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FDI Challenges in Syria

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Abstract: *Foreign Direct Investment (FDI) is recognised as a key contributor to economic expansion, bringing with it capital, technology, knowledge, and access to markets. Governments all over the world work to draw FDI by enacting laws and providing incentives to foster hospitable business environments. Since it aids in the recovery and resuscitation of war-devastated economies, FDI assumes special significance in post-war settings. This chapter focuses on the potential of FDI to restore and strengthen important industries while highlighting the role it played in post-war economic development. FDI stands out as an essential driver for reconstruction in the context of Syria, where the conflict has caused significant harm and economic instability. Construction, manufacturing, energy, and service industries can be strengthen with the support of FDI by adding capital, knowledge, and technology, generating employment opportunities, and accelerating economic recovery.*

Key Words: *Foreign Direct Investment (FDI), Economic Recovery, Conflict-Affected Economies, Syria.*

1. INTRODUCTION:

Foreign Direct Investment (FDI) plays a pivotal role in driving economic growth as an external source of capital. The significance of FDI lies in its ability to bring in substantial financial resources, technology, managerial expertise, and access to new markets, all of which contribute to boosting economic development. Firstly, FDI acts as a catalyst for economic growth by injecting much-needed capital into host countries. This infusion of capital helps finance the development of infrastructure, such as transportation networks, power plants, and telecommunication systems, which are critical for long-term economic expansion. Additionally, FDI brings forth job opportunities, fostering employment and income generation, which, in turn, leads to increased consumer spending and stimulates domestic demand. Secondly, FDI serves as a channel for technology transfer and knowledge diffusion. Multinational corporations (MNCs) that engage in FDI often bring advanced technologies, innovative production methods, and management practices to host countries. This facilitates the spillover of technological advancements, enhances productivity and efficiency, and promotes the growth of domestic industries. The acquisition of new skills and know-how by local workers through interactions with foreign firms further strengthens human capital and boosts overall competitiveness. Also, FDI acts as a gateway to international markets. When foreign investors establish subsidiaries or acquire local companies, they gain access to the host country's market and its neighboring regions. This not only enables the export of goods and services produced locally but also stimulates exports through global value chains and supply networks. Increased trade, in turn, leads to higher export revenues, balance of payments improvements, and enhanced economic integration.

Lastly, Foreign Direct Investment plays a crucial role in driving economic growth by providing external capital, facilitating technology transfer, and opening doors to international markets. Governments worldwide recognize the importance of attracting FDI and often implement policies and incentives to create an enabling environment for foreign investors. By harnessing the potential of FDI, countries can accelerate their economic development, foster industrialization, and improve the well-being of their citizens. In addition to that, FDI plays a vital role in post-war economic development by contributing to the reconstruction and revitalization of war-torn economies. After a conflict, countries often face severe destruction of infrastructure, a depleted workforce, and economic instability. FDI provides a much-needed injection of capital, expertise, and technology, helping to rebuild and develop key sectors. It enables the establishment of new businesses, the modernization of existing industries, and the creation of employment opportunities, thereby driving economic growth.

The ongoing conflict in Syria has resulted in extensive destruction to its infrastructure, leading to the disruption of economic activities and leaving the country in urgent need of reconstruction and development. Unfortunately, there is a lack of data or statistics on Foreign Direct Investment (FDI) in Syria since 2012, with the most recent available information found in the Statistical Yearbook from 2011. Nonetheless, FDI has the potential to play a critical role in the nation's recovery by injecting capital, expertise, and technology. By focusing on sectors such as construction, manufacturing, energy, and services, FDI can help rejuvenate the economy, create much-needed employment opportunities, and generate income for the country.

2. LITERATURE REVIEW:

Foreign Direct Investment (FDI) is widely acknowledged as a key driver of economic development, particularly in developing and post-conflict countries. It brings not only capital inflows but also technology transfer, managerial expertise, and access to global markets. The scholarly literature on FDI has evolved over time, offering theoretical and empirical insights into the determinants of FDI, the role of institutions, and the specific challenges that fragile states like Syria face.

