Kuwait: Notable improvement on the Ease of Doing Business—more is needed for FDI

Kuwait was one of the ten best improvers last year in the World Bank's Doing Business rankings, moving up 14 places to 83. The authorities have made good progress with legislation to create a business-friendly environment that would be able to attract the foreign investment that is needed to diversify the economy away from oil. However, more reforms are required for Kuwait to catch up with its neighbors, by focusing on the conditions and metrics that are the most critical to foreign investors. Kuwait's abundant oil resources, prime geographical location, entrepreneurial spirit and its tech-savvy younger generation bode well for a promising future, to be buttressed by appropriate policies.

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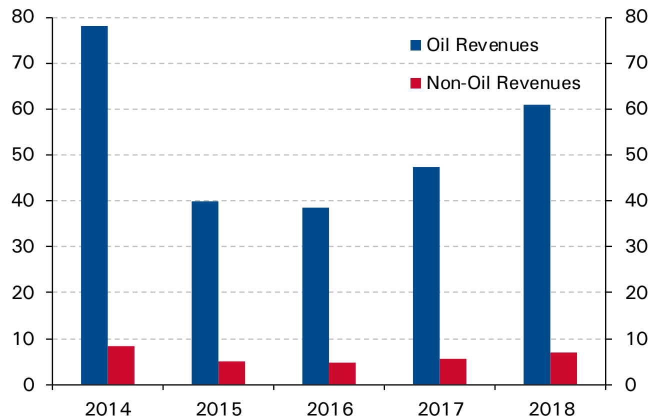
Kuwait's economy, like most GCC countries, is heavily reliant on oil as its primary source of exports and budgetary revenues. Aware of the risks associated with such a heavy dependency on oil, the government has embarked on an economic diversification strategy under the strategic umbrella of the Kuwait 2035 Vision. One of the most important objectives of Kuwait's vision 2035 is to boost private sector activity and ultimately move Kuwait towards a post-oil economy. For this to happen, the overall business environment would need to be made more investment-friendly. Attracting foreign direct investment (FDI) and boosting the non-oil economy will create more jobs for the growing number of Kuwait nationals entering the labor force.

Chart 1: Kuwait Revenues

$billion



Source: Kuwait Ministry of Finance (MoF)

Brief history of Kuwaiti foreign direct investment (FDI) regulations

The "Commercial Law" of 1980 and its subsequent revisions have long governed FDI regulations. The overall terms of this law were unattractive to most foreign investors. For one, the law limits foreign ownership to 49% of the business or project, with local counterparts granted favorable treatment while foreigners were given little space to influence decision-making. This law did not encourage FDI inflows and may have deprived the country from investments and expertise that could have helped boost growth as well as stimulate the development of the private sector.

Having realized the adverse impact of the restrictions on foreign ownership, in 2001, the government introduced a new "Foreign Investment Law" to circumvent the limits set in the "Commercial Law". This law was prepared with a view to grant full ownership to foreign investors in selected sectors (infrastructure, insurance, hospitals, housing, tourism and entertainment). The law also stated that the Council of Ministers should determine the economic activities and projects that the foreign investor would be allowed to invest in. To help in the implementation of this law, the government established the Kuwait Foreign Investment Bureau (KFIB), a division of the Ministry of Commerce and Industry (MOCI). However, the highly-anticipated KFIB was short-lived and later dissolved, having been deemed ineffective by the private sector in facilitating the granting of licenses. This may have led many investors to abandon the pursuit of investment licenses in Kuwait and focus their efforts elsewhere.

In an effort to rectify the limitations in the 2001 FDI law, the authorities replaced it with Law No. 116 of 2013, and created the Kuwait Direct Investment Promotion Authority (KDIPA). The new law makes it easier for investors to obtain an operating license and allows for tax and customs duties relief, real estate allocations, and permission to recruit foreign labor. KDIPA was set up as a "One-Stop Shop" whereby foreign investors' applications for licenses to operate in Kuwait are reviewed and granted based upon a number of requirements.

In 2019, a set of criteria was introduced to assess applications and grant licenses to foreign investors. Decision No. (329) of 2019 enacted five main criteria for assessing licensing and granting incentives. The criteria covered the following: (i) transfer and settlement of technology, including tangible and intangible technological innovation and the enablement of knowledge creation; (ii) human capital, stressing job creation for nationals and employee development programs; (iii) market development; (iv) economic diversification; and (v) sustainable development in the areas of CSR and environmental sustainability. Decisions on licenses and the granting of incentives are based on "Points Scoring Mechanism" (PMS).

