6

Foreign Direct Investment and Competitiveness

6.1 Introduction

Foreign direct investment (FDI) in the EPZ sector has played a pivotal role in the rapid structural transformation of the Mauritian economy away from sugar towards manufacturing for export over the last two decades. It has been an important engine of export growth, domestic capital formation, technology transfer and employment creation. This chapter examines the role of FDI in developing export competitiveness in Mauritius. It begins with an examination of recent trends in FDI in Mauritius and some Asian economies by industrial branch and investor nationality. It then analyses the determinants of foreign investment in the country. Finally, it focuses on foreign investment incentives and the effectiveness of foreign investment promotion efforts in a comparative perspective.

6.2 Trends in Foreign Investment

Mauritus is one of the earliest economies in Africa to develop as a significant location for export-oriented FDI in manufacturing; foreign investment now makes an important contribution to Mauritian economic activity. In 1995, the ratio of foreign affiliate employment to total employment in Mauritius was 27.7 per cent compared with 5.5 per cent in Malawi, 3.4 per cent in Egypt, 2.5 per cent in Kenya and 0.1 per cent in Algeria.[40] By the standards of Asian comparator countries, however, Mauritius has not been a significant destination for foreign investment. Table 6.1 shows data on foreign investment inflows for Mauritius and Asia for 1985-90 and 1991-96.

Mauritius attracted an average of US$ 18.2 million per year in 1991-96, a small decline from US$ 22.0 million per year in 1985-90. In relation to gross domestic investment, The Mauritian reliance on foreign direct investment (1.9 per cent in 1991-95) is comparable to that of Taiwan, Thailand, India and Sri Lanka, but considerably less than Singapore and Malaysia.

FDI inflows to Mauritius have grown relatively sluggishly during the 1990s, at a time when flows to developing countries in general have been increasing dramatically. Total FDI flows to developing countries nearly trebled from US$ 36.8 billion per year in 1988-92 to a historic record level of US$ 128.7 billion in 1996 (from 21 per cent of global FDI to 37 per cent).[41] If the present trends continue, FDI in the developing

Table 6.1 **Inflows of FDI in Selected Countries(1985-96)**
(US$ mn and % of Gross Domestic Investment)

	Mauritius	Singapore	Taiwan	Malaysia	Thailand	India	Sri Lanka
Average annual inflows (US$mn)							
1985-90	22	2952	879	1054	1017	169	37
1991-96	18.2	5601	1233	4660	1935	1132	127
Av. ann. inflows (% of GDI)							
1985-90	4.5	59.3	5.1	43.7	10.2	1.2	6.9
1991-95	1.9	23.3	2.4	21.3	3.6	1.5	5.1

Source: UN World Investment Report, 1997.

Table 6.2 **Distribution of FDI Arrivals in Mauritian Manufacturing 1985-1997** (US$ mn)

Industry	Annual FDI Arrivals *1985-89 (a)*	*1990-92 (b)*	*1993*	*1994*	*1995*	*1996*	*1997*	Cumulative FDI Arrivals *1984-89 US$ mn*	*1984-89 Share %*	*1990-97 US$ mn*	*1990-97 Share %*
Textiles	3.9	1.2	2.5	2	20.7	0	0	19.6	30.6	33.7	43.7
Garments	5.3	10.7	1.2	1.1	0.6	0	0	26.4	41.1	22.4	29.1
Leather, rubber & plastics	0.3	0.8	0.2	0	0.6	0	0	1.5	2.3	1.7	2.2
Fancy goods, maquettes & toys	0.1	0.1	0	0.1	0.1	0	0	0.3	0.4	1.1	1.4
Precious stones & jewellery	0.2	0	0.1	0	0.1	0	0	1.1	1.7	0.6	0.8
Electrical & electronic components	0.2	0	0	0	0.1	0.6	0.3	0.9	1.4	1	1.3
Watches & clocks	0.1	0	0	0	0.3	0	0	0.3	0.5	0.6	0.8
Miscellaneous mfg.	2.8	5.3	1.4	0.2	1.2	2.5	1.5	14.1	22	16	20.7
Total manufacturing	**12.8**	**18.2**	**5.4**	**3.3**	**23.6**	**3.1**	**1.8**	**64.2**	**100**	**77**	**100**

Notes: (a) Average annual FDI inflow, 1985-89. (b) Average annual FDI inflow, 1990-92.
Source: Bank of Mauritius

world may exceed that of the developed world within two decades. South, Southeast and East Asian economies (including those shown in Table 6.1) have been the largest developing country recipients of foreign investment, accounting for US$ 81 billion in 1996 (about two-thirds of total developing country FDI) while African economies (including Mauritius) only received US$ 4.9 billion.

FDI in Mauritius is concentrated in manufacturing. However, manufacturing FDI has been more sluggish than total FDI since 1985. Table 6.2 shows data on FDI arrivals in manufacturing by industry which was obtained from the Bank of Mauritius. Between 1985-89 and 1990-97, total manufacturing FDI fell from $12.8 million to $8.4 million per year, a low figure by international standards. A major concern is that the declines in manufacturing FDI reflect sharp falls in inward investment in the traditionally most dynamic sectors for FDI, garments during 1991-97 and textiles during 1992-94 and 1996-97. FDI arrivals in manufacturing as a whole fell between 1993-94 and 1996-97, but rose between 1990-92 and 1994-95; the increase during 1994-95 should, however, be viewed with caution because it is due to one large textile project from India.

Table 6.3 **Top Five Foreign Investors in Mauritius, 1985-97** (US$ mn)

Country	**Total Investment** 1985-89	1990-97	**Annual Investment** 1985-89	1990-97
Hong Kong	18.7	10	3.7	1.2
China	1.9	1.9	0.4	0.2
France	4.6	9.1	0.9	1.1
UK	3.6	4.5	0.7	0.6
Germany	3.8	5.6	0.8	0.7
Total	**32.6**	**31.1**	**6.5**	**3.9**

Source: World Bank (1994a) and Bank of Mauritius.

Low skill activities accounted for 98.1 per cent of the value of FDI actuals in 1985-89 and for 97.9 per cent in 1990-97 while high skill activities accounted for 1.9 per cent and 2.1 per cent respectively in the two sub-periods. There is thus little diversification and upgrading of FDI since 1985. Textiles and garments account for 72.8 per cent of cumulative FDI in 1990-97, followed by miscellaneous manufactures (20.8 per cent), leather and rubber goods (2.2 per cent), fancy goods and toys (1.4 per cent) and precious stones and jewellery (0.8 per cent). Within high skill items, electric and electronic components (1.3 per cent)

Table 6.4 **Sectoral Distribution of FDI in Malaysia and Thailand**
(Share of Cumulative FDI Approvals by Value)

Malaysia		**Thailand**	
Sub-Sector	***Share***	***Sub-Sector***	***Share***
Transport Equipment	19%	Trade & Services	31%
Basic Metal Products	15%	Electric Appliances	16%
Non Metallic Minerals	12%	Construction	9%
Electrical/Electronics	12%	Chemicals	7%
Paper, Printing & Publishing	11%	Finance & Banking	6%
Food Industry	6%	Mining	6%
Fabricated Metal Products	5%	Metal & Non Metals	4%
Textiles & Apparel	3%	Textiles & Apparel	4%
Chemicals	3%	Machinery & Transport Equip.	4%
Rubber & Rubber Products	3%	Food Industry	3%
Other	11%	Other10%	
Top Foreign Investors	*code*	Top Foreign Investors	*code*
Transport Equipment	1,2,8	Trade & Services	N/A
Basic Metal Products	4,1	Electric Appliances	1,2,4
Non Metallic Minerals	1,5,3	Construction	N/A
Electrical/Electronics	1,4,5	Chemicals	1,7,2
Paper, Printing & Publishing	3,2,8	Finance & Banking	2,6
Food Industry	3,1,2	Mining	N/A
Fabricated Metal Products	4,1,3	Metal & Non Metals	N/A
Textiles & Apparel	4,6,1	Textiles & Apparel	N/A
Chemicals	7,1,2	Machinery & Transport Equip.	N/A
Rubber & Rubber Products	4,1,7	Food Industry	1,2,7

Note: Malaysian data is from MIDA , covering 1985-93. Thai data from BOI for 1970-91. Countries define product segment composition of each sub-sector differently. Malaysia excludes FDI in hotels & tourist complexes. Method of calculating FDI is different in each country. Codes: 1 = Japan; 2 = USA; 3 = Singapore; 4 = Taiwan; 5 = South Korea; 6 = Hong Kong; 7 = Europe; 8 = Australia. Strongly-export oriented activities (above 75% for export) are shaded. N/A = not available.

and watches and clocks (0.8 per cent) are both very small. Although electric and electronic components have declined slightly as a share of cumulative FDI in 1990-97 compared to 1985-89 and watches and clocks have increased. Given that these changes individual high skill activities are very small, the trends should be interpreted with caution.

