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## THE ROLE OF FOREIGN INVESTMENTS IN OIL INDUSTRY

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**Abstract:** *The aim of this paper is to foster long-term growth in Libya and other developing countries, helping them transition into the ranks of developed nations. The two research questions that this paper deals with are: a) What role can foreign investments in the oil sector and manufacturing industries play in the economic diversification of Libya and some countries? b) What measures must be implemented to maximize the positive impact of foreign investments on productivity in Libya and other countries? The relevant literature guiding this research plays a crucial role in advancing the economic and social development of Libya and similar nations. Foreign direct investment (FDI) is regarded as a key mechanism for enhancing productivity, facilitating the transfer of expertise and technology, promoting employment, and boosting export value, particularly in the oil and manufacturing sectors. Two main outcomes emerge from this analysis are the following: firstly, continuing to encourage the prevailing industrial fabric (oil refining industry, food industries, and textile industries) in order to raise the value of exports and preserve jobs on the other hand; secondly, encouraging the development of new and diverse industrial specializations. The policy implications suggest that the impact of foreign investments on the economies of Arab countries varies across different sectors. Consequently, countries that experienced successful economic growth are those that effectively directed investments towards high-value-added economic activities, as exemplified by certain nations, in China and India. The negative effects of these foreign investments were that the presence of foreign investment companies negatively affected national companies. Despite their contribution to increasing exports, foreign investments have had a negative impact on the productivity of the sector. The practical implications highlight that the manufacturing sector plays a crucial role in absorbing the labor force, particularly the operational workforce with average competencies, thereby contributing to the formation and growth of the middle class globally. Foreign direct investments in this sector provide many opportunities to employ the national labour force and raise wages.*

**Keywords:** *foreign investments, oil, economic policy, economic analyses of Libya and the Arab countries*

## 1. INTRODUCTION

Libya, as one of the oil-producing countries with substantial oil reserves, has the potential to develop its national economy, provided that its oil wealth is strategically utilized to foster growth in other sectors, particularly the manufacturing sector. This sector is considered a key driver of economic development due to its forward and backward linkages and the foreign exchange it generates, which are vital for the overall economic progress. The results of both theoretical and applied studies on the relationship between oil revenues and industrial output growth have varied. Some studies suggest that oil resources play a significant role in developing the industrial sector by providing financial surpluses that can be used to fund industrial projects, as well as energy sources essential for operating these projects.

On the other hand, some economic studies examining the relationship between oil revenues and industrial development suggest that the discovery and production of oil can have negative effects on overall economic development and industrial growth, particularly in developing countries. These countries often struggle with weak economic institutions and a lack of the administrative and technical capacity required to create effective development plans and strategies. As a result, despite their vast oil wealth, these nations face challenges in investing surpluses into industrial development, primarily due to the limitations imposed by weak political and administrative systems.

## 2. FOREIGN DIRECT INVESTMENT AND ECONOMIC DEVELOPMENT

The significant importance of foreign direct investment (FDI) and the considerable interest it has garnered have led to numerous studies aimed at analyzing its effects, resulting in a variety of definitions. Despite the differences in the backgrounds and areas of expertise of those defining it, foreign investment is examined from various perspectives and viewpoints [1]. These variations suggest that a single, unified definition may not fully

capture the complexity of the phenomenon, which has multiple dimensions and outcomes. Consequently, it is natural for individuals to have differing interpretations of foreign direct investment based on their perspectives. This concept has also had a profound impact on the broader notion of economic development, making it essential to explore and clarify both concepts.

### 2.1. THE CONCEPT OF FOREIGN DIRECT INVESTMENT

Investment is a concept that is challenging to define in a way that universally appeals to all perspectives. Individuals' views on investment and its nature vary depending on their circumstances, professions, objectives, and other factors that complicate the formulation of a single definition. For example, a manufacturer approaches the investment process from a different angle than a merchant, and their perspectives differ again from those of individual investors who own varying amounts of capital and seek to earn returns in diverse sectors. Broadly speaking, investment can be defined as the optimal allocation or use of capital. From an economic viewpoint, investment involves channeling accumulated savings or wealth into productive ventures that address economic needs while generating a return.