These conditions, though carefully considered, may have been overwhelming and difficult to satisfy for potential investors. According to KDIPA, as long as foreign investor activities do not fall within the Negative List (see below) and as long as they meet the wide-ranging conditions mentioned above and fall within the PMS matrix, investors should be able to obtain the licenses required within 30 days of submitting the application. While KDIPA has been doing a good job by setting clear rules and procedures, foreign investors still voice some concerns in dealing with several government agencies to secure what is needed to start a business.

While many regulations have been relaxed, foreigners still cannot invest in several sectors. The "Negative List" introduced by the Ministerial Resolution No. 75 of 2015 includes the following sectors: extraction of crude oil and natural gas, manufacturing of fertilizers, nitrogen compounds, coke oven products, and gas and distribution of gaseous fuels through mains. The real estate sector is also restricted, excluding privately owned building development projects as well as the security and public administration sectors. Investing in organizations whose activities are based on membership groups or special interests groups or that promote ideas to the public as well as those engaged in hiring labor, including domestic labor, is also prohibited.

Foreign investors that do not qualify under KDIPA or under the FDI law, have another avenue for investment, however. When it comes to joint ownership, Law No. 1 of 2016 "Companies Law", in accordance with the Commercial Law, gives a foreign owner all the practical benefits that come with majority ownership, which is still limited to 51/49% ownership. It recognizes their claim to partial ownership by law, allowing for negotiations and profit distribution that vary from their stated ownership percentages of 51 and 49%, respectively. According to the Doing Business 2020 report, a recent amendment to the Companies Law helps shareholders be better informed.

Furthermore, in late 2018, the Kuwaiti Ministry of Industry and Commerce issued a decision allowing foreign investors to trade and own Kuwaiti bank shares. While there are no set limits on foreign ownership, the Central Bank's approval is required for any share exceeding 5% of a bank's capital. This decision aims to serve the objectives of the 2035 vision, which has the development of the financial sector as one of its main targets.

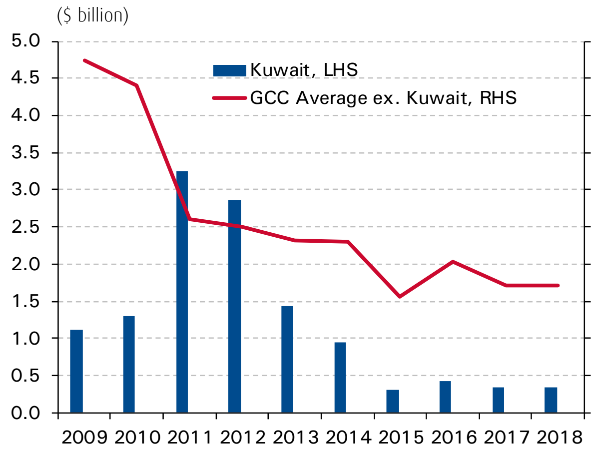
In sum, Kuwait has introduced several measures to open up the economy in an attempt to diversify its economic base and encourage investment flows. According to the latest IMF report (2019), Kuwait has taken steps to reduce FDI regulations but some restrictions persist. While the FDI law of 2001 was a step in the right direction in that it allowed foreigners to own up to 100% of a commercial entity in Kuwait, it was still limited to sectors such as infrastructure, insurance, hospitals, housing, tourism and entertainment.

FDI performance in 2009-2018

FDI started to pick up after the financial crisis in 2009 in anticipation of large-scale development projects before tailing off in 2011. The surge in FDI inflows in 2011 and 2012 was brought on largely by the recapitalization of Gulf Investment Company (GIC) and the telecom company Ooredoo's purchase of Wataniya for about $1.8 billion**.** However, by 2013 we saw a drop in FDI inflows, a trend that has continued to the present. (Chart 1.) The downturn in Kuwait's FDI could be attributed to the remaining difficulties in the Doing Business indicators and to the still somewhat restrictive policies and regulations. While regional tensions and other external factors may have also played a role, other countries in the region (namely the UAE) have not been affected and continued to witness a sharp increase in their FDI inflows.

