indicators	Libya	Latin America & Caribbean Countries	South Asia	Sub-Saharan Africa	World
Combined gross	93	84.5	66	53.8	72.4
GNP per capita in US$ 2012	24,26	10,098	2,778	2,052	13,72
Life expectancy (in 2012)	75.3	74.2	65.6	54	70.8

Source: UNDP (2013: Human Development Index).

Table 4.3 shows the most significant human development indicators. In terms of levels of indicators of human development Libya was above the average for the world, Latin American and Caribbean Countries, South Asia, and Sub-Saharan Africa in three criteria as shown in Table 4.3. Also, the Libyan Standard Indicator for human development achieved 0.769 out of one according to the UNDP Standard Indicator (Human Development Report, 2013:17). African Economic Outlook (AEO) in 2013 stated that, "in 2009 Libya was the second highest level of human resource development within the African region" (AEO, 2012, p. 11).

4.3.1 Privatization Policy Reform

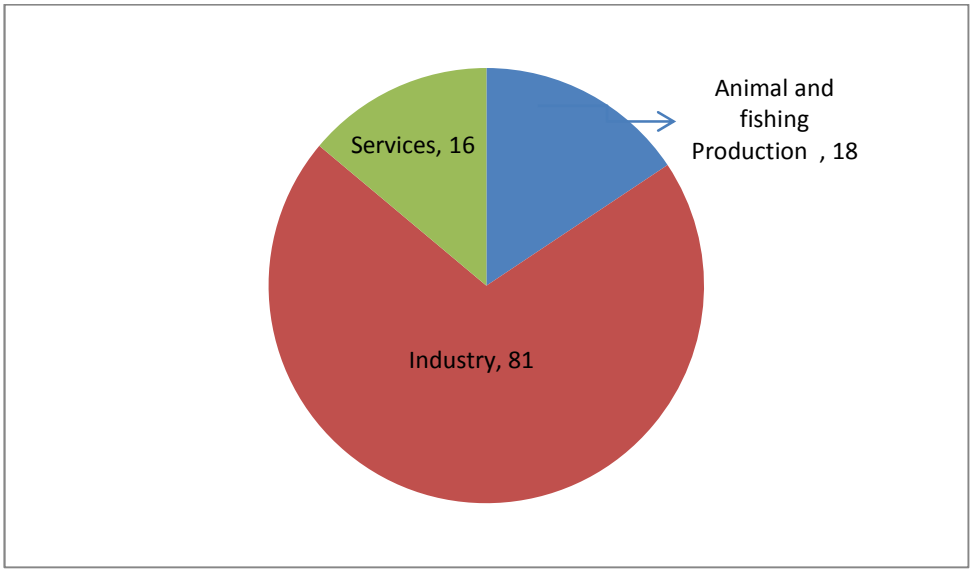
From 1985 onwards, the Libyan government decided to re-open the doors to the local private sector, in an attempt to diversify the sources of income and enhance the competition in the local economy. Law No. 9 of 1985 reopened the door for private sector companies or individuals wishing to be involved in industrial or agricultural economic activities. Later on, the process of privatization of the public sector started, with projects being transferred to the ownership of workforce cooperatives. As a result 4,845 public productive units, mainly from the agricultural sector, accounting for a total of LYD 167.8m were transferred between 1989 and 2001. The form of cooperative privatization was not successful and the process failed to achieve the anticipated goals. Most of the cooperatives failed to survive due to various reasons including weak productivity caused by the lack of qualified managerial and technical staff together with shortages in raw material. These were sometimes not imported when needed due to the international sanctions imposed on Libya in 1992 which worsened the problems of these units by slowing down foreign trade activities. The import of items and skilled labour was only possible via agents which increased costs. As a result only LYD 43.2m of the total had been repaid by 2001 (Shernanna, 2006:46; Obeida, 2007).

Further step towards privatization occurred in 1992 when the Libyan government allowed the private sector to become involves with organizing banking and monetary and credit activities, permitted private banks in the form of stock companies for the first time.

Finally, the regulation of ownership of the public utilities and organization of wholesale trade paved the way for greater private sector involvement (Shukri, 2003:4).

As a result of the policy reforms, some 115 public organizations were transferred into private sector in the period 2004 to 2010, amounting to more than LYD 2 billion. Of the total firms four out 115 or 3.5% had assets of over LYD 100 million, 8.6% had assets of 25-100 million, 14% had assets of LYD 5-25 million, and 26% had assets of LYD 1-5 million while about 47% of the total projects had assets of million or less.

Figure 4-1: Number of Privatization Projects by Sector



The privatization procedures in this period mainly targeted the industrial sector which accounted for over three-quarters of the total and amounted to some LYD 1.5 billion, with 16 projects from the services sector and 18 projects from the agricultural sector as shown in the pie chart above (Privatization and Investment Board Report, 2012).

In a parallel development, an important move was made by the government and commercial banks to provide loans and paper credits to support this process of

transformation to cooperative production in order to help resolve the problem of unemployment by creating new jobs (Obeida, 2007).

4.3.2 Investment Policy

Global business is an interwoven space, where all countries and commercial activities are dependent on each other. Those businesses and countries that are more open to the ever changing dynamics and able to adapt quickly to the growing concerns tend to improve their investment policies (Levy and Nolan, 1991). Thus national policies and regulations are drafted in such a way that they induce foreign investment. Countries need to remain on amicable terms and make their laws as business-friendly as possible. In this context, countries tend to develop laws and regulation that they believe will help boost their economies and improve their chances of further development.

To fully optimize the economic advantages for all the stakeholders involved in the economic activities of a country, it is essential that all the policies make provisions for the instrument and method via which the same can be controlled. The next section addresses the Libyan government's attempts to attract foreign investors and boost economic activities via their investment policies and guarantees.

4.3.2.1 The Libyan Investment Board (PIB)

Foreign investment was originally dealt with by the Ministry of Economics, Commerce and Investment affiliated to the GPC, but in order to improve the poor business conditions in Libya, the Privatization and Investment Board (PIB) was set up in 1998 as first step to help augment foreign investment in different economic sectors of Libya. Positive change in Libya's political relations with the west paved the way for more foreign investment and the introduction of policies designed to improve the non-oil sectors in 2003. Thus, previously low inflows of FDI were replaced with fruitful results (Oxford Business Group, 2008).

To increase its utility beyond its borders and promote the vision of Libya as a trade-friendly country, the government decided to open PIB offices in other countries as well.

In Libya itself, the PIB currently has their main offices in Tripoli, and two branches, one in Benghazi and another in Misratah. Under the provisions of Law No.7 of 2003, the Ministry of Economics usually appoints the chairman and members of the committee which has oversight of the policy of PIB (Otman and Karlberg, 2007).

The duties of the PIB were laid down in Law No.5 of 1997 which outlines the activities and responsibilities of this organisation. It suggests that PIB should pave the way for foreign investment by applying various methods and its role is to PIB formulate plans to attract FDI; keep a check on foreign investment in the country and deal with FDI applications (Otman and Karlberg, 2007). In processing applications, the PIB should consider whether they meet the necessary legal requirements and provide appropriate credentials. It is also expected that they do the research to determine eligibility for the various subsidies and privileges on offer to FDI. It is also expected that they would handle any issues and complaints that may arise in the meantime without the need for legal intervention. The PIB should then forward the applications to the Secretary with their recommendation.

Under the Executive regulation, regular scheduled and unscheduled visits are conducted by the employees of the PIB during the investment projects to rule out any ambiguities or foul play (Otman and Karlberg, 2007). They are provided with special powers to oversee this process and ensure that the rule of law is respected so that any fraudulent activity can be avoided.

It can be said that the main purpose of the PIB is to generate the paperwork and complete any necessary technical and administrative reports. According to the amendments in the articles for law and executive regulation, the authority for the decision-making rested with the Ministry of Economics, Commerce and Investment while the process of the application would be handled by PIB Committee. The General Corporation for the Transfer of Ownership of Companies and Economic Units was assigned the responsibility of being involved in those projects that were approved. Thus, this meant that many

different entities were involved in the process. Analysis showed that there was a need to streamline the process and the idea of a One-Stop Shop was floated.

It was suggested that the PIB should operate via a one-window service meaning that the paperwork and procedures could be speeded up by cutting out unnecessary bureaucracy. A One-Stop Shop solution would remove other central and local government offices from the equation for potential investors, allowing them to directly interact with the One Stop Shop and sort out all their issues at one place only, making the process more user-friendly (Sheibani, 2013).

4.3.2.2 Legislative and Legal Reform

Laws and regulations that were previously enforced were amended in an attempt to give full independence to foreign investors in Libya whilst ensuring that they could not interfere with local investors. This amendment was carried out to ensure that the expertise and the updated technology that might be brought in by the foreign investors would help raise the local market and local products to preferred international standards, making them eligible for international trade and able to earn Libya hefty foreign exchange in return (Sheibani, 2013).

Foreign currency, machinery, factory equipment and spare parts, raw materials and assets including trademarks, logos, brands and patents were all considered under the concept of assets. According to the amendment in the legislation all of these and other types of resources were identified as part of the assets that may be brought into Libya by the foreign investors, both for sole investment and in the case of partnerships with a Libyan national. In another amendment to the legislation in 2006 it was suggested that the invested capital should be a minimum of USD 50 million (or its equivalent in Libyan currency). This, however, was a void condition in case of joint ventures (Government Investment Law No.9 of 2010).

Tourism, real estate, infrastructure, communication, electricity generation, agriculture, industry and services, along with the oil-related industries, were identified in Law No.

108 of 2005 as those sectors in which foreign investment could take place. Investment Law No. 7 of 2003 did not specify any particular type of investment to be covered. However, under the terms of this law, if : the end product is to be used for local consumption or the by-product or intermediate products are to be used in other relevant industries in Libya only or for any other foreign exchange-related activity and those are products or services permitted by the GPC.

The economic activity of those products are protected and allowed under the legislation.

The principle focus was on the fact that the services and products that are being produced by these sectors should help Libya reduce its imports and increase its exports. In both cases, this would ultimately result in growing foreign exchange reserves for the country. In addition, any local or foreign investors had to guarantee they would employ only local labor. If it proved necessary to bring in a foreign expert, then he was obliged to share this specific technical knowledge, instructing locals in Libya. It was further emphasized in Law No.7 of 2003 that all the aforementioned economic activities should help foster growth in those areas of Libya that are deemed backward economically (Otman and Karlberg, 2007).

The law also provided for the rights of the foreign investor which include the right to purchase, lease or rent land in Libya. The companies also have the right to construct buildings on the acquired piece of land. If the business project terminates, or does not start up within the first six months of registration, if it is sold off after five years or phased out, the investor has every right to take out his investment following the same means used to initially bring that investment into the country.

Different laws and regulations were drafted to provide foreign investors with an attractive environment for their business. Investors were provided with specific rights to induce them to stay and invest in Libya. For instance, the investor can close his project, sell it off to someone, transfer his share of profits to anyone, and import the required equipment to run the project without paying any custom duty and request skilled labors from abroad

provided that technicians with the same skills and knowledge are not already available in Libya. Also, the products that are derived from any business that was funded by foreign investment can be exported, without paying any duties and tax. The investor, however, needs to get the approval for this in writing which can be of particular significance since foreign workers tend to send their salaries back to their home country (Alsnusy *et al.,* 2013).

Specific rules and regulations were also laid down for the investors. For instance, when hiring individuals it was mandatory for the investor to give preference to a local Libyan over a foreign individual if both individuals have the same qualifications, experience and skill levels. Investors must initiate their project within six months of being granted a license. They are required to carry out their book-keeping in accordance with Libyan Commercial Law and provide training for the local workforce to equip them with the necessary skills. The Privatization and Investment Board (PIB) should receive annual reports of the activities conducted within the project which also note any changes made to the original plans (Alfaro *et al.,* 2004). Similarly, the aforementioned organization and the Libyan Tax Department should also receive copies of an accountant-approved annual budget for the project.

Like other countries which rely on foreign investments, Libya also offers attractive subsidies to the investors but only after they meet the necessary criteria. Exemptions of tax/duty include office equipment, transport, furniture, machinery and building materials. In order to fully avail themselves of these subsidies offered by the Libyan government, investors must fulfill some basic prerequisites when conducting their business activity. These include: that the project should be run using a renewable energy source; that it should use a minimum amount of water; that it should be located in one of the developing areas of the country; that it should contribute in some way to the food requirements of the country; and finally that it should have minimal effect on the environment, especially with respect to pollution and carbon emissions (PIB, 2013).

Various duties, taxes and custom clearance required under normal circumstances may be relaxed or dispensed with entirely under the terms of this law. This relaxation, especially in the case of raw materials, is generally applied for a period of five years only but later, if Ministry council approval is given, it may be increased for a further three years. Foreign investors are also free from the production and holiday taxes which may otherwise be applicable to products being exported. Sometimes, depending on the sector and nature of the project, investors may even be exempt from income tax for five years after the initiation of the project and this may be extended for a further three years if official approval is given. However, this decision depends on whether the investor agrees to invest any profits within the country or reinvest in the project. Investors are also exempt from the usual stamp duties that would be applied to relevant documentation. Foreign investors do not need to conform to commercial, trade and industrial laws in Libya (Investment Law No. 9 of 2010).

To boost investment, both in local and foreign categories, in sectors such as real estate, telecommunication, tourism, power generation, tourism, agriculture and industrial sectors, many laws were either drafted or amended to the investor's liking. This enhanced the overall financial and business environment of the country. The laws dealt with issues such as free-trade zones, trade agencies and focused economic activities in Libya (Younes *et al.,* 2013).

Huge numbers of resolutions that usually centered on the improvement in operating and business transactions were also passed by the Ministry council to motivate foreign investment (Vandewalle, 1998). One of these resolutions allowed foreign companies and multinationals to establish their branch in Libya. This resolution was conditional on the fact that the company would be given a license to operate for a maximum period of five years and later, following consideration of its impact and other factors, the license could be renewed further. To establish and improve partnership with the locals and the public in general, it was resolved that a stock market should be established to attract foreign investors especially in the non-oil sectors (Shukri, 2003:5).

In order to enhance the business environment for foreign investors, the investment laws gave guarantees that foreign projects would not be subject to seizure, nationalization, dispossession, freezing of funds or reservation, provided they did not obstruct any court order, for which they would have to stand trial like any other citizen. Specified damages and compensation would be required to be paid by the said project. These pledges helped to increase investor confidence in local policies and the business environment. Also, the foreign investors have the right to challenge any law or procedure that they feel is causing them concern via the proper channels. The prerequisite for this challenge, however, is that it should be done within a month of the application of the procedures or the Investment Law, No.9 of 2010. While providing subsidies, guarantees or pledges, laws are drafted in such a way that they should also justify political and national risks and interests of Libya especially in comparison to other countries (PIB, 2013).

4.3.2.3 Financial Sector Reform

In terms of financial sector reform, when Libya achieved its independence only nine branches of foreign banks existed in the country and there was no indigenous national bank. These branches were then nationalized in 1971 and incorporated into the Central Bank of Libya (CBL) until the end of 2007 (Vandewalle, 2012). Nowadays, the Libyan banking system is run by five public commercial banks, five private commercial banks and four specialized banks; all under the aegis of the CBL. Twelve offices working on behalf of the foreign banks also exist in Libya. Libya's financial sector and banking industry also suffered badly, mostly due to the fact that the banks, both public and private, provided traditional services, such as paying out monthly salaries and wages, along with limited banking activities (Brown, 2011). Thus, there was no significant development in the banking sector and even now, only a few banks have advanced facilities such as ATM cash machines (African Economic Outlook, 2013).

The bank credit as a ratio of GNP decreased from 41% in 1995 to 28% in 2008 while the absolute level increased from LYD 4.37 billion in 1995 to LYD 11.81 billion in 2008.

The bank credit to GNP ratio is a significant indicator, pointing at the low level of commercial banking services in Libya (Central Bank of Libya, 2009:29).

The Libyan government has undertaken the process of privatization motivated mainly by the transition from a centralized system to a market economy, and the CBL is looking forward to reorganizing the banking sector. In the move to restructure its commercial banks, the CBL sold off its assets and shares in the Unity Bank and the Sahara Bank to local and foreign investors. It also allowed mergers and acquisitions for the sake of the sector's growth. Thus, Al-Gumhouria Bank was merged with Al-Umma Bank to produce a new Al-Gumhouria bank, with total assets of LYD eight billion (Aljbiri, 2013). To further improve the banking industry, systems such as an Automated Clearing House, Automated Cheque Processing, ATMs, POS, CMS, and Real-Time Gross Settlement (RTGS) are being adopted in Libya's banking services (Aljbiri, 2013).

Two commercial banks were introduced in Libya, entering into partnership with the states of Qatar and the United Arab Emirates. Similarly, foreign banks bought shares in Alwahda and Sahara Banks. Thus, one buyer, the BNP Paribas Group, is not only a stakeholder with a 19% share but is also allowed to buy 51% of shares within three to five years. The partnership between the Arab Bank and Alwahda Bank follows more or less the same conditions. The Banking Law of 2005 which makes significant changes to previous banking practices. Under its terms, commercial banks in Libya are allowed and foreign banks may enter the Libyan market. The banking sector is also allowed to provide loans and financial assistance to foreign investors on condition that the value of the loan does not exceed 30% of the total cost of the project undertaken (Central Bank of Libya, 2008:24; Mireles *et al.,* 2009).

The government realized the need for a Libyan Stock Market, resolving to establish one in 2006. Since it is still relatively new, there is growing concern about its staying power and the weak Libyan economy; market turnover was a mere LYD 250 million based on just over five thousand transactions. There are 28 companies currently listed on the Libyan Stock Market, but only ten in active trading. Predictably, three of these are

commercial banks while the rest are insurance companies and investment companies (Libyan Stock Market, 2015).

4.3.2.4 Other Policy Reforms

In order to make the Libyan economy attractive for foreign investors, the government has taken a number of measures to restructure the economy. Illegal foreign exchange companies and markets were curtailed by the CBL allowing commercial banks to initiate and carry out the transactions in other currencies as well (US State Department, 2011). This resulted in the foreign investors and companies investing and carrying out transactions through proper channels; ultimately this brought down the foreign currency exchange rates and removed the black market foreign exchange dealings from the equation. The overall impact was the initiation of the restructuring of the local economy. The exchange rate dropped to that of the black market and trading was being transacted at one USD for LYD 1.25 in 2010. Foreign investors were able to process their transactions at the same rates especially when the government also allowed a daily maximum transaction of LYD 10,000. These policies propelled the economy in the right direction and the interest and confidence of investors in the Libyan economy grew further (Gailani, 2007; Aljbiri, 2013).

In order to make the Libyan economy attractive for foreign investors, the Libyan government tackled the restructuring of the economy in Libya. Illegal foreign exchange companies and markets were curtailed by the CBL allowing commercial banks to initiate and carry out the transactions in other currencies as well (US State Department, 2011). This resulted in the foreign investors and companies investing and carrying out transactions through proper channels; ultimately this brought down the foreign currency exchange rates and removed the black market foreign exchange dealings from the equation. The overall impact was the initiation of the restructuring of the local economy. As stated above, the exchange rate dropped to that of the black market and trading was being transacted at one US$ for 1.25 LYD in 2010. These policies propelled the economy in the right direction and the interest and confidence of investors in the Libyan

economy grew further where the General Authority for the Ownership of Public Economic Units was established, as a further tool for the augmentation of the privatization program in Libya (Shernanna, 2006:48).

In order to enhance the economic situation and create a favourable business environment, the Libyan government has signed several trade agreements and policy with a number of international organizations. In June 2004 Libya became an associate member of the WTO and could then take advantage of this status. Libya is also a member of two organizations working under the aegis of the World Bank Group: the Multinational Investment Guarantee Agency and the World Association of Investment Promotion Agencies (Mugabe, 2005). It is also a member of the 5 + 5 Western Mediterranean group which consists of four other countries from the Arab Mediterranean countries (Algeria, Mauritania, Morocco and Tunisia) and five countries from the European Mediterranean (France, Spain, Malta, Italy and Portugal). Other economic organizations and associations of which Libya is a part of include the Arab League, the African Union and Organization of the Islamic Conference, making Libya a country with links and connections with all the most important trade and economic associations of the region (Blanchard, 2010).

Despite Libya not being a member of the Treaty of Rome (1957), the EU encouraged its member countries to engage in economic relations with Libya. However, Libya was not able to maintain a full relationship with the EU such as other countries in the region because of the poor relations with most of the EU as discussed early. Later, in 2007, a memorandum of understanding was signed between the EU and Libya which allowed then to maintain trade with EU countries. This allowed for Libya to export mainly agricultural produce and to import goods from EU States. The EU also recommended an easing of the visa policy, both for EU citizens entering Libya or Libyans entering EU countries to boost the economic situation and create a favorable trading environment (Aljbiri, 2013).

4.4 FDI Inflow Trends in MENA and the Wider Region

Over the past three decades, there has been a phenomenal expansion of FDI inflows worldwide (UNCTAD, Investment Report, 2013).Therefore, this section briefly considers recent trends in global FDI inflows and the MENA region, with particular emphasis on FDI inflows to Libya.

4.4.1 Global FDI Trends

In the past few decades, there has been considerable interest in capital flows, international trade in goods and services and the increase of global output between countries. The scale of these FDI flows has expanded dramatically over the past few decades. Table 4.1 presents various indicators related to FDI inflows, demonstrating that there has been a dramatic increase in these globally. With regard to annual FDI inflows around the world, there has been a notable increase from US$ 207 billion in 1990 to US$ 1,401 trillion in 2000 than doubled to accounted US$ 2.1 trillion in 2007 and finally to US$ 1.3 trillion in 2012. This increase appears to be due to the increasing pace of globalization and the fact that there have been significant reforms relating to global trade (World Bank, 2013).

Figure 4-2 Inward FDI Flows in US$ (million) 1990-2012

Year	World	Developing Countries		Developed Countries		MENA Countries	
		FDI inflows	FDI share	FDI inflows	FDI share	FDI inflows	FDI share
1990	207,697	35,096	16.89%	172,526	83.06%	1,287	.619%
1991	154,009	39,770	25.82%	114,035	74.04%	2,230	1.44%
1992	165,973	53,167	32.03%	111,141	66,96%	3,874	2.33%
1993	223,454	76,835	34.38%	143,451	64.19%	3,903	1.74%
1994	256,112	103,502	40.41%	150,560	58.78%	3,557	1.38%
1995	342,544	115,943	33.84%	222,488	64.95%	2,819	.822%
1996	388,998	147,078	37.80%	236,035	60.67%	4,929	1.267%
1997	486,476	190,724	39.20%	285,404	58.66%	6,138	1.261%
1998	707,185	190,729	26.97%	508,421	71.89%	5,113	.723%
1999	1,087,500	228,097	20.97%	850,969	78.25%	4,330	0.398%
2000	1,401,466	256,465	18.29%	1,137,976	81.19%	5,897	0.42%
2001	825,280	214,696	26.01%	601,070	72.83%	9,373	1.13%
2002	628,114	176,063	28.03%	440,778	70.17%	7,257	1.15%
2003	565,739	183,902	32.50%	361,917	63.97%	16,570	2.92%
2004	732,397	291,919	39.85%	410,067	55.98%	25,362	3.46%
2005	985,796	330,130	33.48%	624,565	63.35%	47,564	4.82%
2006	1,459,133	434,366	29.76%	970,098	66.48%	70,489	4.83%
2007	2,099,973	564,930	26.90%	1,444,075	68.76%	80,476	3.83%
2008	1,770,873	630,013	35.57%	1,018,273	57.50%	96,254	5.43%
2009	1,114,189	478,349	42.93%	565,892	50.78%	76,293	6.84%
2010	1,408,57	637,063	45.20%	696,418	49.04%	65,133	4.97%
2011	1,652,511	735,212	44.59%	820,008	49.07%	46,320	2.67%
2012	1,350,926	702,382	52.00%	560,718	47.50%	52,247	3.21%

Source: UNCTAD, Dataset 2013.

A rapid increase in annual FDI inflows has been observed in both developed and developing countries since early of 1990s. The developed countries accounted for 83.06% of FDI inflows in 1990, whilst this figure was just 16.89% in the same year for developing countries. However, developing countries continued to raise their share in total annual FDI inflows from 18.23% in 2000 to 52% in 2012. At the same time, the share of developed countries dropped from 83.06% in 1990 to 47.50% in 2012. These figures indicate the fact that FDI inflows to developing countries grew considerably faster than those to developed countries during the period from the late-twentieth to the early twenty-first century.

According to UNCTAD (2013), FDI flow to developing countries played a crucial economic role in 2012, being estimated at over US$ 700 billion that year, the second

highest volume ever recorded. Conversely, the flow of FDI to developed countries declined to $561 billion which was only one-third of FDI at its peak, recorded in 2007. Hence it can be argued that the global FDI that flows to developing countries varies between a quarter and a third of the total. Moreover, 11 of the top 20 host economies for FDI in 2012 were either developing or transition economies. While FDI increasingly originates from developing countries (more than 30%), it was noted that among the top 20 outward investors, seven were in countries with developing or transition economies.

Over the past decade, however, international FDI inflows have witnessed a period of dramatic fluctuation. Annual FDI inflow reached its peak in 2007 at a level of US$ 2.1 trillion, then there was a decline in 2009 to US$ 1.114 trillion due to the fact that international investors were affected by the global financial and economic crises in the Eurozone and the US which led to lower rates of GDP growth, trade, capital formation and employment, and also led to broad-based financial policy changes in many countries which negatively affected on FDI inflows (World Bank, 2013). From 2010, the FDI rose slow but steady recovery from US$ 1.3 trillion in 2010 to US$ 1.6 trillion in 2011 (UNCTAD, 2013).

4.4.2 The Development of FDI in Libya

As a result of the nationalization programmes carried out by the Libyan government in the 1970s onwards and their attitude to foreign investment, along with the availability of the financial resources from exporting oil and gas, Libya attracted little interest as a host country for FDI, except for the oil sector. This state of affairs started to change, however, following the government reforms and legislation in 1997 which was intended to promote foreign investment. Later on, the Libyan government amended twice more in 2003 and 2010, attempted to attract both foreign investment and Libyan private capital held abroad by reopening many sectors for foreign and local private investment that had previously been closed (Aljbiri, 2013).

As Table 4.5 shows, FDI inflows began to decline in 1973 as a result of the previously mentioned nationalization programmes that targeted foreign companies. FDI stocks continued to decrease in the 1970s from US$ 5183 million in 1972 to US$ 2499 million in 1979, as assets were pulled out of the country. The only year FDI stocks increased in this period was in 1976 due to the joint venture programme between local companies and three foreign companies: Iveco, Calabrese and Massey Ferguson (Ministry of Industry, 1994). Due to continued public sector control of most economic activities in 1980s, the FDI stocks were negative for the most part, except the years of 1980, 1985, 1988 and 1989 as a result of increased investment for the mentioned joint venture above.

In the early 1990s, the Libyan authorities initiated reforms in several areas of economic activities by issuing various laws intended to liberalize their economy in order to make it more attractive to foreign investors. Despite these new policies, FDI inflows remained either negative or low throughout the 1990s, largely as a result of the international sanctions imposed on Libya in 1992 which had a very detrimental impact on the progress of the Libyan economy. These sanctions included a ban on equipment supply or modern technologies, effectively freezing Libyan assets abroad, and an air embargo which resulted in Libya's economic and political isolation from the international community. As a result the losses and increased costs borne by the Libyan economy in the 1990s were estimated at more than US$ two billion (Porter and Vergin, 2006).

Table 4-4: FDI Inflows into Libya: 1971-2013 (millions of US$, at current prices)

YEAR	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979
FDI Stock	NA	5057	5183	4982	4988	4412	4675	4224	3532	2944
FDI Inflows	NA	71	126	-201	16	-576	263	-451	-692	-588
YEAR	**1980**	**1981**	**1982**	**1983**	**1984**	**1985**	**1986**	**1987**	**1988**	**1989**
FDI Stock	1,855	1,11	719	393	376	495	318	312	394	519
FDI Inflows	1,089	-744	-392	-327	-17	119	-177	-98	98	125
YEAR	**1990**	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**
FDI Stock	678	770	869	927	855	766	654	586	459	330
FDI Inflows	159	92	99	58	-73	-88	-112	-68	-128	-128
YEAR	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**
FDI Stock	471	338	483	626	983	2,021	4,085	7,935	11,115	14,425
FDI Inflows	141	-133	145	143	357	1,038	2,064	3,850	3,180	3,310
YEAR	**2010**	**2011**	**2012**	**2013**						
FDI Stock	16,33	16,4	17,759	18,461						
FDI Inflows	1,909	NA	1,425	702						

Source: UNCTAD (2013 Data).
KEY: NA = No data available

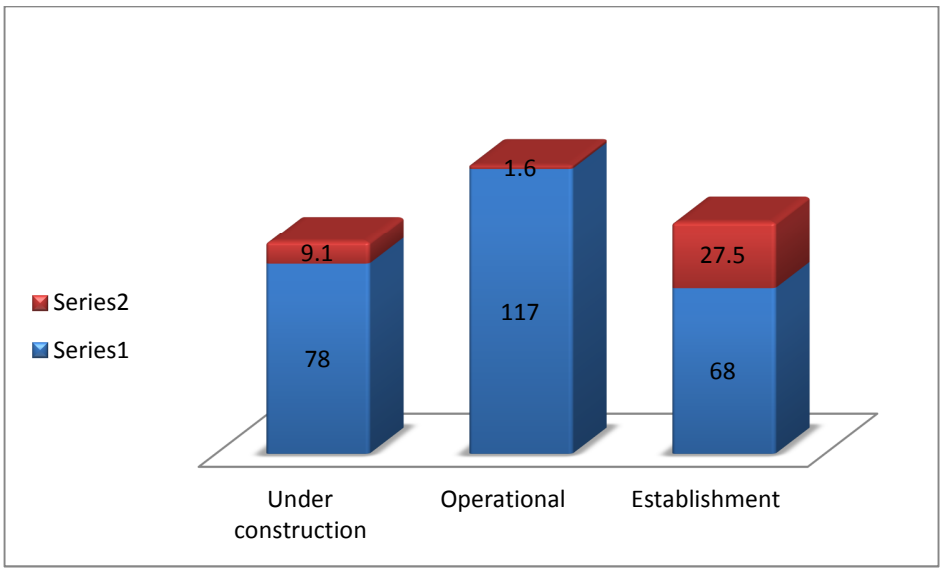
As shown in Table 4.5, the FDI inflows into Libya mostly average negative annual inflows during the year are from 1973-2001, and then began to significantly increase from 2002 as shows in table 4.5. This significant increase was the result of previous economic reforms, the government policies toward encouraging investment, supported by the lifting of UN sanctions in 1999, and finally, the removal of US sanctions in 2004. This level of FDI can be regarded as reasonable considering the short timescale involved and the fact that the previous investment environment acted as a major obstacle to foreign investment, particularly in non-oil sectors (Zoubir, 2009).

4.4.2.1 Overview of FDI Projects in Libya

This section briefly considers recent FDI inflows to Libya, focusing particularly on investment which is operational and under execution. According to PIB data (which excludes the gas and oil sector, which comes under the direction of the National Oil Corporation), during the period 2000-2012, some 263 projects were registered with PIB

with total capital accountant of over US$ 38 billion in various stages- operational, under construction and establishment.

Figure 4-3: Number of FDI Projects by Sectors



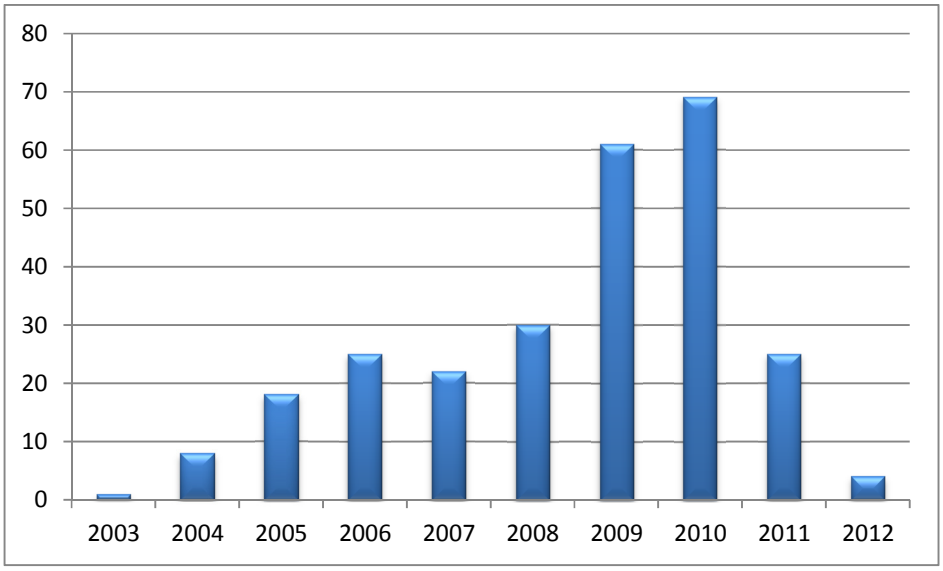
Source: PIB Database (2012)

Looking in more detail at the projects under execution, these accounted for 78 (29.6%) of the total projects, generating a value of over US$ 9 billion. Some 15 are fully foreign-owned companies whilst the other 63 are joint ventures. In terms of employment, these 78 projects created 20,157 new jobs of which 70% (13,897) were occupied by Libyan workers while some 117 projects (44.4% of the total) are operational, with 45 being fully foreign-owned companies and 72 joint ventures. Together they generated a total of US$ 1.6 billion and created 17,362 new jobs with Libyan workers accounting for 14,818 of these, or 85.3% of the workforce. Those projects still at the establishment stage accounted for 68 projects or 25.5% of the total projects registered with PIB and accounted for the remaining value which is about US$ 27.5 billion.

Despite the slow start, FDI volumes increased significantly over this period. This increase in the volume of foreign investment appears to be mainly due to the opening up of the economy to foreign investment under the enactment of the economic reforms such as the

privatization of medium- and large-size Libyan enterprises, and the reduction in trade and non-trade barriers as the country underwent preparations for accession to WTO. These policy changes helped to establish Libya as a market economy by creating business confidence for foreign investors. As a result, the numbers of new foreign investment establishments have been growing since the ending of US sanctions in 2004. An average of 31 new foreign invested firms have been registered annually between 2006 and 2010, in contrast to an average of only nine companies pre-lifting of US sanctions.

Figure 4-4: **Number of Companies Investing in Libya (2003-2012)**



Source: PIB Database (2010 and 2012)

Libya's natural resources and strategic geographical location also attract foreign investment. Since the economic reform in the early 1990s, some 263 projects from 45 countries have invested a total of over US$ 17 billion in Libya. The largest foreign investment inflows were registered there in 2007, amounting to USD 3.8 billion; however the global financial crisis in 2008 had a negative effect on FDI inflows to Libya, as was the case for many other countries and regions (UNCTAD, 2010).

4.4.2.2 Geographic Distribution of FDI

The spatial distribution of projects represents the firm's choice of regional location in which they decide to locate their operations. Libya is divided into four investment regions, known as the Western, the Eastern, the Central, and the Southern (PIB, 2013). Foreign investment is highly concentrated in urban areas with over 85% of total foreign investment being registered in western region especially in and around Tripoli where over half (51.5%) of the Libyan population resides. This appears to be mainly due to the presence of a large domestic market in urban centers and the heavy concentration of population there. The other three regions have received very small amounts of foreign investment. The Eastern Region received about 10% of foreign investment where about 17% of population lives. This region (which consists of five provinces including Benghazi City, one of the country's trade centres, and the Green Mountain area, which is rich in tourism resources) has received foreign investment mainly in the manufacturing and services sectors.

The Central Region has received only about 3% of foreign investment, most of which is in the areas of services and mineral enrichment as this region is also home to the country's largest oil and gas resources. The Southern Region, which has no major cities, has not attracted any foreign investment in non-oil sectors, due to the lack of necessary infrastructure, the small domestic market in non-urban centers and the smaller concentration of the population in desert areas.

It must be mentioned that despite more than a decade of market-oriented reforms, physical infrastructure in rural areas remains far from satisfactory, discouraging foreign firms from relocating there. This might also explain why manufacturing foreign investment is largely located in urban centers and regions located far from the capital city have received the least amount of investment in this sector (PIB Investment Report, 2012).

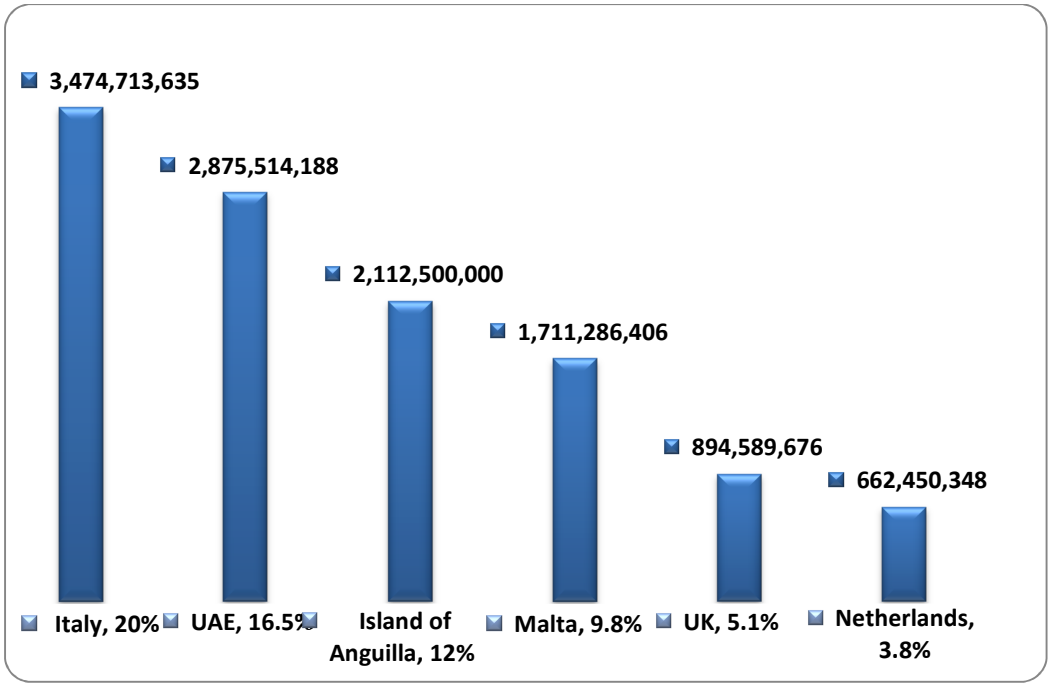
Some 24% of Libya's total population lives in the Southern and Central Regions, but only 3% of the total investment have been made there. The implication of this is that foreign investment has failed to benefit the rural population, leading to a rise in migration to urban centers (PIB Investment Report, 2012).

