

Are Fiscal Incentives the Magic Tool for an increased FDI?

- Algeria's Case Study -

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Abstract:

Algeria is trying to improve its investment climate as one of the most promising solutions in light of the oil crisis the country is experiencing. To achieve that, Algeria has adopted a set of policies and procedures, including the granting of a fiscal incentives package as an attempt to attract investments, especially foreign direct ones.

Therefore, this study aims at identifying the role of Fiscal incentives in attracting foreign direct investment and determining the extent of its success in increasing the flow of this type of investment to Algeria.

Key Words : Fiscal incentives, FDI (Foreign Direct Investments), Attracting investment, Investment climate.

ملخص:

تحاول الجزائر تحسين مناخ الاستثمار باعتباره من أهم الحلول الواعدة في ظل الأزمة البترولية التي تعاني منها، حيث تبنت مجموعة من السياسات والإجراءات، من بينها منح مجموعة من الحوافز الجبائية كمحاولة لجذب الاستثمارات خاصة الأجنبية المباشرة.

وعليه تهدف هذه الدراسة للتعرف على دور الحوافز الجبائية في جذب الاستثمار الأجنبي المباشر ومعرفة مدى نجاحها في زيادة تدفق هذا النوع من الاستثمارات إلى الجزائر.

الكلمات المفتاحية: الحوافز الجبائية، الاستثمار الأجنبي المباشر ، جذب الاستثمارات، مناخ الاستثمار .

Introduction:

In the light of the collapse of oil prices which led to the oil crisis that began in the late 2014, Algeria finds itself obliged to diversify its economy outside the hydrocarbons sector, as for its choices Algeria has many alternatives that can depend on to overcome this crisis one of which, is the FDI "Foreign Direct Investment" .This alternative contributes to economic development through many advantages such as the transfer of modern technology and the creation of jobs.

However the arrival of foreign direct investments to any country depends on the availability of an attractive investment climate. Like any other country, the Algerian government has sought to promote this investment through enactment of a number of laws that contain a host of fiscal incentives as an attempt to create this favourable environment and attract foreign direct investment.

Research' Problematic: Based on the above, we can formulate the problematic of this research in the following question:

Did the Fiscal incentives granted contributed to the increase in the flow of FDI to Algeria?

And for answering this problematic we chose to build this paper on three main axes as follows:

- 1- What is foreign direct investment?
- 2- What is Fiscal Incentives?
- 3- What is The Reality of FDI in Algeria under the Fiscal incentives granted?

Objective and Methodology:

The importance of the study is that it deals with one of the most important topics in the arena, which is the diversification outside the hydrocarbons sector, where FDI is one of the most effective alternatives to do so. We seek to show the most important features of the approach. So the purpose of the present paper was to:

- Introduce the concept of FDI and its forms.
- Know the tax incentives granted by the Algerian state to attract investment.
- Learn about the reality of FDI in Algeria under the tax incentives granted.

To conduct this paper we used the descriptive analytical approach, Data has been collected from multiple sources: books, journals, and websites which helped us to analyze the ideas, and connect them logically and scientifically.

First: What is Foreign Direct Investment?

1. Foreign Investment :

Foreign investment is defined as the investment coming from abroad and the owner of capital, and the contributor to the establishment of investment projects in an economy by an existing institution in another economy.⁽¹⁾

Foreign investment is divided into direct and indirect foreign investment, while FDI ⁽²⁾ is all fixed asset financial investments, Foreign indirect investment is all financial investments in government and institutional bonds, all types of bank loans and all types of shares.⁽³⁾

2. Foreign Direct Investment (FDI) :

The United Nations Conference on Trade and Development (UNCTAD) defines foreign direct investment as an investment involving a long-term relationship that reflects permanent and capable

management interests between the company in the parent country (the country to which the investee belongs) and a company or production unit in another country (The future diameter of investment).⁽⁴⁾

FDI is also defined as requiring supervision (control) of the project by taking the form of establishment of an enterprise by the investor alone or with equal or unequal participation, and also takes the form of a full or partial repurchase of an existing project .⁽⁵⁾

3. Forms of FDI :

The forms of FDI vary depending on the ownership of the project. This property can be absolute or relative, and on this basis FDI can be divided into a **joint investment** which is an investment owned or shared by two or more parties from two different countries on a permanent basis. Such participation is not limited to the share of the capital but extends to the management of the project. Or an **Investment wholly owned by foreigners**, This type of investment means that the foreign investor retains the right to own the investment project, as well as the right to manage it and control all its operations.⁽⁶⁾

4. The Importance of FDI :

The importance of FDI is evident from the many advantages it offers some of which are as follows :⁽⁷⁾

❖ FDI is a major source of external financing for some middle-income countries and this is achieved through the transfer of real resources from abroad such as equipment, machinery necessary for the establishment of investment and the accompanying technical, administrative and organizational expertise, which can break many obstacles to development.