One of the most influential theoretical frameworks in FDI literature is Dunning's Eclectic Paradigm (OLI model), which posits that foreign investment is driven by Ownership-specific advantages, Location-specific factors, and Internalization benefits (Dunning, 1988). This paradigm has laid the foundation for understanding the motives of multinational corporations (MNCs) when choosing investment destinations. In the case of Syria before the conflict, while location factors such as market size and regional trade access were moderately favorable, institutional weaknesses and poor infrastructure posed significant deterrents to foreign investors. Building on this, Narula and Dunning (2000) emphasized that globalization and structural transformation in developing countries depend heavily on the inflow of FDI and the role of MNCs in promoting industrial development. They argue that countries must strengthen their institutional frameworks and innovation systems to fully benefit from FDI. This point is echoed in the context of Syria, where inadequate legal protections, weak governance, and bureaucratic inefficiencies undermined the potential benefits of FDI even before the 2011 crisis. The importance of governance is further stressed by Globerman and Shapiro (2003), who found a strong positive relationship between governance infrastructure and U.S. FDI outflows. Their study underscores that countries with transparent legal systems, effective regulatory frameworks, and political stability are more likely to attract sustainable FDI. This finding is particularly relevant to Syria, where the breakdown of state institutions, lack of judicial independence, and widespread corruption contributed to an inhospitable investment climate.

From a post-conflict perspective, Addison, Geda, Le Billon, and Murshed (2001) argue that rebuilding war-torn economies requires a comprehensive strategy that includes restoring investor confidence, repairing infrastructure, and strengthening institutions. Their framework for post-conflict recovery places FDI at the center of reconstruction efforts, suggesting that foreign investment can catalyze economic revival if coupled with sound policy and governance reforms. This aligns with Syria's situation, where extensive wartime destruction necessitates large-scale capital inflows, though political risks remain a severe constraint.

The interplay between conflict and investment is further explored by Collier and Hoeffler (2004), who demonstrate empirically that civil wars lead to a significant reduction in FDI inflows. Their "greed and grievance" model indicates that countries affected by prolonged conflict suffer from diminished investor confidence due to heightened risk, uncertain property rights, and the threat of violence. In Syria, the onset of the civil war in 2011 led to the near-collapse of FDI, which had shown modest gains in the preceding decade.

In the regional context, Bauer and Yamey (1982) highlight the historical role of foreign investment in developing economies, especially where aid flows are limited. They caution, however, that without adequate institutional capacity, FDI can be misdirected and lead to economic distortions. This argument applies to Syria, where foreign investments prior to 2011 were often concentrated in rent-seeking sectors like oil and gas, with limited spillover to broader economic development.

Syria-specific studies further illustrate these dynamics. Dayyoub, Hamdan, and Rayya (2020) analyze the causal relationship between FDI and GDP growth in Syria and find that while FDI contributed positively to growth, its effect was limited by structural weaknesses. Similarly, Dalloul (2014) finds that while FDI had a statistically significant impact on GDP, the volatility of investment flows and the lack of policy consistency hampered long-term benefits.

The importance of institutional quality is also emphasized by Rodrik, Subramanian, and Trebbi (2004), who assert that institutions matter more than geography or trade openness in determining economic performance. Their cross-country analysis reinforces the need for Syria to prioritize legal and regulatory reforms as a prerequisite for reviving foreign investment.

Finally, the United Nations Conference on Trade and Development (UNCTAD, 2010) provides comparative data and policy recommendations for attracting FDI in low-income and post-crisis economies. It highlights the importance of

integrating FDI policy with sustainable development goals and institutional modernization—recommendations that Syria must consider in any post-conflict recovery framework.
In summary, the literature reveals that FDI inflows are highly sensitive to institutional, political, and economic conditions. While classical determinants like market size and labor cost remain important, the role of governance, legal protections, and post-conflict stabilization efforts are crucial for attracting and retaining FDI. For Syria, which continues to grapple with instability, sanctions, and infrastructural devastation, the road to re-establishing itself as a viable destination for foreign investment is contingent on fundamental structural reforms and peace-building efforts.