The view of foreign direct investment (FDI) flows has evolved in modern economic growth theory, with a growing recognition that FDI can influence not only the level of output per capita but also the growth rate of that output. In contrast, classical economic theories did not place much emphasis on the direct impact of foreign investment on long-term output growth, as they assumed diminishing returns to productive capital. According to these theories, FDI could affect the level of output but not necessarily its growth rate. However, more recent perspectives suggest that foreign direct investment can stimulate the growth rate of per capita income in the host country. This is achieved by expanding the use of local raw materials, implementing modern management

practices, and facilitating the introduction of advanced technologies.

Additionally, external flows, such as foreign direct investment (FDI), provide a means to finance the current account deficit. Unlike foreign debt, FDI does not involve incurring debt or the obligation to repay specific amounts at set times. Moreover, FDI can contribute to the development and training of human resources and encourage investment in research and development. Foreign direct investment comes in various forms, which differ depending on the objectives of the investment and the needs it aims to fulfill.

## 2.2. INVESTMENT IN SEARCH OF NATURAL RESOURCES

Many multinational companies aim to capitalize on the abundant natural resources and raw materials found in developing countries, particularly in sectors like oil, gas, and other extractive industries. This type of foreign direct investment encourages an increase in the export of raw materials while simultaneously driving up imports of capital goods, intermediate production inputs, and consumables.

## 2.3. MARKET-SEEKING INVESTMENT

This type of investment prevailed in the manufacturing sector in developing countries during the sixties and seventies during the application of the import substitution policy. This type is considered a substitute for exports from the country exporting the investment, and its presence in the host country is the result of the restrictions imposed on imports. There are also other reasons for doing this type of investment, including the high cost of transportation in the host country, which makes investing in it more feasible than exporting to it. In this case, this type of investment does not affect production because it replaces exports, but it has positive effects on consumption and Indirect positive impact on trade. This type of investment would contribute to high growth rates in the country hosting the investment by increasing its capital stock. It would also have

expansionary effects on trade in the areas of production and consumption by increasing the host country's exports and increasing its imports of production inputs and goods imported to it from other countries.

## 2.4. PERFORMANCE-SEEKING INVESTMENT

This type of investment occurs when multinational companies concentrate part of their operations in host countries to increase profitability. Rising wage levels in industrialized countries have driven many of these companies to invest in developing countries. Such investment is characterized by its expansionary effects on the host country's trade, leading to the diversification of exports. Additionally, it stimulates consumption by increasing imports of production inputs. This form of investment can take various shapes, including multinational companies relocating labor-intensive production activities to the host country, where national companies carry out these operations under bilateral contracts. Through this arrangement, the company in the host country gains access to foreign markets that it otherwise might not have been able to reach independently. This is because it lacks the distribution networks, information, and channels that multinational companies typically possess, which are essential for expanding into international markets.

The strategy of transferring labor-intensive activities to developing countries has played a crucial role in boosting their industrial exports over recent years. Another variation of this approach involves manufacturing certain components abroad due to high wages in the home country or the appreciation of its currency. However, this process requires a high level of productivity and technical expertise in the host country, which is why it is primarily concentrated in newly industrialized nations. In such countries, local companies often enter into subcontracting agreements with multinational corporations to manufacture entire products, with the multinational company's brand name attached for marketing purposes.

This practice can enhance the production capabilities of the host country's company, potentially leading to the development of local industries capable of producing the product independently. This process is considered a form of quality enhancement. One key advantage of this type of foreign direct investment is that exports of these products to the industrialized country are not subject to trade barriers, as they are effectively linked to the parent company in the home country.

