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Inward FDI Performance in the Muslim World: Assessing Business and Political Environments

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This article aims to make a survey of business and political environments for inward Foreign Direct Investment performance of the Muslim countries. It offers a cross-country analysis of the 57 Muslim majority countries' FDI performance during 1995-2006. The research finds that the business environment in the Muslim countries is not favourable for smooth transactions, and secondly, there exists a high level of political instability throughout the Muslim world. Unfavourable business environment and a high level of political instability might be held responsible for low FDI performance in the Muslim countries.

1. Introduction

In today's globalised economy foreign direct investment (FDI) is one of the most important factors that primarily contributes to the productivity of a nation's economy. Even developed economies in the world substantially depend on inward FDI for their continuous growth and maintenance of economic performance. The lion share of the world's inward FDI finds its destination in the so-called triad-economy namely the United States, European Union and Japan. The developing countries as well rely heavily on inward FDI for increased productivity and economic development. Without inward FDI, national economic

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development is very difficult to achieve. Liberalisation of trade under the World Trade Organization (WTO) is making the global FDI flows even more significant.

There are certain conditions that facilitate FDI inflows, and not all the countries in the world can create and ensure an inviting environment for that. This is a competitive arena. Therefore, countries that can best create a welcoming environment attract greater and competitive inflows. Recent reports on world investment indicate that the Muslim countries in particular in the developing world are among the most unpopular destinations for FDI. According to a 2001 report, Sweden, a country with nine million people, received $12.7 billion in FDI while the entire Muslim world consisting of 57 countries with a population of 1.27 billion received only $13.6 billion. This is about only 2 percent of the total $735 billion in world FDI in the same year (CCEIA, 2003). Such a poor performance of the Muslim world in attracting FDI naturally begs an analysis of the reasons behind it.

This study makes a cross-country analysis of domestic business and political environment of the Muslim world economies in attracting FDI inflows. It demonstrates that the business environment in the Muslim world is not very friendly, and political instability in the Muslim world is a continuous problem that undermines investors' trust. The study argues that comparatively low performance of the Muslim world economies in attracting FDI might be directly related to its weak business environment and high level of political instability.

2. Literature Review

Studies on Muslim world economies as a special category are comparatively few. However, a number of recent studies have taken increasing interest in analysing the role, importance and performance of FDI in economic growth in the Muslim world. Dabour (2000) made a cross-country analysis of FDI performance of the Muslim countries, and found that the performance of the Muslim economies was unsatisfactory during the 1980s and 1990s. The study, however, failed to elaborate the reasons behind the poor performance. A SUSTRIC (2005) study has made an indirect assessment of FDI performance by looking at the level of integration of the Muslim world economies into the world economy. The study found that even if the countries have extensively adopted

trade and financial liberalization, yet in terms of foreign trade, financial integration, production, trade structure and markets they still are in the process of opening up. Other studies have taken sector specific approach such as socio-economic developmental level (Ozgur *et al*., 2004), human resource development (Bayraktar, 2004), trade and labour standard (Konac, 2001), and private sector investment (Bayraktar, 2003) to assess the Muslim world economies which indirectly talks about the performance in FDI. All these studies have indicated underperformance of the Muslim world economies in the concerned sectors which indirectly explains relationship with FDI performance.

Another set of study tends to be country, region specific in addressing the FDI issue directly. Tsen (2005) dealt with FDI in manufacturing industry of Malaysia and found that relatively higher level of human resources, market logistics and infrastructure played important roles in attracting FDI. Khyeda (2007) looked at regulatory restrictions and FDI in Egypt, Saudi Arabia and Turkey and found that despite regulatory ease, structural impediments are still paramount. Compared to studies based on market factors, FDI performance based on political factors is explored even less. One recent study by Suliman and Andre (2009) on 29 Sub-Saharan countries has indicated that FDI inflows respond positively to the literacy rate and to improvements in political rights and civil liberties; war events, by contrast, exert strong negative effects on FDI. This is an important study which relates war with FDI performance, but it deals neither exclusively with the Muslim countries, nor with non-war political instability factors.

While these studies have made important contribution in analyzing particular factors, these can offer only a partial answer to the question- why FDI performance is low in the Muslim world. The existing literature suffers from a number of deficiencies. First, most of the literature does not make a cross-country analysis of all the Muslim countries in this regard, which renders a comparative understanding of the Muslim economies impossible. Second, most of the studies use sector specific analysis which leaves out the possible impacts of other important factors unexplored. Third, apparently no study has been done on the impacts of political environment of the countries to make a comprehensive assessment of poor FDI performance. Therefore, this study is important in a way that it integrates both economic and political environments of the countries under study to offer a comprehensive

analysis of the factors which may have direct influence on FDI performance.

3. Methodology

3.1 The Data

The data for this study come from annual reports published by the established international institutions. The data are of three types which are FDI, business environment and political environment in the Muslim world. The Muslim world here refers to all 57 countries that are members to the Organization of Islamic Conference (OIC). Economic data on FDI inflows are sourced from the *World Development Indicators 07* of the World Bank, *World Investment Report 2000 to 2007* by the United Nations Conference on Trade and Development (UNCTAD), *Annul Reports* by the Islamic Development Bank (IDB), and *World Economic Factbook 2007* by Euromonitor International. Data on business environment in each of the Muslim countries is based on the World Bank and the International Finance Corporation's report *Doingbusiness in 2006*. And finally, the political environment of the Muslim countries is analysed based on data from the Political Instability Task Force (PITF) of the Centre for Global Policy at George Mason University.

3.2 Data Analysis

The data are treated using cross-country analysis method. Each type of data is categorized into a number of variables which are then examined across the number of cases. The measurement of FDI performance is approached by using the UNCTAD barometer of *traditional* and *new* or *welcoming* factors. A total of ten, three traditional and seven welcoming factors are considered as main variables to assess the business environment in the Muslim world. The political environment of the Muslim counties under study is assessed by using five main variables which are ethnic violence, genocide, civil mass unrest, political violence, and adverse regime change. Finally, cross-tabulation of all data is done using descriptive statistics.

