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# BEST PRACTICES FOR CREATING AN ENVIRONMENT CONDUCIVE TO DEVELOPMENT, GROWTH AND INVESTMENT

Note by the UNCTAD secretariat[*]

**Executive summary**

This note proposes a framework and methodology for exchange and dissemination of best practices in the area of foreign direct investment (FDI) and its contribution to development. In this context, it suggests a series of case studies on best practices as a pragmatic tool for transferring know-how in FDI policymaking and policy implementation. Short, accessible case studies are proposed to draw out lessons of good practices by clear identification of objectives, methods and results. Topics will include established and emerging issues, and the case studies will seek best practices in both advanced and less advanced economies. Illustrations of the approach are provided. Experts are requested to comment on the proposed approach to selection and treatment of case studies, sources of best practice examples, means of disseminating the results and appropriate follow-up activities.

[*] This document was submitted on the above-mentioned date as a result of processing delays.

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## INTRODUCTION

1. The Trade and Development Board agreed at its forty-first executive session on 18–20 April 2007 that the Commission on Investment, Technology and Related Financial Issues should convoke an expert meeting on "comparing best practices for creating an environment conducive to maximizing development benefits, economic growth and investment in developing countries and countries with economies in transition". The issue of best practices has subsequently been taken up by the G8 Heiligendamm summit that gave it a strong impetus with a call for UNCTAD and the Organization for Economic Cooperation and Development (OECD) to develop best practices for building an institutional environment conducive to increased foreign investment and sustainable development, including in connection with the twelfth session of the United Nations Conference on Trade and Development (UNCTAD XII) in Accra, Ghana, in 2008.[1] It is against this backdrop that the secretariat has prepared the present issues note for the expert meeting.

2. Today, foreign direct investment (FDI) is recognized as a major potential contributor to growth and development. As demonstrated by the *World Investment Report* over many years, FDI brings not only capital to the host country, but also technology, management know-how and access to new markets. It also generates employment and tax revenues, and contributes to building the productive capacity that enables countries to maximize their opportunities to benefit from globalization (see, e.g. *World Investment Report 1999*). FDI supplements other forms of capital flows, with a long-term commitment to the host economy and its supply capacity. Today, many countries wish to establish investment-friendly policies and actively seek to attract FDI in the interests of building productive capacity, thereby reducing poverty.

3. Creating an environment conducive to development, growth and investment is obviously a multifaceted matter that involves a myriad of policies at national and international levels, including enterprise development policies**.** A comparative analysis of country practices within the framework of the Commission on Investment, Technology and Related Financial Issues requires focus on policies aimed at attracting FDI and maximizing its development benefits.

4. Many approaches can identify best practices. These include those based on global research and policy analysis (e.g. the *World Investment Report* and UNCTAD Investment Briefs), those based on country-specific assessments and policy advice (e.g. investment policy reviews) or those based on general policy diagnostic tools (e.g. OECD's Policy Framework for Investment). A case study-based approach allows policy lessons to be derived directly from the collection and examination of various country experiences.[2] Many countries already apply this method by benchmarking themselves to emulate success stories in their regional context. However, this tends to be narrow in terms of choosing comparative peers and may not always provide suitable solutions. An approach based on a multitude of cases widens this scope to a global pool of existing experiences beyond the usual range of exemplars. Furthermore, a user-friendly approach to best practices through case studies of successful experiences would effectively facilitate the transfer of know-how in investment policy practices.

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[1] See G8 Summit Heiligendamm Declaration, "Growth and responsibility in the world economy", paragraphs 19 and 20.

[2] For a discussion of the case study approach, see R. Yin (1994). *Case Study Research: Design and Methods* (2nd edition). Thousand Oaks, CA: Sage Publishing.