❖ FDI does not establish its rules in the host countries until it does in-depth studies showing the economic and technical feasibility of the project in which it invests.

❖ It increases the use of local resources and employment opportunities for citizens in the host country where FDI is financing in its true meaning by creating many economic exits that drive the manufacturing movement in the host country.

Second: What is Fiscal Incentives ?

1. The Definition of Fiscal Incentives :

A Fiscal incentive is a government measure that is intended to encourage individuals and businesses to spend money or to save money by reducing the amount of tax that they have to pay.⁽⁸⁾

The United Nations Development Program (UNCTAD) defines the incentive as any economic advantage that can be valued with monetary value, provided by the host country for foreign investment.⁽⁹⁾

2. The Fiscal Incentives Objectives:

There are several goals that any country would like to see when conducting Tax incentives but we can divide them into two main categories as follows :⁽¹⁰⁾

2.1. Economic objectives :

❖ It provides an appropriate and encouraging investment climate, leading to increased investments at the home country, also works on the balance of investments in terms of activity and in its orientation towards priority activities in development policy.

❖ Encouraging exports outside hydrocarbons by increasing the competitiveness of local institutions in foreign markets by exempting exported products from a range of local taxes.

❖ Increasing the resources of the public treasury as the expansion of the tax base in the long run under an effective and appropriate tax concession policy would increase the productive branches, the level of their activity and their commitment to their duties towards the public treasury, which would increase the tax revenue in the future.

2.2. Social Objectives :

❖ Reducing and alleviating unemployment by providing new jobs where tax concessions provide financial resources that allow economic agents to reinvest them in other productive branches or establish small enterprises;

❖ Work on the balance of investments at the home country, by directing some of them to disadvantaged areas and to be promoted.

3. The Fiscal incentives granted through the investment laws in Algeria:

The Algerian government has enacted a number of investment laws that include a set of tax advantages, which have been in place for several years since the independence, and they are presented in the following table:

Table 1: The Algerian Investment Laws.

The Law	Publication Date	Objective
Law 63-277 of July 26 th , 1963	Published in the Algerian Official Gazette No. 53 of August 02 nd , 1963	
Order 66-284 of September 15 th , 1966	Issued in the Official Gazette No. 30 of September 17 th , 1966, which contains the Investment Law	This law came to fill the loopholes of Law 63-277 where the order 66 - 284 granted a number of tax concessions and benefits to private capital, whether it was foreign or national.
Law No. 82-11 of August 21 st , 1982	Issued in the Official Gazette No. 34 of August 24 th , 1982, concerning national private economic investment	
Law No. 86-13 of August 19 th , 1986	Issued in Official Gazette No. 35 of August 27 th , 1986.	On the establishment and operation of mixed companies, where this law was amended and complied with Law No. 82-11
Law No. 88-25 of July 12 th , 1988	Published in the Official Gazette No. 28 of July 13 th , 1988.	On the direction of national private economic investments,
Law No. 90-10 of April 14 th , 1990	Issued in Official Gazette No. 16 of April 18 th , 1990.	On cash and loan
The Legislative Decree No. 93-12 dated October 5 th , 1993	Issued in the Official Gazette No. 64 of October 10 th , 1993.	Related to the promotion of investment, this decree came with the freedom of investment condition and granted a number of tax advantages
Decree No. 01-03 dated August 20 th , 2001	Issued in the Official Gazette No. 47 of August 22 nd , 2001.	Concerning investment development. The decree came as a result of the establishment of the National Agency for Investment Development. It also stressed that the investments are carried out in full freedom, taking into consideration legislation, regulations and environmental protection, and also addressed many of the advantages granted to investments,
Decree No. 06-08 of July 15 th , 2006	Issued in the Official Gazette No. 47 of July 19 th , 2006.	Amending and supplementing Order 01-03 on investment development
Executive Decree No. 06-356 of October 09 th , 2006	Issued in the Official Gazette No. 64 dated October 11 th , 2006.	Includes the powers, Organization and Operation of the National Agency for Investment Development.
The legislation did not stop here. There were several decrees and decisions over the years from 2007 until 2016, all of which were aimed at developing investment and offering several tax advantages.		
Law No. 16-09 of August 03 rd , 2016	issued in the Official Gazette No. 46 of August 03 rd , 2016	Concerning the promotion of investment. This law defines the system applied to national and foreign investments in economic activities for the production of goods and services.
After the last law A number of executive decrees issued in Official Gazette No. 16 dated March 08th, 2017 were adopted. They are based on the advantages provided in Law 16-09, but they dealt with some of the points presented previously and added some advantages. These decrees are the following :		
Executive Decree No. 17-100 of March 05 th , 2017.	issued in Official Gazette No. 16 dated March 08 th , 2017	Amended and supplemented by Executive Decree No. 06-356, containing the powers of the National Agency for Investment Development, Organization and Operation.
Executive Decree No. 17-101 of March 05 th , 2017.		Defines the negative lists and the minimum amounts to benefit from the advantages and the application of the advantages to different types of investments.
Executive Decree No. 17-102 of March 05 th , 2017.		Defines the modalities of investment registration as well as the form and results of the certificate.
Decree No. 17-103 of March 05 th , 2017.		Specifies the amount of receivables for processing investment files and the manner of collection.
Executive Decree No. 17-104 of March 05 th , 2017.		Relating to the follow-up of investments and penalties applicable in case of failure to comply with written obligations and obligations.
Executive Decree No. 17-105 of March 05 th , 2017.		Defines the modalities of applying the additional benefits of exploitation granted to investments created for more than 100 jobs.

