Foreign direct investment in Tunisia:
Performance, policies, prospects

Around the turn of the millennium, Tunisia achieved sizeable rates of economic growth. Given the additional fact of an increasing financial deepening and an emerging industry, the country had been considered by many observers as one of the ‘African Lions.’ However, even before the Arab Spring movements started in Tunisia, the average growth rate was still far from the rate required for a fast catch-up with high income economies. This article aims at analysing the role which foreign direct investment (FDI) has played and can play in spurring economic growth in Tunisia. It analyses domestic saving and investment as well as presents patterns of FDI and present promotional policies. The author argues that foreign direct investment can help to overcome some constraints in capital accumulation and even contribute to ‘inclusive growth,’ i.e., a regionally, socially, and inter-generationally balanced growth pattern. There are, however, two preconditions: capital inflows must be directed by appropriate promotional policies and Tunisia must insulate itself from any negative repercussions from the present political unrest in the Middle East and North African region.

Inwestycje zagraniczne w Tunezji
– realizacje, zasady postępowania, perspektywy

Na przełomie tysiącleci Tunezja osiągnęła wysoki wskaźnik tempa wzrostu gospodarczego. Zważywszy dodatkowo na rozwój rynku finansowego oraz dynamicznie wzrastający przemysł, kraj ten uważany jest przez wielu obserwatorów za jeden z afrykańskich „tygrysów gospodarczych”. Jednakże jeszcze przed wydarzeniami Arabskiej Wiosny, mającymi swój początek w Tunezji, średnia stopa wzrostu była nadal daleka od wartości wymaganych, by dorównać gospodarom wysokodochodowym. Niniejszy artykuł ma na celu analizę roli, jaką odgrywają i mogą odgrywać inwestycje zagraniczne podczas gwałtownego wzrostu gospodarczego w Tunezji. Artykuł ten bada zarówno oszczędności i inwestycje krajowe, jak też obecne wzorce inwestycji zagranicznych oraz prezentuje politykę promocyjną. Dowodzi on, że inwestycje zagraniczne mogą pomóc przezwyciężyć pewne ograniczenia w akumulacji kapitału, a nawet przyczynić się do trwałego „wzrostu sprzyjającego włączeniu społecznemu”, tj. zrównoważonego regionalnie, społecznie i międzypokoleniowo modelu wzrostu. Istnieją jednak dwa warunki wstępne: napływ kapitału musi być kierowany przez odpowiednią politykę promocyjną, a Tunezja musi chronić się przed

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Introduction

Foreign Direct Investment (FDI) is investment from foreign sources intended ‘to acquire a lasting management interest’ in a company in the host country [World Bank, 2014a]. FDI can offer a number of advantages for economies aspiring to an economic catch-up, such as Tunisia. Thus, since the 1990s virtually all newly industrialising and developing economies have not only liberalised their capital markets but have also tried to attract direct investment by a variety of incentives. On the other hand, global competition has increasingly forced companies to shift existing production, to establish additional production lines abroad to avoid disadvantages in the home country, such as increasing labour costs, or to exploit advantages in serving external markets from within a host country rather than by exports [Dunning, 1990].

As a result of the increasing demand for and supply of capital in the form of direct investment, in recent years the global market for this type of capital flows has become more competitive on both sides. Authorities of locations in high demand by foreign investors, such as China, could become more selective in what kind of foreign investment to promote in order to best fill the gaps in the internal economic fabric. On the other hand, given the world-wide interest of countries to host foreign investment, transnational companies (TNCs) have an increasing number of options to optimise their choices on where to set up new production sites in order to optimise their value adding chains. Entry conditions usually depend on the respective bargaining powers of the TNC and the host government [Fagre, Wells, 1982].

This article aims at analysing Tunisia’s stance towards FDI and the promotional policies used to improve its bargaining power. It will start in its first section with an overview on the past performance to attract FDI.

1. Performance

Tunisia looks back on a fifty-year history of integration into the world economy. Following short-lived experiments with an inward-looking development strategy immediately after independence in the 1960s, this choice had suggested itself. Given the small size of the internal market, the scope for the diversification
of national production was limited and substantial foreign trade imperative. In 2008, export of goods and services (especially tourism) had reached a high of 56% of GDP. Since then, however, the share has declined – as a result of the Global Financial Crisis, the Eurozone Crisis, and the Arab Spring movement (which had started in Tunis in December 2010) [World Bank, 2014a].

