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Promoting inward and outward foreign direct investment in the post-coronavirus-disease era

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Note by the secretariat

Summary

Foreign direct investment (FDI) has long been recognized as an engine of growth and development, in particular as it constitutes an important source of financing for development. Many Asian and Pacific countries are increasingly becoming important outward investors. If appropriately leveraged, outward investment could be as important for national sustainable development as inward FDI. However, the coronavirus disease pandemic, among other challenges, has severely disrupted global and regional inward and outward FDI flows.

The present document contains information on how Governments can repurpose inward and outward FDI policies and promotion efforts to make them work for sustainable development in an era in which so many things have changed.

The Committee on Trade and Investment is invited to review the findings and policy recommendations contained in the present document with a view to providing guidance on the current and future work of the secretariat in support of member States in the area of FDI.

I. Introduction

1. The investment landscape in Asia and the Pacific has become increasingly uncertain as a result of emerging global and regional political economic risks, such as increased trade tensions, the retreat from multilateralism and transboundary health risks, as evidenced most recently by the coronavirus disease (COVID-19) pandemic.

2. Together these risks have disrupted foreign direct investment (FDI) flows to, from and within Asia and the Pacific. While inward and outward FDI in Asia and the Pacific reached unprecedented levels in 2018, political and economic uncertainties in 2019 caused contractions in the region's share in

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both global inward and outward FDI. As explained in document ESCAP/CTI/2021/1, the region's share in global FDI inflows dropped from 45 per cent in 2018 to 35 per cent in 2019, and its share in global FDI outflows decreased from 52 to 41 per cent. The COVID-19 pandemic and the ensuing lockdown measures have caused FDI to contract even further in 2020. The value of announced greenfield investment projects from January to August 2020 dropped by 40 per cent from the average over the same period in 2019, while outflows dropped by 26 per cent.

3. With the pandemic still unfolding, investment in 2021 is expected to remain below pre-crisis levels. The outlook for FDI beyond 2021 is highly uncertain and dependent on the duration of the crisis and the effectiveness of policy interventions to stimulate investment and navigate the economic effects of the pandemic, as well as geopolitical and ongoing trade tensions. FDI recovery rates are challenging to predict at this stage because they are dependent on both the rate of recovery within the region and the rate of recovery of countries outside of the region.

4. The road to recovery from the COVID-19 pandemic will be hard and gradual, and it will require a significant influx of resources. FDI will be an especially important resource as public financing will be tight.[1] Getting back to pre-COVID-19 FDI levels will take time as cross-border business ties need to be re-established. In addition, appropriate projects to attract investors and convince them to stay and expand also need to be identified. In the meantime, lower levels of investment will lead to heightened competition for investment among Governments. Even before the crisis, countries were under extreme pressure to substantially raise FDI inflow levels to help to meet their investment needs to achieve the Sustainable Development Goals. The unforeseen and significant drop in FDI caused by COVID-19 has simultaneously intensified these pressures and increased the need for financing.

5. Recognizing this, decisive policy action that ensures that investment is channelled into priority sustainable development sectors has never been more critical. Such action must be taken in consultation with the investment promotion authorities and/or agencies of the region to ensure that they are better equipped to support and secure investments in this new and challenging environment.

6. While the pandemic has hampered investment, it has also provided Governments with a unique window of opportunity to re-examine their approaches to inward and outward investment, with a view towards increasing the contribution of FDI to sustainable development in local and regional economies. Additionally, Governments have an opportunity to incorporate an active role for FDI in their pandemic recovery plans. Some Governments in the region have already started doing this, either by implementing stand-alone measures to support investment or by incorporating FDI directly into their COVID-19 recovery plans. Examples of the latter abound: in Azerbaijan, tax incentives for investment into industrial and high technology parks have been expanded; in China, simplified FDI approval processes have been introduced;

[1] Illustrating this, a forthcoming policy brief from the secretariat highlights the extent to which it is still unclear whether developing countries of the region have enough fiscal space to invest in key sustainable development sectors in the recovery period. Furthermore, the packages that Governments have put together, be they small or large, will considerably increase government debt burdens in the medium term and thereby further limit the resources available for development purposes, thereby underscoring the significance of FDI for these purposes in the recovery period.

in Indonesia, the Government is working to pass the omnibus law to overhaul tax and labour market laws to boost FDI; in Kazakhstan, restrictions on new investor visas have been eased; in Pakistan, a new e-portal to facilitate investment has been introduced; in Uzbekistan, the Government has established a presidential advisory board for investment and created a one-stop shop mechanism to facilitate investment; and in Viet Nam, the Government has expanded the list of foreign and domestic small and medium-sized enterprises eligible for investment incentives. In comparison, Myanmar stands out as one of the few countries in the region in which the Government has incorporated a direct role for FDI in its overarching COVID-19 recovery plan by including procedures for fast-tracking approvals for investment in labour-intensive and infrastructure projects as well as a reduction in investment application fees.

7. The pandemic will have lasting effects on national, regional and global investment policymaking. While the priorities of each country in the recovery period differ, all Governments will have to figure out how to tailor their investment policies so that FDI can be most effectively harnessed to enable economies to get back on the path to sustainable development. Such policies must ensure that FDI is repurposed to target priority sectors for sustainable development. Vigorous efforts to re-energize multilateral cooperation on investment, particularly on matters related to investment governance, must complement national efforts. Multilateral cooperation will be especially important to enabling a path to recovery for the least developed countries in the region.

8. The present document contains a discussion of priority areas for repurposing FDI in the evolving COVID-19 context and recovery period. Section II includes information on investment promotion and international investment governance. Section III contains information on outward FDI and how it can be used by home countries, or source countries, to support sustainable development outcomes in their economies. Section IV contains policy recommendations, and section V, issues for consideration by the Committee.