Inward investment in Mauritius has been dominated by a handful of East Asian and European countries. Table 6.3 shows that the top five investors are: Hong Kong, France, Germany, UK and China. These five investors accounted for 40.4 per cent of cumulative FDI in1990-97 compared to 47.7 per cent in 1985-89. Hong Kong (by far the largest single investor, primarily in textiles, garments and sporting goods) has significantly reduced its annual investment between 1985-89 and 1990-97. Chinese, UK and German annual investment have also fallen. Meanwhile, France significantly increased its annual investment over the two periods. French investors are probably the most diversified and have entered garments, leather products, sporting goods, jewellery, watches and clocks and electronic components. German investors have favoured textiles, garments and sporting goods while British investors have focused on textiles and garments. Apart from these, since 1990 there has also been some new Indian investment in textiles, some Malaysian investment in garments and some Japanese investment in fishing and processing of fish.

It is interesting to note the contrast between Mauritius and Malaysia and Thailand in the distribution and origin of FDI (Table 6.4). FDI in both the Asian countries has been concentrated in manufacturing: in Malaysia, it is clustered in transport equipment, basic metal products, non-metallic minerals and electronics, while in Thailand it is more diversified, with trade and services accounting for a large percentage.

The main foreign investors in many of the leading sub-sectors are the same in both countries. Japan is the largest foreign investor, generally concentrating within resource processing industries (chemicals, paper, food); labour-intensive industries (electronics, electrical products, fabricated metal products); and transport equipment. Of other OECD investors, U.S. favours banking and finance, mining and oil and gas industries, and has also been strong in electronics in Thailand, Malaysia and the Philippines; European investors concentrate in chemicals, food and other resource-based activities; and Australian in mining and related activities. NIE outward direct investment tends to be mostly in light manufacturing activities: Korean FDI in footwear, clothing, wood products, and electronics/electrical products; Taiwanese in electronics and other light manufacturing, real estate and pulp and paper products; Singaporean in electronics, food processing and industrial infrastructure.

FDI inflows in Sri Lanka have some similarity with Mauritius, with over 81 per cent of investment in manufacturing (largely textiles, garments and jewellery). Such foreign investment is dominated by Japan and the East Asia NIEs (Hong Kong, Korea, Taiwan and Singapore). Sri Lanka's success in attracting light industrial FDI is noteworthy in view of the prolonged civil conflict; it may be traced to its open door policy towards FDI, unutilised MFA quotas, cheap English-speaking labour, a reasonably efficient bureaucracy, and a good living environment for expatriates.[42]

6.3 Determinants of Foreign Direct Investment

What explains the extent and pattern of inward-investment in Mauritius? In general, international experience suggests that foreign investors go through a three-stage process to select a particular industrial estate location, as summarised in Table 6.5.[43]

- The first stage is an analysis of the large number of the firm-specific variables which push or pull the investor to make the initial decision to invest (through relocation, expansion or consolidation) in a new offshore production location.
- The second stage is the selection of an individual country where a number of national locational factors are examined, including such investment fundamentals as political stability, investment policies, physical infrastructure, skills, a low level of bureaucracy and red tape and the like.
- The third stage, the search for a particular site within a host country, begins usually only once a particular country has been chosen. Depending on the needs of their particular business, investors will evaluate site suitability, distance from transport, labour and input sources, availability of local inputs & distribution network, reliability and cost of utilities services, lease rates and facilities, among other factors.

The mission's interviews with foreign investors and the few available studies suggest that the determinants of foreign investment in Mauritius differ somewhat by industrial activity, market served and nationality of the investor.[44] Export-oriented FDI in textiles, garments and other simple, low skill manufacturing activities were attracted in the 1970s and early 1980s by cheap, literate and bilingual labour; reasonable labour productivity and industrial discipline; preferential access to EC and US markets; political and macroeconomic stability; a low level of bureaucracy and a market-friendly business environment.

Agro-processing investments were induced by the availability of natural resources (like fish);

Table 6.5 **Investment Location Decision-making Process for Foreign Investors**

Location Decision-Making Stages	Factors Affecting Location Decision-making Process
Stage 1: Initial Decision to Invest in an Offshore Location	• Better access to end-user markets
	• Global or regional production and supply strategy
	• Staying ahead of the competition
	• Lowering per unit production costs
	• Technological changes affecting competitiveness
	• Securing access to raw materials
	• Gaining access to technology or skills
Stage 2: Selection of National Location	• Political and macroeconomic stability
	• Favourable foreign investment policies
	• Preferential access to target end-user markets
	• Adequate physical infrastructure and transport services
	• Good supply of trainable labour and adequate skill base
	• Good supplier network and support services
	• Lack of red tape and streamlined procedures
	• Competitive set of investment incentives
Stage 3: Selection of Individual Site	• Physical suitability of the site for industrial process
	• Distance from labour pools & transportation hubs
	• Availability, cost and quality of area labour supply
	• Condition of transportation network and frequency and cost of ground, air & sea freight services
	• Cost and quality of utilities
	• Access to raw material and other inputs
	• SFB and land lease rates and conditions
	• Facilities, services and amenities
	• Capabilities and reputation of management group
	• Good supplier network and support services

Source: Lall, Rao and Wignaraja (1996).

varied micro climates; cheap labour and preferential access to the EC market.

Investments in software activities, (particularly in data entry and labour-intensive developmental work) were induced by cheap, literate, bilingual labour; a spring board to the African market; and a pleasant expatriate living environment.[45] Hong Kong and French investors led the way and others followed.

In the late 1980s and 1990s, however, there has been a significant erosion in the country's locational advantages. As highlighted in Chapter 5, labour costs have risen significantly, labour productivity has declined, and absenteeism and turnover rates have increased. In addition, there is the threat of a reduction or gradual elimination of preferential access to the EC and US markets with the likely re-examination of the Lome Treaty, and there are indications that excessively cumbersome bureaucratic procedures (particularly on investment approvals and work permits for expatriate staff) are a barrier to more inward-investment. Moreover, Mauritius is facing increased competition from lower cost producers in Africa (Madagascar, Kenya and Zimbabwe) and Asia (China, Vietnam, Laos, Bangladesh, Sri

Lanka and India). Of concern is the emerging trend that some leading Hong Kong and French investors, engaged in low skill assembly operations, have begun switching out of Mauritius to other low cost locations in the developing world. Interestingly, about *half the foreign-owned firms in our firm-level survey indicated that they had begun or were considering relocating to other more attractive manufacturing locations in the developing world and Eastern Europe*.

In the medium-term, Mauritius must attract more FDI inflows to maintain manufactured export growth and employment creation. The quality of FDI also matters and it is essential for Mauritius to upgrade FDI from low to high skill activities. The East Asian experience has underlined the link between FDI and growth of merchandise exports, particularly for higher value-added manufactures. FDI has dominated industrial segment such as electronics and electrical machinery; precision assembly and engineering; metal fabrication. The dramatic upgrading of manufactured exports from Thailand and Malaysia, starting from apparel, footwear, electrical appliances and simple machinery in the 1980s, to silicon wafer fabrication, telecommunications and office electronics machinery, and high-end electronics products in the 1990s – was directly the result of increasing sophistication of existing foreign affiliates of MNCs and sustained increases in new FDI.