5. The UNCTAD secretariat proposes to undertake, in the next three years, a series of case studies with the aim of collecting cases for a new series of technical assistance-oriented advisory studies on best practices in investment policies. These will form a basis on which country-specific technical assistance advisory work could be pursued in the future. The preparation of case studies will benefit from intergovernmental debate, which could be used to review and subsequently feed into further research and technical assistance delivery. This will result in an inclusive cycle involving all of UNCTAD's three pillars of work (research, technical assistance, and intergovernmental consensus building), thus contributing to the strengthening of UNCTAD's technical assistance delivery at the country level.[3]

6. The intergovernmental dimension should of course not be confined to UNCTAD-specific mechanisms, but could include regional workshops, follow-up through the World Association of Investment Promotion Agencies (WAIPA), and coordinated collaborative approaches with other international (and regional) organizations such as OECD and the Asia-Pacific Economic Cooperation (APEC) Forum, among others.

## I. FDI POLICY FRAMEWORK

7. 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 domestic market. However, there is much that Government can do to put in place the right conditions for attracting FDI. The national investment framework and general regulatory environment can facilitate the strong attraction of FDI consistent with economic potential and overall development objectives. Governments can also take proactive measures to improve the economic determinants of FDI through measures such as skills and infrastructure development and market-enhancing trade agreements.

8. The enabling national framework for FDI consists of (a) the specific rules and regulations governing the entry of foreign investors, and standards of treatment and protection of foreign investment; and (b) the general operating measures affecting all business, including FDI (but not designed explicitly for foreign investors).

9. In the past 15 years, Governments of developing and transitional economies have generally lowered barriers to FDI entry. They have also enhanced legal protections through national law, contractual arrangements and an expanding network of international treaties. At the same time, FDI to these countries has increased 10-fold and has ventured into areas of sensitive public services hitherto reserved for state enterprises. Inevitably, the language and procedures of treatment and protection regimes have been tested as never before. More investor–State disputes have arisen. Governments need to be more proactive in managing this exposure and could benefit from experiences of best practices.

10. General policy measures (i.e. those affecting all businesses irrespective of ownership) are increasingly assuming great practical importance in attracting and benefiting from FDI. These areas include taxation, foreign exchange arrangements, protection of property rights and enforcement of the rule of law, labour and industrial relations policy, work and residence permits for foreign staff, competition policy and sector regulation. Regulatory policy is

[3] See, in this context, also the Report of the Panel of Eminent Persons on "Increasing the development role and impact of UNCTAD" (Geneva, 2006).

essential to protect the public interest but should be designed effectively and administered efficiently.[4] More dynamic issues are now informing regulatory policy. For example:

(a) The attraction of skills becomes important alongside the protective issues of work and residence permitting.

(b) Measures in the regulatory framework to encourage FDI in less-advantaged areas within countries become more central in enhancing the developmental impact of FDI.

(c) Encouraging foreign affiliates to upgrade and deepen their operations needs ever more attention to increase confidence in the sustainability of FDI.

(d) Responding to new challenges in the regulatory regime of export processing zones in low-to-middle income countries arising from increased labour costs and World Trade Organization (WTO) agreements, taking advantage of policy flexibilities provided therein, becomes more important.

11. Thus, best practices topics in the regulatory framework that go beyond the objectives of removing inhibiting policies or creating an environment conducive to FDI should be chosen. These will provide best practice cases of optimal policies that facilitate the strongest attraction of FDI consistent with economic potential, national development objectives and the evolving international landscape. The proposed best practice cases will not feature investment promotion agencies (IPAs) but, where relevant, their role will be highlighted in good practices emanating from the cases.[5]

12. Substantial experience, not always salutary, is now accumulating of FDI in services that were previously closed to private investment (including telecommunications, electricity, gas supply, ports, airports and roads). These serve the public but are also key "backbone" services that affect the productive capacity of all businesses. Many Governments are seeking an expanded role for private investment in these services and could benefit from examples of best practices in establishing regulations, procedures and institutions to deal with the complexities involved.

## II. APPROACH

### A. Defining "best practice"

13. A "best" replicable practice of a proactive policy measure aimed at increasing the contribution of FDI to development as such does not exist, as no one size fits all. All observed practices have to be seen in their specific national and industrial/sectoral context. Nor can it imply that the practices adopted in the chosen country cases will be without problems or critics. However, leading examples of successful government policy practices can be useful by shedding light on success stories that are, if adopted and adapted to the specific circumstances, replicable by other Governments that are pursuing the same objectives. The case studies will try to show what are the lessons learned, widely applicable, in developing policies for FDI to contribute to development.