4.4.2.3 Source of FDI

Libya has received foreign investment from more than 45 countries. The six major countries are shows in figure 4.5 Italy remains the most important source of FDI into Libya. These six countries accounting for over 20% of total foreign investment; it invested more than US$ 3.4 billion during the 2002-2010. Most Italian investments have been aimed at taking advantage of Libyan natural resources and geographical proximity may also have contributed to attracting Italian investment. Italian investments tend to be in medium-scale projects in the services and manufacturing sector (PIB Investment Report, 2012).

The UAE is the second largest source of foreign investment to Libya, amounting to nearly US$ 3 billion or some 16.5% of the total foreign investment in the country. This is distributed across various sectors but is mainly in the food industry and services sectors. The third largest source of foreign investment comes from the Caribbean island of Anguilla, and accounts for about 12% of the total investments (US$ 2.1 billion), with the focus on manufacturing sector in form of joint-venture. Malta's investment, accounting for about 9.8% of total foreign investment, is mainly concentrated in the areas of health, services and manufacturing. Maltese investors have also implemented some relatively large projects in real estate under construction and they account for 69% of inward foreign investment in the real estate sector.

Figure 4-5: Sources of FDI Inflows by Country of Origin



Source: PIB Database (2012)

Despite the significant influence of UK investment in the past, particularly since Libyan independence until the early of seventies it is currently a relatively small player in foreign investment in Libya (accounting for about 5.1% of total foreign investment). UK firms invest mainly in tourism, health, manufacturing, services and the processed food industry. Finally, Dutch firms account for about 3.8% of total foreign investment i.e. some US$ 662 million. Many other countries including France and the Bahamas have also established large enterprises in the building materials industry, the food industry and services (PIB Investment Report, 2012).

4.4.2.4 Sectors distribution of FDI

The sub-section will focus only on the sectorial distribution of FDI in operational and under construction stages as shown in table 4.5 as those stages are already located in the region and employ workforces. The establishment ones are still not active and in the

license stage. Table 4.6 reviews those which are operational and under construction. These two stages accounted for195 out of 263 projects registered at PIB with total capital of US$ 10, 7 billion.

The manufacturing sector accounted for 104 or 53% of the 195 projects were 59 projects in operation stage. The total capital invested by this sector was US$ 4.1 billion representative the second amount among the sectors and created 11,272 job opportunities for Libyan workforces by 2012. The increasing number of the companies attracted by the manufacturing sector can be explained by the fact that the demand for building materials has increased particularly when the Libyan government's adopted the infrastructure developments program since the start of the new millennium to meet the growing needs of the construction sector coupled with the privatization of the public industries firms (PIB, 2012).

Table 4-5: An overview of Libyan FDI (2012)

Sectors	Number of Projects	%	Total invested (USD)	%	Local Jobs created	% Jobs created By sector
Manufacturing	104	53	4,142,929,716	38.3	11272	39.3
Health	17	9	133,098,274	1.2	948	3.3
Tourism	13	7	1,016,425,723	9.4	3853	13.4
Services	46	24	4,264,463,245	39.2	10006	34.8
Real estate	8	4	1,204,032,693	11.2	2386	8.3
Agriculture	7	3	26,073,571	0.24	257	0.9
Total	**195**	**100**	**10,787,023,222**	**100**	**28, 715**	**100**

Source: Prepared from data provided by PIB (2012).

The service sector consider to be the second largest sector in terms of the number of the projects with 46 projects, were 34 or 74% of the projects in this sector in the operation stage, and the first sector in terms of the amount invested with US$ 4.2 billion as shows in the table 4.6. The most important factor for attracted FDI into services sectors has been the active promotion of tourism activities by the Libyan government in recent years, coupled with the previously inadequate hotel and tourist resort facilities, which have provided opportunities for investment. In addition, investment in the services sector in

general is easier manufacturing and gives returns in relatively shorter periods (The Arab Investment and Export Guarantee Corporation Report, 2011).

Investment in the real estate sector amounted to US$ 1.2 billion (11% of the total capital) whilst the tourism sector produced a comparable amount at US$ one billion (10%). Much lower quantities of investment were registered for the health sector (US$ 133 million) and the agriculture sector, which received least investment (only US$ 26 million), 1.2% and 0.3% respectively of the total capital invested.

The privatization of a state-owned health company attracted investments from several countries such as Tunisia, Malta and Egypt. However, this sector provides very little employment to local workers (only 9% of the total employed by foreign companies) due to the skill-intensive nature of this industry (PIB Investment Report, 2013:4).

The construction sector has only received 4% of total operational foreign investment. The enactment of the Land Ownership Law for Libyan citizens, which does not allow private foreign ownership of land, also appears to have had a negative impact on the growth of this sector. Although the construction sector employs 8.3% of the labor force, it appears that the net impact on job creation for the local population is very small due to the outsourcing of cheap labor from neighboring countries in construction-related activities.

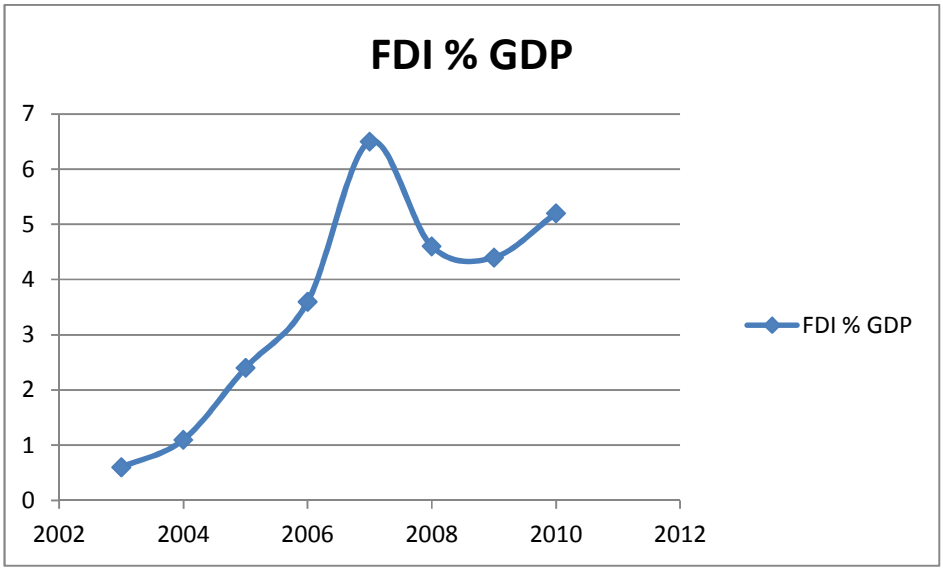
Other sectors, such as agriculture, have received relatively small amounts of foreign investment, accounting for 0.9% of the total foreign investment stock in the country. The low foreign investment in the agriculture sector is due to many reasons, the most important of which is the limited arable land available (less than 0.3% of Libya) and the ownership of land. Furthermore, the high salinity of ground water and the lack of a clear-cut investment scheme associated with resources of water such as man-made river have made it impossible to invest in many areas.

4.5 FDI in the Libyan Economy

FDI is still not an important component of the Libyan economy. Although its share in the economy continued to grow slowly, from a mere 1% in 2004 to more than 6.5% in 2007

it then decreased again in to 5.2% in 2010 (see Figure 4.1). However, compared to the economies of some other countries in the region, where the share of FDI in GDP accounted for similar averages in 2010, Libya has been rise attracting foreign investment as mentioned earlier, mainly due to the opening up of the economy and reform investment policies, which increased the confidence of foreign investors, but yet still more to do in order to enhanced its share in the GDP if really wants to diversification its sources of income (PIB Investment Report, 2012).

Figure 4-6: Inward FDI as a percentage of Libyan GDP (2002-2010)



Source: UNCTAD (2013, Database).

4.6 Conclusion

This chapter has documented the performance of the Libyan economy and its policy regime during the period 1970 to 2010. Since the 1960s, the Libyan economy has been based on its oil and gas sector. After the discovery of oil in the early 1960s, Libya developed under a planned economic system which was highly integrated with the economies of other developing nations. During this era, foreign trade was largely controlled by a few state-owned trade organizations with the government establishing export and import companies and setting ceiling prices. Libya maintained a system of

multiple customs tariffs and many products were subject to export and import prohibitions and a licensing regime.

Libya faced severe macroeconomic constraints and its GDP growth began to fluctuate from its moderate growth during the pre-1990 period. Inflation soared and the national deficit rose and unemployment rose rapidly, due to the weakness of state-owned enterprises. To overcome these economic difficulties, Libya undertook major reforms in early 1990s. These included liberalization of state-controlled prices and tariffs; privatization of state-owned properties; liberalization of trade and investment regimes; establishment of a two-tier banking system, adoption of a floating exchange rate, and promotion of private sector development through a favorable legal environment. The chapter also documented Libya's trade performance following the introduction of market-oriented policies in the early 1990s, and has highlighted that it became more open towards foreign trade compared with the 1980s since UN sanctions were lifted in 1999 and Libya gained accession to observer member status in the WTO.

This chapter also presented the trends of FDI in Libya and its contribution to GDP. Since Libya reformed its foreign investment regime in the late 1990s, FDI inflows have increased significantly, largely due to improved business confidence by foreign investors. A large proportion of foreign investment has gone to manufacturing, where Libya has a comparative advantage, followed by services and real estate. The country's building material industry attracted a significant amount of foreign investment mainly due to its abundant supply of natural resources. The privatization of large enterprises also attracted a significant amount of foreign investment in manufacturing industries and services sectors.

The tourism sector has also attracted foreign investment, but its share is still small in terms of total foreign investment flows. Economic liberalisation has attracted FDI in the construction industry, which has increased in the last five years to meet the growing needs of the housing sector. Libya has failed to attract foreign investment in its agricultural industries, and the investment in tourism still limited which attracted the

main FDI inflows into the neighboring countries (The Arab Investment and Export Guarantee Corporation Report, 2012).

In terms of geographic distribution, foreign investment is mainly concentrated in the urban areas, especially in and around the capital city, Tripoli. Poor physical infrastructure in rural areas appears to have discouraged foreign firms from locating their business in these areas. With regard to source countries of foreign investment, the shares of FDI came from many different countries, but the top six countries which had invested in Libya were Italy, UAE, and the Caribbean island of Anguilla, Malta, UK and the Netherlands. Libya has failed to attract significant investment from other major industrialized economies such as Japan or the USA. Clearly, a large increase in foreign investment has created jobs, mainly in urban centers, while rural and regional areas have failed to benefit from foreign investment inflows.

Chapter 5

Methodology

5.1 Introduction

This chapter discusses as well as justifies the suitability of the choice of the methods adopted to achieve the aims and objectives of this study. In order to understand the underlying causes of natural phenomena and events, researchers have developed a number of methods and techniques to improve the accuracy and depth of the information which they gather. However, the type and nature of this information depends upon the type of methods used; thus, the choice of an appropriate collection method is crucial to the quality of the data needed for this research. The chapter details the research design, strategies and methodology used in this research. It is divided into two main parts; the first deals with the research model, philosophy and approach, while the second discusses the research design, the instrumentation used and the development of appropriate measurement techniques.

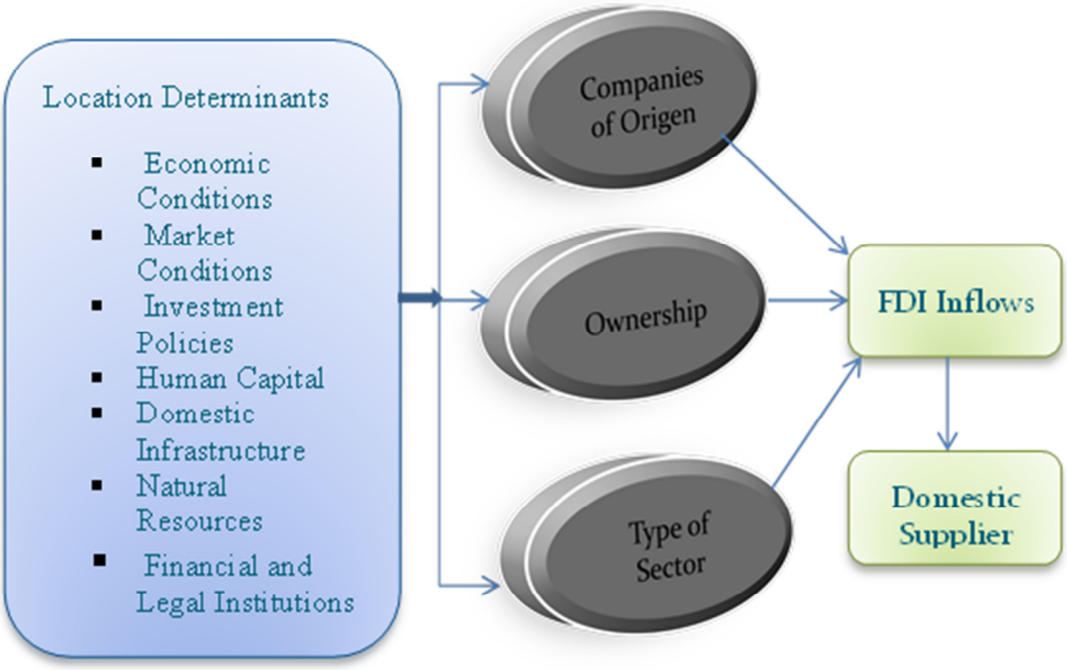
5.2 Research Model

As indicated in Chapter One, the main aim of this study was to identify the major factors which can be considered to be locational determinants of FDI. The study also intends to identify differences which may exist among these factors in relation to various characteristics of FDI, namely nationality, industrial sector and ownership. Finally, the study also assesses the effects of FDI on Libya's local economy be examining supplier-customer linkages.

Since this study aims to identify the views of foreign investors in Libyan, it depended on FDI theory, sector of activity, and mode of entry (country of origin and ownership). The research questions examined in this study were drawn from the proposition that FDI investment decisions are mainly influenced by the characteristics of FDI. However, these characteristics affect the relationship between locational determinants of FDI and

investment decisions differently. They are thus, divided into three groups namely, nationality (MENA or Western countries), sector of activity (manufacturing or services), and type of ownership (fully foreign-owned or joint venture). The theoretical research framework is represented in Figure 5.1.

Figure 5-1: Research Model



5.2.1 Research Philosophy

According to Easterby-Smith *et al.* (2008) and Saunders *et al.* (2009), the research philosophy reflects the researcher's way of thinking about the knowledge development, which consequently determines the way a particular research project should be undertaken, and determines how the overall research process should be carried out including the topic data gathered, analysed and used. Research philosophy also

recommends how to adapt the research design with respect to constraints of knowledge structures (Easterby-Smith *et al.*, 2008). Easterby-Smith *et al.* (2008); Saunders *et al.* (2009) and Easterby-Smith *et al.* (2008) argued that there are two main philosophical traditions that determine how social research is undertaken: positivism and phenomenology (also known as Interpretivism), while Creswell and Clark (2007) stated that the research philosophy depends on the epistemological and ontological assumptions made by the researcher, and is the primary determinant of an appropriate research methodology. This is how researchers express their views about the nature of reality and apply these views to the phenomenon in question (ontology). In view of this, researchers are bound to hold various assumptions which play specific roles in how they acquire knowledge about that phenomenon (epistemology). Ultimately, the acquisition of this knowledge will affect how research should be conducted, in terms of its methodology, as well as the methods used for data collection (Creswell and Clark, 2007; Ryan *et al.,* 2002). It is argued that the assumptions underlying a research design can be derived from one of two research philosophies or paradigms (Collis and Hussey, 2009; Easterby-Smith *et al.,* 2008).

Saunders *et al.* (2009) highlighted that the research philosophy underpins the research strategy, time horizon and data collection methods. It also determines whether the research should follow a deductive or inductive approach. In this context, Saunders *et al.,* (2007) and Easterby-Smith *et al.*, (2008) categorize two common paradigms or philosophies which are widely used in business and management research, and argue that each of these two philosophies has its own advantages and disadvantages. The first of these is the positivist paradigm which relates to the assumptions needed to investigate a phenomenon such as causality, it is used in hypothesizing, and deduction and in identifying causal explanations. It also involves breaking down the research problem into component parts rather than analysing them from a holistic viewpoint or as a whole situation. In order to be able to generalise, a large and sufficient sample size is required, because this allows researchers to draw appropriate conclusions which are representative

of the wider population (Sekaran, 2000; Collis and Hussey, 2009). Furthermore, the positivist paradigm usually focuses on developing and testing theories/ hypotheses, and generalising the research findings. However, as an exception, the positivist approach tends to employ more quantitative deductive methods such as experiments and surveys than inductive methods (Saunders *et al.*, 2009).

The phenomenological paradigm, on the other hand, is known by a variety of names in the literature including the constructivist paradigm, interpretivism, or constructivism (Collis and Hussey, 2009*).* It is:

> *A theoretical point of view that advocates the study of direct experience taken at face value; and one which sees behaviour as determined by the phenomena of experience rather than by external, objective and physically described reality* (Remenyi *et al.,* 1998, p. 34).

Unlike the positivist paradigm, the phenomenological paradigm contributes to the evolution of new theories by attempting to understand peoples' own meanings which are often difficult to control. Furthermore, Saunders *et al.* (2009) note that statistical generalization is less valuable in this paradigm and thus less important, because each research case is seen as being uniquely different from every other. This paradigm relies on the assumption that the researcher interacts with what is being investigated thus creating an interpretation of the phenomenon being investigated based on in-depth knowledge about the situation (Collis and Hussey, 2009). In addition, this paradigm aims to develop a deeper understanding of multidimensional concepts through exploratory techniques, and deals with qualitative methods, such as observation and/or in-depth interviews consistent with the inductive research approach (Gill and Johnson, 2002).

Table 5-1: Positivism and phenomenology compared.

Positivism	Phenomenology
The ideology	
▪ Objectivist: there is an external viewpoint from which it is possible to view the world or organizations. ▪ Observer is independent.	▪ Subjectivist: the world and organizations are socially constructed. ▪ Observer is part of what is being observed.
The Researcher	
▪ Is an object of enquiry who believes that good research is done by undistorted recording of observations using efficiency-driven method of investigation. ▪ Focuses on facts.	▪ Believes that 'to know' is to experience directly, immediately and purely. ▪ Focuses on meanings.
Research progress	
▪ Hypothetico-deductive. ▪ Utilizes quantitative data. ▪ Based on cause and effect. ▪ Context-free. ▪ Scientific and experimentalist.	▪ Gathering data from which ideas are induced. ▪ Use of qualitative words. ▪ Mutual simultaneous shaping of factors. ▪ Context-bound. ▪ Humanistic and interpretivist.
Preferred methods include:	
▪ Uses large samples. ▪ Static design: categories isolated before study. ▪ Focus on explanation and prediction.	▪ Exploring small samples in-depth or overtime. ▪ Emerging design: categories identified during research. ▪ Focus on generating local understanding.

Developed from: Lee and Lings (2008); Bryman and Bell (2007); Maylor and Blackmon (2005); Partington (2002); and Hussey and Hussey (1997).

The authors fail to agree on whether it is better to adopt positivist or phenomenological techniques or a combination of both paradigms as a pragmatic approach. More is said about their respective strengths and weaknesses in table 5.1. However, it has been argued that using mixed methods is likely to provide a richer perspective on the research problem, and could possibly reduce the weakness of using a single method (Sekaran; 2003; Smith *et al.,* 2008).

This research adopted a pragmatic approach, using both the positivistic and phenomenological paradigms. It is argued that since each paradigm has particular strengths and weaknesses, using both paradigms can maximise the advantages from both and minimise the disadvantages of using either one alone. Consistent with this choice and the research objectives, and in line with the used of triangulation methods (Bryman and Bell, 2007; Saunders *et al.,* 2007), this research adopted a mixed method approach. The dominant method was quantitative and relies on data collection using a self-administered questionnaire distributed to foreign companies. This was supplemented by a qualitative method in the form of in-depth interviews.

5.2.2 Research Approach

Based on the available literature, two research approaches have been identified by Bryman (2011) which is deductive (testing theory) and inductive (building theory). The deductive approach is a research strategy which refers to the logic of drawing conclusions on the basis of given facts (Williams and May, 1996). Hence, this type of method implies the collection of a great number of facts, from which conclusions can be drawn. This kind of research begins by developing hypotheses based on theories, collecting data, testing these hypotheses, and supporting or modifying the theory as required (Creswell, 2003). Therefore, deductive research is in line with the positivism paradigm and quantitative research strategies (Saunders *et al.*, 2009). In other words, a number of given facts do not need to be proven, and the conclusion should not be thought of as really new, but only presented in a new form which is more or less inherent in the already given information (Bryman, 2007).

The inductive approach on the other hand is defined as "*the derivation of a general principle or possibly a law in science, which is inferred from specific observations*" (Williams and May, 1996, p. 22). Unlike the deductive approach, the inductive approach begins with data gathering and tries to make sense of this during analysis in order to formulate a theory. Usually, this type of research focuses on data patterns and tries to explain the relationship among variables. An inductive strategy takes advantage of observations and data collection methods to answer research questions for the purposes of building a theory.

However, the reasons for choosing a deductive approach instead of inductive are: First, the literature of FDI allows developing theory which can be tested in later stages. This approach, as argued by Ghauri and Gronhaug (2005), is deduction. Second, deduction can be a lower-risk approach, although there are potential risks, such as the non-return of questionnaires. In contrast, induction is a more risky approach since there is fear of not getting useful data patterns and, thus, theory would not appear (Cooper and Schindler, 2006). Third, when the research attempts to generalize the findings in order to represent the entire population. This makes the choice of the deductive approach most appropriate since deduction aims to generalize findings from sample to population, while the inductive approach aims to generate theory or investigate new ideas (Saunders et al., 2009). In line with the previous argument, the current research study is based on the deductive approach since the factors used in the study and the hypotheses were developed from the literature relating to Dunning's Eclectic theory. Consequently, the qualitative data obtained from a number of interviews conducted with representatives of foreign companies was used in order to gain a better and deeper understanding of the context.

5.2.3 Research Design

There are different types of research design, each one referring to the purpose of the study such as exploratory, descriptive, explanatory and predictive (Collis and Hussey, 2003). An exploratory study looks for patterns, ideas or hypotheses rather than testing or conforming existing hypotheses. Hussey and Hussey (1997, p. 10) observe that

exploratory research "*is conducted into a research problem or issue when there are very few or no earlier studies to which we can refer for information about the issue or problem*". Therefore, this type of study is used when the research aims to examine an unfamiliar topic or to break new ground particularly when the topic has not been previously explored (Collis and Hussey, 2003:5). The exploratory study, using typical techniques such as case studies, and qualitative and quantitative data can be used for historical analysis and observations.

A descriptive study usually describes the development of a particular issue. Quantitative and statistical techniques are often used for data collection and analysis. Unlike the exploratory study, descriptive research is more focused on examining the issues or problem of the study than on trying to break new ground (Collis and Hussey, 2003:5).

An explanatory study is an extension of the descriptive study, although this type of research attempts to explain the reasons underlying the change in a phenomenon and analysing why or how this change occurred (Saunders *et al.,* 2007:140). The predictive study goes further than that of the interpretative research strategy, in the sense that the latter gives an explanation of what happens in a particular case, whereas the former forecasts the likely occurrence of a similar situation in other places. Predictive research aims to analyse certain phenomena by predicting on the basis of default (Collis and Hussey, 2003:6).

Based on the classification above and the objectives of this research, this study could be classified as descriptive, exploratory or explanatory, because the first three objectives are related to the characteristics and distribution of FDI within Libya. Likewise, the fourth and fifth objectives indicate the main locational determinants of FDI flows to Libya and the level of satisfaction of foreign investors. The fifth objective can also be classified as explanatory or analytical research since it attempts to assess the impact of FDI on local economy.

5.2.4 Research Strategy

The design for any research provides the general framework for the acquisition and analysis of data associated with the phenomenon under investigation (Bryman, 2008:40). A number of designs are available for the researcher to choose from depending on the research problems and the associated objectives of the study. Bryman (2008:45) identified five main types of designs, namely, experimental, longitudinal, case study, cross sectional, survey and action research.

An experimental design allows the researcher to investigate the impact of one independent variable on another dependent variable, provided that all other variables which might influence the relationship between the two are kept neutral. The most important characteristic of this design is that it is based on a clear-cut theoretical framework, and focuses on a small number of variables. It is also possible for the experiment to be repeated many times to study the independent effects of isolated variables on each another. A longitudinal design is particularly associated with the areas of social sciences such as sociology and social policies and is not of direct relevance here.

A case study entails a single case or unit being investigated in-depth by the researcher by highlighting all aspects of the case in detail. The unit could be a homogenous entity such as a company, a person or some kind of event (Bryman, 2008:52). This design is useful in cases where adequate information about the unit needs to be gathered, particularly in cases where knowledge of all aspects of the unit or the case history of the person involved is indispensable. Comparative case study design entails studying two contrasting cases by using more or less identical methods). In this case, making comparisons at different levels and relating to different features is important (Bryman, 2008).

Across-sectional design involves data being collected predominantly using questionnaires or structured interview on more than one case (usually considerably more than one) at a single point in time. This is done to collect a body of quantifiable data in connection with

two or more variables (usually more than two), which are then examined to detect patterns of association (Bryman, 2008:53).

A survey design is usually referred to as a comprehensive survey. However, the design might include a limited number of elements, as in the case with survey through using samples which is very common in social sciences, and known as a social survey Saunders *et al.,* 2007. The social survey design constitutes the most appropriate one for the current research for a number of reasons. Firstly, this research aims to explore opinions and perceptions concerning the main factors that determine FDI. In other words, whether the economic reforms and investment policies that adopted by the government are appropriate for attracting further FDI. Secondly, by using the survey, it is possible to collect large amounts of data from a sizeable population in a highly economic way (Saunders *et al.,* 2007:144). The measurement process requires the collection of information about a number of variables in relation to the main locational determinants of FDI in the country which directly affects the degree of satisfaction of foreign investors.

These factors are numerous and diversified including economic reforms, often measured by economic factors, market factors, government investment policy factors, levels of tax and government regulation, and red tape. Utilities and facilities are measured by means of availability of skilled and semi-skilled labor and their wage levels, infrastructure levels, availability and quality of raw material, and research development and training systems as well as financial and legal institutions.

Finally, the method used for data collection to answer the research questions depends on the design of the questionnaire, with the interviews providing further support. This research can also be considered to be a case study using the Libyan investment environment as the research requires an in-depth investigation. In other words, since this study aims to collect detailed data relating to Libyan investment determinants, and assessing the impacts of FDI on the local economy, a case study is suitable for realizing these objectives.

Surveys are selected for this study because commonly used by business and management researchers and are usually associated with the deductive approach used in business studies for several reasons. Firstly, they allow researchers to collect a large amount of data. Secondly, it is possible to use surveys for data gathering in different types of study such as exploratory, descriptive or explanatory. Thirdly, the literature on locational determinants of FDI highly recommends the use of surveys as a method for data collection in situations where the goals is to measure the views of a large section of the population that can only be indirectly observed. By using surveys, it is possible to obtain information that cannot be collected using other methods. Finally, unlike other methods (for example, direct observation) which cannot be generalized due to the smallness of their sample sizes, surveys can lead to generalisations (Saunders *et al.,* 2007:144).

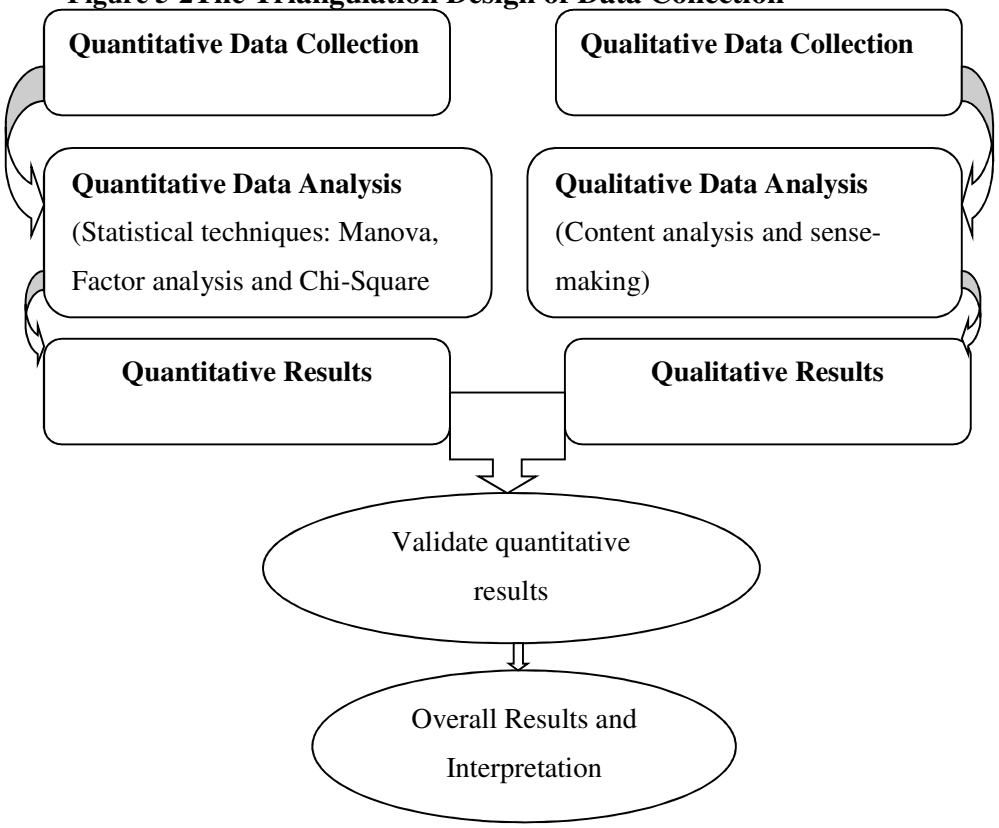
5.3 Primary Data Collection Methods

Beyond the choice of the method used, several other factors such as data, research population, and the resources available to the researcher can affect the nature of the research (Donald *et al.,* 2011:141). Data can be collected from either secondary or primary sources. Secondary data sources that are available to a researcher to obtain necessary information for a research problem include print (such as books, archives, publications, annual reports, and journals) and digital (internet, CD-ROM) (Saunders *et al.,* 2007; Sekaran, 2003). On the other hand, primary data can be obtained by employing various techniques including the ones used in this study, namely, questionnaires (considered to be a quantitative method of collecting data), and interviews (a qualitative data collection method). Most business researchers use a combination of both methods to investigate their research problems and to provide answers to the research questions (Easterby-Smith *et al.*, 2008; Creswell, 2003).

The combination of quantitative and qualitative methods might make the findings support each other and provide more understanding and insight into the context or setting (Creswell and Clark, 2007). In this context, Collis and Hussey (2009) reveal that in-depth

interviews are a good instrument for obtaining qualitative data that complement data gained from a questionnaire survey.

Figure 5-2The Triangulation Design of Data Collection



Source: adapted from Creswell and Clark (2007, p. 63).

Therefore, in this research, a triangulation approach combining quantitative and qualitative methods was adopted in order to achieve the study objectives as shows in Figure 5.1. The data related to gathering information on the main determinants of FDI, and assessing the possible linkage between foreign companies and domestic suppliers was collected by questionnaire, at the same time some interviews were carried out for the same purposes. In other words, a combination of quantitative and qualitative data in the same study will be useful to explore and understand the research issues, and provide support for validating the questionnaire (Bryman & Bell, 2007).

5.3.1 The Questionnaire

It was observed from the literature review that among the number of data collection methods related to survey strategies, namely, structured interviews, structured observation and questionnaires, the latter is the most widely used technique for collecting the required quantitative data, particularly in business and management research. Moreover, this method can cover a large number of respondents, at a reasonable cost and with minimum effort. In essence, questionnaires consist of a number of questions in relation to the subject of the research and members of the research population are asked to respond to these. The questions should always be clear and easy to understand and should all be included in one document. The questionnaire can be presented to participants using any one of four ways: via the internet (either using a website specifically designed for this purpose or by e-mail), over the telephone or by hand (Bryman, 2008).

With regard to the questions, these can either be open-end or close-ended, provided they are initially examined for clarity, gradation, distinction and validity. An initial assessment of the questionnaire should be done using a small experimental sample to establish whether or not all the questions are relevant to the aims of the research. The self-completion or self-administered questionnaire is one method of gathering information and this was selected for this research for a number of reasons. It gives the researcher the chance to explain the research topic in order to encourage the respondents to give their answers honestly and to clarify any questions that might be confusing to them. Employing this method can also help to improve the response rate and reduce the chances of time delays or missing mails.

5.3.1.1 Questionnaire Population and Sample Frame

The sampling frame is a list of all the elements of the study's population from which the researchers draws their sample (Saunders *et al.*, 2009). For this study, the researcher has used firm level as the unit of analysis, focusing on fully foreign-owned and joint-venture

companies in a cross-section of manufacturing and service industries in Libya. The populations of this research depend on the official list obtained from the Register Office of the PIB which contains some 263 companies. The sampling frame was logically established based on foreign ownership (a company with at least one foreign partner), and firms that were already operating in Libya. Consequently, only 111 firms qualified to participate in the study, and due to this small number, the researcher decided to target all of these for this study.

The rationale for this 100% sample was supported by Gay (1996) who argued that, in the case of small populations (N = less than 100), there is little point in sampling and the researcher needs to survey the entire population of the study. General Directors, Assistant/Vice-Directors and Board Chairmen were targeted as the respondents for this research. The reason for choosing them is that they are in a good position to complete the questionnaire and should have the necessary knowledge to provide confidential, accurate and useful data regarding the variables of the study.

5.3.1.2 Questionnaire Measurement Development

Extra care was taken in constructing the questionnaire: several drafts, assessment and pre-testing were all carried out before producing the final version. The questionnaire was designed to capture the information required including locational determinants of FDI, and to assess the impact of foreign companies on the local economy through the supplier-customer linkages. The items used in this questionnaire were composed from existing related literature, and took into consideration comments from a panel of academics and suggestions from international business experts working at the PIB. To ensure that only relevant items were included in the final instrument, the researcher paid extra attention and carefully scrutinised relevant literature for measures used in previous studies, gained further information from personal in-depth interviews and conducted a pilot test.

The variables used in this study were selected, operationalized and measured in two ways. First, to explore the determinants of FDI in Libya, all items and variables used in

this research were developed from various existing literature reviews and those that had previously been employed as locational determinants of FDI in research settings the measures of which had been adopted as having acceptable measurement quality.

Secondly, all those variables were considered that were unique to the conceptual case study; their operational measures had been derived through interviews and discussions with an academic with expertise in international business and three FDI experts working in the PIB. Since these three individuals run investment firms, they were able to increase the richness of the information, by adding new items and verifying the scope and content of the measures. Results from the interview proved to be very helpful in assessing the validity of the items contained in the questionnaire, and minor modifications and adjustments were suggested.

Those items were grouped into seven subgroups as presented in the questionnaire (see Appendix A). Collis and Hussey (2009) recommended that when developing the questionnaire, the researcher should use clear, simple and direct language, and avoid using words that have more than one meaning. In addition, questions should be kept as short as possible without affecting their meaning.

Participants are offered guidance on how to complete the questionnaire in the form of a question that is similar in content to the others in the same section for the purposes of clarity. The questionnaire begins with general questions and then moves onto more specific items, encouraging respondents to answer the rest of the questionnaire without leaving any gaps. The questionnaire design should be related to the type of questions used and these, in turn, should be linked to the research aims and research paradigm adopted in the study (Easterby- Smith *et al.* 2008).

Following feedback suggestions, some statements were rephrased positively while others were stated negatively to avoid biases in the questionnaire. Also, the double-barrel statements were broken down into single statements to ensure the precise meaning of

words. Closed questions were used in the research questionnaire, consisting of optional and "please specify" types of questions.

Furthermore, the questionnaire was then tested in the pilot study for authentication. The questionnaire consisted of three main parts. The first part concerned participant and company profiles while the second part investigated the views of investors regarding locational determinants of FDI. In this research, a five-point Likert scale was used in most questions, except those relating to general information concerning respondent or company profiles. The options ranged from (1= highly discourage, 2= slightly discourage, 3= not effect, 4= slightly encourage, 5= highly encourage), with respect to factors such as economic, market, financial and legal issues, investment policies, incentives, and utilities. Finally, the last part looked at the impact of FDI on local economy through supply linkages and sales.

