VALE COLUMBIA CENTER
ON SUSTAINABLE INTERNATIONAL INVESTMENT
A JOINT CENTER OF COLUMBIA LAW SCHOOL AND THE EARTH INSTITUTE AT COLUMBIA UNIVERSITY

WAIPA
World Association of Investment Promotion Agencies

Investment Promotion Agencies and Sustainable FDI:

Moving toward the fourth generation of investment promotion

Report of the findings of the Survey on Foreign Direct Investment and Sustainable Development undertaken by the Vale Columbia Center on Sustainable International Investment (VCC) and the World Association of Investment Promotion Agencies (WAIPA)
June 25, 2010

The Vale Columbia Center on Sustainable International Investment (VCC) seeks to be a leader on issues related to foreign direct investment (FDI) in the global economy, paying special attention to the sustainability dimension of this investment. It focuses on the analysis and teaching of the implications of FDI for public policy and international investment law. Its objectives are to analyze important topical policy-oriented issues related to FDI, develop and disseminate practical approaches and solutions, and provide students with a challenging learning environment. For more information, please see http://www.vcc.columbia.edu.

The World Association of Investment Promotion Agencies (WAIPA) was established in 1995 and is registered as a non-governmental organization (NGO) in Geneva, Switzerland. WAIPA acts as a forum for investment promotion agencies (IPAs) to provide networking opportunities and facilitate the exchange of best practices in capacity-building and investment promotion. Membership is open to all agencies whose primary function is to promote any country or territory for investment. For more information, please see http://www.waipa.org.

We would like to recognize Vale for making this survey possible, as well as all the IPAs that collaborated in this project by completing the survey. We would also like to recognize the following individuals for feedback on the survey instrument: Oscar Alvarez, Carlos Bronzatto, Henry Loewendahl, Howard Mann, Karin Millett, Theodore Moran, Lisa Sachs, Diana Salazar, and Daniel Torres. Persephone Economou managed the project on behalf of VCC, and Carlos Bronzatto on behalf of WAIPA. The report was drafted by Persephone Economou.

For more information on the VCC-WAIPA Survey on Foreign Direct Investment and Sustainable Development, please contact Karl P. Sauvant – Karl.Sauvant@law.columbia.edu.

Investment Promotion Agencies and Sustainable FDI: Moving toward the fourth generation of investment promotion

Report of the findings of the VCC – WAIPA Survey on Foreign Direct Investment and Sustainable Development

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Summary of findings

This report is based on a survey of investment promotion agencies (IPAs) that are members of the World Association of Investment Promotion Agencies; it was carried out during April-May 2010.

In general IPAs are moving toward what might be termed "the fourth generation" of investment promotion, namely, targeting *sustainable* FDI. This follows the first generation of investment promotion, when countries liberalized their regulatory frameworks for such investment; the second generation, when many IPAs were established to attract FDI; and the third generation, when IPAs targeted particular types of FDI in line with their national objectives. The main findings of the survey are summarized below:

1. The majority of IPAs expect FDI flows to increase only moderately in 2010. This picture changes for 2011, when the majority of IPAs expect a strong or moderate increase. IPAs based in emerging markets are more optimistic about FDI prospects than IPAs based in industrialized countries.

2. The four dimensions of sustainable FDI (economic development, environmental sustainability, social development, good governance) are unevenly addressed by IPA investment promotion strategies. The volume of FDI they attract matters most to IPAs, but that alone is not a consideration of "sustainable FDI." Among the dimensions of sustainable FDI, IPAs are especially concerned about the economic development dimension.

3. The economic development dimension, particularly employment creation, features prominently in investment promotion strategies. The environmental sustainability dimension follows, especially the sustainable management of natural resources. The social dimension is less important; however, labor standards are especially prominent in this category. Good governance is the least visible in IPA strategies.

4. The economic development and environmental sustainability dimensions of sustainable FDI have increased in prominence today compared with five years ago. Going forward, it is again these two dimensions that that are poised to acquire a bigger role in investment promotion strategies.

5. Most IPAs are interested in attracting FDI projects that adhere to a cost-benefit analysis of economic, environmental and social impacts, but are also interested in international labor norms and project monitoring. IPAs pay less attention to principles if these have been framed in the context of well-defined initiatives associated with particular organizations that are internationally recognized. Going forward, they see most of the existing norms that can be used in assessing the four dimensions of sustainable FDI becoming more important.

6. The majority of IPAs require social and environmental assessments for at least certain types of projects (infrastructure, natural resource), typically prior to entering into contracts, but a substantial number do not require such assessments.

7. For IPAs, the governance dimension translates in the transparency of contracts and the public disclosure of information. The majority of IPAs disclose a variety of information as required, although a significant number does not; that has not changed much compared with five years ago.

8. As regards investment incentives, IPAs favor those applied in support of specific economic development objectives, followed by environmental sustainability goals. An important share of IPAs also state explicitly that they do not offer specific incentives for any sustainable FDI dimension. Going forward a new approach is needed as regards the structure of incentives to cover all dimensions of sustainable FDI.

9. As regards their assessment of investment incentives, IPAs feel that those supporting economic development are the most successful, followed by those in support of environmental sustainability.

10. On the whole, the majority of IPAs report that foreign investors pay attention to sustainable FDI, though it is not entirely the case that they do so equally for each of the four dimensions.

11. Going forward, IPAs see themselves in a position to play a greater role in shaping policies of governments conducive to attracting sustainable FDI because their policy advocacy function is expected to become more important for the overwhelming majority.

12. To assist IPAs in attracting sustainable FDI, governments have an important role to play in several areas that include: training IPAs to increase awareness of sustainable FDI overall; establishing clear procedures for assessing and monitoring sustainable FDI projects; training IPAs in assessing projects from a sustainable FDI perspective; adjusting incentive structures to promote sustainable FDI, to the extent that these are needed; removing legislative obstacles that inhibit IPAs from tackling sustainable FDI issues; and rewarding IPAs for success in this area.

Report of the findings

Countries worldwide seek to attract foreign direct investment (FDI) in order to promote development. For that purpose, they have liberalized their regulatory frameworks for such investment; have established investment promotion agencies (IPAs) that actively seek to attract it; and more recently have sought increasingly to target particular types of FDI in line with national objectives. These are the three generations of FDI promotion.

In recent years, awareness has risen that not all FDI is equally desirable. In fact, the very act of "targeting" implies already a focus on certain types of "quality" investment, which at a minimum contributes to economic development. This report, based on the findings of the VCC-WAIPA Survey on Foreign Direct Investment and Sustainable Development goes further in examining the notion of sustainable FDI in the context of investment promotion – the fourth generation of FDI promotion.

The report is structured as follows: Section I discuses prospects for FDI from the perspective of IPAs; Section II discusses the extent to which, and how, IPA investment promotion plans seek to attract sustainable FDI and how IPAs assess its different dimensions; and Section III reports on the use of incentives in targeting sustainable FDI. This is followed by the conclusions. Annex 1 presents the responses to the survey questions.

I. Recent trends and prospects in global FDI: the perspective of IPAs

After a decline in global FDI inflows from a record of nearly US$2 trillion in 2007 to around US$1.7 trillion in 2008 and to US$1.2 trillion in 2009, flows are expected to stage only a modest rebound in 2010 (to a level up to US$1.4 trillion), but a stronger one in 2011[1] (box 1). The drop in FDI flows was caused by the deep recession and sluggish recovery in the industrialized world, the principal source and destination of FDI, as well as the time lag for foreign investors to respond to improved growth conditions. Emerging markets fared better than industrialized countries during the crisis, both on the inward and outward sides. For 2010, there are signs of a rebound in cross border merger and acquisition (M&A) deals -- typically by industrialized country firms, but increasingly by firms based in emerging markets – as financing constraints ease and global recovery sets in, pointing to the rebound in global FDI flows.

The VCC-WAIPA Survey on Foreign Direct Investment and Sustainable Development (box 2) found that the vast majority of IPAs share considerable optimism regarding the growth of FDI in 2011, with most respondents expecting a strong increase, or at least a moderate one (table 1). For 2010, the overall FDI picture is also positive, with most respondents expecting a moderate

[1] For detailed data and an analysis of recent trends in FDI flows, as well as prospects, see UNCTAD (2009). *World Investment Report 2009.* Geneva: UNCTAD, and UNCTAD (2010). *Global Investment Trends Monitor*, No 3 (April). See also P. Economou and K.P. Sauvant, "Recent trends and issues in foreign direct investment, 2008/2009" in Karl P. Sauvant, ed., *Yearbook on International Investment Law & Policy 2009-2010* (New York: Oxford University Press, forthcoming).

increase. The anticipated performance for both 2010 and 2011 supports the trends illustrated in box 1 based on various macroeconomic projections, or findings of other surveys.

Table 1. IPA views on FDI prospects for 2010 and 2011
(Percent)

Year	Strong increase	Moderate increase	No change	Moderate or strong decrease
2010	40	45	6	9
2011	62	32	2	4

Source: Annex 1, question 17.

Emerging market IPAs were particularly optimistic, with 67 percent expecting a strong increase and another 28 percent a moderate increase in FDI flows for 2011. While their optimism was more subdued for 2010, still a bit less than half of the IPAs surveyed expected a strong increase in FDI flows and another 36 percent a moderate increase. Comparatively, industrialized country IPAs were less optimistic for 2010, with 73 percent anticipating a moderate increase. Only 18 percent of industrialized country IPAs expected a strong increase in flows in 2010. That share changed significantly for 2011, when 45 percent of industrialized country IPAs – still well below the corresponding share of emerging market IPAs -- projected a strong increase in investment flows.

Box 1. FDI projections for 2010 and 2011

Only a few organizations have published estimates of FDI flows for 2010 and 2011, and in most cases only for select groups of countries (box table). The estimates suggest a modest increase for 2010, which is expected to rise further in 2011.

Box table. FDI projections for 2010 and 2011
(Billions of dollars)

Organization	Indicator	2010	2011
International Monetary Fund	FDI inflows a/	294.1	322.6
Institute of International Finance	FDI inflows b/	434.9	470.2
World Bank	FDI inflows a/	440	n/a
UNCTAD	FDI inflows (global)	Up to 1,400	n/a
FT Business	Greenfield FDI projects (global)	3-5% increase	n/a

Sources: VCC-WAIPA, based on projections/forecasts by: IMF (2010). *World Economic Outlook.* Washington DC: IMF; Institute of International Finance (2010). *Capital Flows to Emerging Market Economies.* Washington DC: IIF; MIGA (2009). *World Investment and Political Risk.* Washington DC: MIGA; UNCTAD (2010). *Global Investment Trends Monitor*, No 3, April; and fDi Intelligence, *Global Outlook Report 2010*. London: FT Business.
a/ Emerging markets.
b/ Into thirty large emerging markets.

Surveys of investors also paint a rosy scenario for FDI in the aftermath of the crisis, perhaps not surprising given the very sizable decline in FDI flows in 2009. In its latest *World Investment Prospects Survey*, c/ UNCTAD finds investors overall to be optimistic regarding the outlook for FDI, with a recovery expected as early as 2010. Investors become even more optimistic subsequently, with growth in FDI flows expected to accelerate from 2011 onwards. Specifically, more than half of the companies surveyed reported their intention to invest more abroad in 2011 compared with 2008 (the previous peak), as against 33 percent in 2010 and 22 percent 2009. AT Kearney d/ also reports a slow recovery in FDI projects for 2010, which is anticipated to pick up in 2011. Finally, the MIGA-EIU Survey on Political Risk, e/ which sought among other things to gauge corporate FDI intentions for developing countries for the period 2010-2012, indicated that, while the crisis had forced some investors to put on hold overseas expansion plans, and had even led to some cancellations, investors overall continued to view developing countries favorably. The findings of these surveys suggest that the decline in FDI, though sizeable, was a temporary phenomenon of a cyclical nature that is set to be reversed once economic conditions improve.

c/ UNCTAD (2009). *World Investment Prospects Survey, 2009-2011.* Geneva: UNCTAD.
d/ A T Kearney (2010). *Investing in the Rebound – The 2010 A.T. Kearney FDI Confidence Index.* Vienna, VA: AT Kearney.
e/ MIGA (2009). *World Investment and Political Risk.* Washington DC: MIGA.