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[4] For detailed discussion, see Issues Note prepared by the UNCTAD secretariat for the expert meeting on "Effectiveness of FDI Policy Measures", June 2003, available at:
http://www.unctad.org/en/docs/c2em13d2_en.pdf.

[5] UNCTAD will launch a companion series of advisory studies to assist IPAs to enhance their impact in delivering FDI for development.

**B. Methodology**

14. Such a case study approach could take the following form:

(a) The objective set by the Government and its development context;

(b) The methods (strategies, regulations, administrative steps) used to achieve the objective;

(c) The results, against expectations; and

(d) How and why the methods worked and where they fell short.

15. From the case studies, lessons should be drawn that can be useful in designing “good” policy and measuring its results in other countries (and in avoiding the pitfalls and having realistic expectations). The UNCTAD secretariat intends to present case studies in papers that highlight policy lessons that provide useful guides to countries wishing to develop their own policies for similar objectives, with the aim of developing practical policy toolkits for technical cooperation, including capacity-building work. These papers will be short and written in accessible style, presenting lessons in a form that helps replication. Comparing and contrasting the experiences of countries at differing levels of development should provide further useful insights into “best” practices. Not all cases will necessarily be contemporary examples. They can be used to illustrate methods adopted at earlier critical junctures in member countries’ policies towards FDI and national development.

## III. PROPOSED FRAMEWORK FOR BEST POLICY PRACTICE CASES

**A. Key strategic challenges and issues in FDI**

16. It is suggested that the case study topics will cover FDI and development issues arising both from established and emerging challenges over the next 10 years, brought about by both the international and domestic landscapes. Overlying these challenges is that FDI should be a positive and sustainable force in national development, including building national capacities in business, skills and technology, and in assisting the development of less advantaged areas.

17. Topics for case studies will be selected on the basis of their importance and relevance for developing countries and countries with economies in transition. *Importance* means that the topics should reflect the key issues in FDI and development. *Relevance* means that the topics should reflect questions that many Governments are asking (or should be asking) themselves about policy responses to these key issues.

18. Countries differ in their circumstances and thus in their challenges in attracting and benefiting from FDI. Hence, not all case studies will be of equal relevance to all countries. As a first step, it is proposed to undertake case studies of best practices in meeting the broadest strategic challenges. To that end, five strategic FDI challenges have been identified, as they have emerged from UNCTAD’s investment policy reviews and other work (table 1). Accordingly, country case studies will be prepared showing how selected countries have responded to these challenges. Following these five thematic case studies on strategic FDI challenges, a longer series of best practice studies on responses to more specific policy challenges will be prepared (see annex).

19. Some of the topics are of near-universal interest, such as how to attract FDI to the regions. Other topics will be more relevant to some countries than to others. For example, the

topic "how to move foreign affiliates into exporting" is strongly relevant for countries that seek a greater efficiency orientation of FDI. Thus, a systematic competitiveness strategy is likely to be a foundation of specific measures to achieve greater export orientation. These matters will be reflected in the choice of countries to demonstrate best practices and in drawing lessons from their experiences.

**Table 1. Country profiles and key issues**

| Country profile | Case study thematic topics | Examples of most relevant case study issue topics |
|---|---|---|
| I | Devising a systematic competitiveness policy for FDI. | How to foster foreign affiliates' innovation. How to move foreign affiliates into exporting. Fostering local partnerships. Attracting technology-intensive FDI. |
| II | Upgrading efficiency-seeking FDI. | How to anchor FDI in zones. How to use FDI to attract skills. How to attract technology-intensive FDI. How to use FDI to build a regional hub. How to attract FDI in infrastructure. |
| III | Attracting FDI to small markets. | How to use FDI to attract skills. How to use FDI to build a regional hub. How to manage competition issues arising from FDI. |
| IV | Fostering the role of FDI in facilitating the economic transition. | How to afford foreign investors confidence in the commercial justice system. How to fast-track investment reform. How to develop strong partnerships with foreign investors. |
| V | Attracting FDI to post-conflict countries. | How to afford foreign investors confidence in the commercial justice system. How to attract FDI to the regions. How to attract diaspora FDI. |