3. INVESTMENT IN SYRIA BEFORE THE CRISIS:

During the early 1990s, Syria began to adopt few measures to increase the investments such as the Investment Law no. 10 in 1991 which marks the beginning to the economic reforms that the Syrian Govt. began to implement. It aimed at attracting foreign investment and liberalizing its economy. However, progress was slow due to a lack of clear policies, bureaucracy, and a challenging business environment. (Al Hussein Mohammed, 2012) Despite these obstacles, some foreign companies, particularly from Europe and the Arab world, showed interest in investing in Syria. The sectors that received significant FDI during this period were oil and gas, tourism, and telecommunications.
In 2000, Bashar al-Assad became the President of Syria, and there was a renewed focus on economic reforms. The government initiated the Social Market Economy (SME) program to encourage private sector growth and attract foreign investment. Efforts were made to improve the legal and regulatory framework for foreign investors, simplify procedures, and provide incentives such as tax breaks and exemptions.
During this period, Syria witnessed a gradual increase in FDI, primarily in the energy sector. The government opened up the oil and gas industry to foreign investment, leading to the signing of exploration and production agreements with international oil companies. (Aljundi, 2010) These agreements aimed to tap into Syria's significant oil and gas reserves and modernize the sector.
The tenth five-year plan (2006-2010) emphasized the following strategic objectives:

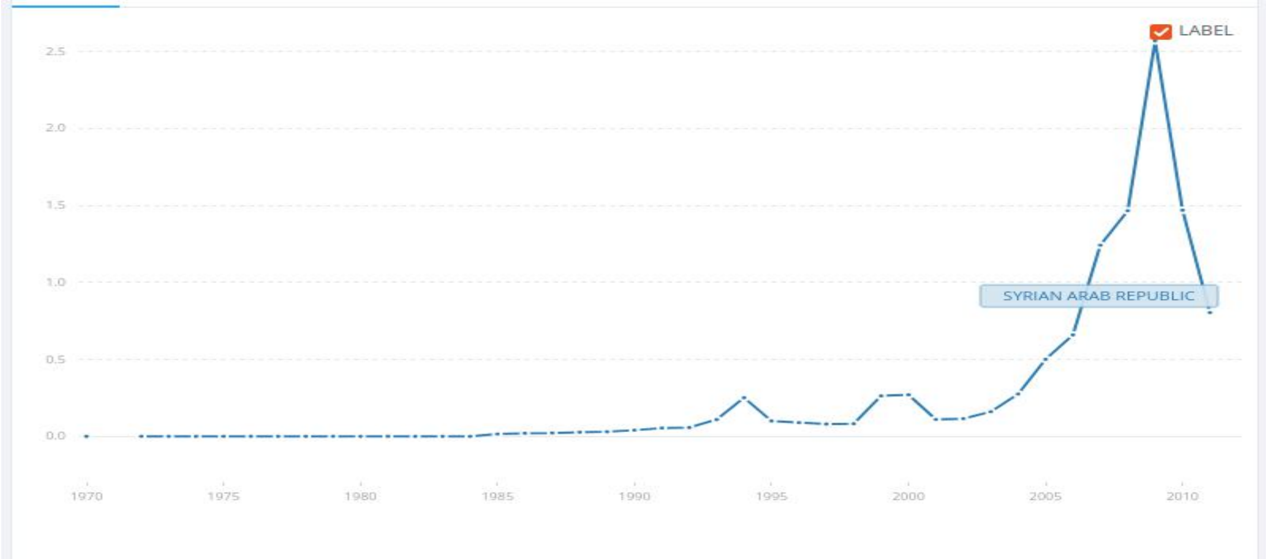
1. Encouraging foreign capital to enter the Syrian market.
2. Facilitate the liquidation of investments and stimulate long-term investment.
3. Increase transparency for financial institutions and relevant government departments.
4. Increase the number of products and services.
5. Complete the establishment of the stock market, and provide the legislative and institutional framework for the securitization of financial assets.
6. Providing the professions and advisory and financial services necessary for the prosperity of the financial sector.
7. Amending the Investment Promotion Law and the Labor Law.
8. Creation of special courts for investment and commercial disputes.
9. Promotion of investments abroad.

