Tax Incentives and the foreign direct investment inflows in Sub-Saharan African Countries

*Elias Igwebuike Agbo (08038972753), Sergius Nwannebuike Udeh (08035554066, sudeh@gouni.edu.ng), and John Onyemaechi Odo (08036766049) **

Abstract

This paper considered tax incentives and foreign direct investment in Sub-Saharan African countries. It employed historical research approach to review the literature on the influence of tax incentives on foreign direct investment in Sub-Sahara African economies, particularly Nigeria. The finds that even as tax concessions, longer tax holidays, withholding tax and other tax expenditures in Sub-Sahara African countries have continued to be in the increase, their impact on FDI has remained generally non-significant. This situation is blamable on the several factors that have played against the business environment for foreign investments in developing countries. Our study recommended that tax incentives should be properly structured to deal with policy lapses by the governments of Sub-Saharan African countries. Otherwise, achieving the main goals such as poverty eradication, sustainable growth and development in the competitive global economy might be unrealizable.

Keywords: Sub-Sahara Africa, Nigeria, tax incentives, tax waivers, foreign direct investment.

1. Introduction

African countries have faced competition and several challenges in striving to attract foreign direct investment (FDI) as a result of the role that FDIs play in the development process (Appiah-Kubi et al, 2021). According to Appiah-Kubi et al. (2021), many of the efforts made became futile as a result of several factors that work against the business environment for foreign investments. There are some motivational factors that influence foreign direct investments in a nation. For several developing countries within Africa, there are some significant economic benefits. Such nations have been able to use the global investment pool and have drastically improved their standard of living(Appiah-Kubi et al., 2021) .As several countries implement a lot of extended venture systems, competitiveness for foreign investors are expected to continue increasing. For this reason, the foreign direct investment decision is increasingly gaining research interest. According to Appiah-Kubi et al.(2021), most researchers have emphasized that factors such as corruption, internal security, rule of law, quality of regulations, the effectiveness of government, voice and accountability, market size and infrastructure, among many others are the economic essentials for investment environment (Love & Klapper,2002; Dupasquier et al., 2012; Maruškinová, et al.2018; Agyemang et al. 2016; Bokpin et al. , 2017; Saini& Singhania,2018; Agyemang et al.,2019; Appiah-Kubi, et al.,2020).

Appiah-Kubi et al. (2020) note that there have been several recommendations for Africa countries to attract significant inflows of foreign direct investment to enhance infrastructural development by the United Nations Sustainable Development Goals (UNSDG).Nations compete for foreign direct investment because foreign investors generate job creation and economic growth, improve the productive resources of the nation, advance information and technology that lead to alleviation of poverty, and benefit the economy in other ways (Lee et al.,2012; Maitahz et al. 2014; Kuzmina et al. 2014; Malec, et al.,2016 and Appiah-Kubi et al., 2020). Several developing countries, especially in Africa, have been coming up with strategies aimed at enhancing the inflows of FDI (Appiah-Kubi et al., 2019).

African countries have been characterized by macroeconomic factors such as poor infrastructure, unemployment, low level of savings, and many others characterize African countries. Foreign direct

**** Elias Igwebuike Agbo, Sergius Nwannebuike Udeh, and John Onyemaechi Odo are lecturers at the Department of Accounting and Finance, Godfrey Okoye University, Enugu, Nigeria.***

investments are capable of constituting an immense substitute to increase the economic productivity of such economies and improve economic growth and its sustainability (Miletkov et al., 2014). These positive advantages that the inflows of foreign direct investment generate have caused competition among several developing countries.

Peters and Kiabel (2015) assert that investors' scale of preference when it comes to factors that influence their investment decision-making factors, such as sound security, exchange rate, political stability, inflation, etc., instead of fiscal incentives. In a bid to surmount this problem, African countries initiate and implement various measures of improving a friendly business environment to attract the inflows of foreign investors.

Tuomi (2011) claims that such measures adopted by African countries include liberalization of the economy, tax incentives, and provision of infrastructure. These measures are adopted by African countries in attracting foreign direct investment. The major tool used by several developing economies in attracting foreign investors are tax incentives such as low corporate tax rates, tax holidays, tax credits, investment allowance, tax deductions, and many others have been (Peters & Kiabel, 2015).

The costs and benefits of tax incentives differ from country to country. Consequently, the effects of tax incentives on the economic growth and expansion of the overall tax are not the same across the board. While in some cases, tax incentives may obviously play a crucial role in attracting new investments that contribute to substantial economic growth and development of the country, in others, a particular tax incentive scheme may bring about few new investments but with a significant cost to the government.

Many Sub- Sahara African countries are cash trapped and unable to have sufficient revenue and meet their budgetary requirements. In spite of this problem, they still offer a wide range of tax incentives. As a result of globalization, it has become very easy for multinational companies to engage in international tax planning and reap maximum economic benefits. In spite of this, many of them remain in a net tax credit position as a result of huge tax incentives. In order to continue to enjoy tax-free status, some of them would close shop soon after opening such, register a new company in the same locality and continue their old business. By so doing, those companies deny the government the much needed revenue that inform the grant of tax incentives. According to Anyadike and Eme (2017), part of the objectives of tax waivers in Nigeria is to boost local industries, make the much-needed raw materials or goods available in the short-term and generate employment. The authors report that after many years, none of these lofty objectives has been achieved. Most of the local industries have closed shops for lack of raw materials. This has resulted in the growing army of the jobless in Nigeria.