The mission's interviews with foreign investors shed some light on important structural factors which may indicate why Mauritius has been unsuccessful in diversifying and upgrading FDI as compared with Malaysia, Thailand and other East Asian economies. These include:

- An inadequate *supply of industrial skills*. It is increasingly recognised that a broad range of managerial, financial and technical skills are necessary to support enterprise competitiveness in skill and technology-intensive activities (especially those in electrical and electronics products, machinery and precision instruments) for export markets. While MNCs can provide many high-level managerial and engineering skills from abroad, this is expensive and does not compensate for a lack of skills in the shop-floor and technical labour force. Thus, East Asian host countries that have large supplies of trained and trainable labour (that is, with education and discipline to absorb new skills) have attracted more and higher quality FDI than Mauritius.
- A lack of *suppliers of raw materials, parts and components*. With the adoption of lean manufacturing methods, a base of competitive suppliers becomes of significance to attracting FDI in industries that are highly linkage-intensive. In engineering and electronic activities, for instance, the availability of a range of local upstream industries and small and medium subcontracting activities are vital to flexibility and cost competitiveness. The importance of this is rising as MNCs introduce management techniques like just-in-time deliveries and total-quality-control to their affiliates in order to become cost efficient. In addition, the existence of a strong supplier base permits the host economy to reap more beneficial spillover effects from MNCs and lowers the initial cost to foreign investors of setting up facilities there. Thus, East Asian economies with a strong base of suppliers have attracted more high quality FDI than Mauritius.
- Limited *technological infrastructure*. The importance of an efficient physical infrastructure is for attracting FDI into high skill activities is evident. Less so is the need for a good technology infrastructure for sophisticated FDI. A capable technology support system with good standards, metrology, quality assurance and applied R&D institutions, able to undertake contract research and provide an information base, can allow foreign affiliates to carry out more advanced technological

tasks in the host country and raise the technological capabilities of local suppliers and competitors. Thus, East Asian economies with an efficient and comprehensive technology infrastructure have attracted more high quality FDI than Mauritius.

- Inadequate *local demand* for high technology products. The constraints created by the relatively small domestic market in Mauritius and the lack of dynamism in African regional market are well known and has been addressed elsewhere in the report.

Competing with the increasing number of emerging competitors in Asia and Africa for export-oriented FDI will require a more intensive effort from the Mauritius government than has been the case to date. Mauritius must actively target FDI in the manufacturing sector to upgrade the technology content of its non-traditional exports. This will require a keener understanding of the determinants of foreign investment, and the significant variations according to investor size, industry sub-sector and nationality. It will also require a streamlining of the investment policy regime; a radical transformation of the country's investment promotion strategy and MEDIA; and the development of a strong technical skill, supplier and technology institutional support base.

6.4 Foreign Investment Policy Regime

Investment incentives are widely used by developed and developing countries, with varying degrees of success, as an important element in their inward investment strategies. In the context of globalisation and increasing competition for FDI, many countries are now using fiscal, financial and other investment incentives to divert production from rival locations. There is a wide range of investment incentives in use and for simplicity, they can be divided into three categories:[46]

- *general incentives* – those available to all promoted investments regardless of export-orientation, industrial sector or other specific eligibility requirements;
- *incentives for promoted activities* such as export manufacturing, high technology or strategic industries; and,
- *incentives for specific industries targeted for promotion*, such as electronics, food processing, among others.

While there are significant variations among the profiled countries, in general, most countries have tended to de-emphasise general incentives in favour of targeted activities and specific industries. The most common promote (i) export production; (ii) capital investment and industry upgrading; (iii) advanced technology industries; and (iv) project location in less developed areas or industrial zones. In most cases, the specific measures utilised include income tax holidays and reductions; targeted deductions, credits and allowances; import duty exemptions or reductions; liberal foreign exchange and capital and profits repatriation policies; personal income tax benefits for mangers; government grants; subsidised credit; government equity participation; and other miscellaneous benefits.

The investment incentive environment for Mauritius is still largely governed by the 1993 Industrial Expansion Act. There are six main incentive schemes for foreign and domestic investors which are provided under the Act: Export Enterprise, Pioneer Status Enterprise, Strategic Local Enterprise, Modernisation and Expansion Enterprise, Industrial Building Enterprise, and Small and Medium Enterprise. Table 6.6 shows recent information on the general investment incentives and those for promoted activities for Mauritius, one South Asian country (Sri Lanka) and three East Asian countries (Taiwan, Thailand and Malaysia). Other South Asian economies like India and Pakistan were excluded from the analysis because historically they have not been major recipients of FDI.

Recent tax changes have made the Mauritian package of investment incentives for EPZs very competitive in one major respect in relation to all the Asian comparators. EPZ firms in Mauritius *currently pay no corporation tax over the life of the company* (down from 15 per cent previously) compared to 3-8 year tax holidays in Thailand, 5 year tax holidays in Taiwan and Sri Lanka, and low corporation tax rates in Malaysia. In the case of non-EPZ projects (e.g. those under the Pioneer Status Enterprise Scheme, Agricultural Development Scheme and Offshore Companies Scheme), Mauritius offers a reasonably attractive 15 per cent flat tax rate and a 10 year tax holiday on dividends as well as free repatriation of capital and profits for non-residents. The main advantages of low corporate tax rates is that compliance and administration is much simpler than other schemes and it acts as a significant incentive because it allows investors to keep a larger proportion of profits. However, particularly compared to the East Asian comparators (Taiwan, Malaysia, Thailand), the Mauritius investment incentive regime has *four major weaknesses*:

First, the limited extent to which Mauritius customises and fine tunes investment incentives to attract investors in targeted industrial activities. As discussed in Section 6.5, there is a long list of targeted industrial activities covering 7 industrial sectors – printing & publishing, information technology, jewellery, light engineering, pharmaceuticals, electronics and agro-industry – and the country's outbound investment missions are attempting to attract potential investors in these areas. However, the problem with the current approach is that it does not pro-actively gear up investment incentives to target industrial activities or major international investors. In a world of increasing competition for FDI, there may be a need to attempt to devise tailor-made incentives for a few particularly attractive potential investments. Success in attracting a few flagship MNCs in new areas is likely to translate into others showing interest in the country. Developed countries like the UK and the US have a long history of tailoring their investment incentives to attract specific activities and firms. Singapore is a famous example of an Asian NIE which has tailored its fiscal incentives to flagship MNCs in specific industries as well as offering large government grants and government equity participation. The lesson of the Singaporean experience is that these measures are typically not given in an unconditional fashion but are linked to specific performance requirements. In 1996, for instance, the Singapore announced a cash-grant based US$ 357 million Innovation Development Scheme to attract MNCs in high-technology activities. The Economic Development Board also has a Co-Investment Programme which takes up equity positions in risky projects with foreign and local investors using a US$ 1 billion fund (by the end of 1995, US$ 410 million had been committed to about 24 projects).

Second, the eligibility requirements for investors to qualify for the incentives are not clearly specified for some schemes. The best illustration of this is the Pioneer Status Enterprise (PSE) Scheme which seeks to promote activities which "involve technology or skills which are above the average existing in Mauritius" and speed up technological upgrading. The requirements to be considered for an enterprise using higher technology or skills are not transparent and can leave room for administrative discretion and uneven application of incentives.[47] In addition, there are no evident performance requirements. By early 1995, over 100 projects with varying degrees of technological sophistication have been awarded certificates under the PSE Scheme including those in watches and clocks, informatics, support services to jewellery, support services to printing and publishing, service firms and others. In contrast, the approach adopted by countries like Malaysia and Thailand is to govern access to incentive packages through very detailed list of eligible activities, specified at the 6-7 digit SIC level. These lists are revised periodically, in line with governmental priorities. In the case of Thailand, more labour-intensive activities are not allowed to locate in the already well-developed Bangkok Metropolitan Area.

