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Effectiveness of foreign direct investment policy measures

Note by the UNCTAD secretariat

Executive summary

Countries seek to attract foreign direct investment (FDI) for the package of benefits that it brings and the positive impacts that it can generate in the host economy. Policy measures to attract FDI include the laws and codes that define the investment framework for foreign investors, as well as the general standards and policies that affect investment activity. There is broad uniformity among countries in their investment frameworks, which reflects the overall trend in policy liberalization of the past decade. However, the variety in country conditions with respect to the general standards and policies that affect investment activity makes this an area of attention for Governments seeking to increase the effectiveness of their policy measures to attract FDI. A further area is suggested by the successful experience of some countries with respect to proactive measures. Governments also use measures beyond attracting FDI, so as to derive wider benefits through linkages with local enterprises.

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INTRODUCTION

1. Countries seek foreign direct investment (FDI) for the package of benefits that it brings and the positive impacts that it can generate in the host economy. Investors are interested, of course, in securing an adequate rate of return; but in the process of making an investment broader effects are generated, directly or indirectly as externalities. The full extent of these benefits is not always certain, and there can also be costs and negative effects.

2. The challenge for policy-makers in designing FDI strategy and policy is to maximize the positive effects and minimize possible negative effects. However, without adequate convergence in foreign investor and national interest, there can be trade-offs between policies to attract FDI and measures to derive full benefits from it.

3. The approach to FDI policy is conditioned by national circumstances and global trends. At the national level, there has been increasing reliance on market forces for the allocation of resources, and on the private sector as the primary engine of economic growth in developing countries. At the international level, there has been rapid expansion of international production and intra-firm trade and technology transfers, leading to strong competition amongst countries for FDI. There is also increasing recognition by investors of their corporate social responsibilities and by their Governments of the need for home country measures to encourage FDI and technology transfer to developing countries, particularly the least developed among them.

4. This note discusses the question of what constitutes effective FDI policy, utilizing the lessons of successful international cases and the knowledge gained through 12 investment policy reviews (IPRs) conducted by UNCTAD.[1]

I. ATTRACTING FDI

5. Some of the fundamental determinants of FDI are largely outside the direct control of national policy – factors such as geographical location, resource endowment and size of

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[1] The countries for which investment policy reviews have been completed to date are Egypt (1999), Uzbekistan (1999), Uganda (2000), Peru (2000), Mauritius (2001), Ecuador (2001), Ethiopia (2002),The United Republic of Tanzania (2002), Botswana (2002), Ghana (2002), Lesotho (2003), and Nepal (2003). The reviews may be downloaded from the UNCTAD Internet website (www.unctad.org/ipr).

domestic market.[2] However, there is much that government can do to put in place the right conditions for attracting FDI. UNCTAD's Inward FDI Performance Index, which ranks countries according to their potential for attracting FDI, shows a number of developing countries with high performance, some in spite of low potential, and a large number of countries with low FDI performance in spite of high potential. In 1998–2000, there were 42 under performers that did not attract their expected share of global FDI.[3]

6. The national investment framework and general regulatory environment can facilitate the strongest attraction of FDI consistent with economic potential. Countries can also act on some of their economic determinants to maximize their economic potential. Dynamic economic determinants include potential market size, availability of assets and efficiency of production. In the presence of a conducive policy environment, proactive measures come into play. These include investment promotion and business facilitation.

1. Policy framework for FDI

7. The enabling national framework for FDI consists of (a) the specific rules and regulations governing entry and admission of foreign investors, and standards of treatment of foreign affiliates, and (b) the general operating measures affecting all business, including FDI (but not designed explicitly for foreign investors). With the liberalization of FDI regimes across developing countries, the first set of measures has increasingly become a less important impediment to FDI inflow than the second set. Thus, cases of poor or discriminatory treatment of foreign investors are now less frequent. But this is less often the case for the general regulatory environment and government administration of business regulation.