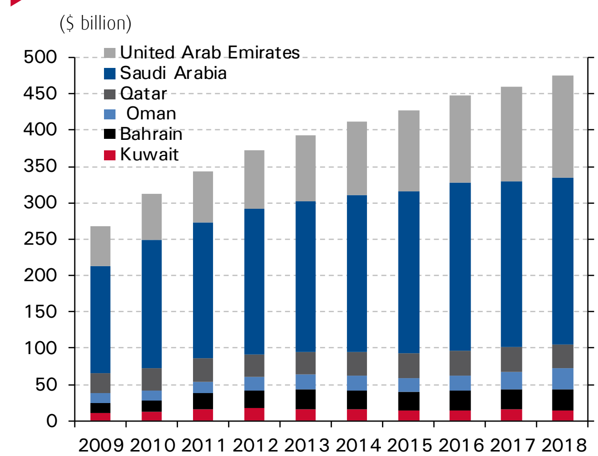
The New Kuwait 2035 initiative carries hope for Kuwait's future. It targets the transformation of Kuwait through 'seven pillars and five strategic directions'. The goals include the improvement of Kuwait's global and regional position. In addition, reforms to the education system will be implemented to better prepare the national youth for the ever-changing labor market. In addition, further reforms should be implemented in administrative and bureaucratic practices to reinforce transparency, accountability and efficiency in the government. The 2035 vision also intends to tackle areas such as healthcare, the environment, and infrastructures.

Chart 2: Kuwait and GCC Average FDI inflows 2009-2018



Source: UNCTAD World Investment Report 2019

Chart 3: GCC Inward FDI Stock 2009-2018



Source: UNCTAD World Investment Report 2019

Ease of Doing Business

One universally accepted measure of the attractiveness of the business environment is the World Bank's "Ease of Doing Business" index. The index comprises ten different criteria or indicators that influence a country's business environment ranking. These criteria include "Starting a Business", "Getting Credit" and "Enforcing Contracts". (Table 1.) While the Doing Business (DB) index, as a measure, is not ideal as it uses the same criteria for all countries regardless of their stage of economic development and instructional setting, it does, nonetheless, offer a general idea about the business environment and allow for comparisons among countries especially those that have similar features such as the GCC countries.

Table 1: World Bank's Ease of Doing Business Indicators

2020 Doing Business Topics Ranking (1-190)

Economy	Global Rank	Starting a Business	Dealing with Construction Permits	Getting Electricity	Registering Property	Getting Credit	Protecting Minority Investors	Paying Taxes	Trading across Borders	Enforcing Contracts	Resolving Insolvency
UAE	16	17	3	1	10	48	13	30	92	9	80
Bahrain	43	67	17	72	17	94	51	1	77	59	60
Saudi Arabia	62	38	38	18	19	80	3	57	86	51	168
Oman	68	32	47	35	52	144	88	11	64	69	97
Qatar	77	108	13	49	1	119	157	3	101	115	123
Kuwait	83	82	68	66	45	119	51	6	162	74	115

Source: World Bank Doing Business report 2020

Recently named one of the top 10 improvers in the Doing Business report, Kuwait moved up 14 places in 2019, from 97 to 83. Improvements were made in several areas including "Starting a Business", "Getting Electricity", "Registering Property" and "Getting Credit". In "Starting a Business" Kuwait made it easier to obtain commercial licenses by merging procedures and streamlining online company registrations through the Kuwait Business Center online platform. "Getting Electricity" has also become more convenient, with the implementation of a geographic information system that streamlines the review of connection requests and a digitized application process. In addition, an online property transfer system eases the property registration process. (Table 4.)

Table 2: World Bank's Ease of Doing Business Indicators

(Rank 1-190)

Economy	2020	2019
United Arab Emirates	16	11
Bahrain	43	62
Saudi Arabia	62	92
Oman	68	78
Qatar	77	83
Kuwait	83	97

Source: World Bank Doing Business Report 2020

Other GCC countries have, however, fared well in the 2020 Ease of Doing Business, with the UAE still leading (Table 2.) Saudi Arabia made significant progress last year, jumping 30 places, as did Bahrain. The UAE slipped to 16 from 11 in 2019, but still ahead of Bahrain, the next best performer in the Middle East region.

Table 3: World Bank's Ease of Doing Business Indicators (Score 0-100)

Economy	2020	2019
United Arab Emirates	80.9	81.28
Bahrain	76	69.85
Saudi Arabia	71.6	63.5
Oman	70	67.19
Qatar	68.7	65.89
Kuwait	67.4	62.2

Source: World Bank Doing Business Report 2020

Doing business and foreign direct investment

The World Bank conducted a study that reviewed the empirical literature and concluded that "business opportunities are considerably the most influential determinants of FDI". The results showed that for developing and economies in transition that seek to attract FDI, such as Kuwait, strong institutions and investor-friendly regulations matter, as does the market size and growth potential.