Additionally, the Syrian government aimed to diversify the economy and attract FDI in sectors like tourism, agriculture, and infrastructure. However, progress in these sectors was limited due to a lack of infrastructure, bureaucratic hurdles, and a challenging business environment. Corruption, inadequate legal protection for foreign investors, and limited access to information were also deterrents to FDI inflows.
Political stability and regional tensions played a crucial role in shaping the FDI landscape during this period. The 2003 invasion of Iraq and the subsequent instability in the region had a negative impact on investor confidence in Syria. As a response, the Syrian Govt. issued
the Legislative Decree No. /8/ of 2007 to encourage investment. which provided the investors with more tax incentives. The decree impacted the foreirgn investment which increased significantly in 2009 before it started to decrease in 2011 due the on crisis as the graph shows.

Prior to the outbreak of the civil war, Syria had been working on economic reforms and attracting foreign investment. The government aimed to diversify the economy, promote private sector growth, and improve the investment climate. Efforts were made to streamline bureaucratic procedures, enhance legal protection for investors, and introduce tax incentives. Some sectors, such as oil and gas, telecommunications, and construction, were more successful in attracting FDI during this period. Syria's energy sector had the potential to appeal to foreign investors due to its significant oil and gas reserves. Telecom companies also saw opportunities in the emerging Syrian market.
It is worth mentioning that the Syrian govt. has adopted an investment policy which does not discriminate between local and foreign investment in terms of incentives given to investors. While there were efforts to attract foreign investment through economic reforms and sector-specific policies, numerous challenges, including political instability, regional

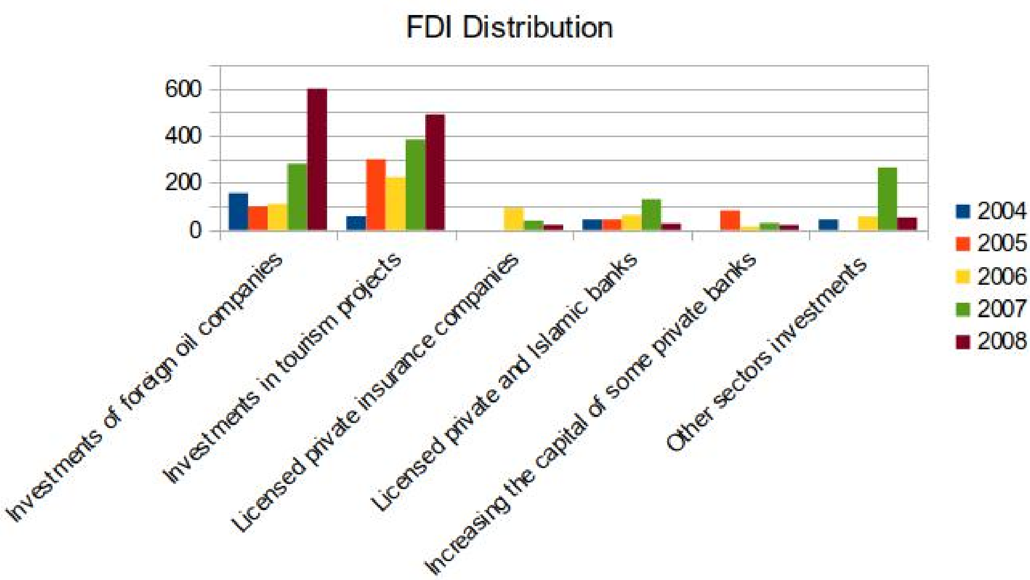
tensions, bureaucratic hurdles, and limited transparency, posed significant obstacles. (Dayyoub Mhmd Ma'en, 2020) These factors limited the inflow of FDI and hindered the country's ability to fully tap into its economic potential.

4. FDI Inflows to Syria 1970-2011:



Source: World Bank, https://data.worldbank.org

The Syrian civil war, which started in 2011, had a devastating impact on the country's economy and FDI prospects. The conflict created a highly unstable and volatile environment, with widespread violence, destruction of infrastructure, and displacement of millions of people. Foreign investors were deterred from entering or continuing operations in Syria due to the significant risks and uncertainties associated with the conflict. The deteriorating security situation, political instability, and international sanctions imposed on the Syrian government further exacerbated the challenges.During the war, the infrastructure of Syria was severely damaged, including industrial zones, transportation networks, and power facilities. This resulted in a loss of investor confidence and a significant decline in FDI. The war also disrupted supply chains, hampered production capabilities, and led to the loss of skilled labour. (Syrian Investment Agency, 2015-2017) Before the Syrian crisis, the main sectors that attracted foreign direct investment (FDI) were oil extraction, tourism, insurance, and banking. These sectors presented opportunities for international companies to invest and establish a presence in Syria.