4. Results and Discussions

4.1 World FDI Inflows

After the year 2000, global FDI inflows recorded continuous downfall until recently. According to the UNCTAD, FDI inflows in 2006 recorded $1,306 billion, compared to $1,411 billion in 2000. Out of the total, $857 billion went to developed countries and $379 billion went to developing countries. The USA, UK and France topped the list in receiving the highest share. A region-wise breakdown of the total inward flows to developing countries downsizes the share further. *Africa* recorded $36 billion which is more than double of 15 billion in 2003. The share of greater *Asia-Pacific* region was $260 billion, of which $200 billion went to South, East and South-East Asian countries where China recorded $69, Hong Kong attracted $43, Singapore $24 and India $ 17 billion. The 14 economies of Arab and west Asian regions recorded $60 billion in total. The *Latin America and Caribbean* region received $84 billion where Brazil and Mexico remained the leading recipients with each securing about $19 billion. Similarly, *Central Asia and Eastern Europe* attracted higher FDI amounting to $69 billion, an impressive increase of 68%. The top five economies namely Russian Federation, Romania, Kazakhstan, Ukraine and Bulgaria of the regions attracted 82% of that total inflow (WIR 2006, 2007, 2008).

4.2 Muslim World FDI inflows

FDI in the Muslim countries is comparatively very low when taken as a group as well as the number of countries and their population size into consideration. Table 1 shows that FDI in 2006 was 117.4 billion which is the highest in a single year during 1995-2006, and was higher than 1995-2000 combined total of 108.5 billion. A trend is clear that since 2002 FDI in the Muslim world has been on the rise every year. However, the Muslim world's global percentage share compared with the total developing economies was quite marginal (9 against 29 per cent).

4.3 Muslim World FDI Inflows Performance Ranking

A country's performance in attracting FDI depends on various factors, and these factors are measured in different ways. The UNCTAD has

developed indices of inward FDI performance and potential. The *Inward FDI Performance Index* measures host countries' performance in receiving inward FDI. The index helps in ranking the countries according to the amount of FDI they attract compared to the size of their economies. It further calculates the ratio of a country's share in global FDI inflows to its share in global GDP. According to the index, a value greater than one indicates a country's higher ability to attract FDI inflows, while a value below one indicates negative ability in doing so. Table 2 shows the world ranking of the Muslim economies measured by *Inward FDI Performance Index* of the UNCTAD.

Similarly, in order to measure a country's potential to attract FDI, the UNCTAD has developed a second set of indices called *Inward FDI Potential Index* consisting of 12 structural variables. Combining the two indices namely the *Inward FDI Performance* and *Inward FDI Potential* an FDI matrix is produced. This matrix puts countries in one of the following four quadrants:

- Front-runners: countries with high FDI potential and performance
- Above potential: countries with low FDI potential but strong FDI performance
- Below potential: countries with high FDI potential but low FDI performance
- Under-performers: countries with both low FDI potential and performance

According to the 2007 index, the top 39 front runner countries included only 9 Muslim countries. There were 15 Muslim countries among the 34 global totals that were ranked as 'above potential.' Eight Muslim countries were included in a total of 34 countries which were grouped in 'below potential' category; and finally, 15 Muslim countries were among the 35 global totals which were ranked as 'under-performers' (see Table 3). However, the Muslim countries' performance and potential recorded higher than the previous years.

The matrix above shows that during 1993-2002 the Muslim economies have closely maintained the number of front-runners (4-6) though the trend is downwards. The number of 'below potential' countries is on the rise but only slightly (9-10). The number of countries with 'above

potential' has decreased by one-third (from 15-10), while the number of 'under-performers' has increased by one-third (from 15 to 22). Compared to 2002, the Muslim world has performed better in 2005 in all the categories. The number of front runner countries has increased by more than double (from 4 to 9); the number of 'above potential' counties has increased by one-third (from 10 to 15); the numbers of countries with 'below potential' and with 'underperformance' have decreased from 10 to 8, and from 22 to 15, respectively.

So, an overall picture that emerges from the above matrix is that the FDI performances as well as potential of the Muslim economies during 2003-2005 did not improve from 1993-1995 level. The question that naturally arises is why the Muslim world economies' performance is so grim? What are the factors that are responsible for the stagnant trend in FDI performance in the Muslim world economies? Answers to these questions can be found in examining the favourable factors that the UNCTAD considers important for inward FDI performance.

4.4 Favourable factors for inward FDI performance:

There are many factors that attract FDI for an economy. Over the decades, the nature of these factors has evolved and changed owing to the changing nature of international finance and investment. FDI itself became a global competitive financial and investment market. Therefore in such a global competitive environment the factors that attract FDI tend to remain competitively changing. Taking this into consideration, the factors that contribute best to inward FDI performance are classified into two: *traditional factors* and *new factors*.

4.4.1 Traditional factors

The *first* important factor that traditionally accounted for high FDI attraction is availability of natural resources and raw materials. The vast reserve of natural resources in many countries attracted FDI during the early decades of the twentieth century when public as well as big private companies in the West invested heavily in extractive economies around the world such as petroleum and mining.

The ***second*** traditional factor is cheap labour cost. This factor emerged after the 1970s following the high economic growth and high labour cost in the USA, Western Europe and Japan. Multinational companies of

these countries started to relocate their production bases in Asian, African and South American countries to exploit the cheap labour cost in these economies. A clear example of this trend is massive FDI inflows and relocation of global Trans-national Corporations (TNCs) in areas like Southeast Asia, and in countries like China and India recently.

The ***third*** traditional factor is the large domestic market. FDI inflows find their destination in economies where local demand for the product is huge due to heavy absorption capacity because of advanced industrialization, and a huge consumer market because of high per capita income and purchasing power. An example of this factor is the heavy concentration of FDI inflows among the triad economies namely the USA, the European Union and Japan. During 1998-2000 the Triad economies accounted for three-quarters of total global FDI inflows, and 85 per cent of outflows. During the same period its inward FDI stocks and outward FDI stocks remained 59 per cent and 78 per cent, respectively. The developed countries' share even surged further in 2004 when they accounted for over 90 per cent of total outward FDI. This is obviously due to the fact that the triad economy is home to most of the nearly 65,000 TNCs and about 850,000 subsidiaries worldwide.

4.4.2 New or welcoming factors

Over the past three decades the significance of the traditional factors in inward FDI performance has waned due to more strategically and technically important factors which are called *new factors* or *welcoming environment* that favour FDI inflows. There are a number of factors that are included in welcoming environment. Some important factors include policy liberalization, rapid technical progress, low transaction cost, image building, new managerial and organizational techniques, and political stability (Singh, 1995; Moran, 2006; Chen, 2000).