II. Imperatives for inward foreign direct investment policy and promotion during and after the coronavirus disease pandemic

9. Responding to the pandemic will require bold, multifaceted and novel approaches to attract, retain and facilitate investment. It also requires that Governments in the region take the necessary steps to reform and improve their investment environments. Investment promotion frameworks and strategies must evolve during and after the crisis and be fit to each country’s unique context and needs. Some Governments may need to focus on institutional restructuring, while others may need to focus on revising their incentive frameworks, while still others may need to focus on how to better seize opportunities in specific sectors in which they have a competitive advantage. It is, however, clear that all Governments will need to refocus their priority FDI markets and sectors so that they align with their sustainable development priorities. In practice, this entails identifying and prioritizing projects for FDI in key sustainable development sectors such as renewable energy, education, health, water and sanitation. Furthermore, it is of paramount importance that the reforms and measures implemented now are done so with a view to keeping

them sustained in the post-pandemic period so that the investment ecosystem[2] can be durably improved. Policymakers should consider the following four key priority areas as they revisit and revamp their investment policies and regulatory frameworks: the digital economy, green growth, local and foreign small and medium-sized enterprises in regional and global value chains, and FDI governance matters.

A. Targeting foreign direct investment in the digital economy

10. The COVID-19 pandemic has accelerated the digital transformation globally by altering the relationship businesses and consumers have with digital technologies in a matter of a few months. Measures enacted by Governments to contain COVID-19 have propelled businesses towards digitization and online operations and services as demand for them has grown. Firms that were more digitally agile have adapted to this new environment most successfully, while those that were not have focused on adapting their business models to the new environment.[3]

11. At the policy level, Governments must begin to focus on their digital competitiveness, which will be determined by good digital infrastructure, a digitally skilled workforce and a dynamic environment for technology companies. These elements must be supported by a fit-for-purpose regulatory framework, a national digital economy plan,[4] and a coherent digital investment policy. That last would, for instance, focus on attracting and promoting FDI into digital infrastructure, digital firms, and wider digital adoption within the economy. To this end, the forthcoming second edition of the *Handbook on Foreign Direct Investment Policies, Promotion and Facilitation for Sustainable Development in Asia and the Pacific* can help to guide and support Governments in developing a conducive and coherent digital investment policy to better attract such investment.

12. It is also essential that Governments and administrative bodies such as investment promotion authorities and agencies better leverage digital technology to alleviate the administrative burdens and reduce the bureaucratic hurdles impeding the delivery of products and foreign investment. In practice, this means offering more efficient digital services, in particular with regard to investment facilitation through online one-stop facilities throughout the investment cycle.

13. Lockdown measures have prompted investment promotion authorities and agencies to provide remote investor services through telephone and video conferences, as well as to strengthen their online presence with the provision of necessary information for investors, particularly with regards to policy, financial and regulatory changes related to COVID-19, on centralized, easily accessible online platforms and through social media. In times when the attraction of new FDI may be difficult, the retention of existing FDI is of crucial importance and it makes it clear that investment promotion authorities and agencies need to scale up their online investment services for existing

[2] In other words, the institutional, legal and regulatory environment for FDI as well as the factors influencing the promotion, attraction and retention of FDI, including, among other things, sectoral composition, the types and modes of FDI, the size of investments and the extent to which companies will be encouraged to reinvest, and the absorptive capacity for FDI.

[3] Matthew Stephenson and Nivedita Sen, “How digital investment can help the COVID-19 recovery”, World Economic Forum, 15 April 2020.

[4] Ibid.

investors. While some of the region's investment promotion authorities and agencies have established good practices in this area, including in Malaysia, the Republic of Korea, Singapore and Thailand, many others from developing countries of the region have struggled to offer these services as they lack access to cloud-based or virtual files and investor information.[5] Without such services, developing country investment promotion authorities and agencies will continue to face an uphill battle with regards to retaining existing investors and attracting new ones during the crisis.

B. Identifying and promoting foreign direct investment for green growth

14. The pandemic has provided a unique reset moment in which Governments in the region and beyond have an unparalleled opportunity to create an enduring inclusive, green and resilient path to recovery. Scaling up FDI in the green economy can significantly contribute to this by channelling more investment into sectors such as climate-friendly infrastructure, including renewable energy, energy efficiency, water purification and distribution systems, transport and housing as well as in conservation and the efficient usage of natural resources, and waste management.[6]

15. To leverage this opportunity, Governments must first start by identifying their priority green sectors, and thereafter design and operationalize ambitious, whole-of-society green investment agendas focused on attracting more and higher quality investment in these sectors. Opportunities are abundant in the region, especially in transport infrastructure, power generation, energy efficiency and sewage. There are some small signals that investor appetite is still strong in these sectors; for example, despite overall levels of lower investment due to the pandemic, the renewable energy sector attracted the largest inflows of greenfield investment in the services sector (28 per cent) in the region in the first eight months of 2020.[7]

16. Alongside these efforts, policymakers must ensure that green sectors are further opened for investment by reducing restrictions; implementing clear policy and regulatory frameworks to attract investors and ensure that there is a level playing field for such investments; introducing financial mechanisms to attract green investments; and encouraging more environmentally friendly corporate behaviour. Furthermore, policymakers must work closely with investment promotion authorities and agencies to design coherent and robust strategies to incentivize green investments, as well as to develop a pipeline of strong bankable projects to attract investors. At the same time, investment promotion authorities and agencies must rethink their strategies for investment promotion and adjust them to fit with the priority sectors identified.

17. Paving the road to a green recovery through FDI will require political will, institutional capacity to design, develop and monitor investment in priority green sectors, and regional cooperation. The forthcoming second edition of the *Handbook on Foreign Direct Investment Policies, Promotion and Facilitation for Sustainable Development in Asia and the Pacific* can

[5] World Bank Group, "The initial response of investment promotion agencies to COVID-19 and some observed effects on foreign direct investment", April 2020.