5.3.1.3 Translation and Questionnaire Pre-testing

It is important to ensure that the questionnaire is designed carefully and needs no more improvements before it is distributed to the target sample. Thus, before the final draft was produced, the questionnaire underwent numerous revisions with the supervisory team, to ensure that it was structured in a way that related to the research objectives and framework (Malhotra and Birks, 2007). The questionnaire was originally written in English (which is not an official language in Libya) and was then translated into Arabic language for those who preferred this language since some companies were from Arabic-speaking countries. The translation process and pilot study underwent several stages. Firstly, the English draft of the questionnaire, as well as the cover letter to be included in the survey package, was produced and then translated into Arabic by the researcher. The cover letter was used to explain the purpose of the questionnaire and to provide details about the study and ensure respondents about the confidentiality of any information they might give. Since this might affect the response rate, the researcher paid extra attention and gave careful consideration to these details.

Next, English and Arabic versions of the questionnaire were sent to two PhD students in different fields studying at UK universities. They were asked to check the layout of the questions, the suitability of the questionnaire design and to provide comments about any unfamiliar terms or difficulties respondents are likely to encounter. The researcher used the suggestions and comments obtained from the pre-test, which were mostly concerned with the formatting and clarity of the questions, to improve the overall quality of the questionnaire.

Thirdly, when the researcher went back to Libya for field study, copies of both the Arabic and the English version of the questionnaire were given to two academic staff with PhD degrees, working in the Economics Department of two different Libyan universities, such as (Tripoli and Benghazi) for further scrutiny regarding the format and wording. Then, the final version of the questionnaire was carefully translated into Arabic and then back-translated into English by individual experts in order to ensure its validity in each language and to check the correctness of the grammar and the level of clarity.

Fourthly, many studies have recommended piloting the questionnaire on a small number of the sample before its actual usage with the full sample. Thus, a total of ten questionnaires were distributed to fully foreign-owned and joint venture companies operating in Libya who were requested to complete the questionnaire. Respondents were then asked to comment on the questionnaire format and wording, and also the validity of each separate item. The purpose of this process was to help finalise the flow of the questionnaire and enhance its reliability. Two weeks later, seven completed questionnaires of the ten distributed were collected, in order to obtain feedback about any unclear issues or problems which had been identified. The researcher discussed the questionnaire with each respondent individually, and addressing all the comments received from the pilot test ensured that the questionnaire met the expectations of the research, in term of information, clarity and precise understanding by the respondents.

5.3.1.4 Conducting the Questionnaire

This research aimed to survey non-Libyan investors, listed by PIB, who run companies or their branches which are associated with non-oil sectors. The study employed a self-administered questionnaire as a method of data collection to avoid any postal delays or lost mail, and to have direct contact with participants in order to explain and clarify any statement that might be confusing to them. Consequently, the researcher distributed the questionnaire by hand.

A covering letter, supporting letters from the University of Huddersfield, the Libyan Cultural Affairs Attaché in London, and the PIB were also attached to the questionnaire. The letter briefly explained the objectives of the study, the importance of respondent participation in the research, and assured participants about the confidentiality of their responses. It also gave contact details for the researcher and his supervisor in order to obtain a high response rate. When distributing the questionnaire to the foreign companies, the researcher also outlined the purpose of the research to respondents and encouraged them to contact him at any time if clarification on any point was necessary. Respondents were also asked to provide their contact details so they could be informed when the questionnaires were to be retrieved after completion.

5.3.2 Interviews

There are three different types of interviews: structured, semi-structured and unstructured. While the second and third types are mostly used in the phenomenological paradigm, the first type is associated with the positivistic approach (Collis and Hussey, 2009). The structured interview usually takes a standard format, with an emphasis on fixed-response categories and systematic sampling. In the unstructured interview, questions and answers are unstructured and the respondent can freely discuss the issues under study, offering opinions and reactions. The advantages of the semi-structured interviews are that "the researcher can prompt and probe deeper into the given situation also, interviewers are able to probe or asked more detailed questions of respondent's

situation. In addition, the researcher can explain or rephrase the questions if respondents are unclear about the questions" Patton (2002, p. 343). The decision to use a particular type of interview as a method of data collection depends on the research questions.

Semi-structured interviews were used as the method of collecting primary qualitative data in this research, covering topics which could not be easily investigated using the type of close-ended questions used in the questionnaire. Thus interviewing was identified as an ideal method of allowing the researcher to verify, build on and add depth to the results of the questionnaire survey (Cooper and Schindler, 2011, p. 183; Saunders *et al.,* 2009). In interviews, the researcher is able to ask follow-up questions to obtain the kind of detailed information that cannot be obtained from the questionnaire (Remenyi *et al.,* 1998). Therefore, the interview offered a useful tool for understanding the construct about the topic under consideration (Easterby-Smith *et al.,* 2008).

5.3.2.1 Interview population

The population of this study covered two groups in order to gain an in-depth understanding of the issues related to FDI in Libya. The first group was comprised of fully foreign-owned and joint-venture companies which can be said to make up the demand side of the equation. The second group included senior officials from the Libyan government dealing with FDI who can be said to form the supply side of the equation. The government officials who were interviewed occupy key supervisory positions at different levels of responsibility from Departmental Heads to a Ministry Undersecretary at four government bodes two were Ministries which are (Ministry of Economics and Ministry of Industry) and other two were government organization which are (PIB and General Planning Council). The population of senior government officials drawn from the management structure of PIB came from Management Committee of PIB has five members including the Secretary and his/her assistant and three departments each department has two members as following:

- Strategic projects and renewable energies management

- Consolidated net management
- Studies and Planning Department
- The Management Board Committee

The Ministry of Economics contains two departments:

- Strategic Planning and Economic Studies
- Research Administration

The Ministry of Industry has two departments:

- Industrial Development and Investment Management
- Strategic Planning.

General Planning Council only target the legal department

Consequently, the government official population included 15 individuals, 11 were selected from the PIB and two from the Ministry of Economics and one from Ministry of industry and one from General Planning Council.

5.3.2.2 Interview Sampling

Interviewing staff from all the fully foreign-owned and joint–venture companies and government officials was impossible due to the given limited time available for fieldwork. For this reason, the survey was limited to a sample which was intended to represent senior government officials and the foreign investor community in Libya. A different criterion was used to choose the interviewees sample for each group. For the foreign companies, this was based on approval given at the questionnaire stage when nine respondents from this group indicated that they would be glad to be interviewed. Four other interviewees from the foreign investor community were judged selected to represent different characteristics such as sectors, ownership and country of origin to make sure that the all types of respondents were covered. Table 5.1 shows the participants of the semi-structured interview sample conducted with 13 representatives of the foreign investor companies.

The interviews were undertaken between September and October 2012 solely by the researcher, using either Arabic or English, as the interviewee preferred because some are from Arabic-speaking states. All of the interviews conducted with representatives of both groups were semi-structured face-to-face.

Table 5-2: Interview Sample: Foreign Investors

Company	Sector	Country of Origin	Ownership	Interviewees
A	Manufacturing	UAE	J-V	General Director
B	Manufacturing	Austria	J-V	General Director
C	Manufacturing	Spain	J-V	General Director
D	Services	UK	J-V	Board Chairman
E	Manufacturing	Italy	J-V	Deputy Director General
F	Services	France	J-V	Director General
G	Services	Tunisia	J-V	Deputy Director General
H	Manufacturing	Cyprus	F	Deputy Director General
I	Services	Egypt	F	General Director
J	Manufacturing	Austria	F	Deputy Director General
K	Manufacturing	Morocco	F	Director General
L	Manufacturing	Egypt	F	Deputy Director General
M	Services	Malta	F	General Director

Source: Field data
KEY:
J-V = Joint-Venture Company
F = Fully Foreign-Owned Company

As a preliminary step to selecting the sample of senior government official, the author relied on a comprehensive survey by sending letters to all potential participants, outlining the main aspects of the interview and asking them to cooperate. Accordingly, only those who responded were interviewed, suggesting that the sample is a convenience sample. Table 5.2 shows that interviews were held with seven senior government officials, three of whom were employed by the PIB, two from Ministry of Economics, one each from the Ministry of Industry and General Planning Council.

Table 5-3: Interview Sample: Government officials

	Sector	Interviewees
A	PIB	Head of Research and Planning Department
B	Ministry of Economics	Undersecretary of the Ministry of Economics
C	Ministry of Economics	Director of Strategic Planning
D	Ministry of Industry	Undersecretary of the Ministry of Industry
E	PIB	Deputy Director of PIB
F	PIB	Director of Investment Management
G	General Planning Council	Legal adviser to General Planning Council

Source: Field data

The interview was carried out by asking 13 representatives of foreign investors and seven senior government officials about three major aspects relating to foreign investment inflows and linkages, namely, location choice, challenges and difficulties and backward linkages of FDI, in order to gain more in-depth insights into some of the issues raised by the questions incorporated in the questionnaire. Thus, the interviews with senior government officials in Libya covered strategies needed to improve the Libyan business environment.

5.3.2.3 Interview Validity

Before commencing the interview, the questions and procedures were reviewed by a academic staff who provided valuable observations and comments. Furthermore, to check the compatibility of the interview method for this purpose, the method was presented to a number of experts at PIB and in academic institutions. Accordingly, two rehearsal interviews were conducted with two representatives, one from the foreign investors and the other one the government officials, to make sure that all the questions were understandable. By taking these steps the researcher ensured that the interviews were able to proceed as planned.

5.3.2.4 Administration for Conducting the Interview

The semi-structured interviews took place from mid-September to end-October 2012. All of the interviews were conducted with the subjects in their offices during working hours. Originally, it was planned to record interview, provided the subjects gave their consent in

advance but some participants only agreed to speak on the condition that the interviews was not recorded. Thus, the researcher took written notes.

At the beginning of each interview the researcher introduced himself to the participants and briefed them about the research, the research questions and the purpose of the interview and the time would take. Interviewees were reassured them that they could discuss things at their own pace without intervention from the researcher who would note their responses. Interview times ranged between 20 and 90 minutes. After each interview, the researcher transcribed the interviewee's responses and sent these to the interviewee so they could review what had been said and raise any concerns they had about the contents. Interviewees were requested to reply within a week of receiving the transcript. As no responses were received by the specified deadline, the researcher was able to move on to the next stage which is analysing the data.

5.4 Limitations and Difficulties

Generally, the fieldwork process was a positive one and respondents were very supportive and co-operative. Despite that, some difficulties arose with the questionnaire survey for investors and with the interviews with both groups of respondents.

1. Following the pilot survey, the researcher realised that the initial questionnaire was relatively long, and that each question comprised many variables which might put respondents off since they would have limited time to answer the questions. Hence, the number of variables for each question was reduced, and all open questions were omitted.
2. The researcher experienced problems in defining the research population, given that some foreign companies registered with PIB were actually local companies owned by Libyan nationals residing overseas. Consequently, differences existed between the PIB's definition of FDI companies and that of the researcher. Thus, for the purposes of this study, all companies owned by expatriate Libyans were

classified by the researcher as local companies even though they were registered with the PIB as FDI companies.

3. The research was heavily dependent on foreign companies and senior government officials, time schedule, as they were very busy and has limited time. The period of time was also very tight for the field survey (which eventually took three months) and preparations for the survey took more time than expected. Distributing the questionnaire and receiving the completed forms back took much longer than anticipated. The researcher made many visits to each company and usually had to wait, even when he had an appointment. Sometimes it took several weeks to schedule an interview with a manager. Some were then too busy to be interviewed; others cancelled and rescheduled their appointments several times. This added to the complexity and the length of the data collection process. For example, it took the researcher over two weeks to obtain a statement of data collection approvals from the Ministry of Higher Education, and more than two months to finish the task of interviewing twenty representatives of foreign investor companies and senior government officials.

4. Some companies could not be accessed by the researcher due to various constraints including their location (in some cases, they were located over 1500 km distance from the researcher's place of residence), finance, time and poor security conditions in some areas of Libyan during the period of the distribution of questionnaires.

5. Despite the cooperation of the PIB staff regarding the collection of the questionnaire, the initial response rate was poor. Only 44% of the total distribution was retrieved. The reason for this low value was that many managers frequently travel outside Libya for other commitments by nature of their work and, thus, were absent when the questionnaires were distributed. A follow-up reminder was sent which resulted in the return ratio increasing to 66.6%.

5.5 Data Analysis Methods

As mentioned early, both quantitative and qualitative approaches were adopted within the present study. The questionnaire was used as a main data collection method and semi-structured interviews were conducted with the managers and chairman board in order to give more details about the results that emerged from the questionnaire. The following sub-sections provide a brief discussion about the pre-tests and the methods used in analysing the obtained data from field study, using SPSS Version 20.

5.5.1 Quantitative Data Analysis

Selecting the right statistical methods depends on the objectives of the study and the nature of the data in line with the research questions and framework. Each part of the questionnaire was analysed using appropriate statistical technique. The first part of the questionnaire consisting of respondents' demographic and company profiles, used descriptive statistics while descriptive statistics and the MANOVA (Multivariate Analysis of Variance) test was employed for the second part. This helped to identify differences in the determinants of FDI among the groups as this study distinguishes between three characteristics of FDI. In the third part chi-square and a cross- tabulation statistical tool was used as the objective of the final part was to assess the impact of FDI on the local economy through supplier-customer linkages.

5.5.1.1 Descriptive Statistics

In order to provide a summary of the respondents' demographic characteristics, the first statistical technique adopted was descriptive analysis. Descriptive statistics, also known as exploratory statistics, involves the transformation of raw data into information which can be described as a set of factors in a situation. This is accomplished by ordering and manipulating the raw data (Sekaran, 2003). The test of non-response bias suggested by Armstrong and Overton (1997) was used to compare the demographic characteristics of early respondents; i.e. questionnaires returned within two weeks after initial distribution,

with those of late respondents, to see if these were feasible representatives of the overall population.

Descriptive statistics such as frequency, means, and percentage were used to determine the sample characteristics in terms of the respondents and responding companies. They were also employed to give insights into the shape of the sample distribution. In addition, means were used to rank a set of items and factors according to the relative importance which each had in the investor's decision to invest in Libya and the research variables that are formulated in the hypothesis to be tested. Chi-square was used to test non-response biases of the responses (see Chapter Six).

5.5.1.2 Factor Analysis

The factor analysis technique was used for three main purposes: first, to understand the structure of a set of variables, second, to construct a questionnaire to measure the underlying and finally, to reduce the data set to a more manageable size while retaining as much of the original information as possible (Field, 2013. p. 673). There are two factor models known respectively as principal component analysis (PCA) and common factor analysis. The latter is also known as exploratory factor analysis. Although there has been a considerable debate over which factor model is more appropriate, when used in empirical research they usually bring similar results and solutions (Hair *et al.*, 2010; Field, 2013). In this context, Field (2013) argued that differences between PCA and common factor analysis arise largely from the calculations, and may be difficult to conceptualize for non-statisticians.

The use of PCA is typically appropriate when the aim is to reduce the original set of variables into smaller sets of combined variables, whereas common factor analysis is generally used when the primary concern is to identify the underlying common dimensions in the original variables (Hair *et al.,* 1998, 2003, 2010). Furthermore, the PCA techniques explored the underlying correlations among a large number of variables (e.g. questionnaire responses) in order to combine them into a smaller set of dimensions

that have a common relationship, known as factors. Additionally, PCA tends to be more stable and is by far the most commonly used model in business research (Hair *et al.,* 2010).

In this study, factor analysis was the second statistical technique used to conduct the PCA with Varimax rotation. This was to find out whether the items which were used to measure each location factor in question B (questionnaire part 2) led to any patterns of factors, and whether they confirm the factors specified in the research framework (construct loaded onto a single factor or divided into multiple factors, in other words, whether the variance accounted for was through a given dimension or not). The results from the PCA report eigenvalues as a criterion for measuring construct variance accounted for by a given dimension. Only factors that have eigenvalues greater than one are considered significant; otherwise they are considered insignificant and disregarded (Steven, 2002; Tabachnick and Fidell, 2007; Hair *et al.,* 2010 and Field, 2013). The next chapter provides a more detailed explanation.

5.5.1.3 Multivariate analysis of variance (MANOVA)

There are a number of statistical tools which can be used to assess the statistical significance of differences between groups such as the t-test, ANOVA and MANOVA. The t-test and ANOVA techniques, also known as univariate tests, are both appropriate to use only in cases when there is one dependent variable. However, MANOVA is an extension of the analysis of variance designed for use in the case of testing several dependent variables (multivariate test) (Steven, 2002; Hair, 2010; Field, 2013; and Pallant, 2013). Therefore, MANOVA is another statistical technique used in this research to test the research hypothesis regarding differences in the set of eleven dependent variables among three groups of FDI companies (independent variable) leading to differences in the set of eleven dependent variables. Hair *et al.* (2010) recommend a multivariate analysis as a statistical technique that can be used to investigate mean differences among groups combining several dependent variables.

MANOVA is used to identify the differences in dependent variables (location factors) based on a firm's characteristics. MANOVA is an extension of analysis of variance (ANOVA) in that it can accommodate more than one dependent variable. As with ANOVA, the independent variables in MANOVA are a categorical variable, and the focal point is on the differences between the levels of each categorical variable. Nevertheless, what makes MANOVA a multivariate procedure is that it examines the differences between groups for more than one dependent variable simultaneously (Hair, 2010; Field, 2013; and Tabachnick and Fidell, 2007). Moreover, MANOVA was been chosen because it accommodates multiple dependent variables while controlling for the Type I error that can be inflated when multiple univariate analyses of variance are employed (Steven, 2002). In the second research objective, the locational determinants of FDI are treated as the dependent variables, whereas the firm's characteristics variables (ownership, nationality and types of investment) are treated as the independent variables. Each independent variable is tested separately.

In the case where significant differences among levels of independent variables were detected (meaning that the collection of the dependent variables differed among levels of the independent variable), the tests of significance used with MANOVA are Hotelling's Trace, Pillai's Trace, Wilks' Lambda, and Roy's Largest Root when assessing the difference between group means. Wilks' Lambda is the test of significance used in this study, and reported an alpha level of .05 as recommended by Field (2013). However, the other tests of significance along with their effect, size and power are reported in this study to provide additional information about their similarities and differences. In the event that the independent variable has two levels, Wilks' Lambda is used; otherwise if the independent variable has more than two levels, the ordinary MANOVA is utilized (Hair *et al.*, 2010).

Finally, MANOVA assumptions are considered in this study. The first assumption was the equivalence of the variance/covariance matrices across all groups. Fortunately, if the groups are of roughly equal size (i.e., if the size of the largest group divided by the size of

the smallest group is equal or less than 1.5), a violation of this assumption has minimal impact (Hair *et al.*, 2010). The Box's M test is used to check for this assumption. Usually, values below .05 indicate a violation of this assumption. The second assumption (homogeneity of variance) is tested using Leven's test of equality of error variance. However, if the groups are roughly of equal size then a violation of this assumption has a minimal impact. The last assumption states that any linear combination of the dependent variables must follow a normal distribution. This assumption is tested by visually inspecting the histogram for each dependent variable. Finally, the recommended sample size for MANOVA is 20 observations per cell. At minimum, the number of subjects in each cell should be more than the number of the dependent variables utilized in the study in order to be considered for this analysis (Hair *et al.*, 2010). The minimum required sample size is satisfied in this study. In this study, MANOVA was chosen to test the research hypothesis whether the dependent variables used in this study varied among the three subgroups or not. In other words, differences were tested for each of the three groups (company ownership, sector of activity, and company's country of origin).

5.5.1.4 The Chi-Square and Cross-Tabulation Test

The chi-square and cross-tabulation test is another statistical test used in this study. Field (2013) was of the view that, the chi-square test can be employed to determine whether the observed frequencies are different from what is expected. This implies whether or not the two variables are associated because it compares the frequency of cases found in the different groups of one variable across the different groups of another variable, and it reveals if there are statistically significant differences between the groups. The interpretation of the outcome of the chi-square test is as follows. If the *p*-value for the scoring of the Pearson chi-square is equal or lower than 0.05, a statistically significant association exist between the two variables and those two variables are significantly different among the groups. This means that the hypothesis of a correlation can be accepted or vice versa (Field, 2013). When employing a chi-square test, a significant assumption has to be made, which is the minimum expected cell frequency. According to

Pallant (2013), minimum expected cell frequency should be 5 or greater than 5 (or at least 80% of the cells have expected frequencies of 5 or more). If this assumption is violated, the outcomes of the chi-square test will be less accurate (but not necessarily false). Therefore, it is more suitable in this case to use Fisher's exact test instead which is also provided as part of the output from chi-square (Field, 2013; and Pallant, 2013).

5.5.2 Qualitative Data Analysis

Unlike quantitative data analysis, there are no standardised techniques for analysing qualitative data. Each approach depends on the nature of the data involving different strategies to deal with the data that was collected (Saunders *et al.,* 2003). Qualitative data analysis consists of identifying, coding, and categorising patterns found in the data (Drever, 1995). At the simplest level, this analysis involves examining the assembled data to determine how the research questions can be addressed.

It can be argued that the content analysis approach is the most appropriate one to be used in analysing data emerging from interviews. According to Louis (2013) content analysis identified as a research technique for the objective, systematic, and quantitative description of manifest content of communication*s*. It can be used to determine the presence of certain words, concepts, themes, phrases, characters, or sentences within texts or sets of texts, and to quantify their presence in an objective manner (Riessman, 2004) defines content analysis as an empirically grounded technique, exploratory in practicability, and predictive and inferential in purpose. What distinguishes content analysis from other methodologies of enquiry is that it analyses data from their contexts or uses.

To conduct content analysis on a text, the content is first of all quantified objectively according to explicitly formulated rules (Sanders, 2009). The text is then coded or broken down into manageable categories and then examined. The results are then used to make inferences about the messages within the texts of which these are a part.

The content analysis in this study employed the following tactics. The first step was to examine the texts (i.e. the interview transcripts) and then code them to verify the existence of certain words or concepts. These words or concepts were then quantified and examined to see how they were related (for example, whether there was a strong presence of positive or negative words used with respect to a specific argument). Some qualitative data can also be approached in a quantitative way. Thus, if an idea appeared in the data frequently, it was reasonable to count how often it appeared. But, it must be made clear that such counts were used to provide a useful summary of some aspects of the analysis and that these figures do not represent a statistical sample. The main purpose for using content analysis is to identify patterns in text and the themes or major ideas emerging from the sources of data. As the analysis was divided into different categories, links were made between categories to demonstrate how the themes emerged and how conclusions about the findings were drawn.

The interpretative technique was manually adopted in order to analyse the data from the interviews. This technique is explained by Bryman (2005:13) as an approach that respects the differences between people and the objects of the natural sciences and thus, requires the social scientist to understand the subjective meaning of social actions.

The data obtained from the interviews was processed and analysed using a number of steps. Data were initially categorised into meaningful themes according to the framework and objectives of the research. These themes were the factors that influence the decision of foreign investors to invest in Libya and the obstacles facing the foreign investors, as well as the factors relating to the difficulties of using local suppliers. When interviews had been recorded, a transcript of the responses is produced and the researcher reviewed this transcribed data carefully by reading and re-reading, line by line in order to identify topic areas related to the research aims. Where no recording was available, a version was made from the notes taken by the interviewer.

The full set of participant responses for a particular question was gathered together. The data was then unitised, which means attaching relevant units of data to the appropriate

themes that had already been devised. A unit of data could vary in length from a phrase to paragraph. Then, themes were generated and the data reorganised thematically. This process continued and was repeated, seeking new themes from the data gathered, and placing the units of the data within suitable themes. This led to the sub-division of the initial themes. Categories of responses to each question were developed and relevant data was placed under each category. The responses were described in terms of the topics or categories and relevant quotations were identified.

The method of analysis used in this research was deductive in nature, in the sense that the concepts identified in the coding process were analysed according to the research framework. Any new themes or concepts that arose in the interviews were handled in a flexible manner and considered in relation to the research framework. All the conclusions drawn from this method are shown in chapter six and then compared with the quantitative findings to illustrate the discussion in chapter seven.

5.6 Conclusion

This chapter presented and justified the research philosophy and design adopted in order to achieve the aim and objectives of this research. The methodology for this study, described as a multi-methods approach (quantitative and qualitative), made use of survey questionnaire and interviews to achieve the research objectives. A rationale for this choice was also provided. A questionnaire was used as the core method of data collection whilst semi-structured interviews were used to clarify and support the results that emerged from this. A detailed explanation was provided of the efforts which were taken to ensure that this instrument was fit for purpose, including a pilot study, use of expert opinion to improve the various drafts of the questionnaires. A detailed description of the questionnaire design and layout, question types and format was given, together with an explanation of how it was administered. The issues of interview population and sample and validity were also discussed, followed by a critical review of the difficulties faced by the researcher during fieldwork. The chapter concludes with descriptions and discussions of the statistical methods used to achieve the objectives of this study.

Chapter 6

Research Findings

6.1 Introduction

This chapter presents the data for analysis that was obtained from the fieldwork conducted in Libya. These include the results of the self-administered questionnaire (see Appendix A for a copy of the questionnaire) and the face-to-face semi-structured interviews (see Appendix B), which were employed in order to achieve the stated research objectives and address the research questions. The study employed the statistical methods outlined in the previous chapter, using SPSS version 20 to present the descriptive findings from the questionnaire survey. The results regarding the state of existing Libyan business environment in terms of promoting and creating a business-friendly environment for both fully foreign-owned and joint venture companies are examined here. Furthermore, this chapter presents the descriptive analysis of the semi-structured interviews which involved a samples of the fully foreign-owned and joint venture companies targeted by this study questionnaire.

This chapter is divided into six sections in addition to the introduction and conclusion. Following the introduction, this chapter begins by describing the process of entering the primary data into the statistical package. A discussion of the descriptive analysis of this data forms the basis of the next section. The next section focuses on the hypothesis test. Later on shifts to the descriptive analysis of the in depth interview data which came from the interviews carried out with representatives of foreign companies and Libyan senior government officials. The chapter concludes with a summary of the main points which have been covered.

6.2 Questionnaire Data Preparation Tests

This process included the preparation or screening of the data, and considering questionnaire response rate, validity and reliability. These processes are discussed in

details in the following sub-section, beginning with the data cleaning which takes place before implementing the statistical methods used to test the research questions, in order to investigate the quality of the data. The data preparation processes consisted of treatment of missing data and testing for outliers, response rate and bias issues.

6.2.1 Data Cleaning

After receiving the returned questionnaires, a four-stage preparation procedure was adopted in order to investigate the quality of the data. This was as follows:

I. Preparing or screening of the data in order to discard unusable questionnaires. The following criteria were used for discarding questionnaires:

- Any questionnaires that failed to provide complete information for major items.
- Any questionnaires completed by unqualified individuals
- Any questionnaires completed by more than one respondent.

II. Data editing and coding were employed to tabulate and edit the data. A five-point Likert-scale range of 1-5 was used to indicate the response to each question.

III. Treatment of missing data. Frequency tests were conducted to assess if there were any missing data as some respondents may have been reluctant to cooperate or may have forgotten to respond to some statements. In some cases, minor missing data were identified and items were considered as incomplete. In addition, in order to provide a full picture of the overall respondent profile, a frequency test was employed to classify respondent profiles. From a total return of 74 questionnaires, 63 were considered complete, and some 11 discarded.

IV. Identification of outliers. Outliers are considered problematic as they are not representative of the sample and can seriously distort statistical results. When comparing group differences, outliers are sought separately within each group and investigated in the data screening process by using a boxplot method. Only one

case of outliers was found in this study but this was not considered problematic for running statistical tests (Field, 2009, p. 153).

6.2.2 Response Rate

From the total sampling frame of 111 fully foreign-owned and joint venture firms, 74 questionnaires were returned, representing a response rate of 66.6% of the total of questionnaires sent. However, visual investigation led to 11 being discarded as unusable meaning that some 63 cases (56.8%) were usable for further data analysis. This low response rate was acceptable according to the guidelines established by Saunders *et al.* (2009), who indicated that the response rate for self-administered questionnaires is usually satisfactory if it is between 30 and 50%. In addition, Brennan (1990) and Comegys (2000) found that the researcher's status has an effect on the response rate with student researchers normally obtaining a lower response rates than corporate or professional researchers. Table 6.1 presents a summary of the information regarding respond rate of the questionnaire.

Table 6-1: Questionnaire Response Rate

Questionnaires	**No.**	**%**
Total of questionnaires distributed	111	100
Total of questionnaires received	74	66.6
Missing questionnaires	37	33.3
Incomplete questionnaires	11	10.0
Usable questionnaires	**63**	**56.8**

6.2.3 Non-Response Bias

After the questionnaires had been sent out to the targeted sample, follow-up was made by the researcher in order to attempt to maximize the response rate. Responses from the two batches of respondents (i.e. those who replied by themselves, and those who replied after the follow-up) were tested for non-response bias.

Non-response bias is usually applied when a researcher conducts a field survey. Due to the nature of this type of study, it would be highly unlikely for all the units of the survey to respond. Therefore, most researchers will draw their conclusions for the study based on the responding sample and will assume that this sample does not greatly differ from the non-respondent sample. If a systematic difference between the respondent and non-respondent sub-samples is observed, the outcomes do not allow researchers to say that the entire sample would have responded in the same way (Bryman and Cramer, 2005).

Since the response rate in this research was 66.6%, this means that there was a non-response rate of about a third, and consequently, testing for non-response bias becomes important in order to ensure that the sample has the potential to represent the entire population. One technique which is commonly used to evaluate the potential non-response bias, as suggested by Bryman and Cramer (2005), they compared the organizational demographic characteristics, such as the size, sector, or age of the organization in order to checks performed to determine whether or not there is a difference between respondents and non-respondents. This study will check the different between two waves of early respondents i.e. those questionnaires returned within two weeks or more after initial distribution (n=49 returned during August 2012) with those of late respondents i.e. those questionnaires returned after a reminder was sent (n= 25 returned during September 2012), to identify whether data received from respondents who responded only after repeated contact resembles that of non-respondents or not.

In this research, testing the differences between respondents and non-respondents was conducted with respect to sector (type of business). Other characteristics, such as age and size were not used in the test since the majority of the fully foreign owned and joint - venture firms are relatively close to each other in age and size (i.e. a vast majority of foreign firms were established after the year 2002, and the majority of them employ less than 300 employees).

Table 6-2: Outcomes of the Chi-square test

Characteristic	Pearson Chi-Square	Df	Sig.
Type of Business	.778	1	.378

The Chi-square test was performed in order to find out whether or not there was a significant difference between respondents and non-respondents with respect to sectors category. The results of the Chi-square test reveal that there was no statistically significant difference between respondents and non-respondents with respect to sector (Chi-square value = 0.778, p = 0.378). This means that the sample was representative and the findings can be generalized from the sample to the population. The outcome of the Chi-square test is shown in Table 6.2.

6.3 Measure Purification of Locational Factors

In order to reduce the possibility that a single item might be misinterpreted, the second part of the questionnaire survey instrument was developed by using multiple-item measurement. Churchill (1979) highlighted three disadvantages of single item measure. Firstly, single items usually have substantial uniqueness in that each item tends to have a low correlation with the attributes being measured and tends to relate to other attributes as well. Secondly, individual items tend to classify people into a small number of groups. Thirdly, individual items typically have a considerable degree of measurement error.

Moreover, Churchill (1979) recommended that the purification process should be applied when dealing with multiple-item measure. Purification involves eliminating items that seem to create confusion among respondents and items that do not discriminate between subjects with fundamentally different positions on the construct being measured. The purification of measures is often used to assess the reliability and validity of the proposed measures. The reliability of multiple-item scales is assessed via unidimensionality and internal consistency (using coefficient alpha), whereas validity is obtained by selecting

items which are based on the literature review, comments from experts, and pilot testing. These two criteria of measure purification are discussed next.

6.3.1 Reliability

Reliability concerns the tendency toward consistency and stability of the results of the same set of sample given by repeated research instruments or measurements (Hair *et al.,* 2010; Sekaran 2003). Reliability of multiple-item scales is assessed by its unidimensionality and internal consistency.

6.3.1.1 Internal Consistency (Cronbach's alpha)

Reliability concerns the tendency toward consistency of the results of the same set of sample given by repeated research instruments or measurements (Hair *et al.,* 2010). In this study, the Cronbach's alpha measurement of internal consistency was undertaken to evaluate the overall reliability of the multiple-item measurement scale.

The internal consistency method assesses the homogeneity of a set of items. The basic rationale for this assessment is that every item in the same factor should behave similarly (Sekaran, 2003). The most popular test of internal consistency or homogeneity among the items is Cronbach's coefficient alpha (Bryman and Bell, 2007; Saunders *et al.,* 2007), which provides a summary measure of the inter-correlations that exist among a set of items. Cronbach's Alpha takes a value ranging between (0 – 1). The higher score, the more reliable indicates that there is similarity (or homogeneity) among the items. The recommended minimum acceptable level of reliability for Cronbach alpha is .60 according to Hair *et al.* (1998). Based on the data collected in this study, all the measures reported an acceptable Cronbach's alpha ranging from 0.694 to 0.885 this indicates that reliability an acceptable reliability as shown in Table 6.3.

Table 6-3: Reliability statistics using Cronbach's Alpha

Items	Number of Items	Cronbach's alpha
Economic Conditions	5	.885
Market Conditions	4	.772
Tax Exemptions	5	.745
Government Regulations and Red Tape	3	.878
Domestic Infrastructure	3	.876
Availability & Wages of Skilled Labor	3	.794
Availability & Wages of Unskilled Labor	2	.707
R&D and Training System	2	.763
Natural Resources	2	806
Financial Accessibility	3	.831
Legal Practice	2	.793
Dependent on the local suppliers to provide related inputs	3	.712
Difficulties regarding local suppliers	5	.694
Target Market	2	.793

6.3.1.2 Unidimensionality (Factor Analysis)

As explained earlier in chapter five, factor analysis was used to analyse quantitative data in this research. Unidimensionality is an assumption for the purpose of underlying the calculation of reliability, and is exhibited when items of a construct have acceptable fit on a single-factor solution (Field, 2013; Hair *et al.,* 2010). In the present study, the measurement of factors was thoroughly derived and cautiously modified from the previously existing literatures which were conducted at a particular period of time and in a specific location. Therefore, in order to guarantee that this measurement was in line with the objectives of this study, and the sample was also suitable for research conducted in Libya, the unidimensionality of each multiple-item scale was assessed by conducting a Principle Component Analysis (PCA) with Varimax rotation. This served the purpose of measuring whether a construct was loaded into a single factor or divided into multiple factors, in other words, whether the variance was accounted for by a given dimension in the research framework or not. The PCA test was conducted only with the items that measured the locational determinant factors used in the second part of the questionnaire.

Before conducting a factor analysis, the most commonly used techniques for examining underlying assumptions were carried out, such as the Kaiser-Meyer-Olkin Measure (KMO) and Bartlett's Test of Sphericity (Aaker *et al.*, 2001; Hair *et al.*, 2010; Steven, 2002; Tabachnick and Fedlle, 2007; Field, 2013). KMO was used as a first assumption to determine whether the given data were appropriate for conducting factor analysis or not. Typically, the KMO value for sampling adequacy varied between 0 and 1.0 (values between 0.5 and 0.7 are average, values between 0.7 and 0.8 are good, values between 0.8 and 0.9 are very good and values above 0.9 are excellent), which indicated that the data was suitable for conducting a factor analysis, while KMO values below 0.4 were considered to be low and values less than 0.3 not appropriate for conducting factor analysis (Hair *et al.*, 2010). This research reported KMO values equal to or above 0.5 as criteria indicating the data's suitability for conducting factor analysis. Bartlett's Test was used to assess the overall significance of all correlations within a correlation matrix, in order to indicate the suitability of the sample for factor analysis (Hair *et al.,* 2010; Field, 2009) and indicated a level of significant value (p should be less than .05). Therefore, it was concluded that the given data were adequate and appropriate for conducting factor analysis as shown below.

The second assumption was to decide which factors should be included; for this, the Kaiser's criterion is used. It indicates that selected factors should have an eigenvalue greater than one. Another criterion used in deciding how many factors should be retained is the percentage of the variance in the original data that is explained by all factors considered together and the ability to logically name the resulting factors. For example, Hair *et al.* (2003, p. 365) state that the ultimate goal is to derive a set of factors that are theoretically meaningful, relatively easy to interpret, and account for as much of the original variance as possible. Therefore, the results from PCA use eigenvalues as a criterion for determining the number of factors and a measure of construct variance accounted for by a given dimension (Field, 2013). Only factors that have eigenvalues greater than one are considered significant, otherwise they are considered insignificant

and ignored. The rationale for the eigenvalues criterion is that any individual factor should account for a variance of at least one if it is to be retained for interpretation (Field, 2013). However, the number of factors that should be selected is very subjective, the most suitable rule is to stop factoring when the factors stop making sense and become meaningless (Field, 2013).

To achieve the third assumption, the PCA with varimax rotation was employed to examine the estimated loadings and to assess the statistical significance of all items loaded in the factor, using values greater than the 0.4 criterion for significant item loading on a single factor (Steven, 2002; Tabachnick and Fedlle, 2007; Field, 2013). If the factor loadings of all the items loaded on the same specific factor exceed 0.4 in the same direction, these outcomes may offer acceptable evidence of dimensionality for those sets of items (Hair *et al.,* 2010, p. 378).

Rotation of factor is a determinant of the number of factors in a set of data, as unrotated factor solutions do not offer an adequate interpretation of the variables under examination (Hair *et al.* 2010; Field, 2013 p. 680). Rotation is used to improve the interpretability and scientific utility of the solution (Tabachnick & Fidell 2007). However, there are two main approaches to factor rotation, resulting in either an oblique (correlated) or an orthogonal (uncorrelated) factor solution (Pallant 2013). According to Tabachnick & Fidell (2007), the application of orthogonal rotation results in solutions that is easier to interpret and to report (Field, 2013 p. 681). In contrast, oblique approaches allow for the factors to be correlated but they are more complex to interpret, describe and report. Varimax rotation of the factors improves interpretation by reducing ambiguities that often accompany initial unrotated factor solutions (Hair *et al.* 2010). For this study, the orthogonal approach with varimax rotation was selected over the oblique method for two reasons: as an attempt to minimise the number of variables that have high loadings on each factor (Pallant, 2013), and because interpretation of a factor is easier because the correlating variables are clearer (Tabachnick & Fidell 2007). Furthermore, varimax rotation also

tends to reapportion variance among factors so that they become relatively equal in importance (Tabachnick & Fidell 2007).