## B. Proposed case studies

20. The identified FDI strategic challenges correspond to five kinds of country profiles that have emerged from the secretariat's work in investment policy reviews and in other areas. Experts may wish to suggest other profiles regarding key strategic FDI challenges:

(a) **Profile I: Large countries**. These countries can attract market-seeking FDI but need a systematic strategy to attract more efficiency-seeking FDI, including moving foreign affiliates up the competitive ladder.

(b) **Profile II: Fast growing middle-income developing countries**. These countries already rely less on market-seeking FDI and have high export propensities. But they need to keep shifting into new industries and into services, not reliant on low-cost labour, to keep attracting efficiency-seeking FDI.

(c) **Profile III: Disadvantaged, small (including landlocked, least developed and island) developing countries.** These countries need careful FDI attraction strategies designed to overcome small domestic markets, low skills and poor infrastructure.

(d) **Profile IV: Countries with economies in transition.** These economies typically began a transition to market economies with well-developed skills, reasonable infrastructure and low sovereign debt. FDI complements these assets by introducing global perspectives on markets and efficiency. The pace of regulatory change has varied from very rapid pro-market reforms (especially in the European Union enlargement countries) to slow or less conventional changes with varying effects on FDI.

(e) **Profile V: Post-conflict countries.** These countries need a special approach to setting priorities in the investment framework and in strategy so as to give confidence to foreign investors, including returnees and the diaspora.

21. The countries chosen to demonstrate "best" practices must obviously be examples of successful practice. Measuring success in this area is not straightforward and can be controversial. The country cases illustrated below are chosen as examples of what could constitute best practice, with the proviso that there may be other cases of similar success. Experts are invited to suggest other examples.

**1. Systematic competitiveness policy to enhance the contribution of FDI**

22. Countries with large markets have found it relatively easy to attract market-seeking FDI. These include Argentina, Brazil, Colombia, Egypt, Indonesia and Nigeria. They have found it more difficult to change orientation towards attracting efficiency-seeking FDI, including inducing foreign affiliates, to become more efficient, export-oriented and innovative and earn a place in their groups' regional and global production mandates. This type of foreign affiliates is more likely to have sustainable and developmental presence in its host country.

23. The challenge for host countries is to devise a strategy that applies consistent competitive pressures (reduced import protection and greater competition in domestic markets) synchronized with appropriate support to business efficiency through regulatory, infrastructure and skills improvement. Such a strategy encompasses both local and foreign investors.

24. Australia is a potential case study of a more advanced economy. In the early to middle part of the last century, Australia promoted a protected inward-looking manufacturing sector to add to its world-class agriculture and mineral resources base. From the 1970's, its objective changed towards promoting a more internationally competitive manufacturing sector. Tariff protection began to decline with the establishment of the Industries Assistance Commission in 1973, as the impact of tariffs on the economy came under greater scrutiny. This wide view was developed by successor organizations which linked reduced market protection to key competitiveness factors such as regulation, skills and infrastructure. This culminated in the establishment of the Productivity Commission in 1998, which has a systematic remit to improve competitiveness. Today, the manufacturing sector is leaner, not a burden on other sectors and can attract FDI to compete in the region and globally in niche areas.

25. A possible developing country case study is Colombia**.** In 1994, Colombia broadened its liberalization programme by adopting a goal of upgrading its industries so as to integrate their production within international supply chains. It created Colombia Compite (Colombia competes) a comprehensive programme involving Government, business, labour and the universities to systematically benchmark and tackle factors crucial for international competitiveness such as trade, skills, transport infrastructure, energy and science, and technology. This approach likely helped Colombia become a thriving player in the region and take advantage of enhanced access to major markets through free-trade agreements.

26. Colombia appears to have adopted a consensus-building approach among stakeholder networks, whereas Australia's approach is more research-based and institutional. Both approaches changed over time and indeed Colombia Compite has evolved recently into "Agenda interna" under new political direction. These and other contrasts could provide interesting insights.