8. Table 1 indicates common features of country practices in terms of core FDI-enabling measures. These are classified on the basis of policy findings that have emerged from the IPRs. "Optimal" represents a regime where the stance of FDI policy facilitates the strongest attraction of FDI consistent with economic potential and national objectives. "Permissive" represents an FDI environment that broadly enables FDI but is non-optimal in attracting levels of FDI consistent with economic potential and national objectives. "Inhibiting" represents a regime that substantially deters FDI.

9. Most countries are reasonably open to entry by foreign investors. However, generally, two current issues bear on the extent to which countries are becoming more rather than less open to FDI *in practice*: the process by which activities are restricted to FDI, and market exclusivity granted to State-owned enterprises or recently privatized entities. The process by which activities are added to or taken off the list of protected activities is often neither well defined nor transparent and could be the result of arbitrary considerations. Sometimes certain types of business are reserved for national investors only. Considerations such as whether

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[2] See *World Investment Report 1998: Trends and Determinants* (New York and Geneva, United Nations Sales No. E.98.II.D.5).

[3] See *World Investment Report 2002: Transnational Corporations and Export Competitiveness* (New York and Geneva, United Nations Sales No. E.02.II.D.4).

preventing FDI will restrict competition or worsen the overall investment climate should be included. Policy on FDI entry should work in tandem with competition policy. Nepal, for example, has reserved activities, including the accounting and legal professions, thus contributing to a general disabling investment climate for other types of investment.

Table 1. Specific standards of entry, treatment and protection of FDI

Policy area	Specific standards Optimal	Permissive	Inhibiting
Entry	Reserved list confined to clear national interests. Flexibility to accept FDI on negative list.	Substantial reserved list based on ad hoc grounds with little flexibility.	Substantial reserved list blocking FDI in areas of potential. Pressure to partner national investors to gain entry.
Admission	FDI not screened for approval unless activity on negative list.	All FDI transparently screened.	Non-transparent screening.
Treatment and protection	Modern legal framework and good track record.	Good recent track record with or without strong legal framework.	Poor track record.
Treaties	Extensive treaty network, including major and regional home countries.	Expanding treaty network.	Small treaty network.

10. Investors tend to favour countries with strong investment protection laws or practice. Good practice exhibited by a sound track record is paramount, but it can be useful, especially for new investors, to provide a strong complementary protection and treatment regime in national law and/or by treaty. The treatment and protection of FDI relate to a country's conduct towards foreign investors in relation to national treatment, fair and equitable treatment, non-discrimination, transfer of funds, expropriation and dispute settlement. The number of bilateral investment treaties varies considerably (around 100 for major outward investors, but only four in Botswana and two in Lesotho). The IPRs found that actual practice is often of a higher standard than the legal framework in place. Weak laws concerning treatment and protection of FDI do not appear to have hindered FDI in countries such as Botswana and Lesotho, as they have shown good practice in that area.

11. General policy measures are increasingly assuming greater practical importance than specific FDI-enabling policies for most countries. Table 2 indicates practice for general standards and policies which impact on FDI, using the regime classification outlined in table 1. The following discussion highlights specific issues of importance.

12. A key general regulatory measure affecting FDI is the **fiscal regime**. Investors will be deterred if tax rates are uncompetitive. This is increasingly an issue as FDI enters export-oriented activities where products must be globally competitive. There has indeed been a trend towards lower corporate taxation in general but also through specific fiscal arrangements. As a result, many countries maintain high general taxes coupled with specific fiscal incentives for priority areas, involving frequent changes in the taxation regime. Some incentives seem excessively generous, unclear or prone to change, casting doubts on their sustainability and efficiency. For instance, Egypt has a high general corporation tax rate coupled with a long-term tax holiday for up to 10 years in manufacturing in the industrial zones. Such a dual approach transmits conflicting signals and can lead to widespread use of incentives creating distortions and additional administrative barriers for investors. However, whatever the effect of fiscal incentives, it should be noted that specific financial incentives can be incompatible with the WTO Agreement on Subsidies and Countervailing Measures when they affect trade, although there are exceptions for least developed countries and some other countries.

