Improving national and international investment regimes

Against a continued backdrop of shifting economic tides, the development of sound investment policy is at the heart of securing sustainable growth and the wealth of benefits it delivers to communities

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Investment policies – at both the national and international levels – are developing against a constantly changing economic environment and evolving political goals. The key policy challenge is how to make foreign direct investment (FDI) instrumental for qualitative and inclusive growth and to find the right equilibrium between investment liberalisation and regulation for the public good. These are key areas of the work of the United Nations Conference on Trade and Development (UNCTAD) on investment for development as recently confirmed at UNCTAD XIII and the third World Investment Forum (WIF) held in Doha, Qatar, in April 2012.

One key message emerging from UNCTAD XIII is that building productive capacity is crucial for fostering sustained economic growth and inclusive development, including poverty reduction. Foreign investment can make an important contribution – directly and indirectly – to achieving these goals.

However, this contribution is not automatic. A comprehensive policy framework is needed to maximise the benefits of FDI, minimise the risks and ensure that investment policies and measures to achieve other relevant policy goals are mutually supportive. Therefore, policy matters.

Benefiting from investment flows

Policies that focus on education, training, health and nutrition, research and development, and incentives for investments in wealth-creating activities can best prepare host countries to benefit from FDI flows. Enterprise development, including access to finance for small and medium-sized enterprises (SMEs), is equally critical to build up a more diversified economy.

It is also a precondition for integrating domestic firms into international value chains. Also of importance are technology policies aimed at strengthening the know-how of countries and improving their competitiveness.

Industrial policies, in particular in developing countries, can play an important role in triggering dynamic and sustainable development, as they can contribute to job creation, economic clustering and export competitiveness. At the same time, it is important to avoid the negative effects of industrial policies in terms of 'beggar-thy-neighbour' strategies, excessive incentives and a return of protectionist tendencies.

Challenges of investment policy

Sustainable development can also be promoted through specific FDI policies. FDI is encouraged by a stable, predictable and enabling investment climate. However, providing such conditions is not enough. FDI policies face a number of additional challenges.

First, policymakers must decide how best to calibrate FDI. They have the choice to promote, restrict or prohibit it. Recent years show a trend towards a more cautious policy approach by governments, seeking to protect critical infrastructure as well as strategic industries, responding to national security concerns. Other policies have also strengthened the regulation of FDI to safeguard other legitimate policy goals. It is particularly important to avoid having such policies degenerate into protectionism.

Second, there is the challenge promoting responsible investment. It has two related aspects, namely how to encourage 'green' investment through the 'right' incentives for investors, and how to develop a proper regulatory framework that fosters social and environmental objectives. Balancing investor rights and obligations is a key task. Attention is also warranted so that regulation does not become a pretext for green protectionism.

Third, there are challenges related to the international investment regime. While continuously expanding – more than 3,000 core treaties existed at the end of 2011 – the universe of international investment agreements (IIAs) has become highly fragmented and complex, presenting an atomised, multilayered and multifaceted network of treaties.

Investment disputes are proliferating, with arbitration tribunals increasingly making judgements on key domestic policies. Core mechanisms of checks and balances existing in domestic laws, such as an appeals mechanism, are non-existent in international investment treaty practice. Another important deficiency of the current IIA system is that it exclusively focuses on investment protection. It is important that future treaties do more to promote responsible investment.

How UNCTAD helps

It is among UNCTAD's core functions to help policymakers address the manifold challenges outlined above. UNCTAD XIII recently confirmed, clarified and expanded this mandate for the next four years.

In fulfilling its task, UNCTAD's work on investment covers a wide range of activities. In addition to its two core products, the biannual World Investment Forum and the annual World Investment Report, UNCTAD also carries out numerous specific programmes, including monitoring of global and regional FDI trends, national and international investment polices, individual country reviews, capacity-building, investment promotion, intellectual property and enterprise development.

With regard to the challenge of supporting the development of appropriate investment policy regimes in developing countries, UNCTAD has most recently developed the comprehensive Investment Policy Framework for Sustainable Development (IPFSD). This takes a fresh look at investment policymaking and examines the universe of national and international policies through the lens of today's key investment policy challenges.