Third, unlike the other comparator countries, Mauritius has generally not developed strong incentives to promote technological upgrading, increased local value-added, promote linkages with local industries, and facilitate research and development. This is especially true in comparison with Singapore, Malaysia and Thailand, who have actively modified their incentives packages to support favoured activities. Moreover, they have augmented their tax incentives with well-funded programs of technical and financial support to target industries. The gap between Mauritius and these countries is most evident with respect to support for R&D activities, manpower development and linkages with local industry:

- R&D: Malaysia permits a double deduction of approved R&D expenditures; a 10 per cent industrial building allowance for specialised facilities; capital allowances for plant and machinery; double deduction of cash contributions made to approved research institutes; 5 year tax holiday for R&D companies, as well as permission to carry-forward accumulated losses to the post tax holiday period. While the offering of tax incentives to foreign investors ceases to be relevant in Mauritius in view of the permanent tax exemption granted, this increases the value of other incentives to engage in technological effort.
- Manpower development: Malaysia and Singapore offer a double deduction of approved training expenses conducted within factories or at approved training centres, plus direct support from well administered central manpower development funds.
- Development of local linkages. In addition to providing direct incentives to indirect exporters and local suppliers, Malaysia, Singapore and Thailand have well-funded

Box 6.1 East Asian Approaches to Developing Industrial Linkages

In an attempt to spread the technological benefits from inward investment, several East Asian economies have designed impressive programmes to foster the creation of intra-firm linkages between MNC affiliates and local SMEs. Such programmes have contributed to increased local content, improved local technological capabilities, more employment and the creation of additional export capacity in these economies. Well known industrial linkage programmes include the following:

- *Production Networks for Exports, People's Republic of China.* China developed networks of local suppliers by targeting local enterprises in selected provinces into training collaborations with MNCs, focusing on light industrial products, textiles, machinery and electronic goods for export. Over 200 rural export enterprises have benefited.
- *BUILD Program, Thailand.* Under this initiative, active match-making, brokering, technical assistance and information dissemination activities are provided by the Thai BOI to encourage industrial linkages between MNCs and local industries.
- *Vendor Support Program, Malaysia.* The Malaysian program is a comprehensive approach to upgrading local supplier capabilities. Debt financing is available on a preferential basis to participating enterprises, venture capital is provided to local firms. Technical assistance is encouraged through active collaboration with MNCs, and industry-led training initiatives, such as the Penang Skills Development Centre.

Table 6.6 **General Investment Incentives and Incentives for Promoted Activities and Industries, Selected Countries**

A General Investment Incentives

	Sri Lanka	**Mauritius**	**Malaysia**	**Thailand**	**Taiwan**
1. Corporate Taxation	*Standard Tax Rate* 35% standard rate plus a surcharge of 15% resulting in maximum rate of 40.25%	*Standard Tax Rate* 35%	*Standard Tax Rate* 30% regular tax rate; 40% for petroleum companies	*Standard Tax Rate* 30% regular tax rate	*Standard Tax Rate* 25% regular rate
	Taxable Basis world-wide income for resident companies locally sourced income for non-resident companies	*Taxable Basis* resident and non-resident companies are taxed on their net profits earned in Mauritius	*Taxable Basis* locally sourced income for resident companies	*Taxable Basis* world-wide income for resident companies locally sourced income for non-resident companies	*Taxable Basis* world-wide income for resident companies locally sourced income for non-resident companies
2. Income Tax Reductions & Holidays	None	15% flat tax rate and 10 year tax holiday on dividends for companies operating under the (i) Pioneer Industries scheme; (ii) Agricultural Development scheme; (iii) Industrial Buildings Incentive scheme; (iv) Export Services Zone scheme; (v) Film Development Scheme; (vi) Hotel Management scheme; (vii) Offshore Companies scheme; (vii) Offshore Banking scheme 0 % income tax rate over the life of the company in EPZs and 10 year exemption on income tax on dividends	15% income tax rate for 5 years for promoted industries under Pioneer Status or Investment Tax Allowance	3-8 year income tax holiday depending on geographical location Zone 1 – 3 year exemption for 80% exporters & those in IEs and IZs; Zone 2 – 3-7 year holiday for 30% exporters & those in IEs and IZs; Zone 3: 8 year holiday & 50% reduction thereafter for 5 years exclusion of dividends from taxable income during income tax holiday	5 year tax holiday with a four year deferral provision or a five year period of accelerated depreciation on production equipment 4 year tax holiday with deferral provisions on expansion projects, or a 15% investment credit on such projects
3. Income Tax Deductions, Credits and Allowances	*Income Tax Credits* none *Income Tax Deductions/Investment Allowances* 200% deduction of overseas promotional expenses	30% tax credit on the purchase of stock of companies engaged in non-sugar, agricultural, shipping, industrial, manufacturing or tourist activities tax credit based on proportion of each	*Income Tax Credits* None *Income Tax Deductions/Investment Allowances* Investment Tax Allowance: 60% of qualifying capital expenditure for 5 years	*Income Tax Credits* None *Income Tax Deductions/Allowances* Zone 3: double deduction of water, power & transport costs for 10 years from first sales date	*Income Tax Credits* None *Income Tax Deductions/Investment Allowances* 5-20% deduction from income tax for investments in automation equipment or

	Sri Lanka	Mauritius	Malaysia	Thailand	Taiwan
3. *Income Tax Deductions, Credits and Allowances (Cont.)*	200% deduction of R&D expenditures 3 year, 100% depreciation allowance on plant, machinery and equipment	enterprise's export sales: 10-30% export sales receives a 30% credit; 30-50% export sales gets a 45% credit; exports above 50% receive a 60% credit *Income Tax Deductions/Investment Allowances* 50% initial allowance for plant (excluding building) machinery, equipment, and 10-20% straight line depreciation additional 20% depreciation for (i) capital expenditures on industrial premises and hotel construction; (ii) cost of new machinery or plant expenditures on repair of premises are deductible 200% deduction of qualifying export promotion expenses and export credit insurance premiums	Reinvestment Allowance: 50% of capital expenditures 100% industrial adjustment allowance accelerated depreciation for plants & machinery	Zone 3: 25% deduction from net profits costs of project's infrastructure and facilities 5% depreciation for buildings & 20% for machinery	technology, R&D outlays, training or international brand image establishment
	Loss Carry-Over Provision	*Loss Carry-Over Provision*	*Loss Carry-Over Provision*	*Loss Carry-Over Provision*	*Loss Carry-Over Provision*
	indefinite loss carry-forward period	subject to certain conditions, the previous year's losses can be carried-forward one year	indefinite loss carry-forward period	net losses can be carried forward a period of 5 years	net losses can be carried forward a period of 5 years
4. Import Duty Exemptions	no general reductions or exemptions except through EPZs, duty drawback scheme and other export mechanisms	none, except for companies engaged in direct or indirect exports under the EPZ, ESZ, Pioneer Status schemes	100% exemption for all goods not produced locally 2% maximum duty on raw material imports	Zones 1 and 2: 50% reduction of duties on machinery with 10% or above duty rate located in IE or IZ Zone 3: 100% exemption on machinery; plus 5 year, 75% exemption of raw and "essential" materials not produced locally	100% exemption for raw materials, parts and machinery imports

	Sri Lanka	Mauritius	Malaysia	Thailand	Taiwan
5. Foreign Exchange Controls Capital & Profits Repatriation	no exchange controls on current account transactions repatriation of profits, dividends, royalties and interest are unrestricted, but subject to 15% withholding tax	*Exchange Controls* virtually no exchange controls – (i) rupee is convertible on current account; only capital transactions require authorisation; (ii) export and non-resident companies can maintain foreign currency accounts in Mauritius or externally; (iii) export and non-resident companies can borrow freely overseas *Remittance and Repatriation Rules* no restrictions on profits and royalties remittances, and capital repatriation, subject to exchange controls and withholding taxes EPZ and Pioneer Status companies are guaranteed free repatriation of capital (excluding appreciation), profits and dividends withholding taxes for non-treaty countries are 20% on dividends and royalties	no exchange controls on current account transactions no restrictions on repatriations 85% withholding tax on royalties and 10-15% on interest remittances	no exchange controls on current account transactions no restrictions on repatriations 5 year exemption on royalty, goodwill, dividend taxes of 10%	no exchange controls on current account transactions no restrictions on repatriations for FIA companies, subject to 20% withholding tax on dividends FIA firms can repatriate capital gains or capital within 1 year of start-up
6. Personal Income Tax Benefits	None	None	None	None	None
7. Other Incentives	any company under Section 17 of BOI law creating 100 new jobs after 8/11/95 will be eligible to import a duty-free vehicle worth US$30,000	None	capital gains exemption on real property held for a minimum of 5 years additional export incentives (through duty/indirect tax	additional export incentives (through duty/ indirect tax drawback, bonded warehouse, bonded manufacturing warehouse, EPZ); export	additional export incentives (through duty/ indirect tax drawback, bonded warehouse, bonded manufacturing warehouse, EPZ); export

7.