[6] Organization for Economic Cooperation and Development (OECD), *Policy Framework for Investment, 2015 Edition* (Paris, 2015).

[7] ESCAP calculations based on fDi Intelligence. Available at www.fdimarkets.com (accessed on 25 October 2020).

support these efforts.[8] Governments should also consider developing tailored indicators to assess, evaluate and measure the sustainability, or in this particular case, green, characteristics of investments. At the regional level, building resilience in the recovery period will require Governments to work together to attract and channel investment into transboundary, climate-friendly infrastructure. To this end, the Asia-Pacific Research and Training Network on Foreign Direct Investment platform[9] can serve as a regional investment cooperation mechanism to bring Governments together to share their experiences on developing and operationalizing sustainable and green investment policies and frameworks.

C. Support local and foreign small and medium-sized enterprises in regional and global value chains

18. Lockdown measures to contain the pandemic and the accelerated shift towards digital technologies have hastened the reorganization of global value chains. The pandemic has prompted companies to offer more digital services and further automate processes to ensure the speedy delivery of products and services in this new operating environment. Rising digitization and automation, combined with ongoing trade tensions between the United States of America and China, had already been pushing many firms to re-envision the global value chain landscape. Large-scale and widespread demand and supply shocks to global value chains caused by the response to the pandemic have intensified pressure on lead firms to rethink supply chain dependencies and to find ways to make them more resilient. Looking ahead, this may prompt more lead firms to reshore or nearshore critical parts and equipment in the short and medium term.[10] This will have important consequences for value-chain-linked FDI in the region’s economies as well as more broadly for the region’s small and medium-sized enterprises that are both highly integrated into and dependent on value chain networks. Indeed, a recent survey from the World Association of Investment Promotion Agencies indicated that the biggest COVID-19-related concerns of investment promotion authorities and agencies are value chain disruptions and their effects on the small and medium-sized enterprises and the value-chain-linked FDI they support and promote. Short-term risks for small and medium-sized enterprises include the loss of backward linkages to foreign investors that had previously bought parts, components, materials and services from them. In the medium and long run,

[8] Tools developed by the Centre on Green Finance and Investment of OECD, such as *Policy Guidance for Investment in Clean Energy Infrastructure: Expanding Access to Clean Energy for Green Growth and Development* (Paris, 2015), as well as OECD, *Investing in Climate, Investing in Growth* (Paris, 2017), can also serve as additional resources to assist countries in building their capacity design and operationalize green investment frameworks. Furthermore, working to ensure that investors are a part of the United Nations Global Compact can help encourage more responsible and environmentally friendly corporate behaviour from investors.

[9] https://artnet.unescap.org/fdi.

[10] In certain cases, Governments in the region are already encouraging companies to reshore or relocate production. For instance, as a part of its $989 billion COVID-19 economic support package announced in April 2020, the Government of Japan allocated $2.2 billion towards encouraging Japanese manufacturers to reshore production from China. The initiative was initially introduced in 2019 to mitigate supply side disruptions from the United States-China trade tensions, and subsequently incorporated under the COVID-19 recovery plan. See United Nations Conference on Trade and Development (UNCTAD), “Investment policy responses to the COVID-19 pandemic”, Investment Policy Monitor, special issue, No. 4 (May 2020).

this could mean the loss of potential spillovers through the transfer of technology, skills and other human capital.[11]

19. The immediate policy responses of Governments in the region should continue to be targeted on relieving the burden of small and medium-sized enterprises participating in global value chains. Most Governments in the region have extended State support for small and medium-sized enterprises, but it is imperative that Governments focus on local and foreign small and medium-sized enterprises. For instance, financial and fiscal aid targeting both types of firms are critical to keeping supply chains intact in the short and medium term. Such aid could include guaranteed recovery of delayed payments, indirect financing to suppliers through their buyers, tax credits and other fiscal benefits to firms, co-financing of development programmes, and direct provision of financing to local firms.[12]

20. To strengthen value chain resilience in the medium and long term, Governments, together with businesses, should assess their vulnerabilities,[13] particularly to any future risks, and identify opportunities to leverage competitive advantages in key priority sectors that would enable them to integrate more effectively into global value chains and generate more value-chain-linked FDI. The COVID-19 crisis has highlighted that such an assessment must also include an evaluation of the supply of essential goods and, in particular, whether they need to be reoriented closer to home.

21. At the same time, investment promotion authorities and agencies must step up their efforts to support and retain small and medium-sized enterprises' links with existing foreign investors while also continuing to promote value-chain-linked FDI. This includes deploying more and better online tools and services that can support investments, as well as providing investors with up-to-date information on COVID-19 services and incentive schemes.

22. For Asia and the Pacific, global value chain shocks offer an opportunity to expand and better leverage regional value chains. Doing so, however, will depend on scaling up investment, including FDI, to improve digital, transport and trade connectivity. Regional cooperation efforts to attract and channel FDI into enhancing connectivity could be effectively harnessed by utilizing the secretariat's existing Asia-Pacific Research and Training Network on Foreign Direct Investment platform for investment cooperation and knowledge-sharing.

D. Addressing multilevel foreign direct investment governance

23. Reforming national and international investment governance must remain a priority in the current and post-COVID-19 context. The FDI policy response at the national level has varied across the region, with a growing number of Governments introducing restrictive measures on new investment to safeguard domestic capacity in strategic sectors such as the health care, pharmaceutical, medical device and equipment sectors. For instance, the Government of Australia has temporarily tightened its rules on foreign

[11] UNCTAD, "Investment Policy Responses to the COVID-19 Pandemic".

[12] Ibid.