Source: Syrian Investment Agency- Investment reports 2009

However, due to the ongoing conflict, reliable data and statistics on FDI in Syria after 2012 are unavailable, making it challenging to assess the current state of FDI. According to the Investment report in Syria in 2019, FDI inflows amounted to approximately 41 million USD from only nine projects. This indicates a significant decline compared to pre-crisis levels. Additionally, while local investments focused on the industrial, agricultural, and renewable energy sectors, they were unable to fully meet the market demand. The conflict and subsequent challenges have hindered the growth and attraction of FDI in Syria, impacting the country's economic recovery and development.

4. CONCEPTUAL FRAMEWORK :

Determinants of FDI

Foreign Direct Investment (FDI) inflows are influenced by a set of classical determinants widely discussed in international business and economic literature. These determinants help explain why multinational corporations (MNCs) choose to invest in specific host countries. One of the most comprehensive frameworks is Dunning’s Eclectic Paradigm (OLI framework), which posits that firms invest abroad when they possess Ownership-specific advantages (O), see Location-specific advantages (L), and find it beneficial to Internalize operations (I) rather than outsource them (Dunning, 1988).

Market size and growth potential are key location advantages, as firms prefer investing in countries with large or growing consumer markets. Syria, before the war, had a population of approximately 22 million, offering a modest market with potential for expansion. Natural resources, particularly oil and gas, also represent a major location advantage, attracting FDI in extractive industries. Labor availability and cost are equally significant; lower wages combined with a semi-skilled workforce provide cost efficiency for production.

Macroeconomic stability is another determinant. Countries with stable inflation, predictable exchange rates, and consistent fiscal policies attract more FDI. Syria, from 2000–2010, maintained moderate GDP growth (3.4%–6.8%) and exchange rate stability, largely due to central bank interventions and economic liberalization efforts. Additionally, openness to international trade, such as reduced tariffs and fewer capital controls, signals a business-friendly environment and strengthens investor confidence.

Legal and regulatory frameworks also play a critical role. Investors are attracted to countries with clear, enforceable property rights, transparent dispute settlement mechanisms, and tax or investment incentives. Syria passed several investment promotion laws during the 2000s, such as Investment Law No. 10 (1991) and Legislative Decree No. 8 (2007), offering tax breaks and guarantees against expropriation.

Infrastructure quality—including roads, telecommunications, ports, and power—directly affects operational efficiency. While Syria showed improvements in its infrastructure pre-2011, it remained inadequate compared to regional competitors.

In conclusion, FDI determinants are multifaceted and interrelated. Although Syria demonstrated some favorable characteristics such as resource endowments and policy reforms during 2000–2010, deficiencies in legal enforcement, infrastructure, and institutional quality limited the country’s ability to attract diversified and long-term foreign investment.

Obstacles to FDI in Post-War Syria

The Syrian civil war, which began in 2011, has introduced severe and persistent obstacles to foreign direct investment. The conflict not only disrupted Syria’s macroeconomic fundamentals but also led to a complete breakdown of essential state functions, undermining the environment required for sustainable FDI. These post-conflict barriers go beyond conventional investment risks and are deeply rooted in the destruction of physical infrastructure, the erosion of institutional trust, and Syria’s isolation from global financial systems. One of the most visible obstacles is the destruction of infrastructure. The war caused extensive damage to roads, bridges, power grids, industrial zones, and housing. According to United Nations estimates, rebuilding Syria’s infrastructure would cost hundreds of billions of dollars. Without functioning infrastructure, logistics, energy supply, and communication systems are unreliable, increasing the cost and uncertainty of doing business. Another major barrier is institutional weakness and legal uncertainty. Post-war Syria suffers from a fragile judicial system, unclear property rights (especially due to widespread displacement), and corruption in licensing and procurement. Although Syria had passed pro-investor legislation before the conflict, enforcement remains inconsistent, and foreign firms cannot rely on impartial dispute resolution. Political instability and security risks remain acute concerns. Many regions remain contested or governed by different factions, and national reconciliation is incomplete. The lack of a unified and stable political framework deters long-term investment commitments and exacerbates business risks.