The opening-up to FDI as a part of an outward-looking development strategy became relevant in the 1990s (see Figure 1). For many years, international observers deemed Tunisia’s political system to be stable – as well as business-friendly, even if nepotistic. Investors’ confidence declined dramatically during the Arab Spring and has not yet risen to pre-crisis level.

![Figure 1. Net inflows of FDI (new inflows less disinvestment), Tunisia, 1990 to 2015](source: [World Bank, 2014a].)

Given the historical relationship and the geographical proximity, it is not surprising that France is the most important country of origin of FDI (38%), followed by Italy (25%) and Germany (8%) [FIPA, 2014]. Presently, more than 3,000 foreign-funded or joint capital companies are operational in Tunisia, generating about one third of the country’s exports and providing about one fifth of total employment [US DoS, 2014].

Tunisia has rather leniently regulated foreign business activity, which is reflected in its high ranking in the World Bank’s Ease of Doing Business Index [World Bank, 2014b]. The workforce includes a large share of semi-skilled and skilled labour based on a lower secondary school completion rate of nearly 80%. On the other hand, the high unemployment leads to low wages. Both factors combine to low unit labour costs. In addition, due to its closeness to the European Union,
the country is considered well serving as an export platform to one of the world’s largest unified markets.

From 2007 to 2013 Tunisia’s energy sector received the bulk of FDI inflows (56%), while manufacturing received 24%, services 19% and agricultural less than 1%. The most important subsectors in manufacturing were the chemical and rubber industry and the electrical and electronics industry [FIPA, 2014]. As shown in Table 1, in terms of employment-generation by FDI, the most important sector is textiles and clothing, followed by the electric and electronic industry.

Some foreign investment in Tunisia resulted from the recent privatisation of state-owned enterprises, especially in infrastructure (such as acquisition of shares of telecommunication operator Tunisiana by Qatar Telecom) but also in other subsectors such as banking (e.g. the acquisition of BT shares by French Crédit Mutuel). Large foreign investments in the energy sector include British Gas, which developed Miskar offshore gas field. Turkish TAV constructed the Enfidha International Airport, predominantly serving the tourism industry. Further large-scale investments include those by Alcatel and Siemens in telecommunications, Sanofi Aventis and Pfizer in pharmaceuticals, Nestlé in food processing, Toyota and Pi-relli in automotive and Zodiac Aerospace in aircraft industry [US DoS, 2014].

### Table 1. Foreign-funded companies per sector and their employment, Tunisia, 2013

<table>
<thead>
<tr>
<th>(Sub-)Sector</th>
<th>Companies</th>
<th>Employment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Manufacturing industries</td>
<td>2,496</td>
<td>282,859</td>
</tr>
<tr>
<td>o/w textiles and clothing</td>
<td>1,096</td>
<td>123,179</td>
</tr>
<tr>
<td>o/w electric and electronic</td>
<td>272</td>
<td>70,013</td>
</tr>
<tr>
<td>o/w mechanical, metallurgy</td>
<td>329</td>
<td>19,871</td>
</tr>
<tr>
<td>o/w leather and footwear</td>
<td>143</td>
<td>19,416</td>
</tr>
<tr>
<td>o/w agri-business</td>
<td>166</td>
<td>14,323</td>
</tr>
<tr>
<td>Services</td>
<td>438</td>
<td>32,583</td>
</tr>
<tr>
<td>o/w call centres</td>
<td>50</td>
<td>14,078</td>
</tr>
<tr>
<td>o/w telecommunications</td>
<td>7</td>
<td>10,021</td>
</tr>
<tr>
<td>Agriculture</td>
<td>80</td>
<td>2,539</td>
</tr>
<tr>
<td>Tourism</td>
<td>148</td>
<td>15,968</td>
</tr>
<tr>
<td>o/w lodging</td>
<td>94</td>
<td>14,965</td>
</tr>
<tr>
<td>Total</td>
<td>3,162</td>
<td>333,949</td>
</tr>
</tbody>
</table>

Source: [FIPA, 2014].

