Madagascar: 2009 Investment Climate Statement

Openness to Foreign Investment

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The GOM officially welcomes foreign investment and the country's regulatory framework is evolving to become more investor-friendly. Administrative level implementation, however, often lags official policy. Madagascar has generally not been an easy place to launch and grow a business – for nationals and foreign investors – but the significant stock of foreign investment is evidence of the rewards available. Although the current government has expressed a commitment to improve the investment climate, in practice, conflicts of interest and the lack of a level playing field continue to plague investors. A lack of transparency in contracting and in government regulatory decisions also dampens the investment climate.

According to the Malagasy Central Bank, foreign direct investment (FDI) inflows to Madagascar in 2007 amounted to USD 777.1 million representing 10.5 percent of GDP. The most active sectors in FDI in 2007 were extractive industries, telecommunications, and public works. The projection for 2008 is to reach an FDI inflow of USD 1.35 billion, driven again by the same sectors.

The Bretton Woods institutions have generally endorsed the government's macro-economic regime, although they questioned certain non-transparent budget and tax decisions in late 2008. Better governance is a priority, which the government and donors agree must be given special attention, including the improvement of the regulatory system and the fight against corruption. The poor quality and high cost of physical infrastructure (road, electricity, telecommunications, port efficiency, air cargo capacity) and the limited availability of credit and financing instruments constitute investment climate bottlenecks that offset Madagascar's advantage from a low-wage, productive work force. The Malagasy government, in collaboration with donor institutions and countries, is analyzing impediments to investment with a view towards eliminating the most serious drawbacks. Madagascar moved up 7 rankings in the World Bank 2009 "Doing Business Report," ranking 144th out of 181 countries, compared to 151st in the 2008 report.

In September 2006, the Madagascar Action Plan (MAP), a five-year development strategy paper (2007-2011), was presented to the public and private sectors, as well as to donors. The MAP is guiding government strategy in encouraging growth as a market-based economy, in attempting to alleviate poverty and improve social indicators, and in attracting foreign investment.

A new export promotion law adopted by the Parliament in December 2008 grants some benefits to exporters, including the reduction of the customs tax rate on imported capital goods and raw materials to five percent (previously ranging from 10 to 20 percent). Additional benefits include export tax exemption, freedom of opening bank accounts abroad, and the creation of an export agency under the economic ministry to facilitate and promote exports. In 2008, the Economic Development Board of Madagascar (EDBM) continued to assist foreign investors and conducted various road shows abroad to attract foreign investments. The creation of the American Chamber of Commerce in Madagascar (AMCHAM) in December 2008 should help boost trade and investment between the U.S. and Madagascar.

The first country to sign a Millennium Challenge Account (MCA) Compact, in April 2005 in the amount of USD 110 million, Madagascar is making strides in implementing various activities in the areas of financial services, land tenure, and agribusiness investment.

There is no law or regulation authorizing private firms to adopt articles of incorporation or association that limit or prohibit foreign investment, participation or control. Further, there is no official practice to restrict foreign investment, participation in, or control of domestic enterprises. There is no mandatory screening of foreign investment and there is no discrimination against foreign investors at the time of the initial investment or after the investment is made, such as through special tax treatment, access to licenses, approvals, or procurement.

To show transparency and good governance in the management of revenues from extractive resources, the GOM and the main operators in the extractive industries such as Exxon Mobil, Rio Tinto, Madagascar Oil, and Sherritt continued to take the necessary steps to implement the Extractive Industries Transparence Initiative (EITI) in 2008.

Conversion and Transfer Policies

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In 1998, the GOM lifted all restrictions on current payment and transfers and accepted the obligations of Article VIII of the IMF articles of Agreement, which provides for the complete elimination of exchange controls. There are no restrictions on converting or transferring funds associated with foreign investment, including remittances of investment capital, earnings, loan repayments, and lease payments into a freely usable currency at legal market clearing rate. When delays occur in conversion or funds transfer, they are due to temporary shortages of foreign exchange. By law, foreign investors must make remittances through banks. There is no limitation on the inflow or outflow of funds for remittances of profits, debt service, capital, and returns on intellectual property. Exporters and foreign investors may maintain bank accounts in foreign currencies. Madagascar has a flexible exchange rate policy, allowing underlying exchange market pressures to determine rates and limiting central bank intervention to dampening temporary shocks and achieving its external reserves objectives.

Madagascar, through donors' assistance, is working to pass comprehensive legislation to regulate and facilitate electronic transactions (e-commerce).