International sanctions, especially by the United States and the European Union, compound these obstacles. These sanctions restrict foreign financial transactions, hinder access to international banking systems, and limit the ability of foreign firms to insure assets or repatriate profits. Even firms willing to take commercial risks in Syria may find themselves in violation of international legal frameworks.

Additionally, the loss of human capital is a critical impediment. Millions of Syrians have fled the country, including skilled professionals and entrepreneurs. The resulting brain drain hampers not only the labor supply but also innovation and managerial capacity needed for efficient business operations. Corruption and bureaucratic inefficiencies further discourage FDI. A study by Dalloul (2014) suggested that corruption accounted for nearly 30% of GDP, reflecting a deep structural issue that inflates operational costs and creates legal vulnerabilities for investors. In sum, the post-war context in Syria has layered traditional investment barriers with acute political, legal, and institutional challenges, rendering the country one of the least attractive destinations for FDI in the region without comprehensive reforms.

Theoretical Implications of State Fragility on Capital Flows

The dynamics of foreign direct investment in fragile or conflict-affected states diverge significantly from those in stable developing economies. Theoretical literature on state fragility and capital flows suggests that weak institutions, civil conflict, and political instability not only deter FDI but also fundamentally alter the investment calculus of multinational firms. Syria, as a case study, exemplifies the challenges outlined in these theoretical frameworks.

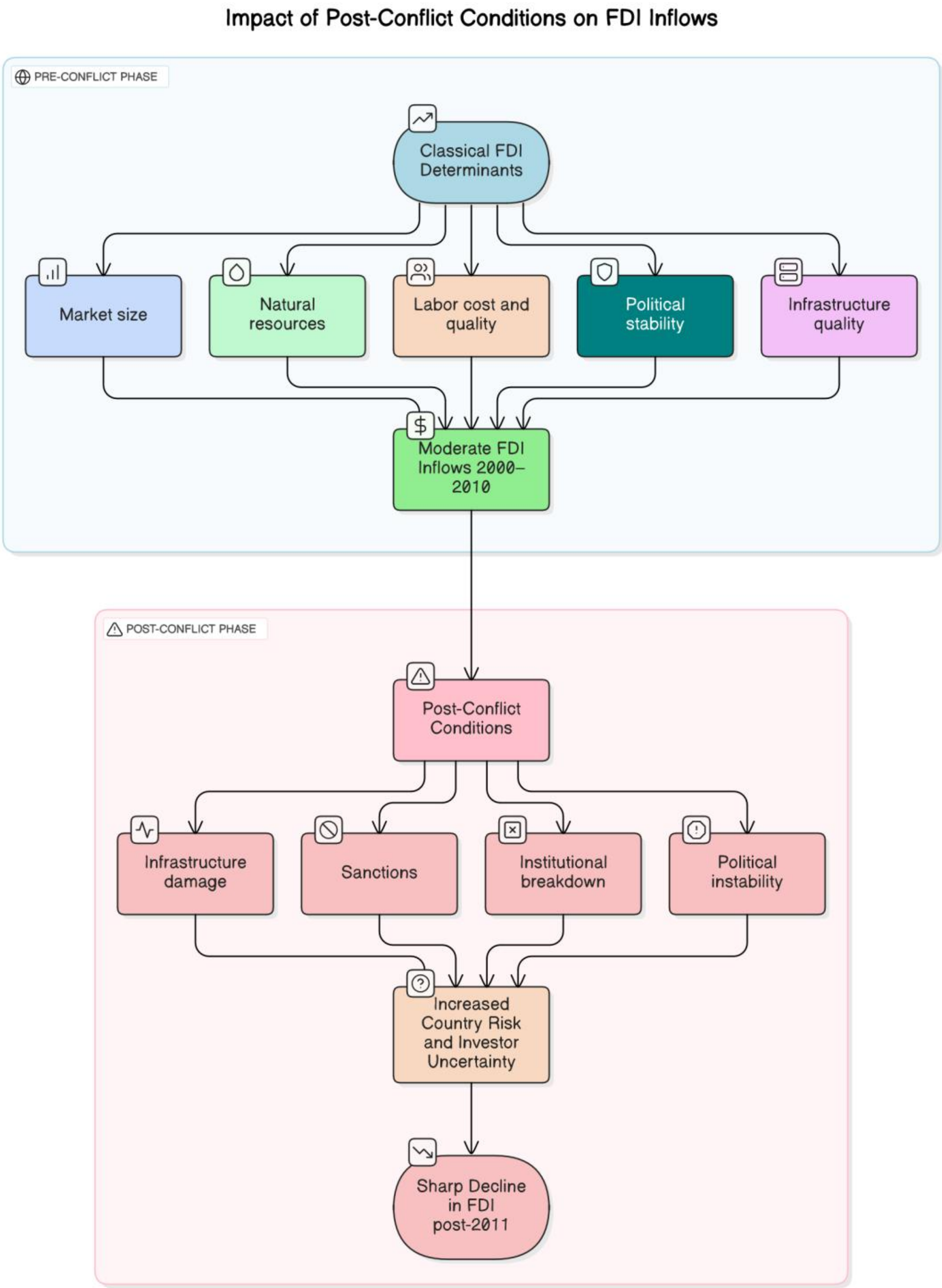
According to Institutional Theory, the quality of formal institutions—laws, regulations, enforcement mechanisms—and informal institutions—norms, trust, and governance—are fundamental in shaping investor behavior (Rodrik, Subramanian, & Trebbi, 2004). In fragile states, these institutions are either absent or dysfunctional. Syria's prolonged conflict has rendered its regulatory institutions ineffective and politicized, leading to an unpredictable business climate. As institutional quality deteriorates, foreign investors face higher transaction costs, increased uncertainty, and limited legal recourse.