### 3. THE CONCEPT OF ECONOMIC DEVELOPMENT

Economists make a clear distinction between the concepts of economic growth and economic development. **Economic growth** refers to an increase in the real output of goods and services, typically measured by the growth in national income or GDP at constant prices. For countries that rely heavily on the production and export of natural resources such as oil, gas, coal, coffee, and iron, economic growth can be achieved through higher production levels of these commodities, provided global market prices remain stable. However, rapid and short-term growth does not necessarily equate to **economic development**. True economic development involves structural changes within the economy that lead to improvements in living standards and long-term societal well-being, beyond just short-term increases in output. [3].

Economic development should not be seen as a complete, superficial, temporary, and transient change limited to the elements of development. Rather, it is a complex, intertwined plan that aims to fundamentally change the economic structure and result in raising the rate of productivity to the extent of the efficient use of national and global resources and the available technological level. There is no doubt that this process is arduous and long. It is not easy to bring about such a change. Economic structures show resistance to any change, and the more backward the economy is, the stronger the resistance becomes, and vice versa. The term economic development is also related to

the long term, so the increase in national product must be continuous and uninterrupted for a long time. The long term should not be measured in a few years, but rather it must last at least fifteen years. The truth is that continuing economic development is a problem that both rich and poor countries suffer from. But accelerating development is more important for poor countries.

The study of economic development is one of the relatively recent studies that focused on economics after the beginning of the twentieth century, especially in developing countries. In general, economic development can be defined as: "a process in which real income increases cumulatively, rapidly, and continuously over a period of time, so that this increase is greater than the rate of population growth while providing productive and social services, protecting renewable resources from pollution, and preserving non-renewable resources from depletion". Other perspectives on economic development emphasize the importance of efficiently utilizing existing scarce or idle resources. According to this view, achieving continuous and sustainable growth requires not only optimizing resource allocation but also addressing the institutional, political, social, and economic mechanisms and tools within both the public and private sectors. Such a comprehensive approach is essential to driving improvements in living standards in a consistent and accelerated manner.

### 4. ECONOMIC EFFECTS OF OIL REVENUE

Oil revenues have played a somewhat contradictory role in the economic development of developing countries, particularly those lacking essential development components such as strong institutions and technical or administrative expertise. On one hand, oil revenues have significant positive effects. They serve as a primary source of capital to finance economic development projects, programs, and plans, reducing the need for taxing individuals or borrowing from abroad. This, in turn, helps foster industrial, agricultural, and

service sector growth in countries reliant on these revenues. Additionally, oil revenues provide the foreign exchange necessary to import goods and services that cannot be produced locally. On the other hand, oil revenues also have negative implications for economic development, with some of the most significant challenges being the following:

- 1) Monetary expansion and financial inflation due to the economic backwardness in the oil-producing countries and their inability to provide the volume of the gross national product necessary to cover the increase in domestic demand for goods and services, which causes the prices of goods and services to rise faster than the increase in the gross national product.
- 2) Fluctuation in the volume of oil revenues due to fluctuations in oil prices in global markets. Therefore, the revenues of oil-producing countries are unstable, and their economic performance depends on external factors, which exposes the national economy of those countries to serious risks.
- 3) High consumption rate and increased dependence on imports due to the financial expansion resulting from the increase in oil exports and the resulting increase in the incomes of individuals working in the public and private sectors.

## 5. ADVANTAGES OF FOREIGN DIRECT INVESTMENT AND CRITICISMS DIRECTED AT IT

Efforts to encourage the flow of foreign direct investment aim to benefit from the technology and technical and administrative knowledge that accompany the flow of this investment, as some countries may have the necessary funds to establish projects, but the lack of modern technology prevents the implementation of these projects. The most important advantages of foreign investment can be summarized. Direct and criticisms directed at him are as follows:

- Training local workers who have job opportunities in branches of foreign companies,

and acquiring modern technological skills using the latest work and training methods. Workers in these branches transfer and use their scientific, technical and administrative skills and knowledge to local companies when they join them. It is argued that in some cases, foreign direct investment does not play a noticeable role in the field of local labour acquiring modern technological skills, due to the small number of job opportunities produced by those investments due to their use of capital-intensive technological methods [4].

