CAN FDI CONTRIBUTE TO INCLUSIVE GROWTH: ROLE OF INVESTMENT FACILITATION

Iza Lejarraga
Head of Unit, Investment Policy Linkages
OECD Investment Division

FIFD Workshop on Investment Facilitation for Development
“What Investment can do for Trade Connectivity and Development – Investment Needs and Bottlenecks”
Geneva, 10 July 2017
Main points

1. Firms establish global supply relationships through **trade and FDI**: need policy frameworks that reflect the complexity of GVCs.

2. Achieving the SDGs will require **higher levels of FDI**, particularly to developing countries, but also **type and composition of FDI**.

3. **Transparency commitments** are associated with **trade-boosting effects**: similar effects can be expected for investment, and may be particularly important for more sophisticated forms of FDI.
GVCs has been largely looked at through the trade angle: need to better understand links to investment and other economic relationships.
Global supply chains in electronics: Firms combine trade, FDI, and other non-equity forms of control

Source: OECD, based on FactSet Supply Chain database – Results are preliminary, not for citation.
Firms combining several modes of internationalisation perform better.

Firms that are majority foreign-owned and active traders create better jobs and add more value.

---

**Wages relative to domestic firms not involved in GVCs**

<table>
<thead>
<tr>
<th>Mode</th>
<th>Cross-country average</th>
</tr>
</thead>
<tbody>
<tr>
<td>FDI-Export-Import</td>
<td>~3.5</td>
</tr>
<tr>
<td>FDI only</td>
<td>~2</td>
</tr>
<tr>
<td>Export-Import only</td>
<td>~1.5</td>
</tr>
</tbody>
</table>

**Productivity relative to domestic firms not in GVCs**

<table>
<thead>
<tr>
<th>Mode</th>
<th>Cross-country average</th>
</tr>
</thead>
<tbody>
<tr>
<td>FDI-Export-Import</td>
<td>~7</td>
</tr>
<tr>
<td>FDI only</td>
<td>~6</td>
</tr>
<tr>
<td>Export-Import only</td>
<td>~4</td>
</tr>
</tbody>
</table>

Source: OECD and WBG, based on calculations from World Bank Enterprise Surveys (2016) – Results are preliminary, not for citation.
Almost 70% of RTAs signed since 2001 cover investment; 9 out of 10 RTAs with investment involve non-OECD country.

Source: OECD based on WTO RTAs Database and WB Database.
Countries with similar levels of FDI can have different effects

Vietnam (net FDI 11.8 B)

Colombia (net FDI 11.7 B)

Source: OECD, based on data from MIT and Harvard (Observatory of Economic Complexity)
Higher complexity of FDI associated with higher productivity and lower inequality.

China (FDI 2.3 % of GDP)

Kenya (FDI 2.3 % of GDP)

Source: OECD, based on data from MIT and Harvard (Observatory of Economic Complexity)
Lower inequality: Geographic dispersion of FDI

**Regional Concentration Index for FDI, 2009-2014, selected countries**

Lower concentration:
Spread of FDI is greater across regions within country

Source: OECD and WBG, based on calculations from FDI Markets – Results are preliminary, not for citation.
Lower inequality: domestic linkages in FDI sectors

Concentration in sectors that source locally

Higher linkages: FDI is concentrated in sectors that source more from the local economy

High linkages: Korea

Low linkages: Costa Rica

Source: OECD and WBG, calculations on International Trade Centre Investment Database (2016); OECD Input-Output Database (2014) – Results are preliminary, not for citation.
Lower inequality: gender inclusiveness in foreign-owned firms

Foreign-owned firms female employees relative to domestic firms (ratio)

Share of women employed higher in foreign firms

Source: OECD and WBG, based on calculations from World Bank Enterprise Surveys (2016) – Results are preliminary, not for citation.
Economic complexity requires higher levels of transparency

- Importance of institutional quality (transparency, enforceability) in products with high proportion of intermediates inputs that require external contracting and sourcing arrangements (Levchenko 2007); relationship-specific investments (Nunn 2007); other trade and FDI (Rodrik).