Further, Anyadike and Eme (2017) observe that in other economies, waivers are seen as a mechanism for achieving set economic goals such as protection of local industries, job creation, export promotion as well as generation and preservation of foreign exchange. For instance, China, India, Malaysia, Japan and many other economies have at various times used waivers, concessions and grants to protect and build local manufacturing and agriculture. However, the situation in Nigeria is different. For instance, in 2014, the Coordinating Minister for the Economy and Minister of Finance, Dr. Ngozi Okonjo-Iweala, declared that Nigeria had lost N797.8 billion between 2011 and May 2014 to import waivers and tax holiday concessions. Of the amount, N25.814 billion was the level between January and May of that year. Anyadike & Eme, 2017 regret that none of the objectives of tax waiver has been met in Nigeria. The system has been too corrupt. According to Anyadike and Eme (2017), some beneficiaries sell duly-approved waivers for essential goods to importers of cars or other products which are of little or no benefit to the economy. Some defaulting companies in duties and levies to the Federal Government even got fresh waivers to import more in an era of impunity where monitoring was zero and the system was run without human face(Anyadike & Eme,2017).

In Nigeria particularly, many multinational firms carrying out operation within pay little or no tax to the

government for several years. Many of them that operate in the export processing zones close down after enjoying the ten-year tax holiday period and relocate to China, India, Uganda and Ghana which either had introduced similar incentives or provide infrastructural facilities that lower production costs. Furthermore, the appropriateness of providing tax incentives in developing countries has become a subject for debate, as they have come quite often with huge costs in the form of administrative fees, expenses, and inefficient allocation of capital, foregone revenue, and many more.

Several scholars have discussed the likely effects, including their benefits and risks of tax incentives (Peters & Kiabel, 2015).A number of studies have been carried out on the effect of tax incentives on foreign direct investment. Apart from the fact that majority of such studies focused on developed countries, and relatively few on African countries, they emerged with conflicting results. For African countries, effective tax incentives have been cited as a major factor in enhancing investment in developing countries (Peters & Kiabel, 2015). Considering the significant role that foreign direct investment is expected to play in the economic progress of developing economies, the governments in Africa must focus on the formulation and execution of schemes and strategies that would serve as incentives for foreign businesses to channel FDIs into their economies. To provide a guide to the African governments in their policy formulation and implementation in this regard, an empirical study that investigates the impact of tax incentives on foreign direct investment inflows deserves to be embarked upon. This study seeks to achieve this. In addition, in alignment with Richard et al. (2021), we contend that understanding the scope and impact of tax incentives is a necessary condition for the reform of tax incentive systems in Sub-Sahara Africa, enabling citizens to assess whether policymakers are making informed decisions to increase revenue at a time when Africa's financing gap is widening. Hence, the justification for this study.

Consequently, the objective of this paper is to investigate the extent to which effective tax incentives have influenced the inflows of foreign direct investments in Sub-Sahara Africa with particular interest in Nigeria.

2.0 Review of the related literature

2.1 Conceptual framework

2.1.1 Tax incentives

Tax incentives are some government measures which are intended to encourage individual tax paying entities to spend money or to save money by decreasing the amount of tax that they have to pay. Tax incentive is a reduction made by the government in the amount of tax payable by a particular group of people or type of organization or a change in the tax system that benefits those people. It is an aspect of a country's tax code which is designed to encourage a particular economic activity by reducing. Tax incentives can have both positive and negative impacts on an economy. If implemented and designed properly, tax incentives can attract investment to a country. Additional benefits of tax incentives include increased employment, higher number of capital transfers, research and technology development, and also improvement to less developed areas. Also, if implemented properly, tax incentives can enhance economic welfare through increasing economic growth and government tax revenue (after the expiration of the tax holiday/incentive period). On the other hand, tax incentive can cause negative effects on a government's financial condition(McDonald et al., 2020) among other negative effects, if they are not properly designed and implemented(Easson & Zolt, n.d) Tax incentives have traditionally been used by governments as tools for promoting a particular economic goal. According to Trepelkov and Verdi (2018), they are preferential tax treatments which are offered to a selected group of taxpayers. Tax incentives come in several forms and are aimed at attracting greater investment, spurring growth, and creating jobs. They take the form of exemptions, tax holidays, credits, investment allowances, preferential tax rates and import tariffs (or customs duties), and deferral of tax liability(Richard et al.,2021). The justification for using tax incentives

has been the need to: (i) correct market inefficiencies associated with the externalities of certain economic activities; (ii) target new industries and mobile investments that are subject to tax competition; (iii) generate a form of agglomeration economies or concentration externalities; and (iv) subsidize companies during their sector's downturn (Trepelkov & Verdi, 2018). In addition, it is usual for developed countries to employ tax incentives to promote research and development activities and export activities. Also, tax incentives are used to support the competitiveness of the enterprises of developed countries in the global market, to attract foreign investment and foster national industries. Tax incentives according to Kuewumi (1996) encompass all the measures adopted by government to motivate tax payers to respond favorably to their tax obligations. It includes adjustments to tax policy aimed at lessening the effects of taxation on an industry, a group of persons or the provision of certain services.