- The branches of multinational companies provide the needs of local companies for machinery, equipment, and technical assistance on favourable terms in the local market, which allows local companies the opportunity to produce goods with international specifications, and thus the ability to export their products to foreign markets. It is taken into account that such machines, equipment and production methods are characterized by capital intensity, which may not be appropriate to the conditions of the host country with its relative abundance of unskilled labor, and such technology is not adapted to suit the economic and social conditions of the host country except in rare cases.
- The emergence of competition between branches of multinational companies and local companies, which pushes the latter towards trying to obtain, adapt and develop the latest technical and administrative systems. The ability of local companies to acquire modern systems increases with the development of their technical, technological and human capacity. However, on the other hand, foreign companies may work in seizing local companies that are competitors in the local market, and create monopolistic situations for multinational companies.
- Adding foreign investments to the capital composition of the host country's economy and compensating for the lack of savings as a result of the renewed flow of those investments or reinvesting their returns. There is a possibility that these investments will

contribute to treating the structural imbalance of the host country's economy, if they flow into the industrial sector and infrastructure projects necessary for the establishment of a modern economy. However, foreign investments may not be directed to the economic sectors in a way that contributes to resolving the structural imbalance using modern technology, which leads to the establishment of a dual economy in that country, where the economy of the host country becomes composed of two sectors, one of which is relatively advanced from a technological standpoint and is represented by branches of foreign companies. The other is technologically backwards and contains local companies. In addition, the investments of these companies may be directed towards extractive industries in order to exploit the natural resources of the host country without manufacturing those resources in that country, and thus limited contribution to the development of the manufacturing sector.

- Supporting the host country's balance of payments. The international or direct effects of foreign direct investment on the host country's balance of payments may be positive, due to the increase in that country's foreign exchange earnings (capital operations account). This is in addition to the fact that foreign direct investment provides the host country with greater capabilities. To conquer export markets and increase their export revenues, but these effects on the balance of payments in the medium term are often negative due to the following reasons:

A) The positive effects on the balance of payments that accompany the influx of foreign investment quickly turn into negative effects after a while. As foreign investment will lead to an increase in the host country's imports of intermediate goods and services, multinational companies will also begin to transfer their profits abroad, in addition to paying interest on the financing received for those companies from banks abroad, and paying for patents and aid. This is in addition

to transferring a portion of the salaries of foreign workers in these projects abroad.

B) Despite the possibility of increasing the host country's exports through the activity of multinational companies and their extensive network of contacts in international markets, there are practices on the part of those companies that limit the importance of this possibility, and among these practices is the company itself limiting the exports of its branches in the host country, as the branch is very It is prohibited to compete with the parent company in global markets, or perhaps those branches are only allowed to export to specific markets in accordance with what are called "restrictive conditions." These practices have constituted a noticeable trend on the part of multinational companies, for some considerations such as the parent company's desire to protect its markets. Or the markets of some of its branches. The parent company may also seek to regulate the return on the technology and technical knowledge that it possesses, as limiting the ability of some branches to access certain markets creates an appropriate opportunity for other branches to buy technical knowledge and whose production covers those markets.

C) There is also the potential for increased pressure on the host country's balance of payments due to the export and import pricing policies implemented by multinational companies, particularly when capital is integrated across several of their branches. In such cases, the parent company may adopt practices such as undervaluing the prices of exports and imports between its subsidiaries. The underlying motivation for this pricing strategy is often to shift the tax burden from a high-tax jurisdiction to one with lower tax rates, thereby minimizing overall tax liabilities. This practice can distort trade balances and negatively affect the host country's economic stability

and revenue generation. Or it may resort to this as a hidden means of transferring profits from a country that imposes strict restrictions on Transferring profits and capital to another country with less stringent restrictions in this area.