Political Risk Theory further explains how instability affects capital allocation. Investors are highly sensitive to expropriation risks, currency volatility, and regime unpredictability. In Syria, the presence of multiple authorities across regions, international sanctions, and the prospect of military escalation significantly elevate political risk. As a result, FDI either diverts to safer neighboring countries or takes the form of short-term, speculative investment rather than long-term greenfield ventures.

The Conflict-Investment Nexus, advanced by Collier and Hoeffler (2004), emphasizes that civil wars drastically reduce FDI inflows by over 70% due to violence, infrastructure loss, and macroeconomic instability. They also highlight the "conflict trap," where conflict deters investment, which in turn reduces economic growth, increasing the likelihood of renewed conflict. Syria, with its shrinking GDP and disrupted markets, fits this model closely.

Additionally, OECD and World Bank frameworks on fragile states categorize countries like Syria as "low institutional capacity" environments, which require specialized investment frameworks. In such cases, traditional FDI theories—based on market size and cost advantages—are insufficient. Instead, the emphasis shifts toward risk mitigation strategies, public-private partnerships, and multilateral guarantees through institutions like MIGA (Multilateral Investment Guarantee Agency).

Therefore, the theoretical implication is that state fragility transforms the structure, type, and motivation of FDI. Instead of profit-maximizing capital inflows, post-conflict environments attract investment only under heavy risk guarantees, donor-backed development programs, or for extractive and enclave-based industries that require minimal local integration. For Syria to transition out of this model, comprehensive peace-building, institutional reform, and global reintegration are essential.