Since a number of factors were identified, they should be interpreted based on the factor loading, which is the correlation between each of the original items and those newly extracted from the factor analysis. Factor loading is a measure of the relative importance of each item in representing that factor. Thus, the greater the absolute size of an item's loading, the more important it is in interpreting and naming the factor. The results of running a factor analysis are shown below, dealing with each of these factors separately in more detail in relation to the research framework.

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- **Economic Situation and FDI in Libya**

To find out whether the items which were used to measure the economic situation lead to any patterns of factors, and whether they confirm the specified dimension in the theoretical framework, factor analysis was used. The results of running the factor analysis are shown in Table 6.4.

Table 6-4: KMO and Bartlett's Test

Kaiser-Meyer-Olkin Measure of Sampling Adequacy		.838
Bartlett's Test of Sphericity	Approx. Chi-Square	194.957
	Df	10
	Sig	.000

The KMO value here is .838, which is regarded as good value (Field, 2013). Moreover, Bartlett's Test of Sphericity is highly significant (Sig. = .000). Thus, factor analysis is appropriate for this study's data.

Table 6-5: Total Variance Explained by Each Factor

Component	Initial Eigenvalues		
	Total	% of Variance	Cumulative %
1	3.536	70.710	70.710
2	.691	13.826	84.537
3	.355	7.106	91.643
4	.222	4.443	96.086
5	.196	3.914	100.000

The outcome of PCA with varimax rotation indicates that all the items that examined the economic situation were grouped into one single factor with eigenvalues of 3.536 which is greater than one and explaining 70.710% of the variance between the five items, as shown in Table 6.5; and the range of factor loading was 0.679-0.902, as highlighted in Table 6.6 below.

Table 6-6: Component Matrix

Items	Component
	1
Economic growth	.679
Inflation rate	880
Stability of Exchange Rate	839
Extent of government intervention in the economy	.902
Privatization procedures	.884

- **Market Conditions and FDI in Libya**

In the case of Marketing Conditions, this factor was measured by four items and in order to test whether they confirm the factor specified in the measure used in the framework, factor analysis was used. The outcomes of running the factor analysis are shown in Table 6.7 which indicates that the data were appropriate to run factor analysis. The KMO value here is .763, which is regarded as good according to Field (2013). Moreover, Bartlett's Test of Sphericity is highly significant (Sig. = .000) as Table 6.7 indicates.

Table 6-7: KMO and Bartlett's Test

Kaiser-Meyer-Olkin Measure of Sampling Adequacy		.763
Bartlett's Test of Sphericity	Approx. Chi-Square	74.025
	Df	6
	Sig	.000

The outcome of PCA with varimax rotation indicates that when all the items that examined Market Conditions were grouped into one single factor with eigenvalues greater than one and explaining 60.028% of the variance between the five items, as shown in Table 6.8.

Table 6-8: Total Variance Explained by Each Factor

Component	Initial Eigenvalues		
	Total	% of Variance	Cumulative %
1	2.401	60.028	60.028
2	.800	19.991	80.018
3	.492	12.304	92.322
4	.307	7.678	100.000

Also, the range of factor loading was 0.563-0.854, as highlighted in Table 6.9.

Table 6-9: Component Matrix

Items	**Component**
	1
Trend and growth of Local Market	.575
Competition in Local Market and market potential	.771
Availability and reliability of market information	.854
Existence of distribution channels	.563

- **Investment Policy and FDI in Libya**

With respect to the case of the Libyan government's investment policy toward attracting foreign investment, factor analysis was used to see whether the original items would combine in one factor to make new factors, and if this were the case, to check their consistency with the factors included in the research theoretical framework. In order to use factor analysis, the KMO test and Bartlett's Test were checked as Table 6.10 shows.

Table 6-10: KMO and Bartlett's Test

Kaiser-Meyer-Olkin Measure of Sampling Adequacy		.817
Bartlett's Test of Sphericity	Approx. Chi-Square	225.040
	Df	28
	Sig	.000

The KMO value here is greater than the minimum requirement of .4, and therefore, is regarded as a very good value. Moreover, the Bartlett's Test of Sphericity assumption is met as well, being highly significant (Sig. = .000). Thus, factor analysis is appropriate for this data.

This factor was divided into two dimensions. Table 6.11 provides the total variance that is explained by each factor (component), the result shows that, the two factors have eigenvalues of more than one, explaining a total 68.582% of the variance between the nine items. Based on the varimax rotation result there was one questionnaire item (item G) with a loading value less than .04 of the first component which indicates that the item is not adequate for the given pair of items. This means that this item should be dropped from the analysis (Field, 2013).

Table 6-11: Total Variance Explained by Each Factor

Component	Initial Eigenvalues		
	Total	% of Variance	Cumulative %
1	3.779	47.236	47.236
2	1.708	21.346	68.582
3	.695	8.682	77.263
4	.596	7.449	84.712
5	.389	4.857	89.569
6	.330	4.131	93.700
7	.287	3.594	97.294
8	.217	2.706	100.000

However, those two factors renames depends on their loading to tax exemption factor which explain 47.236% of the variance between the five items and the range of factor loading was 0.732-0.872, and government regulation factor explaining 21.346% with three items, and the range of factor loading was 0.608-0.904 as indicated in Table 6.12.

Table 6-12: Component Matrix

Items	Component	
	1	2
Regulation and control on foreign exchange transactions	.893	
Government bureaucratic procedures or red tape	.904	
Extent of corruption	.608	
Exemptions for import duties on imported raw materials		.846
Exemptions for import duties on imported machinery components		.872
Exemptions for tax holidays corporate tax		.817
Exemptions for tax on repatriation of dividends and income		.858
Tax in general		.732

- **Human Capital and FDI in Libya**

In the case of human capital, the factor was measured by a number of five items. These items were set to represent the factors included in this study's theoretical framework.

Table 6-13: KMO and Bartlett's Test

Kaiser-Meyer-Olkin Measure of Sampling Adequacy		.549
Bartlett's Test of Sphericity	Approx. Chi-Square	83.233
	Df	10
	Sig	.000

The KMO value is .549, which is above the minimum requirement of 0.5 and regarded as an average value according to Field (2013). Moreover, Bartlett's Test of Sphericity is highly significant (Sig. = .000) as shown in Table 6.13. Thus, factor analysis is appropriate for this study's data.

Table 6-14: Total Variance Explained by Each Factor

Component	Initial Eigenvalues		
	Total	% of Variance	Cumulative %
1	2.237	44.732	44.732
2	1.292	25.831	70.563
3	.828	16.554	87.117
4	.344	6.881	93.998
5	.300	6.002	100.000

Table 6.14 shows the PCA results indicate that this factor was divided into two dimensions (factors), and renamed as Skilled Labour and Semi-Skilled Labour, each factor having eigenvalues of more than one, and explaining some 70.563% of the total variance between the five items with the first factor explaining 44.732%, and the second factor explaining 25.831%.

Table 6-15: Component Matrix

Items	**Component**	
	1	2
Availability of technical and skilled labour	.775	
Wages for technical and skilled labour	.867	
Salaries required for managerial staff	.809	
Availability of semi-skilled labour		.828
Wages for semi-skilled labour		.826

Table 6.15 indicates that the first factor is made up of three items, all of which are related to skilled labour, namely: (1) availability of technical and skilled labour; (2) wages for technical and skilled labour and (3) salaries required for managerial staff. Thus this factor has been renamed as availability and wages of skilled labour. Two items are now loading onto the second factor; these items are related to availability and wages of semi-skilled labour; for example, the availability of semi-skilled labour and wages for semi-skilled

labour. The range of skilled factor loading was.775-.867 and the range of semi-skilled labour factor loading was .826 - .828.

- **Natural Resources and FDI in Libya**

Factor analysis was used for the case of the Natural Resources to see whether the original items combine in any patterns to make new factors, and if this is the case, to check their consistency with the factors included in the research theoretical framework. In order to use factor analysis, its assumptions were tested.

Table 6-16: KMO and Bartlett's Test

Kaiser-Meyer-Olkin Measure of Sampling Adequacy		.500
Bartlett's Test of Sphericity	Approx. Chi-Square	109.639
	Df	10
	Sig	.001

The KMO value here is equal to the minimum requirement of .5, and therefore, is regarded as an average value. Moreover, the Bartlett's Test of Sphericity assumption is met as well, being significant at Sig. = .001, as shown in Table 6.16. Thus, factor analysis is appropriate for this data.

Table 6-17: Total Variance Explained by Each Factor

Component	Initial Eigenvalues		
	Total	% of Variance	Cumulative %
1	1.424	71.197	71.197
2	.576	28.803	100.00

Table 6.17 shows the PCA results which indicated a single factor, namely, availability and quality of natural resources, which has eigenvalues of more than one, and explaining 71.197% of the total variance between the two items. Table 6.18 indicates that the two items are loaded into one factor; ranging from 0.814 to .844 for each item.

Table 6-18: Component Matrix

Items	Component
	1
Availability of natural resources	.814
Quality of natural resources	.844

- **Domestic Infrastructure and FDI in Libya**

With the case of Domestic Infrastructure, which divided into two factors, each factor included a number of items, which set to represent the factors included in this study's theoretical framework. The results of running this factor analysis are shown in Table 6.19.

Table 6-19: KMO and Bartlett's Test

Kaiser-Meyer-Olkin Measure of Sampling Adequacy		.642
Bartlett's Test of Sphericity	Approx. Chi-Square	79.629
	Df	10
	Sig	.000

The KMO value is .642, which is above the minimum requirement of 0.5 and is regarded as an average value according to Field (2013). Moreover, Bartlett's Test of Sphericity is highly significant (Sig. = .000). Thus, factor analysis is appropriate for this study's data.
Table 6.20 provides the results of total variance between the two factors which have eigenvalues of more than one, explaining 71.791% of that variance between the five items. It is noticeable that the first factor explains 47.453% of total variance while the second factor explains 24.339% of total variance.

Table 6-20: Total Variance Explained by Each Factor

Component	Initial Eigenvalues		
	Total	% of Variance	Cumulative %
1	2.373	47.453	47.453
2	1.217	24.339	71.791
3	.640	12.799	84.591
4	.466	9.311	93.902
5	.305	6.098	100.000

The PCA results show that the set of two factors represents one dimension for each factor as followed: domestic infrastructure and R&D and training system. The ranges of factor loading are 0.725-0.866 and 0.901-0.925 respectively (see Table 6.21).

Table 6-21: Component Matrix

Items	**Component**	
	1	2
Quality of telecommunication services	.789	
Quality of transportation services system	.725	
Quality of electricity supplies services	.866	
R&D and training system		.901
Cost of training		.925

- **Financial and Legal Institutions and FDI in Libya**

In the case of the Financial and Legal Institutions factor, analysis was used to see whether the original items combine in any patterns to make new factors, and if any, to check their consistency with the factors included in the research theoretical framework. In order to use factor analysis, its assumptions were tested.

Table 6-22: KMO and Bartlett's Test

Kaiser-Meyer-Olkin Measure of Sampling Adequacy		.579
Bartlett's Test of Sphericity	Approx. Chi-Square	121.654
	Df	10
	Sig	.000

The result in Table 6.22 indicated that the KMO value here is above the minimum requirement of .5, and is therefore regarded as an average value. Moreover, the Bartlett's Test of Sphericity assumption is met as well and is highly significant (Sig. = .000), suggesting that factor analysis is appropriate for this data.

Table 6-23: Total Variance Explained by Each Factor

Component	Initial Eigenvalues		
	Total	% of Variance	Cumulative %
1	2.369	47.390	47.390
2	1.576	31.525	78.915
3	.522	10.450	89.365
4	.332	6.639	96.004
5	.200	3.996	100.000

Table 6.23 shows the PCA results which indicated two factors (financial factor and legal factor), having eigenvalues of more than one, and explaining about 78.915% of the total explaining 31.525%.

Table 6-24: Component Matrix

Items	**Component**	
	1	2
Access to local source of fund	.897	
Accounting and audit system	.870	
Availability of financial system	.823	
Length of time of legal provisions		.892
Labour legislation		.927

Table 6.24 presents the PCA results indicating that the set of two factors represents one dimension for each factor as follows: (1) financial and (2) legal practice, the range of factor loading are 0.823-0.897 and 0.892-0.927, respectively.

After completing all of the above processes, the outcome of PCA with varimax rotation indicated that four of the seven dimensions (factors) were regrouped and then renamed while the other three dimensions remained in the same constructs, making 11 factors or constructs all together which were as follows:

1. Economic Conditions
2. Market Conditions
3. Tax Exemptions
4. Government Regulations and Red Tape
5. Availability of and Wages for Skilled Labor
6. Availability of and Wages for Semi-Skilled Labor
7. Natural Resources
8. Domestic Infrastructure
9. R& D and Training System
10. Financial Accessibility
11. Legal Practice.

6.3.2 Validity

The credibility of the research instrument which is used to collect data is significant issue. In this context, Black (1999) distinguishes between two types of validity. The first is content validity which is based on the assumption that there is a clear specification of the issue being studied and that the instrument used in the research (i.e. the questionnaire in this instance) has the potential to provide adequate coverage of the research questions guiding the study. The second is the construct validity which is concerned with how well a measure represents a concept i.e. if the numerical representation in a quantitative scale used in the questionnaire has the potential to accurately represent levels of that concept (Knight, 2002).

In this study, there was careful scrutiny of existing literature and of measures used in previous research. In addition, some in-depth interviews with top executives of FDIs and scholars were conducted to evaluate the instrument to be used, and a pilot test of the questionnaire was carried out to ensure that only relevant items which fitted with the investment issues for the case of Libya were included.

6.4 Descriptive Statistics of Respondent Data

The purpose of this section is to describe the characteristics of the respondents of the fully foreign-owned and joint venture companies that participated in this study. This descriptive statistical analysis consists of general information about the respondents, the responding companies, respondents' perceptions of the factors influencing the decision to invest in Libya, and the use of local suppliers.

6.4.1 Characteristics of Respondent Demographics

The first section in the questionnaire (Section A) was intended to gather general information about participants. Table 6.25 presents the characteristics of the questionnaire respondents, including nationality, educational level, position in the company and professional experience, using data extracted from the 63 usable questionnaires used for the statistical test. These data are presented in detail in the following sections.

6.4.1.1 Respondents' Nationality

As shown in Table 6.25, the majority of respondents (33.3%) were of Libyan nationality, with Tunisian responses coming second in the ranking (15.9%) and British responses third (7.9%). Italian and Maltese responses received joint fourth ranking with 6.3% for each nationality while French responses were in fifth position with 4.8%. The remaining 16 firms were composed of other nationalities from the following regions and countries: MENA (Bahrain, Egypt, Morocco, Qatar, and UAE); Europe (Austria, Belgium, Cyprus, German, Greece, Luxembourg, Netherlands, Portugal, Spain, and Switzerland) and North America (Canada and USA).

Table 6-25: Summary of Questionnaire Respondent Profiles

Characteristics of Respondent	Frequency	Percentage
Nationality of Respondent		
▪ Libyan	21	33.3
▪ Tunisian	10	15.9
▪ British	5	7.9
▪ Italian	4	6.3
▪ Maltese	4	6.3
▪ French	3	4.8
▪ Others	16	25.4
Job Title of Respondent		
▪ Accounting	8	12.7
▪ Business Management	20	31.7
▪ Finance	15	23.8
▪ Economy	6	9.5
▪ Others	14	22.2
Educational Level		
▪ Diploma	4	6.3
▪ Bachelor's Degree	45	71.4
▪ Postgraduate	14	22.3
Position of Respondent		
▪ Board Chairman	17	27
▪ General Director	24	38.1
▪ Deputy Director	23	34.9
Number of Years Working in the Firm		
▪ Less than two years	2	3.2
▪ Two–Five years	35	55.6
▪ More than five years	26	41.3

6.4.1.2 Job Title and Educational Level of Respondents

Table 6.25 shows that according to their job title, most of the respondents (77.7%) work in the areas of accounting, business management, finance or economy, occupying senior positions in their company (see following section). They are well-educated, with 71.4% holding a bachelor's degree and nearly a quarter (22.2%) of the respondents having postgraduate qualifications (either Masters or PhDs). All of the respondents hold some qualification, the remaining 6.3% holding a diploma.

6.4.1.3 Position of Respondents

The questionnaires addressing FDI were distributed to top management of the companies by position, in order to ensure the accuracy of their responses, an adequate level of awareness of relevant issues, and an expert knowledge of company policies. Over a quarter (27%) of the total usable questionnaires were completed by the Board Chairmen as members of the first-tier management that were the target of this survey. Some 38.1% questionnaires were completed by General Directors who were second-tier executives with good knowledge of company policies. Another 34.9% were completed by Deputy Directors.

6.4.1.4 Experience with Current Company

As shown in Table 6.25 more than half (55%) of the 63 respondents had worked with their current companies for a period of between two and five years while 41.3% had more than five years' experience and 3.2% had two years' experience. This indicated that the respondents have a medium level of experience. This is not surprising given that FDI is relatively new in Libya.

6.4.2 Characteristics of Participant Companies

Since this study deals with the economic activities of foreign companies based in Libya, it is appropriate to highlight the characteristics of the companies involved. This sub-section aims to providing a summary of the information related to the characteristics of the foreign companies that participated in this study, including company location, nationality, length of time the company has been operational in Libya, sector of activity, and company ownership.

6.4.2.1 Company Location in Libya

Table 6.26 shows that more than half of the companies (57.1%) are located in the Libyan capital, Tripoli, followed by Al Gfara (15.9%), Benghazi (12.7%), Misratah (3.2%) and other cities (11.1%).

6.4.2.2 Nationality of Foreign Companies

The profile of the major foreign partner for the respondent companies was as follows: Western (European and North American), 57.1%; MENA 36.5%; and others, 6.3%. The Western group consisted of Austria, Belgium, Canada, Cyprus**,** France, German, Greece, Italy, Luxembourg, Malta, Netherlands, Portugal, Spain, Switzerland, the United Kingdom, and USA, while MENA included Bahrain, Egypt, Iran, Morocco, Qatar, Tunisia, Turkey, and UAE. Others countries mentioned were China and South Korea.

Table 6-26: Summary of Company Characteristics for Questionnaire Responses

Characteristics of Respondent	Frequency	Percentage
Company Location in Libya		
▪ Tripoli	36	57.1
▪ Al Gfara	10	15.9
▪ Benghazi	8	12.7
▪ Misratah	2	3.2
▪ Other	7	11.1
Nationality of Foreign Partner		
▪ Western	36	57.1
▪ MENA	23	36.5
▪ Other	4	6.3
Company presence in Libya		
▪ Less than two years	2	3.2
▪ Two - five years	26	41.6
▪ More than five years	35	55.6
Sector of Activity		
▪ Manufacturing	25	39.7
▪ Building Materials Industry	10	15.9
▪ Other Services	10	15.9
▪ Health and Medical Service	9	14.3
▪ Oil and Gas Services	6	9.5
▪ Tourist Service	2	3.2
▪ Banking, Insurance and Financial Services	1	1.6
Company Ownership		
▪ Fully Foreign-Owned	23	36.5
▪ Joint-Venture	40	63.5

6.4.2.3 Length of Company Presence in Libya

As mentioned earlier in Chapter Three, in general the foreign companies have limited business experience in Libya as significant FDI inflows only began after 2003. In terms of the length of time the company has been operational in Libya, for 3.2% this period of time was less than two years, for 41.6% it was more than two year but less than five, but over half the companies surveyed (55.6%) had been operating there for over five years.

6.4.2.4 Sector of Activity

With regard to the specific sector of activity in which the company operates, as Table 6.26 shows, questionnaire results indicated that among the participating companies some 39.7% were in manufacturing business and 15.9% in the building materials industry. With regard to the service sector, 14.3% were in health and medical services, 9.5% were in oil services, and 15.9% were in other services (non-specified). Only 1.6% was in banking sector.

6.4.2.5 Company Ownership

Question 10 of the questionnaire was intended to provide information about the entry of companies and whether this took the form of a fully foreign-owned company or a joint venture. Table 6.26 highlights that most of the investor companies (63.5%) were joint-venture while 36.5% were wholly foreign-owned.

Table 6.27 summarizes the characteristics of FDI companies. The first characteristic relates to the nationality of the company. Two main groupings have been established: MENA (36.5%) or Western (57.1%), as these two sides of the world are different in several aspects, including culture, lifestyle and working patterns, attitudes, etc.

Table 6-27: Summary of Questionnaire Characteristics of FDI Companies

	Group One			Group Two		
Characteristic	**Description**	**No.**	**%**	**Description**	**No.**	**%**
Nationality	MENA	23	36.5	Western	36	57.1
Industry	Manufacturing	35	55.5	Services	28	44.4
Ownership	Fully Foreign-owned	23	36.5	Joint-Venture	40	63.5

The second categorization related to company ownership which was considered to be either fully foreign-owned (36.5%) or joint- venture (63.5%). The study aimed to investigate if there were any significant differences between fully foreign-owned and joint-venture companies in term of locational determinants. The third characteristic was linked to sector of activity: manufacturing (57.1%) or services (42.9%), since these are the major kinds of business incorporation.

6.4.3 Perceptions of Location Factors

The second part of the questionnaire was designed to investigate the locational determinant factors of FDI that were discussed in the previous chapter. These factors are: Economic Situation; Market Conditions; Investment Policy and government regulations, Domestic Infrastructure, Human Capital, Natural Resources, and Financial and Legal Institutions. Each of these dimensions (factors) has been measured by a group of items that is built on a five-point Likert scale (1= highly discourage no affect, 2= slightly discourage, 3= no affect, 4= slightly encourage, 5= highly encourage). The participants were asked to indicate to what degree each factor mentioned in the statement given would encourage/discourage their investment.

Table 6-28: **Descriptive Statistics for Location Factors**

FDI Determinants Factors	No. of Items	Mean	**No.**	St. D
Economic Conditions	5	**4.31**	63	.59537
Market Conditions	4	**3.57**	63	.72237
Tax Exemptions	5	**4.27**	63	.47534
Government Regulation and Red Tape	4	2.45	63	.75325
Availability and Wages of Skilled Labor	3	**3.83**	63	.33044
Availability and Wages of Semi-Skilled Labor	2	**3.43**	63	.84478
Availability of Natural Resources	2	**3.54**	63	.74217
Domestic Infrastructure	3	2.42	63	.48651
R&D and Training Systems	2	2.30	63	.84022
Financial Accessibility	3	2.97	63	.79675
Legal Practice	2	1.97	63	.58801

As presented in Table 6.28, the results from the overall sample indicated that the mean and standard deviation of items used to measure Economic Situation, Market Conditions, Tax Exemptions, Human Capital and Natural Resources were all above average of 3, while the items that represent the Government Regulation and Red Tape, Domestic Infrastructure, R&D and Training Systems and Financial and Legal Institutions items were between the average.

6.4.4 Foreign Companies and Dependency on Local Suppliers

The involvement of local suppliers is required for foreign companies, but these suppliers must be of the appropriate quality and quantity. Therefore, two items were incorporated to investigate the opinion of the representatives in relation to the dependence of their companies on local suppliers to provide related inputs and services, as well as highlighting any problems involved. Thus Question 16 reveals the degree to which international companies depend on local suppliers, while Question 17 investigates the most significant difficulties involved, particularly in relation to the availability, quality and cost of these services in the local market. It should be noted that as Question 17 was a multiple choice item, and while the first option referred to "No significant difficulties", a fifth option was open, allowing participants to mention any other difficulties they had experienced.

Nearly half of the international companies operating in Libya were not dependent on local suppliers, while about quarter of these companies were partly dependent on local suppliers but a number of difficulties were mentioned in connection to the use of local suppliers. The major problems identified were scarcity and poor quality, in addition to the high cost of these inputs in some cases.

6.4.4.1 Dependency of Foreign Companies on Local Suppliers

The findings in Table 6.29 reveal that about 31 companies (49.2%) of the respondents stated that their companies do not rely at all on local suppliers to provide related inputs,

while 17 out of 63 companies (27.0%) were dependent on local suppliers and 15 companies were partly dependent on them. This result indicates that nearly half of the foreign companies do not depend on local suppliers to provide related inputs while over a quarter of the foreign companies are partly dependent on local suppliers for the same purpose.

Table 6-29: Dependency of Foreign Companies on Local Suppliers

	Frequency	%	Valid %	Cumulative %
Mainly dependent	17	27.0	27.0	27.0
Partly dependent	15	23.8	23.8	23.8
Mainly not dependent	31	49.2	49.2	49.2
TOTAL	**63**	**100.0**	**100.0**	**100.0**

6.4.4.2 Perceptions of Difficulties regarding Local Suppliers

Table 6.30 shows that 42.8% of the total number of representatives highlights that there are limited materials suppliers in the local market. These findings also indicate that 28.6% of all participants refer to poor quality of materials and 6.3% refer to the high cost of these. Some 17.4% refer to other problems such as delays. Only 4.8% indicated that they were satisfied.

Table 6-30: Perceptions of Difficulties regarding Local Suppliers

	Frequency	%	Valid %	Cumulative %
None	3	4.8	4.8	4.8
Limited supply of materials	27	42.8	42.8	65.1
Inadequate quality	18	28.6	28.6	93.7
Materials too costly	4	6.3	6.3	100.0
Others (delays)	11	17.4	17.4	
TOTAL	**63**	**100.0**	**100.0**	

6.4.4.3 Perceptions of production strategy

The company's strategy refers to whether they produce for/serve the local market or are export-oriented. In this regards, participants were asking about their companies targeting local market or to exports.

Table 6-31: Production Strategy

	Frequency	%	Valid %	Cumulative %
Serve Local Market	57	90.5	90.5	90.5
Serve both Local and Export Market	6	9.5	9.5	100.0
TOTAL	**63**	**100.0**	**100.0**	

The findings in Table 6.31 highlight that the majority of respondents said that their companies were producing for/servicing the local economy. In this regard 90.5% and 9.5% of the participants were making considerable or significant efforts respectively to target the local market.

6.5 Hypotheses testing of FDI characteristics

In this research, in addition to identifying the main locational determinant factors that influenced foreign investor decisions to invest in Libya, and in order to achieve the second objective of the study, the characteristics of FDI were introduced, to test if there is a difference between each characteristic of FDI regarding locational determinants, and if so, how and why? The characteristics were used as independent variables of the equation whilst the eleven locational factors of FDI were used as dependent variables of the equation. The three main characteristics considered in this study were sector of activity, entry mode (i.e. ownership whether full foreign owned or joint venture), and company nationality (western or MENA firm). The quantitative approach involves the MANOVA test of variance as the statistical tool employed to test the research hypotheses and to investigate the determinants of FDI based on the characteristics of FDI. MANOVA was performed to test whether the eleven factors used in this study varied among the firms

with sector of activity (manufacturing or services), entry mode (i.e. ownership whether full foreign owned or joint venture), and company nationality (western or MENA firm).

This section aims to examine the three main groups of FDI characteristics (see Table 5.7 in Chapter Five) using three hypotheses. In order to test each hypothesis, the MANOVA test was employed to illustrate the differences between each group regarding dependent variables; the MANOVA results were introduced for each group (independent variables) to clarify in which ways dependent variables differ. The three hypotheses are:

H1: Factors which encourage/discourage FDI in Libya differ in relation to ownership depending on whether they are Fully Foreign-Owned or Joint-Venture companies.

H2: Factors which encourage/discourage FDI in Libya differ in relation to the company's country of origin i.e. whether this is Western or MENA.

H3: Factors which encourage/discourage FDI in Libya differ in relation to the company type of sector whether this is manufacturing or services.

Since testing of the hypotheses of this study investigates mean differences among groups based on the combination of several dependent variables, therefore the multivariate statistical tests such as MANOVA which deals with Multivariate Analysis of Variance, and MANCOVA for Multivariate Analysis of Covariance, are theoretically best suited for this research. They have a number of advantages over univariate statistical tests such as ANOVA (Analysis of Variance) or ANCOVA (Analysis of Covariance), which are used to test mean difference among groups on a single dependent variable. Firstly, when there are several dependent variables, running a multivariate statistical test is more effective than a series of univariates to help protect against inflated Type I error due to multiple tests of (likely) correlated dependent variables. Secondly, multivariate statistics help the researcher to improve the chances of discovering results from different dependent variables and their interactions in other words, MANOVE takes into account the correlation among the dependent variable (location determinants of FDI), while univariate tests ignore this information; and none of the individual ANOVAs may

produce a significant main effect on a dependent variable, but in combination they might, which suggests that the variables are more meaningful taken together than considered separately (Steven,2002. P. 174; Tabachnick and Fidell 2007 and Field, 2013. P. 624).

This research used MANOVA instead of MANCOVA because in this study independent variables took the form of categorical variables, whereas for MANCOVA independent variables need to be continuous or interval scale variables which are added as covariates. However, before performing MANOVA, it is essential to test for underlying assumptions concerning the data and methodology matched. Those processes are described in detail in the following sections.

Before running MANOVA, there is a number of pre-requirements, which include examinations of multivariate normality, equality of the covariance matrix, the sensitivity of outliers must be performed (Stevens, 2002; Tabachnick and Fidell, 2007; Hair *et al.* 2010, p361, and Field, 2013).

I. Multivariate Normality

Checking the normality distribution is a prerequisite before running MANOVA and refers to the shape of data distribution for an individual matrix variable and its correspondence to the normal distribution; multivariate normality assumes that individual variables are normally distributed. In practical terms, the normality of data distribution is assessed by using histograms and normal probability plots. The histogram is the simplest diagnostic for the set of predictor variables, providing a visual check for a distribution approximating normal distribution (Hair *et al.,* 2010).

Hair *et al.* (2010, p.363) suggest that in order to verify the existence of distributional normality, the benchmark for testing should be in moderately sized groups of 30 cases or more. Therefore, the sample size of 63 in the current study was considered to be acceptable. In this study each variable was examined for distributional normality by conducting scatter plot and histogram in order to confirm the acceptance normality. The

visual investigation, distributions for each factor showed normality distributed. Therefore, the assumptions of MANOVA were met (Appendix C).

II. Sensitivity of Outliers

MANOVA is especially sensitive to outliers and their impact on Type I errors. An outlier is a case with an extreme value on one variable. This type of observation that appears to deviate markedly from other observations in the sample can be considered to be problematic because it is not representative of the population, runs counter to the objectives of the analysis, and can seriously distort statistical data (Hair *et al.,* 2010, p.363; Tabachnick and Fidell 2007, p.72).

Theoretically, outliers are either eliminated from the cases in the analysis, or the data is transformed to reduce their impact, or the score is changed by recording these values as missing and replacing them using one of the following three options. The first is to change the score by the next highest score plus one in the dataset. The second option is to convert back from a z-score of 3.29 by calculating the mean and standard deviation of the data, then comparing all the data with a z-score of 3.29. Any examples which are greater than this can be considered to be outliers and can be dealt with by adding three times the standard deviation to the mean, and replacing the outliers with that score. The third option is to replace the outliers by the mean plus a figure which is twice the standard deviation, instead of three times as in the above method (Field, 2013).

In this study, outliers were investigated in each group separately in the data screening process by using a boxplot method. Only one case of outliers was found in this study and considered not problematic to running statistical tests (Field, 2009, p. 153). Therefore, the second assumption of MANOVA was satisfied (Appendix D).

III. Equality of Covariance Matrixes

The other assumption of MANOVA is the equivalence of covariance matrix across all the groups. The homogeneity of variances assumes that the dependent variable exhibits equal levels of variance across the range of predictor variables (Hair *et al.,* 2010). Tabachnick

and Fidell (2007, p.85) clarify that "*the homogeneity is related to the assumption of normality because when the assumption of multivariate normality is met, the relationships between variables are homogeneity*".

MANOVA requires a test of equivalence of covariance matrix of the dependent variables. In practical terms, a violation of this assumption has a minimal impact if the groups are of approximately equal size. To provide the test of equality of covariance matrix, SPSS uses Box's M Test of covariance matrices, and if the sig. value is larger than 0.01, the assumption has not been violated (Hair *et al.,* 2010). The covariance matrix outcomes of all subgroups showed different levels of insignificance, indicating that there was an equality of covariance matrix. Therefore; the assumptions of MANOVA were met.

IV. Linearity

This assumption refers to the presence of a straight-line relationship between each pair of dependent variables. The linearity can be assessed in a number of ways; one of the most common tests is scatterplots, used to generate a matrix of scatterplots between each pair of variables separately for each group. In the current study, each variable was examined for distributional normality by creating scatterplots and histograms in order to confirm the assumption of the linearity (Appendix E). The visual investigation and distributions for each factor showed a straight-line relationship between each pair of dependent variables. Therefore, the linearity assumptions of MANOVA were met (Field, 2013).

V. Preforming MANOVA test

The first step in the MANOVA test is to run Box's M test of equality of covariance matrices, which was performed between the groups in order to test the MANOVA assumption that the observed covariance matrices of the dependent variables are equal across groups. The Box's M test shows the assumption of equality of covariance matrices, which examine whether the data used violates the assumption of homogeneity of variance covariance matrices. If the value of Sig is larger than .05, that means the covariance matrices are roughly equal as assumed (Field, 2013 p. 647).

The next step in a MANOVA test shows the equality of error variances for all eleven FDI locational determinants, based on a series of Levene's tests. If the results show that all the dependent variables are statistically non-significant (p value <.05), this indicates that the variance of the dependent variable is equal across the groups. In other words, the homogeneity of variances assumption is considered to have been satisfied (Tabachnick and Fidell, 2013).

While the set of multivariate tests indicate whether there are statistically significant differences among the groups on linear combinations of dependent variables, MANOVA provides a number of statistics to choose from (Pillai's Trace; Wilks' Lambda; Hotelling's Trace; and Roy's Largest Root). There are only two levels where an effect on all of the tests will be identical. Wilk's Lambda, Hotelling's Trace and Pillai's trace all pool the variance from all the dimensions to create the test statistic. Roy's Largest Root only uses the variance from the dimension that separates the groups the most (the largest "root" or difference). As the sample size used in the analysis increases, the values produced by all the above tests become similar (Tabachnick and Fidell, 2007; Hair *et al.* 2010 and Field, 2013). Field (2013) recommend Wilks' Lambda for general use because it is the easiest to understand and therefore the most commonly used measure. Wilks' Lambda provides a statistic which can vary between 0 and 1 and which indicates whether the means of groups differ. A value of 1 indicates the groups have the same mean.

The MANOVA test provides the results between subject group's effects to investigate further in relation to each of eleven dependent variables. Whether each group differs on all of the dependent factors or just some of them, as shown in Tables 6.34, 6.37 and 6.40, indicate that for the eleven factors, there were some dependent factors which were significantly different between each pair from the three groups of ownership, sector and nationality. The P values of some of the dependent variables for each pair of groups were <0.05 (Field, 2013), thus the results provide evidence of acceptance of the three hypothesis, which represent the three groups.

H:1 **Factors which encourage/discourage FDI in Libya differ in relation to ownership depending on whether they are Fully Foreign-Owned or Joint-Venture companies.**

This group was divided into two subgroups by ownership, i.e. fully foreign-owned and joint-venture companies, in order to test whether the eleven locational determinants used in this study varied among the two subgroups. As can be seen in Table 6.32 the Box's M test value of 114.852 was associated with a p value of .028, which was interpreted as non-significant based on guidelines by Hair *et al* (2010, p.378) (i.e. p<.001). Thus, the covariance matrices between the groups were assumed to be equal for the purposes of the MANOVA.

Table 6-32: **Box's M Test of Equality of Covariance Matrices**

Box's M	114.852
F	1.361
Df1	66
Df2	6901.823
Sig.	.028

A series of Levene's tests was used to test the homogeneity of variance assumptions for all eleven FDI locational determinants. The result shows that Levene's test for all dependent variables is statistically non- significant (p value <.05), indicating that the variance of the dependent variable is equal across the groups (see Appendix E). Thus, the homogeneity of variance assumption was considered to have been satisfied.

Table 6.33 shows that there is a significant difference among the two subgroups (p value level of .000), indicating that these two groups viewed the eleven locational factors differently.

Table 6-33: Multivariate tests

	Effect	Value	**F**	Hypothesis df	Error df	**Sig.**	Partial Eta Squared	Observed Power
Company ownership	Pillai's Trace	.673	**8.342**	11.000	51.000	**.000**	.646	1.000
	Wilks' Lambda	.327	**8.564**	11.000	51.000	**.000**	.683	1.000
	Hotelling's Trace	2.060	**9.549**	11.000	51.000	**.000**	.673	1.000
	Roy's Largest Root	2.060	**9.549**	11.000	51.000	**.000**	.673	1.000

The results of the one-way MANOVA revealed a significant multivariate difference between ownership subgroups: Wilks' Lambda =.327, F (11, 51.00) = 9.549, p <. 001, Partial Eta Squared = .673. The power to detect the effect was 1.00. Thus Hypothesis H1**:** Factors which encourage/discourage FDI in Libya differ in relation to ownership depending on whether they are Fully Foreign-Owned or a Joint-Venture company was confirmed.

Finally, the individual mean difference comparisons across both levels of company ownership and all eleven locational determinants factors were examined in order to provide more disaggregated evidence on the nature of how the ownership of the two company types varied across the eleven factors. Table 6.34 presents a comparison of FDI preferences between those companies which have foreigners as their major shareholder (fully foreign-owned companies) and those which are shared between local and foreign partners (joint-venture companies). Only one encourage factor was viewed in statistically significantly different by these two subgroups. This was: market conditions with p levels of.000. Market Conditions was considered to be an encouraging factor for both subgroups, but seen as more favourable for joint venture-owned FDI. On the other hand, availability of domestic infrastructure, domestic spending on R&D and Training Systems, and government regulation and red tape affected both subgroups with significant negative signs, indicated that these factors were viewed as more of an obstacle to wholly foreign-owned FDI.