First, policy liberalization is the key to attract FDI today. Policy liberalization includes among others, ease of entry and exit (starting and closing a business), appropriate standard of treatment and dispute settlement, reduction of tariff barriers, and transparent regulatory framework. The transparent regulatory framework is highly associated with good support (Shatz and Venables, 2000; Yang *et al.,* 2000).

Second, rapid technical progress or change is inevitable for attracting FDI inflows. New transport, faster delivery service, latest communication and information technology allow firms to spread and operate international investment and business more efficiently and smoothly. Investors usually come with latest technologies for operation, so the host countries must have the ability to provide the complementary human capital, infrastructure, supplies and institutions to operate technologies efficiently and flexibly (Billington, 1999; Cheng and Kwan, 2000; Noorbakhsh *et al.,* 2001).

Third, low transaction cost is a factor of paramount importance for FDI inflows. Transaction cost can include a wide range of costs such as interest rate, fund transfer, royalties and fees, tariffs, permission and registration, and bribery. Low transaction cost in these fields invites higher FDI inflows (Cheng and Kwan, 2000).

Fourth, image building and good support ensure market predictability and stability, non-discriminatory standard treatment, competitive business environment and friendly political support. A country with a reputable image of investment friendly welcoming environment consisting of all the factors is able to attract higher FDI inflows (Ewi-Ghee, 2001).

Fifth, new managerial and organizational techniques put emphasis on careful targeting of core competent sectors in which a country desires to attract FDI (Zhang and Markusen, 1999).

Finally, political stability of a country is a major factor that helps in predictability of business environment on a long term basis. Political stability guarantees stable FDI regimes, low risk and steady return for investment (Noorbakhsh *et al.,* 2001).

4.5 Assessing the Factors for Poor FDI Inflows in the Muslim Economies:

In order to explain why the Muslim world's performance in FDI inflows is poor, this section will evaluate the traditional and new factors discussed above in the Muslim world economies.

4.5.1 Traditional Factors

1. Natural Resources: petroleum and gas

In terms of natural resources the Muslim world is arguably very rich. Ten among the 57 Muslim countries have the largest petroleum reserve in the world. Seventeen of the Muslim countries have proven reserve of between 1.35 to 563 billion barrels. Algeria, Bahrain, Bangladesh, Brunei, Egypt, Gabon, Indonesia, Iran, Iraq, Kuwait, Libya, Malaysia, Nigeria, Qatar, Saudi Arabia, UAE have the highest level of petroleum reserve (see Table 4). At present Saudi Arabia is the largest oil producing country in the world and the Muslim world holds two-third of world petroleum reserve. In terms of natural gas, the Muslim world has high proven reserve as well. Saudi Arabia, UAE and Nigeria have the fourth, fifth and ninth largest global reserve, respectively (see Table 5). Many of the Sub-Saharan Muslim countries such as Sierra Leone have huge mineral resources like gold and diamond. Again all sub-Saharan Muslim countries along with Bangladesh, Indonesia and Malaysia have some of the highest global concentrations of natural rainforest, tin and rubber. So, in terms of natural primary commodities the Muslim world is considerably rich, and in some cases richer than many highly industrial countries.

However, raw natural resources are no longer a highly attractive factor now in FDI. Countries completely devoid of natural resources such as Hong Kong, Singapore and Taiwan receive the lion share of FDI in Asia. Therefore, low FDI inflow in the Muslim countries despite having high reserve of raw natural resources is not something unexpected. However, it is to be noted that all the large petroleum companies invest heavily in the Muslim world's petroleum industry.

2. Cheap labour cost

Traditionally it is understood that FDI favours a destination where the labour cost is comparatively cheaper. This is so because the companies always want to make profit by cutting production cost. Labour market in the Muslim world is also one of the cheapest in the world. An estimated 545.1 million out of a total 1.2 billion population comprises the labour force of the Muslim world. Compared to that the high income countries have 492.8 million labour force which makes the Muslim world labour market cheaper because of the over-supply of labour.

However, cheap labour cost is no longer a strong factor for high FDI inflow. The labour cost in the Triad and highly developed economies in the North is among the highest in the world, yet these economies continue to remain the most popular destinations for FDI. Similarly, newly industrialized economies in Asia such as Hong Kong, Singapore, South Korea and Taiwan also maintain a very high level of labour cost compared to the Muslim world, yet these economies attract the lion share of FDI in Asia. This is because labour is no longer valued in terms of cost alone, but it is valued more in terms of real productivity, skill and innovativeness. This fact indicates that as cheap labour cost does not necessarily attract FDI anymore, high labour cost does not necessarily deter it either. So the Muslim world's low share in FDI despite cheap labour cost is not something exceptional.

3. Large domestic market

In terms of population size the Muslim world's share is huge. However, distribution of the estimated 1.2 billion population among the Muslim countries is highly uneven as well. Only about ten of the 57 countries host over 70 per cent of the total population. However, large population size does not necessarily indicate large economic market for FDI. The ten most densely populated countries in the Muslim world are among the least developed group of countries. This means that these countries are industrially backward, underdeveloped and thus their per capita income is very low. Total Gross National Income (GNI) of the Muslim countries in 2005 was US$2,352.2 billion, compared to US$34,523.8 billion for the High Income Countries. Accordingly, the average per capita GNI for the 57 Muslim countries was US$1,670 compared to US$35,131 for the OECD countries (IDB 2007). According to another estimate, "an average person in a developed country earned 11.5 times more than a person in a developing country in 1990, the income gap increased to 21.5 times in 2003. In the case of OIC countries the gap grew from 14 to 23 times during the same period" (SESRTCIC, 2005). Low per capita income indicates low purchasing power which means less consumption. Therefore, though the Muslim world has a huge population size, its domestic consumer market is considerably small.

In contrast, the developed countries of the North and the Asian Tigers have huge domestic markets. Due to high income, the purchasing power of the people as well as the rate of consumption in these countries is also

very high. This certainly indicates the business profitability of the foreign investment in these countries.

4.6 New Factors or Welcoming Environment

New factors or welcoming environment is indeed the deciding factor today for greater FDI inflow. The Muslim world's conditions of new factors are far below compared to that of the OECD countries. Table 6 shows average indicators on various factors relating to welcoming environment.