Foreign-funded enterprises in Tunisia usually produce labour-intensive and mainly low-end components. Zodiac, for instance, produces airplane interiors and electrical installation. Some authors believe that foreign-funded enterprises have low propensity to innovate [Kriaa, Karray, 2010; El Elj, 2012]. This holds true
even in high-tech industries. For instance, Sanofis’s main activity (under the name Winthrop) is a laboratory for generic medicaments. A further point of concern for Tunisian policy makers is the high concentration of FDI in the Greater Tunis region and the North East and Central East regions – about one third in each of the three regions in terms of employment created by foreign funded enterprises – while the remaining parts of the country are seldom targeted [FIPA, 2014].

When comparing Tunisia with its most important competitor as a host country for FDI in the North African region, Morocco, three observations stand out. First, while Tunisia’s share in the world’s total stocks has declined over the past two decades, Morocco’s share has increased (Figure 2). Secondly, the relative importance of FDI stocks in the economy (inward stocks of FDI as a percentage of GDP) has heavily increased in Morocco since the turn of the millennium, while there is small change in Tunisia (Figure 3). Finally, inflows of FDI to Tunisia have been heavily affected by the political and economic turbulences since 2009, while Morocco had arguably been perceived as a more stable environment for foreign investment.

![Figure 2. Changes in the share of FDI stocks in the world’s total: developing countries in general and Tunisia and Morocco in particular, 1990 to 2012, Index 1990: 100](image)

Source: Computed with data from: [UNCTAD, 2014].

### 2. The rationale for a FDI-backed catch-up in Tunisia

Given the present difficulties to attract FDI, the Tunisian government would be well advised to increase its promotional endeavours as well as to readjust the targeting. The most important reasons are: first, FDI can contribute to bridging the
gap between domestic saving rates and the investment rates which are required to sustain economic growth; secondly, FDI, if well directed, can improve the quality of growth.

2.1. Supplementing domestic savings and increasing capital formation

During the first years of the new millennium, a number of African countries achieved considerable attention for their economic performance. Egypt, Morocco, Tunisia and South Africa were not only regarded as being able to sooner or later catch up with upper middle and high income countries but were also accredited as potential growth engines for the African region and beyond. In the consultancy industry, the term ‘African Lions’ was coined for these economies in analogy to the ‘East Asian Tigers,’ which ‘leaped forward’ in the 1970s [McKinsey Global Institute, 2010].

Despite this flattery, it is apparent that Tunisia’s average annual growth rate over the past decade has been far from the double-digit growth rates which South Korea and China achieved during their catch-up period [World Bank, 1993]. Today, the GDP per capita in Tunisia amounts to US$ 9,900 (Purchasing Power Parity, 2013 estimates), hence the World Bank classification of Tunisia as an Upper Middle Income Country. Assuming future annual growth rates equal to their previous ten year average, it would take Tunisia 60 years to catch up with the EU average (US$ 34,240; 1.3% average growth rate 2000–2009). Thus, in view of the

Figure 3. FDI Stocks as Percentage of GDP, Tunisia and Morocco, 1990 to 2012
Source: Computed with data from: [UNCTAD, 2014].
prevailing high unemployment and the rapid population growth, spurring economic growth becomes imperative.

An iron law of economics holds that in order to grow, economies must save and subsequently invest a certain proportion of their gross national income. The more an economy can save and invest, the faster it can grow. In other words: crucial to any catching-up process is the readiness of the present generation to forgo (large) parts of their consumption possibilities and increase savings and investments. However, the actual growth rate for any level of saving and investment is determined by the economy's capital productivity. The classical formulation of this law is the Harrod–Domar equation: \( g_Y = s/k \), with \( g_Y \) being the growth rate of GDP, \( s \) the savings ratio and \( k \) the capital-to-output ratio, hence \( 1/k \) being capital productivity.

As a matter of fact, the present investment rates of Tunisia compare unfavourably with those of the fast catching-up economies of East Asia. In the first decade of the new millennium, Tunisia’s gross capital formation hovered around 25% of GDP (see Table 2). Moreover, even in comparison with the ‘average’ lower and upper middle income country, domestic saving rates in Tunisia have been rather low (see Table 3). In contrast, Korea’s domestic saving and investment rates have amounted to over 30% of GDP since the mid-1980s, and China’s saving and investment rates have even exceeded 40% since the mid-1990s.

