The World Bank Doing Business Rankings: Do they really matter for FDI investment?

By Dinuk Jayasuriya
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A large body of literature argues that foreign direct investment (FDI) promotes economic growth with some even arguing that FDI in turn reduces poverty. How then can countries attract FDI? Currency depreciation, strong GDP growth, low inflation and a greater openness (percentage of imports and exports over GDP) have all been considered as determinants. ‘Governance’ factors have also be touted as important; for example, appropriate regulatory quality, strong rule of law, government effectiveness, low corruption and high levels of political freedom might also promote FDI. Nevertheless, the literature is mixed with reference to the significance and the magnitude of all these variables.

One item that seems to generate much press in relation to contributions to FDI Inflows are the World Bank Doing Business Rankings, which ranks countries according to their Ease of Doing Business. The components of the rankings including ease of starting a business, registering property, getting credit, protecting investors, paying taxes, trading across borders and enforcing contracts. These are largely measured across time and cost to complete procedures.

Many countries and the media place much emphasis on their rankings with some believing that improvements in their global rankings improve FDI Inflows. The World Bank itself does not suggest this – however it is interesting to investigate whether a relationship exists – and if so whether improvements in rankings should be promoted as a mechanism to improve FDI Inflows.

Devpolicy’s latest Discussion Paper, entitled “Improvements in the World Bank’s Ease of Doing Business Rankings: Do they Translate into Greater Foreign Direct Investment Inflows?”, investigates this relationship and finds that for the average country, the relationship is positive and significant. However, the relationship is not significant for the average developing country. A possible reason comes to mind; recent work by Mary Hallward-Driemeier and Lant Pritchett in their paper “The Investment Climate When Firms

Have Climate Control" show that *actual* experiences of firms in regards to the time and cost for compliance (as measured by enterprise surveys) differ to the *official* time and cost for compliance (as measured by the doing business rankings). Firms may note this difference and may ignore the official rankings when focusing on FDI inflows into developing countries as they are more likely than developed countries to struggle with compliance.

While robust, the results are from a panel of 86 countries over 4 years. As more time series data becomes available, it would be interesting to see if the results change.

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