**2. Upgrading efficiency-seeking FDI**

27. Export-oriented FDI, often located in export-processing zones, has assisted the growth of many countries. This has usually relied on low-cost labour and is often supported by trade

preferences. These countries have attained lower middle-income developing status (around $3,000 gross domestic product (GDP) per capita), and can no longer rely on low-cost labour to attract efficiency-seeking FDI. Additional sources of competitiveness – skills and infrastructure – must be found and export-processing zones have to evolve to continue performing as relevant platforms for FDI attraction. Moreover, the shift to higher labour value-added investment may have to spread beyond zones, which often co-exist with protected non-dynamic manufacturing for local consumption.

28. Countries in this category include Costa Rica, the Dominican Republic, Mauritius, Peru, and Thailand. Low-income, but high-growth, countries will soon enter this category. Indeed some, such as Viet Nam, are already facing challenges simply in maintaining key infrastructure capacity in electricity and other services.

29. Case studies will select countries that have "upgraded". Possible cases are Costa Rica, Malaysia and Mexico.

30. Malaysia was an early starter among developing countries in attracting FDI in its industrialization. For some time, it has set the objective of moving into higher value added and more technology intensive manufacturing. For this purpose it has adopted or adapted numerous methods as part of an activist industrial policy, including preparing 10-year industrial master plans and signalling its intentions through incentives schemes and high-profile programmes. Foreign affiliates may account for up to half of Malaysia's manufacturing exports.[6] In FDI-targeting terms, the shift has translated into the targeting of so-called "quality investors". In the *World Investment Report 2002* ranking of the "top 20 manufacturing export winners by technology category 1985–2000", Malaysia ranked second in the high technology category and seventh in medium technology. Malaysia has advanced to a per capita GDP of $5,000.

31. Costa Rica ($4,500 GDP per capita) and Mexico ($6,400 GDP per capita) have both undertaken significant industrial upgrading involving FDI. In both cases, the upgrading has been narrowly based. Mexico's diversification from its well-known *maquiladora* profile has been based on FDI – principally from the United States – in automobiles and electronics. Costa Rica's performance is dominated by a single electronics investor. Further research, and advice from experts, will be needed to shed further light on these countries' experiences and the lessons that can be drawn from them.[7]

### 3. Attracting FDI to small countries

32. Small countries face special problems in overcoming size constraints. Local markets may be too small to attract significant transnational corporations and the entry of FDI could undermine meaningful internal competition. Attracting market-seeking FDI through tariff protection will not encourage sustainable competitive outcomes, yet skills and infrastructure may also be poor and thus unhelpful in attracting efficiency-seeking FDI. Nevertheless, there are cases of small countries that have succeeded, with Ireland and Singapore as the best-known cases among advanced countries. Among developing and transitional economies, Estonia (population 1.3 million) and Jamaica (population 2.6 million) stand out statistically for their ability to overcome these constraints.

33. Since regaining independence in 1991, Estonia has actively sought FDI. Methods employed have included emphasizing its access to the larger Baltic market of 90 million people (pre-dating its European Union accession in 2004), implementing an exceptionally

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[6] See *World Investment Report 2002*.
[7] Or indeed whether attracting flagship investors could itself represent a best practice method.

open and well-regulated regime for investment (Estonia rates very highly in international rankings), targeting investment from its Nordic neighbours (which account for about 75 per cent of FDI), and to some extent providing a platform for third-country investment into Russia. Estonia promotes its ability to host small, flexible foreign investors and does not appear to rely on fiscal incentives. However, much of current FDI stock is likely to be in backbone services areas such in banking, transport and utilities. Estonia's stock of FDI in 2005 was $4.2 billion and (excluding tax havens) is in the top 20 countries in relation to FDI stock as a proportion of GDP. This achievement from a low base in 1991 suggests that Estonia can offer a useful study of best practices in a small economy of both attracting and benefiting from FDI.