Expropriation and Compensation

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There are no recent cases of expropriation actions by the GOM nor do Government policies suggest that it is likely to take such actions in the near future. Since the country is under an IMF poverty reduction and growth facility (PRGF) agreement, there is little risk of future expropriation. The state divestiture from public enterprises has been a cornerstone of government policy; however, government proposals in late 2008 to recreate a state oil company have called this policy into question. There are no laws requiring local ownership in specific economic sectors except in oil exploration, in which the Government office called OMNIS must be the partner of all foreign companies.

Dispute Settlement

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Madagascar's legal system is based on French civil law and its provisions contain adequate protections for private property rights. Malagasy commercial law consists largely of the Code of Commerce and Annexed laws, which are reportedly applied in a non-discriminatory manner. Madagascar has a written bankruptcy law, created in 1996 and currently included in the Code of Commerce. The Malagasy judicial system is slow and complex and has a reputation of opacity and corruption. U.S. assistance has supported the development of alternative dispute resolution systems to provide more rapid, more transparent, and less costly resolution of commercial disputes.

Under the privatization law, the GOM accepts binding international arbitration of investment disputes between foreign investors and the state. The courts recognize and enforce foreign arbitral awards and international arbitration is accepted as a means for settling investment disputes between private parties. The Malagasy Arbitration and Mediation Center (CAMM, in its French acronym) was created in 2000 as a private organization to promote and facilitate the use of arbitration to resolve commercial disputes and to lessen reliance on a court system that is, at a minimum, overburdened. As a result, many private contracts now include arbitration clauses. The EDBM is also responsible for investment dispute resolution; however, it has been unable to resolve several concerns raised by American companies regarding conflicts of interest and the lack of transparency in contracting and in government regulatory decision making.

Madagascar is a signatory to the International Center for the Settlement of Investment Disputes (ICSID) Convention. Madagascar is also a signatory to the New York Convention of 1958 on the Recognition and Enforcement of Foreign Arbitral Awards and Madagascar has been a member of the Multilateral Investment Guarantee Agency (MIGA) since 1989. The Malagasy government has expressed interest in negotiating a bilateral investment treaty (BIT) with the U.S. Initial discussions began in late 2008.

Performance Requirements and Incentives Return to top

As a signatory of the WTO Agreement, Madagascar is bound by the WTO TRIMS (Trade Related Investment Measures). Performance requirements are not imposed as conditions for establishing or maintaining investments, except in the Export Processing Zones (EPZ) regime under which firms must export 95 percent of output to qualify for EPZ investment incentives. Foreign or local investors can benefit from tax exemptions provided their EPZ projects fall into the following categories:

- Investment in export-oriented manufacturing industries;
- Development or management of industrial free zones; or
- Provision of services to EPZ companies.

The EPZ law approved in December 2007 granted the following advantages and tax incentives to EPZ companies:

- The EDBM is in charge of EPZ companies' approval. The EDBM has to deliver an eligibility certificate within 20 days of deposit of file.
- 15 years tax exemption for EPZ companies
- No VAT or customs duties on imports of raw materials
- No registration taxes
- No customs tax on exported goods
- Income tax on expatriate not exceeding 30 percent of the taxable basis
- Free access to foreign currency deposited in the company's foreign currency bank account.

The new export promotion law that was adopted in December 2008 determined that these EPZ provisions (advantages and tax incentives) would only be offered until December 2010. Already existing EPZ companies will continue to enjoy the advantages described above after that date.

There are no requirements restricting the mobility of foreign investors. The regime for visas, residence and work permits is, on its face, neither discriminatory nor excessively onerous. Since the creation of the EDBM, processing of residence and work permits has been streamlined.

There is no requirement that investors purchase from local sources, or export a certain percentage of output (except for EPZ companies), or only have access to foreign exchange in relation to their exports.   There is no requirement that nationals own shares of foreign companies, that the share of foreign equity is reduced over time, or that technology is transferred on certain terms. There are no government-imposed conditions on permission to invest (although investors must apply for such permission), including location in a specific geographical area, specific percentage of local content or local equity, substitution for imports, export requirements or targets, employment of host country nationals, or technology transfer. Investors are not required to disclose proprietary information to the government as part of the regulatory approval process. U.S. and other foreign firms are able to participate in government-financed and/or subsidized research and development programs on a national treatment basis. There are officially no discriminatory or preferential export or import policies, which would affect foreign investors, nor discriminatory tariff or non-tariff barriers, or other measures such as import or price controls. However, as of January 2009, the government was in the process of recreating a state oil company with exclusive rights to import certain petroleum products, as well as implementing an administrative pricing mechanism for these products. Also, in practice, there is at times an unlevel playing field in terms of tariff and tax burden among private companies.