	Sri Lanka	Mauritius	Malaysia	Thailand	Taiwan
Other Incentives (cont)	minimum investment entry requirement for foreign investments to receive BOI incentives is reduced from US$150,000 to US$50,000 requirement to remit export proceeds to Sri Lanka within 180 days will "be relaxed" additional export incentives (through EPZ, bonded manufacturing warehouse, bonded warehouse, duty drawback/ exemption schemes); export credit guarantee & insurance scheme		drawback, licensed manufacturing warehouse, bonded warehouse, free industrial zone, free commercial zone schemes); export credit, credit guarantee & insurance; export-import bank	credit, credit guarantee & insurance; export-import bank	credit, credit guarantee & insurance; EX-IM bank various provisions relaxing equity restrictions, nationality requirements for FIA companies national treatment and protections extended to FIA companies
B Incentives for Promoted Activities					
1. Income Tax Reductions and Exemptions	*Export Manufacturing and Services Projects Using "Higher Technology"* 5 year profits & dividends tax holiday for new & existing firms, followed by 15% tax rate for 15 years exemption from income tax on capital gains resulting from transfer of shares of an enterprise *Large Scale Development Projects* export-oriented & flagship companies: 10-20 year income tax holiday for export-oriented companies, followed by a 15% tax rate for 20 years no income or turnover taxes on income sourced from Sri Lanka for non-resident persons or partnerships engaged	*Export Activities* EPZs – 0 % income tax rate over the life of the company and 10 year exemption on income tax on dividends ESZs – 15% income tax rate over the life of the company and 10 year exemption on income tax on dividends *Strategic Industries* Pioneer Industries – 15% income tax rate over the life of the company and 10 year exemption on income tax on dividends	*Environmental Protection* 15% income tax rate for 5 years for companies involved in storage, treatment & disposal of toxic & hazardous wastes *Research and Development* 5 year income tax holiday for companies undertaking R&D for a specified industry; dividends to shareholders are tax exempt *Small Scale Industries* automatic Pioneer Status (15% income tax rate for 5 years) *Strategic Industries* 10 year income tax holiday or Investment Tax Allowance	*Enterprises Relocating from Zone 1 to Zone 2* 3 year income tax holidays 7 year income tax holiday if they relocate to IEs or IZs[a] *Enterprises Relocating to Zone 3* 8 year income tax holiday, followed by a 50% reduction for 5 years *Research and Development Activities* 3 year extension of income tax holiday period, not to exceed 8 years [b] *Priority Activities*[c] 8 year income tax holiday, regardless of location	*Export Activities and High Technology* lower income tax rate for EPZ industries, exemption from VAT and commodity taxes 5 year holiday with four year deferral provision for enterprises in the Hsinch Science-based Industrial Park

	Sri Lanka	Mauritius	Malaysia	Thailand	Taiwan
	by the company non export-oriented: 10-20 years, followed by a 15% rate for 15 years thereafter *Projects Using Higher Technology, Not Meeting Export Requirement* case-by-case decision by the BOI *Projects Meeting Export Requirement, not High Tech* 15% tax rate for 20 years		*High Technology Projects* 5 year income tax holiday or Investment Tax Allowance		
2. Income Tax Deductions, Credits & Allowances	*Research and Development* 200% deduction of R&D expenditures *Export Activities* 200% deduction of overseas promotional expenses	none for specific activities	*Environmental Protection* 40% initial and 20% annual allowance on capital expenses on facilities for toxic/hazardous waste *Research and Development* 50% capital allowance for plant & machinery used for approved R&D for a period of 10 years Investment Tax Allowance of 100% of R&D activities expenditures of holding or affiliate companies for 10 years 10% initial, and 2% annual Industrial Building Allowance 200% deduction of cash payment for contracted R&D services *Training Activities* Investment Tax Allowance of 100% for 10 years for companies which	*Enterprises Relocating to Zone 3* double deduction of water, power & transport costs for 10 years from first sales date 25% deduction from net profits costs of project's infrastructure and facilities	*Research and Development & Energy Conservation* 2 year accelerated depreciation for machinery designed for R&D, conservation energy 20% deduction from income for R&D outlays 5 year accelerated depreciation on production equipment for firms in the Hsinchu Science-based park 15% investment tax credit for expansion projects in the Hsinchu Science-based park

	Sri Lanka	Mauritius	Malaysia	Thailand	Taiwan
			undertake technical or vocational training		
			100% single deduction of cash contribution made to a technical or vocational training institution		
			200% deduction of expenses incurred on approved training given to manufacturing and non-manufacturing companies employing less than 50 workers		
			10% initial, and 2% annual Industrial Building Allowance		
			Small Scale Industries 50% reinvestment allowance		
			Research and Development accumulated losses during tax relief period can be carried-forward		
			Export Activities 200% deduction of export credit refinancing premium & export promotion expenses d		
			10% initial Industrial Building Allowance		
3. Import Duty Exemptions	*For export-oriented projects* 100% exemption from duties & related charges on plant, machinery & equipment, and on raw materials & other project related goods, for the life of the project *For other projects* 100% exemption for duties & related	*Export Activities* EPZs: exemption from customs duty, import levy and sales tax on plant, equipment, spares, raw materials and components *Strategic Industries* Pioneer industries: exemption form customs duty, import levy and sales tax on plant, equipment,	*Small Scale Industries* 100% of duties on raw materials, components, machinery & equipment not available locally *Environmental Protection* 100% of duties on raw materials, components, machinery & equipment	*Research and Development Activities* 100% exemption from duties on machinery & equipment for 8 years *Priority Activities* Zones 1 & 2: 50% import duty reduction on machinery subject to duty rates 10% or more Zone 3: 100% import duty exemption on machinery	*Export Activities & High Technology Activities* exemption from duties on raw material, parts & machinery imports in EPZs and Hsinchu Science-based Industrial Park

	Sri Lanka	Mauritius	Malaysia	Thailand	Taiwan
3. *Import Duty Exemptions (cont)*	charges on plant, machinery & equipment, and on raw materials & other project related goods, during the project implementation period, as approved by BOI	spares, raw materials and components	*Export Manufacturing* 100% of duties on raw materials, components, machinery & equipment not available locally or of inadequate price/quality *Training Institutions* 100% of duties on raw materials, components, machinery & equipment		
4. Foreign Exchange Controls/ Capital and Profits Repatriation	*Export-oriented projects* exemption from Exchange Control Act ability to (i) operate foreign currency account; (ii) borrow offshore; (iii) access domestic credit market unrestricted repatriation of profits and capital, subject to 15% withholding tax *Large Scale Development Projects* eligibility for exemption from Exchange Control Act	None	None	None	None
5. Personal Income Tax Benefits	*Export-oriented projects* expatriate employees receive 15% income tax rate during first 3 years of project operation *"Flagship Companies"* expatriate employees receive a 15% income tax rate during the tax holiday period	None	None	None	None
6. Other Incentives	*Export-Oriented Enterprises Using Higher Technology* exemption from the Import & Export Control Act	Electronics, jewellery, and engineering firms are allowed to sell unlimited quantities in the domestic market.	None	*Priority Activities* no limit on the percentage of equity held by foreign share-	low-interest financing, cash grants and venture capital investment in the Hsinchu Science-based park

Sri Lanka	Mauritius	Malaysia	Thailand	Taiwan
Export Activities	50% reduction in registration fee on land & buildings for agricultural holdings		holders that are submitted to the BOI within 1996	equity capitalisation of investors' patents or know-how in the Hsinchu Science-based park
duty-free imports of raw materials, intermediate goods, inputs, and capital equipment available through various schemes administered by the EDB, Customs and others	EPZ and ESZ firms can sell 10-15% of their production in the domestic market, with the permission of the ministry of trade			
various EDB schemes: (i) low cost financing up to Rs 1 million to meet 50% of certain export project costs for qualifying export manufacturers and processors; (ii) equity investment for small scale exporters exporting at least 50% of production; (iii) preferential loans for financially ailing export projects; (iv) provision of Pioneering Status for qualifying export projects, providing for equity investment and 50% of costs of technical assistance; product design; seed planting material & breeding stock; airfares for promotion & training; 100% of freight & insurance costs of samples; 100% of cost of product testing; 50% of costs of export packaging; 50% of advertising costs; (iv) 80% grant assistance for Pioneering Export Project Ideas scheme; (v) cash assistance to SMEs to participate in trade fairs; (vi) preferential loans to SME exporters; among other schemes	Pioneer Status industries can sell 100% to the local market under certain conditions			