34. Jamaica also rates highly in its ability to attract FDI despite its small size. Its methods have included joining regional arrangements to enhance its potential market and tapping investment from a large country in close proximity (the United States). Its offer of business-friendly policies includes interventionist policies (such as special conditions incentives for FDI in exported goods and services) and related investor targeting.

35. Uganda and the United Republic of Tanzania may also provide good examples of best practices in this context.

**4. Fostering the role of FDI in facilitating economic transition**

36. Aside from bringing to the host country a bundle of assets, FDI can also contribute to the establishment of a general regulatory and institutional framework conducive to growth and development, diversification of the ownership structure and reform of the public sector. The positive contribution of FDI in this respect to China, Lithuania and Viet Nam is a case in point.

37. Lithuania had a relatively diversified industrial base and high human capital when it proclaimed its independence in 1990. The economy's industrial and services sectors nevertheless needed to undergo significant reforms in the transition towards a market economy. In order to rapidly achieve the transition, Lithuania sought to attract significant levels of FDI. The Government's main strategy was to build on existing industrial assets and human capital and to focus most of its efforts on modernizing the legal and regulatory framework for investment. It aimed to create a stable and open framework underpinned by fair and efficient regulatory institutions. It opened most sectors to FDI and guaranteed national treatment and protection of assets. The Government also set up two main initiatives to make laws and regulations investment-friendly. The "Sunset Commission" was established to identify and eliminate useless or redundant rules, regulations or institutions. The "Sunrise Commission", in turn, was created to streamline functions and procedures governing investment issues. These reform efforts were also strengthened and directed by the WTO accession procedure and by the need to adapt domestic law so as to join the European Union. These efforts, coupled with the boost derived from EU membership, have been very successful with a significant impact on the economy. By 2006, Lithuania ranked 16th on the World Bank's ease of doing business ranking, ahead of many other OECD countries and first among all transition economies. Strong GDP growth has been achieved and FDI flows were $1 billion in 2005.

38. A possible second case is Viet Nam. Since the 1990s, it has adopted a carefully modulated approach to reform of the national investment framework whilst encouraging export processing zones as the lynchpin of FDI attraction.

39. Lithuania and Viet Nam provide contrasting approaches to investment framework reform in formerly centrally planned economies – “big bang” versus “two-speed”. In both cases, FDI attraction has been significant but what common and contrasting lessons can be learned about the broader developmental impact of FDI?

**5. Attracting FDI to post-conflict countries**

40. Many countries have recently emerged from conflict, including Afghanistan, Croatia, Haiti, El Salvador, Rwanda, and Timor-Leste. Others, such as Algeria, Mozambique, Uganda and Viet Nam have a longer post-conflict experience. Once a degree of security and stability has been attained, the questions that arise are how FDI can be attracted and what areas can FDI contribute the most to building peace by improving economic conditions. The first generation of FDI is likely to be returnees whose early return could help to restore banking services, basic logistics and merchandising operations and mobile telecommunications. Later, FDI could be considered to rebuild key public services such as electricity generation, ports and airports. Diaspora investment may also be an important source of FDI in property development and services. Finally, the challenge is to attract FDI that consolidates the peace through employment generation, local business stimulation and regional development and stabilization. Possible case studies are Croatia and Mozambique.

41. Croatia declared independence in 1991 although a fully peaceful situation was not achieved until 1995. Throughout the 1990s, Croatia faced the twin challenges of moving from a centrally planned economy and rehabilitating a war-stricken country. Its objective was to encourage private investment in the rehabilitation process. A determined effort was made to stabilize the macroeconomy through tight monetary policy. A large part of the Croatian economy was put under the process of privatization on the basis of a 1991 law. This was open in most cases to foreign investors but there were important exceptions in banking, energy, utilities and defence industries. Early privatization was slow and in due course the 1991 law was amended with a particular view to attracting more foreign investment. The first investment promotion agency was not established until 1996. Free zones have also been created. Croatia has joined regional trade and investment organizations and in 2000 it joined WTO. As a result, the stock of FDI has risen impressively, from only $126 million in 1991 to over $12 billion in 2005[8]). This includes success in attracting FDI via privatization whilst large foreign investors such as Ericsson and Siemens have established major software development centres in Zagreb, Split and Osijek, employing about 2,000 highly skilled engineers.