Table 2. General standards and policies which influence FDI

	General standards		
Policy area	**Optimal**	**Permissive**	**Inhibiting**
Fiscal	Competitive and well-defined general regime with variations based on sectoral and strategic needs. Adequate tax treaty network.	Uncompetitive but well-defined general tax regime with piecemeal incentives. Expanding tax treaty network.	Uncompetitive high tax regime with significant interpretation difficulties. Inadequate tax treaty network.
Revenue administration	Fair and prompt action on assessments, refunds and clearances.	Fair but inefficient administration.	Widespread avoidance, arbitrary and/or corrupt assessment.
Exchange control	None.	Controls maintained but administered flexibly with no access problems.	Volatile, access difficult. Non-market exchange rates.
Land and labour	Market-driven access to land and labour within specific and transparent public interest safeguards.	Over-regulated but not unduly restrictive controls on land and labour.	Rigid anti-market controls with uncompetitive statutory requirements. Land titles not fully bankable.
Competition policy	Strong, well-enforced competition law. FDI increases competitiveness of intermediate goods and services.	Significant pockets of market concentration and barriers to entry. Inappropriate controls.	Pervasive private and public monopoly.

Policy area	General standards Optimal	Permissive	Inhibiting
Expatriate work and residence permits	Flexible. Responsive to investor needs.	Balanced rules. Inefficient administration.	Severe labour market tests. Arbitrary and unpredictable treatment.
Sectoral regulation	Modern laws confined to regulating for clear public purposes.	Some unnecessary or poorly structured regulations creating irritants but not obstacles to business.	Uncompetitive rules or uncertainties for investors as to rights or obligations.
Intellectual property protection	Modern and well-enforced laws. Compatible with the Agreement on Trade-Related Aspects of Intellectual Property Rights.	Developing framework and enforcement.	Poor legal regime and/or widespread abuse.
Environmental regulation	Modern law with clear and efficiently enforced standards.	Insufficiently developed standards and processes relying on ad hoc treatment.	Inadequate legal guidance to investors on obligations and liabilities.
Corporate governance and accounting standards	Modern commercial laws and international accounting standards.	Dated but mostly functional commercial and accounting regime.	Substantial gaps and uncertainties.
Rule of law	Impartial and efficient judicial process and law enforcement.	Some discrimination or inefficiency.	Non-independent judiciary. Insecure legal and personal environment.

13. Foreign investors need ready access to **foreign exchange** for their operations. Countries unable to meet that standard will not be competitive in attracting FDI, except in hard-currency earning projects or under conditions of special foreign exchange accounts. A trend towards the liberalization of foreign exchange controls is emerging, in middle-income countries as well as least developed countries. Nevertheless, some countries continue to impose severe foreign exchange restrictions or non-market exchange rates.

14. Sound **industrial relations** can give countries an edge in attracting FDI. The state of industrial relations can be a significant positive or negative factor in investor-entry decisions. Labour regulation includes the setting of minimum wages and other employee benefits, union rights, regulation of working conditions, rights of employers to “hire and fire”, and procedures for settlement of industrial disputes. Sound industrial relations are particularly important for countries seeking to attract FDI in labour-intensive export manufacturing, where the costs and appropriate regulation of labour are still central to the competitiveness of the sector, and where investors can be “footloose” with many possible alternative investment locations. In Ghana, labour-right provisions are generally negotiated under firm-specific collective bargaining agreements that can involve a lengthy and difficult process. Labour

disputes contributed to the decision of a foreign investor in the garment sector to leave the country altogether. Lesotho, on the other hand, introduced an independent and full-time Directorate of Industrial Dispute Prevention and Resolution to handle industrial disputes impartially. This approach is considered more successful in attracting FDI in labour-intensive industries such as garments than the models used by some of its competitor countries.