	Sri Lanka	Mauritius	Malaysia	Thailand	Taiwan
C Incentives for Specific Industires					
1. Income Tax Reductions or Exemptions	*Large Scale Infrastructure Projects* 10-20 year tax holiday depending on project size, followed by 15% tax rate for 20 years *Small Scale Infrastructure Projects* 15% tax rate for a period of 7-10 years depending on project type and size *Tourism, Recreation and Leisure Projects* 15% tax rate for 15 years *Agriculture Sector Projects* 5 year profits & dividends tax holiday; 90% export activities have an additional 15% tax rate for 15 years *Dairy & Livestock Projects* 15% tax rate for 15 years *Training Institutions* 15% tax rate for 10 years *Mining and Non-Renewable Resource Processing Projects* case-by-case decision by the BOI and MOI		*Venture Capital* 100% income tax exemption for venture capital companies *Operational Headquarters Companies* lower income taxes for operational headquarters companies *Forest Plantations* 10 year income tax holiday	*Priority Activities* [c] 8 year income tax holiday, regardless of location	*Emerging Industries* telecommunications information products consumer electronics semiconductors precision machinery & automation aerospace advanced materials fine chemicals and pharmaceuticals healthcare pollution control *Key Technologies* optical electronics computer software applications of advanced materials biotechnology energy conservation advanced sensors industrial automation resource exploitation
2. Income Tax Deductions, Credits & Allowances	None		*Agriculture* 5% allowance on fob value of agricultural product exports 50%/year allowance on crop planting & building/road construction	None	*Venture Capital* 20% tax credit for investments in high-tech or venture capital business for at least 2 years

	Sri Lanka	Mauritius	Malaysia	Thailand	Taiwan
2. Income Tax Deductions, Credits & Allowances			accelerated depreciation of agricultural buildings abatement incentive for integrated agricultural projects *Forest Plantations* 100% Investment Tax Allowance for 5 years *Tourism* 10% initial and 2% annual allowance on capital expenditure on hotel buildings double deduction of approved training expenditures		
3. Import Duty Exemptions	*Large Scale Infrastructure Projects and Export-Oriented Agriculture, Dairy & Livestock Projects* 100% exemption for duties & related charges on plant, machinery & equipment, and on raw materials & other project related goods, for the life of the project *Small Scale Infrastructure, Tourism, Training, and Non Export-Oriented Agriculture, Dairy & Livestock Projects* 100% exemption for duties & related charges on plant, machinery & equipment, and on raw materials & other project related goods, during the project implementation period, as approved by BOI		None	*Priority Activities* Zones 1 & 2: 50% import duty reduction on machinery subject to duty rates 10% or more Zone 3: 100% import duty exemption on machinery	None

	Sri Lanka	Mauritius	Malaysia	Thailand	Taiwan
	Mining and Non-Renewable Resource Processing Projects case-by-case decision by the BOI and MOI			None	None
4. Foreign Exchange Controls/Capital & Profits Repatriation	*Large Scale Infrastructure, Agriculture Sector, Dairy & Livestock Projects* eligibility for exemption from Exchange Control Act *Tourism, Recreation and Leisure Projects* eligibility for foreign borrowings to meet the cost of imported operational items with the prior approval of the Controller of Exchange *Mining and Non-Renewable Resource Processing Projects* case-by-case decision by the BOI and MOI		*Operational/Headquarters Companies* ability to hold and operate foreign exchange account in Malaysia ability to borrow freely in Ringgit up to a maximum of M$10 million in Malaysia ability to borrow freely in foreign exchange overseas or in the Labuan Offshore International Financial Center		
5. Personal Income Tax Benefits	*Large Scale Infrastructure Projects (<US$50 million)* expatriate employees are subject to 15% tax rate during first three years of operation *Large Scale Infrastructure Projects (Flagship Companies >US$50 million)* expatriate employees are subject to 15% tax rate during corporate income tax holiday period *Small Scale Infrastructure, Tourism, Training Projects* expatriate employees are subject to 15% tax rate during first three years of operation	None	None	None	None

	Sri Lanka	Mauritius	Malaysia	Thailand	Taiwan
6. Other Incentives	*Rubber Products* cash grant from EDB based on volume of raw rubber used by exporters *Gems and Jewellery* preferential debt funding for (i) technical assistance; (ii) specialist courses; (iii) product improvement programs from EDB *Electronics* EDB cash grants limited to a maximum of 3% of fob value of annual exports or Rs30 million during first year of commercial operation for new investors; EDB cash grants limited to 3% of the increase in annual export value over the previous year EDB cash reimbursements of various training and testing activities *Spices, Essential Oils, Oleo Resins, Cashew, Herbs and Papain for Export* EDB loans for 50% of buildings, machinery & equipment cost of new processing facilities & cultivation of value-added crops *Fruits, Vegetables, Cut Flowers & Foliage* EDB loans for 50% of costs to procure/produce inputs such as seeds, planting materials EDB loans for 50% of costs to procure/produce inputs such as seeds, planting materials for nucleus farms & contract growing	None	None	*Priority Activities* no limit on the percentage of equity held by foreign shareholders that is submitted to the BOI within 1996	None

Notes:

a Thailand: in the case of relocated enterprises, the tax holiday period starts from the first day the relocated enterprise generates revenue.

b Thailand: income tax incentives for R&D activities require benefiting projects to make investment in R&D activities equivalent to the income tax exemption. Machinery, equipment & Thai personnel used must be approved by the BOI.

c Thailand: "Priority Activities" are (i) basic transportation systems; (ii) public utilities; (iii) environmental protection/restoration; (iv) direct involvement in technological development – e.g., mould, die, jig, fixture, casting industries; (v) basic industries (tools; cutting tools; grinding tools; sintered products; surface treatment; heat treatment; centres for precision machining; electronic connectors; Ni-Cd & rechargeable batteries; batteries or cells; engineering plastics.

d Malaysia: Eligible export promotion expenses include (i) overseas advertising; (ii) supply of free samples abroad; (iii) preparation of tenders for supply of goods overseas; (iv) supply of technical information; (v) exhibits or participation in overseas exhibits approved by MITI; (vi) public relations expenditures; (vii) business travel expenses; (viii) accommodation & sustenance expenses (limited to M$200/day); (ix) cost of maintaining sales offices abroad for promotion of exports.

e Sri Lanka: Export-oriented projects include (i) manufacturing and services projects using higher technology; (ii) large scale development projects; (iii) projects satisfying export requirement but not using higher technology.

Source: Sri Lankan information from "BOI Incentives," 9 November 1995 and "Incentives for the Sri Lankan Exporter", EDB. Other data compiled from various official sources.

programs to develop linkages between direct and indirect exporters through direct financial support, provision of technical assistance, venture capital, and industry-led training initiatives (Box 6.1)

Fourth, there is insufficient monitoring within Mauritius of the investment incentive regimes of competitor countries for foreign direct investment, particularly those in South and East Asia. The Commonwealth mission did not find any evidence of the existence of an up-to-date information system for investment incentives (fiscal incentives, financial incentives and other incentives) in competitor countries nor of local institutional capability within government to compute effective corporate tax rates.[48]

To address these weaknesses, we recommend that *Mauritius undertake a comprehensive appraisal of its investment incentives in a comparative perspective with a view to streamlining and modernising the foreign investment policy regime*. Based on our preliminary work we feel that the appraisal should focus on the issue of providing a limited number of extra financial incentives (e.g. cash grants or equity participation schemes) for particularly attractive potential investments in the target industrial sectors; the issue of clarifying and simplifying the eligibility requirements for the investment incentive schemes (particularly the PSE Scheme); the issue of developing strong incentives to promote technological upgrading, increased value added, and local linkages; and the issue of creating an up-to date information system on investment incentives for competitor countries.

6.5 Effectiveness of Foreign Investment Promotion

There is a wide range of functions which have been undertaken by investment promotion systems in developing countries, reflecting differences in historical circumstances, policy emphasis, resource availability and the capabilities of the government and the private sector. In general, the primary functions can be grouped under four headings:[49]

- investment approval and regulation (e.g. screening and approving investments; monitoring compliance; compiling statistics on investment impact);
- investment facilitation (e.g. trouble shooting problems of investors; assisting in securing of all secondary licenses and permits);
- research and development (e.g. investment policy impact analysis, policy development and advocacy, publications);
- investment promotion (image building, investor services and investment generation).