[13] For instance, such an assessment must look at vulnerabilities in planning and supplier networks, as well as transportation and logistics, product complexity, organizational capacity and maturity. See Knut Alicke, Xavier Azscue and Edward Barriball, "Supply-chain recovery in coronavirus times – plan for now and the future", McKinsey & Company, 18 March 2020.

takeovers; the Government of India has implemented FDI screening procedures for investments originating from neighbouring countries; the Government of Japan has introduced investment screening measures in the pharmaceutical and medical devices sector; the Government of New Zealand has implemented temporary changes to investment screening rules; and the Government of the Russian Federation has introduced screening procedures on temporary foreign acquisitions. While these restrictions have all impacted FDI inflows to the region, outflows have also been impacted as key host countries in Europe and North America have also introduced similar protectionist measures in these sectors.

24. These restrictions have added a whole new layer of complexity to FDI transactions. While they may in the short term be in the interest of protecting public health, they must have clear sunset clauses so that they do not hinder investment from rebounding in the recovery period and from contributing to sustainable development.

25. The pandemic is also having significant impacts on international investment governance. Lockdown measures have forced many firms to shut down their activities and delay and/or cancel their planned investments. Such measures call into question the extent to which foreign investors are protected under existing investment treaties and whether they may be able to challenge pandemic-related policy measures through arbitration proceedings. Outcomes of any such disputes would be subject to interpretations of the flexibility of States to enact emergency measures aimed at protecting public health. It is therefore important that Governments in the region prepare for potential disputes while simultaneously ensuring that dispute prevention and management mechanisms continue to be reinforced. To this end, investment promotion authorities and agencies and other administrative agencies involved in investment projects should ensure they are fully up to date on their Governments' international obligations and also maintain an open and supportive line of communication with investors in order to better anticipate any issues before a potential dispute claim may arise.

26. At a broader level, the crisis also provides an opportunity for Governments to step up their efforts to reform the international investment governance regime to make it more fit for purpose, responsive to the sustainable development agenda, and coherent with national investment laws. For instance, reforming international investment agreements to make them more sustainable development-oriented could make a major contribution to helping countries achieve the Sustainable Development Goals.

27. With current delays and cancellations of negotiation rounds due to the pandemic slowing investment treaty making, Governments have a unique chance to revisit and reformulate their international investment agreement strategies. Countries with special needs in particular should utilize this opportunity to build their capacity to formulate a coherent international investment agreement strategy based on their own national sustainable development challenges and priorities.[14]

28. To be sure, reforming the international investment agreement regime with a view to making it more sustainable development-oriented and coherent with national investment laws in the Asia-Pacific region is a formidable

[14] *Foreign Direct Investment and Sustainable Development in International Investment Governance*, Studies in Trade, Investment and Innovation, No. 90 (United Nations publication, 2019).

challenge that requires significant political will. It is a challenge that demands Governments of the region work together to address the reforms needed while simultaneously developing their own country strategy based on national sustainable development challenges and priorities. The Economic and Social Commission for Asia and the Pacific (ESCAP) is well placed to bring the region's policymakers and stakeholders together to collectively develop strategies to implement sustainable development reforms of the international investment agreement regime and to offer its member States FDI policy advisory and technical capacity-building services.

III. Leveraging outward foreign direct investment for home country sustainable development

29. In the previous section, several priority areas that policymakers must focus on to repurpose inward FDI for sustainable development and to ensure that investment governance regimes are sustainable development-oriented were introduced. However, the emergence and growth of outward FDI from Asia and the Pacific demands that due regard also be paid to the role it can play in stimulating positive, sustainable outcomes in home and host countries. This is made even more apparent by the fact that despite overall drops in global shares of outward FDI, Asia and the Pacific has been the largest source of outward FDI globally since 2018.[15]

30. Although a growing number of firms from Asia and the Pacific are becoming active outward investors, policy action to support, facilitate and even promote outward FDI is still needed in most developing countries in the region. The lack of evidence-based research on outward FDI has been a key impediment to developing such policies. More specifically, while there is a rich history of research and evidence to support the importance and development effects of inward FDI on host countries, the extent to which outward FDI can and does yield positive development outcomes in home countries is a nascent area of study, especially in relation to developing countries. There are even fewer studies on the types and combinations of institutions, policies and tools available to policymakers to support and facilitate outward FDI for sustainable development. The lack of evidence-based research on outward FDI is concerning because, among other things, it can be a strategic tool that enables firms to access global markets and integrate into global production systems and value chains, which, in turn, helps firms and industries in home economies to strengthen competitiveness and consequently facilitate more inclusive and sustainable growth opportunities for those economies.

31. Recognizing this knowledge gap, and to better understand the emerging potential of outward FDI, the secretariat, with the support of the region's investment promotion authorities and agencies, has been developing a research and evidence-based policy advisory stream on outward FDI and home country sustainable development since 2018.[16] The following subsection contains information on that work. This is a new niche area of work for the secretariat and a novel area to focus on regarding FDI. Its very novelty means that it would be neither prudent nor possible at this stage to only provide a set of succinct

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[15] See ESCAP/CTI/2021/1.

[16] In the report of the 9th meeting of the Asia-Pacific Foreign Direct Investment Network for Least Developed and Landlocked Developing Countries, member States requested the secretariat to further develop this research stream, including through the development and release of a publication on outward FDI and home country sustainable development. The report of the meeting is available at www.unescap.org/sites/default/files/9th%20FDI%20Network_Report-final_0.pdf.

policy priorities on outward FDI like those in section II above. At the time of writing, most developing countries in Asia and the Pacific have a limited knowledge of how outward FDI can contribute to home country sustainable development and do not have outward FDI policies or strategies. Consequently, the particular challenge they face is how to make outward FDI a part of their broader development strategy, complementing other development policies in areas such as inward FDI and trade. The topic is broadly introduced in order to underscore the importance of developing an outward FDI policy or strategy. Then the topic of how outward FDI can deliver home country effects is addressed. Finally, a menu of options[17] for policymakers to consider when developing an outward FDI strategy is presented.