42. Mozambique’s peace agreement was signed in 1992, followed by a two-year United Nations stabilization presence. The country aimed to rehabilitate key services and industries with private investment. Its key method was to quickly launch a process of “deep economic reform”.[9] This included a privatization programme, which pre-dates the peace agreement, but by 1997/98 had extended to large enterprises in key agro-industries and was open to FDI. The Mozal aluminum smelter was opened in 2000 and has since expanded after preparations began in 1997. This mega-project, involving several foreign investors, has been important in highlighting areas of need for continuing investment-related reforms and enhancing Mozambique’s credibility and visibility with foreign investors. Its FDI stock has surged from $90 million in 1992 to $2.4 billion in 2005.[10] FDI can now be instrumental to sustain peace through employment generation and regional development, especially in agro-industry.

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[8] UNCTAD FDI/TNC Database.
[9] UNCTAD-ICC (2002) An Investment Guide to Mozambique.
[10] UNCTAD FDI/TNC Database.

43. Case studies of Croatia and Mozambique should offer many similar insights into good practices. They should also offer contrasting examples of how countries at differing levels of industrialization and quality of skills and infrastructure can attract and benefit from FDI in post-conflict environments.

**C. Examples of issue-based case studies**

**1. Example A: How to attract skills in special FDI programmes**

44. The entry of foreign personnel is governed in all countries by a work and residence permitting regime. This regime is properly geared to protecting the national interest in terms of safeguarding job opportunities for qualified citizens and enhancing their skills through training. Such regimes essentially react to the foreign hiring requirements of investors. Some countries have added a more proactive dimension by devising skills attraction programmes. They recognize that skills, whether technical, professional or entrepreneurial, are important aspects of competitiveness and development. Infusing foreign skills can fill critical gaps and/or help to jump-start new industries, especially in services. When investment through business talent programmes (and not just employment) is part of such schemes, they become a useful specialized form of FDI attraction. The most developed versions of these schemes can be found in advanced countries such as Australia, Canada and Singapore. In less advanced countries, such as Malaysia and Mauritius, they have been employed in a much more limited fashion in selected priority industries. There does not appear to be a good example of these programmes among either developing or transitional economies. UNCTAD is preparing such a programme for Rwanda, taking into account the Australian and Singaporean experiences.

45. Singapore realized from the very early stages of implementation of its industrialization and export-oriented policy in the 1960s that development would have to be driven by human capital accumulation, as it had no natural resources base. Yet Singapore also suffered from a shortage of skills in the 1960s. In order to rapidly build skills, the Government put in place a two-pronged policy: (a) building local skills through a strong educational system; and (b) importing selected desired and needed skills from abroad. Singapore has put in place one of the most proactive and efficient skills attraction programmes in the world. Methods include: (a) drawing up a “talents in demand” list which includes the specific sets of skills that Singapore actively seeks to attract based on its development policies; (b) facilitating the entry and settlement of foreigners; (c) establishing “Contact Singapore”, a dedicated government agency, with five field offices, in order to promote the entry of desired skills; and (d) proactive promotion of Singapore as a place to live and work. The policy, in conjunction with other measures, has played a significant role in allowing Singapore to achieve its current level of development and prosperity, and the Government continues to see its targeted skills attraction programme as a building block for future growth and development.

**2. Example B: How to use FDI to improve infrastructure – electricity**

46. UNCTAD has reported on least developed countries (LDCs) that “Poor physical infrastructure is a major constraint on faster economic growth, substantial poverty reduction and the development of productive capacities in the LDCs”.[11] Similar issues arise in higher-income developing countries where fast growth gives rise to capacity constraints and is a significant factor in influencing the location of efficiency-seeking FDI. Many countries wish to attract private investment to supplement (and sometimes co-finance with) public

[11] UNCTAD (2006). *The Least Developed Countries Report 2006: Developing Productive Capacities*. p.193.

investment because the financial needs are so large. In Viet Nam, for example, electricity demand is growing at nearly 20 per cent per year. The investment requirements in generation alone are $3 billion annually, which is believed to be beyond the capacity of the State sector.