The foreign investment promotion system in Mauritius, which is highly decentralised and not under the preview of a single agency, currently involves three principal institutions:[50]

- The *Industrial Development Committee* (IDC) screens all new foreign investment applications. This inter-ministerial committee, which is chaired by the Minister of Industry and Commerce and composed of representatives from at least 9 government institutions, only has the authority to recommend investment applications.[51] Final approval to invest needs authorisation from the Prime Minister's Office and a host of secondary clearances are required from other government bodies.
- A *One-Stop Shop*, created in 1990, which provides post-approval services to investors particularly to obtain various government clearances and permits to establish enterprises (including building and work permits and local authority licenses). This institution also provides information on available incentive schemes, advises investors on procedural issues and attempts to resolve bureaucratic problems.

- MEDIA which carries out foreign investment promotion and research and development activities. Formerly, MEDIA had a generalised investment promotion approach which highlighted the locational advantages which Mauritius has and did not emphasise specific activities or markets which offered the highest prospects of success. Recently it has attempted to shift to a more targeted investment promotion strategy which focuses on 7 specific sectors (including printing & publishing, information technology, jewellery, light engineering, pharmaceuticals, electronics and agro-industry). With a small investment promotion budget of US$ 0.4 million in 1995-96, MEDIA commissioned studies highlighting investment opportunities in the target sectors, prepared promotional material, undertook outbound investment promotion missions, participated in overseas trade fairs and provided information to visiting overseas investor delegations.[52] In 1994-1995, MEDIA organised five outbound missions to India, France, UK, Germany and the USA and serviced three inward investment delegations from France, UK and India. It has also commissioned sectoral studies from overseas consultants on several target sectors and attempts to keep them up-to-date. In 1996-97, MEDIA plans to carry out 8 outbound investment promotion missions (including ones to Malaysia, Hong Kong, India, France, Germany and Australia).

The purpose of a country's investment promotion system is clearly to attract concrete investments. Although there have been numerous attempts, it is quite difficult to accurately gauge the effectiveness of a country's investment promotion efforts. Two summary indicators are shown in Table 6.7 for Mauritius and selected Asian countries. The investment realisation rate (i.e. the share of investment approval that is implemented in a given period) is an aggregate measure of effectiveness which is commonly used. The investment realisation rate in Mauritius is quite good; it is below established East Asian NIEs like Thailand and Malaysia, but above new entrants such as Vietnam, the Philippines and Sri Lanka. Another measure of effectiveness is the return on investment promotion agency (IPA) running costs (defined as the ratio of FDI to the annual IPA budget in a given period). This measure should be interpreted with caution because the figures do not take account of the share of investment which a given agency was actually involved in.

Table 6.7 **Investment Realisation Rates and Return on IPA Running Costs, Selected Countries**

Country	Investment Realisation Rate (a)	Return on IPA Running Costs (b)
Mauritius	60%	8.1
Malaysia	72.2%	481.8
Thailand	67.4 %	230.0
Philippines	58.2%	500.0
Vietnam	48.7%	N/A
Singapore	N/A	276.0
Sri Lanka	27.1%	39.0

Note: (a) Based on 1994 performance data. Figures for Mauritius are for 1991-94 and for the rest are the latest estimates.

(b) Ratio of FDI inflow to Investment Promotion Agency (IPA) Budget in1995.

Source: Lall, Rao and Wignaraja (1996); UNCTAD (1996); *Industry Focus*, Jan-Feb 1995 p. 4; BOI (Sri Lanka).

Bearing this in mind, the return on IPA running costs in Mauritius turns out to the lowest among the Asian sample. A final measure of effectiveness is the number of site visits by foreign investors per outbound investment promotion mission. In 1995, for instance, there were only about 11.5 site visits by foreign investors per outbound mission which is a small number by Asian standards.[53] As a comparison, Sri Lanka and Bangladesh receive over 50 site visits by foreign investors per outbound mission. Thus, *according to these simple measures of effectiveness, the record of the Mauritius foreign investment promotion system is rather mixed by Asian standards and there is scope for improvement.*

Our discussions with foreign investors and the government have indicated several negative attributes in the current foreign investment promotion system and strategy in Mauritius.

Table 6.8 **Average Processing Time for Foreign Investment Approvals in Selected Countries**

Mauritius	9-30 weeks
Singapore	3-4 weeks max
Sri Lanka	4 weeks
Thailand	4-5 weeks
Indonesia	5-6 weeks
Taiwan	4-8 weeks
Malaysia	8-12 weeks

Sources: Enterprise-Survey of the Commonwealth Mission; Asiaweek, October 13, 1995; Lall and Rao (1995).

First, there are relatively long delays in getting foreign investment approvals in Mauritius by international standards. Table 6.8 shows the average processing time for FDI approvals in Mauritius (from our enterprise survey) and six other Asian countries.[54] The data indicate that it takes between 9 to 32 weeks to obtain approval in Mauritius compared to 3 to 4 weeks in Singapore, 4 weeks in Sri Lanka, 4 to 5 weeks in Thailand, 5 to 6 weeks in Indonesia, 4 to 8 weeks in Taiwan and 8 to 12 weeks in Malaysia.[55] Singapore is generally regarded as having one of the most rapid FDI approval processes in the World and, in some cases, approval is granted within one week. Impressionistic evidence suggests that a major streamlining of approval procedures has taken place recently in Sri Lanka with an increase in the power and autonomy of the Board of Investment which has cut approval times down to a few weeks compared to several months previously.[56]

The approval process in Mauritius involves several stages and seems over-elaborate. A foreign investor has to submit a detailed proposal to the Industrial Development Committee, receive further clearances from Customs and the Ministry of Labour and final authorisation to invest from the Prime Minister's Office. The Industrial Development Committee stage generally takes about 4 weeks but major delays, sometimes lasting 12 weeks, seem to occur at the Ministry of Labour over the issue of granting of work permits to expatriate technical staff and at the Prime Minister's Office over the issues connected with security clearances for workers and the foreign investor. In contrast, it takes only about one week to get an electricity connection and two weeks for a telephone connection indicating that post-approval services are generally quite efficient.

Second, the Mauritian new targeted investment promotion strategy contains serious design flaws which reduce its effectiveness. Table 6.9 shows the details of FDI targeting strategies in Mauritius, Ireland, Wales, Malaysia and India. Ireland, Wales and, to a lesser extent, Malaysia, are generally regarded as having successful investment targeting strategies, while India has a largely passive and non-selective approach. The data on Mauritius is from the mission's interviews with MEDIA and data on the other countries are from Tillet (1996).

On the basis of the information in Table 6.9, we ranked the overall effectiveness of FDI targeting strategies in the five sample countries. The results indicated that compared to those of more successful countries (e.g. Ireland, Wales and Malaysia), the investment promotion approach in Mauritius could benefit from some "strategic re-engineering". The data show that the targeting strategies of the three successful countries had several features in common: they tended to operate through longer planning cycles (typically 5 years) which gives sufficient time for the initiation, development and implementation of a strategic programme to take effect; they tended to set clear targets and have a range of monitoring criteria which facilitates transparent performance measurement; they tended to have a clear focus with defined target sectors and markets so that resources were effectively allocated; they tended to be very active in targeting potential foreign investors and developing long-term relationships with them in order to induce new investment. The

Table 6.9 **Effectiveness of FDI Targeting Strategies in Selected Countries**

Criteria	Ireland	Wales	Malaysia	India	Mauritius
Length of planning cycle (a)	Long	Long	Long	Short	Short
Clear targets set?	Yes	Yes	Yes	No	Yes
Number of primary target sectors	5	5	20	None officially	7
Examples of target sectors	Electronics, software medical equipment, Finance services	Electronics, Plastics, Vehicles, Business Services	Financial services, Food processing, Telecom Services, HQ operations	—	Printing & publishing, Information technology, Jewellery, Light engineering, Pharmaceuticals, Electronics, Agro-industry
Number of target countries	N/A	4 main, 5 secondary	6 main, 2 secondary	6 main, 4 secondary	10 main, several secondary
Individual firms targeted?	Yes	Yes	Rarely	No	Sometimes
Market awareness of target sectors	High	Medium to High	Low to Medium	Low	Low
Overall rating (b)	1	2	2	3	3

Note: (a) Long term is defined as 3 years plus and short term is one year. (b) Our score based on available information in the table where 1 is good, 2 is satisfactory, and 3 needs improvement.

Source: Adapted from Tillet (1996); Interviews with MEDIA, September 1996.

net result is that the market had a good awareness of target sectors in successful countries.