A. Outward foreign direct investment from Asia and the Pacific

32. Outward FDI stock from developing countries in Asia and the Pacific has grown more than tenfold from $360 billion in 2008 to $4 trillion in 2018. A similar trend is also apparent in outward FDI flows. Between 2008 and 2018, developing countries in the region (excluding China) provided on average $150 billion in outward FDI annually. To understand the importance of outward FDI for developing countries in Asia and the Pacific, it is important to not only consider outward FDI stocks and flows per country, but to also examine the extent to which each country is internationalized through outward FDI by looking at the outward FDI to gross domestic product (GDP) ratios of each country. Some smaller economies rank quite highly by this measure because even when their absolute levels of outward FDI stock cannot match those of the region's largest countries, their outward FDI may still be considerable when viewed relative to the size of their economies (table 1).

[17] The secretariat, together with the World Economic Forum and King's College London, is currently developing this menu of options, therefore only a simplified version is presented in the present document.

Table 1
Developing countries in Asia and the Pacific by outward foreign direct investment as a percentage of gross domestic product, 2016–2018

Rank	*Country*	*Per cent of gross domestic product*
1	Singapore	282
2	Azerbaijan	52
3	Malaysia	39
4	Tonga	26
5	Russian Federation	24
6	Thailand	23
7	Georgia	15
8	Philippines	15
9	China	14
10	Kazakhstan	13
11	Indonesia	6.6
12	India	6.1
13	Turkey	5.5
14	Armenia	5.1
15	Solomon Islands	4.8
16	Viet Nam	4.5
17	Mongolia	4.2
18	Timor-Leste	3.8
19	Cambodia	3.7
20	Vanuatu	2.9
21	Samoa	2.7
22	Papua New Guinea	2.1
23	Fiji	1.9
24	Sri Lanka	1.6
25	Federated States of Micronesia	1.4
26	Lao People's Democratic Republic	0.9
27	Islamic Republic of Iran	0.8
28	Kiribati	0.7
29	Pakistan	0.7
30	Bangladesh	0.1
31	Afghanistan	0.07
32	Kyrgyzstan	0.06

Source: *Outward Foreign Direct Investment and Home Country Sustainable Development*, Studies in Trade, Investment and Innovation, No. 93 (United Nations publication, 2020).

33. Singapore, as a small financial centre with large absolute amounts of outward FDI, tops the ranking. It is followed by Azerbaijan at a distant second place and Malaysia in third place. Large countries with considerable outward FDI, such as China, India and the Russian Federation, blend in with other small and medium-sized economies at varying levels of development, including Georgia, Kazakhstan, the Philippines, Tonga and Thailand. These findings demonstrate the importance of moving beyond country size and development level in an analysis of outward FDI and its implications for sustainable development and investment policymaking.

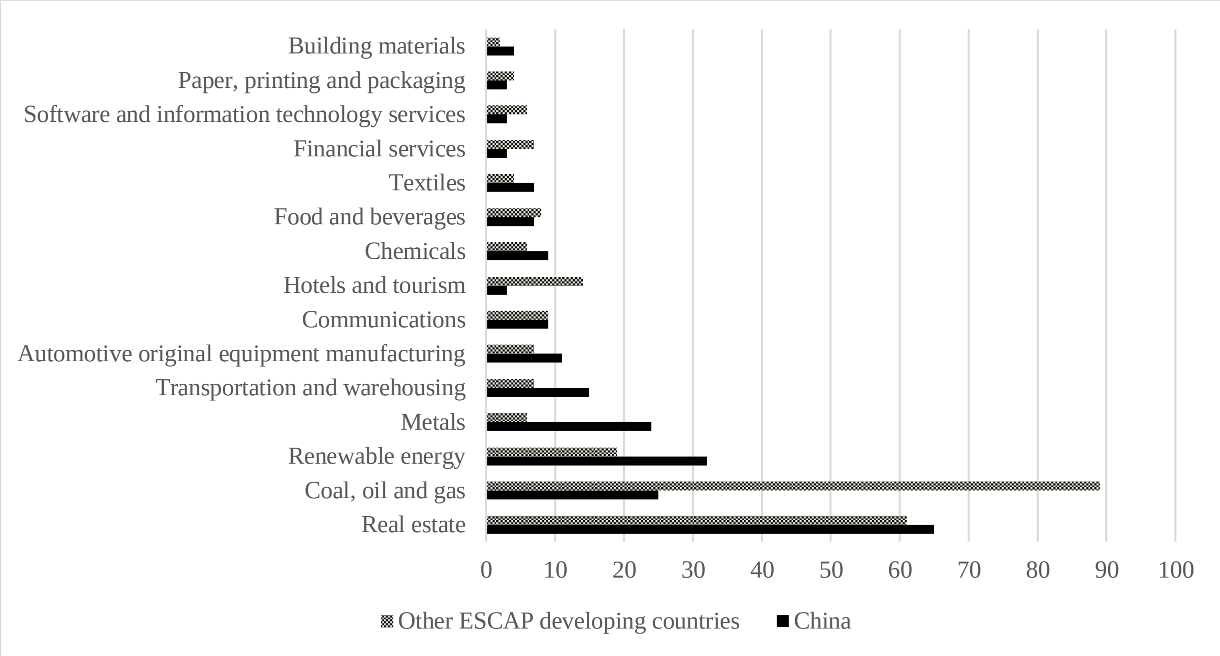
34. Most outward FDI from developing countries in the region has been targeted at developed economies. These economies are attractive investment locations due to the large size of their markets and their leading technologies and know-how. The possibility of acquiring technological, managerial and other specific capabilities in developed economies has provided some firms with opportunities to catch up and reach the knowledge frontier faster than would be possible solely through in-house innovation.