Table 4: Kuwait's Improvements in the following Doing Business Indicators

Change in score	Improvement in Indicators	Reforms
+10.5	Dealing with construction permits	Kuwait Municipality made dealing with construction permits easier by streamlining its permitting process, integrating additional authorities to its electronic permitting platform, and enhancing interagency communication, thus reducing the number of procedures and the time to obtain a construction permit.
+10.1	Getting electricity	Ministry of Electricity and Water (MoEW) made getting electricity easier by digitizing the application streamlining connection works and meter installations, and using a geographic information process, system (GIS) to review connection requests, which reduced the number of procedures and the time for getting electricity.
+10.0	Getting credit	Credit Information Network Company (Ci-Net), in cooperation with the Central Bank of Kuwait (CBK), improved access to credit information by guaranteeing borrowers the legal right to inspect their credit data and offering credit scores as a value-added service to banks and financial institutions, in accordance with Law No. 9 of 2019 regulating exchange of credit information
+7.0	Starting a business	Ministry of Commerce & Industry MOCI (Kuwait Business Centre) and the Pubic Authority for Civil Information (PACI), merged procedures to obtain a commercial license and streamlined online company registration through e-link which reduced the number of procedures and the time needed to issue a commercial license.
+6.7	Registering property	Ministry of Justice (MoJ) and Kuwait Municipality coordinated to make property registration easier by streamlining the inspection and registration processes, which reduced the number of procedures and the time to register property, as well as improving the quality of the land administration index by publishing official service standards on property transfers on the MoJ website.
+2.1	Trading across borders	Kuwait General Directorate for Customs (KGDC) made trading across borders easier by improving the customs risk management system, and by implementing a new electronic clearance system as per several Customs Circulars issued which resulted a reduction in the time required for border compliance for exports and imports.

Source: World Bank Doing Business Report 2020, Kuwait Direct Investment Promotion Authority (KDIPA)

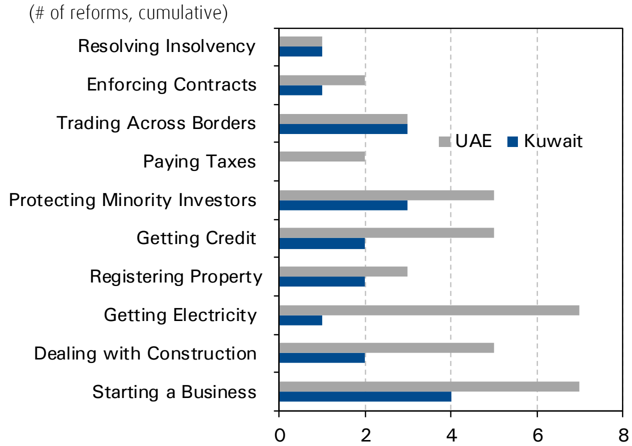
Research suggests that there is a positive correlation between the World Bank's Doing Business indicators and foreign direct investment. The question that is often raised is whether a country's Doing Business ranking really matters for FDI. A study conducted by the School of Economics, University College Dublin, empirically tested this hypothesis and found that a good ranking in the Ease of Doing Business is positively correlated with FDI inflows. The study showed that a positive relationship between FDI and DB ranking holds on average, but the strength of this relationship varies by country. This might be due to other factors that are not captured by the DB index, such as governance, institutional strength and infrastructure quality, among others.

Some Doing Business indicators are more important than others for FDI inflows. In particular, the "Trading across Borders" index has been shown to have the most influence on FDI inflows. Kuwait scored low on this index (ranked 162 globally). It also scored low on "Getting Credit" and "Resolving Insolvency". According to the DB 2020 report, Kuwait has made modest progress in improving policies and regulations pertaining to the above-mentioned indices, which are typically good FDI catalysts, but much more needs to be done in this area.

Dealing with insolvency issues will require an efficient legal system and a dispute settlement mechanism. The existence of a modern, fair and consistent legal system that can deal with disputes efficiently and quickly is very important for foreign investors. They need to be assured that the law would be enforced in a consistent, timely, and non-discriminatory manner. Kuwait's low rank in this indicator is mainly due to the low recovery rate compared to other high-income OECD countries, and the time it takes to resolve insolvency, which is about 4.2 years, double the amount of time in the MENA region, for example.