Box 2. The VCC-WAIPA Survey on FDI and Sustainable Development

During April and May 2010, the Vale Columbia Center on Sustainable International Investment (VCC) and the World Association of Investment Promotion Agencies (WAIPA) undertook an online survey on Foreign Direct Investment and Sustainable Development. The survey sought to benchmark the position of investment promotion agencies (IPAs) vis-à-vis the different dimensions of sustainable FDI. More specifically, the survey sought to find out the extent to which IPAs are familiar overall with sustainable FDI issues and to what extent and in what ways they factor these into their investment promotion strategies and investment attraction tools. In addition, the survey sought to identify whether IPAs use investment incentives to attract sustainable investment. The objective here was to assess if IPAs are explicitly interested in attracting companies that undertake sustainable FDI and to find out how they go about achieving this. Finally, the survey sought to gather examples of individual experiences of IPAs with investors who undertook sustainable FDI.

The survey was aimed at the universe of WAIPA members that are IPAs (national or sub-national) and was sent to 215 IPAs (of which 51 were sub-national IPAs) located in 160 countries. The response rate was 23 percent (50 agencies). The response rate for national IPAs alone was 27 percent. Agencies based in emerging markets accounted for 78 percent of the respondents. Six provincial IPAs also completed the survey questionnaire. In two of these cases, the national IPAs did not complete the survey.

II. Investment promotion strategies and sustainable investment

Over time, investment promotion functions and strategies have evolved.[2] What has been termed "first generation" investment promotion involved the liberalization of FDI regimes and adoption of market-friendly policies. It was a passive stage in terms of seeking investment, but it was necessary for ensuring that host countries would be open to receive FDI. This was followed by the "second generation" of investment promotion. At that stage, many IPAs were established to facilitate foreign investors, and investment promotion became pro-active through the marketing of the host country as an investment location. "Third generation" investment promotion followed and it is this stage in which many IPAs are today. Its main characteristic is the targeting of specific industries (or even individual firms) that are deemed to be a good match for the host country.

Following this progression, one could think of a "fourth generation" of investment promotion, in which IPAs focus on attracting sustainable FDI. For the purpose of the survey, "sustainable FDI" was defined in terms of four dimensions: economic development (linkages, technology transfer, training, etc.); environmental sustainability (minimizing the adverse environmental impacts of investments, mobilizing environmental technologies for conservation, etc.); social development (labor and employment standards, community health, education, training, etc.); and good governance (fair and efficient negotiations, contracts, etc.). More generally, sustainable FDI is FDI that contributes to a host country's sustainable development. The volume of investment is not a factor, per se, of sustainable FDI. There are indications from the VCC-WAIPA Survey on FDI and Sustainable Development that IPAs are beginning to pursue fourth generation investment promotion strategies.

At the onset, it is important to keep in mind that IPAs are often created through special legislative acts (e.g. the Foreign Investment Promotion Act[3] in the case of the Republic of Korea). These specify explicitly their institutional structures and functions vis-à-vis FDI promotion and set the broad parameters for the types of activities they can engage in. As such, IPAs are executing agencies of their host country governments and do not possess sufficient autonomy to set policies and development goals themselves in terms of the type of FDI (or quantity of investment) they are setting out to attract. However, as their policy advocacy role becomes more important, IPAs will have a greater voice in setting the goals of investment promotion.

Typically, IPAs today are primarily (a) facilitators for foreign investors seeking to establish operations in the host country; they do so by being one-stop shops for foreign investors; (b) generators of new FDI projects by targeting specific foreign investors overall, or in specific priority sectors that the country seeks to promote; in this respect, an IPA's function is to apply

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[2] See detailed discussion in UNCTAD (2001). *World Investment Report 2001.* Geneva: UNCTAD.

[3] Foreign Investment Promotion Act, Republic of Korea, enacted on September 16, 1998 as Act No. 5559, United Nations Treaty Collection (available online: http://untreaty.un.org/cod/avl/pdf/ls/Shin_RelDocs.pdf).

the right incentives; and to a lesser extent (c) image builders or developers of country brands used to market the country in order to attract, encourage and promote FDI.[4]

In general, IPAs use their resources to facilitate and attract all types of investment, while paying special attention to their priority sectors, or other objectives, such as the development of economically disadvantaged regions within their countries or employment creation. For many IPAs, a successful investment promotion strategy, or marketing campaign, is judged on the basis of the volume of FDI that actually enters the country. However, volume alone has no relation to whether a FDI project fulfills the four dimensions of sustainability. For an investment to be considered sustainable it needs to perform well on all of the sustainable development dimensions. An investment promotion strategy that looks *only* at FDI volume will not necessarily be successful in attracting sustainable FDI (and be part of the fourth generation of investment promotion). Instead, IPAs should evaluate the sustainability of each FDI project along the four dimensions, namely, economic development, environmental sustainability, social development and good governance. Of course the contribution of each of these to sustainable FDI can be uneven and careful assessments of whether an investment is sustainable on balance are therefore necessary.

All of this is not to say that IPAs thus far have not been concerned at all with sustainable FDI. In fact, the opposite is the case (at least for some of the dimensions), as has been illustrated already by a report based on a survey of corporate IPA web sites (box 3). That report concluded that a significant proportion of IPAs (just under half of those surveyed) included in their web sites information about sustainable FDI considerations, such as environmental protection, social benefits, economic linkages, and capacity building, but without explicitly grouping these concepts together as "sustainable FDI." Just under half of the IPA web sites surveyed provided information on general or specific incentives aimed at promoting FDI with environmental, social or economic benefits. Furthermore, much of the literature has shown evidence of positive contributions of FDI to the economic development dimension,[5] as well as to the other dimensions of sustainable FDI.[6] But room for improvement remains, for example, through a better distribution of the benefits associated with FDI or improved governance.

For most IPAs today, the main goal remains the attraction of more FDI into the host country. The volume of FDI – quantity, rather than quality -- is an important focus, even when priority sectors or other objective have been established. However, when a foreign investment is made by a well-known company, which is susceptible to public scrutiny and aware of reputational risks, there is a greater likelihood that the company will go out of its way to ensure that it also brings in quality through positive contributions to the different dimensions of sustainable FDI. It should also be

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[4] See Millennium Cities Initiative and Vale Columbia Center on Sustainable International Investment, *Handbook on Investment Promotion in Medium-size, Low-budget Cities in Emerging Markets* (New York: MCI and VCC, 2009), available at www.vcc.columbia.edu

[5] For a review of that literature, see UNCTAD, *World Investment Report 1999.* Geneva: UNCTAD.

[6] See, for example, Theodore H. Moran (2010), "Enhancing the contribution of foreign direct investment to development: a new agenda for the corporate social responsibility community, international labor and civil society, aid donors, and multilateral financial institutions", World Trade Organization, *mimeo,* and Theodore H. Moran (forthcoming). *Foreign Direct Investment and Development: Launching a Second Generation of Policy Research, Avoiding the Mistakes of the First*. Washington, DC: Peterson Institute of International Economics.

noted that many countries have some legal restrictions on FDI that has harmful effects on such things as environmental preservation or public hygiene (e.g. Republic of Korea) and occupational safety (e.g. Mauritius), or mandate compliance of investments with national environmental protection acts or national spatial development acts (e.g. Bulgaria). These are safety nets that aim at ensuring that no harm is done, rather than aim at attracting sustainable FDI.

The next sections in this report present the findings of the VCC-WAIPA Survey on FDI and Sustainable Development. As mentioned earlier (box 2), some three-quarters of the respondents are based in emerging markets, so the responses reflect primarily their views. Moreover, an important caveat needs to be kept in mind: in general, the IPAs that responded to the survey are aware of the importance of all (or most) dimensions of sustainable FDI. This may have resulted in some degree of bias in favor of answers that indicate that they do pay attention to these dimensions, when, in reality, this may be more in principle and less in practice.

Box 3. What are IPAs doing to attract sustainable FDI?

A recent report a/ based on a survey of websites sought to examine what IPAs are doing to attract FDI that contributes to sustainable development. The survey was essentially an examination of English language websites of IPAs in 53 low and middle income countries located in Africa, South Asia, East Asia and the Pacific, and Latin America and the Caribbean, which took place at the end of 2006. The survey sought to identify information on (i) image building – efforts to present the country as concerned about specific dimensions of sustainable development, such as environmental protection; and (ii) investment generation, through different sets of incentives, such as those offered to investors to promote FDI with economic, environmental and social benefits; incentives targeting specific types of investors who are committed to corporate social responsibility and sustainable development; and incentives targeting investment into sustainable activities. The survey sought to identify how IPAs communicate information on these two sets of information to investors through their websites. The assumption was that the more important sustainable development issues are to an IPA, the more likely it would be for information and policies on these issues to be explicitly portrayed on their websites.

The survey found that IPA websites focus the most on economic benefits, such as promoting linkages between foreign investors and domestic enterprises. To the extent that it could be discerned from their websites, IPAs also adopted a variety of strategies for targeting sustainable FDI. As regards image building and country branding, environmental protection, strict labor standards, and sustainable forest management were some of the main types of information found on IPA web sites. Such information is important when seeking to establish an investment brand based on all-inclusive sustainable development, and not on country image alone, for example, based on nature, biodiversity, wildlife, and a pristine environment. While marketing messages may seek to advertise and brand a country's image, investors are more likely to pay closer attention to sectors that have been chosen as priority to receive support, especially in the form of incentives or other benefits, when choosing among countries in their short lists.

(Box 3 continued)

The survey found that environmental aspects, such as policies, management and legislation, were mentioned in ten IPA websites. Social aspects were less frequently mentioned. As regards the use of incentives, environmental protection was one eligibility criterion for qualifying for a general incentives package in some cases, and the same applied to social benefits for select IPAs. Sectors for which incentives were offered by select IPAs included clean technologies and production, renewable energies and waste management. Only a small proportion of IPAs offered information on sectors, or targeted explicitly those investors who were committed to sustainable development. However, a high proportion of IPAs presented information on their websites that covered many aspects of sustainable development, but without explicitly mentioning this term.

a/ Maryanne Grieg-Gran and Johanna Edlund (2008). "Attracting FDI that contributes to sustainable development: a review of current IPA practice", in IIED and WAIPA, eds., *Responsible Enterprise, Foreign Direct Investment and Investment Promotion*. London and Geneva: IIED and WAIPA.

(a) Does sustainable investment feature in investment promotion strategies?