The welcoming environment can be assessed from two perspectives. First, business environment where foreign investors look at a number of factors that make investment or doing business with a particular country smooth and easier. Therefore, the new factors mentioned earlier can be assessed through a number of business environment indicators. Among these indicators are easiness in starting a business, dealing with licences, registering properties, laws of protecting investors, payment of taxes, trading across nations and enforcement of legal contracts in settling disputes. These are the yardsticks related to policy liberalisation, transaction cost, new managerial techniques and image building environment of a destination economy. The easier and smoother the environment is in a country in these indicators the higher the FDI in that country. The Muslim world on an average performs lower in these indicators compared to developed countries.

The second perspective of the welcoming environment is political environment of the host or destination country. Usually, political stability together with high business environment attracts high FDI. Similarly, political instability may deter high FDI regardless of high or low business environment.

4.7 Assessing the Business Environment in the Muslim World

Here the Muslim world countries' performance on business environment or indictors will be based on the report published by *Doingbusiness in 2006* (see Table 6).

1. Starting a business

One of the most important indicators to assess the business environment of an economy is to see how easily and smoothly a new business can be started. In starting a new business, whereas the OECD countries take on an average 6.2 numbers of procedures and 16.6 days to complete, the Muslim world countries take 9.82 procedures and 53.23 days to complete. In this regard, Chad requires the highest number of procedures amounting to 19 and Afghanistan requires the lowest 3. In terms of number of days Surinam, Mozambique, Palestine, Indonesia and Mauritania take longest amounting to 694, 153, 106, 97 and 82 days, respectively. Only Afghanistan, Turkey and Tunisia require fewest days 8, 9 and 11, respectively.

2. Dealing with licences

Licensing is required in doing business overseas. To issue a business license to a foreign company, the OECD countries take an average of 14 procedures to be completed in 149.5 days. The Muslim countries require 18.8 procedures to meet and take 230.15 days to complete. Sierra Leone requires highest number of procedures 48, followed by Burkina Faso and Kazakhstan 32 each. Maldives and Uzbekistan require lowest number of procedures- 9, while Pakistan takes 12 followed by Bangladesh and Yemen 13 each. In terms of number of days, Iran scores highest amounting to 668 days followed by Ivory Coast 569, Nigeria 465, Cameroon 444 and Benin 333 days. Tunisia requires the lowest number of days 79, followed by Yemen 107, UAE and KSA 125 and Maldives 131 days.

3. Registering property

In registering properties of the companies, there are big differences between the OECD and the Muslim world countries. The OECD countries require 4.7 procedures and take 31.8 days to complete the registration process. The Muslim world countries maintain corresponding scores of 6.31 and 71.31 in these regards. Nigeria, Algeria and Uzbekistan require highest number of procedures amounting to 16, 15 and 12, respectively; while only Oman requires 2 procedures, the lowest among the Muslim countries. In terms of number of days, Bangladesh scores highest requiring 425 days followed by Afghanistan 252, sierra Leon 235, Togo 212, Surinam 193, Egypt 192 and Malaysia 144, while Saudi Arabia, Kyrgyz Republic., UAE, Turkey, Sudan and Iraq take shortest time ranging between 4-9 days.

4. Protecting investors
Offering attractive protective incentives is also a crucial factor in FDI inflow. Protection incentive refers to legal support in time of difficulties. The OECD countries score 6.3 on disclosure index and 6.0 on investor protection index signifying the higher the score the greater the protection incentives. The Muslim countries maintain 5.43 and 4.43 on the two indexes, respectively. Only Malaysia and Bangladesh offer the highest protection incentives scoring 8.7 and 6.7, respectively. In this regard, Malaysia, Bangladesh, Kuwait (6.3) and Pakistan (6.3) outperform the OECD average, and Kyrgyz Republic maintains equal status with the OECD countries.

5. Paying tax
Tax payment to the host country by foreign investors is a matter of competition and negotiation. Usually countries which charge fewer or lower tax attract higher FDI from global multinational companies. Therefore, to attract higher FDI, many countries initially offer even tax holidays for big companies. However, countries normally impose various types of tax on investment as well as profits. So, the countries that offer competitive tax incentives such as number of taxes to be paid, rate of tax on profit and payment facility are among the top concerns of the investors. The OECD countries charge on an average 15.3 different taxes, impose 47.8 percent tax on profit. In the OECD countries, companies need to spend 202.9 hours on an average to pay the taxes.

In the case of Muslim countries, the average number of taxes is as high as 38.10. Uzbekistan is the only country that imposes highest number of taxes amounting to 130, followed by Kyrgyz Republic 89, Benin 72, Sudan 66, Chad 65 and Algeria 61. Six Muslim countries impose number of taxes ranging from 50 to 60, and twenty-four countries impose 15-50 different taxes. Maldives and Afghanistan charges 1 and 2 different taxes, respectively. Five other countries charge taxes up to 15.

In comparison to the OECD countries, companies in the Muslim countries spend on an average an impressive 323.36 hours to pay tax. Cameroon scores the highest registering 1300 hours followed by Nigeria 1120, Azerbaijan 1000, and Senegal and Mauritania each 696 hours. In twenty-five countries, the companies spend between 200-500 hours on paying tax. UAE takes lowest amount of time from companies

amounting to 12 hours, followed by Iraq 48, Oman 52 and Saudi Arabia 75 hours.

Percentage of tax rate on profit is lower (46.61) in the Muslim countries compared to that of the OECD countries (47.8). Sierra Leone imposes the highest percentage (277.0) followed by Mauritania 104.3. Sixteen countries impose a percentage that range from 47 to 100, while twenty six countries impose lower than 47 percent. Maldives, Iraq and Uzbekistan impose lowest percentage registering 5.5, 5.6 and 10, respectively.

6. Trading across boarders

In a globalised economy, faster movement of goods from production facilities to consumer markets, or from production bases to assembly line factories is very important. The easier or the less bureaucratic the process is the faster the movement is. The easiness of faster cross-border trade is measured, among others, by the number of documents and signatures required for export and import. For export, the OECD countries require 4.8 different documents and 4 signatures, and for import they require 5.9 documents and 5 signatures.

Compared to the OECD countries, the Muslim countries require 8.56 documents and 16.02 signatures on an average for export. For export, Uzbekistan requires 44 different documents, the highest among the Muslim countries, while Jordan, Saudi Arabia and Tunisia each require only 5 documents. Kazakhstan and Tajikistan each require 14, followed by Uganda 13, Sudan 12 and 33 countries require 6-10 documents. In terms of signature, Iraq requires 70 and Afghanistan 66, the two countries that require highest number of signatures in the Muslim world. Indonesia and UAE each require only 3 signatures, the fewest in number, for export.