Right to Private Ownership and Establishment

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Foreign and domestic private entities may establish and own business enterprises and engage in all forms of remunerative activity. They may freely establish, acquire, and dispose of interests in business enterprises. The government remains a minority shareholder in some privatized companies, such as Telma, and continues to own Air Madagascar, but competitive equality is the official standard applied to all private enterprises with respect to access to markets, credit, and other business operations such as licenses and supplies. In practice; however, politically-connected companies are sometimes given preferential market access. The private sector often complains about government interference in some sectors of the economy, including flour and vegetable oil.

Protection of Property Rights

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Secured interests in property are recognized, but not yet enforced in the country. Banks and insurance companies use mortgages to guarantee loans relating to commercial property.

A prohibition on land ownership by foreigners impedes access to real property. A system of long-term leases – up to 99 years – was established in 2008 following the adoption of investment law 2007-036 to address the issue, but there have been long delays and few successes so far in the approval of land leases for foreigners. The new investment law grants land and properties to companies registered in Madagascar under certain conditions fixed by EDBM, which issues authorization documents. In addition, MCA's contribution to the land tenure issue is improving the land rights process.

Madagascar is a member of the WIPO (World Intellectual Property Organization) and is signatory to the WTO TRIPS agreement on trade related aspects of intellectual property. Two government offices share responsibility for the protection of intellectual property rights: the Malagasy Office for Industrial Property (OMAPI) and the Malagasy Copyright Office (OMDA). Protection of intellectual property rights is uneven. Officially, authorities protect against infringement, but in reality, enforcement capacity is quite limited. Major brands are generally respected but pirated copies of movie DVDs, music CDs and tapes, electronic equipment and spare parts are sold openly. Some television stations regularly show pirated copies of first-run U.S. and European movies. On July 17, 2006, an inter-ministerial decree was issued to reinforce measures to fight counterfeiting of literary and artistic works. Upon evidence of illegal activity, OMDA and its partners (police, customs officers, tax officers, controllers of the ministry of commerce) proceed to the seizure of all illegally reproduced recorded products, be they illegally manufactured or imported, and specific materials used for such dealings. Those products are subject to public destruction in presence of the contravener(s). A control committee was set up to follow-up the application of such decree. To conclude, enforcement of intellectual property rights is limited due to a shortage of trained personnel, legal capacity and resources.

Transparency of Regulatory System

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Excessively complex and inconsistently applied bureaucratic regulations are an impediment to investment and can be a breeding ground for corrupt practices. The lack of transparency in government regulatory decisions has generated complaints from current investors. As part of its emphasis on good governance, the GOM is seeking to streamline processes and improve administrative efficiency and transparency at all levels. Thanks to the EDBM, registration of companies now only takes around 4 days.

Tax, labor, environment, health, and safety standards are not used to impede foreign investment, and there are no informal regulatory processes managed by non-governmental organizations or private sector associations.

Accounting systems are transparent and consistent with international norms, and there are no private sector and/or government/authority efforts to restrict foreign participation in industry standard-setting consortia or organizations.

Efficient Capital Markets and Portfolio Investment
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In spite of the general under-development of the banking system, banks are free to support the flow of resources in the product and factors markets. Credit is usually allocated on market terms and the private sector/foreign investors are able to get credit on the local market. However, many of the EPZ companies use the services of banks in neighboring Mauritius, where the sector is more developed.

There are no cross-shareholding arrangements used by private firms to restrict foreign investment through mergers and acquisitions. There are no visible private sector and/or government efforts to restrict foreign participation in industry or control of domestic enterprises.

Within the Malagasy law, there is an effective regulatory system established to encourage and facilitate portfolio investment and the estimated total assets of the country's largest bank are around USD 400 million.

The government announced in January 2009 that the Malagasy Bank for Construction and Development (BMCD) would be launched in 2009. The bank's main mission will be to assist small and medium enterprises.

Political Violence
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Political violence is relatively uncommon in Madagascar. The political crisis of January-June 2002 involved a division of the country between two rival governments but was remarkably restrained in terms of violence. Civil disturbances are uncommon and there have been no notable cases of politically motivated damage to projects. Public safety is adequate; although standard warnings to guard against street crime and theft from vehicles and to minimize or avoid night time road travel, particularly in rural areas apply. Madagascar, being an island, has no belligerent neighbors.

Corruption
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Complicated administrative procedures introduce delays, uncertainties and multiply the possibilities for corruption. Combating corruption is a stated priority of the Malagasy government and senior officials appear to be taking that effort seriously. BIANCO, the Anti-corruption Independent Office created in 2004, continues to implement the anti-corruption policy. Ten sectors are targeted in the fight against corruption: justice, gendarmerie, police, tax office, customs, treasury, land, trade, education, and health.

Giving or accepting a bribe is a criminal act and is sentenced by court.

In 2008, Transparency International ranked Madagascar 85th out of 180 countries surveyed, as it scored 3.4 in the Corruption Perception Index (CPI), indicating a severe (albeit improving) corruption problem.