35. When they do invest in developing countries, firms from developing countries in the region tend to invest in nearby countries, highlighting the importance of proximity in investment decisions and offering an explanation for the steady growth in and importance of intraregional FDI flows in the region. With regard to the latter, for example, intraregional greenfield investment accounted for 47 per cent of total greenfield investment in the region in 2019.[18]

36. Market-, strategic asset- and efficiency-seeking are important motivations for outward FDI from developing countries in Asia and the Pacific. Figure I shows greenfield outward FDI from these countries by industrial activity. Manufacturing could indicate market- and efficiency-seeking FDI, while logistics, business services, sales and marketing, and similar activities suggest market-seeking motivations. Extraction is a comparatively small category, while electricity ranks third, after construction. Investments in design, development and testing, and research and development indicate strategic asset-seeking motivations. In sum, the sectoral distribution of outward FDI from developing countries in Asia and the Pacific is diverse, meaning that a variety of home country effects could result from such investments.

[18] See ESCAP/CTI/2021/1.

Figure I
Greenfield outward foreign direct investment from developing countries in Asia and the Pacific, by activity, 2016–2018
(Billions of United States dollars)



Source: *Outward Foreign Direct Investment and Home Country Sustainable Development*, Studies in Trade, Investment and Innovation, No. 93.

37. The sheer scale of outward FDI from the region, its increasingly intraregional character, and its sector distribution underscore the need to explore how these flows can be harnessed to support the achievement of the Sustainable Development Goals, particularly in source countries.

B. Home country effects of outward foreign direct investment and the Sustainable Development Goals

38. Outward FDI can facilitate positive development outcomes in home countries by generating financial earnings, enhancing exports, facilitating more domestic investment, transferring know-how, nurturing innovation, upgrading industries, improving standards, enhancing productivity, facilitating access to resources and tangible assets, generating employment and promoting economic growth. Indeed, the economic and sustainable development areas affected by outward FDI are similar to those affected by the operations of multinational enterprises in host economies – yet the direction of the effect is reversed.[19]

39. Given this association between outward FDI and economic development as well as findings that FDI and the international operations of multinational enterprises have been conducive to achieving the Sustainable

[19] Matthew Stephenson, "Investment as a two-way street: how China used inward and outward investment policy for structural transformation, and how this paradigm can be useful for other emerging economies", PhD dissertation (Graduate Institute of International and Development Studies, 2018).

Development Goals,[20] it is possible to link the Goals to various home country effects.[21] However, in line with the overall literature on investment and development, the Goals in their original conceptualization have focused primarily on the development implications of investments made in an economy (thus including inward FDI), rather than outward FDI specifically. In particular, target 17.5 is aimed at countries adopting and implementing investment promotion regimes for least developed countries.[22] Presumably this was meant to reference inward investment, though outward FDI could in fact be included in the portfolio of activities to maximize the potential benefits from investment promotion. Thus, it is conceivable that outward FDI plays an important role next to inward FDI, though the link between the Goals and outward FDI still requires further specification.

40. Table 2 therefore is an overview of home country effects from outward FDI that have been found to exist, explaining the characteristics of each impact and the mechanisms through which they occur. In total, it lists 10 home country effects plus economic growth as a general consequence of all other effects and links them to the Sustainable Development Goals they can help to achieve.

[20] UNCTAD, "Investment by south TNCs reached a record level: acquiring developed country foreign affiliates in the developing world", *Global Investment Trends Monitor*, No. 16 (April 2014).

[21] Matthew Stephenson, "OFDI and development: policy considerations to leverage a new pathway for growth", in *Towards Sustainable Development: Lessons from MDGs & Pathways for SDGs*, Syed Munir Khasru, ed. (Dhaka, Institute for Policy, Advocacy, and Governance, 2017), pp. 367–386.

[22] *Foreign Direct Investment and Sustainable Development in International Investment Governance*, Studies in Trade, Investment and Innovation, No. 90.

Table 2
Outward foreign direct investment home country effects and the applicable Sustainable Development Goals and targets

Home country effect	*Foreign pursuit*	*Channels*	*Applicable Sustainable Development Goals and targets*
Increased financial earnings	Profits overseas	Repatriated earnings	17.3 (Mobilize additional financial resources)
Higher export earnings and more domestic output	Foreign market access	Export opportunities for home country firms	17.11 (Increase the exports of developing countries); 9.2 (Promote inclusive and sustainable industrialization)
Larger domestic investment	Consequence of financial earnings and improved economic conditions		9.2 (Promote inclusive and sustainable industrialization)
Increased know-how, innovation, number of patents	Research and development, direct know-how acquisition and reverse spillovers	Know-how transfer and subsequent domestic spillovers	9.5/9.b (Upgrade the technological capabilities, support domestic technology development); 8.2 (Achieve higher levels of economic productivity); 7.a (Facilitate access to clean energy research and technology); 12.a (Strengthen scientific and technological capacity); 17.16 (Mobilize and share knowledge, expertise, technology and financial resources)
Improved standards and practices	Adoption from abroad	Implemented at home	12.6 (Encourage companies to adopt sustainable practices)
Industrial upgrading	Greater competitiveness, efficient use of labour force Consequence of increased know-how, innovation, patents and capital goods	Skills upgrade, international competition	9.5/9.b (Upgrade the technological capabilities, support domestic technology development); 8.2 (Achieve higher levels of economic productivity); 7.b (Upgrade technology for supplying modern and sustainable energy services); 12.a (Strengthen scientific and technological capacity)
Productivity growth	Consequence of all intangible returns		8.2 (Achieve higher levels of economic productivity)
Higher resource availability	Acquisition of natural resources	Greater availability or direct transportation to home country	7 (Affordable and clean energy); 9.2 (Promote inclusive and sustainable industrialization)
Improved tangible assets and products	Acquisition of capital goods, machinery etc.	Installation and use in home country factories or businesses	9.5/9.b (Upgrade the technological capabilities, support domestic technology development)
Higher employment and wages	Consequence of other home country effects		8.5 (Achieve full and productive employment and decent work)
Economic growth	Consequence of all other home country effects		8.1 (Sustain per capita economic growth in accordance with national circumstances), 1 (No poverty)

Source: *Outward Foreign Direct Investment and Home Country Sustainable Development,* Studies in Trade, Investment and Innovation, No. 93.