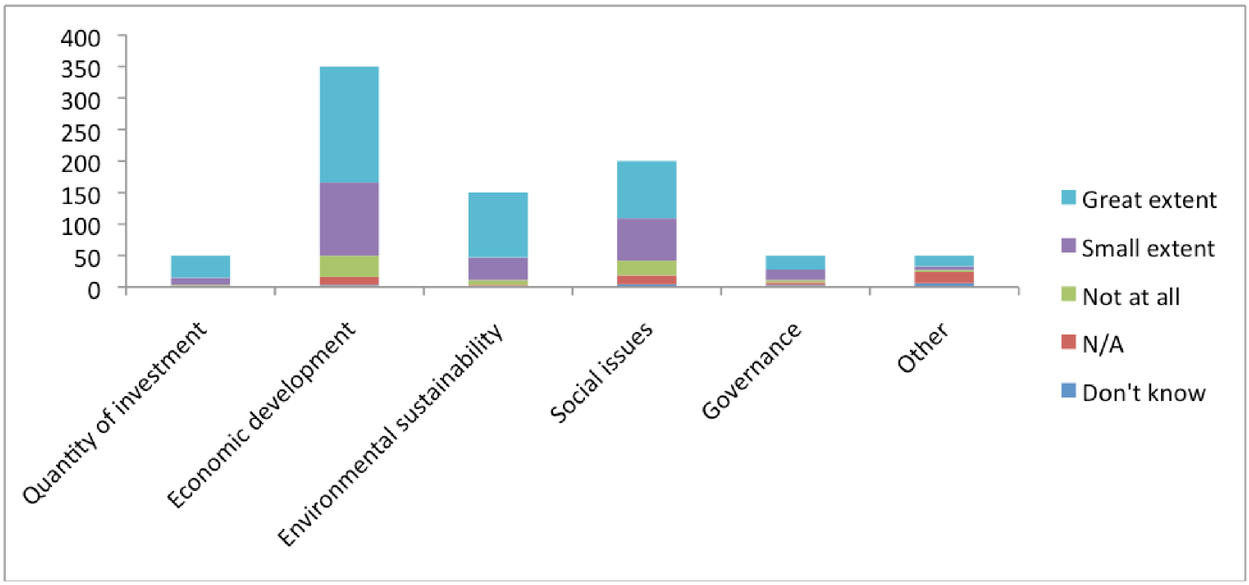
The emphasis that investment promotion strategies place on the volume of investment was illustrated by the responses to the VCC-WAIPA survey: some 70 percent of respondents considered investment volume to a great extent in their investment promotion strategies (though employment creation was the single most important consideration). When grouping the responses to the individual categories into the four dimensions of sustainable FDI (economic development, environmental sustainability, social development,[7] and good governance), the *economic development dimension* clearly ranked in top place (figure 1). One reason for which IPAs may be keen to attract as much FDI as they can, is because host countries do recognize the potential benefits of FDI in terms of its contribution to economic development. Not surprisingly, alleviating unemployment, linkages with the domestic economy, acquiring new technologies, and R&D centers were among the most prominent economic development variables. Offering training and boosting exports were also important, but to a lesser extent.

In general, variables that reflected the *environmental sustainability, social development and good governance* dimensions of sustainable FDI did not fare as well as those representing economic development. Environmental sustainability ranked next in importance, with a significant share of respondents considering it to a great extent in their investment promotion strategies. Among the specific variables in this dimension, the sustainable management of natural resources ranked in first place (this is likely of most relevance to resource-endowed countries). Pollution prevention

[7] The social development dimension includes corporate social responsibility, a broader concept that also includes elements that can be included into the other dimensions of sustainable FDI (e.g. environmental sustainability). For a detailed discussion, see UNCTAD (1999). *World Investment Report 1999*. Geneva: UNCTAD.

and abatement mechanisms were also important considerations. In the social dimension, labor standards ranked the highest. The least important social development issue was land acquisition and the involuntary resettlement of people. The governance dimension, essentially transparency variables, was the least important consideration in investment promotion strategies.

Figure 1. To what extent do you consider the following sustainability dimensions in your investment promotion strategy?
(Number of responses)

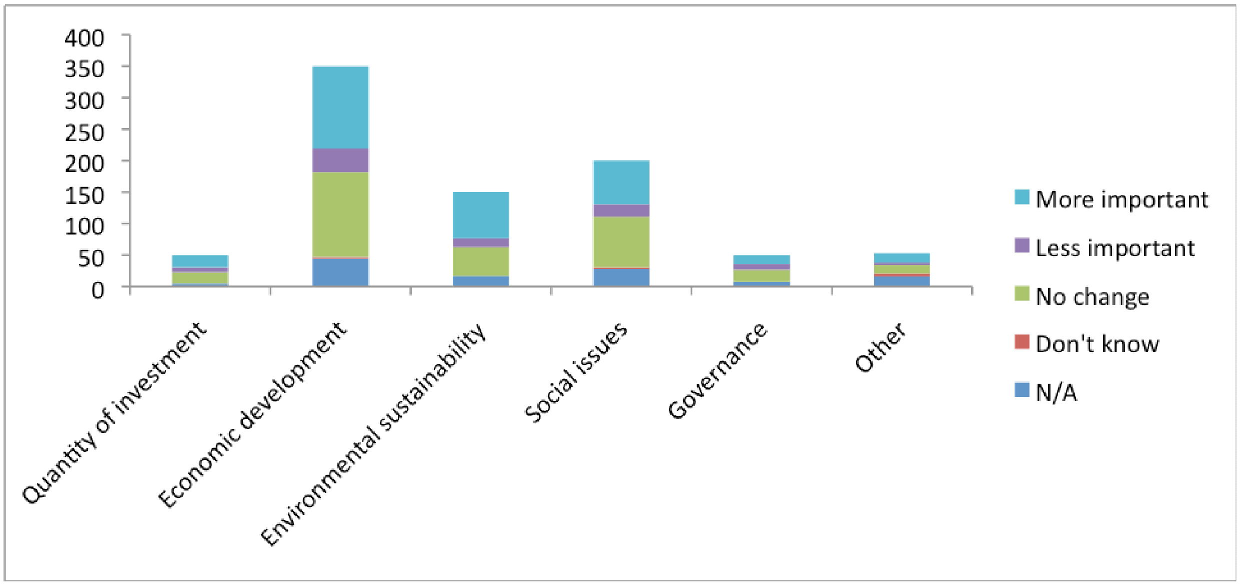


Source: Annex 1, question 2.

While the environmental, social and governance dimensions of sustainable FDI are not as much at the forefront of investment promotion strategies today as economic development, encouragingly this picture is far better than five years ago. All of the variables covering the *environmental sustainability* dimension have become more important in investment promotion strategies today compared with five years ago (figure 2). The environmental impact of an investment was the consideration that had increased the most in significance among all dimensions of sustainable FDI (on par with transfer of technology). As regards each of the *social benefit* (with the exception of corporate social responsibility, which has become more important) and *governance* categories, the majority of respondents did not indicate any change in their inclusion in investment promotion strategies today compared with five years ago.

Overall, a nearly equal share of respondents found the *economic development* dimension to have become important as those that found it unchanged compared with five years ago. Within the economic development dimension, employment creation, linkages with domestic companies and technology transfer had become more important today than five years ago. As regards the volume of investment, an almost equal share of respondents found it to have become more important as unchanged.

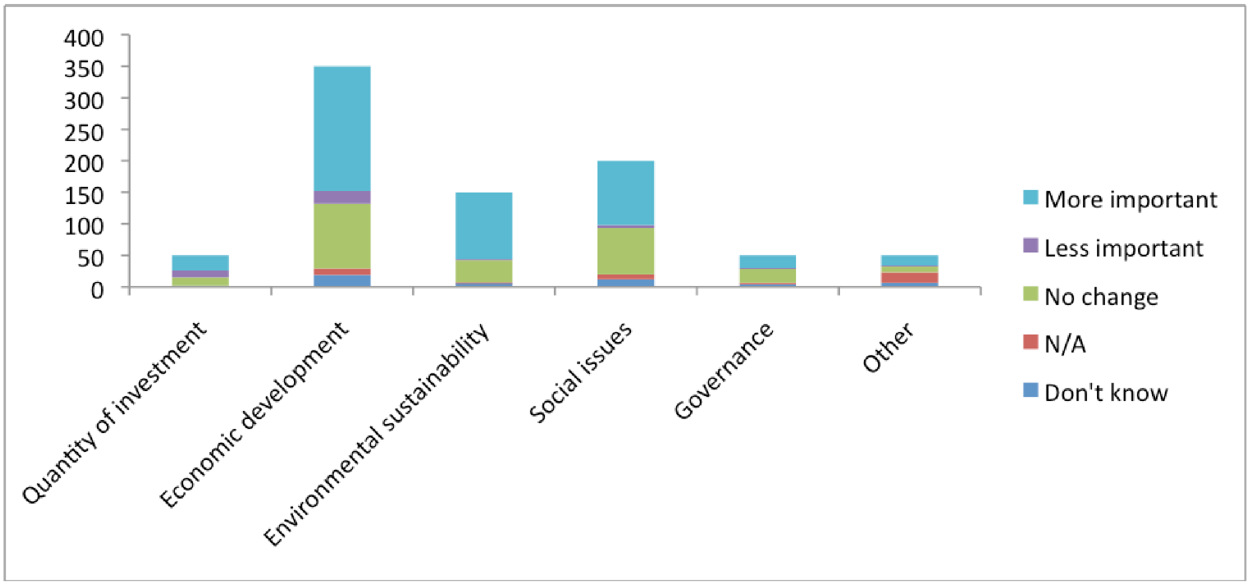
Figure 2. How have these sustainability considerations changed compared to five years ago?
(Number of responses)



Source: Annex 1, question 3.

Going forward IPAs expect the picture to change considerably (figure 3). With the exception of good governance, the three other dimensions of sustainable FDI are expected to become more important. Nevertheless, in relative terms, it is the *economic development* and *environmental sustainability* dimensions that are expected to become even more significant considerations in investment promotion strategies. Environmental impacts of investment and pollution prevention and abatement mechanisms were the environmental sustainability variables expected to increase the most in prominence. Technology transfer/R&D and employment creation were the economic development considerations exhibiting the biggest increases, followed by linkages with domestic firms and environmental impacts of investment. The *social* dimension is also expected to become more prominent, but less so. For the *governance* dimension, a smaller share of respondents felt that it will become more important, while the majority believed there will be no change.

Figure 3. How do you expect the sustainability considerations to change over the next five years?
(Number of responses)

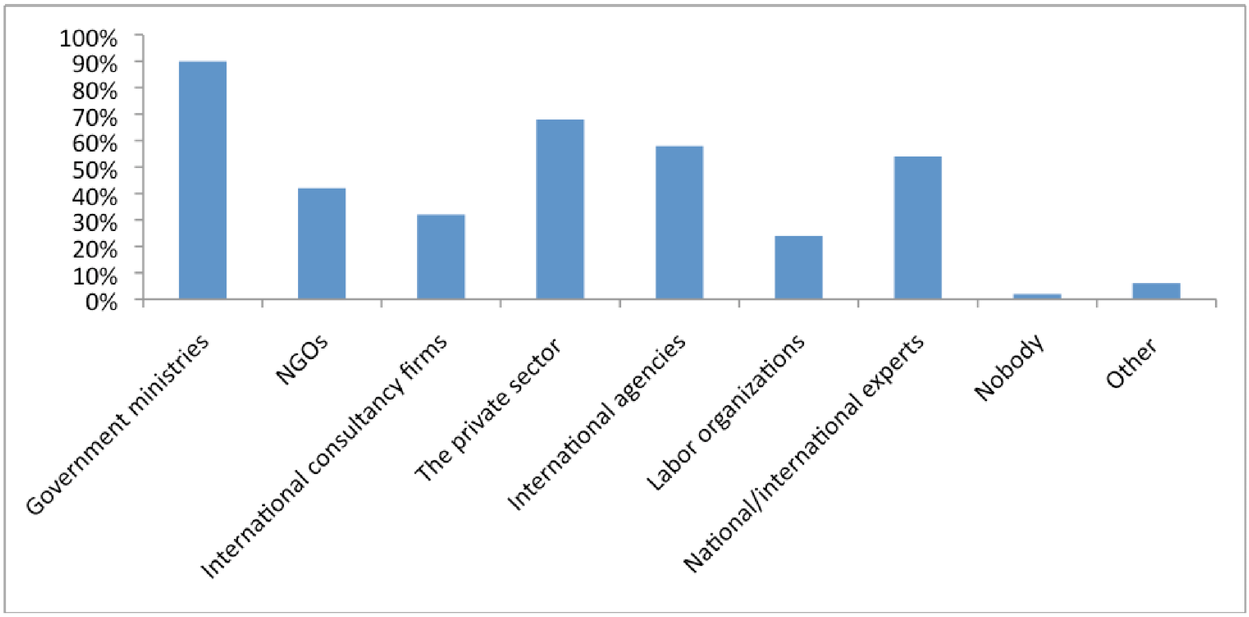


Source: Annex 1, question 4.