In contrast, the Mauritian FDI targeting strategy operated on the basis of a short, planning cycle which is closed linked to MEDIA's annual Actions Plans. A one year planning cycle is an insufficient time horizon for formulating and implementing a strategic programme, particularly to attract technologically sophisticated foreign investment. The country's limited financial and manpower resources were also spread too thinly for the strategy to have much impact because of an emphasis on too many varied sectors and target markets (in 1996 there seemed to be 7 target sectors covering much of manufacturing and about 10 main target markets covering Asia, Australia, the US and Europe). There were wasted attempts to try to develop industrial sectors where the island has no obvious short or medium-term comparative advantage (e.g. light engineering) and attract investors from countries were there is likely to be little interest (e.g.

Australia). Additionally, there seemed to be the virtual absence of a regular monitoring exercise to evaluate the performance of the FDI strategy and a lack of basic monitoring criteria in place. Finally, there was a rather passive approach to dealing with potential high profile investors in target sectors and inadequate emphasis on developing long-term relationships with them to induce sustained inward investment. This may stem from an absence of detailed and up-to-date overseas intelligence about potential investors in particular target activities. The net result is that the market had a low degree of awareness of the country's target sectors.

Third, there seems to be insufficient attention paid by the Mauritian government to encouraging expansion by existing MNC affiliates, widely recognised as a crucial aspect of investment promotion in the Asian NIEs and developed countries. MEDIA and other government institutions have tended to focus their financial and manpower resources on attempting to attract new foreign investors to Mauritius and there has been a tendency to overlook the potential for significant new investment by existing affiliates. As discussed in Chapter 4, the mission's interviews with MNC affiliates indicated that some of them felt that the government had lost touch with investor concerns about the environment, particularly in relation to policy uncertainty, cumbersome bureaucratic procedures, lack of skilled manpower, rising labour costs and high sea freight costs/infrequent sailings. The costs associated with encouraging such expansions are

Box 6.2 Singapore's Regional Headquarters Programme

Singapore has one of the most impressive programmes in Asia to attract MNCs to establish regional headquarters (RHQs) in the county. By the end of 1996, over 100 companies had set up RHQs under the programme. The RHQs, which are concentrated in high growth industries (e.g. electronics, chemicals, engineering services, hospitality and franchise management services), carry out a wide range of activities ranging from servicing regional customers to R&D work. In 1996, total business spending by the RHQ sector amounted to S$ 712 million (a 10 % increase over 1995) and 3000 new jobs were created. Of the 22 RHQs awarded in 1996, over half were either Fortune Global 500 firms or leaders in their respective industries (9 of European origin, 6 from the USA and 4 from Japan).

Singapore's relative attraction compared to other Asian centres like Hong Kong is due to several advantages: a strategic geographical location, well-educated professional manpower, excellent infrastructure, low property tax rates, a rapidly growing financial and RHQ sector, and a high quality expatriate lifestyle and attractive tax incentives under the RHQ programme. The Government of Singapore has devised three types of incentive schemes under the RHQ programme: the operational headquarters scheme (OHQ), the business headquarters scheme (BHQ) and the manufacturing head quarters scheme (MHQ). The OHQ scheme offers a 10 % tax rate for corporate income from approved services provided in Singapore and no taxation for income earned by overseas subsidiaries. The BHQ scheme offers incentives under the Economic Expansion Act and tax exemption for offshore companies. The MHQ scheme for firms, which have a significant manufacturing presence in Singapore and provide regional technical services, offers incentives like low corporate tax rates and double deduction of qualifying R&D expenses against income. The RHQ programme is administered by the Economic Development Board and strongly supported by the other government agencies such as the Inland Revenue Authority and the Ministry of Finance.

Source: Singapore Economic Development Board.

Table 6.10 **Characteristics of Investment Promotion Agencies**

Name	Type of Organisation	Annual Budget (Latest Year)	Functional Structure	Private Sector Participation	Civil Service Pay Scale	Investment Screening
CINDE, Costa Rica	Private Association	US$11 million	Facilitator	Yes, private board	No	No
Foreign Investment Promotion Board, India	Government organisation	US$ 2.4 million	Single ministry	No	Yes	Yes
Irish Development Authority, Ireland	Quasi-Government	US$75 million	One-stop shop	Yes	Yes, but with adjustments	Yes
Malaysian Industrial Development Authority, Malaysia	Quasi-government	US$15 million	Facilitator	No	Yes, but with adjustments	Yes
Mauritius Export Development & Investment Authority, Mauritius	Quasi-Government	US$ 3.1 million	Facilitator	Yes, 50% of board consists of private sector	Yes	Yes
Board of Investment, Sri Lanka	Quasi-Government	N/A	One-stop shop	No	Yes	Yes
Board of Investments, Thailand	Government Organisation	US$10 million	Facilitator	Yes	Yes, but with adjustments	Yes
Economic Development Board, Singapore	Quasi-Government	US$45 million	One-stop shop	Yes	Yes, but with adjustments	Yes

Source: Adapted from Lall, Rao and Wignaraja, 1996; Interviews with MEDIA, September 1996.

typically lower than the marketing costs needed to attract new foreign investment while the economic benefits and the effects on the country's image can be significant.

Fourth, a notable gap in the investment promotion strategy of Mauritius is the absence of a programme to induce MNCs to set up regional head quarters for Africa in the country (see Box 6.2 on Singapore's successful regional head quarters programme). Mauritius has the potential to become one of the more attractive sites in Africa for locating regional head quarters. The two important regional competitors are Johannesburg and Harare. Johannesburg's claim comes from a pool of professional manpower and good infrastructural facilities, but it suffers from a negative image problem caused by a high crime rate and highly political trade unions. Harare has a base of educated manpower, good infrastructure, little trade union activity and a pleasant expatriate living environment, but there is some uncertainty in the foreign investment climate due to the Government of Zimbabwe's new indigenisation policy. By comparison, Mauritius offers educated manpower, good infrastructure, little trade union activity, a pleasant expatriate living environment and a stable foreign investment regime. The locational disadvantages – including high labour costs, high air fares and limited land for expansion – are not so significant relative to the many advantages and could be offset by appropriate policy actions including the formulation of a programme to attract MNCs to set up RHQs.

Fifth, although MEDIA has a private sector-oriented Board and a high share of university graduates amongst its staff, it still lacks sufficient autonomy and power to undertake pro-active investment promotion activities. In particular, staff remuneration, budgeting and procurement requirements are subject to public sector rules, and flexibility in hiring, compensating and firing staff is somewhat limited. This makes the process of reforming the organisation from within and hiring and retaining high calibre staff quite difficult. International experience suggests that good practice IPA's are increasing getting more autonomous and powerful and are moving away from standard Civil Service practices governing pay and other operational issues (see Table 6.10).

Thus, we recommend that Mauritius takes steps *to increase the effectiveness of its foreign investment promotion strategy*. It should establish a new specialised agency for foreign investment promotion, as indicated by the Finance Minister. This new agency should be staffed by people with the appropriate private sector experience and offer competitive pay, benefits and comprehensive training. The new agency should place considerable emphasis on targeting selected activities and investors, re-vamping the current investment promotion strategy by carrying out an investor perception study and developing a pro-active approach to investment promotion.

One key element of the pro-active role to investment promotion should be a regional headquarters (RHQ) programme to attract leading MNCs to set up bases for the African region. In this vein, Singapore's RHQ programme offers valuable insights on detailed incentive packages and institutional support.

The current One Stop Shop should be incorporated into the new agency and provide high quality post-approval investor services, such as obtaining work permits and various infrastructure facilities. MEDIA, which currently undertakes investment as well as trade promotion and industrial estate management, should be transformed into a specialised trade promotion organisation, with its management and development of industrial estates hived off to the private sector.

Apart from the above, the approval process must be greatly simplified and streamlined immediately, reducing the number of stages in the approval process to a single stage, centring on one Foreign Investment Approval Committee. This committee should consist of high-level representatives from a maximum of six ministries, chaired by a senior Cabinet minister, and should meet twice a month. A target 2-4 weeks should be set for the completion of the foreign investment approval process under normal circumstances. Difficult cases could be referred to a sub-group of the Foreign Investment Approval Committee which would draw on expertise in all areas of government. An appeals procedure should also be established for cases of investors which have been rejected. This should be followed by the abolition of all foreign investment approval processes and a concentration on investment promotion.