## 6. THE IMPACT OF FOREIGN DIRECT INVESTMENTS ON EXPORT DIVERSIFICATION

Foreign companies generally, in their investment policy, localize their industrial facilities in host countries to take advantage of the advantages available in these countries, which are mainly represented by lower production costs. Thus, these companies promote their products either in the internal market of the host country or conquer new markets. In the first case, this policy is used to avoid transportation costs and customs duties, which you may face when exporting from the country of origin to the host country, but in this case, it is required to have a wide internal market and consumers with great purchasing power to absorb the products of this type of company. In this context, it can be argued that the impact of foreign investment on exports may be weak or even non-existent in certain cases. However, when foreign direct investment targets new markets, it can lead to an integration between such investments and a boost in exports from the host countries, particularly when these countries lack the capacity to distribute their products or face export restrictions. Therefore, it is essential for host countries to adopt an industrialization strategy that prioritizes export growth rather than solely focusing on import substitution manufacturing. The success of countries like the “Asian Tigers” can be attributed to the development of industries that initially thrived under protectionist measures, which were gradually eased in favor of strengthening export-oriented industries. Creating a regional economic space based on integration and trade exchange, as well as establishing free trade agreements, plays a significant role in attracting investors who seek to export beyond the host countries without facing customs barriers. This, in turn, can enhance

export growth and improve the overall balance of trade performance. However, foreign investment also tends to coincide with an increase in imports, driven by the high demand for intermediate products used in the production of finished goods and equipment. This reliance on imports can hinder the achievement of a balanced trade performance, particularly in the early stages of industrialization. However, despite the varied conclusions of research focused on the relationship between investment and economic outcomes, the experiences of most emerging countries have demonstrated that reliance on foreign direct investments (FDI) has significantly contributed to enhancing the competitiveness of their industrial exports, as well as diversifying and improving their export offerings. The geographical distribution of foreign direct investments in Libya shows a similar trend. Between 2018 and 2022, the total foreign direct investments flowing into Libya amounted to 4,729.618 million dinars, as shown in Table No. (1).

The number of countries making direct investments in Libya totals 30, including 9 Arab nations. The distribution of foreign direct investments (FDI) during the period from 2018 to 2022 is as follows:

- A) **Britain** leads the list of investing countries, with investments amounting to 2,757.729 million dinars, or 58.3% of the total foreign direct investments during the period.
- B) **Mauritius** comes in second place, with investments reaching 650.000 million dinars, representing 13.74% of the total foreign investments in Libya from 2018 to 2022.
- C) **The United Arab Emirates (UAE)** ranks third among all investing countries and holds the first position among Arab nations, with investments totaling 311.461 million dinars, or 6.5% of the total foreign direct investments during the same period.
- D) **Algeria** holds the fourth position overall and ranks second among Arab countries, with investments amounting to 260.427 million dinars, or 5.51% of the total foreign direct investments received by Libya between 2018 and 2022.

E) The total investments from **Arab countries** in Libya reached 843.992 million dinars, accounting for 17.8% of the total foreign direct investments during the period.

This data highlights the major contributors to Libya's foreign direct investment landscape, with particular emphasis on the dominance of Britain and the significant role of Arab nations in shaping the country's economic engagement.

**Table 1. Geographical distribution of inward foreign direct investments by country to Libya during the period 2018-2022 (Million dinars)**

number	Country	The value of inward foreign direct investments	Contribution percentage %
1	Saudi Arabia	4.900	0.10
2	Bahrain	7.800	0.16
3	The UAE	311.461	6.50
4	Palestine	4.076	0.08
5	Jordan	19.088	0.40
6	Morocco	6.582	0.14
7	Tunisia	105.976	2.24
8	Egypt	123.682	2.61
9	Algeria	260.427	5.51
10	Bosnia	3.864	0.08
11	China	6.662	0.14
12	Germany	13.064	0.27
13	Austria	2.232	0.05
14	Greece	1.424	0.03
15	America	50.585	1.07
16	Belgium	4.297	0.09
17	Türkiye	4.286	0.09
18	Belarus Russia	9.945	0.21
19	Slovakia	0.629	0.01
20	Switzerland	22.541	0.48
21	France	14.955	0.32
22	Cyprus	43.358	0.92
23	Canada	2.499	0.05
24	South Korea	19.500	0.41
25	Malta	170.530	3.60
26	Mauritius	650.000	13.74
27	Holland	3.712	0.08
28	Spain	6.773	0.14
29	Britain	2,757.729	58.30
30	Italy	97.041	2.05
<b>Total</b>		4,729.618	