(b) How do IPAs incorporate sustainable investment issues into their strategies?

The VCC-WAIPA survey sought to identify how IPAs set about incorporating the different sustainable FDI dimensions into their investment promotion strategies. First and foremost, IPAs confer with government ministries, or other government entities (figure 4), as they do for many other issues they might face. This finding is not surprising given that the overwhelming majority of IPAs report to national ministries or other departments (see discussion below). Indirectly, therefore, the answers to this question also inform about the importance that national governments attribute to sustainable FDI. If governments pay special attention to sustainable FDI, it is likely that these will also be reflected in investment promotion strategies of IPAs.

Figure 4. When formulating your investment promotion strategy, who do you interact with primarily regarding sustainable development issues?
(Percent)

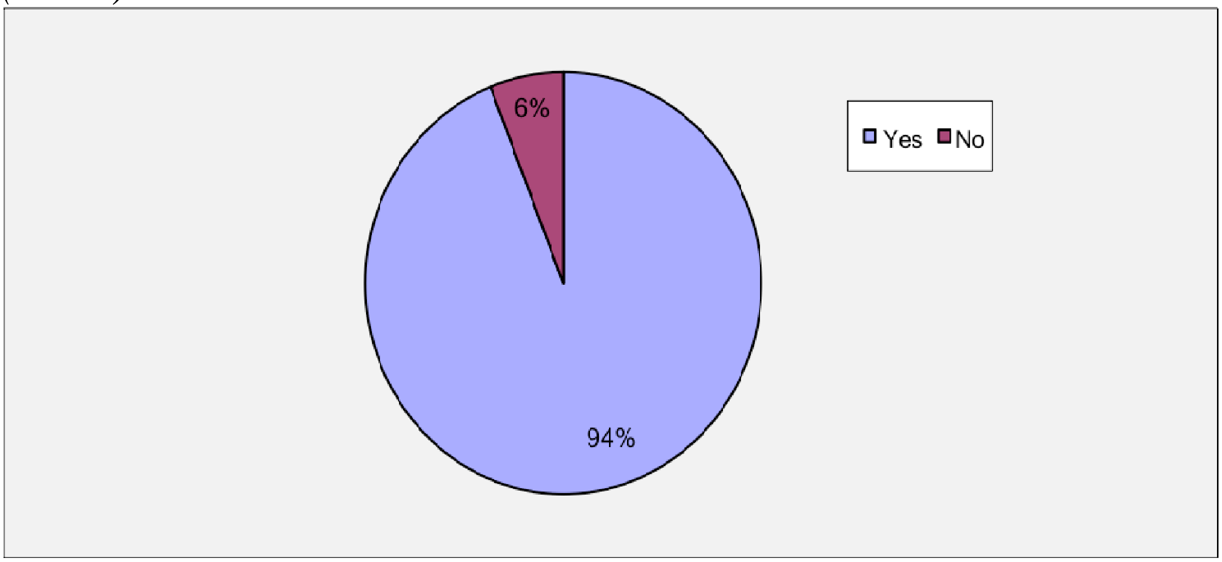


Source: Annex 1, question 5.

IPAs also consult with the domestic private sector (e.g. business associations) and may also seek advice from international or national experts and multilateral organizations (to which they may turn to receive technical assistance or training). To a much lesser extent, IPAs consult with labor organizations (e.g. labor unions). All in all, IPAs appear to be making an effort to receive a broad range of opinions regarding attracting sustainable FDI; likely, the most weight is given to those of the government.

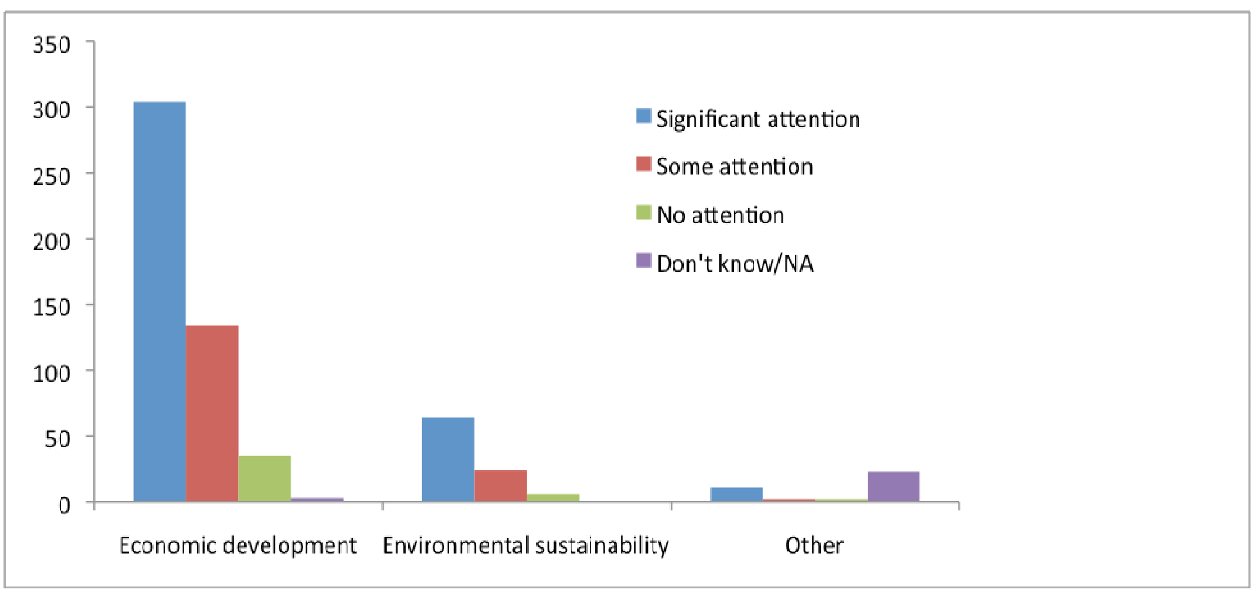
Typically, national governments and IPAs set up *priority sectors* for investment promotion that are in line with the countries' economic development goals. Virtually all IPAs that responded to the survey have priority sectors into which they seek to attract investment (figure 5). For a large majority, the choice of priority sector is at least partly informed by one or more categories of the economic development dimension of sustainable FDI (figure 6) and underscores the importance placed on it by governments.

Figure 5. Do you have priority areas/sectors for attracting FDI?
(Percent)



Source: Annex 1, figure 6.

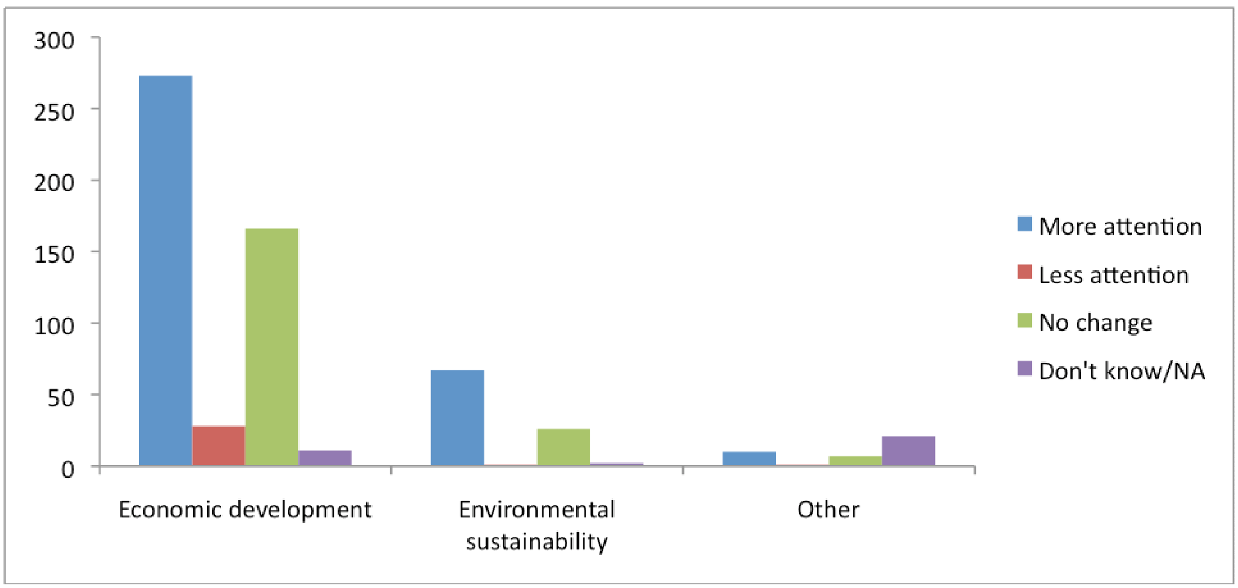
Figure 6. When selecting priority areas/sectors, how much attention do you pay to the dimensions of sustainable FDI?
(Number of responses)



Source: Annex 1, question 7.

Economic development factors have been at the forefront in choosing priority sectors, and the expectation is that this will continue in the future (figure 7), particularly as regards employment creation, the transfer of technology and skills, building new industry clusters, and channeling investment into economically disadvantaged regions of the country. The environmental sustainability dimension also received significant attention, though considerably less than the economic development dimension. Going forward, all environmental sustainability factors are poised to become more important, in particular sectors associated with "green" technologies.

Figure 7. Over the next five years, in selecting priority sectors for FDI, how do you think your answers might change?
(Number of responses)

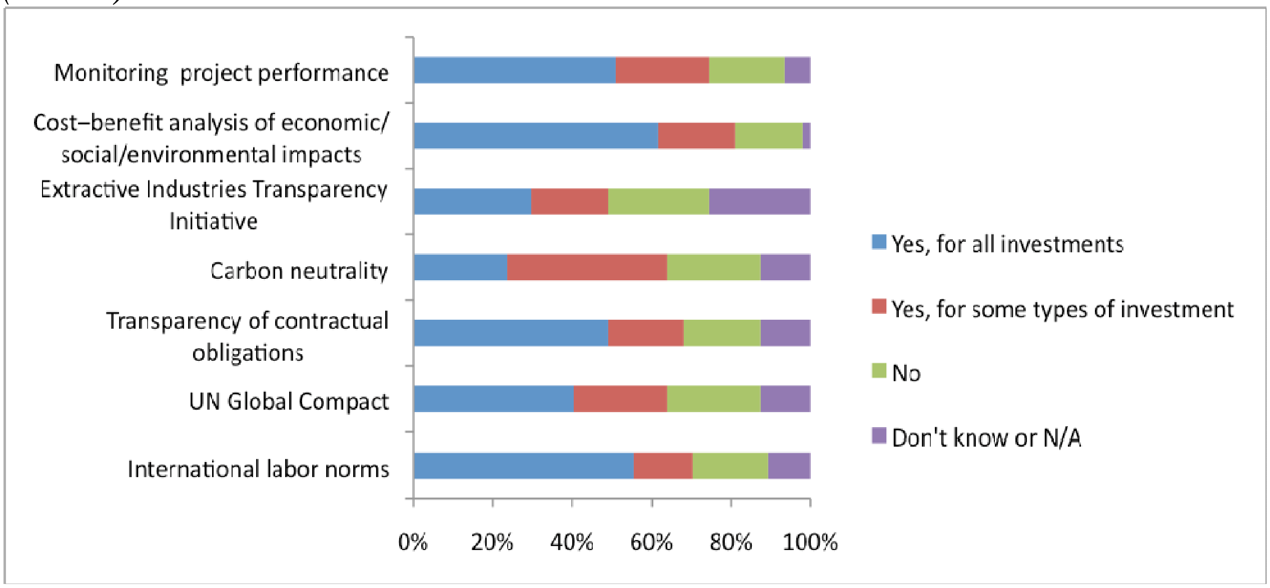


Source: Annex 1, question 8.