Table 6-34: MANOVA Results for Company Ownership

FDI Determinants Factors	p=	Fully foreign-owned		Joint-Venture	
		Mean	Rank	Mean	Rank
Economic Conditions	.344	4.41	1	4.26	1
Market Conditions	.000	**3.09***	6	3.86	3
Tax Exemptions	.412	4.34	2	4.24	2
Government Regulation and Red Tape	.000	**1.95***	9	2.74	8
Domestic Infrastructure	.020	**2.22**	8	2.51	10
Availability & Wages of Skilled Labor	.995	3.84	3	3.84	4
Availability & Wages of semi-skilled Labor	.450	3.54	4	3.37	6
R&D & Training Systems	.013	**1.91**	10	2.27	9
Natural Resources	.232	3. 39	5	3.63	5
Financial Accessibility	.139	2.84	7	3.15	7
Legal Practice	.435	1.89	11	2.01	11

* The mean difference is significant at the .05 level.

Economic Conditions and Tax Exemptions were ranked as the top two factors for both groups. Market Conditions was ranked third for joint-venture companies, while the equivalent factor for fully foreign-owned companies was Availability and Wages of Skilled Labour. Availability and Wages of semi-skilled Labour was ranked fourth by fully foreign-owned companies but ranked sixth by joint-ventures. Since the latter had much better access to unskilled labour than their fully foreign-owned counterparts, they did not pay much attention to this factor. Foreign investors, on the other hand, were much more concerned about Government Regulation and Red Tape, i.e. the leakage of profits to government agencies, and transparency, together with Legal Practice, i.e. the opportunistic behaviour of their competitors.

H:2 Factors which encourage/discourage FDI in Libya differ in relation to the company's country of origin i.e. whether this is Western or MENA.

This group was divided into two subgroups by national origin i.e. Western or MENA FDI, in order to test whether the eleven locational determinants used in this study varied among the two groups.

Table 6-35: Box's M Test of Equality of Covariance Matrices

Box's M	123.585
F	1.453
Df1	66
Df2	7096.277
Sig.	.010

Prior to conducting the MANOVA, Box's M Test of equality of covariance matrices was performed between the groups in order to test the MANOVA assumption that the observed covariance matrices of the dependent variables are equal across groups. As can be seen in Table 6.35 a Box's M Test value of 123.585 was associated with a p value of .010, which was interpreted as non-significant based on Hair *et al.*'s (2010, p.378) guideline ($p<.001$). Thus, the covariance matrices between the groups were assumed to be equal for the purposes of the MANOVA.

The homogeneity of variance assumption was tested for all eleven FDI locational determinants, based on a series of Levene's tests. The result shows that Levene's test for all dependent variables is statistically non- significant (p value <.05), indicating that the variance of the dependent variable is equal across the groups (see Appendix E). Thus, the homogeneity of variance assumption was considered to have been satisfied.

Table 6.36 shows that there is a significant difference among the two subgroups (p value of .000), indicating that these two groups viewed the eleven locational factors differently.

Table 6-36: Multivariate tests

	Effect	Value	**F**	Hypothesis df	Error df	**Sig.**	Partial Eta Squared	Observed Power
Nationality of company	Pillai's Trace	.837	3.335	22.000	102.000	.000	.418	1.000
	Wilks' Lambda	.302	3.732	22.000	100.000	.000	.451	1.000
	Hotelling's Trace	1.857	4.137	22.000	98.000	.000	.482	1.000
	Roy's Largest Root	1.564	7.252	11.000	51.000	.000	.610	1.000

Results of the one-way MANOVA revealed a significant multivariate main effect for nationality group: Wilks' Lambda =.302, F (22, 100.00) = 3.73, p <. 001, Partial Eta Squared = .451. Power to detect the effect was 1.00. Thus Hypothesis H2**:** Factors which encourage/discourage FDI in Libya differ in relation to the company's country of origin i.e. whether this is Western or MENA was confirmed.

Finally, the individual mean difference comparisons across both levels of company ownership and all eleven locational determinants factors were examined in order to provide more disaggregated evidence on the nature of how the nationality of the two company types varied across the eleven factors. As can be seen in Table 6.37, the results revealed that, between these two groups of nationality, four incentives were considered in significantly statistically different ways. These were: economic conditions (p value level of 0.000), tax exemptions (p value level of 0.000), financial accessibility (p value level of 0.008) and availability natural resources (p value level of 0.004). For all those factors, the group including industrialised countries produced higher scores than MENA countries.

Table 6-37: MANOVA Result of Companies Country of Origin

FDI Determinants Factor	P =	MENA		Western	
		Mean	Rank	Mean	Rank
Economic Conditions	.000	**3.85***	2	4.59	1
Market Conditions	.027	**3.82**	3	3.39	6
Tax Exemptions	.000	**3.86***	1	4.52	2
Government Regulation and Red Tape	.695	2.51	8	2.42	8
Domestic Infrastructure	.501	2.42	9	2.34	9
Availability & Wages of Skilled Labour	.097	**3.73**	4	3.88	3
Availability & Wages of Unskilled Labour	.788	3.48	5	3.41	5
R&D & Training Systems	.513	2.32	10	2.26	10
Natural Resources	.004	3.18*	6	3.48	4
Financial Accessibility	.008	**3.16***	7	2.90	7
Legal Practice	.834	1.93	11	1.90	11

* The mean difference is significant at the .05 level.
** The mean difference is significant at the .10 level.

In addition, Western companies gave the first rank to the economic situation factor (mean 4.59), while MENA viewed this factor as the second (mean 3.85). This was because Western FDI chose Libya because of the stability of the economic situation there, while MENA investors, such as Tunisia or Egypt, can secure raw materials from their home country, which is not costly due to near distance to Libya.

H:3 Factors which encourage/discourage FDI in Libya differ in relation to the company sector of activity whether this is manufacturing or services.

This group was divided into two subgroups by sector of activity i.e. manufacturing industry and services, in order to test whether the eleven locational determinants used in this study varied among the two groups.

Table 6-38: Box's M Test of Equality of Covariance Matrices

Box's M	136.745
F	1.664
Df1	66
Df2	10699.877
Sig.	.071

Prior to conducting the MANOVA, Box's M Test of equality of covariance matrices was performed between the groups in order to test the MANOVA assumption that the observed covariance matrices of the dependent variables are equal across groups. As can be seen in Table 6.38 the Box's M Test value of 136.745 was associated with a p value of .071, which was interpreted as non-significant based on Hair *et al.* (2010, p.378) guidelines (p<.001). Thus, the covariance matrices between the groups were assumed to be equal for the purposes of the MANOVA.

The homogeneity of variance assumption was tested for all eleven FDI locational determinants, based on a series of Levene's tests. The outcome shows that the all dependent variables was statistically non- significant (p value <.05), indicating that the variance of the dependent variable is equal across groups (see Appendix E). Thus the homogeneity of variance assumption was considered to have been satisfied.

Table 6.39 shows that there is a significant difference among the two groups for the eleven locational determinants factors.

Table 6-39: Multivariate tests

	Effect	Value	**F**	Hypothesis df	Error df	**Sig.**	Partial Eta Squared	Observed Power
Sector Type	Pillai's Trace	.926	57.812	11.000	51.000	.000	.926	1.000
	Wilks' Lambda	.074	57.812	11.000	51.000	.000	.926	1.000
	Hotelling's Trace	12.469	57.812	11.000	51.000	.000	.926	1.000
	Roy's Largest Root	12.469	57.812	11.000	51.000	.000	.926	1.000

Results of MANOVA test revealed a significant multivariate main effect for sectorial group, Wilks' Lambda =.074, F (11, 51.00) = 57.81, P <. 001, Partial Eta Squared = .926. Power to detect the effect was 1.00. Thus Hypothesis H3**:** Factors which encourage/discourage FDI inflow in Libya differ in relation to the company sector of activity i.e. manufacturing or services was confirmed.

Finally, the individual mean difference comparisons across all both groups of sector activity and all eleven locational determinants factors were examined in order to provide more disaggregated evidence regarding how the nature of these two sectors varied across the eleven factors. As can be seen in Table 6.40, the results revealed that, between these two subgroups of sectors, five encouraging factors out of eleven were statistically significantly different (at p value less than 0.05 levels). These were market conditions, availability and wages of semi-skilled Labor, availability of natural resources, and financial accessibility. Across all those factors, manufacturing companies produced higher scores than their service industry counterparts. The results show an insignificant difference in the means of four other locational determinants of FDI (economic conditions, tax exemptions, availability and wages of skilled labor, and legal practice) between the manufacturing and the services sector. In terms of discouraging factor it's appears that three factor (government regulation, domestic infrastructure and training system in the country), were statistically negative different between these two groups.

Table 6-40: MANOVA Results for Sector of Activity

FDI Determinants Factor	p=	Manufacturing		Services	
		Mean	Rank	Mean	Rank
Economic Conditions	.060	**4.44****	1	4.15	2
Market Conditions	.000	**4.15***	3	2.86	5
Tax Exemptions	.106	4.36	2	4.17	1
Government Regulation and Red Tape	.000	**2.83***	8	1.97	9
Domestic Infrastructure	.000	**2.68***	9	2.05	8
Availability & Wages of Skilled Labour	.271	3.88	6	3.78	3
Availability & Wages of semi-skilled Labour	.000	**4.00***	5	2.73	6
R&D & Training Systems	.000	**2.36**	10	1.85	11
Natural Resources	.000	**4.03***	4	2.93	4
Financial Accessibility	.000	**3.66***	7	2.26	7
Legal Practice	.046	**2.10**	11	1.88	10

* The mean difference is significant at the .05 level.
** The mean difference is significant at the .10 level.

6.6 Interview Data Descriptive Analysis

The main purpose of the in depth face- to face interview method in this study is to clarify and add more in-depth analysis and understanding of the Libyan locational factors and backward linkages of FDI that have been mentioned in the questionnaire findings. Samples of the interviews with representatives of fully foreign-owned and joint-venture companies, and senior officials from the Libyan government were selected to represent the supply and demand side of the equation which captures their respective views regarding FDI in the country.

As explained in Chapter Five, this study adopted content analysis to analyse the qualitative data collected from semi-structured interviews owing to the suitability of this technique for the nature of the research undertaken. This technique is widely used in Social Sciences studies due to its ability to reflect the reality of a phenomenon and derive meaningful information from texts. As Easterby-Smith *et al.* (2008) explain, content analysis is very useful, more appropriate and more aligned with a deductive approach as is the case with the present study, rather than with the inductive hypothesis-generating approach.

The process of content analysis begins with identifying key constructs, themes, outlines or categories based on the theoretical research model or on the research objectives the researcher seeks to explore. Based on this, and the findings from the survey, the key constructs that were used as the main categories in content analysis are related to:

- whether the interviewees believe that each of the locational factors (i.e. Economic Conditions, Market Conditions, Investment Policy, Human Capital, Natural Resources, Domestic Infrastructure, Financial and Legal Institutions) tends to encourage or discourage FDI in general terms,
- whether foreign companies have linkages with local companies in term to provide related inputs/services, and
- to what extent they use local and domestic suppliers, how they use them and why.

Therefore, their answers are analysed and presented in this order.

When analysing the interview data, factors were classified as those that encourage the investor's decisions to invest in Libya and those that impede it, highlighting the challenges and difficulties that face the foreign companies. The following sub-sections outline the descriptive findings from both interview groups.

6.6.1 Descriptive Results of Foreign Investor Interviews

The results from the interviews in table 4.41 shows that all the locational factors of FDI listed in the questionnaire were discussed by all 13 participants, but not all of them have mentioned all the factors together. Furthermore, the interviews revealed a new factor which can be classified as an advantage, namely, i.e. the proximity of Libya to the company's own home base.

When analysing the interview data, factors were classified into those that influence the foreign investor's decision positively and those that are seen as difficulties related to the Libyan context. The following tables present the results of the interviews and interview data is summarized here quantitatively, using frequencies and percentages.

Table 6-41: Interview results for most important locational factors of FDI

Locational Factors Encouraging FDI	Number of interviews =13	
	Number of mentions	%
Economic Conditions	12	92.3
Market Conditions	9	69.2
Tax Exemptions	11	84.6
Availability & Wages of Skilled Labour	10	76.9
Availability & Wages of semi-skilled Labour	4	30.8
Natural Resources	8	61.5
Proximity of Libya to Company's Home Base	8	61.5

Source: Data analysis results of interviews

From the results of the interviews, it clears that in the view of top management the most important factors were: Economic Conditions, Tax Exemptions, Availability and Wages of Skilled Labour, Market Conditions, Availability and Wages of semi-skilled Labour, and Natural Resources which confirmed the questionnaire findings. An additional factor which emerged was Geographical Location which equates to the proximity of the distance between the company's home country and Libya.

With regard to difficulties, the results of the interviews with the top management of the foreign companies in Libya show that the majority of the participants (some 84%) identified Legal Practice as the most discouraging factor, followed by Domestic Infrastructure, which was mentioned by 10 participants (76.9%). Government Regulation and Red Tape, R&D and Training Systems were also considered to be obstacles facing those wishing to invest in Libya. Also, seven (53.8) of the company's representatives were concerned about the Libyan security situation.

Table 6-42: Interview results for difficulties related to investment

Locational Factors Discouraging FDI	Number of interviews =13	
	Number of mentions	%
Government Regulation and Red Tape	9	69.2
Domestic Infrastructure	10	76.9
R&D and Training System	6	46.1
Financial Accessibility	6	46.1
Legal Practice	11	84.6
Internal Security	7	53.8

Source: Data analysis results of interviews

In terms of the backward linkages of foreign companies and their relation to domestic suppliers, the results of the interviews with the representatives of the foreign companies were differed slightly depending on the type of sector in which the company operated. Some nine of the interviewed company representatives (69%) were dependent on

domestic inputs. In terms of dependence on domestic suppliers, the results indicated that 11 of the 13 companies (84%) were not dependent on domestic suppliers, due to a number of difficulties. The major problems were identified as scarcity of domestic suppliers and poor quality of services by the domestic suppliers.

6.6.2 Interview Findings from Libyan Senior Government Officials

The main purpose of the questionnaire and the semi-structured interviews that used in this research were to establish the perceptions of investors regarding the Libyan business environment in relation to FDI, by investigating various variables, as the demand side of the equation. In order to ascertain the official view or the supply side, semi-structured interviews was conducted with senior officials from the Libyan government dealing with FDI issues in October 2012. The interviews were held with seven senior officials, three of whom were employed by the PIB, two from the Ministry of Economics and one each from the Ministry of Industry and the General Planning Council. The table 6.43 summarised the interviews results, referring to three main aspects.

Table 6-43: **Summary of Interview Results**

Issue	Coded Response
Evaluate the experience of FDI and assess the main factors that attract FDI to Libya.	The majority of participants approved that the economic reforms and the investment promoting policies that adopted by the government has enhancing the FDI inflows to the country. However, more efforts need to facilitate the difficulties and obstacles that disrupt the foreign capital and required careful examination, and identification of effective solutions. They also highlighted the need to promote the present strengths of the Libyan investment environment in order to attracting more FDI.
Challenges and difficulties facing the public authorities wishing to improve the business environment.	The Interviewees highlighted the key difficulties were instability of the political and administrative, the lack of the efficiency procedures, the absence of effective e-government-based services and nonexistence electronic services in the banking sector were also viewed as important issues. In addition, the network of the PIB within the government structure should be improved by giving it more power and autonomy to make investment decisions.
General strategy for improving the business environment.	The majority of the interviewees confirmed the absence of clear formal government strategy plane regarding to numerous aspects of foreign investment. However, the available general framework of this strategy provides by the government is the foreign investment Law, which aims to diversification of the economy through open all sectors apart from oil and gas for foreign investors, attracting modern technology into the country, encouraging partnerships between local and foreign investors, developing local products by training the local workforce. In addition, the law fixes the minimum capital required, and is open to investment from all nationalities. Interviewees suggested that the top priority is more effective formal strategy plane to meet the local market requirements of different economic activities, and dealing with the current shortcomings of economic development.

6.7 Summary

This chapter has presented a descriptive analysis of the data findings collected by 63 questionnaires and 20 interviews (used to explain and support the questionnaire results). Following data preparation, non-response bias was verified to ensure there was no statistically significant difference between respondents and non-respondents with respect to industry category (type of business). Using descriptive analysis of the data, a summary of the demographic characteristics of the respondents and their companies was provided, using means, frequencies and standard deviation. The issues of reliability and validity were also addressed. Factor analysis technique was used to explore possible underlying correlations among a large number of variables (i.e. the questionnaire responses) and identify factors, including MANOVA, Chi-square and the cross-tabulation.

The chapter ended with a descriptive summary of the interview results based on a thematic analysis approach. Opinions regarding location factors and difficulties related to foreign investment were presented and analysed. Results identified the most encouraging and discouraging factors and found significant differences in the views of the groups representing the supply and demand side of the equation respectively. Moreover, results suggested a lack of linkage between foreign companies and Libyan suppliers. A full discussion of the results of these findings will be presented in the next chapter.

Chapter 7

Discussion of the Quantitative and Qualitative Findings

7.1 Introduction

This chapter analyses the data from both the self-administered questionnaires and the interviews in relation to the objectives of this research to provide an integrated and systematic understanding of the subject matter in the study context. This chapter also evaluates the findings of the study in the light of the previous studies and on the basis of theoretical framework of the research. Therefore, the chapter is divided into seven sections. Following this introduction, there is an examination of the main factors which respondents identified as encouraging or discouraging FDI in Libya. The focus then shifts to an investigation of the differences in locational determinant factors from the perspective of each type of FDI. The following sections explore the linkage of FDI with domestic suppliers in the Libyan context and the chapter concludes by presenting a summary from the interviews and also revisits the key research questions of this study.

The following section will be discussed the first objective of the research, which aimed to identify those factors which are most likely to encourage or discourage FDI when used as determinants for considering locations for foreign investors. In order to clarify the key findings and discuss these in detail, each factor will be discussed separately by presenting the key finding from the questionnaire and comparing these with findings from the interviews. These results are then discussed in relation to findings from the FDI literature. The following subsections present their views regarding these issues.

7.2 To identify those factors which are most likely to encourage or discourage FDI when used as determinants for considering locations for new investment abroad.

Table 7.1 shows the FDI determinants factors means as calculated with the statistical tools. Also, the mean was the statistical tool used to rank the factors by degree of

importance while the standard deviation values for each factor indicated consistency among the respondent replies. The overall results from the sample reveal that six of eleven location factors were considered to provide positive incentives (mean score above 3.0) for FDI in Libya while in view of most foreign investors, the other five were considered to be either unimportant or to discourage investment. According to the sample of foreign investors in Libya, the six factors which most encouraged FDI were Economic Situation (mean=4.31 and ranked first), followed by Tax Exemptions (mean=4.27 and ranked second), Availability and Wages of Skilled Labor (mean=3.83 and ranked third), Market Conditions (mean=3.57 and ranked fourth), and Natural Resources (mean=3.53 and ranked fifth) , while of those factors considered to offer encouragement, Availability and Wages of Semi-Skilled Labor received the lowest mean 3.43 and ranking (sixth). Unsurprisingly, analysis reveals that these six key factors were most related to profitability and efficiency in the business operation of FDI. While the remaining five factors considered to be unfavourable in views of the foreign investors.

Table 7-1 Key Factors that Influencing Investors Decision

FDI Determinants Factors	No. of Items	Mean	Rank	St. D
Economic Conditions	5	**4.31**	1	.59537
Market Conditions	4	**3.57**	4	.72237
Tax Exemptions	5	**4.27**	2	.47534
Government Regulation and Red Tape	4	2.45	8	.75325
Availability and Wages of Skilled Labor	3	**3.83**	3	.33044
Availability and Wages of Semi-Skilled Labor	2	**3.43**	6	.84478
Availability of Natural Resources	2	**3.54**	5	.74217
Domestic Infrastructure	3	2.42	9	.48651
R&D and Training Systems	2	2.30	10	.84022
Financial Accessibility	3	2.97	7	.79675
Legal Practice	2	1.97	11	.58801

Note: Important determinant factors that encourage FDI have a mean score equal to or more than 3.0

The findings were divided into two main parts. The first part focuses on the factors which are considered to be encouraging investment in views of foreign investors, while the second part focuses on those which are deemed to be discouraging.

7.2.1 Factors which Encourage FDI

7.2.1.1 Economic Conditions

The key findings from both questionnaire and interviews participants show that economic stability is considered to be a critical factor in attracting FDI to Libya. This factor mainly covered measurements of economic indicators, such as GDP growth, exchange rate stability and inflation rate, all of which featured prominently in interviews with company representatives. The major importance given to Libyan economic stability implied that most foreign investors intending to operate in Libya were market seekers, concentrating mainly on the Libyan domestic market, rather than other forms of FDI such as efficiency seekers, or strategic seekers. As a result, these companies needed to feel more confident that the economic factor was favourable before investing abroad. These findings confirmed the secondary data discussed earlier (see Chapter Four) regarding Libyan economic indicators, as the country's inflation rate ranged from 3.2% to 2.4% over the last decade; the exchange rate for the Libyan dinar was approximately 1.30 against the American dollar, and the average annual rate of economic growth was 6.2% (Central Bank of Libya Annual Report, 2010).

The interviews contacted with the representatives of foreign firms confirm these results, since almost all of interviewees (12 of the 13 interviewees or 92.3%) thought that the Libyan domestic economic situation was the most important factor and that this has had a major positive impact on the decisions by foreign investors to invest in Libya. They stated that the rapid GDP growth, economic growth, and the stability of the overall economic situation such as relatively low inflation rate, and the stability of the Libyan currency make the business environment there more attractive for foreign companies. The following are examples of their replies:

> *Developing the Libyan business environment and economic reform have contributed to the stability of the overall macro-economic situation, such as the inflation rate, and increasing GDP growth. In my opinion, this can be considered*

to be one of the most important locational advantages, making Libya more attractive for FDI (Deputy Director General of Company E).

The indicators of economic stability, such as stability of local currency and the growth rate, are the most important factors collectively encouraging FDI in the Libyan context (Deputy Director General of Company H).

The General Director of Company M echoed these sentiments but also made a point about the need for improvements:

Our decision to invest in Libya was based on the stability of the overall economic situation of the country. However, this needs to be matched by more advanced development of infrastructure projects and improvements to the services provided by government institutions, such as financial and legal services.

Privatisation also seems to be very important, particularly for joint-venture type FDI. Seven of the 13 participating companies advocate the importance of this factor. The responses by companies A, B, C, H, J, K, and L were in line with the questionnaire finding which is that privatisation has a positive effect on attracting foreign investors, but respondents made some suggestions about further steps which needed to be taken. Thus, according to the Deputy Director General of Company H:

Privatisation initiatives should be expanded to cover most of the services provided by the public sector, especially the financial and oil sectors, in order to create a more competitive environment. Moreover, the procedures of the privatisation process should be simplified in order to attract overseas investors to contribute to this process.

The findings mirror the FDI literature since, as expected, economic stability is crucial for attracting FDI as it provides confidence and certainty for businesses. The above result is consistent with a number of previous studies which have found a significant positive relationship between macro-economic stability factors and FDI inflow. Arratibel, et al (2011) examined the inflows of FDI to Cambodia from 17 countries using panel data

technique over the period 1995-2005. Their findings emphasised that economic indicators, such as economic growth and stability of the exchange rate, were the most important factors driving FDI inflow to the country. In addition, Bellak *et al*. (2009) studied the determinants of FDI to eight Central-East Europe Countries in the years 1995-2004 and found that economic growth in the host countries measured by per capita income and privatisation programme policy had acted as a favourable factor in attracting FDI.

A study of the determinants of FDI Australian carried out by Sharma and Bandara (2010) revealed that countries with a stable macro-economic environment tend to attract more foreign investment inflow. Krugman (1995) had previously argued that FDI, unlike other capital inflows, such as portfolio investment, is not liquid meaning that once an investment has been made, it is not easy to pull out. For this reasons, investors look for countries that are economically stable.

7.2.1.2 Tax Exemptions

Incentives relating to tax emerged as the second most important factor among those seen as offering encouragement to attract FDI. As can be seen from Table 7.1, the results show that all concessions, including exemptions on import tariff, corporate income tax, tax on repatriation of dividends and income of Libyan people, were considered to have a high degree of importance by the foreign investors; the overall mean value of 4.27 indicates that Tax Exemptions have a very important effect on the FDI location decision. Furthermore, the small standard deviation values of 0.47 for this factor indicate that respondent replies were highly consistent, suggesting consensus among the sample respondents regarding the importance of this factor. Taxes directly affect profitability of the subsidiary and, consequently, the dividend pay-out to its parent company. High tax rates lower profits in a way that is beyond the control of business. In addition, high tariffs on imported raw material and machinery significantly increase production costs, which naturally make the FDI less competitive in comparison with its local counterparts. Since net profit after tax is paid out to the FDI parent company overseas, flexibility and

favourable regulation regarding the tax on repatriation of income and dividends enables foreign companies to enjoy the full benefits of their investment. In short, countries that provide favourable tax regimes attract more foreign investment. This positive attitude towards these tax exemptions is perhaps not surprising since a number of the foreign companies at the operational stage still benefit from these incentives.

During the interview process, most participants (11 out of 13 or 84.6%) emphasised that incentives such as tax exemptions had significantly influenced their investment location decision at various levels, and companies made a number of recommendations regarding further improvements in this area, one interviewee stated that:

> *Despite the encouraging tax incentives in Libya which represent a significant attraction for FDI, the Libyan tax system still suffers from too much bureaucracy, a legacy from the previous period* (General Manager, Company H).

Turning to the policy dimension of variable tax incentives, findings seem to indicate that reducing the level of taxes would encourage more foreign investors. These results may be explained by the fact that since most of the foreign companies in Libya are relatively new investors in many activities, they are still benefiting from incentives including Investment Laws Nos. 5, 7 and 9 which offered five years of exemptions with extra incentives applying under certain conditions. Extra government incentives were included for projects that contribute to Libya's regional development food security, and at the same time, are environmentally sustainable.

The findings of this aspect of the research are consistent with the results of number of existing empirical studies on the effects of government tax incentive on inflows of FDI including Oman (2000) and Bustos (2011), all of which concluded that governments can influence investor decisions via-offering fiscal incentives. Similarly, Bellak *et al.* (2009) reported that host country tax exemptions acted as a positive attraction for FDI.

7.2.1.3 Availability and Wages of Skilled Labor

The results of the survey as shown in Table 7.1 reveal that the Availability and Wages of Skilled Labour, in particular those aspects which related directly to human capital, such as (availability of skilled labour, wages for technical labour, and salaries required for managerial staff), appear to be important for foreign companies, as this was ranked third with a mean of 3.83. This factor relates to the profitability and efficiency of business operations. Human capital is an important determinant of the marginal value of investment, as higher quality labour implies higher profitability or higher product quality and, thus, promotes competitive advantage for FDI.

During the interviews, human capital issues regarding availability of skilled labour and rates of pay were discussed. Nine of the thirteen interviewees from foreign companies (69%) mentioned the availability of skilled labour as an important factor for their investment decision and that is was easy to obtain Libyan managers at appropriate wages.

According to one respondent:

> *The quality and cost of labour are very important elements for any investment decision to gain competitive advantage in the marketplace. We consider the availability of skilled local labour and reasonable wages as incentive factors for entering the Libyan market, but the government should understand that there is a technical revolution, matched by the availability of a good HRM system which is based on international HR practices* (Chairman of the Board, Company D).

These findings support the earlier questionnaire results which consider availability of skilled labour as the third most important factor affecting FDI decisions. The positive attitude of foreign investors towards the availability and wage levels of skilled Libyan labour can be explained by the fact that the government-initiated human development programmes have been successful. As a result, Libya is now classified as a high performing country, according to the Human Development Report 2013. The report ranks

Libya at 64 out of a total of 186 countries surveyed, with a Human Development Indicator of 0.769 where one is the maximum (Human Development Report 2013: 17).

On the other hand, this result can also be explained by the fact that as a consequence of the restructuring of the Libyan economy, one of the negative effects of the privatisation programme, particularly in the non-oil sector, was the loss of more than quarter of a million jobs, which led to an abundance of labour supply in the labour market of both skilled and semi-skilled workers. These results are consistent with a number of studies relating to the link between FDI and the availability and cost of a skilled local workforce. For example, Lemi and Asefa (2001), and Bellak *et al.* (2008) reached the same conclusion in their studies of the relationship between availability and cost of labour force and FDI inflows into countries in Sub-Saharan Africa. Both argued that the availability and cost of a skilled labour force had had positive effects on FDI inflows to the region. In the same vein, Bhavan *et al.* (2011) showed that the availability of human capital and wage costs are important factors for attracting FDI to South Asian countries. Their results also supported theories considering rates of pay, since higher wages make local production more expensive and lead to reduced FDI.

7.2.1.4 Market Conditions

There is a strong indication that the representatives of fully foreign-owned and joint venture companies consider Market Conditions in Libya as a significant factor for attracting FDI. This factor relates to the demands of the Libyan economy and includes four items, namely competition in the domestic market and market potential, existence of distribution channels, trends and growth in the local market, and availability and reliability of market information. As shown in Table 7.1, Market Conditions were ranked by participants as the fourth most encouraging factor for FDI in Libya, with a mean of 3.57. This factor was viewed favourably because of high demand in the domestic market for goods and services together with the fact that Libya was considered to be the link between North African and Middle East countries and also acted as the Northern gateway to the African continent.

These results merit further contextualization. The Libyan economy is small, both in terms of population, which in 2010 numbered approximately six million, and in terms of local market size: in 2010, nominal GNP was LYD 105.0 billion. But the Libyan market is experiencing rapid growth, having expanded faster than the global economy during the years 2008- 2010 of the last decade when the average growth rate in Libya was 6.2% compared to 4.3% for global growth. In addition, the demand for goods and services as measured by per capita income is increasing from USD 8073 in 2005 to USD 13319 in 2010 (UNCTAD, 2013). This rapid growth can be explained mainly by the increases in oil prices in the international market.

Some 69% of the interviewees expressed the opinion that market growth has had a significant positive impact on their investment activities in Libya, particularly those who have invested in the manufacturing sector. Respondents noted that the high demand in the domestic market makes Libya attractive for FDI, but suggested that more needed to be done in terms of providing a database about Libyan's domestic market demand in order to promote competition and sustain economic development in the country. It was noted that political instability in Libya did not appear to have affected demand for their products. This was supported by the representative for Company B:

> *The high demand for our products and services in the manufacturing industry was one of the reasons for investing in Libya. Despite the political crisis in 2011, our production and sales operations returned to their normal rates as demand for our products and services has outstripped supply.*

The Deputy Director General Company L states:

> *As an international company, we believe that market growth and the end of the State domination of the local market was an important signal for us as foreign investors because this makes Libyan markets more open to international investment. This creates a new competitive environment which presents us with new challenges.*

There is a clear indication that there is a positive relationship between Libya's market situation, particularly its market growth rate, and FDI. This finding suggests that growth in the domestic market has been one of the most important factors in attracting foreign investment into Libya which has arrived to meet the demands of a growing urban population. These findings are consistent with number of previous studies such as (Kolstad and Villanger, 2008; Chidlow *et al.* 2009; Bellak *et al.* 2008; Rogman and Ebbers, 2013). These studies found that different measures of market size and openness to trade are found to be significantly related to FDI inflows in the host country.

7.2.1.5 Natural Resources

The survey of representatives of foreign companies revealed that the availability and quality of natural resources are important elements in influencing investor decisions. This factor has been measured using two questions that were built on a five-point Likert scale that included availability and cost of natural resources**.** In this regard, the results show with a mean of 3.53 the availability of natural resources ranked fifth highest in terms of encouraging factors. It was expected that resources seeking FDI particularly from manufacturing would consider investing in natural resources as important factor for their production.

The results of the interviews show that about eight out thirteen (61%) of the interviewed companies would consider natural resources in their investment decisions, with the industrial companies being more interested in natural resources than the service companies. Interviewees from companies C, E, J, H, B and L revealed that the availability and cost of natural resources had influenced their company's decision to invest in Libya due to interest in making use of these resources, while this factor was of little concern to most of the companies in the services sector. In this context, the General Director of company C explained:

> *One of the local economic advantages in Libyan market is the availability of the huge natural resources, which makes the country an attractive investment*

destination for foreign investors. Due to the nature of our business in the building materials industry which is highly dependent on natural resources, this significantly influenced our investment decision in Libya.

This result supports Dunning's (1979, 1993) theory which highlighted that the availability of host country natural resources was one of the critical factors in attracting FDI. These results are also consistent with a number of empirical studies (Asiedu, 2011; Onyeiwu and Shrestha, 2004; Buckley *et al.,* 2007; Acheampong and Qsei, 2014) all of which concluded that countries which are rich in natural resources are able to attract more FDI inflows, because multinational companies, particularly those working in the industrial sector, are seeking resources to meet the growing demand for these resources which may be exorbitantly expensive in their home countries.

In order to identify potential difficulties in relation to using natural resources, respondents were asked about any problems which they had encountered when using local raw materials to increase productivity. The results show that six out of eight representatives of fully foreign-owned and joint venture companies in the manufacturing sector (or 75%) stated they had experienced problems using the local natural resources. More specifically, 50% of participants considered the resources to be inadequate to their needs (companies E, H and J), 33.3%, argued they were of a low quality (companies C, and L) and 16.6% stated they proved to be prohibitively expensive (company B). These results indicated that companies in the manufacturing sector suffer the most from the problems associated with natural resources, and that these problems increased for those industrial companies operating in capital cities such as Tripoli and Benghazi which appeared to suffer most from inadequate and poor quality materials. In this context, the interviewee from General Director Company B observed:

Natural resources are considered to be an important element for most industrial companies with products which depend on natural resources and when such resources are extensively available in Libya, this makes the country an attractive place to invest in manufacturing industry. However, mismanagement of the

country's natural resources may result in insufficient utilization of these resources. I recommend that the local authority identify the locations of such natural resources in the country, which makes these places inevitable attractive to any investor who intends to enter the country. This would help reduce investment costs.

During the interview, respondents were asked about sources of their company's production input. Most of the responses (90%), particularly those from the manufacturing companies, indicated that their raw materials are sourced from Libyan's domestic market. However, most of the providers of raw materials are overseas companies which serve the foreign companies in Libyan market and only two companies (L, C) reported that they source 40% of their raw material from Libyan suppliers.

This outcome is consistent with the secondary data discussed earlier in section 4.3 which indicated that only sectors such as agricultural and maritime and construction contributed to GDP, with 3.3% and 7.9% respectively in 2010, which decreased to 0.8% and 1.3% respectively in 2012. The manufacturing sector contributed only 5.7% to Libyan GDP in 2010 which fell to 3.2% in 2012, as a result of the political crisis in 2011(Central Bank of Libya, Annual Report, 2013). This may explained by the fact that despite the availability of various natural resources in Libya, these are still not well planned and their mismanagement has meant that there has been a failure to use these resources effectively as indicated above by General Director of company B.

7.2.1.6 Availability and Wages of Semi-Skilled Labour

In addition to analysing the importance of skilled labour in FDI decisions, it is also useful to examine another issue related to human capital, namely the availability of a semi-skilled labour force in Libya. According to the existing literature, the availability of a semi-skilled labour may also be an important factor in facilitating those economic activities that depend on this form of human capital Bavan *et al.* (2011).

Results from Table 7.1 reveal that the Availability and Wages of Semi-Skilled Labour factor received an overall mean score of 3.43 and ranked sixth, which is still above the average, indicating that whilst it is not as important for foreign investors as Availability and Wages of Skilled Labour, it still merits attention in the view of the foreign companies operating in Libya. This factor included two items, which are availability of semi-skilled labour and also wages. All the respondents were asked to comment on the importance of both these items separately in relation to their company's investment decision.

Unlike the above results of the questionnaire, the interviewees' responses varied depending on the sector in which the company operated. Availability and wages of semi-skilled labour did not feature as an important factor for the representatives of services companies as it was found that the entire sample of the service sector considers semi-skilled labour as unimportant for their investment decision. It is perhaps not surprising that none of the services companies mentioned this factor because the nature of their company activity which requires skilled labour. On the other hand, in the manufacturing sector there are only four out of eight companies acknowledge the important of semi-skilled labour, whilst the other four companies indicated that this factor is not important for their companies' activities because they believed that their companies are not at the position of requiring skilled employees their production at the current stage.

This discrepancy between the questionnaire and the interviews findings may also have been influenced by the small number of companies participating in the interviews which were only thirteen in total.

In this context The Senior Government Officials were asked following question about their views regarding the current business environment in Libya:

Which factor or factors do you think had the biggest influence on foreign company decisions to invest in Libya?

In order to obtain the point of view of some senior government officials regarding the prime determinants of Libyan FDI, some seven government officials were interviewed

about their opinions on the main factors that attract FDI into the country. In general, there was a consensus of views between foreign investors and government representatives concerning the major locational factors which prove attractive to FDI, but the government officials weighted these factors differently, highlighting that the availability of their national natural resources as the most significant factor likely to influencing FDI decisions. They then ranked the overall macro-economic stability of Libya, the advantages afforded by its geographical location, and market conditions, respectively. They rated Human Capital and government Tax Exemptions as the least important of those factors they identified as likely to encourage FDI. According to the Director of Investment Management at the PIB:

> *We rely heavily on Libya's abundance of natural resources and geographical location, as it is close to most industrialized countries; these are considered to be the two most important factors in attracting FDI currently. Our goal is to achieve regional development, especially in rural areas which are rich in natural resources. We also seek to diversify our national economic sources of income which in turn reduces dependency on oil income. In addition, we believe that the stability of the economy, and the level of aggregate demand for goods and services in the local market, is considered to be other attractive factors.*

However, most of the government representatives argued that even though the abundance of the natural resources has been given a top priority in Libyan investment policy, they are aware that these natural resources are not yet utilized effectively, due to a number of problems which have had negative impact on the economic development programme, intended to create an alternative source to energy sector revenues. They acknowledge that this is mainly due to the government's mismanagement of the natural resources. In this context, the Director of Investment Management stated that: "*Failure to use the available local resources in the optimum manner is the major stumbling block in the Libyan development agenda*".