Table 2. Capital formation, domestic savings and selected forms of capital imports in Tunisia, 1990–2012

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Time period</th>
<th>Percentage of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross capital formation</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>1990–1999</td>
<td>26.0</td>
</tr>
<tr>
<td></td>
<td>2000–2009</td>
<td>24.3</td>
</tr>
<tr>
<td></td>
<td>2010–2012</td>
<td>25.1</td>
</tr>
<tr>
<td>Gross domestic savings</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>1990–1999</td>
<td>21.8</td>
</tr>
<tr>
<td></td>
<td>2000–2009</td>
<td>21.6</td>
</tr>
<tr>
<td></td>
<td>2010–2012</td>
<td>18.1</td>
</tr>
<tr>
<td>Personal remittances received</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>1990–1999</td>
<td>3.6</td>
</tr>
<tr>
<td></td>
<td>2000–2009</td>
<td>4.4</td>
</tr>
<tr>
<td></td>
<td>2010–2012</td>
<td>4.7</td>
</tr>
<tr>
<td>Foreign direct investment, net inflows</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>1990–1999</td>
<td>2.0</td>
</tr>
<tr>
<td></td>
<td>2000–2009</td>
<td>3.8</td>
</tr>
<tr>
<td></td>
<td>2010–2012</td>
<td>2.5</td>
</tr>
</tbody>
</table>

Source: Computed with data from: [World Bank, 2014a].

Admittedly, from the point of view of standard economic theory, a divergence between the national saving rate and the national investment should not be of
concern today. Rather, domestic saving rates should be expected to be uncorrelated with domestic investment rates. The reason is that under the assumption of perfect capital mobility, savers would invest where it is most profitable, which is not necessarily in their home country. Borrowers, on the other hand, would not need the funds from domestic savers if they could borrow from international markets at world rates [Feldstein, Horioka, 1980]. Ultimately, this would lead to an international equalisation of capital returns.

In real world economics, however, this effect has not transpired in spite of the deregulation of the global financial markets. Obstfeld and Rogoff [2000] considered this contradiction as one of the ‘six major puzzles’ in international economics. A hands-on reason for this paradox may be that market distortion is still being created by governments via institutional barriers against capital outflows or by their incentives to invest at home. A more profound explanation is provided by the New Growth Theory [Romer, 1993]. This theory argues that human capital has neutral or even positive returns to scale and increasing rather than decreasing marginal returns. Thus, clustering of human capital (and complementary physical capital) in high-growth and high-profit areas and sectors becomes more plausible in modern, innovation-based economies than an equal dispersion of investment. As a consequence, newly industrialising economies should increase both their investment rates and their domestic saving rates to spur economic growth.

Domestic savings and capital formation can be raised by a variety of public policies, including interest rate policies and the institutional development of the financial system of a country (which is called ‘financial deepening’ by: [Shaw, 1973]). Financial deepening as an instrument for economic development increases the provision of financial services with a wider choice of options available to all kinds of producers and consumers. It allows the mobilisation of domestic savings including those from poorer strata of society and from rural areas, channelling these additional funds to investment. Various indicators for the extent of financial depth exist, including the ratio of domestic credits to the private sector by banks compared to GDP and the ratio of money and quasi money (M2) to GDP.

Admittedly, Tunisia has succeeded in improving its financial systems during the past couple of years. From 1990–1999 to 2000–2009, the banks’ provision of credit as measured by the credit-to-GDP ratio increased from 51% to 55% and the M2-to-GDP ratio increased from 47% to 54% [World Bank, 2014a]. Recently, even more progress has been made (see Table 3). Nevertheless, there is still a far way to go. Small and medium-sized enterprises have difficulties in accessing credits from banks [US DoS, 2014]. Although government regulations hold down lending rates, non-interest costs for borrowing are high, including massive collateral requirements. Apart from bank credits, other financing instruments are not much used. While banks account for 90% of financing, stock market provides only 6 to
7% of total corporate finance. The Bourse de Tunis lists only a few dozen companies. No bond market exists and private equity is a niche market only [US DoS, 2014].