47. Electricity is a key element of infrastructure though not necessarily the most glamorous. UNCTAD's report on least developed countries states that the "electricity divide" has not received the attention the digital divide has received.[12] But there are many examples of unsatisfactory attempts to introduce FDI to the sector, including through privatization and concessioning. Thus, it will be useful to identify cases that have been relatively successful.[13]

48. Chile has actively sought private investment in its power sector since 1982, well before most other developing countries. In two decades of reforms it has split up and privatized the two major state enterprises in the industry, separated generation from transmission and distribution, and sought to create an appropriately regulated market that fosters competition. Private investment, including from major foreign investors, now predominates in all industry segments. Near universal coverage has been achieved and technical standards (e.g. losses) have improved significantly. Chile has had to cope with high growth in demand, a sustained drought in the late 1990s, which severely affected hydro output, undue concentration of private ownership (at times both laterally and vertically), and periods when the independence of the regulator has been questioned. Many of these issues have resonance in other countries and Chile's responses, while maintaining course to attract private investment, will enrich this study of best practices.

49. A possible second case is that of New Zealand, which has achieved high levels of private investment in an ostensibly unbundled system. But it appears to face competition issues due to concentration of ownership at both generation and distribution levels, and indeed cross-ownership between these segments. Regulatory oversight has increased and New Zealand's response to competition concerns, whilst maintaining a favourable investment climate, should be of interest to many smaller developing and transitional economies.

50. These cases should provide good examples of best practices in achieving national economic goals through private investment in this important sector. One lesson is likely to be that great patience and perseverance is needed – over decades rather than years – to achieve satisfactory outcomes.

## IV. ISSUES TO BE ADDRESSED BY EXPERTS

51. In the light of the above, experts are asked to elaborate on the following questions:

(a) Are the challenges identified correctly? Are they key in terms of relevance and importance for developing countries? And what other challenges could you suggest?

(b) What topics would you consider useful in this context?

(c) What do you see as strength and weaknesses of the suggested methodology to be applied for this work so that genuinely useful conclusions can be drawn from the case studies? What are your suggestions for improvements in this regard?

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[12] *Ibid.*, p.199.

[13] An industry expert who was requested by the UNCTAD secretariat to nominate countries exhibiting best practices advised that it would be more appropriate to identify countries with the least worst practices.

(d) How should lessons learned be disseminated and how can they be adopted and/or adapted to country-level application?

(e) What additional "policy toolkits" should be envisioned to assist countries wishing to adopt/adapt these best policy practices?

(f) What is the role of international organizations, including UNCTAD (with respect to policy research, capacity and institution-building to developing countries, and international consensus-building on key investment-related development issues including through exchange of best practices)?

## Annex

## CASE STUDIES OF BEST PRACTICES

**Thematic topics**

(a) How to devise a systematic competitiveness policy for FDI.

(b) How to upgrade efficiency-seeking FDI.

(c) How to attract FDI to small economies.

(d) How to foster the role of FDI in countries with economies in transition.

(e) How to attract FDI in post-conflict countries.

**"Long list" of possible case studies on specific issues**

(a) How to attract skills.

(b) How to use FDI to improve infrastructure – electricity.

(c) How to use FDI to improve infrastructure – ports.

(d) How to attract FDI in higher education.

(e) How to attract more technology-intensive FDI.

(f) How to foster foreign affiliate innovation.

(g) How to attract FDI to the regions.

(h) How to develop strong partnerships with foreign investors.

(i) How to move foreign affiliates into exports.

(j) How to revitalize FDI in export processing zones.

(k) How to use FDI to build a regional hub.

(l) How to attract diaspora FDI.

(m) How to leverage investment promotion in international investment arrangements.

(n) How to manage revenues from FDI in extractive industries.

(o) How to fast-track investment reform.

(p) How to give foreign investors confidence in the commercial justice system.

(q) How to manage competition issues with foreign investors.

(r) How to proactively manage investor-State disputes arising from international agreements.

(s) How to implement a modern FDI entry regulation system.

(t) How to improve work and residence permitting.

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