An oil-station worker in Abuja, Nigeria. In developing countries, industrial policies can contribute to generating jobs and making exports more competitive

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The IPFSD focuses explicitly on the sustainable development dimension. It comprises a set of core principles covering such areas as development strategies, investment protection and promotion and facilitation, corporate social responsibility and international investment agreements. The principles are complemented by guidelines for national investment policies, policy options for the negotiation of development-friendly IIAs, as well as criteria to evaluate policy effectiveness.

The IPFSD leaves national policymakers space to 'adapt and adopt' as appropriate. It can also serve as the basis for capacity-building on investment policy. The framework has been designed as a living document that will be continuously updated based on feedback from policy forums and from work in the field. It will thus provide a platform for open-sourcing best-practice investment policies.

In recent years, G20 activities have gained crucial importance for investment policy making. At their Seoul Summit in 2010, G20 members recognised "the critical role of the private sector to create jobs and wealth, and the need for a policy environment that supports sustainable private-sector-led investment and growth".

Post-summit projects

Several initiatives involving UNCTAD have been launched in the aftermath of this summit, including the development of key indicators for measuring and maximising the economic and employment impact of private-sector investment and a project to identify and promote the best existing standards (developmental, social and environmental) for responsible investment in value chains. The G20 endorsed the International Principles for Responsible Agricultural Investment as developed by UNCTAD jointly with the Food and Agriculture Organization, the World Bank and the International Fund for Agriculture and Development. Equally important is the G20's call upon UNCTAD, the World Trade Organization and the Organisation for Economic Co-operation and Development to monitor policies of G20 member countries with a view to identifying cases of trade or investment protectionism.

Following up on these numerous cases of cooperation, UNCTAD invites the G20 to take an active part in the further development and practical application of the IPFSD. In this context, UNCTAD supports the suggestion of the B20 task force recommendations for the upcoming G20 Los Cabos Summit to establish a working group on investment. Such a working group could contribute not only to identifying and addressing existing investment barriers, but also – and of equal importance – to fostering sustainable and responsible investment. ■

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Liberalising trade: mapping the way ahead

While the troubled financial sector has occupied the minds of the world's leaders, the subject of trade has been neglected. Without adequate attention to the issue, the potential for protectionism increases

By Tu Xinquan, University of International Business and Economics, Beijing

Since the global financial crisis hit in 2008, financial liberalisation has become a 'bad boy' disliked by all governments. Paradoxically, the financial sector has been attracting the most attention and inputs from world leaders simply because it has created the most trouble. In contrast, the trade sector, a long-time contributor to global economic growth, is somewhat neglected. Trade issues and officials are much less noticed than those in finance and banking in the context of the G20. Finance ministers and central bankers convene each year, but trade ministers do not. Nonetheless, the spectre of protectionism never vanishes.

In some sense, trade has become a victim of its own success. Thanks to successive trade liberalisation under the auspices of the multilateral trading system, the world managed to deter economic nationalism and protectionism and to maintain overall openness following the 2008 crisis. Despite the great trade collapse in 2009, world trade contributed to economic growth again in 2010 with a rebound of 13.8 per cent. Meanwhile, protectionist fears, which peaked in 2009, gradually dissolved. Consequently, world leaders felt that with the current multilevel trading system in hand, trade no longer required much concern or attention. Therefore, although the G20 summit always calls for an early conclusion of the Doha Round, trade negotiators in Geneva received no direction or support from their capitals and delivered no substantial offers.

In fact, the world trading system is hardly immune from erosion by nationalism and protectionism. With world trade sharply decelerating with only five per cent growth in 2011 and an even slower 3.7 per cent rise likely in 2012, trade tensions have been mounting since the second half of 2011. According to the recent Global Trade Alert report, initial reports of the incidence of protectionism in the third quarter of 2011 are as high as in the most troubling quarters in 2009. In the first quarter of 2012, according to China's Ministry of Commerce, China has received 17 remedy cases covering $2.6 billion of exports – increases of 88 per cent and 106 per cent respectively.

Another concern is that more conflicts are happening among leading countries. In particular, those governments have intervened in new industrial developments during the crisis with the intention of taking the lead in emerging industries. Many subsidy programmes initiated early in the crisis are now becoming the subject of conflicts. Disputes among China, India, the United States and the European Union (EU) over local content requirements, technology transfers and subsidies in the new energy industry are cases in point. The open world trading system may soon face its greatest test.