(c) How do IPAs assess sustainable FDI projects?

When trying to zero in on how IPAs assess each of the various *s*ustainable FDI dimensions of projects, a mixed picture emerges (figure 8). On the one hand, the majority of IPAs claimed that they sought projects that adhered to cost-benefit analyses based on economic development, environmental and social factors (at least for certain projects in specific sectors or of specific size). They also paid attention to monitoring project performance. Cost-benefit analysis and project monitoring seemed to resonate well with the IPAs, perhaps because they are more familiar with these concepts. The environmental sustainability dimension (e.g. carbon neutrality) was also important, but only for select projects, as might be expected. Governance variables (e.g. contract transparency) scored high for all or some types of investment. Adhering to international labor standards for all or some types of investments was also among the top responses. In all cases, however, there was a rather high share of respondents that answered negatively or not at all.

Figure 8. Does your agency seek especially investments that adhere to any of the following standards/norms?
(Percent)



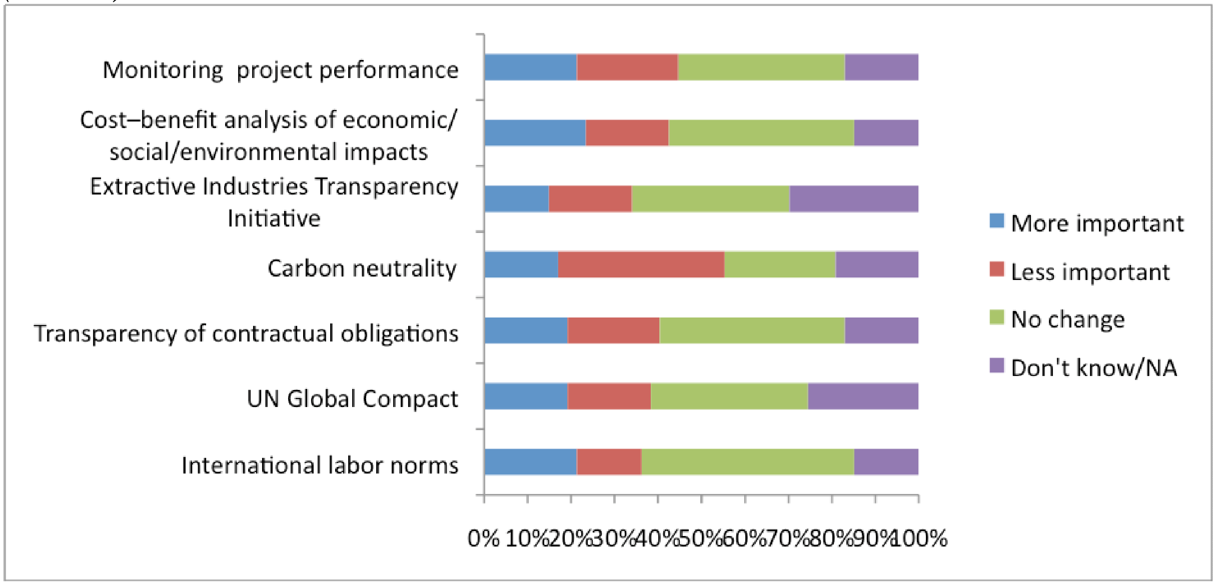
Source: Annex 1, question 9.

On the other hand, when it comes to specific norms or standards, such as those set in the United Nations Global Compact or in the Extractive Industries Transparency Initiative, respondents -- while there was a significant share of positive answers -- were less likely to seek investments that adhered to them. While a share of respondents sought projects that adhered to these principles, a nearly equal share did not, or did not answer the question. The fact that a relatively large share of IPAs chose not to respond to this question also suggests a possible lack of familiarity with such well-defined principles and standards. All in all, it seems that, while IPAs in general may support criteria to assess sustainable FDI dimensions, they do so only in a general manner, and they are unlikely to seek projects that follow well specified, internationally set principles or standards, either because they are deemed less important or because the IPAs are not familiar with them.

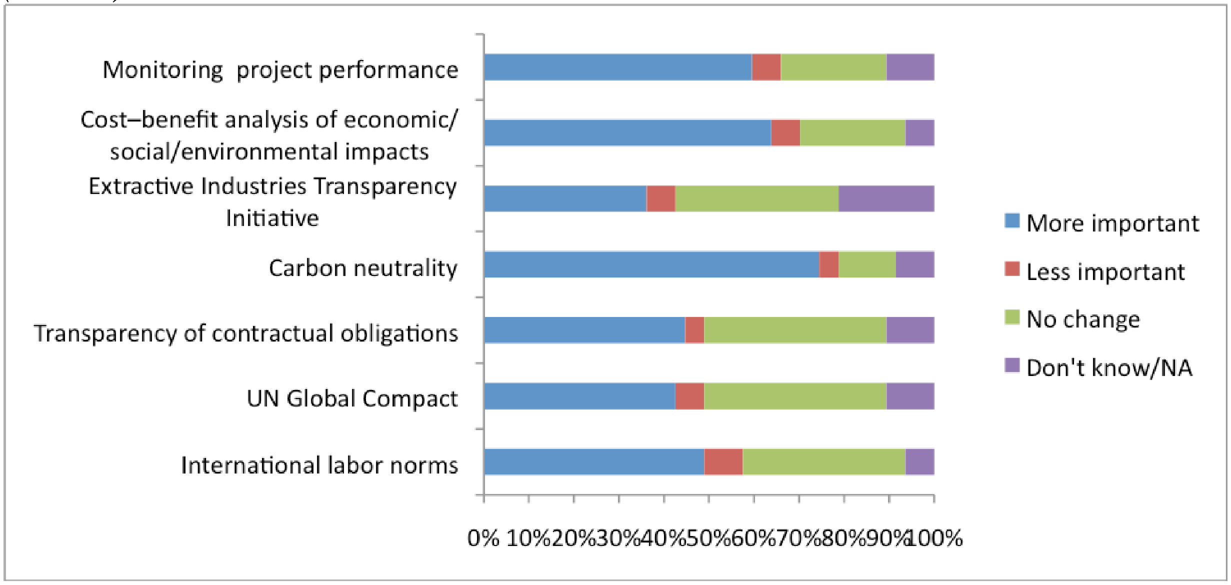
This mixed picture of today seems to have *not* changed significantly compared with five years ago, with the exception of carbon neutrality. A significant proportion of respondents said that no change had occurred (and a significant share also responded "don't know/not applicable") (figure 9). In the case of carbon neutrality, the majority of respondents claimed that it had become less important today, and it is unclear why this should be the case.

However, going forward, virtually all standards and norms reflecting the different dimensions of sustainable FDI are expected to become more important (figure 9). Carbon neutrality is in top place in terms of responses, while cost-benefit analyses and project monitoring also rank high. For the governance variables, such as the Extractive Industries Transparency Initiative and the transparency of contracts, the picture is more mixed: while these are regarded as more important going forward, for a nearly equal share of respondents they expected no change. On the whole, it appears that IPAs will continue to put the emphasis on a case-by-case approach in terms of cost-benefit analysis of each project and on monitoring project performance. As they become more familiar with internationally set norms and standards, the likelihood of seeking investment projects that adhere to these increases.

Figure 9. Compared with five years ago, do you find the following standards/norms more or less important?
(Percent)



Do you expect to find the following standards/norms more or less important five years from now?
(Percent)

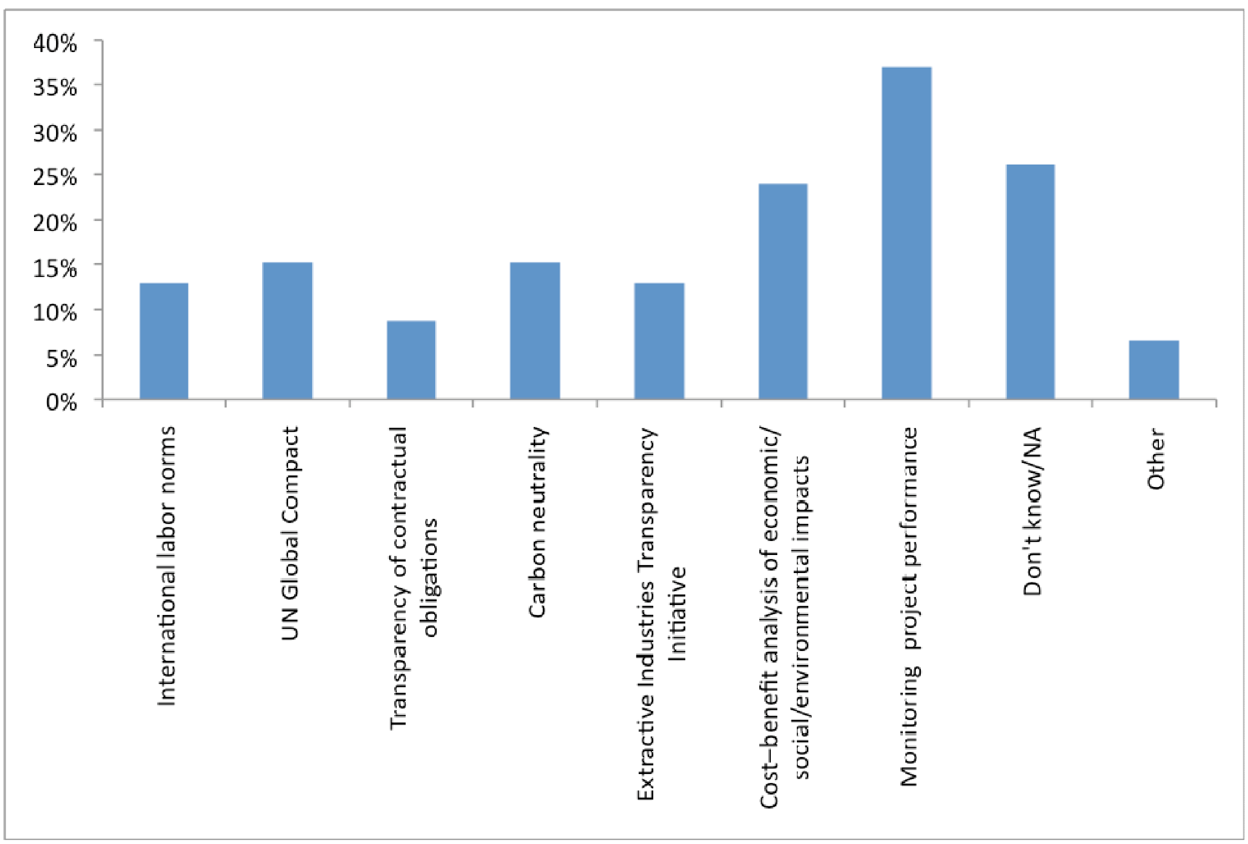


Source: Annex 1, question 10.