The Head of the Research and Planning Department at PIB highlighted the fact that the process of economic development requires more emphasis on the use of domestic natural raw materials to enhance production, observing that:

> *The available resources should be accurately defined and plans should be introduced to achieve their sustainability, on the one hand, and promote regional development on the other, particularly in those rural areas where these resources are abundantly available.*

Another respondent Director of Investment Management at PIB argued that:

> *The poor management of raw materials in Libya was due to the fact that most provinces have no plans at all or they have but did not provide them to the PIB, which complicates the task of allocating sites for FDI.*

The government officials emphasized that raw materials in Libya are mismanaged, as a result of the lack of cooperation between the relevant government bodies with regard to planning the available economic resources and, also, as a result of poor coordination between the PIB and most of the provinces in relation to the creation of an investment map. They attributed this to the fact that a number of decision-makers in these provincial locations have poor investment knowledge. They suggested that the available materials should be estimated and that these locations should be incorporated into an investment map in order to allow potential investment projects to be placed close to the sites where raw materials are to be found in rural zones. This would make the processing for final consumption of the materials easier. In this context, the Head of PIB's Research and Planning Department advocated the following approach:

> *The general management of resources in Libya requires an effective scheme which coordinates between the relevant government's bodies with regard to planning the availability of natural resources. One way to achieve that is by ensuring that any information regarding the availability of such resources gets into the hands of international investors.*

Furthermore, interviewees confirmed that there are a number of problems associated with the quality of raw materials because they are transferred from the quarries and mines to the production sites in industrial cities in Tripoli and Benghazi by using inappropriate ways. Moreover, the scarcity of these material suppliers together with the disorganized marketing process has led to an increase in prices. Most of the senior officials who were interviewed blame the poor performance of government policy in relation to the above mentioned aspects associated with raw materials.

With regard to tax exemptions and other financial incentives, government officials weighted these differently to the foreign investors. They agreed that the exemptions were important locational factors but they argue that these cannot be adopted as long-term strategies to attract FDI. The Deputy Director of PIB indicates the need to think carefully about future developments:

> *In my opinion, the laws and regulations provided by the government to encourage investment, such as tax incentives and the one-stop shop scheme have become some of the essentials; however, the Libyan government needs to adopt long-term projects. The government accepts responsibility for 15-20% of the project costs to encourage the investors which makes a big difference, as well as putting Libya into a position of being able to compete with neighboring countries and helping the country to exist on global investment.*

In terms of Human Capital, most of the official respondents were convinced that FDI has created good employment opportunities for many local workers, helping to reduce the levels of unemployment in the country, which was one of the major problems facing the Libyan economy. According to the PIB Report (2012), by the end of 2010, more than 14,000 of the local labour force were being employed by fully foreign-owned and joint-venture companies. Interviewees also believe that FDI in Libya has led to an increase in the efficiency of human resources by means of training in new techniques which will definitely result in the emergence of an appropriate environment for creativity and productivity. For example, the emergence of foreign companies has opened up the

economy to international competition. Also, they suggested that the government has a responsibility to expend more effort on meeting the needs of fully foreign-owned companies and joint ventures by providing appropriately skilled and well-trained employees.

7.2.2 Factors which Discourage FDI

On the negative side, the foreign investors mentioned five unfavourable factors which are likely to obstruct FDI and to hinder Libyan's investment environment: Legal Practice, R&D and Training Systems, Domestic Infrastructure, Government Regulation and Red Tape, and Financial Accessibility, as shown in Table 7.1. These factors negatively impact on operating efficiency, and, thus the profitability of the firms.

7.2.2.1 Government Regulation and Red Tape

The second factor identified as discouraging FDI is Government Regulation and Red Tape, which affects property and equity ownership by foreigners, and regulates and controls foreign exchange transactions which are directly related to Libyan investment laws. As Table 7.2 shows, with a mean of 2.45, most of the foreign investors viewed Government Regulation and Red Tape as another discouraging or unfavourable factor. It is well known that unnecessarily time-consuming government bureaucracy may increase operating costs. At high levels of bureaucracy may exist nepotism and corruption, as customers may have to pay to speed up services and approvals (Helmy, 2013).

These negative attitudes among the representatives of companies can be explained by the fact that Libya has experienced institutional and regulatory instability for more than three decades. This should not be surprising given that the political system in Libya has passed through three distinct phases during its development, beginning as a Constitutional Monarchy in 1951, becoming a Socialist Republic in 1969, and then shifting to a system of “people’s power/authority” in 1977. All these changes in the political system negatively affected the stability of Libya’s State institutions. In particular, the period of the so-called “people’s power/authority” system in 1977 caused confusion for State

institutions. For example, the highest institution, the Council of Ministers, was reshuffled more than 14 times between 1977 and 1994, and six times between 2003 and 2011 (Vandewalle, 2012).

The majority of the investors who were interviewed seemed to be unhappy with government regulations and expressed their dissatisfaction with the large number of documents required by the government offices and frequent delays in processing applications. Ten company representatives (over 76%) complained about the administrative system, and the results suggest that companies that are fully owned by foreign investors and those in the services sector companies suffer the most.

There are also issues with the possibility of exporting capital; with the results revealing that the problem of outward transfer of funds has become more complicated over time, even though the Libyan investment laws allow foreign investors to transfer net profits. In this specific case, the difficulty is associated with the administrative procedures, which require the approval in advance of the Central Bank of Libya. According to the General Director of Company I:

> *We have spent a lot of time with government officials in resolving problems related to taxation policies, such as customs and duties imposed by the government on imported goods, and on remittances abroad. In addition, there are complexities in the procedures when signing a new agreement.*

The Deputy Director General of Company L added:

> *There are restrictions imposed by government on property ownership by foreign investors, and therefore, in my opinion such restrictions should be eliminated in order to encourage foreign investments.*

As previously mentioned, nepotism and corruption among government officials and a reluctance to change and adapt to new ways is a worldwide phenomenon, particularly in the developing world, but the scale of the problem differs from one country to another. In the case of Libya this problem may have been exacerbated by institutional instability due

to changes in the administrative sub-divisions as explained above which has negatively affected the performance of the public administration (Shirnninah, 2007).

The literature review concerning the determinants of FDI (as discussed in Chapter Two) reflects the fact that the experience of many countries indicate that flexibility in government regulation and rules such as property rights, transparent economic policies and a lower level of bureaucracy for foreign investors help to increase FDI inflows to the host country (OECD, 2003). Other studies have argued that the simplification of the procedures and stability of the administrative system in general function as important factors in attracting more FDI; for example; Gray (2003) highlight the significance of simple and prompt procedures based on a so-called one-stop shop approach in improving FDI inflows. Kamali (2004) reached the same conclusion in the case of Egypt.

What are the challenges and difficulties facing the public authorities wishing to improve procedures and facilitate administrative routines to attract more FDI?

Senior government officials were also asked about the challenges facing the general administration to minimise the levels of bureaucracy and how this situation can be improved. Most of these interviewees believed that, despite the positive investment incentives that were being offered under different investment laws, still more needed to be done in order to attract more FDI to Libya. It was also suggested that the administration ought to speed up procedures in order to make the business environment more attractive to investors. This implies raising the competence of the public administration by training with the aim of producing a better qualified workforce, and raises the need for an effective one-window policy, particularly in relation to taxation, customs, and power supply and employment process. In this regard, the Head of the Department of Investment commented on developments at PIB:

> *The PIB has established a "one-stop shop" service in an attempt to simplify the bureaucratic procedures, by offering all requirements and services needs such as labour, power supply, taxation etc. to investors*

Another interviewee argued that:

> *One of the challenging problems facing the strategies associated with the attraction of FDI into Libya is the speeding up of procedures and facilitating administrative routines and training government staff to cope with the investors' requirements* (Deputy Director of PIB, 2012).

A key problem is that the administrative system lacks coordination between different government bodies and this issue goes beyond the One-Stop Shop policy to the establishment of the investment map discussed previously. Since 2007, the PIB has been attempting to introduce the One-Stop Shop policy in response to Law No. 150 of 2007, to speed up and simplify FDI applications by reducing bureaucracy through the establishment of a single office (PIB, 2013; Younes, 2013).

From the field survey, it appeared that foreign investors still have to deal with more than one office, and that the PIB plays the role of an intermediary, providing investors with the documents required by the various government bodies. The poor coordination between the various bodies is a consequence of the traditional mechanism of the general administration and the inefficiency of the administrative system reflected in its totally bureaucratic approach. This was supported by one senior government official (Undersecretary of the Economic Ministry) who explained that: "*We are not sure whether PIB will become an independent government entity or will follow another government's departments when a new structure will be put into place*"). Such uncertainty is likely to have a negative impact on the performance of the public administration.

Legislation means that the PIB's role is confined to facilitating administrative procedures and prevents it from deciding on the merits of applications. Thus, the main task of the PIB is to compile technical reports in relation to FDI applications, whilst decision-making rests with the Ministry of Economy, Trade, and Investment after consultation with the Prime Minister. According to the government policy statement and laws related to foreign

investors, the PIB has to provide a report within 60 days of the application to the appropriate authorities (Government Investment Law No. 5 of 1997).

In this context, the Libyan government should improve its e-infrastructure, particularly making more use of the Internet to enable it to adapt and activate e-government services to allow people and the business sector to interact so that business and government activities could be electronically linked. This process of communication between local government and the people could create a reasonable outflow of information enabling effective participation in the processing and implementation of decisions. The advantages of adopting e-trade and e-government are that helps greatly to smooth the flow of information and promote public awareness which would help to raise economic efficiency to international standards.

7.2.2.2 Domestic Infrastructure

All the respondents were asked to state their opinions about Domestic Infrastructure in Libya which was measured by three questions about the quality of telecommunications services, quality of transportation services and quality of electricity supply services on a five-point Likert scale. The results in Table 7.19 reveal that the investors working in Libya also considered this to be another discouraging factor, since it obtained a mean score of 2.45.

This outcome can be explained by number of problems and weaknesses related to Libya's domestic infrastructure. In terms of the telecommunications sector, although real development has taken place in this sector, this has been obscured by the fact that Libya is still lagging behind in some aspects of telecommunications such as information technology. The reason for this is the high level of computer illiteracy coupled with poor infrastructure which means that the information technology is currently not accessible to a huge sector of the population.

In terms of land transport services, the response from foreign investors can be explained by a number of negative issues associated with land transport, most importantly traffic

congestion in the centers of the major cities, due to the failure of road planning to cope with increasing traffic volumes. The results in the case of maritime and air transport are probably due to the fact that both sectors are suffering from problems highlighted in the Government Transport Sector Report (2010). With regard to the former, the report pointed out that most companies operating in ports suffer from mismanagement and have failed to renovate and upgrade the country's seaports. As a result, in comparison to international standards, most of the Libyan ports services are lacking in terms of management and mechanization and have limited capacity. Libyan air transport fails to benefit from the country's location as the gateway to Africa because of similar shortcomings (National Council Planning Report, 2010).

With regard to electricity supply, Libya does have an extended network of electric power lines covering most of the country. However, this sector still suffers from major technical problems, the most important of which is its inability to cope with its ability to keep pace with growing demand which is a vital concern for many foreign companies, particularly those operating in rural areas where the power supply may be inadequate or intermittent (National Council Planning Report, 2010).

These failures became clear in the research interviews, when nine of the thirteen company representatives (69%) voiced concerns in relation to the shortcomings in these areas. According to the General Manager of the Company F: "*In principle, the infrastructure is still at an emerging stage, for example, the power supplies is poor, being neither adequate nor stable and the communication system has limited capacity*". The General Manager of Company J expressed some concerns about the telephone network, describing it as "*frequently uncertain*".

The respondents for companies G, M, and D all pointed out the outstanding improvements which had been made in transport but noted that problems with telecommunications and electricity supplies still persist. According to the General Manager of the Company L: "*Telecommunications are not at the expected level, especially in industrial cities, where our factories are located"*.

Libyan domestic infrastructure can still be described as modest in terms of quality and is facing increasing demands as a result of rising population levels and the subsequent expansion in urban areas. Despite the enormous natural resources owned by Libya and the government-funded infrastructure development projects that begin in the 1970s and lasted until 2011, the situation has not improved as required. The 1980s witnessed a fall in oil prices which meant that the government could not afford to provide the necessary funds to make the improvements to the infrastructure; then, in the 1990s, when Libya was under UN sanctions, once again a lack of government funds to improve the infrastructure had a negative impact on the country's development. In the last decade, supported by the increase in oil prices, Libya invested over US $120 billion in improving domestic infrastructure but many of these projects are still incomplete and some have been delayed because of the political and security situation after 2011 (General Planning Centre, Report, 2012).

Research has shown that infrastructure plays a major role in attracting business activities to the host countries, boosting its location advantage (Quazi *et al*. 2014). Improving infrastructure leads to an increase in the level of quality services and productivity which, in turn, fulfils the investor's needs and demands and achieves investor satisfaction (Alavinasab, 2013). On the other hand, Moosa and Cardak (2006) argued that poor infrastructure increases the cost of business which reduces the rate of return on investment and vice versa.

What are the challenges and difficulties facing the public authorities wishing to improve the domestic infrastructure in order to attract more FDI?

Most of the senior government officials who were interviewed highlighted that good infrastructure is a very important factor in attracting FDI and they agreed that Libya's domestic infrastructure is still under development. They also noted that this creates problems, leading to a lack of coordination between different government departments on many key issues due to ineffective exchange of information, given that the use of the

internet and other forms of electronic communication are scarce or even non-existent. It was also acknowledged that the government should add more efforts on upgrading the seaports and airports and establishing companies to operate public transport as these three sectors complement each other to boost economic efficiency which in turn will help in attracting FDI. The Undersecretary for Economics, Trade and Investment said:

> *We realise that there are complaints about the infrastructure in the country as a consequence of the poor coordination between different government departments. This is because infrastructure projects have not yet been completed. The government is working hard to provide services of the expected standards which usually take some time and therefore, the government allocated approximately 120 billion dollars for infrastructure projects for this purpose. Moreover, the conflicts in 2011* [the Arab Spring] *brought us other challenges in improving the quality of the infrastructure projects.*

Another respondent Director of Investment Management stated that:

> *Investor satisfaction is considered to be one of our priorities, and therefore, we pay constant attention to investor needs. We have established a Customer Services Department specifically for this purpose with a hotline number in case of any issues that they want to discuss with us regarding their business.*

Another interviewee suggested that:

> *The improvement and completion of infrastructure facilities should be an urgent priority. The most important element should be the availability of a powerful database relating to the different economic activities. The organisation of this information would help in the success of economic feasibility studies* (Deputy Director of PIB, 2012).

The government officials believe that the experience of a number of developing countries has proved that improving domestic infrastructure such as seaports and air transport can play a major role in economic development. Providing services which are of an

international standard can help the country to play an active role within the international transport system. This is borne out by the experience of Dubai, Qatar, Singapore, and South Korea, which have been successful due to investing in their infrastructure, particularly in air and sea transport companies, and locating these correctly. These factors have created an attractive environment for both foreign and local investors in relation to these sectors. These interviewees also considered that the deregulation of the air and sea transport industries, including open air and sea access, will be essential in order to provide new perspectives on existing practices as will use of the latest technologies to meet international standards, enabling Libya to compete and benefit from its unique location.

7.2.2.3 R&D and Training Systems

Foreign company representatives also complained about the quality and cost of training centres and both questionnaire and interview findings indicate that this issue needs attention because it is important to their companies. This factor also included the quality of Training Systems, and the cost of training. The questionnaire findings in Table 7.2 show that quality of the training systems is another discouraging factor, with a mean score of 2.30.

During the interviews the vast majority of respondents from the foreign companies described the Libyan R&D standard as being very low in comparison to other developing regions such as South East Asia and Latin America. This result reflected the lack of the government spending on R&D. Interviewees provided a range of responses to this issue but most complained about the quality of Libya's Training Systems. According to the Deputy Director General of Company J:

> *In order to develop workers' skills and competencies we need to send them abroad for training and exposure. However, this is associated with high costs that can increase the cost of production.*

Another Deputy Director General of Company E adds:

We believe in the importance of training programmes to benefit our employees because we believe that they produce positive results that reflect on the company's productivity, but the local training centres are poor in terms of quality and at the same time they are associated with high cost.

A similar response to this issue came from the General Director of Company C:

In fact, there are the training courses available, but the efficiency and quality of these training courses still needs more improvement to satisfy the company's HR needs.

What are the challenges and difficulties facing the public authorities wishing to improve the quality of training centres in order to attract more FDI?

During the interviews, the government representatives expressed the opinion that the government's latest move to establish industrial research centres and training centres was a step in the right direction. This needed to be followed, however, by more expenditure on R&D, and the private sector should work hand-in-hand with the government. The experience of East and South East Asia in this field, particularly Singapore and Korea, should be studied and followed, because of its evident success. In this context, the Head of Research and Planning Department of PIB stated that:

More vocational content needs to be embedded within the country's education system, rather than concentrating on social sciences, because the Libyan labour market is already saturated with social studies' outputs graduates from this area. This could help to reduce the high unemployment rates in the country caused by the lack of skilled labour. In this regard, we urge private employers to participate in the HRD.

The Undersecretary of the Ministry of Industry commented:

The Libyan government should pay more attention to improving the use of technology by establishing more R&D Centres all around the country and

following up the latest developments in the technological world, to transfer the country to e-government-based services, because it is not possible to depend totally on foreign companies bringing technology and innovation.

In Korea, for example, R &D expenditure has grown faster than GDP. In 2011 it stood at 4.04% of GDP, which was one of the highest R&D /GNP ratios among the East Asian countries. The private sector responded positively to government initiatives. R&D expenditure has also nearly equalled the growth of GDP in Israel. In 2011 it reached 3.97% of GDP, making this the highest R&D/GNP ratio among the Middle East countries (World Bank Data, 2013).

7.2.2.4 Financial Accessibility

The results of the survey, shown in Table 7.2, reveal that Financial Accessibility has also been ranked as another deterrent factor for FDI in Libya, with a mean score of 2.97. This factor was measured by three items referring to the ease of access to local sources of funding, the reliability of accounting and auditing system, and the availability of the financial system in general. In the opinion of foreign investors, the services provided by banks and other aspects of Financial Accessibility are unsatisfactory.

In relation to accounting procedures and access to local sources of funding, the outcomes indicated that the representatives of foreign companies seemed to be less concerned about accounting and auditing procedures. This situation can be explained by the fact that the accounting and auditing procedures are based on the same principles and procedures followed in most countries. However, the foreign investor's particularly foreign owned companies more concerned about the access to the local sources of funding. In general, the banking sector in Libya still struggling with problems related to the structure of the banking sector since the major private and public banks still offer old-style services such as the payment of wages and have limited provision of credit facilities (Alrafadi at el 2014).

When interviewed, 46.1% of the participants reported their companies consider this financial factor as another problem which leading to reduce successful investment. They are aware of the value of financial services and major role that financial services play in achieving a successful business especially in trading companies; some 53.9% of the interviewees did not mention anything regarding this factor. The General Director of Company F stated:

> *The services provided by commercial banks fall far below the expectations of our company; electronic services such as internet banking are not available while cash machine services are limited.*

The Central Bank of Libya (CBL) has outlined its aims, strategies, and policies in order to promote the role of private commercial banks. This is particularly important following the adoption of new measures to restructure the economy in order to relieve the State of some of its economic responsibilities by encouraging the local and foreign private sector to resume economic activity. In this context, significant efforts have been made to recover and improve banking services, particularly the introduction of Law No. 1 of 2005 which allowed foreign capital to invest in the banking sector via buying shares in local banks after an absence for almost four decades. Foreign banks were also permitted to establish branches in Libya (Government Law No. 1 of 2005).

As a result of this law, two commercial banks have bought shares in Sahara and Al Wahda Banks. BNP Paribas Group became a strategic partner of Sahara Bank by purchasing 19.0% of the shares and retaining the right to a further 51.0% of the shares within three to five years. Similarly, a strategic partnership was established between the Arab Bank and AlWahda Bank under the same conditions, while another two foreign banks have been established in partnership with the states of Qatar and the UAE (Central Bank of Libya, 2010).

Furthermore, the Libyan Centre for Credit Information was established in 2009. This Centre gathers personal credit information on current and potential borrowers from the

member banks, in order to help banks make the correct lending decisions. Thus, it improves banking performance by using hazard perception to minimise potential losses, predict problems involved with borrowers, and allow the most appropriate solution when necessary. Under the provisions of Law No. 3 of 2006 commercial banks are allowed to provide loans and other financial facilities to foreign companies investing in Libya (Aljbiri, 2013).

As discussed in Chapter Four, despite the CBL's policies in terms of the establishment of private banks, the emergence of foreign banks as shareholders in local banks and the restructuring of the Libyan banking system though providing advanced services to across links and communicating networks between banking system such as the Real-Time Cross-Settlement system, the Automated Clearing House, Automated Cheque Processing, ATM, POS and CMS, but still limited improvement of the banking services sector, because these services remain inactivated (Central Bank of Libya, Annual Report 2010).

What are the challenges and difficulties facing the public authorities wishing to improve the quality of financial sector in order to attract more FDI?

During the interviews, the senior Libyan officials were asked about the challenges they believed were involved in relation to the improvement and development of financial services in Libya. The results revealed that they are well aware of the problems associated with the financial services as these are still below the international standard in terms of their quality and with regard to the technology used by most of the banks. Moreover, mismanagement has meant the low level of service persists. One of the interviewees warned that the Libyan banking system needed to change:

> *It's the era of electronic services, the use of up-to-date technology such ATM machines and internet banking have become essential element for improving banking services in order to help to integrate financially with the global economy.*

As the interviewee notes, electronic services provided via modern technology such as ATM, internet banking, etc. are an essential element for improving banking services in order help Libya to integrate with the global banking services. If the government would promote further diversification of the banking services, this would also open the doors to the growing sector of Islamic banks which would attract customers wishing to follow Islamic principles.

7.2.2.5 Legal Practice

Table 7.2 shows that the Libyan legal system is considered to be the most discouraging factor in the view of the foreign companies that operate in Libya (mean = 1.96). This factor includes elements such as the length of time it takes for legal issues to be resolved and labour legislation.

This outcome could be explained by the fact that the lack of institutional stability in Libya has negatively affected the performance of the public administration, including the country's legal institutions. A series of changes to the administrative sub-divisions of the country which was initially divided into three regions, then into ten provinces, then 13 provinces, and finally 31 provinces which led to multiple restructuring of the Courts according to the administrative sub-division, which caused the accumulation of many issues (Shirnninah, 2007).

Interviewees also indicated that fully foreign-owned companies and joint ventures alike still find it difficult to import foreign labour when appropriately skilled local labour is not available, even though Libyan investment Law permitted the entry of foreign labour when there is no local alternative. These difficulties could be due to the issue of Libya's illegal labour force of immigrants, which according to unofficial estimates exceeds two million (National Council for Planning, 2008).

Similarly, findings from the interviews conducted with almost all the foreign investors revealed that factors related to the legal system, including the length of time required to resolve legal issues, and labour legislation, still represent a significant barrier for them.

The respondents emphasised the necessity for urgent reforms in the Libyan legal system with it taking a long time (up to five years) to achieve final results in cases of litigation or enforcement of laws.

In this context, the interviewee from Company I mentioned that: "*Legislative reform should be urgently achieved"*. The General Manager of Company L added: "*Legislative stability, judiciary system reform, and speeding up the resolution of cases which often takes a long time, is a crucially important determinant for FDI"*. According to the representative of company D: "*There is a need to reform the judiciary system, especially in relation to commercial cases*". Another interviewee also noted that: "*Legislative reforms need to be undertaken, with clear and transparent rules being applied"* (Company J). Finally, the representative of Company F added: "*Liberalizing labour law in accordance with international standards is urgently required*".

An efficient, effective and fair regulatory and legal system is an important consideration in FDI decisions. It is important to note that some degree of government regulation is essential in protecting the interests of producers and consumers, and thereby ensuring the integrity and smooth functioning of the marketplace.

Legal and judicial systems that work effectively, efficiently, and fairly form the backbone of national economic and social development. National and international investors need to know that the rules they operate under will be expeditiously and fairly enforced.

Libya's overloaded court system acts as another deterrent to foreign investment. Although a well-established court system and judiciary are in place, judicial procedures tend to be costly and subject to long delays. The average commercial case lasts three years and business people run the risk of being tried, convicted and sentenced before they even know they have been charged (EU Report, 2007). A major programme of modernisation, reform and retraining is underway. In the meantime, local contractual agreements are generally secure and arbitration is often used as a more effective means than litigation to settle disputes. Briefly, there is no doubt that increased clarity and

stability of regulation, and enhanced quality and reliability of the legal system and legal protection, are required to make Libyan's investment climate more attractive to foreign investors.

7.3 Second Objective: To identify differences in locational determinant factors applied by each type of FDI in relation to company ownership, nationality and business sector

The second objective of the current study is to investigate the differences in locational determinant factors affecting FDI in different types of companies focusing on ownership (fully foreign-owned or joint venture), nationality (Western or MENA) or business sector (manufacturing or services). The hypotheses were tested as showed in section 6.5 and the results are discussed below.

7.3.1 Company Ownership

The comparison in this case focuses on the investment preference of companies having a foreigner as their major shareholder (fully foreign-owned firms) and joint venture companies which consist of a Libyan and a foreign partner. The results revealed that two factors were significantly different between these two groups of ownership at 95% confidence level, as seen in Table 7.2, were the market conditions shows positive significant the government regulation and red tape was significantly negative among these groups . Economic conditions and tax exemptions were ranked the most important factor for both groups, as these factors affect business performance and profitability, but they were considered more favorably by fully foreign-owned FDI, since they are particularly affected by both factors.

Table 7-2: **MANOVA Results by Company Ownership**

FDI Determinant Factors	p=	Foreign-Owned		Joint Venture	
		Mean	Rank	Mean	Rank
Economic Conditions	.344	4.41	1	4.26	1
Market Conditions	.000	**3.09***	6	3.86	3
Tax Exemptions	.412	4.34	2	4.24	2
Government Regulation and Red Tape	.000	**1.95***	9	2.74	8
Domestic Infrastructure	.020	2.22	8	2.51	10
Availability & Wages of Skilled Labor	.995	3.84	3	3.84	4
Availability & Wages of semi-skilled Labor	.450	3.54	4	3.37	6
R&D and Training Systems	.013	1.91	10	2.27	9
Availability Natural Resources	.232	3. 39	5	3.63	5
Financial Accessibility	.139	2.84	7	3.15	7
Legal Practice	.435	1.89	11	2.01	11

*The mean difference is significant at the .05 level.

As previously noted, Economic Conditions and Tax Exemptions were ranked as the top two factors for both groups. Market Conditions was ranked as third most important factor for joint venture companies, while the third for fully foreign-owned companies was the Availability and Wages of Skilled Labour. These results can be explained by the fact that most of the joint-venture firms that have entered the Libyan market take the form of a partnership with a local company and were attracted to target the Libyan market as a result of the privatization of food industries and other production of goods for the purpose of local market sufficiency. Skilled Labour and Semi-Skilled Labour were ranked third and fourth respectively by fully foreign-owned companies whilst joint-venture companies ranked these in sixth position. This is probably due to the fact that the latter had much better access to the local labour market and, thus, did not pay much attention to this factor.

In general, the mean scores rating for fully foreign-owned companies showed higher scores than those of their joint-venture counterparts. This revealed that fully foreign-owned FDI required more favourable incentives from host countries than joint ventures,

in order to alleviate reduce their liabilities as foreigners. Foreign investors, on the other hand, were discouraged by factors such as Government Regulation and Red Tape, Domestic Infrastructure, R&D and Training Systems, and Legal Practice viewing these as factors which increased their investment costs.

Thus, the hypothesis H1: Factors which encourage/discourage FDI in Libya differ in relation to ownership, depending on whether they are Fully Foreign-Owned or joint-venture companies, is accepted. There were two significantly different factors: Government Regulation and Red Tape, and Market Conditions.

7.3.2 Nationality

Individual mean differences were compared across two levels of nationality and all eleven locational determinant factors in order to provide more disaggregated evidence on the nature of how nationality impacted on the eleven locational factors. Companies were categorised as either MENA or Westerners (covering European and North American countries). As Table 7.3 demonstrates, the results revealed that, between these two groups of nationality, four factors were statistically significantly different. These were economic conditions (p value level of 0.000), tax exemptions (p value level of 0.000), Financial Accessibility (p value level of 0.008) and availability of natural resources (p value level of 0.004). For almost all those factors, companies from industrialised countries gave higher scores than MENA. This implied that Western investors required more investment preferences as they had to face more costs as the inevitably the risks were higher when entering into markets/countries with very different characteristics to those of their home countries.

Table 7-3: MANOVA Results for Nationality of Companies

FDI Determinant Factor	p=	MENA		Western	
		Mean	Rank	Mean	Rank
Economic Conditions	.000	**3.85***	2	4.59	1
Market Conditions	.027	**3.82**	3	3.39	6
Tax Exemptions	.000	**3.86***	1	4.52	2
Government Regulation & Red Tape	.695	2.51	8	2.42	8
Domestic Infrastructure	.501	2.42	9	2.34	9
Availability & Wages of Skilled Labor	.097	**3.73**	4	3.88	3
Availability & Wages of Semi-Skilled Labor	.788	3.48	5	3.41	5
R&D & Training Systems	.513	2.32	10	2.26	10
Availability Natural Resources	.004	**3.18***	6	3.48	4
Financial Accessibility	.008	**3.16****	7	2.90	7
Legal Practice	.834	1.93	11	1.90	11

* The mean difference is significant at the .05 level.
** The mean difference is significant at the .10 level.

In addition, the top two encouraging factors for both MENA and Westerners FDI were economic conditions and tax exemptions, since these directly affected the profitability of the companies. The market conditions factor was ranked as the third most favorable for MENA FDI, while for Westerners this was availability and wages of skilled labor. MENA viewed market conditions in Libya as another significant factor for their investment decisions, due to the importance of the fact that it has signed free trade agreements with many countries in the region and belong to the International Trade Association MENA investor's benefit from the fact that their countries of origin and Libya are quite similar in many respects, in terms of investment attitude, culture, demographics, geography, and lifestyle. Westerner's investors may ranked availability and wages of skilled labor third because they are used to different training patterns. Western countries tend to transfer their technologically know-how by using a "*job manual*", while the MENA countries prefer "*on-the-job training*". The Western approach requires more skilled individuals to grasp often complex explanations whilst on-the-job training can be delivered to unskilled labour that is ready to learn from more experienced staff.

Westerner's investors also put more emphasis on the availability and quality of natural Resources. This was because most of this FDI group were resource-seekers, aiming to change their production based on the availability of local resources (around 69% of the total Western sample). MENA FDI were not overly concerned about this, as they can easily import necessary resources from their home country, since the distances and import costs are relatively small, especially when exemptions on import duties from the region are available. The Tax Exemptions factor was statistically different between Western investors. MENA companies were not very concerned about this factor because most of the companies in the region were already exempt from import duties as a consequence of trade agreements between MENA countries.

Another factor that differed statistically to a significant degree between the two subgroups was Financial Accessibility. The MENA FDI viewed Libya's Financial as a significant factor influencing their investment decisions while Western firms did not. This is due to the fact that most of the MENA FDI took the form of joint ventures with local partners who can easily access local sources of funding, as they benefit from the government's support to domestic firms. Unsurprisingly, Legal Practice, Domestic Infrastructure, Government Regulation and Red Tape, and R&D and Training Systems were considered by both subgroups in the overall sample to be the factors which acted as the greatest discouragement for investing in Libya.

Thus, Hypothesis H2 Factors which encourage/discourage FDI in Libya differ in relation to the company's country of origin i.e. whether this is Western or MENA is accepted. There were four significantly different factors: Economic Conditions, Market Conditions, Supply and Availability of Natural Resources and Tax Exemptions.

7.3.3 Sector of Activity

As shown in Table 7.4, when locational factors of FDI were considered for different industry types, namely, manufacturing and service industries, the results revealed that between these two subgroups five factors out of eleven were statistically significantly

different (p value less than 0.05 levels). These were Economic Conditions, Market Conditions, Availability and Wages of Semi-Skilled Labor, , Availability of Natural Resources, and Financial Accessibility which appears more important for manufacturing the services. While Government Regulation and Red Tape, Domestic Infrastructure and R&D and Training Systems shows negatively significant deferent between these group. Across all those factors, manufacturing companies received higher scores than companies in the services sector did. Both groups had similar favourable factors in their top two (Economic Conditions and Tax Exemptions), which was in line with the overall sample ranking.

Table 7-4: MANOVA Results for Sector of Activity

FDI Determinants Factor	p=	Manufacturing		Services	
		Mean	Rank	Mean	Rank
Economic Conditions	.060	**4.44****	1	4.15	2
Market Conditions	.000	**4.15***	3	2.86	3
Tax Exemptions	.106	4.36	2	4.17	1
Government Regulation and Red Tape	.000	**2.83***	8	1.97	9
Domestic Infrastructure	.000	**2.68***	9	2.05	8
Availability & Wages of Skilled Labor	.271	3.88	6	3.78	5
Availability & Wages of Semi-Skilled Labor	.000	**4.00***	5	2.73	6
R&D and Training Systems	.000	**2.36***	10	1.85	10
Availability Natural Resources	.000	**4.03***	4	2.93	4
Financial Accessibility	.000	**3.66***	7	2.26	7
Legal Practice	.046	2.10	11	1.88	11

* The mean difference is significant at the .05 level.
** The mean difference is significant at the .10 level.

Companies in the services sector highlighted only three variables as the main factors underpinning their investment decision in Libya: Availability and Wages of Skilled Labour, Tax Exemptions and Economic Conditions. This was in line with the fact that service firms in general do better business in those countries which are developed with high economic growth rates and overall economic stability. While on the other hand, manufacturing companies pointed out five variables as encouraging their business which are the Skilled Labor, Tax Exemptions and Economic Conditions and they placed significantly more emphasis on Market Conditions and semi-skilled labour and financial

factor with 95% confident level. This can be explained by the fact that manufacturing industry firms generally perform well when countries have a high economic growth rate, can provide distribution channels for their goods (i.e. where there is demand) and a market for physical/tangible products.

In terms of discouraging factors, foreign companies found factors such as legal practice was viewed as the most negative factor for both subgroups. In addition, for manufacturing FDI, Domestic Infrastructure, R&D and Training Systems, Legal Practice and Government Regulation and Red Tape were considered to be major obstacles to doing business in Libya, as the manufacturing investors needed intense and reliable monitoring, and a an effective, efficient and fair legal system was needed to resolve the business issues facing their companies in an acceptable period of time, instead of waiting for several years for adjudication. For companies in the services sector, factors such as Availability and Wages of semi-skilled Labour, Availability of Natural Resources, Legal Practice, Domestic Infrastructure, and Market Conditions, were more likely to be unimportant, producing a mean score of less than 3.0, which could be interpreted as either unfavourable or unimportant, as servicing business did not rely much on these factors.

Businesses in the services sector did not require complicated accounting systems, which can easily to monitor, so they did not pay as much attention to matters such as Financial Accountability and Legal Practice. Also, they can adjust more easily adapt their services to changes in consumer behaviour, or even competitors' strategies, reflected in their unconcern about the Market Conditions factor. In sum, Hypothesis H3: Factors which encourage/discourage FDI in Libya differ in relation to the company sector of activity i.e. manufacturing or a service is accepted.

7.4 Third Objective: To assess the effects of FDI on the local economy through the linkage between foreign companies and domestic suppliers (Supplier relationships)

Respondents were asked to estimate the level of their dependency on local suppliers and to address the obstacles they faced in relation to using local suppliers. This linkage between foreign investors and local suppliers is analyzed and discussed in this section. The overall sample results are shown in Table 6.29. Nearly 27% of the respondents said they were dependent on local suppliers to provide related inputs; 23.8% of the respondents were partly dependent but nearly a half of the respondents (49%) were not dependent at all.

Given that the majority of the sample are only partly dependent on local suppliers or have no linkages with them at all, an additional follow-up question was asked to ascertain the reasons for this lack of linkage with local suppliers. The overall sample result, shown in Table 6.30, shows that 42.8% of the total number of representatives highlighted limited supply of materials in the local market while 28.6% participants referred to poor quality materials and 6.3% to the high cost of materials. A further17.4% mentioned other problems such as delays and over only 4.8% was fully satisfied with their linkage with local suppliers.

In order to explore these areas of linkage and the obstacles to dealing with local suppliers in Libya, the data was divided into two groups to investigate the differences among the groups regarding supplier linkage, as perceived by the representatives of the companies that participated in the research. This linkage was analysed as two independent variables: (1) the ownership of the companies (fully foreign-owned or joint ventures) and (2) the economic sector in which each company operates in Libya (manufacturing or services). The general findings of the analysis were weak, however, either before or after considering the effect of the two independent variables on the data, since it emerged that only fully foreign-owned company respondents in the company ownership group were more dependent on Libyan local suppliers (see Table 7.6).