Such measures may subsume the adoption of benign low tax rate; the effective dissemination of fiscal information by tax authority; or the non-imposition of tax at all. Similarly, tax incentive is considered as a deliberate reduction in tax liability granted by government in order to encourage particular economic units (e.g. corporate bodies to act in some desirable ways (e.g. invest more, produce more, employ more, export more, save more, conserve less, pollute less, and so on). Any tax is amenable to being modified to create a tax incentive. The reduction in tax liability, which a tax incentive constitutes, can be achieved through a reduction in tax rate, reduction in tax base, and so on.

2.1.2 Foreign direct investment

Foreign direct investment is an investment by a multinational corporation in foreign countries in order to control assets and manage production activities in those countries (Dutse, 2008). Macrotrends (2021) defines Foreign Direct Investment (FDI) as direct investment equity flows in the reporting economy. It is the sum of equity capital, reinvestment of earnings, and other capital. Direct investment is a category of cross-border investment associated with a resident in one economy which has control or a significant degree of influence on the management of an enterprise that is resident in another economy. Ownership of 10 percent or more of the ordinary shares of voting stock is the criterion for determining the existence of a direct investment relationship (Macrotrends, 2021).

There is a disagreement among policy makers and scholars on the benefits and costs of FDI to the host countries. The critics argue that there may be evidence of benefits in the short run but in the long run the cost may be far more enormous than the supposed benefits. On the other hand, the advocates for FDI argue that it sets an economy on the path to development. The pro-FDI argument is based on the opportunity that FDI offers the host countries to close the gaps between domestic savings, foreign exchange, government revenue, skills and the planned levels of these resources necessary to achieve development targets.

Based on the Harrod-Domar development model, a nation whose rate of savings falls short of the level sufficient to enable it achieve a planned level of investment can fill the gap with foreign capital. The neo-classical scholars contend that this will make a nation achieve its target rate of growth. FDI contributes to a nation's development by filling the gap between targeted or desired investment and locally mobilized savings. Another role played by foreign direct investment is its contribution to filling the gap between target foreign exchange requirements and those derived from net export earnings. This foreign exchange or trade gap, it is argued, can be filled by an inflow of foreign capital. If the multinational enterprise is able to generate net positive export earnings, the deficit incurred by the host country can be removed over time. This is the basis of arguing that the operations of multinational corporations leave a positive effect on the balance of payments of the host nation. Again, pro-FDI scholars argue that by taxing multinational corporation's profits the government of the host nation mobilizes sufficient funds for development projects. One other advantage that FDI confers on the host country is a whole lot of packages such as management, entrepreneurship, technology and skills. Multinational corporations not only provide circulating capital but also new factories and

sophisticated technological knowledge which can be transferred to their local counterparts by means of training programs and the process of learning by doing.

2.2 Theoretical framework

2.2.1 Trickle-down theory

Trickle-down theory also called trickle-down economics states that tax breaks and benefits for companies and the wealthy will trickle down to everyone else. According to Kenton(2021), this theory argues that income and capital gains tax breaks or other financial benefits to large businesses, investors, and entrepreneurs stimulate economic growth based on two assumptions, namely (i)All members of society benefit from growth, and (ii)Growth is most likely to come from those that have the resources and skills to increase productive output. Trickle-down economics involves less regulation and tax cuts for those in high-income tax brackets as well as corporations. However, critics contend that the added benefits the wealthy receive add to the growing income inequality in the country. Trickle-down economics is political, not scientific (Kenton.2021). The first reference to trickle-down economics was made by American comedian and commentator, Will Rogers. Trickle-down economics comes in several forms. For instance, while the supply-side theorists believe that less regulation, tax cuts for corporations, and high-income earners would motivate companies and the wealthy to raise output and create better jobs, the demand-side theorists believe in subsidies and tariffs, whereby the wealthy need protections to keep paying their employees or to raise spending.

An advisor to the Reagan administration, developed a bell-curve style analysis that plotted the relationship between changes in the official government tax rate and actual tax receipts. This became known as the Laffer Curve. A nonlinear shape of Laffer Curve, developed by an American economist Arthur Laffer suggests that taxes could be too light or too onerous to produce maximum revenue. This implies that a 0% income tax rate and a 100% income tax rate each produces $0 in receipts to the government. At 0%, no tax can be collected; at 100%, there is no incentive to generate income. This should mean that specific cuts in tax rates would boost total receipts by encouraging more taxable income. Laffer's idea that tax cuts could drive growth and tax revenue was quickly labeled "trickle-down."