Against OECD countries' requirements of 5.9 documents and 5 signatures, the Muslim countries on an average require 11.95 documents and 24.73 signatures for import. Three countries namely Iraq, Ivory Coast and Niger each require 19 documents, while five other countries each require 18 documents for import, and twenty-eight countries each requires 10-17 documents for import. While only nine countries require up to 10 documents, among which UAE requires the lowest number (6). In terms of signatures for import, the Muslim countries maintain a high

number. Iraq requires 75 signatures for import followed by Nigeria 71, Mali 60, Afghanistan 57, Azerbaijan 55, and Niger 52. Seventeen countries require between 20-50 signatures, and twenty other countries require between 5-20 signatures. Only UAE and Maldives require fewest numbers of signatures, 3 and 4, respectively. Four countries are equal to the OECD countries or better.

7. Enforcing contracts
The ease or difficulty of enforcing commercial contracts is determined by following the evolution of a payment dispute and tracking the time and number of procedures involved from the moment a plaintiff files the lawsuit until actual payment. The shorter the time and procedures required the better the enforcing contract environment. The OECD countries require an average 22.2 procedures and 351.2 days to settle the dispute. In contrast, the Muslim countries require an average 41.02 procedures and an impressive 524.31 days to settle the dispute. Uzbekistan requires staggeringly 195 procedures, followed by Iraq 65, Cameroon and Sierra Leon each 58. Only Uganda requires the fewest numbers of procedures (15). This means majority of the Muslim state requires between 15- 58 procedures.

In terms of days, Afghanistan takes 1624, followed by Bangladesh 1442, Surinam 1290 and Egypt 1010 days. Thirty-two countries take 350 days and above, and nine countries take fewer days than the OECD countries. Kyrgyz Republic takes the fewest (140) followed by Kazakhstan 183 days.

4.8 Assessing the Political Environment in the Muslim World

In addition to a friendly business environment, political environment is also considered to be an important factor that influences the level of FDI inflow. Political environment is defined as stability or instability of the overall political system, practices and interactions in a country. Earlier studies have shown a strong positive correlation between high political instability and low FDI inflow (Campos *et al.,* 1999). The political environment factor is particularly relevant for the Muslim world in relation to FDI, as political instability is a dominant phenomenon in many parts of the Muslim world.

Whether or not political instability in the Muslim world has directly affected its FDI is a matter of extensive investigation, but there is strong evidence that instability in general has a negative impact on FDI. Richard has found that instability of the political regime and civil protest are significantly related to long-run economic growth and that a hundred percent increase of these dimensions is associated with a lower real per capita growth rate of two percent and one percent, respectively (Jong-A-Ping, 2006).

Earlier studies have used a number of indicators to measure political instability. For instance, Campos *et al.* (1999) have used seven indicators which are: (1) military coups, (2) constitutional changes, (3) revolutions, (4) cabinet changes, (5) government crises, (6) riots, and (7) political assassinations. Probably the most comprehensive and extensive use of indicators in a similar study is done by Richard who has employed 26 widely used indicators analysing 98 countries. This study has found four dimensions of political instability which are: (1) mass civil protest, (2) politically motivated aggression, (3) instability *within* the political regime, and (4) instability *of* the political regime. Similar indicators such as the number of *coups d'état* or proxies such as the number of political assassinations and political revolutions are also used to measure political instability are used by different other studies (Londregan and Poole, 1990; Barro, 1991). All these studies suggest that a high frequency of incidents in these indicators indicates a high level of instability.

The Muslim world appears to be particularly vulnerable to high political instability, especially after the end of the Cold War and the 9/11 incident in the USA. The Western world has branded the Muslim world as a particular category where it is waging a vigorous two-prong campaign. The first one is a political campaign to liberalise and democratise the political system and pushing the Islamic political ideologues to the corner. The second one is a military campaign to fight against the so-called Muslim terrorists. Both this political and military campaigns have created a strong resistance against the West which in many of the Muslim countries culminated in persistent political violence and instability. The Muslim countries' domestic political instability has increased sharply after the 9/11 incident. In fact, most of the post-9/11 global political instability is concentrated in the Muslim world related directly or indirectly to the Western campaign for liberal democracy and

war against terrorism. Examples may include continuous instability in Afghanistan, Iraq, Sudan, Pakistan, Lebanon, Bangladesh and Indonesia, and occasional instability in all the Muslim countries. According to the *Global Report on Conflict, Governance and State Fragility 2007*, there are nineteen countries in civil war of various degrees at present, of which eleven are Muslim countries, namely Afghanistan, Chad, Iraq, Palestine, Nigeria, Pakistan, Somalia, Sudan, Turkey, Uganda, and Yemen (Marshall and Goldstone. 2007). In addition, Lebanon has experienced cross-border instability in 2006 and civil war in 2008. The Report has identified four countries as "high incidence states" of which two are Muslim countries: Afghanistan and Pakistan. The so-called "war on terror" is apparently concentrated in the Muslim world, especially in the Middle East and South Asia.

In studying political instability in the Muslim world, Gurr *et al.* (2005) have used five particular indicators. These indicators are: (1) regime type, (2) bordering states with any type of armed conflict, (3) infant mortality, (4) minority rule, and (5) leaders' years in office. Assessing these indicators, the study found that political instability in the Muslim world over the last half-a-century has remained very high. It found that the percentage of counties experienced increase in political instability rose sharply during the 1990s; and the number of new episodes of instability also correspondingly increased during the early years of the 1960s, 1970s, 1980s and 1990s (see Graph 1).

Probably the most comprehensive resource to assess political instability in the Muslim world is the database prepared by the Political Instability Task Force (PITF 2007). The PITF has conducted a survey on *Internal Wars and Failures of Governance, 1955-2006* using five variables: (1) ethnic wars, (2) revolutionary wars, (3) genocides, (4) politicides (politically motivated killing), and (5) adverse regime change. The survey found 54 cases of political instability in Muslim countries between 1955 and 2003 during which the late 1960s and early 1990s were found to be peak periods. The average number of new episodes per year in the Muslim world was 1.78 in 1990-98 which is much higher than previous decades. A total of 14 new episodes of political instability occurred in Muslim countries in the 1990s, nine in sub-Saharan Africa and four in former communist states. Such finding of the PITF is supported by another study which suggests that the Muslim factor was closely linked to instability in Africa: 70 percent of predominantly

Muslim countries in Africa south of the Sahara experienced instability in the years after state formation whereas only one-third of non-Muslim African countries did (Gurr *et al.,* 2005). Though in the late 1990s, instability in Muslim countries declined significantly, it increased rapidly after 9/11 incident in 2001, and by 2003, 16 percent of Muslim countries were experiencing political instability. Table 7 indicates the state of instability measured by high casualty terrorist bombing in the Muslim countries. During 1995 to 2007, a total of estimated 505 cases of terrorist bombings resulting in at least 15 deaths per incident occurred in 14 out of total 57 Muslim states. Most of these incidents occurred in the Middle Eastern, North African and South Asian Muslim states.