These results might have been expected as the private sector in Libya an emerging sector and the quality of its products are likely to be of moderate or low quality. As explained in Chapter Three, Libya imports most of its goods and mainly exports its oil and gas

production. Its weaknesses in the export sector are mainly due to both quality and price factors. Foreign companies need intermediate inputs, during their operations, which could be obtained from foreign markets (imports) or from the host country's local producers. One of the main factors for a company investing abroad is cost reduction, mainly by depending on the host country's' production factors. Therefore, foreign companies only seek to import inputs if the local market is not able to supply these. In this case, local suppliers are incapable of producing what is required which leads to an increase in the dependency of foreign companies on imported inputs rather than local ones.

7.4.1 Company ownership and local supplier

To examine whether or not there was a relationship between the use of local suppliers and type of company ownership, a Chi-square test was used. As can be seen from Table 7.5, the chi-square value for availability of local suppliers is 14.987 with one degree of freedom, 17.005 for difficulties in relation to local suppliers with three degrees of freedom, and 0.029 for company's target markets with one degree of freedom. On the other hand, the p value is 0.005 for dependency on local suppliers, .002 for difficulties in relation to local suppliers, and 0.865 for the company's market strategy. Since the observed p value is less than alpha (alpha = 0.05), in the case of dependency on local suppliers, the results were considered statistically significant. Thus, in order to give further meaning to the findings, cross-tabulation was utilized.

Table 7-5: Chi-Square Test: Company Ownership and Dependency on Local Suppliers

	Dependence on Local Suppliers	Difficulties with Local Suppliers	company's target markets
Chi-Square[a b]	14.98	17.005	.029
Df	1	3	1
Asymp. Sig.	.005	.002	.865

[a] 0 cells (.0%) have expected frequencies less than 5. The minimum expected cell frequency is 34.0.
[b] 0 cells (.0%) have expected frequencies less than 5. The minimum expected cell frequency is 13.6.

As Chapter Six demonstrated, more than quarter of the fully foreign-owned companies and joint ventures operating in Libya depend on local suppliers for the required raw materials, particularly fully foreign-owned companies.

The use of local suppliers varies according to the type of company ownership. Table 7.6 shows how the ownership of the foreign companies (fully foreign-owned or joint ventures) related to their use of the available local suppliers in terms of participant perceptions.

Table 7-6: **Cross Tabulation of Company Ownership and Dependence on Local Suppliers**

Ownership	Quantity	Dependence on Local Suppliers			Total
		Mainly	Partly	None	
Fully Foreign-Owned	Number	11	5	7	23
	%	47.8	21.7	30.4	100.0
Joint-Venture	Number	6	10	24	40
	%	15.0	25.0	60.0	100.0
Total	Number	17	15	31	63
	%	27.0	23.8	47.0	100.0

Table 7.6 highlights the relationship between company ownership and use of local supplier. From the information in the table, it is apparent that joint venture companies make less use of local suppliers compared with fully foreign-owned companies: 60.0%, 30% respectively. However, in general, as indicated in the results above, foreign investors as a whole were 53% dependent or partly depend on local suppliers while 47% were totally not depend on local suppliers. The surprising result is that the fully foreign-owned companies were more dependent on local suppliers than joint-venture companies. This result may be caused by the fact that most of the joint-venture companies are based in the food industry and services which may mean they are market-seeking FDI while the fully foreign-owned companies are resource-seeking.

Table 7.7 indicates that there is a relationship between company ownership and the difficulties companies face in obtaining input from local suppliers. From the findings, it can be established that the main problem for both fully foreign-owned and joint-venture

companies is the limited supply of materials (42.8%) followed by the poor quality of the materials provided by local supplier. The representatives of fully foreign-owned companies indicated that the main problem they faced when dealing with local suppliers was insufficient quantity (65.2%), compared with 30.0% for joint-venture companies. The poor quality of materials supplied rated as second most problematic issue according to respondents with 26.1% for fully foreign-owned and 30.0% for joint venture companies. The high cost of local materials and other services such as the delay in delivery is considered as the third main problem as identified by respondents, with 27.5% of the joint-venture company representatives considering this to be a problem, while this was not a problem with the fully foreign-owned companies as it was indicted 0% in the table 7.7.

Table 7-7: **Cross Tabulation of Company Ownership and Difficulties with Local Suppliers**

Ownerships	Quantity	Difficulties with Local Suppliers					**Total**
		None	Limited Supply Of Materials	Inadequate Quality	Expensive Materials	Other	
Fully foreign-owned	Number	2	15	6	0	0	23
	%	8.7	65.2	26.1	0.0	0.0	100.0
Joint venture	Number	1	12	12	4	11	40
	%	2.5	30.0	30.0	10.0	27.5	100.0
TOTAL	Number	3	27	18	4	11	63
	%	4.8	42.8	28.6	6.3	17.5	100.0

However, it is important to note that only 4.8% of the representatives within both fully foreign-owned and joint-venture companies appear to be content with the materials from local suppliers in terms of quantity, price and quality.

7.4.2 Company Sector of Activity and Local Suppliers

Table 7.8 shows that the chi-square value for dependence on local suppliers was 0.68 with one degree of freedom, while chi-square value for difficulties in relation to local

suppliers was 21.191 with four degree of freedom and finally 1.326 for company strategy on the market serviced with one degree of freedom. The p values are 0.409 for dependence on local suppliers, .000 for difficulties with local suppliers and 0.249 for the company strategy on the market serviced. Since, the observed p value is less than alpha (alpha = 0.05), in the case of difficulties with local suppliers, the results were considered statistically significant. However, in order to give further meaning to the findings, cross-tabulation was carried out.

Table 7-8: Chi-square test: Company Sector of Activity and Dependence on Local Suppliers

	Dependence on Local Suppliers	Difficulties with Local Suppliers	Company Strategy on Market Serviced
Chi-Square [a,b]	0.681	21.191	1.326
Df	1	4	1
Asymp. Sig.	.409	.000	.249

[a] 0 cells (.0%) have expected frequencies less than 5. The minimum expected cell frequency is 34.0.
[b] 0 cells (.0%) have expected frequencies less than 5. The minimum expected cell frequency is 13.6.

These results indicate that there is no significant difference between all the groups regarding company strategy (i.e. whether targeting the local market or exporting). In other words, all the companies serviced the local market (i.e. no statistically significant differences exist between the two categories of the groups in terms of target market).

Table 7.9 indicates the relationship between both sectors and the type of difficulties that face companies in relation to local suppliers. The representatives had to choose one from a series of options to describe the type of main obstacles facing them in relation to using local suppliers. From the results, it is apparent that the scarcity of local suppliers constitutes a major problem for manufacturing companies in the opinion of 60.0% of the respondents from these companies. Delays in products/materials supplied was ranked second in the opinion of 20.0% of manufacturing respondents, while 11.4% complain about the poor quality of the materials provided by local suppliers. Overall, only 8.6% were satisfied.

As far as the services sector is concerned, the main problem identified is the inadequate quality of materials provided by local suppliers (50.0%), while the limited supply of materials came second, attracting 21.4% of respondent complaints. The high price of materials and other problems such as supplier delays and a lack of communication between suppliers and clients were ranked third (14.3%).

Table 7-9: Cross Tabulation of Sector of Activities and Difficulties with Local Suppliers

Sector	Quantity	Difficulties with Local Suppliers					**Total**
		None	Limited Supply Of Materials	Inadequate Quality	Expensive Materials	Other	
Manufacturing	Number	3	21	4	0	7	35
	%	8.6	60.0	11.4	0.0	20.0	100.0
Services	Number	0	6	14	4	4	28
	%	0.0	21.4	50.0	14.3	14.3	100.0
TOTAL	Number	3	27	18	4	11	63
	%	4.8	42.9	28.6	6.3	17.5	100.0

It can also be concluded from the findings that respondents from both sectors face fewer difficulties in relation to cost (6.3%), with 42.9% and 28.6% related to the limited supply of materials and inadequate quality respectively.

7.5 Interview Findings regarding Supplier Relationships

Based on the interview findings regarding relationships with local suppliers, it can be concluded that foreign companies in Libya consider local suppliers as a major element in the success of their investment. They are also aware of the value of developing relationships with domestic suppliers, and capability, commitment to product and service quality and value for money are the top reasons for selecting a supplier.

The interview findings revealed that 11 of the 13 or 84.6% of participants reported that the supplier's capability and commitment to product and service quality are important for their companies. Six of the 11 interviewees talked about their standards when choosing

suppliers. They mentioned that they depend on supplier reputation and experience. The Deputy Director General of company L stated:

> *Our company is aware of the role of the suppliers in the production process and our company's overall development. So we rely on the dependable suppliers who have the ability to supply our company with quality products and services. From this perspective, our company rank criteria such as experience and good reputation in order to select the best suppliers, and to create a long-term relationship with our suppliers.*

The General Director of Company C noted:

> *The local private sector alone is incapable of creating the possible alternatives at this time as it is currently not in a position to provide international companies with competitive inputs. This due to the numerous problems associated with this sector, such as lack of technical know-how, mismanagement, lack of skilled labor, and inadequate capital.*

Surprisingly, the material inputs sourced within the local economy are generally provided by foreign companies working in the local economy or in some cases from state-owned businesses. There is very little collaboration with other Libyan privately-owned companies. In general, participant companies do not source from domestic suppliers for various reasons including limited range of suppliers or in some cases the material inputs are not available locally or if available, are of inferior quality and/or generally more expensive. Also, in some cases, the Head Office, parent company or customer tells factory managers to buy from specific suppliers which are generally located abroad.

Almost all the foreign companies sold their products on the local markets. Only three of the 13 respondents that answered this question reported selling their products in domestic market and other regional markets (Companies E, H, and L). Two of these companies (E, L) state that no more than 30% of their company production is exported.

In short, the domestic private sector could act as an obstacle for host countries hoping to attract FDI. In this case, Libyan's private sector was considered to be weak, and this is a problem both for FDI and for the Libyan economy in general. That is why the availability and quality of local products is considered by the majority of the sample as either limited or low. Product quality, which is very important for the foreign companies, is still lower in Libya than the standard available elsewhere, and the prices were considered high.

If the domestic private sector was strong enough, it could supply foreign companies with good quality components, which would offset their dependence on imported ones. That is certainly the main cause for the widening gap between exports and imports in non-oil exports in Libyan during the last decades. Alfaro (2004) found that the lack of an adequately developed private sector might present a problem. A general problem of this kind often brings specific problems in its wake, such as the lack of good suppliers or good partners. This was reinforced by a number of participants during the interviews.

Challenges and Difficulties Facing the Public Authorities: The Need for a General Strategy to Improve the Business Environment

The senior government officials who were interviewed emphasised that, despite the short period for which FDI had existed, the PIB had attracted a great deal of FDI from many different nationalities into all Libya's economic sectors over the last decade. They were aware, however, that the investment climate in Libya is not yet ready to compete with other countries in the region. Before the political changes that took place in 2011, there was a restricted political system in the country which allowed only certain investments to be made to serve political interests. After these political changes, the situation was more worsen due to the poor security issues. According to the Head of Research and Planning Department at PIB:

> *The previous period proved that Libya was a unspoiled economy, rich in natural resources, which prompted many foreign companies to invest in various economic sectors.*

Similarly, the Deputy Director of PIB argues that:

> *Investors are generally attracted by several factors, such as economic stability and policies associated with FDI and they are looking for a guarantee of continuity and success from their investment and the size of revenue they expect from this investment is appropriate in the Libyan context, but the impact of the security situation, particularly after 2011, cannot be ignored.*

In the opinion of most interviewees, the biggest challenge facing the investment authorities is to find an alternative for oil as the mainstay of the Libyan economy. Thus, adopting a diversification policy to reduce Libya's economic dependence on oil is considered to be of key importance. In this context, the government officials believe that in order to decrease the pressure on budgetary resources and reduce spending on economic activities, the government should invest in local resources to enhance productivity which would lead to a dynamic, free-market economy. As a result, this might create new jobs opportunities which would eventually increase the rate of employer productivity but this is not the case, as indicated by the General Director of company C:

> *In fact, a future clear investment plan to reduce the Libyan economy's dependence on oil is missing.*

Another obstacle highlighted by most of the government officials was the failure of the public administration to implement its strategy to attract more FDI. They referred to the failure to launch the one-window policy because this presented a major challenge in coordinating between various Libyan authorities and institutions in different areas, particularly those associated with taxation, customs, and other business-related services. The Head of the Research and Planning Department expressed his sense of frustration:

> *The lack of coordination among government bodies goes beyond the one-window policy to include the establishment of the investment scheme. For example: a number of the provinces have not yet provided the Investment Board with their*

plans in relation to their industrial areas, because these plans are non-existent in most provinces. This makes it a more difficult task for the General Board for Industrial Areas to allocate such areas for foreign investors.

The interviewees confirm that no formal strategy planning was available from the government in relation to various aspects of FDI. However, the Law for the Promotion of Investment of Foreign Capital in Libya has defined the areas open to investment activities. These include all sectors apart from oil and gas. The Law allows all sizes of company to invest as long as they meet the minimum capital requirements of LYD 5 million in the case of independent foreign investment or LYD 2 million in the case of joint foreign and local companies. However, the Head of the Research and Planning Department argued that:

The general tendency during the last five years has been for encouraging partnerships between foreign and local investors by facilitating the procedures for joint projects and facilitating technology transfer to local firms. In addition, the Foreign Investment Law has provided tax exemptions to those projects that contribute to the development of local products, feature food security programmes, and use advanced technology.

The Director of Investment Management added:

The implementation of the one-window policy combined with the simplification of procedures for dealing with FDI projects, improving the coordination between the different authorities and institutions in relation to foreign investment, and allocating well-planned investment sites should constitute the essence of the strategies for attracting more FDI into the country.

The role of the PIB in this regard is to seek to encourage foreign investors and work to provide them with better benefits and exemptions in the field of investment. They are also trying to persuade the authorities concerned to amend some laws and regulations and to revise these in accordance with recent developments to help increase the level of

competition in this area. They should focus on the importance of foreign investment and associated features so that the State will not only implement projects and transfer of capital funds, but rather import expertise, technologies and successful experiences in any field.

The interviewees disclosed that the laws and regulations that encourage investment such as the one-window policy or tax exemptions have become one of the essentials to attract FDI. In order to overcome the barriers and affectively compete with the neighbouring countries Libya should adopt long-term investment projects lasting for decades. In this case, for example, the Libyan state would bear 15% or 20% of the cost of the project, thereby encouraging the investor and making a big difference, which would allow Libya to compete with neighbouring countries.

With regard to the future expectations regarding FDI in Libya, in general the perception of respondents was positive but they were concerned about the security issues that were mentioned previously. The Director of Investment Management commented:

> *From my point of view, the future of foreign investment in Libya is promising, in spite of all the challenges and difficulties, if we are able to come through all this and create an investment climate that meets the expectations of investors and supports and encourages investment projects and forges ahead, upgrading our services and depending on the country's geographical location and its tremendous natural resources. Even the current obstacles, such as infrastructure and financial services, can be considered to be opportunities for other investors to develop these sectors, but everything depends on the stability of the country's political situation.*

7.6 Further Comments from Interviewees

Respondents were also asked if they wished to add any further comments and the majority focused their responses on the urgent need for carrying out reforms of the Libyan administrative system, voicing their concerns about the crucial importance of this.

Libya's location was another advantageous factor that had considerable impact on decisions to invest there in the opinion of foreign interviewees. Most the interviewees from fully foreign-owned companies indicated that the country's geographical location had positively influenced their investment decision. For some, it was the lack of distance between their home country and Libya, while others referred to its proximity to major international markets. In this regard, the representative of company G stated:

> *When we decided to invest overseas, we first reviewed the company's strategies in investing internationally; then we studied what host countries have that could help us to achieve our investments goals. Finally, the geographical location of the host country can be crucial factor in taking the investment decision. As a result, we consider Libya geographical location has had a significant impact on the company's investment decision.*

During the interviews, respondents from some companies voiced their concerns about internal security issues in Libya. Representatives from companies G, D, L, F and C mentioned that these had affected them negatively. Terrorist attacks impact negatively on Libya's attraction to FDI, particularly in the east of the country.

Generally, foreign companies were positive about the future, because of the improvements and reforms they had witnessed during the last decade. However, they believed that the success of failure of FD1 would be conditioned by the continuation of economic, administrative, legal, and other reforms. Solving local and regional political problems and would create a less uncertain and more attractive investment climate in the MENA countries, and in turn, would encourage more foreign companies to invest in Libya.

Senior government officials were aware that the coordination between different government departments is lacking in most vital matters and that the exchange of information is ineffective: the use of internet and other forms of electronic

communication are scarce or even non-existent. This justifies the efforts that have to be made to achieve the e-government in order to boost economic efficiency.

7.7 Conclusion

This chapter has presented and analysed the findings of the data collected by means of the questionnaires and in depth interviews. It can be concluded from the analysis of the objective findings that most representatives considered Economic Conditions, Market Conditions, Tax Exemptions, Human Capital (skilled and unskilled) and Natural Resources as encouraging factors at varying levels, together with the quality and availability of economic resources in the Libyan economy. However, it is also true that many of the respondents faced difficulties in relation to using those resources.

In short, most fully foreign-owned and joint-venture companies face some difficulties in the Libyan investment climate. The results indicate that legal obstacles were the most problematic followed by bureaucratic procedures, Domestic Infrastructure, the training system and, to a lesser extent, financial obstacles. The findings show that the majority of those involved are unsatisfied with a number of the legal issues as mentioned previously.

The results of the semi-structured interviews also revealed that investor concerns about proposed policies to improve the inwards flow of FDI vary. They suggest that simplifying administrative procedures, improving financial services and the infrastructure should have top priority. With regard to the second objective, findings show that there are differences in perceptions regarding location factors depending on the type of FDI, related to nationality, ownership and industrial activity sector.

The third objective aimed to explore FDI linkage with domestic suppliers and it was found that there is a lack of linkage between FDI and domestic suppliers. In general, company interviewees do not source from Libyan suppliers for various reasons including limited availability of suppliers or material inputs and concerns about inferior quality and/or cost.

Chapter 8

Conclusion and Recommendations

8.1 Introduction

In Libya, the encouragement of foreign direct investment (FDI) is viewed by policy-makers as a primary means for diversifying the economy and improving the participation of the private sector in the economy. Currently, the non-oil sectors account for only about one-third of Libyan GDP, so FDI is seen as an important way to reduce the heavy reliance on oil revenues. The attraction of foreign investment is achieved by focusing on those factors that affect the foreign firm's decisions to invest in Libya, which at the micro and macroeconomic levels include such things as the economic situation, market situation, labour wages, infrastructure and institutional quality of the host economy, and the characteristics of the source of FDI. The purpose of this thesis is to explore these factors by examining the Libyan location factors and the role of government policies and incentives in influencing FDI inflows into Libya. Additionally, this thesis will assess the linkage between FDI and the Libyan domestic suppliers. Ultimately, the aim is to help to provide a better understanding of the important determinants and impact of FDI in order to enhance the level of foreign investment in the Libyan economy.

In addition to the introduction and concluding chapters, the thesis has been organized into two parts, containing six chapters. The literature review on the determinants of FDI from theoretical perspectives is discussed in Chapter 2 and based on the findings of this review, a theoretical framework was built to help to identify the factors that may influence the foreign company's decisions to invest in Libya. The determinants of FDI from an empirical perspective are discussed in Chapter 3. Chapter 4 discusses the general geographical, political, social and economic background of Libya, including the legislation in relation to FDI. Chapters 5 to 7, which make up the second part of the thesis, contain the empirical part of the study and represent its three main contributions. The adopted methodology of the study is presented in Chapter 5, which adopted a survey

questionnaire for primary data collection targeting representatives of a sample of 74 fully foreign-owned and joint-venture companies and supplemented by a total of 20 depth interviews. 11 interviews targeted the questionnaires' sample and the other 7 interviews were conducted with Libyan senior officials to gain a more in-depth understanding of the research issues. Chapter 6 analyses the determinants of incoming FDI and examines the linkage of FDI with domestic suppliers, utilising descriptive statistics (e.g. means and percentage) and advanced statistical techniques including PCA, MANOVA, Chi-square, cross-tabulation and the thematic approach which was applied to analyse the interview data. Finally, Chapter 7 discussed the research findings.

In this chapter the thesis is concluded. Section 8.2 summarizes and draws out the findings of the three analyses, covering the determinants of incoming FDI; differences in various types of FDI views regarding host country locational factors; and the linkage between FDI and domestic suppliers. Section 8.3 highlights the study's contributions and section 8.4 presents the overall conclusions, outlining policy implications and recommendations. Finally, section 8.5 discusses some limitations of the study, including the data, and suggests possible areas for future research.

The next section summarises the key results which emerged from the analysis of the statistical data and the interviews. This is followed by a discussion of the original research contribution made by this study. A series of recommendations derived from these findings are then presented, and the chapter concludes by identifying the limitations of the study and suggesting future research directions.

8.2 Summary of Findings

This section highlights the key research findings that were revealed in chapters Six and Seven, summarising these in relation to the research objectives.

8.2.1 Findings Related to Factors which Encourage or Discourage FDI in Libya

In line with the first research objective (to identify those factors which are most likely to encourage and to discourage FDI inflows into Libya), the study's findings revealed that

the most important locational determinants which encouraged FDI in Libya were economic conditions, tax exemptions, human capital, market conditions, and natural resources as well as the geographical location advantage. Therefore, the Libyan investment authorities (PIB) should focus on these factors as a priority for attracting FDI. A comparison of the incentives identified by company representatives with those already provided by the PIB showed that one of these was currently provided, namely, tax exemptions. These included exemptions from corporate tax, from import duties on imported raw materials and machinery; and exemption from withholding tax on dividend pay-outs to foreign parent companies.

8.2.1.1 Economic Conditions

The results of this study revealed that the main encouraging locational determinants for FDI inflows into Libya were economic conditions. This factor referred to economic indicators such as growth rate of GDP, inflation rate, the comparative stability of the Libyan currency, privatization procedures and extent of government intervention in the economy used as indicators of economy liberalization. Libya's economic conditions were considered favourable, compared to those of its neighbouring countries. In addition, just a few years after the ending of UN sanctions in 1999, the Libyan dinar (LYD) was considered stable, ranging from LYD 1.25-1.30 against US$ 1, which enabled foreign investors to manage their profit or return on investment easily, as they did not have to pay for currency exchange management.

8.2.1.2 Market Conditions

Another key result emerging from this study is that market conditions are of significant interest to the foreign companies working in Libya. Although the Libyan market is small in terms of population (just about six million in 2012) and GDP (approximately LYD 105 billion in 2010); demand in this country is classified as high since the economy is expanding due to the high rates of both population growth (1.8% per annum) and economic growth (6.0% per annum).

8.2.1.3 Tax Exemptions

As the study shows, tax exemptions including tax holidays, tariff concessions, and corporate tax are considered to have a great influence on inward FDI location decisions by foreign companies. However, although general attitudes are positive for this factor, exemptions are always conditional and the discretionary decision relating to them is taken by a public employee, meaning that foreign companies must cope with high levels of bureaucracy to benefit from these incentives.

8.2.1.4 Human Resources

The field study showed that the quality and wage levels of human resources in terms of skilled and semi-skilled workers were important factors in the views of the majority of the company's representatives. However, companies face difficulties associated with employment, particularly in relation to the complex procedures of immigration laws for importing foreign labour, which is necessary when the local supply of skilled labour is inadequate.

8.2.1.5 Natural Resources

The foreign company representatives considered the abundance of natural resources in Libya as an important factor when making their investment decisions. However, the interview analysis suggested that there is a degree of mismanagement in relation to natural resources. This is due to the fact that very limited research has been conducted in order to incorporate these resources in an investment map which would mean that projects could be located close to those sites where these materials are produced, however, these are currently under-utilized.

It is recommended that a specialised market for Libya's natural resources should be created, supported by the relevant bodies to ensure the quality of these resources. In addition, the sectors involved with these materials, such as the food industry, cement and construction industry, petrochemicals, glass and paper industries should be commercially promoted for FDI. Also, an effective strategy including an investment map should be

adopted and must be regularly reviewed. This map should be considered an important tool to help the process of organising investment in natural resources by locating industrial estates near to the sites of production of these resources, and their potential markets.

8.2.1.6 Geographical Location Advantage

This factor was not measured in the questionnaire but emerged from the interview process and was mentioned by eight company representatives. The researcher concludes that Libya's geographical location was considered to be another factor that influenced investor decisions.

A summary of the major findings of the interviews with foreign investors and senior government officials regarding locational factors revealed that there are some differences in the viewpoints expressed by these two groups. This indicated that when making their investment decisions, foreign investors do not rate some locational incentives as being as attractive as government officials may have imagined.

Besides attempting to identify those factors which encouraged FDI, this research also considered those factors that might act as a deterrent to FDI investors in the Libyan context. These unfavourable factors were: undeveloped domestic infrastructure, R&D, training systems, financial accessibility, legal practice, government regulation and red tape. This implied that the Libyan government should not pay only attention to attracting investors with encouraging factors, but should also focus on remedying those issues which acted as discouraging factors.

8.2.1.7 Government Regulation and Red Tape

The study found that company representatives considered the instability of Libya's public institutions and ineffective regulations as another problem, with complaints mainly relating to land ownership and bureaucracy. Multiple government bodies are often involved in administrative processes and a lack of coordination amongst these tends to increase the amount of documentation and waiting time required.

The Libyan government must pay more attention to reducing bureaucracy and red tape in order to improve domestic infrastructure and minimize delays and corruption, both of which were considered to be uncontrollable business costs for FDI. If these costs are high, investors will not take the risk, as the net return to them may not achieve the targeted levels, leading to a loss of opportunity. Furthermore, the Libyan government should pay more attention to improving the enforcement of property and equity ownership law. Enhancing this enforcement will provide a measure of reassurance to foreign investors that their property rights will be reasonably protected, encouraging re-investment.

8.2.1.8 Domestic Infrastructure including R&D and Training Systems

Both questionnaire and interview results highlight that dissatisfaction exists among company representatives with regard to the poor infrastructure services in Libya, this includes telecommunications, transportation and electricity supply. Furthermore, foreign investors complained about other infrastructure services including availability, quality and costs of training centers in Libya.

Integrated development of infrastructure should be the main aim of the new development strategy. It is important to complete and improve the infrastructure services particularly in the area of power supply. It is essential that the Libyan national grid for electric power be connected to stable networks to avoid power cuts which cause damage that far exceeds the connection costs. Information technology and e-government are crucial for the development of the country and to make it attractive for FDI. This framework is possible given the technological advances which have taken place in the area of telecommunications allowing the uninhibited flow of information and maximizing the benefits of the information revolution.

8.2.1.9 Financial Accessibility

The results from the questionnaire analysis indicated that company respondents were unimpressed by Libya's banking services which they describe as unsatisfactory. Fully

foreign-owned firms also complained about lack of access to local sources of funding, and Libyan accounting and auditing procedures. The fact that the six main banks in Libya are still owned by the public sector and that they are yet to embrace advanced technology of the kind readily available elsewhere could be the main reason for the poor performance of the banking sector.

Financial services must be reformed to create an efficient and progressive financial industry. There is a need to improve the infrastructure of the financial services by introducing electronic banking and financial services, essential for ensuring capital growth and financial development. Furthermore, in the short-term, it is also crucial to allow Islamic financial institutions to play a role in the Libyan market, which would enhance the financial base.

8.2.1.10 Legal Practice

The findings of the study show that almost all of the foreign firm representatives consider Libya's legal system to be poor, the most discouraging aspects of this being the slowness of the judicial system and the country's complicated labour legislation. The negative perceptions of legal practice in Libya emphasizes that it must focus more on developing its accounting and legal systems, and enhancing corporate governance, in order to ensure transparency among FDI partners. This would result in high trust and, in turn, further investment.

8.2.1.11 Internal Security

This factor was not measured in the questionnaire but it did emerge from the interview process and was mentioned by five managers. It can be concluded that the current state of the country's internal security is considered to be another factor which may discourage FDI inflow to Libya.

8.2.2 Second objective:

For the purposes of the second research objective (to identify differences in locational determinant factors that influenced each type of FDI), the results show that:

8.2.2.1 Ownership (Joint Venture and Fully Foreign-Owned)

When the data was divided by ownership into two groups (Joint Venture and Fully Foreign-Owned), these two sub-groups of foreign investors only had different views on two factors; market conditions and financial associability, which were significantly different at a 95% confidence level. It can be concluded that most of the joint-venture firms that have entered the Libyan market take the form of a partnership with a local company and were attracted to target the Libyan market as a result of the privatization of food industries and other production of goods for the purpose of local market sufficiency.

Factors such as government regulation and red tape, domestic infrastructure, R&D and training systems, and legal practice were viewed by both subgroups as factors which increased their investment costs. The financial factor was reported as an encouraging factor by joint venture companies as these firms had easier to access to local sources of funds, while this factor carried less weight in the view of fully foreign-owned firms. The remaining factors were important for both subgroups.

8.2.2.2 Nationality Groups (MENA and Westerners)

Based on nationality group (MENA and Westerners), each subgroup reported different preferred determinant factors. Five factors were significantly different at a 95% confidence level, namely, economic conditions, including, tax exemptions, market conditions, natural resources and financial accessibility. The other factor, skilled labour, was different at a 90% confidence level. The Western FDI company typically places more emphasis on factors such as economic conditions, market conditions, skilled labour and natural resources than the MENA FDI companies. It may be concluded that Western firms generally required stronger preference factors than MENA because Westerners may

have to bear higher costs derived from distance from home markets, physical distance, culture and demographic differences, and so on.

The top three encouraging factors for MENA firms are: economic conditions, market condition and tax exemptions. The first two were shared by Westerners, while the third ranked factor for Western FDI was skilled labour. MENA companies felt that market conditions and financial factors were important because most of the firms from this region were market-seeking food industries and joint-ventures rather than resources-seeking. Also these firm's benefit from both ventures; with a local partner to access local sources of funds, and free trade agreements between the region's countries, they can export and import their production and raw materials free of tax in region. On the other hand, Westerners viewed the availability of skilled labour as an encouraging factor because they were concerned about complex labour legislation laws. Importing overseas labour would need complex procedures implying time and money for them, and could affect their final return on investment.

With regard to discouraging factors, both took into account government regulations and red tape, domestic infrastructure including the training system, and legal practices which were the factors that were judged as acting as a disincentive to business performance for both sub-groups.

8.2.2.3 Industry Type

Under the results based on industry type group (Manufacturing and Services), the most important factors for both manufacturing and services groups were economic conditions, market conditions and tax exemptions. However, five factors showed significant differences between the two groups, namely, the economic conditions, market condition, semi-skilled labour, natural resources and financial accessibility.

The manufacturing companies considered six factors as being important, namely: semi-skilled labour, tax exemptions, market conditions, natural resources, financial accessibility and economic conditions, whilst in the view of investors from the services

sector, only three were reported as having particular importance. These were economic conditions, tax exemptions, and skilled labour. The manufacturing companies considered natural resources and semi-skilled labour as encouraging factors, as the industry activities were more reliant on natural resources and semi-skilled labour. Market conditions were also viewed as more important for manufacturers than service providers; given the huge amount of investment required, incorrect calculations and forecasts relating to market conditions, such as trends and the size of the market, and degree of market competition, could result in high amounts of loss. On the other hand, services FDI firms ranked economic conditions and skilled labour as more important than the manufacturers did, as these factors determine the market size and potential for growth.

With regard to discouraging factors, manufacturers disliked government regulations and red tape, legal practices, domestic infrastructure and training systems, while service firms shared the same view on these barriers and several other factors such as semi-skilled labour, natural resources, and market conditions. This may be because services firms had no involvement in the labour and raw material factors, and due to the small amount of investment which this sector requires, their losses were limited.

The Libyan government needs to prioritize which characteristics of FDI it wishes to focus on, e.g. specific industrial sectors, nationality, etc., and produce incentives which are directly targeted at this FDI. If these characteristics change, the government also needs to change the incentives that are offered accordingly.

In conclusion, as evidenced by the research results described above, the different types of FDI have different preferences in terms of their locational determinant factors. Thus, they each require different incentives to encourage their investment. However, it is recommended to policy-makers that as different types of FDI viewed each locational determinant factor differently, incentives provided by the government should be restricted to and designed to target specific types of FDI as these incentives can be managed and controlled by the host government, in order to gain the desired benefits and prevent spill-over effects.

8.2.3 Third objective: Exploring FDI Linkages with Domestic Suppliers

There appeared to be rather poor linkage between FDI and domestic suppliers in both fully foreign-owned companies and joint ventures, and also in both the industrial sectors studied. In most cases, even when materials are sourced from the Libyan market, the suppliers of these materials are foreign-owned firms, following their main customer. This suggests an important difference between foreign firms working in the local market and domestic Libyan firms.

Even when materials are available from Libyan suppliers (which is rarely the case), both types of company appear to avoid sourcing these inputs because they are generally of inadequate quality and more costly than other alternatives; in some cases there is mismanagement by the supplier. However the reasons for this situation differ somewhat in the case of each type of FDI. In the industry group (manufacturing and services), the foreign investors in the services sector still rely on their traditional suppliers from abroad because many of the materials they need are simply not produced by Libyan companies. Even when they are available, Libyan-made components are commonly of lower quality and often more expensive than imported equivalents. The manufacturing sector blames the difficulties of using domestic suppliers mainly on their limitations and low quality service.

With regard to ownership (fully foreign-owned companies and joint ventures), the results indicate that fully foreign-owned companies were more dependent on local suppliers than joint-venture companies because most of the foreign-owned companies are resource-seeking and these are available locally, but the suppliers are foreign companies operating in the Libyan market. The joint-venture companies appear to be less dependent on suppliers from the Libyan market due to the fact that most of the joint-venture companies are based in the food industry which is dependent on imported inputs.

The two groups faced different difficulties in obtaining input from local suppliers. The fully foreign-owned companies indicated that the main problems they faced were

insufficient quantity and poor quality when input was available. Joint-venture companies claimed that their difficulties related to inadequate quality, delays in delivery and higher prices compared to other alternatives.

These results indicate that there is no significant difference between all the groups regarding company strategy (i.e. whether targeting the local market or exporting). In other words, all the companies serviced the local market (i.e. no statistically significant differences exist between the two categories of groups in terms of the target market).
The lack of linkage may not necessarily reflect the choice of foreign companies, but may be due to a lack of local alternatives for suppliers. Thus, expansion of the private sector is essential to make the Libyan economy attractive to FDI. Extending the ownership base of economic activity by means of a policy aimed at opening the doors to the private sector, both local and foreign, to diversify income and create more jobs, has to be part of the new development strategy. This requires the development of appropriate policies and measures for stimulating the private sector.

8.3 Contributions to knowledge

Over the last few decades, research in developed and developing countries has shown that the relationship between the host country's economic stability and encouragement policies and foreign capital inflows is positive, implying that countries with low levels of economic risk and encouraging policies will attract more FDI than countries with high levels of risk and less promoting policies. In particular, countries with more encouraging policies are more likely to attract whole investments than those with high risk, suggesting that policies that improve economic stability and stimulate the FDI firm's will potentially make the country more attractive. Although the motivation for FDI has been determined by the host country's location factors as important elements in the international business literature, the previous studies considered mostly the overall relationship between FDI inflows and location factors. The review of the literature also shows that there are very limited studies that have examined the influence of FDI characteristics such as foreign company nationality, industrial sector, and ownership on location factors. This research

therefore aims to identify the relationship between each type of investment and the location factors. The research selects Libya as a case for this exploration which is a country still at a transition stage that aims to move from a central economy to a more free market economy and relative openness. Such exploration provides unique insights into how FDI determinates issues different to those of developed countries. To examine such issues, the research has utilized both quantitative and qualitative data on FDI from foreign companies, the Libyan Ministry of Economic, the Ministry of Industry, GPC and PIB. It is the first time these data has been gathered and used for an academic study which in itself is a major contribution to the study. More precisely, the main contribution of this research is presented as follows:

- The research findings confirmed that the preferences of each type of FDI such as nationality (Western or MENA), industry type (manufacturing or services), and ownership (fully foreign-owned or joint venture), regarding location factors were different from the overall direct relationship. This adds to the existing body of knowledge, and clearly reflects the third element of Dunning's (1979) theory (host country's locational factors), since it was found that each type of FDI viewed these factors differently as shown below. This finding also provides more accuracy and new evidence for the (L) part of Dunning's theory, as this part of the theory has been tested and accepted by previous studies as mentioned in chapter three.
- Most of the studies on FDI have been conducted in either developed and developing countries used cross-sectional studies; while single country studies considering FDI in emerging and transitional economies are still scarce, particularly in the MENA region (see Chapter Three). Moreover, previous studies of FDI in developing countries presented their findings without the help of an appropriate theoretical framework and in some studies used Dunning's theory approach, but they focused only on overall determinants and effect of FDI (see Chapter Three).

- This study expands on previous empirical studies of FDI by examining a wide range of host country variables, including economic and market situation, investment policies, utilities and facilities influence on inflows of each type of FDI.
- As mentioned earlier, few studies of FDI locational determinants in Libya have been conducted. This study adds to the existing body of knowledge in this academic area, by identifying in detail those factors which are most likely to encourage or discourage FDI in Libya as a transition country, particularly after later economic reforms and political changes.
- This research used questionnaires and interviews to collect primary data in order to gain in-depth understanding of determinants, obstacles and effects of inflowing FDI in the context of Libya. This is considered a contribution to knowledge since every time a social scientist collects primary data, a new contribution to the overall social knowledge is made (Hox and Boeije, 2005).
- Very few studies have recognized the possible linkages between FDI and domestic suppliers, which represent a challenge for host countries in developing their private sector and maximizing the benefits of FDI. Therefore, this study helps to fill this gap in the existing literature. Nevertheless, in the case of Libya, the research found only a limited relationship between FDI and domestic suppliers. This thesis of course cannot claim to offer a definitive judgment on the importance of FDI, but rather it should be viewed as a further step in this direction.
- With regards to the study context, this is the first Libyan case study to have studied the importance of government incentives in attracting FDI by applying these to the characteristics of foreign investment. In addition, this research can be considered the first attempt to assess the relationship between FDI and domestic suppliers in the Libyan context.