Relating the questions on attracting projects that fit sustainable FDI criteria with the earlier set of questions that addressed the inclusion of sustainable FDI dimensions in IPA strategies yields some interesting findings. In evaluating sustainable FDI projects, IPAs feel more comfortable doing so in ways that leave some room to maneuver (e.g. cost-benefit analysis), rather than having to make a clear-cut decision of whether or not a project adheres to an international norm or standard. One of the many possible reasons for this is that IPAs may not be familiar with internationally set norms and standards, especially as regards their application at the project level, or that they may not feel equipped to make such assessments.

When faced with the choice of "sacrificing" a particular individual norm or standard in exchange for additional investment, a significant share of IPAs (about a quarter) did not respond, while the majority claimed they would do away with monitoring project performance, followed by cost-benefit analyses of economic, environmental and social impacts, and carbon neutrality and the UN Global Compact tied in third place (figure 10). The rest of the norms or standards were more or less similarly ranked in terms of readiness to drop.

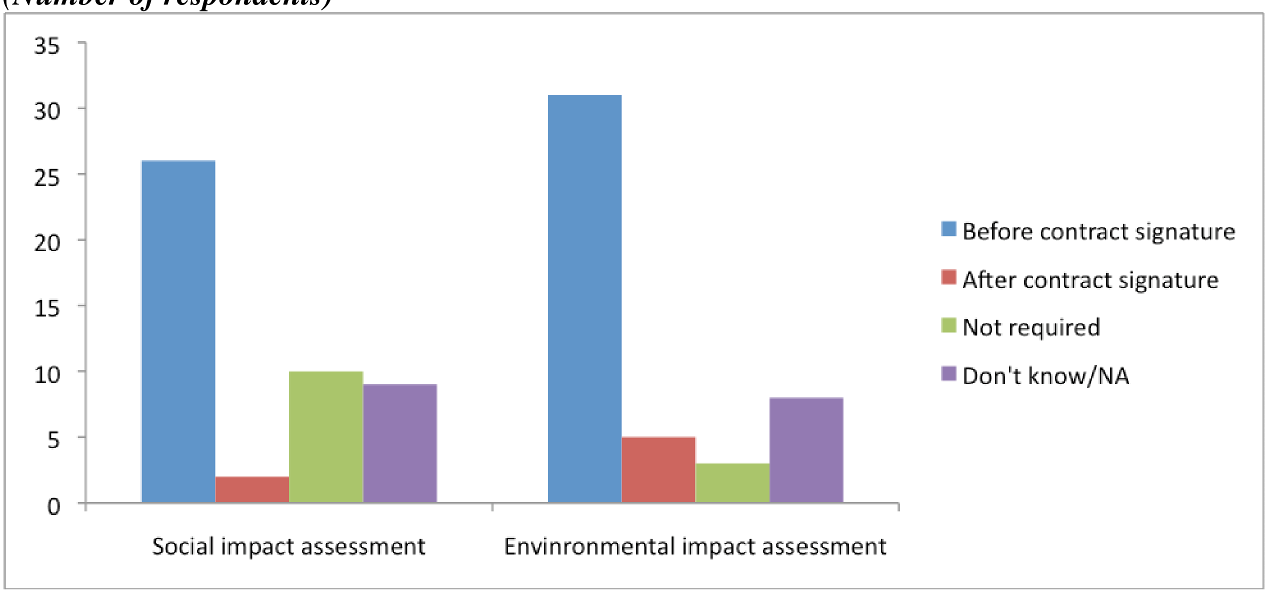
Figure 10. Which of the standards/norms would your agency be willing to forego in order to attract more investment or maintain current levels?
(Percent)



Source: Annex 1, question 11.

The majority of IPAs required both social and environmental impact assessments for FDI projects in all or in selected industries. More than half of the respondents required *social impact assessments* (in all or in select sectors), mostly before the signing of a contract, but for just over a fifth, such an assessment was not required at all (and a minority did not know or thought this question not to be applicable to its circumstances) (figure 11). Two thirds of the respondents required *environmental impact assessments*, at least for some projects, mostly before the signing of a contract, while around 6 percent did not have this as a requirement (and a minority did not answer the question or thought it not to be applicable). This is a rather positive finding that suggests that IPAs do perform some form of assessment of environmental and social effects, if not for all industries, at least for presumably those that are more likely to experience potentially bigger impacts. Assessments at the project level appear to be a preferred way for IPAs to address the other dimensions of sustainable FDI beyond the economic development dimension. From the perspective of IPAs, the advantages of these assessments might be that they allow them to weigh the different dimensions of sustainable FDI, e.g., potentially negative environmental or social impacts against potentially positive economic contributions.

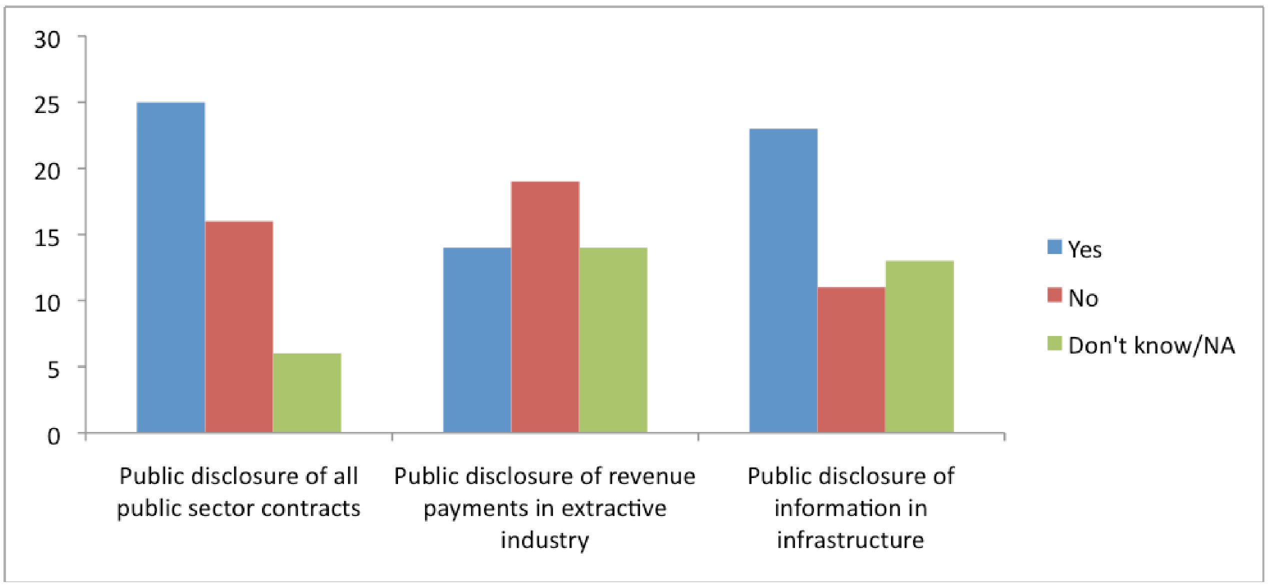
Figure 11. At which stage in the investment approval process are investors (in all or in select sectors) required to provide assessments?
(Number of respondents)



Source: Annex 1, question 12.

At the individual project level, the *good governance* dimension of sustainable FDI is more relevant than it is for investment promotion strategies, particularly as regards the public disclosure of various types of information relating to sustainable FDI projects (figure 12). Examples of these included disclosure of information on public sector contracts with foreign investors, royalties paid by investors in the extractive industries, as well as information relating to government support and investor obligations for infrastructure projects. As might be expected, the picture was mixed depending on the type of information to be disclosed. Public sector contract awards to foreign investors were disclosed by more than half of the respondents, while also more than half claimed to do the same for obligations related to infrastructure projects (with a significant share claiming that they did not disclose such information and the remaining being unable to answer this question). In the case of royalty payments, the majority of respondents claimed not to be requiring the disclosure of such information (and a significant share was unable to answer the question or thought it not applicable).

Figure 12. Does your agency (or relevant ministries) currently require any of the following disclosures during the investment approval process?
(Number of respondents)

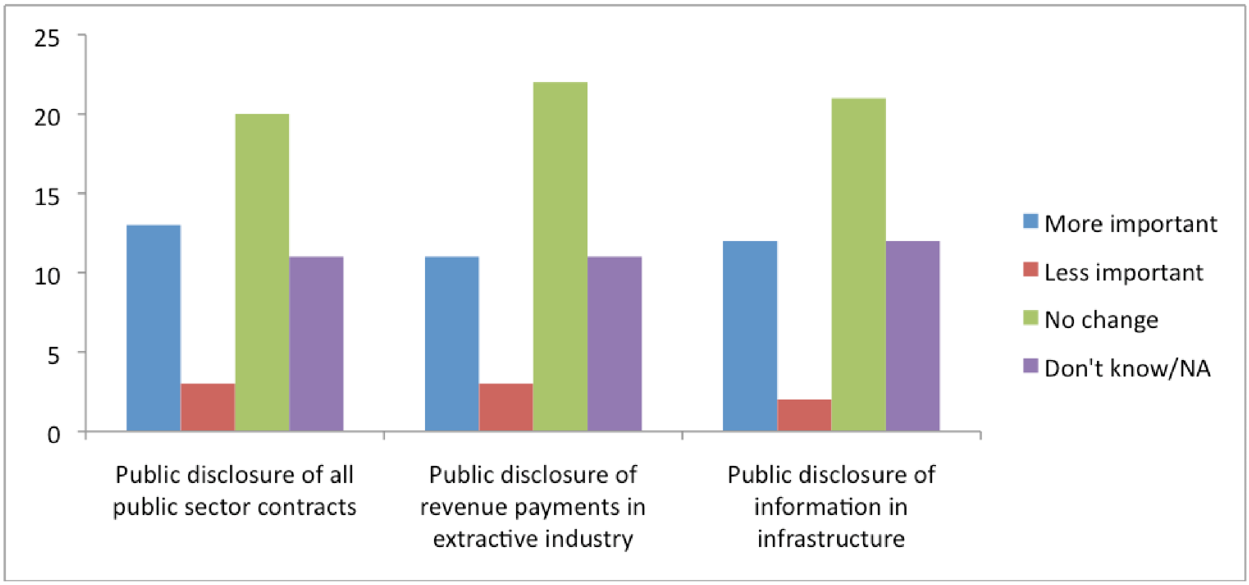


Source: Annex 1, question 13.

There is no doubt that the good governance dimension on the whole appears to be more neglected by IPAs than the other dimensions of sustainable FDI, perhaps in large part because issues such as transparency and disclosure of information largely fall outside their mandates as they relate to investment promotion *per se*. To the extent these are required by national laws, IPAs will certainly oblige, but if that is not the case they will not on their own accord pursue the path of disclosure and transparency.

The mixed picture of today regarding disclosure of information does *not* seem to have changed compared with five years ago (figure 13). For all variables in the governance dimension, the majority of respondents claimed that there has been no significant change in public disclosure. In all cases a minority share of respondents indicated that the public disclosure of information had become more important. As in the previous question, a minority was not able to answer the question.