Table 3. Financial sector indicators, Tunisia compared to selected country groups, 2012

<table>
<thead>
<tr>
<th>Country group/country</th>
<th>Lower middle income countries</th>
<th>Tunisia</th>
<th>Upper middle income countries</th>
<th>High income OECD members</th>
</tr>
</thead>
<tbody>
<tr>
<td>GNI per capita</td>
<td>1,045–4,125</td>
<td>4,240</td>
<td>4,126–12,745</td>
<td>12,745</td>
</tr>
<tr>
<td>Indicator as % of GDP</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average gross domestic savings</td>
<td>23.2</td>
<td>15.1</td>
<td>33.0</td>
<td>19.0</td>
</tr>
<tr>
<td>Average gross capital formation</td>
<td>28.7</td>
<td>24.3</td>
<td>32.4</td>
<td>19.6</td>
</tr>
<tr>
<td>Domestic credit to private sector by banks</td>
<td>39.3</td>
<td>72.1</td>
<td>88.1</td>
<td>97.7</td>
</tr>
<tr>
<td>Money and Quasi-Money (M2)</td>
<td>58.5</td>
<td>67.4</td>
<td>119.9</td>
<td>140.9</td>
</tr>
<tr>
<td>Foreign direct investment, net inflows</td>
<td>2.1</td>
<td>3.4</td>
<td>3.1</td>
<td>1.5</td>
</tr>
</tbody>
</table>

Source: [World Bank, 2014a].

As long as these difficulties exist, an easier way to increase investment is by capital imports. Of course, FDI is only one form of capital imports. It is not necessarily a silver bullet nor has it actually been extensively used by all successful catching-up economies. Korea, for instance, relied – in addition to domestic savings – on external credits during its high-growth period and FDI inflows have seldom exceeded the threshold of 1% of GDP. China, on the other hand, embarked on an explicitly FDI-backed growth strategy and used FDI to further increase its already extraordinarily high investment ratio. Even in China, however, FDI has always been a supplement to rather than a substitute for the country’s own endeavours. FDI inflows to China since the mid-1990s have never been larger than 4% of its GDP. Among the newly industrialising economies Malaysia is one of the few exceptions with FDI inflows in comparison to GDP exceeding at least in some years the 5%-ratio. In the case of Tunisia, however, in addition to bridging the gap between the actual and the necessary investment rates, a significant advantage of a FDI-based capital import strategy should not be overlooked: the potential contribution to the improvement of the quality of economic growth.

2.2. Elaborating the complexity of the economic structure

Due to its impact on productivity, foreign direct investment is of higher relevance for newly industrialising countries than short-term capital inflows (portfo-
FDI is usually accompanied by an implicit transfer of more advanced technologies, often supplemented by on-the-job vocational training. Furthermore, foreign-funded enterprises may provide a benchmark for management practices in local enterprises and thus encourage the transfer of up-to-date management know-how. As FDI is geared towards a long-term engagement, it helps to insulate the capital provision from the vicissitudes of international financial markets. When investing in infrastructure, FDI can serve as a substitute for internal capital formation without increasing government debts. Finally, competition increases on the internal market of the host country—a fact which could contribute to optimising factor allocation.

FDI can also be instrumental in influencing the structure of the economy. The impact of the structure of an economy on its overall growth can best be understood by applying Hausmann’s complexity approach [Hausmann et al., 2011]. In this view, the complexity of an economy depends on two factors: directly on the diversity of its products and inversely on their ubiquitousness. An economy producing and exporting products which many other economies also produce (i.e. ubiquitous products) cannot be considered to have highly specialised knowledge which lays the foundation for future growth. On the other hand, an economy producing and exporting products which only few other countries can produce is presumed to use highly sophisticated knowledge the uniqueness of the export is not a result of the fact that the product is simply rarely found in other countries. Therefore, it is necessary to simultaneously take into account the diversity of a country’s export structure. The reason behind this is that producing only one or a few unique products (such as a rare mineral) while not producing many other products at the same time points to the fact that this economy lacks the knowledge relevant for the production of highly sophisticated products.