Chart 4: Reforms by Doing Business indicator 2009-2020

(# of reforms, cumulative)



Source: World Bank Doing Business Report 2020

The credit reporting systems and the effectiveness of collateral and bankruptcy laws should be strengthened. The ranking of economies on the ease of "Getting Credit" is determined by the "Strength of Legal Rights" index and the "Depth of Credit Information" index. The strength of the legal rights is low in Kuwait (1 out of 12) compared to 3.1 in MENA and 6.1 in high income OECD countries. Though the "Depth of Credit Information" index is high (8), "Credit Registry Coverage" and "Credit Bureau Coverage" are low by international standards.

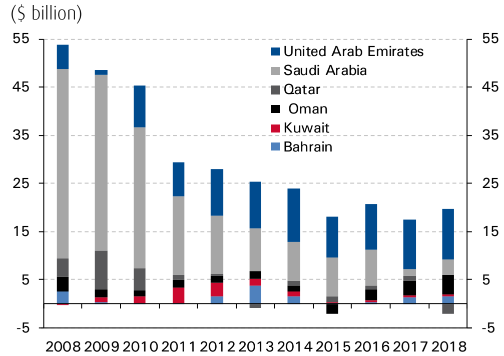
Creating a level playing field for all investors would be of great benefit to Kuwait. One could conceive a situation where the business environment is more appealing to domestic investors yet hinders foreigners from investing in the country due to legal and procedural restrictions that could make the country impenetrable. These restrictions include: ownership and minority shareholders rights; tax systems; labor laws; limitations on what sectors foreign investors can engage in; and repatriation of income, to name just a few, are major impediments to FDI.

In conclusion, while Kuwait has made decent progress in improving its business environment, more work needs to be done to make up for the slow progress of the past. Attracting FDI is important not only for boosting economic activity but also for potentially attracting foreign investment in new sectors that could ultimately reduce the dependence on oil and diversify the sources of revenues. Diversification would also shield the economy from erratic movements in oil prices and their adverse impact on economic performance and economic policies. To this end, the authorities and KDIPA are aware of the need to accelerate the pace of reforms to improve several key areas in the World Bank Doing Business scores. Reforms are a continuous process and many measures are needed for the country to gain some competitive advantage. Kuwait is fortunate to have abundant wealth (oil and financial), a prime location, entrepreneurial spirit, and a tech-savvy generation. These all bode well for a promising future if supported by the right policies.

Investment and Doing Business in GCC Countries

FDI inflows to the GCC region have consistently underperformed and remained concentrated in only a few sectors. Over the past several years, GCC governments have attempted to loosen FDI restrictions and open their economies to boost FDI inflows. The UAE, Oman and Bahrain have created economic free zones with looser regulations sectors. However, investment outside these "free zones" has remained off-limits for foreign investors. The heaviest restrictions fall on foreign land ownership as it is strictly limited to specific zones in most GCC counties, governments (Bahrain), tourist areas (Oman) or areas for housing (Qatar). In Kuwait, however, non-GCC citizens are strictly prohibited from land ownership.

Chart 5: GCC FDI Inflows



Source: UNCTAD World Investment Report 2019

The UAE is considered the most liberal in terms of FDI regulations among the GCC. In response to the FDI slowdown in recent years, the UAE has undertaken major reform of its FDI laws. The new "FDI Law", Law No. 19 of 2018, which was announced officially in July of 2019, allows foreign investors 100% ownership in 122 economic activities spanning 13 sectors outside the economic free zones. These include manufacturing, agriculture and renewable energy.

Saudi Arabia (KSA) has made major strides toward improving the business environment and attracting FDI. In order support the Vision 2030, the kingdom has been revising its policies and regulations. Saudi Arabian General Investment Authority (SAGIA), an entity authorized to oversee FDI in KSA, has removed several restrictions on foreign investors and eased the licensing requirements. However, restrictions remain in the following sectors: oil exploration, and real-estate investment in Makkah and Medina.

Qatar too introduced many changes to attract foreign investment. At the start of 2019, Qatar issued a new FDI Law, Law No. 1 of 2019, which introduced wide-ranging changes that opened up the economy to foreign investment in almost all sectors. Restrictions still apply though in the following sectors: banking, insurance, commercial agency activities, security and defense.

Bahrain and Oman have been making a conscious effort to attract foreign investors. The signing of a bilateral Free Trade Agreement between Bahrain and the United States allows for the relaxation of restrictions on investment and trade. This should further support Bahrain's economic growth in the coming years. Restrictions on foreigners still apply in property ownership, though. However, a foreigner can acquire land in certain designated areas. As for Oman, it has been open for 100% foreign investment ownership since 2016, and has witnessed strong FDI inflows from 2015 to 2018 (from outflows of $2.2 billion in 2015 to a net inflow of $4.2 billion in 2018).

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