Source: Authors treatment based on the Executive decrees issued in the Official Gazette.

(11) ❖ Among the most important tax advantages granted by the previous laws we cite the following

- **General Privileges**
 - Exemption from VAT on goods and services imported or acquired locally that enter directly into the completion of the investment.
 - A 90% reduction in the amount of the annual rent payable by the State Property Department during the period of completion of the investment.
 - Exemption for ten years from the real estate tax on the real estate properties that fall within the framework of the investment from the date of acquisition.
 - After reviewing the project in the stage of exploitation by the tax authorities at the request of the investor, for three years he will benefit from:
 - a. An exemption from corporate profits tax ;
 - b. An exemption from fees for professional activity ;
 - c. A reduction of 50 % of the amount of the annual rental fee determined by the State Property Authority.
- **Privileges for the southern and high plateaus, as well as for any other region whose development requires special contribution by the State**

In addition to the above mentioned advantages:

 - The State shall, in part, be responsible for the expenses of the works relating to the basic facilities necessary for the completion of the investment, after being evaluated by the Agency.
 - Reduction of the amount of the annual rental fee determined by the interests of state property.
 - The duration of the benefits of exploitation granted shall be increased from three years to five years when the investment establishes more than 100 permanent jobs during the period from the date of its registration until the end of the first year of the exploitation phase at most.
 - Benefit from the duty-free procurement system, materials and components involved in the production of goods benefiting from the VAT exemption.

Third: What is The Reality of FDI in Algeria under the Fiscal incentives granted?

1. In Figures :The Investment in Algeria :

Table 1: The Algerian Investment Laws.

Period	Capital' Source	Projects' Number	The Financial Value In Million DA	Employment Positions
2012-2002	Local investments	31 594	1 743 783	256 156
	Foreign investments	410	803 057	42 959
	Total	32 004	2 546 840	299 115
2016-2002	Local investments	62 982	10 584 134	1 018 887
	Foreign investments	822	2 216 699	119 525
	Total	63 804	12 800 834	1 138 412

Source: Authors treatment, based on the Data presented in the official website of the National Agency for Investment Development: www.andi.dz.

The table above shows the following:

* During the period 2002-2012: the lion's share in the number of projects received by the local investments, which amounted to 99% of the total investments, while the number of projects for foreign investment 1%, despite the small proportion of the number of projects, but the financial value was 32% compared to Domestic investments with a financial value of 68%. Foreign investment also contributed to the creation of 14% of the jobs, while domestic investments created 86% of the jobs.

* During the period 2002-2016: We notice a significant increase in the total number of investments compared to the period 2002-2012, where this increase reached 49.8%, within a small period estimated at four years. Among the reasons for this increase is the policy adopted by the Algerian State to promote and encourage investment.

Table 2: Distribution of Foreign Investments by Sector of Activity For the period 2002-2016.