2.3. Empirical review

Beyer and Schwefel (2002) reveal no courting among tax concessions and FDI appeal in transitional economies. Wilson and Wildasin (2004) define withholding tax as an income tax that is paid to the government through the corporation, as opposed to the employee wherein countries implement tax rate strategies in a bid to steer the investment of internationally mobile capital. The current proof on the relationship between tax and investment in business international locations cannot simply be extrapolated to growing countries. In addition, Asiedu (2006) finds that even inside growing nations, tax results on FDI might be exceptional in Africa. Different tax incentives have additionally different effects on the user cost of capital. Lei Guangping (2006) cited in Yan (2016) found that the reaction to different types of business tax incentives are not the same. The study also concluded that tax incentives can neither make up for the defect in the investment climate in the country, nor produce the desired external effects. However, when other factors (such as infrastructure, trans- port costs, political and economic stability) are substantially equal to a regional tax, they are likely to have a great impact on investor choice. However, this effect is not stereotyped, as it all depends on the tax means used, multinational characteristics, and the relationship between the national tax system and investment between the receiving countries. According to Rendon-Garza(2006), tax competition should be taken into consideration as the government's planned reduction inside the domestic tax costs for economic activities by way of foreigners with the sole motive of attracting foreign mobile capital and enhancing economic functions.

Djankov et al. (2010) in partnership with Price Waterhouse Coopers surveyed 85 countries. It emerged that corporate tax quotes harm gross investment, FDI, and entrepreneurship. The conclusions show divergent views on the

effectiveness of tax incentives on FDI attraction. Walid (2010) analyzed the monetary factors and risks on FDI on a full-scale level from 1997 to 2007 by utilizing a multiple linear regression model, which uncovered that there exists a critical and positive connection between FDI, and monetary factors used for the examination. Taking all the variables into account, the examination suggested the advancement of FDI through tax incentives to draw in new investments. Kransdoff (2010) in his observation of the usefulness of tax incentives on foreign direct investment attraction in South Africa presumes that taxation is crucial in attracting performance-searching for FDI. For instance, Djankov et al. (2010) point to the ambiguous impact of tax holidays on the value of capital, relying on the span of the investment, the evolution of the sales, and the quantity to which the invested capital is deductible. Tuomi (2011) additionally examined the function of investment climate and tax incentives within the foreign businesses' investment choices in South Africa. The study uncovered those monetary incentives assuming a negligible position within the choice for the majority of foreign firms. Through spatial econometrics strategies, Klemm and Van Parys (2012) researched the results of tax incentives in over 40 Latin American and Caribbean countries during 1985–2004.They found out that there is proof for vital communication in tax holidays, notwithstanding notable rivalry over the corporate income tax (CIT) rate. Additionally, there was proof that lower CIT rates and longer tax holidays are viable for attracting FDI in Latin America and the Caribbean. While other studies that include Klemm and Parys (2012) discover tax incentives to be crucial to luring foreign direct investment in low-income countries, Van Parys and James (2010) additionally find tax concessions to have a very positive impact inside the Caribbean Island countries.

The evidence of several studies recommends that by and large, investment incentives are not a large reason for internal FDI. Furthermore, in any event, when incentives prevail concerning drawing in foreign direct investment, their expenses can surpass the resultant advantages. Regardless of these discoveries, motivation plans keep on extending. This proposes that either the macro analyses are missing some aspect or that the lack of microeconomic exploration is permitting governments to limit the worth of scholarly examinations. Fawowe (2013) in his study examined whether fiscal incentives promote investment in Nigeria via constructed indexes from 1970. The empirical results of his study revealed a noteworthy negative relationship between fiscal incentives and FDI in Nigeria. The results recommend that Nigeria effectively concentrate on the removing factors such as insufficient infrastructure, low-quality institutions, and poor regulations that could discourage foreign investors.

Obeng (2014) contemplated the impact of corporate tax on regional explicit investment in Ghana, to be specific, mining, assembling, and administration areas, utilizing the Johansen co-integration strategy and quarterly information from 1986 to 2012. Factors utilized in the examination were genuine corporate tax rate, exchange rate, net exports, inflation, and investments in different areas. The paper tracked down that corporate tax affects FDI inflows into those areas. The paper therefore suggested that government authorities should maintain a low tax rate to drive more FDI into the country. By using static error correction modeling (ECM), Peters and Kiabel (2015) inspected the impact of tax incentives in the choice of foreign investors to locate in Nigeria, utilizing information from the yearly measurable bulletin of the Central Bank of Nigeria and the World Bank World Development Indicators Database. Their outcomes uncovered that FDI reaction to tax incentives is adversely critical. They further suggested that reliance on tax ought to be decreased and more consideration be focused on different incentive techniques, such as stabilizing financial changes and the political environment. With some data from 36 cities, Yan (2016) built a model to examine whether a series of tax incentives for promoting FDI inflows had a significant effect or not after 2001. The results showed that after WTO, preferential tax policies which were taken to promote FDI inflows and upgrade industrial structure indeed had some effect. From sub-regional perspective, preferential tax policies for central and western regions attracted FDI, while the effect in the eastern region was no longer significant. Majavu and Kapingura (2016), in their examination to distinguish

the determinants of FDI inflows into the South African economy, applied the VEC model to many factors such as exchange rate, inflation, market openness, and corporate tax, in addition to using foreign direct investment as the dependent variable. The experimental outcomes showed that these factors are significant drivers of FDI inflows into the South African financial system with corporate tax applying measurably critical negative impact both in the short and long term. Since reports show that Nigeria has recorded huge losses in tax incentives over the years, questions have had to be asked whether Nigeria really needs tax incentives in the economic space, especially in the midst of the recent economic recession. Onapajo and Ezuma (n.d) sought an explanation of the reasoning behind the tax waivers granted to multinational corporations (MNCs). The authors wanted to find out if the idea behind tax waivers is mainly driven economically or if there are other political (or ulterior) motives behind it. They found that there is no substantial evidence to prove that the tax waivers are a major driver for Foreign Direct Investment (FDI) into the country. Rather, according to them, the system of tax waivers has been a conduit for MNCs to evade taxes and perpetuate corruption in the system.