On July 19, 2008, SAMIFIN, the office in charge of the fight against money laundering was created. Its objective is to investigate all allegations of money laundering coming from financial institutions, including those involving corruption.

Bilateral Investment Agreements

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According to ICSID (International Center for the Settlement of Investment Disputes) and UNCTAD, Madagascar has concluded bilateral investment agreements with Switzerland, Sweden, Norway, Mauritius, Germany, France, Thailand, Belgium, China, and Canada. Also, Madagascar has signed double taxation treaties with France and Mauritius. The Malagasy government has expressed interest in negotiating a bilateral investment treaty with the U.S. Initial discussions began in late 2008.

OPIC and Other Investment Insurance Programs

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On March 31, 1998, OPIC and Madagascar signed a bilateral Investment Incentive Agreement, which updates the old agreement of 1963.

Madagascar is a member of the MIGA (Multilateral Investment Guarantee Agency). The average annual exchange rate for 2008 was 1708 ariary per one USD. As of January 2009, the ariary had depreciated to around 1890 per one USD. To the benefit of Malagasy exporters, further modest depreciation is expected in 2009.

Labor

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Madagascar has a significant pool of available labor, due to the combined impact of unemployment and under-employment. Private sector wages have been relatively stable and are below those in most competitor countries; indeed, this fact, combined with the high quality of much Malagasy labor, may constitute the country's strongest asset for foreign investors. The minimum wage for the non-agricultural private sector in 2008 was 70,025 ariary per month, approximately USD 41. The Constitution and Labor Code grant workers in the private and public sectors the right to establish and join labor unions, and to bargain collectively. The National Labor Code and implementing legislation prescribe working conditions, wages, and standard for worksite safety. As a member of the ILO (International Labor Organization), Madagascar adheres to the ILO convention protecting workers rights.

Foreign-Trade Zones/Free Ports

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The incentives available in the Export Processing Zone (EPZ) are described in "Performance Requirements and Incentives". There is no distinction between foreign and domestically owned firms in terms of eligibility for EPZ treatment, which has been granted by the EDBM since December 2007. Again, as stated earlier, EPZ incentives will be offered only through December 2010, but pre-existing EPZ firms will maintain their incentives and status beyond that date.

Foreign Direct Investment Statistics

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According to a World Bank survey, Madagascar is among the 40 most difficult countries in the world in which to conduct business. The main reasons are the weaknesses of the judicial system and the banking system (high interest rates and unavailability of credit), the high cost and low quality of electric power, high tax rates, red tape, corruption, conflicts of interest, a lack of transparency in decision-making, and the high costs of ground and air transport and telecommunications.

In 2007, FDI inflows to Madagascar amounted to USD 777.1 million or 10.5 percent of GDP. Compared to 2006, FDI inflows more than doubled in 2007. Although this increase boosted GDP figures, it did not create significant numbers of jobs. FDI was concentrated in the following sectors: extractive industry (USD 472.9 million, or more than 60 percent of the total), telecommunications (USD 191.6 million), building and public works (USD 58.2 million), financial activities (USD 21.3 million) and oil product distribution (USD 12 million). This rebound was fuelled essentially by investment in mineral exploration, particularly by the ilmenite investment project of QIT Madagascar Mineral (Rio Tinto) and by the nickel and cobalt investment project of Ambatovy, a joint venture including Sherritt International, SNC-Lavalin, Sumitomo Corporation, and Korea Resources Corporation.

The main partner countries of Madagascar in terms of 2007 FDI flows were Canada with 46 percent of new FDI, followed by France with 21 percent, and Mauritius with 16 percent. The United States contributed 4.5 percent to 2007 FDI inflows. Canadian investment increased by 146 percent in 2007. Ninety-nine percent of Canadian investment was concentrated in the extractive industry. French investments in 2007 were six times higher than in 2006 and were allocated in the telecommunication sector (54 percent), building and public works (36 percent), and financial activities (7 percent). Mauritian investments increased five times and were concentrated in the telecommunications sector (81 percent), but also included oil product distribution (10 percent), manufacturing (4 percent), and financial sector (4 percent).

U.S. investment covers a broad spectrum of sectors including oil exploration, apparel, mining, and handicrafts.

Several additional large mining projects are on the horizon, and the government is in the final stages of liberalizing the telecommunications sector. Thus, the investment trends of 2008 – which have not generated the significant employment opportunities that are badly needed -- will likely continue in 2009. However, the agribusiness sector has the potential to attract sizable, job-generating investments, particularly in palm oil, corn and sugar, if land tenure complications can be resolved. Tourism is the other sector most often cited for its potential for both foreign investment and job creation.

FDI inflows in 2008 are projected to reach USD 1.35 billion.