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Moreover, macroeconomic conditions in both developed countries, such as the United States and those of the European Union, and emerging economies such as China and India are worsening at the same time. China faces an unexpected simultaneous deceleration in key indicators such as gross domestic product, investment, consumption exports and imports in the first four months of 2012. India's economic growth in the first quarter is also down to 6.1 per cent.

The EU area still sees no growth in the first quarter, while the US economy has grown only 2.2 per cent, also slower than last year. More unfortunately, a difficult economic situation meets a complicated political atmosphere. Several major countries will experience leadership changes, the most significant of which could take place in the United States and China. No matter what the result is, their incumbent governments are facing more domestic pressures. In February, US president Barack Obama created the Interagency Trade Enforcement Center in response to criticism from Republican presidential candidate Mitt Romney over his handling of China, pledging to "bring the full resources of the federal government to bear on investigations… to counter any unfair trading practices around the world, including by countries like China".

Initiatives to liberalise trade

Some might argue that trade has remained a focus of many governments, on the evidence of numerous bilateral and regional free trade agreements (FTAs) that have been signed. These preferential agreements are not necessarily stumbling blocks to multilateralism. Some high-profile regional initiatives have been launched recently, including the Trans-Pacific Partnership and the China-Japan-Korea FTA. If they eventually work out, some economically significant freer trade actions may result. Nonetheless, they cannot substitute for a multilateral mechanism. In particular, it is politically and economically difficult to reach bilateral agreements between major economies where trade disputes happen most frequently. There are no FTAs yet between the members of the G7 and Brazil, Russia, India, China or South Africa – the BRICS countries. Even among the G7 countries, there are only the North American Free Trade Agreement (NAFTA) and the EU.

A container ship prepares to leave port in Tokyo. Understanding the importance of the multilateral trading system is vital to the prospects of global economic recovery

Moreover, bilateral and regional FTAs will fragment the global trade system.

The World Trade Organization (WTO) remains the most efficient and legitimate mechanism of global economic governance. Since major economies have global trade interests, the WTO is the best venue for them to make domestically and internationally balanced trade-offs with their trading partners, especially their extra-regional ones.

The dilemma is one must pay the most in order to get the most. However, politicians are reluctant to make hard decisions. With more than 150 members and a single-undertaking negotiation approach, it is a formidable task to reach consensus in the WTO. The Doha Round is despairingly deadlocked. Undoubtedly, the WTO needs to be reformed to make progress. An applicable model for future negotiations might be the model of the International Technology Agreement, celebrating its 15th anniversary in 2012. Non-discriminatory and non-mandatory sectoralism could be used to conquer the obstacles to liberalise trade in sensitive products.

Nevertheless, before turning to future negotiations, the WTO must conclude the Doha Round. It cannot afford a total failure of this round, which has taken 10 years of constant effort. To avoid that catastrophe, members must accept a partial success. Each member should lower its ambitions in exchange for fewer requests on itself.

Maintaining Doha Round support

Making a deal would already be a victory for the WTO, regardless of whether the deal is big or small. Even a small deal requires political resolutions and contributions from major members. World leaders should focus on the issue for a period of time and delegate more authority to their negotiators. More importantly, they should secure domestic support for, or at least tolerance of, a smaller Doha package. First and foremost, they should go beyond mere rhetoric and invest visible resources and commitments in the multilateral system.

Trade is a microeconomic topic in textbooks. The significance paid to trade in national economic policymaking differs among countries. Top leaders might not keep a close eye on what happens in Geneva. They rarely visit the WTO or get personally involved in trade negotiations.

The G20 members are now all WTO members. They are also the most influential ones. Perhaps the G20 could convene a face-to-face discussion or even negotiation including these top leaders along with their trade ministers and the WTO director-general. A quick conclusion may be unrealistic, but it would be most helpful for these leaders to understand what the multilateral trading system means for the world and themselves, and what they can and should do to revitalise the stalled Doha negotiations.

Jagdish Bhagwati claims that the most important reason for the stalemate of Doha is a leadership deficit, meaning the ignorance of the US of the WTO. But leaders' absence in trade negotiations in major countries might be more harmful. Hopefully, Los Cabos will see the deeper involvement of top leaders of major powers in the priority issue of world trade. ■