Lodhi (2017), utilizing the ARDL, dissected the effect of tax incentives on investment in Pakistan from 1990 to 2014. FDI and domestic investment were the reliable factors while corporate tax rates and levy costs were the unbiased variables. The discoveries uncovered that the corporate tax rate is altogether adversely connected with domestic investment and FDI inflows in Pakistan in both the short and long term. It was therefore suggested that the public authority of Pakistan reduce the corporate tax rates and duties to drive investment to Pakistan. Anyadike and Eme (2017) examined the economic implications of the abuses of waiver in Nigeria. The paper addressed those challenges using secondary sources. The paper suggested among others that the National Assembly should complement the executive arm of government to end tax waiver abuses in Nigeria. Agbo et al. (2018) investigated the effect of foreign direct investment on economic growth with specific reference to the Nigerian economy. Multiple regression analysis technique was employed in estimating the model. The data used for the study were extracted from the Central Bank of Nigeria statistical bulletin from 1980 – 2012. The results of the study showed that foreign direct investment has a positive relationship with Nigerian economic growth. Similarly, exchange rate was found to be positively correlated with Nigerian economic growth. Etim et al. (2019), in their investigation over 19 years, determined the result of cost focused and benefit-fixed tax technique incentives on FDI in Nigeria. This was accomplished by using secondary data sourced from the CBN and World Bank data sets via multiple regression strategies. The discoveries uncovered that the expense-focused tax strategy incentives had a powerful impact on FDI when compared with benefit-focused tax strategy incentives; however, there was no critical connection between cost-focused versus benefit-based tax strategy incentives and FDI in Nigeria. It was consequently recommended that nontax incentive mediations should be sought after by the government as a fundamental enhancement to the tax strategy incentives to drive FDI inflows into Nigeria. Abille et al. (2020) attempted to explore the function of fiscal incentives in attracting foreign direct investment inflows into Ghana by using data from 1975 to 2017. This was done by applying the distributed lag (ARDL) bounds test technique, which showed that corporate tax rates have a significant negative impact on FDI inflows into the Ghanaian economy in the long run. They recommended that the Ghana Revenue Service redesign the corporate tax administration in the country to control policy lapses. Appiah-Kubi et al. (2021) analyzed the effect of tax incentives on foreign direct investment in African countries based on data from 2000–2018. The study employed panel data on forty (40) African countries and an econometric model of four proxies of tax incentives, after controlling other variables, with robust Random Effect as its discussion estimator. The results of the study revealed that FDI responds to lower corporate income tax. Furthermore, the study found that foreign direct investment predominates in African economies with longer tax holidays and withholding tax. However, tax concession was found to be insignificant to the inflows of FDIs in Africa. The authors recommend proper restructuring of the tax incentives to deal with policy lapses by the

governments of Africa to enable them achieve the four main goals, i.e., poverty eradication, sustainable growth and development, African integration in the competitive global economy, and women empowerment. Considering that FDI has an immense role in economic development, empirical literature reveals the knowledge gap to be addressed and thereby providing an impetus for our study. Developing countries with poor technological development and a shortage of capital have adopted tax incentives as effective strategies and schemes. The following therefore constitutes some of the empirical literature that exists on this subject matter.

3. Methodology

This study aligns with the work of OECD (2021) in adopting the historical research design. Its few limitations notwithstanding, the main advantage of historical research is that it is the only research method that can study evidence from the past, it is well suited for trend analysis and permits the investigation of topics that could be studied in no other way. Historical research or historiography, "attempts to systematically recapture the complex nuances, the people, meanings, events and even ideas of the past that have influenced and shaped the present". (Berg & Lure, 2012: 305)

4. Up-date on the nature and quantum of tax incentives offered by Sub-Sahara African countries, the FDI inflows experienced by them, the challenges and suggested remedies

4.1 Tax incentives in Sub-Sahara African countries

According to a 2020 study of tax incentives in the United States, "states spent between 5 USD and 216 USD per capita on incentives for firms." (Slattery & Zidar, 2020). Slattery and Zidar (2020) affirm the existence of some evidence that this tax expenditure lead to direct employment gains. However, there is no strong evidence that the incentives increased economic growth. Setzler and Tintelnot (2021) report that a 2021 study found that multinational firms boosted wages and employment in localities, but that the surplus that the firms generated tended to go back to them in the form of local subsidies. According to KPMG(2016) cited in Setzler and Tintelnot (2021), many African countries have incentives related to manufacturing- an indication that African countries are reforming the incentive policies to include manufacturing incentive with the intention of attracting manufacturing Foreign Direct Investment within their countries. South Africa, Nigeria and Morocco are the only countries in Sub-Sahara Africa that offer cash grants in addition to tax incentives; all of them require prior approval by government (KPMG, 2016).Table 1 presents the incentives offered