Both dimensions are recorded by the economic complexity index ECI [Hausmann et al., 2011]. Based on figures of 2008, Japan’s ECI value (+2.32) and Germany’s (+1.99) were the highest. Both countries export many goods that cannot be produced by many other countries—i.e. their exports are of low ubiquity or high uniqueness. In addition, Japan and Germany produce and export many other commodities. This means that the low ubiquity of some of their export products cannot be supposed to be the result of rarity, but the result of the fact that other economies are not able to produce them. Due to the advantage in terms of knowledge endowment, Japan and Germany have a high growth potential in a post-Heckscher/Ohlin-world, where competitive advantage is no longer generated by the labour and capital costs of a product but by its innovative content (a fact which has been termed ‘Schumpeterian competition’). On the other hand, countries with a low ECI value, such as Angola (-1.793) or Mauritania (-1.907), export a few products which are of relatively high ubiquity and which are usually exported by countries that are not very diversified in their export structure.
Using the 2008 value of the ECI as a yardstick, Tunisia displays the highest economic complexity of all African economies: + 0.294. Its world-wide rank is 47, compared to a rather low rank 80 as far as income per capita is concerned. Given the globally increasing relevance of knowledge-based production, this divergence indicates considerable and quick catching up potential for Tunisia.

The actual contribution of industry to the overall production, however, declined even if slightly during the first decade of the new millennium: industry value added as percentage of GDP dropped from 32% to 30% [World Bank, 2014a]. Manufacturing value added (MVA) grew on average annually by 3.6% in Tunisia – well below the overall growth rate of the economy, and a fact pointing to an insidious de-industrialisation.

Thus, Tunisia needs to be aware that the complexity of its economy may be deteriorating. By locating FDI to diversify the economy and upgrade its complexity, Tunisian authorities can try to reverse this process. Is the Tunisian investment policy conducive for this task?

3. Policies

Different camps in economic policy advise different approaches to promote economic diversification and growth in emerging economies. Basically, a market-optimistic ‘functional approach’ and a state-optimistic ‘selective approach’ [Lall, 2000] can be discerned. While the functional approach seeks to strengthen the working of institutions and markets and argues in favour of a general openness of an economy, the selective approach seeks to directly influence the structure of an economy. However, not only the impartiality of the administration, but also the tools for a careful benefit-cost-analysis of selective interventions are indispensable when applying this approach. In the situation of a catching-up industrialisation, when many traits of the ‘future’ economy can be derived from the example of more progressed economies, the argument can be made in favour of the selective approach. Japan’s catching-up industrialisation in the 1950s to 1970s has often been used as an example for this type of industrial policies. Given, however, the fact that information is missing with respect to designing appropriate industrial policies and to evaluating the benefits and costs of selective interventions, Tunisia so far has rightly chosen to apply a mixture of ‘functional’ and ‘selective’ industrial policies.
3.1. Present instruments

Tunisia’s promotional policies for foreign direct investment date back to the 1990s. The Investment Code (last version of 2009) has given priority to sectors with high employment potential and export-orientation. In view of the low level of physical infrastructure and economic development in the western and southern regions reducing regional economic disparities has been made an additional goal [US DoS, 2014]. A further objective was the protection of local industrial development cores in spite of a general open-doors policy towards capital imports. For this purpose, investment was divided into two categories: ‘off shore’ investment, with more than 70% of final production destined for exports, and ‘on shore’ investment, which to a substantial part aims at the internal market. Incentives for these two categories have been very different. In addition, certain segments of the economy have been discouraged or even exempted from foreign investment, such as restaurants, real estate and the acquisition of agricultural land.

Investment incentives include [see: US DoS, 2014; RoT, 2014]: a tax exemption for profits from investment in priority development areas, tax-free imports of raw materials and an investment subsidy of 8–25% of the total value of the investment (up to US$ 230,000 in general and US$ 715,000 in priority regional development areas). In addition, the government will assume up to 16% of social security costs for the first 7 to 10 years of the investment for the employment of new college graduates. Training costs are also partly covered. Large investments with high job creation potential may benefit from the free use of state-owned land. Additional incentives are available to promote investment in designated regional investment zones in economically depressed areas and in particular sectors, including health, education, training, transportation, environmental protection, waste treatment and R&D.

Presently, a new Investment Promotion Code is being formulated by the new Tunisian government [World Bank, 2013]. Given the prevalent high structural unemployment, Tunisia’s government will have to balance the impact of FDI on technical progress and human capital formation with its impact on employment creation. In addition, explicit risks for the economic and political stability of the host country resulting from foreign direct investment should not be overlooked. These stumbling blocks on the way to a full use of FDI for Tunisia’s economic development will be discussed in the following section.