41. While empirical research examining the existence and extent of home country effects of outward FDI is still in its infancy, an initial assessment by the secretariat has confirmed that outward FDI positively impacts GDP, exports, and research and development expenditure in the region's developing countries. For instance, every dollar of outward FDI from the region's developing economies could increase GDP by $8.6 and exports by $5 in the home economies of those countries. Outward FDI can also have an impact on the innovative capacity of developing countries in the region, with every $100 billion spent leading to as much as a 0.725 per cent increase on research and development expenditures as a percentage of GDP.[23]

42. Outward FDI offers promising, untapped potential for helping source countries achieve their sustainable development priorities. It is, however, important to recognize that the strength of home country effects is highly dependent on the context in which it occurs and the characteristics of the investments. For instance, the type, motivation, and mode of entry of outward FDI will affect the extent of the home country effect. Additionally, the strength of the effect in the home country will also be influenced by the absorptive capacity of the home economy.[24]

43. Governments therefore have an important role to play in monitoring and influencing the consequences of outward FDI. Policy and regulations can promote the positive effects of outward FDI while attempting to mitigate any unfavourable effects. For example, Governments play a major role in maximizing the absorptive capacity of countries and their firms through appropriate policies on science, education, the legal environment and other areas.

44. Some countries in the region have begun to recognize this. For instance, the Governments of China, Malaysia, the Philippines, Singapore and Thailand – all countries that have experienced considerable amounts of outward FDI in recent years – have all introduced policies and measures to harness outward FDI for their own development priorities. These Governments have, for instance, reduced and abolished regulatory restrictions on most outward FDI and designated responsibility for outward FDI to specific government agencies. Investment-related services, offering information on outward FDI, matchmaking services and missions to promising investment destinations, are all common in these countries. Some have arrangements in place to provide financial support for outward FDI projects. Nevertheless, there is still scope for further, more comprehensive and strategic approaches to utilizing outward FDI policies and measures for the achievement of positive development outcomes in these countries.

45. On the whole, however, most Governments of developing countries in the region have limited knowledge about the link between home-country measures[25] and positive development outcomes and remain hesitant to introduce outward FDI policies because of their limited knowledge. Many face considerable challenges in developing and implementing a targeted and

[23] Ibid.

[24] It is also important to recognize that while outward FDI can have favourable effects on home economies, it may also have unfavourable effects. For instance, crowding out domestic investment, harming the balance of payments and contributing to currency depreciation, leading to capital flight.

[25] Home country measures are all policies, regulations, measures and institutional adjustments implemented by the home countries of firms that choose to invest abroad in order to manage and encourage outward FDI flows to other countries.

coherent outward FDI strategy that harnesses these outflows to achieve sustainable development in their home country. These Governments therefore face a considerable challenge in making outward FDI a part of their broader development strategy that complements other development policies in areas such as trade and inward investment. Government officials therefore need support in developing and implementing policies and regulatory frameworks to facilitate and guide outward FDI to ensure it contributes to sustainable development.

C. Outward foreign direct investment policy options

46. An overview of the specific options and tools available to Governments to facilitate, promote and regulate outward FDI with the aim of achieving positive development outcomes is provided in figure II. Governments can use this menu of options to develop a tailored outward FDI policy. In terms of sequencing, Governments should first identify which home country effect they would like to achieve and the factors that may influence the extent to which they can be achieved. Next, the most effective home country measures should be identified, as well as whether any specific investments, sectors or companies should be targeted to stimulate these effects. Various combinations of effects-influencing factors, home country measures and targets can be developed in order to tailor outward FDI policies to the specific needs and development characteristics of the home country.

Figure II
A menu of options for Governments to leverage outward foreign direct investment for home country development

Home country effects	Influencing factors	Home country measures	Targeting
• Financial earnings	• Host economy	• Institutions	• Investment motivation
• Export/output	• Investing multinational enterprise	• Regulations	• Investment strategy
• Domestic investment	• Industrial sector	• Services	• Entry mode
• Know-how	• Investment motivation	• Financial support	• Investment destination
• Improved standards	• Entry mode	• Fiscal support	• Investment size
• Industrial upgrading	• Degree of ownership	• Investment insurance	• Company size
• Productivity	• Time since investment	• Treaties	• Company ownership
• Resources capacities	• Policy context	• Operational support	• Company nationality
• Tangible assets / products	• Absorptive capacity	• Maximizing benefits	• Business experience
• Employment	• Transmission channels	• Monitoring and evaluation	• Industrial sector
• Economic growth			• Outward foreign direct investment that would otherwise not occur
			• Realization of home country effects

Source: *Outward Foreign Direct Investment and Home Country Sustainable Development*, Studies in Trade, Investment and Innovation, No. 93.

47. It is possible to build multiple combinations of options across the four categories to develop strategic approaches for outward FDI policy. For example, if the desired home country effect is to enhance export earnings, then greenfield investments, market-seeking motivations and sectors where the home economy has strong, internationally competitive products might be identified as important influencing factors. In light of these objectives and considerations, a Government might put home country measures in place that focus on providing services to help companies to enter overseas markets through greenfield investments. It may tailor its service provision to competitive sectors or focus on small and medium-sized enterprises with

known difficulties in internationalization and foreign market access. When the objective is to enhance domestic know-how, the focus might rest more on full acquisitions in developed economies in sectors where domestic know-how is needed and absorptive capacity is sufficient, with promotion concentrated on offering financial support and matchmaking services. These are just some general examples of how the options in the four categories can be combined to develop appropriate and suitable investment policies aimed at nurturing specific home country effects. There are many possible combinations, and some may work better than others.