Source: Investment Promotion Authority annual report for the period 2018-2022 [5]

The analysis of foreign direct investments (FDI) across various economic sectors reveals that these investments have not met expectations, with the majority being concentrated in the oil and gas sector. This focus on oil and gas allows the utilization of local resources for further investments, but the Libyan economy requires investment and partnerships in other sectors that can renew resources and enable the commencement of production across all industries. The relatively low level of foreign investment in other economic sectors can be attributed to several key factors, the most significant of which are as follows:

1. The lack of a competitive market, as the Libyan economy has not yet reached the level of required reforms, and this is considered relatively acceptable given the economic blockade that Libya went through during the crises that the Libyan economy went through.
2. In addition to what was mentioned previously, a foreign investor cannot take a risk unless he notices that the private sector is taking a risk in the host country, but what is observed in the Libyan economy is that commercial activity related to importing is predominant, due to the high returns it achieves compared to investment activity, as well as The facilities and manipulations in this field encourage private individuals to continue this activity instead of venturing into the investment process.

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## ULOGA STRANIH ULAGANJA U NAFTNOJ INDUSTRIJI

**Rezime:** Svrha istraživanja je da unapredi dugoročni rast u Libiji i mnogim zemljama u razvoju i omogućiti im da se pridruže razvijenim zemljama. Dva istraživačka pitanja kojima se ovaj rad bavi su: a) Koju ulogu mogu imati strane investicije u naftnom sektoru i proizvodnoj industriji u ekonomskoj diversifikaciji Libije i drugih zemalja? b) Koje su prateće mere koje je potrebno preduzeti da bi se povećao pozitivan uticaj stranih investicija na produktivnost Libijske ekonomije? Važna literatura koja vodi ovo istraživanje doprinosi ekonomskom i društvenom razvoju Libije i nekih zemalja. Direktno strane investicije smatraju se mehanizmom za poboljšanje produktivnosti, transfer stručnosti i tehnologije, podsticanje zapošljavanja i povećanje vrednosti izvoza, posebno u sektoru nafte i proizvodnje. Dizajn kvalitativnog istraživanja fokusiran je na najuspešnije ekonomske subjekte koji imaju koristi od iskustava. Međunarodna zajednica igra ključnu ulogu u strukturnoj transformaciji ekonomije Libije i drugih zemalja na severu Afrike i Bliskom istoku. U radu se došlo do dva glavna rezultata. Prvi je da je neophodno nastaviti sa podsticanjem preovlađujućeg industrijskog tkiva (industrija prerade nafte, prehrambena industrija i tekstilna industrija) u cilju podizanja vrednosti izvoza i očuvanja radnih mesta. Drugo, paralelno sa podsticanjem razvoja, neophodno je podsticati i industrijsku specijalizaciju Libijske ekonomije. Političke implikacije rezultata istraživanja su da uticaj stranih investicija na privredu arapskih zemalja varira od jednog sektora do drugog. Dakle, zemlje koje su ostvarile uspešan privredni procvat su one koje su bile u mogućnosti da usmere investicije u privredne aktivnosti sa visokom dodatnom vrednošću, kao što se desilo u Kini i Indiji. Negativni efekti stranih investicija su bili da je prisustvo stranih investicionih kompanija negativno uticalo na domaća preduzeća. Uprkos njihovom doprinosu povećanju izvoza, oni su negativno uticali na produktivnost sektora. Implikacije rezultata istraživanja na društvenu praksu jeste da proizvodni sektor igra važnu ulogu u apsorpciji radne snage, posebno one operativne koja ima prosečne kompetencije, i time doprinosi formiranju i rastu srednje klase u svetu. Direktno strane investicije u ovom sektoru pružaju mnoge mogućnosti za zapošljavanje domaće radne snage i podizanje plata.

**Ključne reči:** strane investicije, nafta, ekonomska politika, ekonomske analize Libije i arapskih zemalja.