Figure 13. Have any of the disclosure items become more or less important now compared with five years ago?
(Number of respondents)

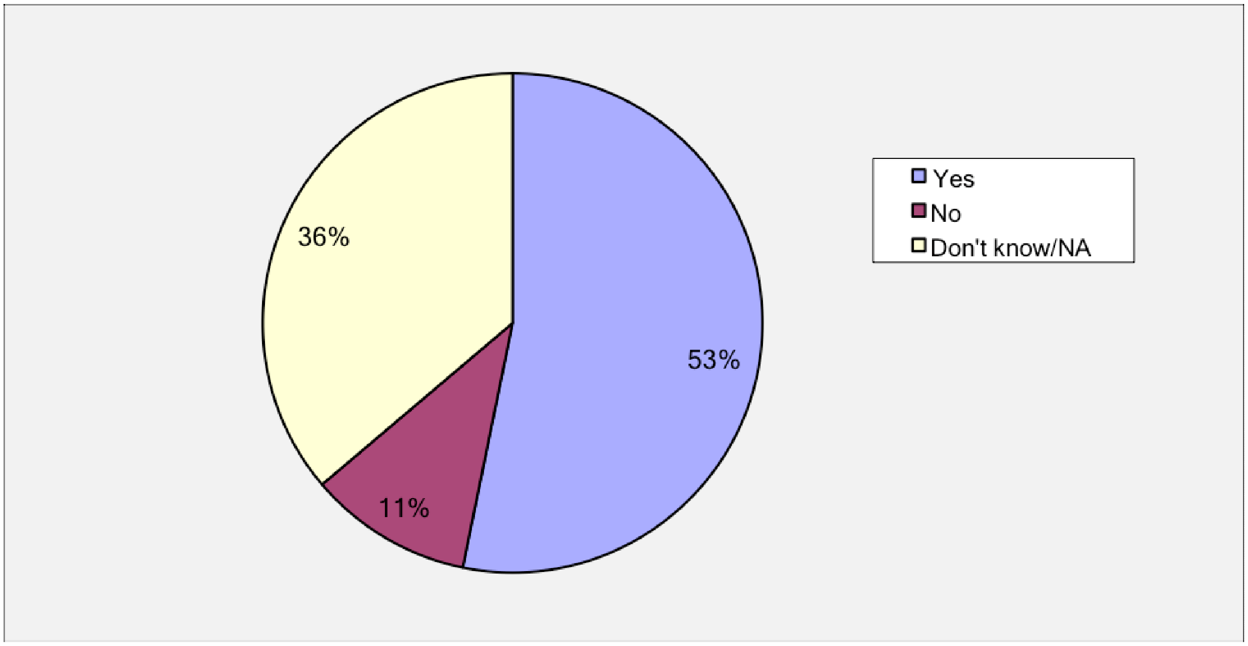


Source: Annex 1, question 14.

The majority of the IPAs felt that there have been foreign investors who stood out as having established sustainable FDI projects in their countries (figure 14), but almost one third was not able to answer this question.

Some IPAs offered anecdotal evidence regarding sustainable FDI by companies in different sectors (from electronics to mining), mostly examples concerning the economic development or environmental sustainability dimensions. Examples of sustainable FDI projects included multinational enterprises that had made large investments, or had created considerable employment, but also firms that had engaged in "green" projects or philanthropy. While some of these examples illustrate positive contributions to one or more dimensions of sustainable FDI, a holistic assessment across all four dimensions is needed to characterize an investment as sustainable. Furthermore, the size of an investment project alone (as mentioned earlier) does not even enter the definition of sustainable FDI and hence no such project can be characterized as sustainable on that basis alone. The same applies to philanthropic acts of foreign investors.

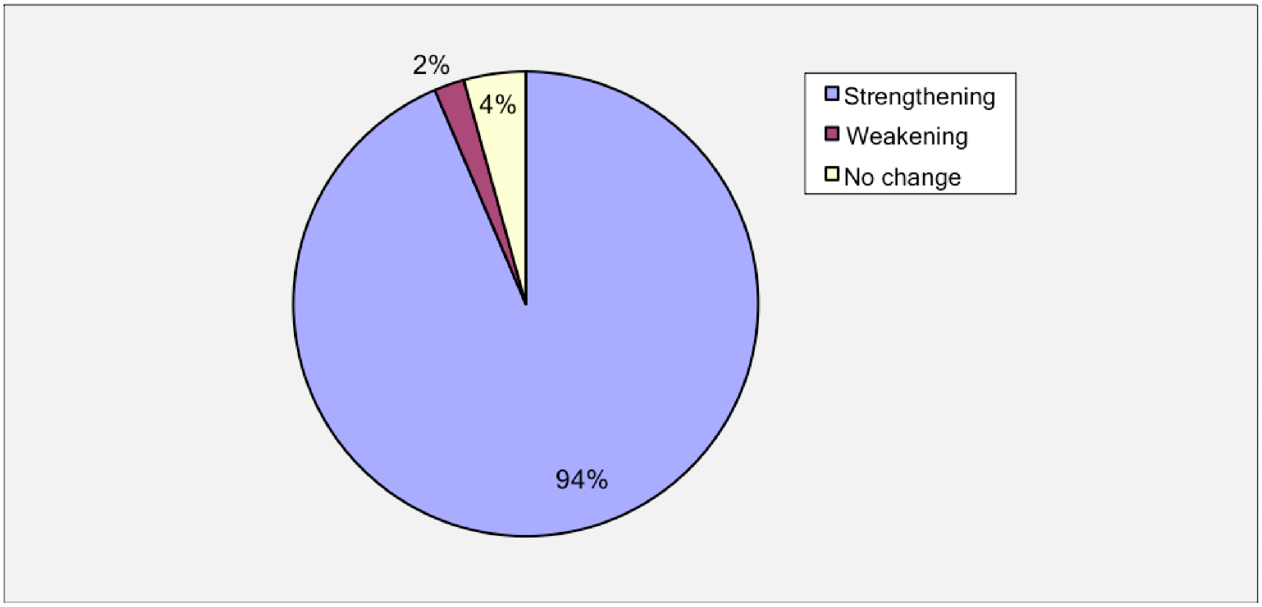
Figure 14. Do any companies that have invested in your country stand out in terms of contributing to sustainable development?
(Percent)



Source: Annex 1, question 15.

With virtually no exception, IPAs believed that their policy advocacy role would become more important going forward (figure 15). This is important because, even though IPAs at present might feel constrained by what is stipulated in investment promotion acts, government policies or guidance by ministries, going forward they will have a bigger say in formulating the national FDI policy agenda. Clearly, IPAs see themselves as playing a more active role in this respect.

Figure 15. In what way do you see your policy advocacy role changing over the next five years?
(Percent)

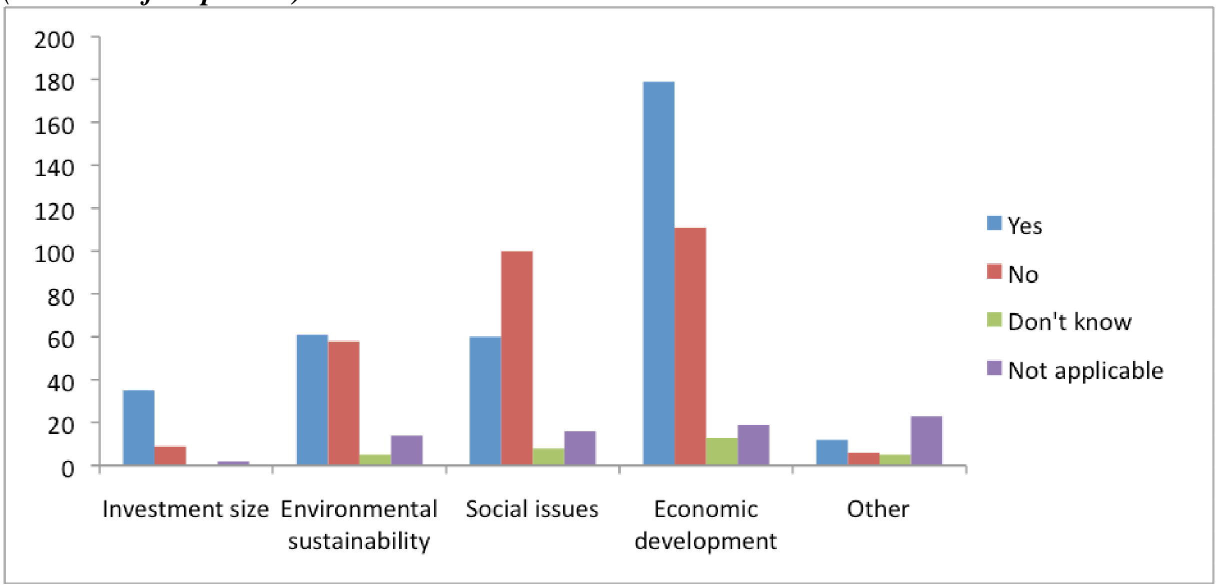


Source: Annex 1, question 16.

III. The role of incentives in promoting sustainable investment

This section of the VCC-WAIPA survey sought to investigate in what ways, and to what extent, the existing structure of incentives for investment supports the four dimensions of sustainable FDI. For most IPAs, the structure of investment incentives mirrored the relative importance they attributed to each of these dimensions in their investment promotion strategies (figure 16). Unsurprisingly, most IPAs offered incentives based on the economic development dimension of sustainable FDI. Investments that lead to the transfer of technology and the establishment of R&D facilities, help create employment or help to locate production facilities in economically disadvantaged regions of the country were the most frequently cited. Key economic development benefits associated with FDI were clearly viewed as worthy of support through incentives. Given budget constraints, it is not surprising that IPAs would favor economic considerations, with which they are more familiar, over the environmental, social or governance dimensions of sustainable FDI.

Figure 16. Do you offer incentives to foreign investors for projects based on the amount of FDI or the dimensions of sustainable FDI?
(Number of responses)



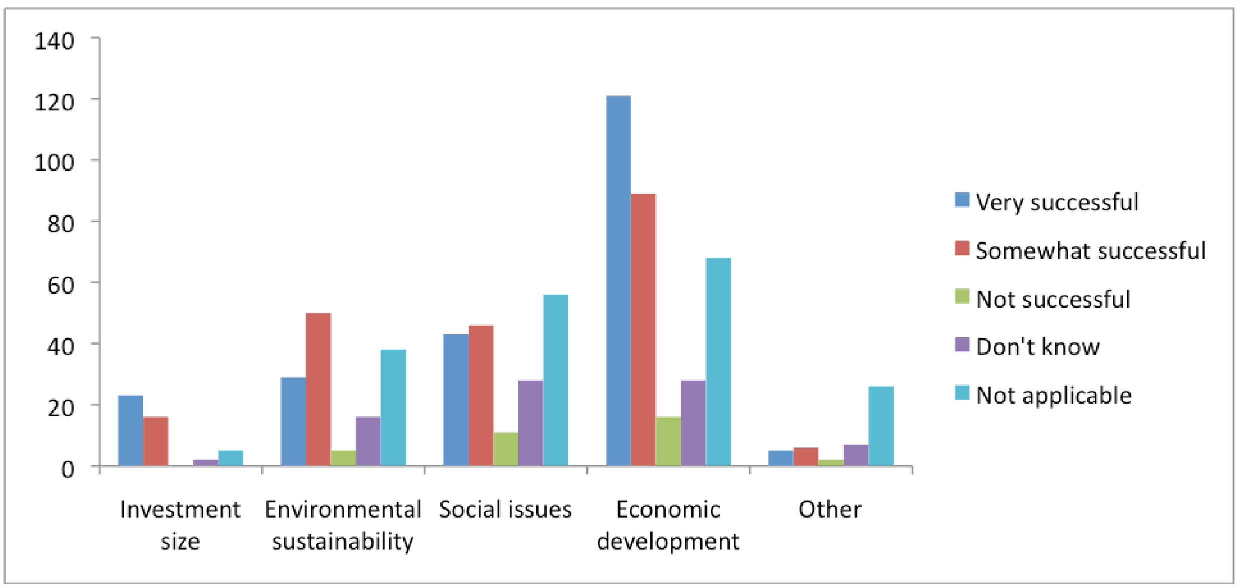
Source: Annex 1, question 18.