As to the indicators used in the PITF survey, *adverse regime change*—characterized by military coups, revolution, and collapses of state authority—was found to be the most common cause of political instability in Muslim countries, occurring 46 times since 1955. Table 8 indicates that during 1995 to 2006, there were 67 incidents of military coups in 25 out of total 57 Muslim states. These coups were largely concentrated in the Sub-Saharan and West African Muslim states. *Revolutionary and ethnic wars*, occurring 35 times, have caused significant instability, during that same period. The Task Force identified fifteen of the 36 incidents of *genocide or politicide* that occurred in predominantly Muslim countries. According to the survey, Muslim countries experienced one instability in every four years between 1955 and 2003, which is higher than non-Muslim countries for which one in seven years was recorded. The survey found that Muslim countries have experienced more political instability than non-Muslim countries in the last fifty years.

According to another source, there were 41 instances of political violence and instability during 1990-2007 in the Muslim world in connection to various causes such as political groups, ethnic tension, and inter-state conflicts. Out of 41 instances, 14 were ongoing in the year 2008 which included Afghanistan, Iraq, Pakistan, Turkey, Lebanon, Sudan and Chad. However, the PITF does not record instability due to opposition politics which disrupts normal economic activities, transportation stoppage and public order. Such type of instability may not involve civilian deaths sometimes. However, they cause severe political instability. For instance, in Bangladesh the opposition parties often call for *hartal* (transportation strike, and total stoppage of all

public activities) to protest against government policy. Such *hartals* may take place locally or nationwide ranging from half-a-day to even for weeks consecutively. According to some conservative estimates, some 611 incidents of *hartals* were called by the opposition parties in Bangladesh during 1995-2002, and an estimated equal number of *hartals* might have taken place during 2003-2006 (Moniruzzaman, 2009). This tactic of opposition politics is also practiced in Pakistan as well. These types of political activities create serious political instability which directly undermines foreign investment. So, if this factor is included in the instability indicators, then it is more likely that the level of political instability in the Muslim world would become higher.

It is clear from the above description that political instability in the Muslim world is a persistent phenomenon, and its level and magnitude are also highest in the world. Whether there is a direct correlation between such high political instability and low FDI in the Muslim world is to be verified through further research. However, as earlier studies generally suggest a positive correlation between the two, it can be assumed that high political instability has significant negative impact on FDI in the Muslim countries. The only Muslim country, after UAE, that has maintained steady and high FDI inflows over a decade is Malaysia where political stability, moderate level of industrial development and technological progress, and a very favorable business environment are found to be the most contributing factors.

5. Conclusions

In the contemporary global economy, FDI finds its destinations in the economies where competitive business environment is offered. The traditional factors of natural resources and cheap labour cost do not matter much as determinants of FDI. The highly industrialised countries in the North do not possess abundant wealth compared to the Muslim world, and the labour costs in these countries are among the highest in the world. Similarly, the newly industrialized countries in Asia such as Singapore, Hong Kong, South Korea and Taiwan are devoid of natural resources and maintain a very high level of labour cost. Yet these countries are among the most popular destinations of FDI. In terms of domestic market and consumer size, these countries rank among the top in the world. So this factor appears to be positively related to high FDI inflow.

The Muslim world possesses abundance of natural resources and raw materials, and offers cheap labour cost. But the domestic market size is small as the people's purchasing power is low. This potentially detracts FDI in the Muslim world. However, the biggest problem lies not in these traditional factors of FDI determinants but in the "new factors" or welcoming environment which characterizes the quality of business environment. Several indicators related to business environment suggest that the Muslim world economies are mostly not business friendly. Lack of regulatory changes, bureaucratic stagnation and high cost of operation are among the major weaknesses of the Muslim economies.

In addition to economic factors, the political factor is also largely responsible for low FDI inflow in the Muslim world. Most of the Muslim countries are politically unstable, and many of them are categorized as high risk countries. Furthermore, political instability in these countries is not temporary; rather it tends to persist for decades. Therefore, political instability makes the weak business environment prone to further risk.

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Appendices:

Table 1: FDI inflows to the Muslim World
(US$ Billions)

Regions	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Muslim World	18.2	24.6	25.1	15.5	13.5	11.6	17.7	24	33.9	45.4	69.1	117.4
% of world	5.4	6.3	5.1	2.2	1.2	0.8	2.1	3.9	6.1	6.4	7.5	9.0
Developing Economies	121.3	157	205.4	205.8	248.7	275.8	232.9	176.4	179.0	283.0	314.3	379.0
% of world	35.6	40	42	28.9	22.6	19.6	28	28.6	31.7	32.0	33.2	29.0

Sources: *Annual Report 2007* (IDB); *World Investment Report 2006*, *2007* (UNCTAD).

Table 2: Ranking of the Muslim Countries by inward FDI Performance Index, 2004-06

Economy	World Rank	Index value		Economy	World Rank	Index value
Albania	60	1.737		Malaysia	62	1.693
Azerbaijan	12	5.436		Mali	71	1.447
Bahrain	11	5.494		Morocco	55	2.003
Bangladesh	121	0.428		Mozambique	84	1.171
Benin	109	0.627		Niger	127	0.338
Brunei	51	2.090		Nigeria	66	1.594
Burkina Faso	132	0.209		Oman	88	1.051
Cameroon	101	0.769		Pakistan	89	1.045
Côte d'Ivoire	99	0.777		Qatar	68	1.505
Egypt	33	2.765		Saudi Arabia	63	1.630
Gabon	67	1.542		Senegal	128	0.329
Gambia	13	5.371		Sierra Leone	54	2.046
Guinea	75	1.393		Sudan	19	4.163
Guyana	20	3.936		Suriname	3	9.454
Indonesia	95	0.908		Syria	98	0.784
Iran	133	0.117		Tajikistan	16	4.548
Jordan	8	6.357		Togo	76	1.375
Kazakhstan	26	3.181		Tunisia	41	2.480
Kuwait	136	0.078		Turkey	73	1.413
Kyrgyzstan	43	2.461		Uganda	77	1.370
Lebanon	14	5.362		UAE	24	3.316
Libya	81	1.246		Uzbekistan	118	0.499
				Yemen	140	- 0.520

Source: Adopted from UNCTAD, *World Investment Report 2007*, Geneva: The UN.