3.2. Stumbling blocks

FDI may aggravate social inequality in newly industrialising economies. Admittedly, this expectation contradicts the prediction of conventional two-factor models of international trade that wages in labour-abundant developing coun-
tries will increase following a free-trade induced specialisation of the economy on labour-intensive products (Stolper–Samuelson factor price equalisation theorem). However, Kremer and Maskin [2006] predicted a different outcome of economic integration. They considered different types of labour (managing and operational workforce in rich countries, skilled and unskilled in poor ones), i.e. a $n$-factor model, as well as a deep integration into the world economy by shifting production sites in addition to a shallow integration by trading commodities only. Their model of internationalised production predicts only wages for high-skilled workers in developing countries to be high and rising, while low-skilled workers’ wages will be stagnant (in agriculture, informal sector services and local crafts). Basically, the effect of increasing inequality results from two sources: first, the comparatively higher productivity of workers in foreign-funded enterprises as they combine with the workforce and capital of the developed economies in a global production network; second, a low supply of skilled workers from the educational systems of developing countries. This combination explains the relatively high price of skilled labour in developing countries. A further reason is that demand for local products and hence for labour force in locally-funded enterprises tends to decrease as income increases (negative price elasticity of income).

FDI may result in a net creation of jobs – although generalisations should be treated with caution, since less competitive but more labour-intensive local producers can be crowded out. Also, foreign-funded enterprises may fail to establish backward and forward linkages to the local economy, necessary for spillover effects to marginalised regions and traditional economic sectors. The reason is that foreign-funded enterprises tend to import most of their inputs in order to guarantee the high product quality necessary for the output to meet the quality requirements of global value chains. Further challenges for Tunisia will be to create a more regionally balanced growth pattern and the securing of the natural resources for future generations. A permanent adjustment and improvement of incentives, infrastructural preconditions and governance seem necessary [Ezzine, 2014].

Beyond FDI promotion, policies to improve ‘inclusiveness’ of growth will be decisive for sustaining economic development. Although Tunisia seems to be on the right track, there is still a far way to go [Wohlmut, 2014]. Wohlmut emphasises the ‘human’ dimensions of development (health, education) and employment creation. The creation of an environment conducive for the small and medium-sized enterprises, i.e. the potential employment-generating growth engines, the creation of the basic conditions for the absorption of modern technology and effective government are seen to be instrumental for inclusive growth. Kappel and Pfeiffer framed a catalogue of operational preconditions to assess the economic development potential, which include structural transformation and growth of total factor productivity, financial deepening, infrastructure develop-
ment, education, institution building and openness. Also according to the index elaborated from these criteria, Tunisia is among the few African economies which showed some characteristics of the potential for well-founded growth, scoring 18th out of 106 developing countries around the world [Kappel, Pfeiffer, 2013].

Finally, given the strong economic ties between the Maghreb and the Eurozone, there have been negative spillovers from the Eurozone crisis [Bass, Steinbeck, 2013]. And there is still a number of challenges beyond the economic sphere: militant Islamist tendencies within the country cannot be neglected and cause investors to be reluctant. In addition, Tunisia’s neighbour Libya is on the brink of a collapse of government authority if not an outright civil war, causing a substantial refugee problem for Tunisia. To continue a path to economic prosperity, Tunisia must insulate itself from any negative repercussions from the present political unrest in the Middle East and North African region.

Conclusions

Tunisia looks back on a fifty-year history of integration into the world economy. The opening-up to FDI became relevant in the 1990s and capital inflow increased until the onset of the recent crises. Despite a rather lenient regulation of foreign business activity and the participation of foreign firms in the privatisation process, the increase in inflows has lost momentum. This makes the case for an increase in the promotional endeavours. One reason is that the countries’ low savings and investment rate need to be supplemented by capital imports. A second reason lies in the contribution of FDI to improve the quality of economic growth. In particular, FDI can be instrumental in maintaining an already relatively high economic complexity in Tunisia. Given the prevalent high structural unemployment, however, the Tunisian government will have to balance the impact of FDI on technical progress with its impact on employment creation. This may call for a more selective approach to promotional policies.

References