The question regarding incentives and the size of investment was posed slightly differently: it was in relation to offering incentives for large investment projects (e.g. in infrastructure), or projects by small and medium-sized investors. The majority of respondents did not offer incentives based on size (at least not on size alone). For the variables reflecting the four dimensions of sustainable FDI, a mixed picture emerged. Clearly, the economic development dimension received the most responses (over half of respondents replied positively). For the environmental sustainability dimension, the picture was mixed. A nearly equal share of the respondents specifically stated that they offer incentives for investments with an environmental sustainability dimension as those that said they did not. Just over a third of the respondents stated that they did not offer incentives for projects with social benefits, but just under one fifth said they did. So, apart from the economic development dimension of sustainable FDI, the other dimensions presented a more mixed picture.

Although the above responses seem somewhat negative as regards the non-economic development dimensions, it should be kept in mind that, given budget constraints, when faced with choices of which types of projects to promote, IPAs will likely opt for those that have potential economic development benefits. That is not to say that these projects have solely positive economic effects; it is quite possible that they also carry positive environmental or social benefits, hence contributing to these two other dimensions of sustainable FDI. However, IPAs at present are less likely to use incentives to attract projects on the basis environmental sustainability and social issues alone.

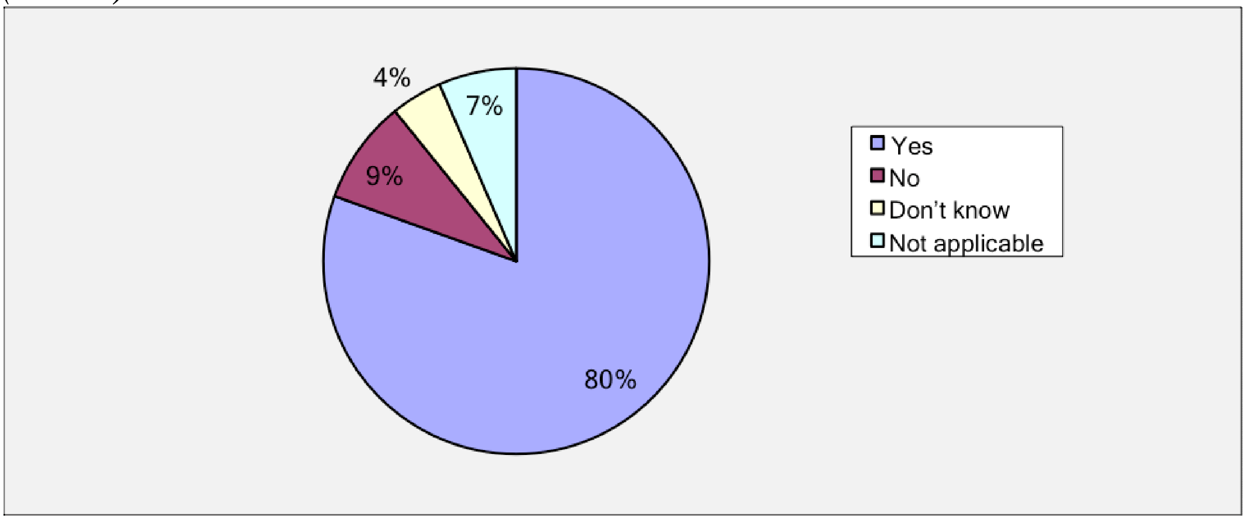
For the economic development dimension, the success of investment incentives offered by IPAs was evaluated by the majority as very successful or somewhat successful (figure 17). The majority of IPAs viewed incentives promoting the environmental dimension of sustainable FDI as somewhat successful, but a significant share did not find this question applicable. A significant share of IPAs viewed incentives promoting the social dimension of sustainable FDI projects as very or somewhat successful, but the majority did not find this question applicable either. To the extent that IPAs were in a position to evaluate the success of incentives for attracting sustainable FDI, they gave higher marks to incentives for economic development. IPAs were rather unsure of the success of incentives for the other dimensions of sustainable FDI, largely because they do not offer incentives specifically aimed at them. Importantly, the majority of IPAs considered the structure of incentives to be transparent to investors (figure 18).

Figure 17. How successful have you been in attracting FDI projects through the incentives you offer?
(Number of responses)



Source: Annex 1, question 19.

Figure 18. Do you think that the structure of incentives you offer is transparent for investors?
(Percent)



Source: Annex 1, question 20.

V. Conclusions

The functions and mandates of IPAs, as well as the methods and processes used to carry these out, have evolved over the past decade. IPAs have moved from first generation to third generation of investment promotion, and are now entering the fourth generation as they focus more on sustainable FDI. Nevertheless, IPAs continue to be first and foremost public agencies that treat the facilitation of *all* FDI into the host country as one of their principal tasks. This means that they are responsive to all foreign investors who knock at their door. However, the longer an IPA has been in existence, and the more successful it has been in attracting FDI, the more likely it is to move beyond facilitation to targeting sustainable FDI that contributes in terms of quality and not sheer volume alone.

Attracting a greater volume of investment is not necessarily disadvantageous from a sustainable FDI perspective. After all, FDI capital is needed in order to make at least some positive contribution to any of the dimensions of sustainable FDI (though non-equity investments are another option). But seeking to maximize the amount of FDI a country receives should not be an objective on its own accord, because quantity alone does not ensure the potentially positive effects that FDI can have on sustainable development. Furthermore, linkages among the four dimensions of sustainable FDI should not be ignored. For example, directing investment to disadvantaged regions within a country was frequently encountered in investment promotion strategies and was supported through incentives. This of course can lead to greater economic opportunities in these regions with the potential of reducing income inequality in the country, a social component of sustainable FDI.

IPAs are increasingly tasked to promote FDI into priority sectors (or to promote particular types of FDI across all sectors), and they do so usually through incentives. The structure of incentives favors mostly the economic development dimension of sustainable FDI. A new approach is needed in terms of incentive structures also geared to the other dimensions of sustainable FDI.

Increasingly, IPAs engage in greater policy advocacy and provide relevant information and feedback to governments about their countries' investment environments and administrative processes. As IPAs become more sophisticated, more geared to investor needs and more aware of the potential contributions of sustainable FDI, they can play a bigger role in shaping the national policy agenda.

One message of this survey is that, despite their growing awareness of the dimensions of sustainable FDI, IPAs are still not in full grasp of a variety of issues related to it. This is new territory for many IPAs, especially those that are still performing the more traditional tasks in investment promotion. Granted is also the fact that some of the dimensions of sustainable FDI may fall beyond the purview of IPAs and may need to be addressed instead by government ministries, or other government entities, or by legislation. After all, IPAs do not always have sufficient autonomy to do so on their own, and it is up to national governments to set the path toward sustainable FDI to be followed by IPAs.

Many IPAs see their job as having to attract as much FDI capital as possible, and frequently this is all that is expected from them. Indeed, IPA performance (and reward) systems have been evaluated traditionally by such tangible variables as number of leads, approved projects and the value of investment approvals. Judging the quality of FDI as defined here is a new concept. For example, on governance, especially as regards disclosure policies, IPAs may feel that confidentiality is important to foreign investors, and they may therefore be reluctant to pursue such disclosure practices unless mandated by legislation.

One observation is that IPAs are aware that sustainable FDI can provide significant benefits to their economies. The benefits cannot be taken for granted, nor do they happen automatically. IPAs (and governments) are therefore beginning to pay more attention to the benefits stemming from sustainable FDI, and do so increasingly by following a more holistic approach that at least tries to looks at a wider range of aspects when assessing investment projects. And while the economic development dimension of sustainable FDI has been the one more explicitly taken into account up until now, this means that more attention will be paid to the other dimensions going forward.

A few areas for possible extension of the findings of this survey exist. Firstly, it is worthwhile investigating the structure of IPAs, as well as the monitoring and evaluation and reward systems in place. How is an IPA's performance benchmarked and evaluated and what are the incentives for achieving set targets or doing well otherwise? How are these targets set and how has that changed over time? Are IPAs evaluated in terms of the *quantity* of investment (e.g. number or value of projects approved), or also the *quality* of investment measured with metrics that cover all dimensions of sustainable FDI?

Secondly, it may be worthwhile examining investment promotion acts to review the framework within which IPAs operate. Such acts might be limiting IPAs from extending their reach to cover all sustainable FDI dimensions and may require appropriate amendments on the part of governments. IPAs are after all executive organs of policy makers, and it is up to the latter to ensure that they are well equipped in terms of legislative authority to address all sustainable FDI dimensions in their investment promotion activities. This can go beyond legislation to include training IPA staff on, for example, sustainable FDI project assessments, international norms and standards and monitoring and evaluating sustainable FDI projects.

Finally, IPAs often express concern about “incentive wars” among countries for attracting FDI. An issue to explore relates to what might happen should an IPA adopt high norms and standards regarding sustainable FDI, but other IPAs do not follow suit. If this were to happen, one scenario could be that the IPA would feel that it is in a disadvantageous position when competing for FDI with other countries. In other words, there may be a trade-off between quantity and quality of FDI. Further examination of this issue could shed light on whether such a trade off is likely to hamper the attractiveness of a location or whether there may indeed exist a “win-win” scenario for the host country.

The findings of the VCC-WAIPA survey benchmark where IPAs stand today in terms of attracting sustainable FDI. IPAs are taking nascent steps toward fourth generation investment promotion strategies and practices, as they recognize more and more the benefits associated with the quality of such investment -- but more can be done to accelerate that process.

Annex 1. Survey questions (see attached Excel file for the responses)

Question 1. Where is your investment promotion agency located
Question 2. To what extent do you consider the following in your investment promotion strategy?
Question 3. How have your answers to (2) above changed compared to five years ago?
Question 4. How do you expect your answers to (2) to change over the next five years?
Question 5. When formulating your investment promotion strategy, who do you interact with primarily regarding sustainable development issues?
Question 6. Do you have "priority" areas/sectors for attracting foreign direct investment?
Question 7. If Yes to (6), in selecting "priority" areas/sectors, how much attention do you pay to the following?
Question 8. If yes to (6), over the next five years, in selecting "priority" sectors for foreign direct investment, how do you think your answers might change?
Question 9. Does your agency seek especially investments that adhere to any of the following?
Question 10. Compared with five years ago, how has your answer to the above changed?
And how do you expect it to change five years from now?
Question 11. Which of these would your agency be willing to forego in order to attract more investment or maintain current levels? (select two)
Question 12. At which point in the investment approval process are investors (all or in select sectors) required to provide the following:
Question 13. Does your agency (or relevant ministries) currently require:
Question 14. Have your answers to the above changed over the past five years?
Question 15. Do any companies that have invested in your country stand out in terms of contributing to sustainable development?

Question 16. In what way do you see your "policy advocacy" role changing over the next five years?
Question 17. In your assessment, what do you expect investor interest in your country to be in 2010 (compared with 2009); and what do you expect investor interest to be in 2011 (compared with 2010)?
Question 18. Do you offer incentives to foreign investors for projects that have the following characteristics?
Question 19. How successful have you been in attracting FDI projects that have these characteristics through the incentives you offer?
Question 20. Do you think that the structure of incentives you offer is transparent for investors?

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