Table 3: Matrix of Inward FDI Performance and Potential of the Muslim Economies

	High FDI Performance	Low FDI performance
	2003- 2005	
High FDI potential	**Front Runners ((9)** Azerbaijan, Bahrain, Brunei Darussalam, Jordan, Kazakhstan, Malaysia, Qatar, United Arab Emirates.	**Below potential (8)** Algeria, Islamic Republic of Iran, Kuwait, Libya ,Oman, Saudi Arabia, Tunisia, Turkey.
Low FDI potential	**Above potential (15)** Albania, Egypt, Gabon, Gambia, Guyana, Kyrgyzstan, Lebanon, Mali, Morocco, Mozambique, Sierra Leone, Sudan, Suriname, Tajikistan, Uganda.	**Underperformers (15)** Bangladesh, Benin, Burkina Faso, Cameroon, Côte d'Ivoire, Guinea, Indonesia, Niger, Nigeria, Pakistan, Senegal, Syria, Togo, Uzbekistan, Yemen.
2000-2002		
High FDI potential	**Front Runners (4)** Brunei, Malaysia, Jordan, Guyana.	**Below Potential (10)** Bahrain, Egypt, Iran, Kuwait, Lebanon, Libya, Oman, Qatar, Saudi Arabia, United Arab Emirates.
Low FDI potential	**Above Potential (10)** Albania, Azerbaijan, Gambia, Kazakhstan, Mali, Morocco, Mozambique, Sudan, Tunisia, Togo.	**Under-Performers (22)** Algeria, Bangladesh, Benin, Burkina Faso, Cameroon, Cote de Ivorie, Gabon, Guinea, Indonesia, Kyrgyzstan, Malawi, Niger, Nigeria, Pakistan, Senegal, Sierra Leone, Suriname, Syria, Tajikistan, Turkey, Uzbekistan, Yemen.
1993-1995		
High FDI potential	**Front Runners (6)** Bahrain, Brunei, Guyana, Indonesia, Malaysia, Qatar.	**Below Potential (9)** Iran, Jordan, Kuwait, Libya, Oman, Saudi Arabia, Surinam, UAE, Uzbekistan.
Low FDI potential	**Above Potential (15)** Albania, Azerbaijan, Cote de Ivorie, Egypt, Gambia, Kazakhstan, Kyrgyzstan, Mali, Morocco, Mozambique, Nigeria, Tajikistan, Tunisia, Yemen, Zambia.	**Under-Performers (15)** Algeria, Bangladesh, Benin, Burkina Faso, Cameroon, Gabon, Guinea, Malawi, Niger, Pakistan, Senegal, Sierra Leone, Syria, Togo, Turkey.

Source: Adapted from UNCTAD, *World Investment Report 2004*, *2006* and *2007*.

Table 4: Oil Reserve in the Muslim Countries

Billions of barrels

	1-10	11-50	51-100	101-150	151-200	201-250	251-300	301-563
Countries (*n*)	**6**	**5**	**2**	**2**	**0**	**0**	**1**	**1**

Millions of Barrels

	1-10	11-50	51-100	101-150	151-200	201-250	251-300	301-900
Countries (*n*)	**6**	**3**	**1**	**3**	**1**	**0**	**1**	**5**

Source: compiled from *Euromonitor International 2007*. London: Euromonitor International Inc.

Table 5: Gas Reserve in the Muslim Countries

Trillion Cubic Feet

	1-10	11-50	51-100	101-150	151-200	201-250	251-300	301- 945
Countries (*n*)	**3**	**3**	**4**	**0**	**0**	**3**	**0**	**2**

Billions of Cubic Feet

	1-10	11-50	51-100	101-150	151-200	201-250	251-300	301-945
Countries (*n*)	**9**	**3**	**1**	**1**	**2**	**0**	**0**	**0**

Source: compiled from *Euromonitor International 2007*. London: Euromonitor International Inc.

Table 6: Business Environment in the Muslim World

	OECD*	Muslim World**		
Variables	Average	Average	Max	Min
Starting a business				
Procedures (n)	6.2	9.82	19 Chad	3 Afghanistan
Days (n)	16.6	53.23	694 Surinam	8 Afghanistan
Dealing with License				
Procedures	14	18.8	48 Sierra Leone	9 Maldives
Days	149.5	230.15	668 Iran	79 Tunisia
Registering property				
Procedures	4.7	6.31	16 Nigeria	2 Oman
Days	31.8	71.31	425 Bangladesh	4 UAE
Protecting investors				
Disclosure index***	6.3	5.43	10 Malaysia	0.0 7 countries
Protection index***	6.0	4.43	8.7 Malaysia	0.7 Afghanistan
Paying tax				
Number of tax	15.3	38.10	130 Uzbekistan	1 Maldives
Hours spent	202.9	323.36	1300 Cameroon	12 UAE
Rate (% of profit)	47.8	46.61	227 Sierra Leone	5.5 Maldives

Table 6: Business Environment in the Muslim World (Contd)

	OECD*	Muslim World**		
Variables	Average	Average	Max	Min
Trading across border				
Documents req for export	4.8	8.56	44 Uzbekistan	5 Tunisia
Signatures req for export	4	16.02	70 Iraq	3Indonesia, UAE
Documents req for import	5.9	11.95	19 Iraq, Niger,	6 UAE Cote d'Ivorie
Signatures req for import	5	24.73	75 Iraq	3 UAE
Enforcing contract				
Procedures	22.2	41.02	195 Uzbekistan	15 Uganda
Days	351.2	524.31	1624 Afghanistan	140 Kyrgyz

Source: Compiled by the author from *Doingbusiness in 2006*, Washington D.C.: The World Bank and International Finance Corporation.

* OECD (Organization for Economic Cooperation and Development) consists of 30 countries: Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Japan, South Korea, Luxemburg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Slovak Republic, Spain, Sweden, Switzerland, Turkey, United Kingdom, and United States.