15. **Competition policy** and other regulatory measures may be relevant for maintaining cost competitiveness when backbone infrastructure or services are not provided under competitive conditions. This includes situations where there is a public monopoly or where private operators have taken over activities previously under public control. Complementary policy and an appropriate regulatory framework can be crucial for guiding successful private participation in infrastructure and services. Successful experiences of privatization in telecommunications and power in Peru emphasized disposal of assets to industry investors with performance standards rather than to financial investors, which led to a significant influx of additional capital and management skills. Less successful experiences in Ghana and the United Republic of Tanzania suggest that it is important to combine privatization with effective competition policy in order to ensure competitive practices by telecommunication operations and improvements according to required standards. The formulation of competition laws needs to be followed by effective implementation.

16. Availability of relevant skills (both technical and managerial) is another factor that can influence the decision to invest. To overcome the problem of skills shortage, host countries could introduce policies and regulatory measures which allow firms to recruit skilled foreign staff. Indeed, experience shows that countries and regions that actively encourage the inflow of foreign talent are more likely to attract skill-intensive investment (for example, Singapore and Silicon Valley) than those that restrict access to foreign skills. However, the practice of granting work and residence permits could vary from one country to another considerably. In addition to attracting key specialized skills in particular services, some countries are concerned with preventing the influx of low-skilled labour, for example Botswana. Immigration policy is not sufficiently differentiated in many countries in terms of those two concerns.

2. Proactive measures

17. Proactive measures involve augmenting the dynamic economic determinants of the host country and providing internationally competitive business facilitation.

18. Countries are often able to enhance the dynamic economic determinants that attract FDI. Investors are attracted to a country for its market, resources and other assets, and efficiency. Trading agreements can enlarge market size. Resources such as labour can be made more productive through training. Efficiency can be improved through reduction of input and transaction costs. A significant attractor of FDI in the 1990s was resource- and asset-seeking opportunities in privatization, which can also improve efficiency.

19. **Preferential market access**, especially to key markets, can strengthen a country's locational advantages for attracting export-oriented FDI and appears to be an important pull

factor for many developing countries. Least developed countries, for example, could benefit from the European Union's Everything But Arms (EBA) initiative which gives duty and quota-free access to a wide range of goods, and African, Caribbean and Pacific countries benefit from preferential treatment under successive Lomé Conventions and the Cotonou agreement. The African Growth and Opportunity Act (AGOA) of the United States for sub-Saharan African countries offers an important source of duty-free access to the United States market, especially in the textile and apparel sectors, thereby creating opportunities for investors. However, AGOA and other preferences are time-bound (and include provisions to enhance rules of origin), and while they are subject to extension, it is important to use them to improve the competitiveness of activities in order to withstand competition after preferences elapse or rules of origin kick in. Moreover, with global trade liberalization, preferential margins are being progressively eroded. Trade preferences in key markets should thus be seen as a temporary window of opportunity.

20. **Regional trade access** is important for many developing countries, especially small and landlocked economies. Regional trade agreements among developing countries include the Common Market for Eastern and Southern Africa, the East African Community, the Southern African Development Community and the Community of Andean Nations. Bilateral agreements include Nepal's access to the Indian market. Economic integration not only enlarges the size of the market, it also deepens the economic base of all member countries. This is because it increases the feasibility of decomposing production and R&D processes, as demonstrated by the experience of the Association of South-East Asian Nations. Centres of excellence at the subregional and regional levels can be attractive collaboration projects for foreign enterprises.