Sector	Projects Number	%	Value in Million DA	%	Employment Positions	%
Agriculture	14	1.70	4 373	0.20	618	0.52
Building	137	16.67	77 661	3.50	23 040	19.28
Industry	495	60.22	1 783 922	80.48	70 793	59.23
Health	6	0.73	13 572	0.61	2 196	1.84
Transportation	25	3.04	14 820	0.67	6 309	1.44
Tourism	14	1.70	113 772	5.13	6 309	5.28
Services	130	15.82	119 139	5.37	13 342	11.16
Telecommunications	1	0.12	89 441	4.03	1 500	1.25
Total	822	100	2216699	100	119525	100

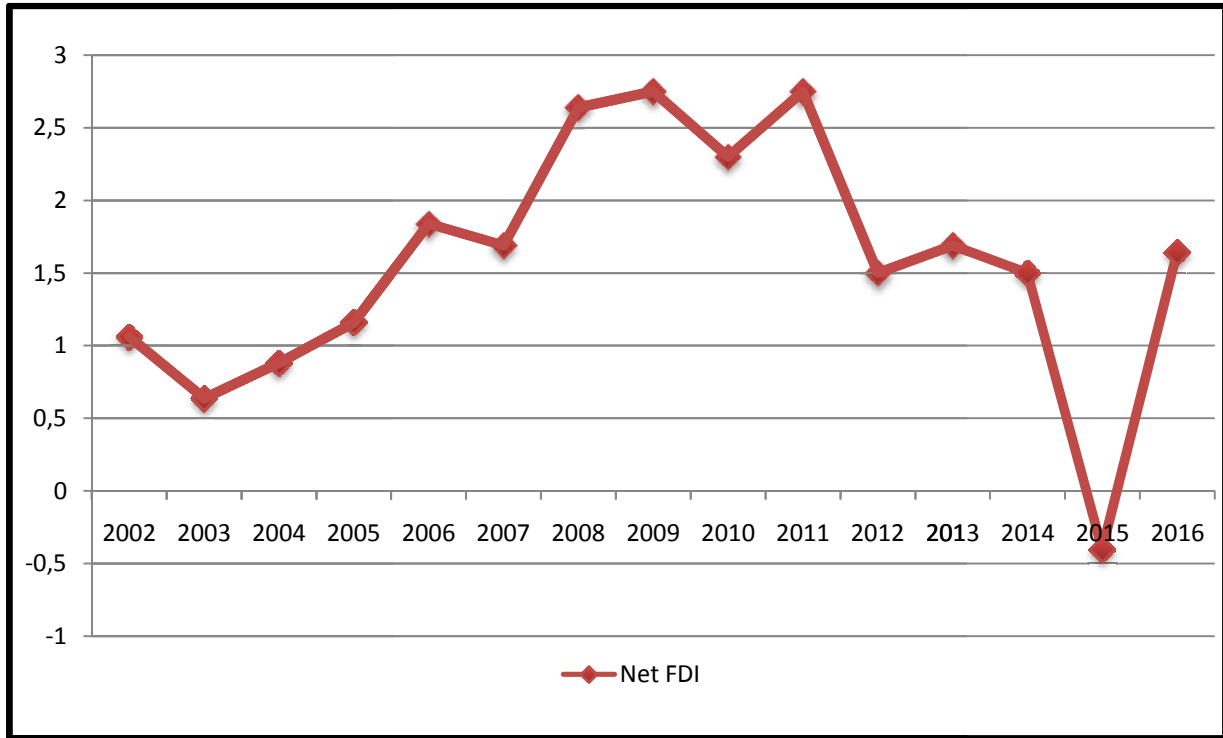
Source: Authors treatment, Op.cit: www.andi.dz.

❖ The table above shows that most of the foreign investment projects were in the industrial sector with 60.22% of the total foreign investments. This is due to the fact that it contains the hydrocarbons sector, which is one of the most attractive sectors for foreign investment, followed by the construction sector with 16.67% , Followed by the services sector (15.82%), transport, tourism and agriculture, followed by health and communications which almost has a 01% of the investments .

It is clear that foreign investment in Algeria is concentrated in the industrial sector especially hydrocarbons, while Algeria needs to upgrade other sectors, especially agriculture and tourism, which is pushing Algeria to find solutions to entice the foreign investor to other sectors outside the hydrocarbons.