- Adequate appropriation of returns by minimising expropriation risks (e.g., anti-corruption and anti-bribery measures)

- Improving rule-making by making regulatory processes open and participatory (e.g., public comment procedures)

- Reducing costs of uncertainty and contract enforcement (e.g., mechanisms for dispute prevention & resolution)

- Reducing market entry costs through information and simplification (publication, notification, enquiry points, single window)
Empirical evidence on the trade impact of transparency measures: Can countries stand to gain from similar efforts in investment?

- RTAs with comprehensive mechanisms for transparency are more strongly trade-promoting than those with a limited set of transparency measures:
  - Each additional transparency obligation negotiated in an RTA is associated with an increase in bilateral trade flows of over 1 percent. Overall, the expected increase in intra-regional trade could be of about 15 percent.
  - Consistent with World Bank-APEC study estimating that improving transparency in APEC could raise intra-APEC trade by approximately US $148 billion or 7.5 per cent of baseline trade in the region (Helble, Shepherd, Wilson 2007).

- The readiness of countries to embrace transparency commitments is associated with good governance conditions such as the maturity of democratic institutions, regulatory quality, and the rule of law.

Thank you for your attention

Contact:
Iza Lejarraga (Iza.LEJARRAGA@oecd.org)
OECD Investment Division
• Improve information on what types and composition of FDI is flowing into a country: FDI comes in different forms
• Countries want to devise policies that don’t just maximise the amount of FDI, but maximise the benefits from FDI

2. FDI as a source of capital: additional benefits

• As more countries have access to global capital markets, thinking more of FDI in terms of additional benefits it can bring: new knowledge and opportunities for people. These dimensions need to be better captured in the metrics on FDI.

3. Transparency has trade-boosting effects

• FDI is—broadly speaking—considered positive for economic growth, albeit under specific conditions: the evidence reveal wide heterogeneity, suggesting that effects are not uniform and domestic conditions matter
• Policy design can improve if based on the specific context of the country
Outcomes of FDI are Endogenously Determined

- **Value of FDI is endogenous.** Differences in FDI outcomes depend on the interaction between the type of investment and the policies, institutions, and conditions of the host economy.

- **Value of FDI cannot be assessed by only looking at aggregates.** Need more nuanced, disaggregated and comparable metrics that capture differences in outcomes across countries.
Interaction of FDI with policies and country conditions

Policies & Framework Conditions
- Policies
  - Investment policies
  - Complementary policies
- Conditions
  - Human & physical capital
  - Institutions
- Exogenous
  - Market size
  - Geography
- Complexity
  - Diversification
  - Sophistication

FDI Types Composition
- Motive
  - Natural resource-seeking
  - Market-seeking
  - Efficiency-seeking
  - Strategic asset-seeking
- Entry mode
  - Greenfield
  - M&A
- Ownership
  - Equity or contractual
  - 100% or Joint venture
- Sectoral
  - Sector distribution
  - Services

FDI Outcomes
- Growth
  - Productivity
  - Wages
  - R&D intensity
  - Diversification
  - Skills spill-overs
- Inclusiveness
  - Job creation
  - Domestic linkages
  - Gender inclusion
  - Spatial dispersion
Outcomes-based FDI Indicators: comparable metrics across countries

**GROWTH**
- Indicator on FDI productivity
- Indicator on FDI diversification
- Indicator on FDI sophistication
- Indicator on FDI vertical integration
- Indicator on FDI R&D intensity
- Indicator of FDI wage premium
- Others that should be considered?

**INCLUSIVENESS**
- Indicator on FDI job creation
- Indicator on FDI skills intensity
- Indicator on FDI gender inclusion
- Indicator on FDI linkages
- Indicator of FDI geographic concentration
- Indicators of FDI contribution to tax base
- Others that should be considered?
Knowledge Gaps

Dearth of information

Growing but limited literature

Large body of evidence

- Productivity
- Wages
- Vertical integration
- Jobs
- Skills
- Domestic investment
- SME Linkages
- Diversification
- Gender
- Geo-graphic dispersion
- Sophistication
9 out of 10 RTAs with investment involve a non-OECD economy

Before Doha

- RTAs with investment: 28%
- RTAs without investment: 72%

Since Doha

- RTAs with investment: 31%
- RTAs without investment: 69%

Source: OECD based on WB RTAs database and other sources