Table 1: Incentives offered by some African countries

	Offer Tax Incentives	Offer Cash Grants	Pre-approval requirements	SEZ/Export Free-zones	CIT Rate (%)	Reduced CIT Rate (SEZ /Free-zones)	Job creation requirement	Training incentive
Algeria	Yes	No	Yes	Yes	23	0 (i)	Yes	No
Angola	Yes	No	Yes	Yes	30	-	Yes	No
Botswana	Yes	No	Yes	No	22	15	Yes	Yes
Cameroon	Yes	No	Yes	Yes	33	0	No	No
Chad	Yes	No	Yes	No	40	-	No	No
DRC	Yes	No	Yes	No	35	0 (ii)	No	No
Djibouti	Yes	No	Yes	Yes	25	0	No	No
Ethiopia	Yes	No	Yes	Yes	30	Tax Holiday Period	No	No
Ghana	Yes	No	Yes	Yes	25	0	No	No
Kenya	Yes	No	Yes	Yes	30	0	No	Yes
Libya	Yes	No	Yes	No	20	Tax Holiday Period	No	No
Malawi	Yes	No	No	Yes	30	-	No	No
Mauritius	Yes	No	No	Yes	15	15	No	No
Morocco	Yes	Yes (iii)	Yes	Yes	30	10	No	Yes
Mozambique	Yes	No	Yes	Yes	32	Tax Holiday Period	No	Yes
Namibia	Yes	No	Yes	Yes	33	-	No	Yes
Nigeria	Yes	Yes	Yes	Yes	30	0	Yes	Yes
Rwanda	Yes	No	Yes	Yes	30	0	Yes	No
Senegal	Yes	No	Yes	No	30	15 (iv)	No	No
Sierra Leone	Yes	No	Yes	No	30	-	Yes	Yes
South Africa	Yes	Yes	Yes	Yes	28	15	Yes	Yes
Sudan	Yes	No	Yes	Yes	35	0	No	No
Swaziland	Yes	No	No	Yes (v)	27.5	-	No	Yes
Tanzania	Yes	No	Yes	Yes	30	Tax Holiday Period	No	No
Tunisia	Yes	Yes	Yes	No	25	-	No	Yes
Uganda	Yes	No	Yes	Yes	35	-	No	No
Zambia	Yes	No	Yes	Yes	35	15	No	No
Zimbabwe	Yes	No	Yes	No	25.75	15 (iii)	No	No

Source: KPMG(2016) African Incentive Survey, 2016

4.2 Tax incentives regime in Nigeria

Various Ministries, Departments, Agencies and Commissions are charged with administering tax incentives in Nigeria. According to Marwam et al (2018), the extensive use of tax holidays reduced rates. Also, generous allowances by Nigeria eroded her revenues from CIT, which only yielded 1 percent of GDP in 2016. In spite of imposing a relatively high statutory rate of 30 percent, Nigeria's CIT efficiency, as measured by the ratio of CIT revenues to the GDP and the corporate tax rate, is only 0.03 when calculated with respect to the non-oil economy only, and 0.06 when CIT revenue is compared to GDP. These values are significantly lower than the 0.07 ECOWAS average and the 0.13 average for the group of emerging and developing economies. This indicates that Nigeria's corporate tax base has been eroded by tax expenditures. Nigeria was reported to have lost 1.3trillion naira to granting of tax waivers to companies operating in three sectors of the economy in the last five years. Table 2 shows Nigeria's partial estimate of tax expenditures for the period between 2011 and 2015.

Table 2. Nigeria: Partial estimate of tax expenditures

Partial Qualification of Tax Expenditures

(Billion Naira)	Import Duty Waivers	Vat Waivers/ Concessions	Pioneer Status (oil companies)	Pioneer Status(nonoil Companies) CIT	Duty Waiver	Total	% GDP
2011	78.5	52.5	15.74	5.3	0.3	152	0.24%
2012	128.5	47.1	77.86	4.8	0.3	259	0.36%
2013	46.1	24.3	107.73	17.3	2.1	198	0.24%
2014	87.7	22.9	18.72	24.7	3.0	256	0.17%
2015	162.8	81.9		14.6	2.3	261	0.27%
Total	503.6	227.8	219.5	66.7	8.0	1026	

Source: Report of the Inter-Ministerial Committee on the Review of Duty Waivers, Exemptions, Concessions and Incentives (May 2016)

Nigeria offers several types of tax incentives and allowances (Marwam, et al, 2018). The income tax system has generous incentives in the form of tax holidays of 3 to 5 years for pioneer industries and products, complete exemption of tax at the federal, state and local levels for companies that are under the free zones regime, as well as several waivers and reductions by presidential decree or as contained in the CITA for preferential sectors (NIPC, 2017). The justification for tax incentives is to change relative prices, profits and costs to attract investment in a desired direction. However, if tax incentives are granted almost to all sectors of the economy their efficiency is diffused and make little difference in attracting investments ((Marwam, et al,2018).The Nigerian government is accused of often trying to rationalize the country's endemic use of tax incentives as one of the strategies of increasing non-oil revenues . They set up an Inter-Ministerial Committee in January 2016 to undertake a review of tax expenditures resulting from 52 types of incentives being implemented by the Federal Government through its agencies (NCS, FIRS and NIPC). The Committee's preliminary findings based on a partial quantification of expenditures indicate that between 2011 and 2015, the government conceded N1 trillion, or 1.28 percent of GDP to the granting of only four types of incentives: import duty and VAT waivers, concessions, grants, and pioneer status. The largest share of incentives came from the granting of import duty waivers, which represented almost half of the total cost of incentives ((Marwam, et al., 2018).