** Based on data from 46 countries. No data were available for 11 countries: Bahrain, Brunei, Comoros, Djibouti, Gabon, Gambia, Guinea Bissau, Libya, Qatar, Somalia and Turkmenistan.

*** On a 0-10 scale, the higher the score, the better the protection level.

Table 7: High Casualty Terrorist Bombing (death 15+), Sept 1995 - Sept 2007

Year	Incident (*n*)	Death (*n*)	Countries (*n*)	Countries
1995	2	62	1	PAK
1996	2	36	2	SAU, TUR
1997	3	111	2	ALG, EGY
1998	7	211	3	ALG, PAK, TUR
1999	1	16	1	UZB
2000	3	49	2	INS, PAK
2001	2	37	2	BNG, PAK
2002	12	347	6	TUR, PAK, ALG, AFG, BNG, INS
2003	29	556	6	SAU, MOR,IRQ, PAK, TUR, AFG
2004	55	1409	5	IRQ, PAK, SAU, BNG, EGY
2005	115	2452	8	IRQ,LEB,PAK,SOM,INS,AFG,EGY, JOR
2006	130	2696	4	IRQ, AFG, PAK, EGY
2007	144	4185	4	AFG, IRQ, PAK, ALG
Total:	505	12140	14 (of 57)	

Keys: AFG-Afghanistan, ALG-Algeria, BNG-Bangladesh, EGY-Egypt, INS-Indonesia, IRQ-Iraq, JOR- Jordan, LEB- Lebanon, MOR-Morocco, PAK- Pakistan, SAU- Saudi Arabia, SOM-Somalia, TUR-Turkey, UZB-Uzbekistan.

Source: Compiled by the author from database on High Casualty Terrorist Bombing, available at Center for Systemic Peace (Integrated Network for Societal Conflict Research, INSCR), http://www.systemicpeace.org/inscr/HCTBSep07.pdf , accessed on June 14, 2008.

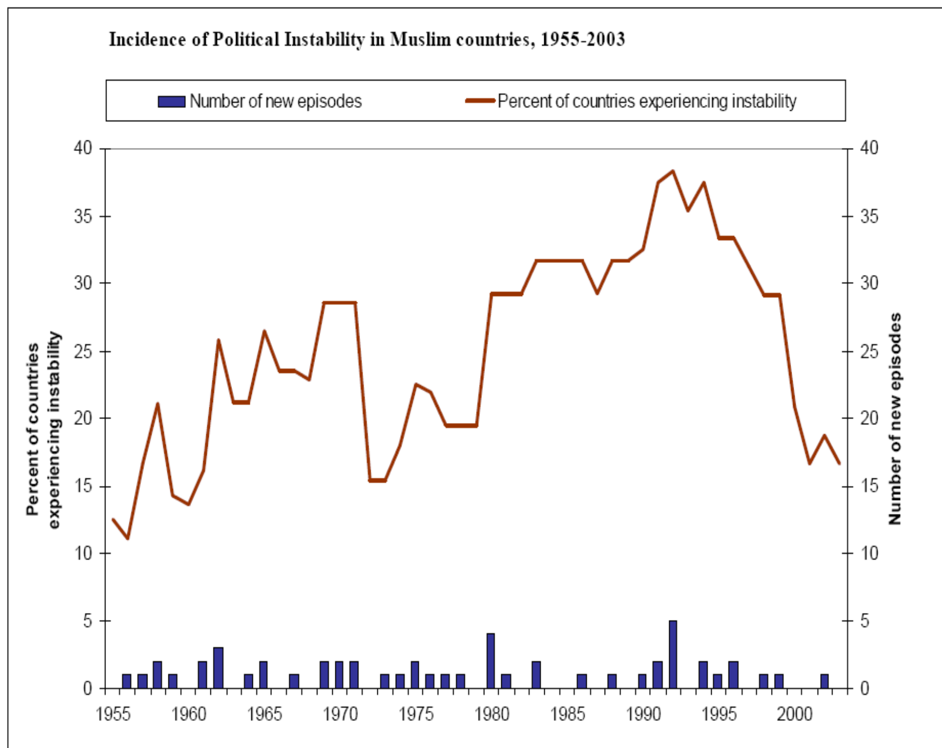
Table 8: Regime Instability (military coups) 1995-2006

Year	Incident (*n*)	Countries (*n*)	Countries
1995	14	11	AZE, BEN, COM, GAM, IRQ, IVO, MAU, NIG, PAK, QAT, SIE
1996	10	9	AZE, BNG, GUI, IRQ, MLI, NIR, QAT, SIE, SUD
1997	4	4	AZE, GUI, NIG, SIE
1998	4	4	AZE, ALB, GNB, NIR
1999	5	5	COM, GNB, IVO, NIR, PAK
2000	5	5	AZE, COM, DJI, GNB, IRQ
2001	2	2	GNB, IVO
2002	3	3	AFG, TKM, IVO
2003	5	5	BFO, GNB, GUI, KYR, MAU
2004	5	3	MAU, NIG, SUD
2005	5	5	AZE, GNB, MAU, OMA, TOG
2006	5	4	CHA, GAM, GUI, MAU
Total	67	25 (of 57)	

Keys: ALB- Albania, AZE (Azerbijan), BEN- Benin, BFO- Burkina Faso, BNG- Bangladesh, CHA- Chad, COM- Comoros, DJI- Djibouti, GAM- Gambia, GUI- Guinea, GNB- Guinea-Bissau, IRQ- Iraq, IVO- Ivory Coast, KYR- Kyrgyzstan, Mau- Mauritania, MLI- Mali, NIG- Nigeria, NIR- Niger, OMA- Oman, PAK- Pakistan, QAT- Qatar, SIE- Sierra Leone, SUD- Sudan, TKM- Turkmenistan, TOG- Togo.

Source: Compiled by the author from database on Coup d'Etat, available at Center for Systemic Peace (Integrated Network for Societal Conflict Research, INSCR), http://www.systemicpeace.org/inscr/CSPCoupsCodebook2006.pdf , accessed on June 14, 2008.

Graph 1: Political Instability in the Muslim World, 1955-2003



Source: Gurr et al. *Forecasting Instability: Are Ethnic Wars and Muslim Countries Different?* Paper presented at the 2005 Annual Meeting of the American Political Science Association, September 1-4, available at http://globalpolicy.gmu.edu/pitf/pitfp5.htm, last accessed on July 14, 2008.