In Figures : Foreign direct investment in Algeria :

Figure 1: The Distribution of the Algerian net FDI received during the period 2002-2016



Source : Authors treatment, based on the Data presented in the official website of the World Bank: www.worldbank.org

❖ The previous figure shows the fluctuation of the distribution of foreign direct investment received for Algeria during the period 2002-2016, where the decline in 2003 was known to return to a continuous increase until the year 2006, Among its reasons are the various tax advantages offered to investors, followed by the decline in 2007 after that, foreign direct investment witnessed a rise to the end of 2009, when the foreign investment reached its peak despite the existence of the global financial crisis, and this was because of the measures adopted by the Algerian state to maintain foreign investment, to fall again in 2010, followed by a significant increase in 2011 accompanied by a significant decline in 2012, and then remain between the rise and decline during the years 2013 and 2014, respectively, to witness a very sharp decline in 2015 and this was because of the oil crisis, which started its signs by the end of 2014, to return and record a significant rise during the year 2016 This is due to the tax advantages given in Law 16-09 on the promotion of investment and the efforts of the State to improve the investment climate, Despite the continuation of the oil crisis, foreign investment returned a very high rise compared to 2015.

It is noticeable from the above that the situation of variation and volatility in foreign direct investment in Algeria, despite the multiplicity of tax advantages granted, but they were not able to make foreign direct investment up to the required level, but compared with the pre-period of the year 2002 were the country suffered from the instability of the security situation this was a significant improvement, In the volume of FDI .

Finally, it can be said that the fiscal advantages play a role in increasing the inflow of foreign direct investment to Algeria, especially those provided by Law No. 16-09. However, it cannot be considered as the only factor in the flow of FDI, because there are several interrelated factors that allow the creation of an attractive Investment climate.

Conclusion:

Despite the efforts exerted by the Algerian government to encourage FDI through its enactment of a series of successive laws rich in tax incentives, the most important of which is Law 16-09, the rate of inflow of foreign investment remained very low compared to domestic investments. Also more than half of foreign investments In Algeria are concentrated in the hydrocarbons sector. So the FDI in Algeria remains in a fluctuation state between decline and rise, which confirms the presence of other factors affecting it, maybe the most important one, is the 49/51 rule on investment. And it can be said that fiscal incentives alone are not enough to attract FDI , because they are only one ring In the investment climate chain, and in order for the state to attract these type of investments, the establishment of an appropriate climate in all its political and economic aspects is required .

And we can summarize the main recommendations, reached through this study as follows:

- Administrative corruption must be eliminated first, to easily focus on other investment attracting factors.
- Attractive incentives should be put in place to guide foreign investments outside the hydrocarbons sector, especially in light of Algeria's backward oil crisis.
- The Algerian government must not focus on one factor only to attract the investment, but it must create a climate full of temptation to the foreign investor.
- We must seek to diversify the nationality of the foreign investor, and focus as a first step on the Arab ones because of the ease of attracting them.

¹ Zgheib Shahrazad, **Foreign Direct Investment in Algeria** (Arabic source), Journal of Human Sciences, University of Mohammed Khader Biskra, ISSN 8, 2005.

² **FDI** : Foreign Direct Investment.

³ Dr. Sahnoun Farouk, **Measuring the Impact of Some Quantitative Indicators of Macroeconomics on Foreign Direct Investment, Case Study of Algeria**(Arabic source), Magister Thesis, Quantitative Techniques Applied in Management, Faculty of Economic Sciences and Management Sciences, Farhat Abbas University, Setif, 2009-2010, p16.

⁴ [http://unctad.org/en/Pages/DIAE/Foreign-Direct-Investment-\(FDI\).aspx](http://unctad.org/en/Pages/DIAE/Foreign-Direct-Investment-(FDI).aspx) , (accessed May 30 , 2018)

⁵ Dr. Sahnoun Farouk, **Op.Cit**, p.16.

⁶ Clive Collis ,The Role of the Joint Venture mode of Foreign Direct Investment in the development of the Chinese automobile Industry, Conference Paper, Gerpisa colloquium, Paris , 2011.

⁷ https://www.tutorialspoint.com/international_finance/foreign_direct_investment.htm (accessed May 30 , 2018).

⁸ <https://www.collinsdictionary.com/dictionary/english/tax-incentive> (accessed May 30 , 2018).

⁹ <http://unctad.org/SearchCenter/Pages/Results.aspx?k=tax%20incentives> (accessed May 30 , 2018).

¹⁰ http://unctad.org/fr/Docs/iteipcmisc3_en.pdf (accessed May 30 , 2018).

¹¹ Law No. 16-09 of 29 shawwal 1437 corresponding to August 3, 2016, concerning the promotion of investment.

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