According to Richard et al. (2021), Nigeria is facing a fiscal crisis. In 2019, tax incentives cost the federal government US$3.2 billion in revenue. However, the situation was not perculiar to Nigeria as the revenues forgone through tax expenditures (a broader term that includes tax incentives) in low- and lower-middle-income countries averaged just under 2.7% of GDP in 2019. In some countries, the figure is much higher: 8% of GDP in Mauritania and more than 6% in Cape Verde. Richard et al.(2021) estimated that the Sub-Saharan African countries collectively experienced forgone revenues of roughly US$46 billion in 2019.This amount is bigger than what they received in foreign assistance in 2019 (US$41 billion) and owe in debt service payments in 2021 (US$35 billion).

Richard, et al. (2021) consider tax incentives as often becoming a black box. According to the authors, while the Global Tax Expenditure Database has tax expenditure data for 97 countries, very few low- and lower-middle-income countries publish such data. This makes it challenging to assess the impact of tax incentives. According to Richard et al. (2021), nearly 60% of low- and lower-middle-income countries do not provide information on the types of tax incentives

offered and their revenue implications, while eight countries provide only aggregated data. Their authors assert that only half (28 of 54) African countries publicly reported their tax expenditures at least once between 2000 and 2019.Even at that, quality of their data has often been poor.

4.3 Current status of foreign direct investment in Sub-Sahara Africa

According to KPMG (2016), Nigeria is making effort to attract foreign direct investments in order to grow other sectors of the economy with the decline of revenue from the oil sector. Ugbodaga (2021) reports that FDI inflows to Nigeria increased to $2.4 billion in 2020 from $2.3 in the previous year despite the COVID-19 pandemic that plagued global economies. Nigeria emerged as the third largest economy, alongside Ethiopia ($2.4 billion), that attracted FDI inflows in Africa in 2020.

According to Trading Economics(2021), Foreign Direct Investment in Nigeria increased by 2138.38 USD Million in the first quarter of 2021.It averaged 949.31 USD Million from 1990 until 2021, reaching an all- time high of 3084.90 USD Million in the fourth quarter of 2012 and a record low of 63.50 USD Million in the fourth quarter of 1990.

Egypt was reported to have been the largest recipient of FDI in Africa, however, with a significant reduction of 35 percent to $5.9 billion in 2020;it was followed by the Republic of the Congo ($4 billion), while South Africa was fourth with $3.1 billion (a decline of 39 percent).It was also reported by the UN body that the COVID-19 crisis caused a dramatic fall in FDIs in 2020 - thereby pushing global FDI flows to $1 trillion from $1.5 trillion in 2019 (a decline of 35 percent). The level of decrease is almost 20 percent below the 2009 trough after the global financial crisis. The UN body said that FDI outflows in Africa likewise declined by 16 percent to $40 billion — the lowest in 15 years — while its outflows fell by two thirds in 2020 to $1.6 billion from $4.9 billion in 2019.

According to UNCTAD (2020) FDI flows in Africa are expected to rise in 2021 but to a limited extent. It predicted that vaccine availability, domestic economic recovery policies and international financial support would be critical to the revival of FDI and the post-pandemic recovery in the continent. Finally, it projected that global FDIs will remain at a low level – about $1.2 trillion, over 2021 and 2022.

4.4 Principles to be adopted to increase the transparency and governance of tax incentives for investment in developing countries

OECD (2021) observes that the problem of tax base erosion due to tax incentives is worsened by the lack of transparency and clarity in the provision, administration and governance of tax incentives. It notes that the granting of tax incentives for investment is often done outside of a country's tax laws and administration, sometimes under multiple pieces of legislation. Generally, despite the widespread use of tax incentives for investment, there is inadequate analysis of their costs and benefits in a national context to support government decision-making. Also only limited data are collected on granted tax incentives, qualifying investments made, direct (and indirect) benefits to the host economy, and the cost of these tax incentives in terms of foregone revenue. Furthermore, even the information that ought be more readily available – lists of tax incentives and beneficiaries – is rarely collected or reported

Consequently, OECD (2021) suggests that to increase the transparency and governance of tax incentives for investment in developing countries the relevant governments should take the following actions:

(i) Make a public statement regarding all tax incentives for investment and their objectives within a governing framework;

(ii) Use tax laws only to provide tax incentives for investment;

(iii) Pull together all the tax incentives that are for investment under the authority of one government body, if possible;

(iv) Insist that tax incentives for investment are ratified through the law making body or parliament;

(iv) Administer tax incentives for investment transparently;

(v) Compute the amount of revenue forgone that is attributable to tax incentives for investment and release a statement of tax expenditures publicly;

(vi) Review the continuance of existing tax incentives periodically by assessing the extent to which they meet the stated objectives;
(vii) With a regular statement of tax expenditures, highlight the largest beneficiaries of tax incentives for investment by specific tax provision, where possible;
(ix) Engage in a systematic collection of data to underpin the statement of tax expenditures for investment and to monitor the overall effects and effectiveness of individual tax incentives;
(x) Increase regional co-operation to avoid harmful tax competition.