21. **Human resource development** is a key requirement for developing the dynamic economic determinants of all host countries. The availability of cheap and unskilled labour is no longer a special locational advantage for attracting FDI, as many countries have the same advantage plus others (such as market size). At the same time, with growing knowledge-intensity of production, transnational corporations (TNCs) are increasingly demanding a minimum level of productivity and technical, supervisory and management skills in their operations worldwide. The experience from IPRs shows that there is a lack of suitably qualified managerial and technical personnel in reviewed countries and that education and training systems are often not adapted to the needs of a rapidly evolving international production system. While human resource development is a long-term process, a variety of proactive measures are possible in order to speed up the process of building the relevant skills. These include the following: market-based incentives for firms to undertake quality-training programmes that go beyond their immediate enterprise needs; adapting existing vocational training institutions to the needs identified by industry; attracting foreign education institutions to establish regional specialized training centres; twinning programmes between local and foreign universities; easing restrictions on employment of foreign workers to fill gaps in management and specialised skills; and attracting foreign or expatriate talent to fill gaps in higher-value-added services. Countries that have adapted to the needs of industry in their educational structure, including technical and engineering curricula, have been able to attract significant FDI inflows (e.g. Singapore, Malaysia and more recently Costa Rica).

22. **Privatization** has been an important channel for attracting asset-seeking FDI. However, the lessons emerging from IPRs indicate that to ensure maximum effect, the privatization process must be efficiently administered and, as mentioned earlier, competition policy and appropriate regulatory institutions must be in place, especially for successful private sector participation in infrastructure and services.

23. **FDI targeting** involves creating investment packages around potential opportunities in new sectors. In the 1970s, for example, Malaysia targeted export-oriented FDI in electronics, and with no prior manufacturing export base became the world's largest exporter of electronic semi-conductors within a decade. The success of FDI targeting lies in devising and implementing a cohesive and coherent strategy based on extensive feedback from potential investors, outside and within the country, on the type of conditions that need to be created, and facilities provided, to ensure that a substantial flow of quality FDI is generated in the targeted sector.

24. Singapore is another example of a country that has relied on targeting to move comparatively smoothly from attracting FDI in light manufacturing to FDI in capital-intensive manufacturing, and, more recently, FDI in knowledge-intensive activities. The fiscal regime targeted incentives for pioneer investors that would bring new industries to Singapore. The creation of joint Government–investor technology and training centres helped attract knowledge-intensive FDI in electronics, while the establishment of local branches of foreign business schools has attracted good students. A regionalization programme encourages TNCs to establish regional headquarters while leaving lower-value-added activities elsewhere. Other trade, education and substantial training policies have moved in tandem and focused on the effective targeting of FDI into higher-value-added activities.

25. Targeting existing investors to reinvest and upgrade has also been an effective strategy for many countries. This was one of the many policy recommendations proposed to Egypt, which has been relatively unsuccessful in attracting export-oriented FDI, as investors prefer to produce for the large domestic market. However, existing investors can be encouraged to upgrade and expand production from the local to the regional market through incentives and support services such as those provided in the industrial zones.

26. Mauritius has now reached the point where rising wage levels make it more difficult to compete for FDI in textiles and garments, and firms have had to turn to outward investment of their own on the African mainland in order to remain competitive in the low-end segment of the industry while attempting to upgrade production at home in the high-end segments. Their success will depend on acquiring new skills and technology capabilities and their ability to target FDI which will enable them to move into higher-value sectors, including financial services, business services and information technology, to service the regional market. The challenge lies in removing the constraints of the high cost of telecommunications services and the limited pool of skilled professionals.

27. Nearly all countries have institutions for **investment promotion and business facilitation**. The more active investment promotion agencies (IPAs) target particular foreign investors in line with the country's overall FDI strategy. The targeting of leading TNCs has

led to successful FDI inflows in to Costa Rica, Ireland and Singapore. IPAs in successful countries have had significant influence over national policy (in order to plan for specific investor needs such as skilled labour and infrastructure), have engaged in significant FDI promotion activities (site visits, matchmaking etc.), have helped with obtaining permits, and have been able to follow a strategy consistently over a long period (by developing investment packages around potential opportunities).