8.4 Policy Implications and Recommendation

- The Libyan government should not only pay attention to attracting investors by using factors to encourage FDI, but should also focus on remedying those issues which acted as disincentives. Moreover, the investment authorities should have regular meetings with foreign company representatives to identify their needs.
- Since different types of FDI viewed each locational determinant factor differently, incentives provided by the government should be restricted to and designed to target specific FDI. Also, the results are important for host countries, as they will be able to deal with each type of FDI according to the above characteristics.
- This research serves to provide government policy-makers with data about the effects of nationality, industry type and ownership on locational determinant factors of FDI. They will then be in a better position to adjust or plan their policies according to the kinds of FDI they would like to attract, in order to gain the highest benefits from incoming FDI.
- It is recommended that a specialised market for Libya's natural resources should be created, supported by the relevant bodies to ensure the quality of these resources.
- The Libyan government must pay more attention to reducing bureaucracy and red tape in order to improve the domestic infrastructure and minimize delays and corruption by adopting a one-stop shop policy to create a satisfactory environment for FDI.
- An effective strategy including an investment map should be adopted and must be regularly reviewed. This map should be considered as an important tool to help the process of organising investment in natural resources by helping to locate industrial estates near to the sites of production of these resources, and their potential markets.

- Overall development of domestic infrastructures such as information technology, e-government, R&D and training centres, and the financial sector are essential to make the country more attractive for FDI.
- The government should focus more on developing its accounting and legal systems, and on enhancing corporate governance, in order to ensure transparency among investor partners, leading to an increase in FDI.
- The Libyan government should expand the private sector in order to make the Libyan economy more attractive for FDI.

8.5 Limitations and Future Research

This research has some limitations which suggest opportunities for future studies, as the world situation is rapidly evolving. These limitations and suggestions for further research are as follows:

- This study used the survey method to focus on the topic which is considered to be a sensitive issue in management information. The data obtained in this study comes from a relatively small sample size with skewed demographic characteristics. The informants may not have been the right people to respond to the questions asked; since top management often assign this type of task to other individuals whom they believe would be able to provide the appropriate information. However, these persons, such as General Director, Board Chairman Deputy Director General, etc., may know about the specific aspects of the organization which they deal with but may not have a thorough understanding or an overarching perspective. As a result, multiple data sampling methods, such as econometrics, focus groups, and a larger sample size should be adopted in future research to better validate the model. This would be helpful to confirm the robustness of the model and enhance the practical implications of the findings.
- This research focused on FDI that has at least one foreign shareholder holding at least 10% of total shares, as defined by the United Nations. This percentage of minimum foreign shareholding may be so small that sometimes the foreign

investor may not have any decision-making responsibilities regarding FDI policy. Therefore, replication of this study is recommended with a stricter definition of foreign shareholding, for example, specifying a holding of at least 50%, in order to identify if this causes any changes to the research results, and to widen the applicability of the findings.

- Three characteristics were introduced to mediate the relationships between locational determinant factors and FDI in Libya. Each characteristic was divided into two subgroups. However, in order to get more information about the effect of such a group, further separation should be carried out. For example, in the case of nationality, the MENA and Western groupings could be subdivided, and the same technique could be employed to the industrial sector divisions. In addition, in the current rapidly changing environment, it would also be useful to examine the potential of other characteristics for use in a future model, including size of labour force and age of company.
- This research approach used a subgroup analysis of respondents, which in some cases, such as mode of investment type, resulted in sample sizes which were too small. The sampling strategy should be carefully planned and implemented in order to enhance the sample size. Replication of this study should be done with a larger sample in order to confirm the reliability and generalization of the research findings. Once a large sample size is chosen, then other statistical methods such as regression are also applicable.
- The study only focused on the relationship between FDI and domestic suppliers. Future research should examine wider spill-over effects such as backward and forward linkages. In addition, to confirm the reliability and validity of the research results presented in this study, replication of this study should be carried out with a different dataset to generalize the findings.
- The scope of this study did not cover the costs and benefits of providing FDI incentives, and the effect of FDI on direct spill-over. Future research should take

into consideration these two issues, as the incentives should only be provided if the country can enjoy significant net gains from FDI.

- Finally, this study covered a period of ten years, ending in 2012. Therefore, studies are required to periodically assess the changes in the business and political environment in Libya. It would be very useful to conduct an econometric study regarding determinants and the impact of FDI in Libya using available secondary data.

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Appendix -A- Questionnaire Covering Letter

Questionnaire Survey

Perceptions of Foreign Companies/ Fully Owned and Joint - Venture on Foreign Direct Investment in Libya

Dear participant,

This survey is part of a Ph.D. research project conducted by me at the Business school, University of Huddersfield, United Kingdom. The main aims are to gather information from foreign companies/ Department and Individuals working in Libya in order to understand the issues related to Foreign Direct Investment in the country.

Kindly you are requested to spare some of your valuable time to complete this questionnaire. Please be assured that all the information you provided will be treated with extreme confidentiality, therefore please note that you not be asked for your name. Your cooperation will contribute to the successful completion of this research, and therefore is very much appreciated.

Once again, the information provided will be confidential and will be only used for academic purpose.

Please do not hesitate to contact me on the address shown below if you require further clarification.

Thank you very much for your time and cooperation.

Yours sincerely,

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Appendix –B- Research Questionnaire

This questionnaire includes a number of questions that basically attempt to capture your personal perceptions about the main factors that influence your company to invest in Libya and the related variables that you think they might most and more effectiveness for your company decision. We are particularly interested in your own personal beliefs, opinions and experiences. There are useful instructions to guide you how to answer the questions at the beginning of each section.

A1- *This section seeks to present a **profile of the respondent**. Please tick the appropriate answer for each question.*

A1.1 - Nationality

☐ **1)** British ☐ **2)** Italian

☐ **3)** Maltese ☐ **4)** French

☐ **5)** Libyan ☐ **6)** Tunisian

☐ **7)** Others (please specify).....

A1.2 - Education Level

☐ **1)** Secondary ☐ **2)** Diploma

☐ **3)** Bachelor's degree ☐ **4)** Post-graduate(e.g.MSc, PhD)

☐ **5)** Others (e.g. qualifications).....

A1.4 - Position at work

☐ **1)** General Director ☐ **2)** Assistant/vice-director

☐ **3)** Board Chairman ☐ **4)** Other (please specify)……..

☐ **5)** Head of Department

A1.5 - Experience		**Less than 2 years**	**2 – 5 years**	**6– years or more**
		1	**2**	**3**
a	With the current company	☐	☐	☐

A2- *The following questions describe a* ***profile and characteristics of your company****. For each question; please tick the appropriate box.*

A2.1 - Company's Nationality

☐ **1)** UK
☐ **2)** Germany
☐ **3)** Italy
☐ **4)** USA
☐ **5)** France
☐ **6)** Tunisai
☐ **7)** Malta
☐ **8)** Others (please specify) .....

A2.2 - The company Location in Libya

☐ **1)** Tripoli
☐ **2)** Benghazi
☐ **3)** Al Jfara
☐ **4)** Misrata
☐ **5)** Others (please specify) .....

A2.3 - Company operation Age in Libya

☐ **1)** Less than 2 years
☐ **2)** 2 - 5 years
☐ **3)** More than 5 years

A2.5- Type Of company ownership

☐ 1) Full foreign -owned company
☐ **2)** Joint-venture company

Part 2- It relates to the factors that influence the sample companies to invest in Libya

B- This section aims to describe the main factors that encouraging or discouraging foreign investors to invest in Libya such as. (*Economic factors, market factor, human capital, investment policies factors, domestic infrastructure factors, natural resources and financial & legal factors).*

B1- *Please use the numbers to indicate your firm's value to the degree of influence of each of the following factors has on encouraging or discouraging your investment in Libya by marking the relevant box.*

		Highly Discourage 1	**Slightly Discourage 2**	**Not effect 3**	**Encourage 4**	**Highly Encourage 5**
B1.1	***Economic factors***					
A	Economic Growth	1	2	3	4	5
B	Inflation rate	1	2	3	4	5
C	Stability of Exchange rate	1	2	3	4	5
D	Extent of government intervention in the economy	1	2	3	4	5
E	Privatisation procedures	1	2	3	4	5
B1.2	***Market factors***					
A	Trend & growth of Local Market	1	2	3	4	5
B	Competition in Local market & Market potential	1	2	3	4	5
C	Availability & Reliability of market information	1	2	3	4	5
D	Existence of distribution channels	1	2	3	4	5
B1.3	***Libyan government investment policies and incentive factors***					
A	Exemptions of import duties on imported Raw materials	1	2	3	4	5
B	Exemptions of import duties on imported machinery components	1	2	3	4	5
C	Exemptions of corporate tax	1	2	3	4	5
D	Exemptions of tax on repatriation of dividend and income	1	2	3	4	5
E	Tax Exemptions in general	1	2	3	4	5
F	Regulation on property & land ownership by foreigners	1	2	3	4	5
G	Regulation and control on transfer profits	1	2	3	4	5
H	Government bureaucratic procedures or red tape	1	2	3	4	5
I	Extent of corruption	1	2	3	4	5
B1.4	***Utility & Facility factors (Infrastructure)***					
A	Quality of Telecommunication services	1	2	3	4	5
B	Quality of transportation services system	1	2	3	4	5
C	Quality of Electricity services	1	2	3	4	5
D	Quality of Natural resources	1	2	3	4	5
E	Availability of Natural resources	1	2	3	4	5
F	Availability of technical & Skilled labour	1	2	3	4	5
G	Availability of Semi-skilled labour	1	2	3	4	5
H	Wages for Semi-skilled labour	1	2	3	4	5
I	Wages for technical & Skilled labour	1	2	3	4	5
J	Salaries required for managerial staff	1	2	3	4	5
K	Research Development and training system	1	2	3	4	5
L	Costs of Training	1	2	3	4	5

B1- *Please use numbers to indicate the importance of the following factors by marking the relevant box. Continued.*

Strongly Discourage 1	Discourage 2	Slightly Encourage 3	Encourage 4	Very Encourage 5

B1.5	***Financial & Legal factors***						
A	Access to local source of fund	1	2	3	4	5	
B	Accounting & Audit system	1	2	3	4	5	
C	Availability of Financial system	1	2	3	4	5	
D	length of time of Legal provisions	1	2	3	4	5	
E	Labour legislation	1	2	3	4	5	
F	Others (please describe below)	1	2	3	4	5	

Part 3- It relates to supply linkages and sales to the consumers and other firms

C- This section seeks to identify the linkages between foreign investors and Local Supplier and the companies target markets. *Please indicate **to what extent** your firms depend on local supplier in terms of inputs materials.*

C1- Please indicate to what extent your company depend on local supplier

☐ Mainly depend ☐ Partly depend ☐ Mainly not depend

C2- *This section depend on your answer of the previous section, the following statements describe the reasons that explain if the main inputs / suppliers not obtained from the local economy. On the scale below, please circle the appropriate number that, most closely represent your true belief about your company's strategy could select more than one answer.*

1	None
2	A limited supply of materials
3	An inadequate quality
4	Too costly materials
	Other reasons please specify. ……

C3- Please indicate what market is your company targeting

☐ Local Market ☐ both locally and export.

D- Additional comments, please use the space provided below to indicate any additional suggestions or information that you believe will be important for this study

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*Thank you for your assistance and **participation** in completing this questionnaire. Please tick **[√]** below*

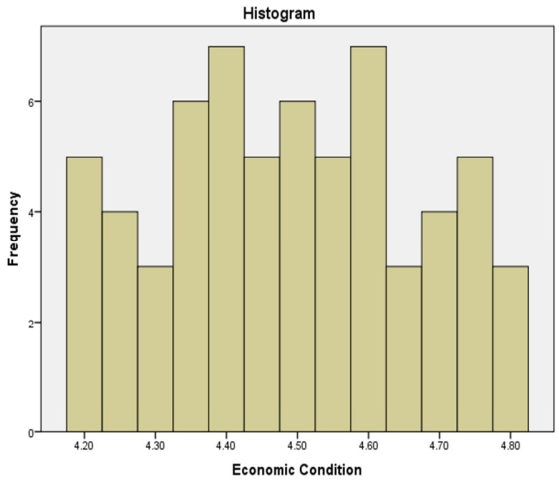
- if you would like to receive a copy of a summary of the research results ☐
- if you interested to participate in a future short interview about the issues raised in this questionnaire ☐

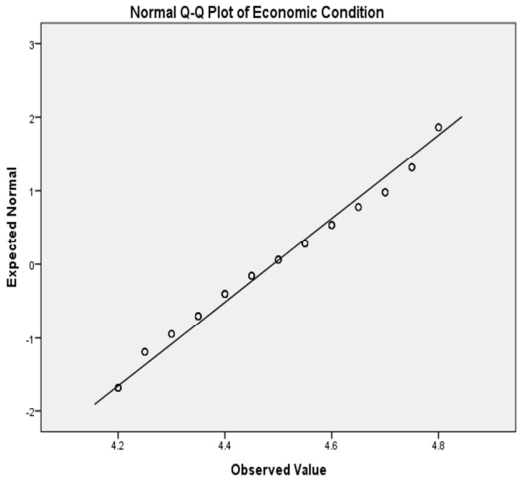
Please provide contact details for arranging the interview:

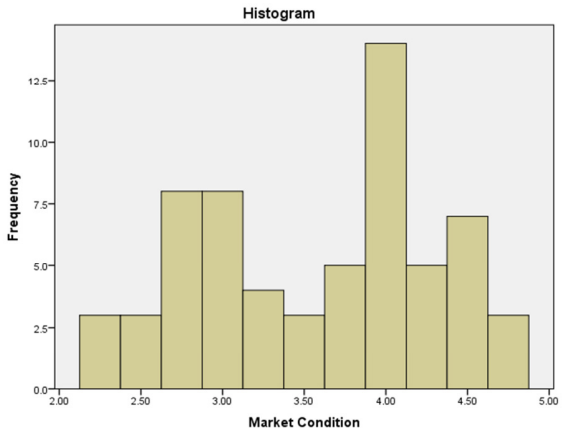
Company's name: …….....
Your name: ……..…….....
Telephone number: …….....
Email address: ……..…….……

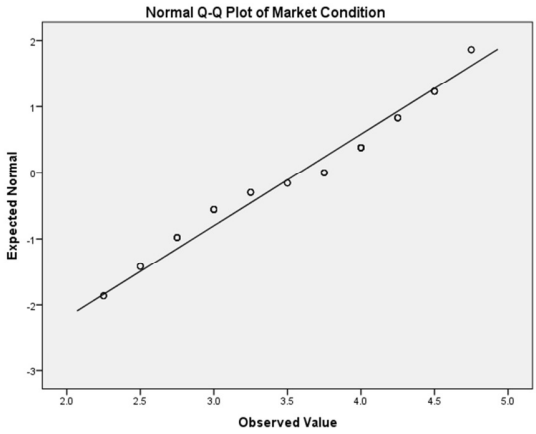
Sincerely,
Ibrahim Ahmouda

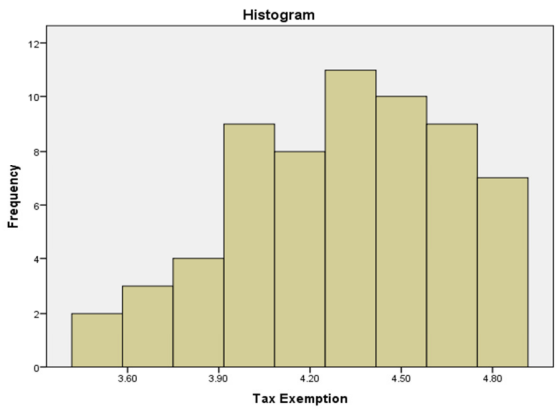
Appendix -C- Normality Test

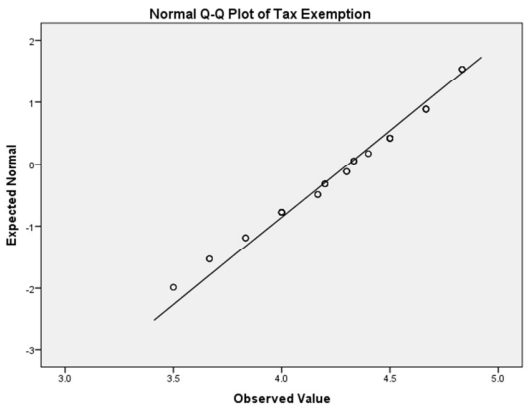


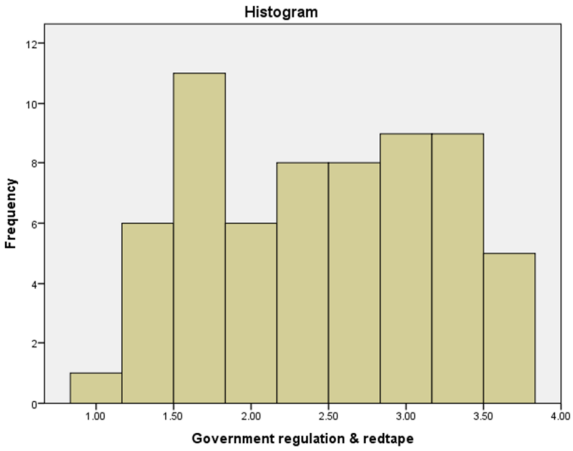


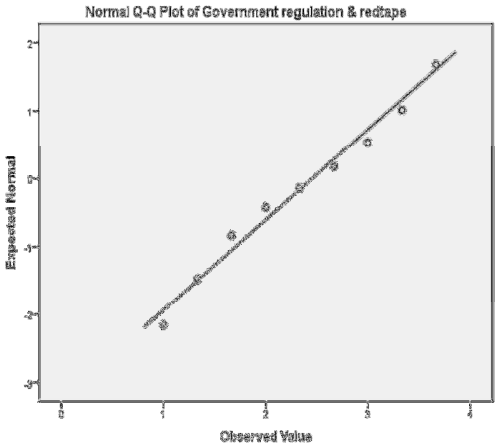


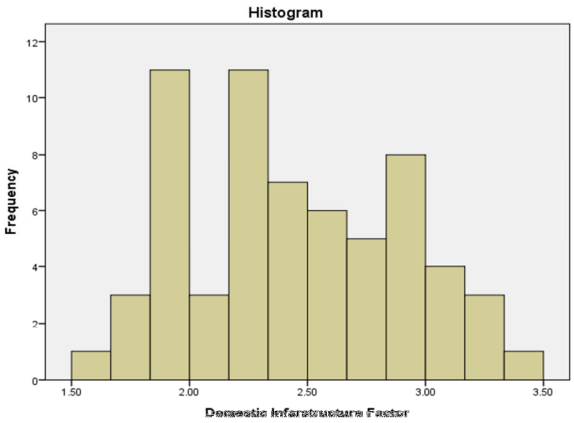


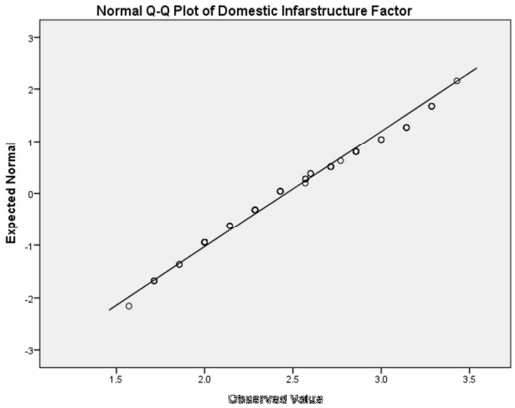


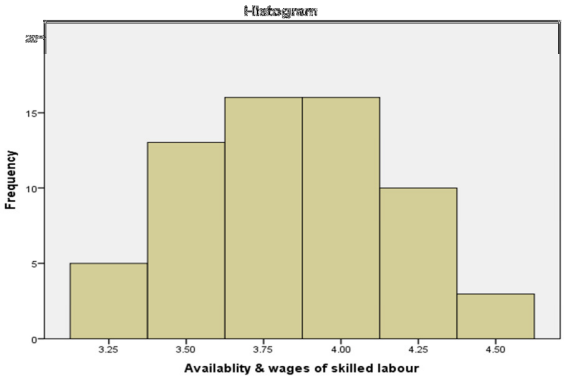


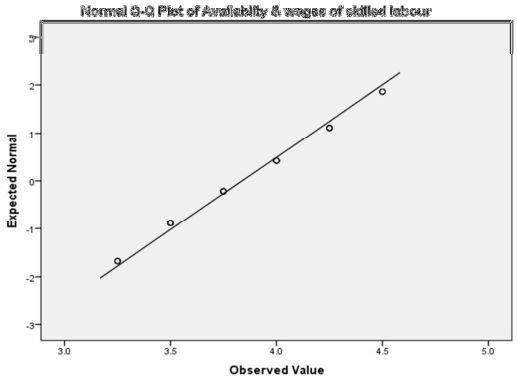

Histogram
Frequency
Government regulation & redtape

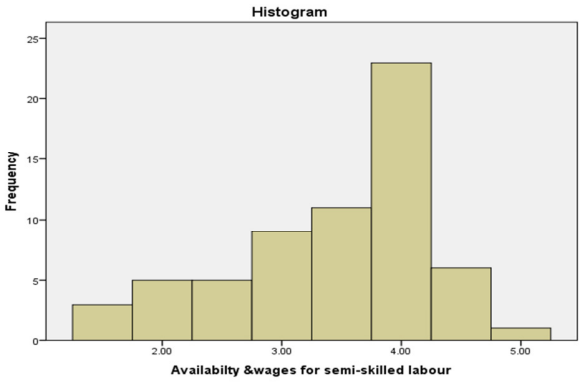

Normal Q-Q Plot of Government regulation & redtape
Expected Normal
Observed Value

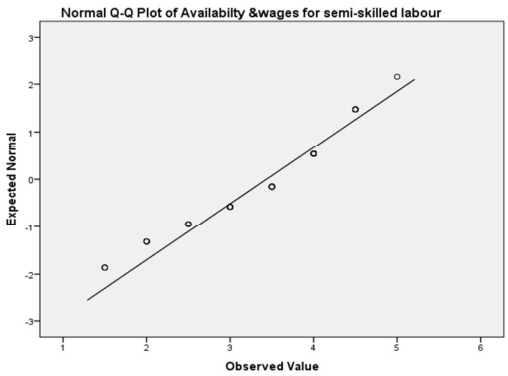

Histogram
Frequency
Domestic Infarstructure Factor

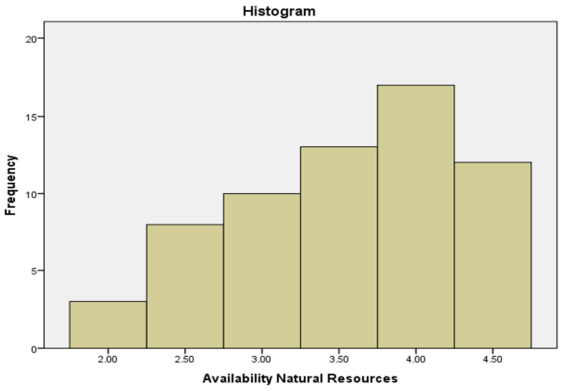

Normal Q-Q Plot of Domestic Infarstructure Factor
Expected Normal
Observed Value

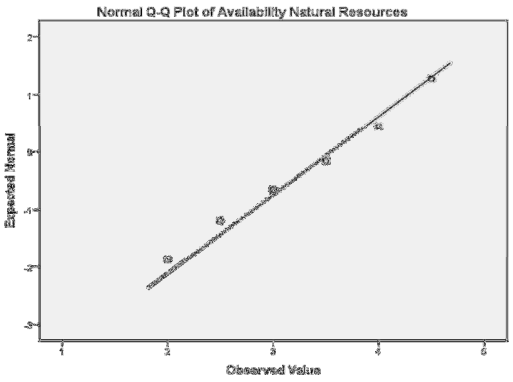

Histogram
Frequency
Availablity & wages of skilled labour

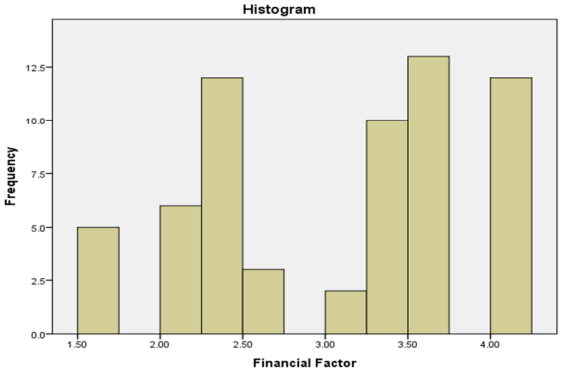

Normal Q-Q Plot of Availablity & wages of skilled labour
Expected Normal
Observed Value

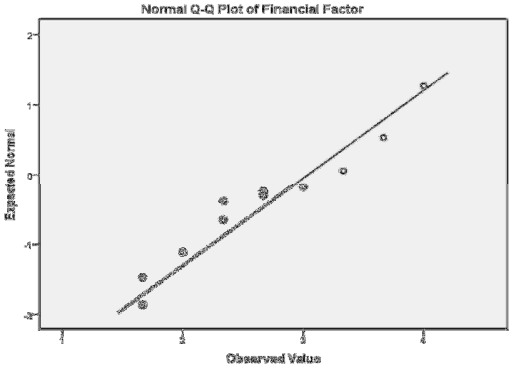

Histogram
Frequency
Availabilty &wages for semi-skilled labour

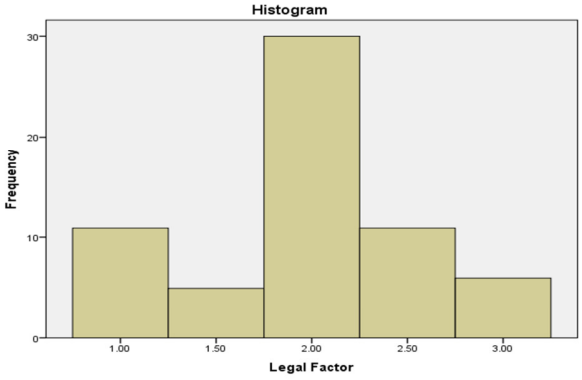

Normal Q-Q Plot of Availabilty &wages for semi-skilled labour
Expected Normal
Observed Value

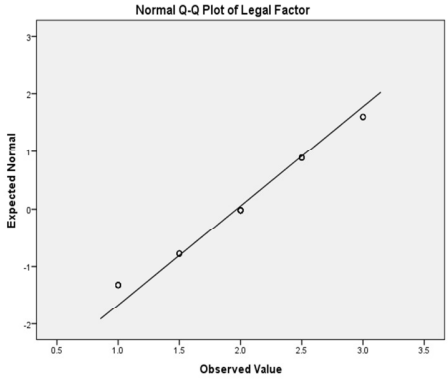

Histogram
Frequency
Availability Natural Resources

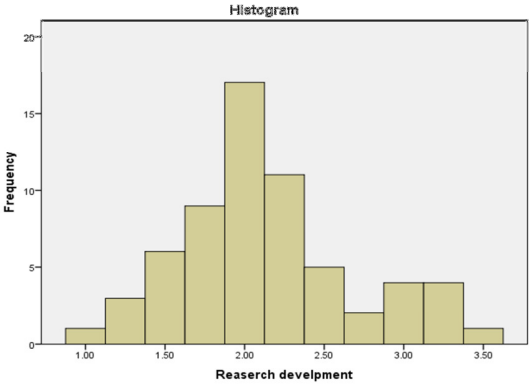

Normal Q-Q Plot of Availability Natural Resources
Expected Normal
Observed Value

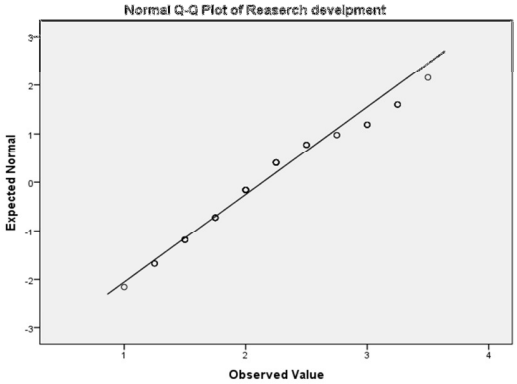

Histogram
Frequency
Financial Factor


Normal Q-Q Plot of Financial Factor
Expected Normal
Observed Value

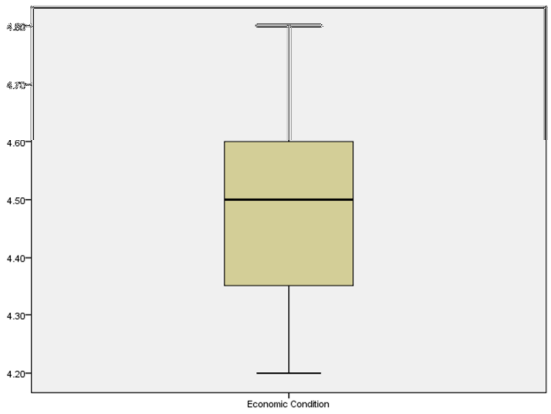

Histogram
Frequency
Legal Factor
1.00
1.50
2.00
2.50
3.00
0
10
20
30

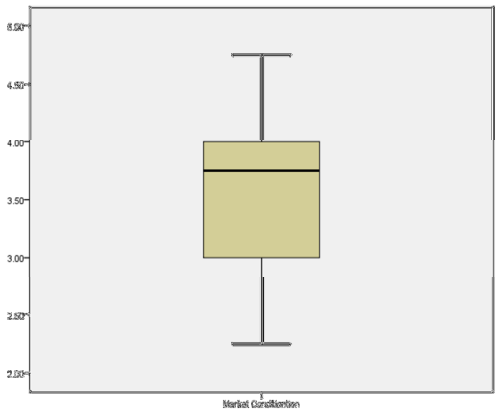

Normal Q-Q Plot of Legal Factor
Expected Normal
Observed Value
0.5
1.0
1.5
2.0
2.5
3.0
3.5
-2
-1
0
1
2
3

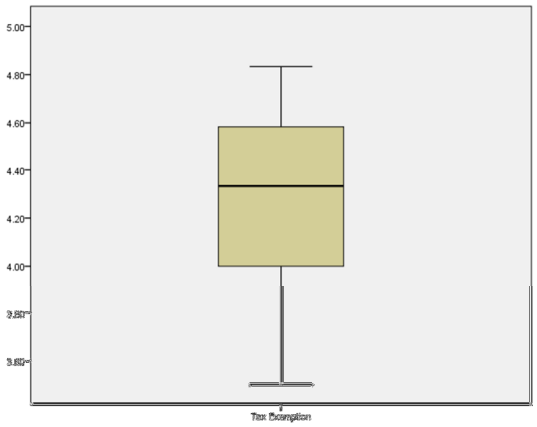

Histogram
Frequency
Reaserch develpment
1.00
1.50
2.00
2.50
3.00
3.50
0
5
10
15
20

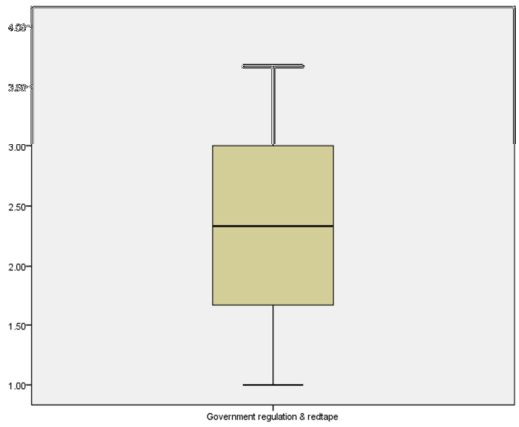

Normal Q-Q Plot of Reaserch develpment
Expected Normal
Observed Value
1
2
3
4
-3
-2
-1
0
1
2
3

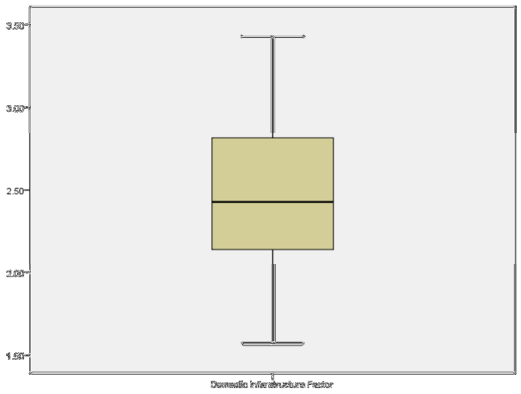
Appendix -D- Outliers Test



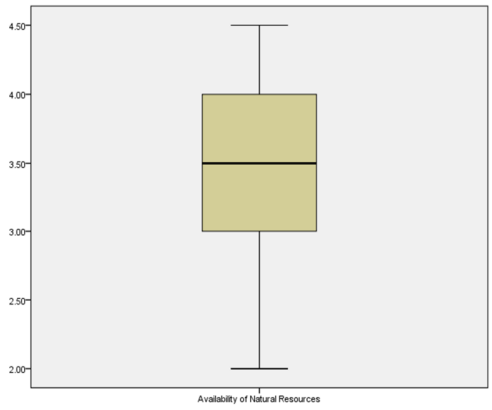


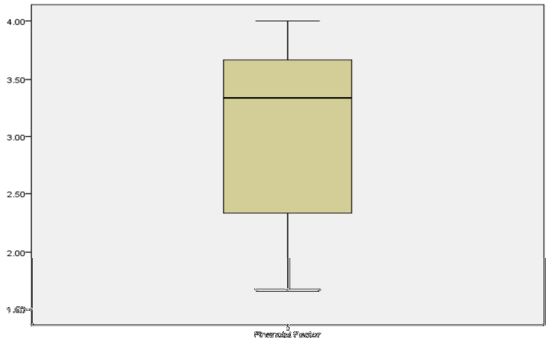


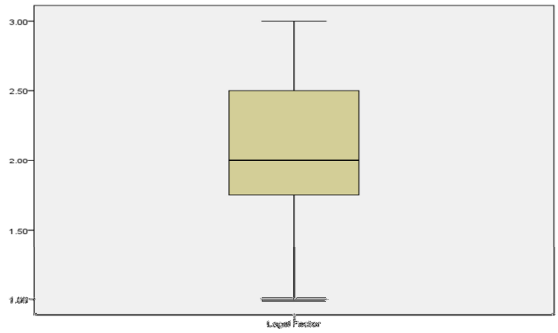


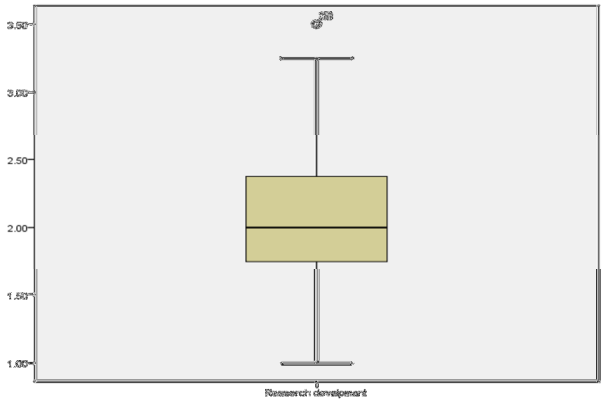


5.00
4.00
3.00
2.00
1.00


4.50
4.00
3.50
3.00
2.50
2.00
Availability of Natural Resources


4.00
3.50
3.00
2.50
2.00


3.00
2.50
2.00
1.50


3.50
2.50
2.00
1.50
Research development

Appendix -E- Leven Test

FDI Location Factor (Ownership group)	F	df1	df2	Sig.
Economic Conditions	1.721	1	61	.195
Market Conditions	.197	1	61	.659
Tax Exemptions	.344	1	61	.560
Government Regulation and Red Tape	2.017	1	61	.161
Domestic Infrastructure	1.082	1	61	.302
Availability and Wages of Skilled Labor	.005	1	61	.946
Availability and Wages of semi-skilled Labor	1.008	1	61	.319
R&D and Training Systems	1.887	1	61	.175
Natural Resources	1.497	1	61	.226
Financial Accessibility	2.045	1	61	.158
Legal Practice	1.278	1	61	.263
Tests the null hypothesis that the error variance of the dependent variable is equal across groups.				
FDI Location Factor (Country of origin group)	F	df1	df2	Sig.
Economic Conditions	2.505	2	60	.090
Market Conditions	2.283	2	60	.111
Tax Exemptions	8.463	2	60	.103
Government Regulation and Red Tape	1.493	2	60	.233
Domestic Infrastructure	.460	2	60	.634
Availability & Wages of Skilled Labour	.846	2	60	.434
Availability & Wages of semi-skilled Labour	.571	2	60	.568
R&D& Training Systems	.292	2	60	.748
Natural Resources	3.602	2	60	.193
Financial Accessibility	.381	2	60	.685
Legal Practice	2.634	2	60	.180
Tests the null hypothesis that the error variance of the dependent variable is equal across groups.				
FDI Location Factor (type of business group)	F	df1	df2	Sig.
Economic Conditions	2.167	1	61	.146
Market Conditions	.014	1	61	.907
Tax Exemptions	1.181	1	61	.281
Government Regulation and Red Tape	.665	1	61	.418
Domestic Infrastructure	7.085	1	61	.010
Availability & Wages of Skilled Labor	.214	1	61	.645
Availability & Wages of Unskilled Labor	19.426	1	61	.128
R&D& Training Systems	7.546	1	61	.108
Natural Resources	4.043	1	61	.249
Financial Accessibility	1.610	1	61	.209
Legal Practice	.297	1	61	.587
Tests the null hypothesis that the error variance of the dependent variable is equal across groups				