In addition to the actions to be taken by governments, other stakeholders have the following responsibilities:

(a) Business entities should refrain from seeking or accepting exemptions not contemplated in the statutory or regulatory framework related to taxation, financial incentives, or other issues.
(b) The civil society should draw attention to, and publicize, the revenues forgone from wasteful tax incentives that could free up resources for development.
(c) Development partners and donors need to include tax incentives and revenues forgone in the dialogue with governments in developing countries and provide appropriate technical advice and assistance.
(d) International assistance providing countries and organizations should provide technical and other assistance aimed at building the capacity of developing countries to collect and analyze the data required to enhance the transparency of tax incentives for investment.

4.5 Tax Incentives and the Nigerian Economy

Taxation is very essential for sustainable development and the growth of emerging economies especially where natural resources are relatively scarce. Tax incentives are basically designed to attract new investments and to expand existing ones in priori industries which is based on the country development plan. In literature, the broadening of a country's taxable capacity is often linked to the generous incentives prevalent in its tax system. The provisions of generous exemptions often tend to erode the tax base, which in turn, affects income elasticity of a tax through tax-to-base elasticity (Osoro, 1993).

Nigeria's experience in the granting of tax incentives can be traced to the commencement of British Administration in the territory when all sorts of reliefs, allowances, and tax holidays were granted to British companies and individuals as an attraction to establish trade links with it. Specifically, tax incentives for industrial development started in 1958 and included:

(i) Pioneer companies relief, which exempted companies operating in pioneer industries for up to 5 years from paying company income tax;
(ii). Companies Income Tax relief which gave capital allowances regarding investments in machinery, building, loss carry-forward facility, etc.
(iii) Import duties relief which exempted selected pioneer companies from paying import duties on imported inputs; and
(iv) Approved user scheme, under which import duties were refunded to the approved enterprises which import in the export-tuned production. Generally, tax incentives have operated under the following sub-heads in Nigeria: tax holidays, investment allowance, rural investment allowance, tax free interest, deductible capital allowance, research and development, tax-free dividends, tax treaties, reliefs and allowances; and capital allowances.

Current policy of Nigerian Government is to ensure: incentives are sector based and not granted arbitrarily, the benefit to the Nigerian economy exceeds the cost of taxes foregone, and incentives are reviewed regularly to confirm if they are serving the expected purpose, while foreign investors enjoying incentives are expected to voluntarily plough back into the Nigerian economy.

5. Conclusion and recommendations

In due recognition of the role played by foreign direct investments in the development process, Sub-Sahara African countries have been in a serious competition and faced several challenges while striving to attract them. This study employed the historical research approach with the purpose of obtaining an updated literature on what has been the effect of tax incentives on foreign direct investment in Sub-Sahara African countries. Nigeria was the major location of the study. We found that as good as employing tax incentives is a good economic strategy for enhancing economic growth, they have suffered serious abuse in the hands of corrupt politicians. Consequently, even as tax concessions, longer tax holidays, withholding tax and other tax expenditures in Sub-Sahara African countries have continued to be in the increase, their impact on FDI has remained weak generally. This situation is equally blamable on a number of factors that have played against the business environment for foreign investments in developing countries. Our study recommends that tax incentives should be properly structured to deal with policy lapses by the governments of Sub-Sahara African countries. In addition, our study recommends the following actions to be taken by the governments of Sub-Sahara African countries:

(i) Governments should embark on an extensive review of tax incentives using independent audit firms. This should be used as a parameter to judge if tax incentives are really beneficial or not to the economy.
(ii) There should be an efficient monitoring and evaluation system which would offer a periodic and timely evaluation of the tax incentives so as to prevent abuse by the MNCs and their local collaborators.

(iii) The governments should incorporate the abuse of tax waivers in their anti-corruption drive. The individual found to be culprits ought to be punished under the framework of the existing anticorruption institutions.
(iv) The governments should empower its tax institutions with the intention of enhancing transparency around tax waivers given to MNCs.
(v) The legislatures of Sub-Sahara African countries need to improve on its oversight functions on the issue of tax waivers. The issues concerning tax waivers must be seriously checkmated by them.
(vi) Policy inconsistencies and reversal construed in order to meet the desires of the political class in power, who also double as importers, exporters and manufacturers should be discouraged.
(vii) The practice of excluding vatable items to suit some sectors of the economy need to be discontinued.
(viii)Excessive dependence on external capital should be discouraged as that will lead to greater vulnerability to external sources of uncertainty.
(ix) The resource-rich countries need to reap benefits from FDI and foster linkages in order to diversify their economies. This study anticipates that fostering local firms and human resources to reap the benefits from FDI will probably be the next area of focus for many SSA countries.

The unavailability of required data as well as the reliability of some available data on tax incentives posed some limitations to the use of time series data to determine the impact of tax incentives on FDI of Sub-Sahara African countries. We hope that future research will be able to overcome the limitations not addressed explicitly by this study.

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