28. A useful function of IPAs is the provision of **after-care** investment services. Support of existing firms can be an important source of additional investment, either through existing firms or through a positive signal to potential investors. Satisfied investors can have a positive demonstration effect and can be used for promotion purposes, as has been the case, for instance, in Chile and Costa Rica. The IPRs show that some IPAs have good relationships with existing investors, such as in Lesotho, while others do not.

29. While the policy framework, economic determinants and business facilitation are considered here separately, it is frequently the combination of these factors that attracts FDI. For instance, the IPR of the United Republic of Tanzania shows that the significant and sudden inflow of FDI into mining took place only after a critical mass of policy changes, in particular a new and competitive mining code.

II. BENEFITING FROM FDI

30. The benefits that can be derived from FDI are many. The IPRs provide evidence of benefits in terms of employment generation, wages, linkages with local firms, capital and technology flows exports, voluntary health and education programmes, and the range of new product and services provided. However, not all countries benefit equally from FDI. In fact, in some cases it may even have a negative effect in terms of, for example, crowding out domestic private investment and damaging the local environment. Evidence from IPRs also indicates that in many countries there appear to be missed opportunities in establishing local linkages. For instance, nearly all inputs in the pharmaceutical industry in Egypt are imported. There are also cases where linkages have been established, for instance in the mining industry in Peru and the United Republic of Tanzania, but could be developed further.

31. Government policies can mitigate some of the potentially negative effects of FDI. As discussed earlier, competition policy and an appropriate regulatory framework are crucial for guiding successful private participation in infrastructure. Environment policy is equally desirable, particularly in countries with fragile ecosystems or sizeable resource extraction activities. Labour laws and health and safety standards can ensure decent work conditions. These measures are part of the general standards that apply to all enterprises and are consistent with the non-discrimination and national treatment principles that most countries accord to foreign investors.

32. **Public–private dialogue** can help raise corporate awareness and encourage socially responsible actions by corporations. From a development perspective, corporate responsibility may involve facilitating the transfer of appropriate technology, assisting in the

development of social services, training of local workers and building of linkages with local enterprises. National business councils can help promote public–private dialogue, particularly when local enterprises and other stakeholders are involved. Regional and municipal councils can also be effective.

33. A strong technological base is an important asset for countries wishing to attract FDI and benefit from it through linkages and technological learning. Unfortunately, many developing countries either lack an effective national science and technology policy or where such a policy is in place, it tends to lack coherence with other key policies that influence investment and enterprise development. A number of the IPRs conducted by UNCTAD reveal a mismatch between national science and technology policies and objectives of countries and their overall investment policies and strategies. For instance, despite the substantial research and development (R&D) capacity in the United Republic of Tanzania only a small proportion of the technological needs and demands of the productive sector originate from local sources. There is a need to update national science and technology policies and build a more focused, market-oriented, coordinated and appropriate technology support infrastructure. This should be complemented by policies and incentive schemes that support focused technology activities at the enterprise level. Where a national innovation system has been designed, such as in Ecuador and Peru, the policy focus needs to shift towards effective implementation.

34. Governments can be proactive in encouraging and deepening **linkages** between foreign enterprises and local companies (see table 3). The following discussion highlights specific issues and methods of linkage promotion.

Table 3. Specific measures by Governments (of host and home countries) to promote linkages

Technology upgrading	**Training**
Partnership with foreign affiliates. Incentives for R&D cooperation. Home country incentives. Promote suppliers' associations.	Collaborate with private sector on one-stop service. Support private sector training programmes. Collaborate with international agencies.
Information and matchmaking	**Financial assistance**
Provide relevant information.	Legal protection against unfair contractual arrangements and other unfair business practices.
Maintain updated electronic databases.	Guarantee recovery of delayed payments.
Act as honest broker in negotiations.	Indirect financing to suppliers through their buyers.
Support suppliers' audits.	Tax credits and other fiscal benefits to firms providing long-term funds to suppliers.
Provide advice on subcontracting.	Co-finance development programmes with private sector.
Sponsor fairs, exhibitions and, conferences.	Directly provide finance to local firms.
Organize meetings and, visits to plants.	Home country measures: · Two-step loans. · Using official development assistance

Source: UNCTAD, *World Investment Report 2001: Promoting Linkages*, table VI.1, p. 210.