Source: the coneptual framworke is suggested by the authors

5. A STEP TOWARDS THE SOLUTION:

Considering the fact that Syria is a country that is still suffering from the ongoing crisis, rebuilding the whole economy is a Herculean task, however foucing on reconstructing one sector is more practical and applicable idea. That includes the procces of undergoing a process of industrialization and shift resources from low-productivity sectors (such as agriculture) to high-productivity sectors (such as manufacturing or services). (Hirschman. 1958) However, the application of such a method is not possible in Syria taking into account the lack of resources and the damaged infrastructure. That'swhy there is need to find a fast and practical solution. (FDI) can serve as a crucial external resource of capital that has the potential to contribute significantly to the reconstruction of the Syrian economy. Given the extensive devastation caused by years of conflict, the country requires substantial financial resources to rebuild its infrastructure, revive its industries, and create employment opportunities. (Dayyoub Mhmd Ma’en, 2020) FDI can play a vital role in this process by bringing in much-needed investment, expertise, and technology from abroad. It can help finance critical sectors such as construction, energy, telecommunications, and manufacturing, fostering economic growth and revitalizing the country's productive capacity. Moreover, FDI can facilitate knowledge transfer, skill development, and the adoption of best practices, promoting innovation and productivity gains in the domestic economy. However, to effectively harness the potential of FDI, it is essential for Syria to provide a stable and investor-friendly environment, with transparent regulations, protection of property rights, improved governance, and security guarantees. Additionally, efforts should be made to address social and political challenges, rebuild trust, and create a conducive atmosphere for sustainable investment inflows that contribute to the long-term reconstruction and development of the Syrian economy.

6. RECOMMENDATIONS:

In light of the pressing challenges facing Syria, the following policy recommendations are offered to address the urgent need for peace and stability, reanimate the industrial sector through increased investment, and align the education system with market requirements:

- Prioritize Peace and Political Stability: The Government of Syria should prioritize efforts to bring about lasting peace and political stability in the country. This involves engaging in comprehensive dialogue and negotiations with all relevant parties, seeking diplomatic solutions, and implementing confidence-building measures. Establishing a stable political environment is crucial to creating a conducive atmosphere for economic growth and attracting investment.
- Promote Investment in the Industrial Sector: Recognizing the importance of the industrial sector in driving economic development and job creation, the Syrian government should implement policies and initiatives to attract both domestic and foreign investment. Special emphasis should be placed on promoting foreign investment in key industrial sub-sectors, such as manufacturing, energy, and infrastructure. This can be achieved through streamlined regulations, incentives, and targeted marketing campaigns to showcase the investment opportunities available in Syria's industrial sector.
- Develop a Special FDI Policy for Industrial Development: The government should draft a specific Foreign Direct Investment (FDI) policy that focuses on the development of the industrial sector. This policy should aim to attract foreign investors who are willing to invest in industrial projects, transfer technology, rebuilding the infrastructure and contribute to the development of local talent. The policy should outline clear guidelines, streamlined approval processes, and incentives for investors to encourage long-term commitments and partnerships. Additionally, it should prioritize the hiring and training of local labor to enhance employment opportunities and contribute to the country's overall socio-economic development.
- Enhance the Education System to Meet Market Requirements: Recognizing the importance of a skilled workforce for industrial development, the Syrian government should undertake comprehensive reforms in the education system. This includes updating curricula, improving vocational and technical training programs, and enhancing the quality of education at the pre-university and undergraduate levels. Collaboration between educational institutions and the private sector should be fostered to align educational offerings with the evolving needs of the job market. Furthermore, promoting entrepreneurship and innovation should be integrated into the education system to cultivate a culture of creativity and adaptability among students.

By implementing these policy recommendations, the Government of Syria can foster an environment of stability, attract investment to the industrial sector, and ensure the education system produces a skilled workforce. These measures will not only contribute to the economic recovery and reconstruction of Syria but also lay the foundation for sustainable development and a prosperous future for the country and its people.

The policy suggestions presented above, in conclusion, offer a thorough framework for the Government of Syria to solve the short- and long-term issues it faces. The government can foster an atmosphere that is conducive to economic growth and draw in much-needed investment by placing a high priority on peace and political stability. Putting an emphasis on the industrial sector and creating a specialised FDI strategy will aid in reviving important industries, creating job opportunities, and fostering technological developments through international collaboration. The workforce will be given the skills and information required for a dynamic and competitive economy If the educational system is updated to suit market demands. If adequately carried out, these policy suggestions could help Syria move towards a more promising future by promoting sustainable growth and enhancing the quality of life for its people. In order to make these proposals a reality and create the groundwork for prosperity and stability in the years to come, it is imperative for the government to act swiftly and in partnership with the appropriate stakeholders.

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