35. Linkages are often lacking because local firms cannot meet international production standards, as well as corporate requirements in terms of consistency/continuity and volumes of production. Government and the private sector can work together to establish one-stop centres, where entrepreneurs have access to **business development services** and inputs (i.e. entrepreneurship training, information, finance, quality control, networking and business counselling). Such programmes, for example EMPRETEC and Enterprise Africa, are already in operation in some countries, and under consideration in others.

36. There are examples where **local supplier upgrading** programmes in technology and skills have helped to stimulate linkages between local firms and TNCs, and where local firms have subsequently developed into exporters themselves. The Irish National Linkage Programme was designed to raise local organizational and marketing skills, as well as quality and productivity, to the standard required by TNCs. Many local companies have subsequently reached a critical scale to be able to compete internationally. Singapore also sought to upgrade local industries through the establishment of a Local Industry Upgrading Programme (LIUP), under which TNCs were encouraged to enter into long-term supply contracts with local firms, leading to upgrading. Local firms benefited most in the electronics sector by supplying maintenance services, components and equipment to the semiconductor TNCs.

37. The Malaysian Penang Skills Development Centre is sometimes considered best practice in public–private training cooperation. It utilizes a set of public–private partnerships between the Government and TNCs in order to develop local supply capacity through coaching and mentoring programmes. In these supplier development programmes, TNCs and large enterprises agree to assist their small suppliers by continuously improving skills and technology. The centre was initially financed by the public sector (grants, training materials, equipment and trainers) and the private sector (donations, loan of equipment, furniture and, private training facilities) pooling their resources. It is now self-financing.

38. There may be a useful role for **incentive schemes** to encourage firms to collaborate with other stakeholders in enhancing the level of skills, technology and infrastructure in the host country. In the past, host Governments have used direct measures, such as local content, export performance and transfer of technology requirements. However, such measures are now being phased out by most developing countries because they are incompatible with their obligations under the WTO Agreements (such as the Agreement on Trade-Related Investment Measures), or with their own market-friendly outward-oriented development strategies. In such a situation, development-oriented incentives assume greater significance. Such incentives (fiscal or financial) could be given to foreign firms as well as to large domestic firms for: (a) encouraging innovation in domestic firms; (b) promoting R&D cooperation with other smaller domestic firms and research institutes; (c) compensating for upgrading the level of skills of employees. Special funds could be established for providing such incentives.

39. Home country measures, such as tax incentives and the use of official development assistance for capacity building, infrastructure development and enterprise support and training programmes aimed specifically at encouraging FDI inflows, can play an important complementary role in such collaborative efforts, particularly in the least developed countries and other structurally weak economies.

III. ISSUES TO BE ADDRESSED BY EXPERTS

40. In the light of the above, experts may, *inter alia*, wish to comment on the issues raised in this note and exchange views on the following questions:

(a) *What are the most effective policies that countries can undertake to attract FDI? What actions can the international community take to support such policies, including home country measures?*

(b) *Which policies are effective in promoting participation of foreign investors in the development of human resources and technological capability building? What measures have been found to encourage and deepen linkages with the local economy? How can corporate social responsibility be encouraged and made more effective?*

(c) *What are private sector views on effective FDI policy measures and the role of investment promotion institutions?*

(d) *What examples can be provided for FDI-led improvement in country competitiveness and achievement of national development objectives? What appropriate development-oriented incentives can countries offer?*

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