48. As many smaller countries in the region are still in the process of introducing and enhancing their policy approaches towards outward FDI, this menu of options might help them to navigate an increasingly important, yet complex area of economic policymaking. The secretariat, together with the World Economic Forum and King's College London, is therefore in the process of developing this menu of options into a novel policy toolkit for maximizing outward FDI for home country sustainable development. This will be the first policy toolkit ever designed for outward FDI and home country sustainable development, and it will be released in early 2021. Of course, it is important that such a policy toolkit is also refined as more relevant findings emerge over time and Governments in Asia, the Pacific and beyond gain further experience with the utilization of home country measures to leverage outward FDI for development.

IV. Policy recommendations

49. The COVID-19 pandemic has accentuated economic and social inequalities in Asia and the Pacific. Appropriate policy responses to the public health and economic emergency can accelerate long-needed transformations towards sustainable development in the region by putting in place the right conditions to attract, retain and bolster FDI that prioritizes sustainable development. Bold, new actions taken by Governments today will set the national development trajectory for perhaps the next decade and longer.

50. Given the considerable uncertainty on the road ahead, however, policies must be resolutely supportive and carefully sequenced if they are to build and sustain a recovery in and across the region's economies. Furthermore, as the crisis is still unfolding, a certain degree of flexibility must be incorporated into any and all revamped FDI policies so that they can evolve and facilitate a sustainable recovery. Therefore, it is recommended that Governments consider taking the actions detailed below at the national and international policy levels.

51. At the national level, Governments must remain open to FDI. In practice this means improving incentives for FDI in priority sustainable development sectors while also removing hindrances to it, as well as introducing sunset clauses into any new restrictive measures that have been implemented in direct response to the pandemic. Alongside these efforts, current FDI policies must be reviewed and revised to ensure they complement sustainable development priorities and enable Governments to attract, retain and facilitate investments to support digital transformation and green growth, as well as to enhance public health-care systems, including the production of medications and vaccines. To this end, simplifying investment processes to ensure openness to and clarity of rules regarding foreign investment, as well as establishing a business climate conducive for investment, will help to mobilize investments that provide the greatest benefits in terms of sustainable development.

52. To support these efforts, policymakers and investment promotion authorities and agencies need to develop the appropriate indicators to enable them to assess, measure and monitor the impact of individual FDI projects on sustainable development, namely the contribution of FDI projects to national sustainable development priorities. The secretariat is currently developing guidelines and templates for such indicators for the three dimensions of sustainable development. This will help countries to target and prioritize specific FDI from specific sources in specific priority sectors.

53. Considering the untapped potential of outward FDI, it is imperative that policymakers focus on designing and implementing strategies and measures to facilitate inward and outward FDI. Indeed, there is much scope for Governments in the region to develop comprehensive and strategic approaches to utilizing outward FDI policies and measures to achieve positive, sustainable development outcomes.

54. At the international level, it is imperative that the negotiation rounds of international treaty making resume and that countries work together to enhance and streamline international investment governance and rebalance investment promotion authorities and agencies to make them more sustainable development oriented. The Asia-Pacific Foreign Direct Investment Network for Least Developed and Landlocked Developing Countries has been brought under the umbrella of the Asia-Pacific Research and Training Network on Foreign Direct Investment platform. Through the Network, the platform has become an important mechanism for discussion and knowledge-sharing among member States on these issues of international investment governance reform.

55. Regional cooperation together with political commitment to keeping countries open to investment and to reforming the international investment governance regime will be critical to helping economies and businesses build back better in the recovery period and harness the potential of regional value-chain-linked FDI. In particular, such cooperation can help to pave the way towards a green recovery in the region, attract and facilitate investments to address transboundary challenges, make national and international investment governance more coherent and sustainable development oriented, and enable countries to more effectively harness intraregional investment flows.

56. Developing countries of the region, particularly least developed countries, will require additional support to develop and operationalize policies, strategies and investment frameworks in line with those mentioned above. While the impact of the COVID-19 pandemic on investment levels in the region has varied by country, countries with special needs undeniably have been hit the hardest because they have a lower capacity to operationalize the same broad economic and investment policy measures to support, attract and retain investments during the crisis and because they are more reliant on investment linked to global value chains, which have been considerably disrupted by the pandemic. Regional cooperation and technical capacity-building support from the secretariat are essential to helping these countries mitigate the negative effects of the pandemic on FDI. The Asia-Pacific Research and Training Network on Foreign Direct Investment platform is an important tool for these countries, especially as it facilitates the sharing of knowledge and experiences with designing and operationalizing FDI policies in support of the 2030 Agenda for Sustainable Development.

57. In addition, given the rise in outward FDI from the region and the increasing significance of intraregional FDI flows, there is a need to broaden investment cooperation at the regional and intergovernmental levels. While

matchmaking services have long been offered by investment promotion authorities and agencies, they are an underdeveloped means for targeting intraregional investment flows, particularly among developing countries of the region, and specifically for investment flows in priority Sustainable Development Goal sectors in host countries. While inward FDI is typically promoted by one agency in a country, generally an investment promotion authority or agency, outward FDI promotion efforts are usually under the purview of several agencies that often do not communicate with each other.[26] Yet, their respective connections and interactions with the business communities within their home economies means that they have a large repository of knowledge of potential outward investors for sustainable investment projects in host countries of the region. Therefore, the Asia-Pacific Research and Training Network on Foreign Direct Investment platform could meaningfully engage and bring together the multitude of actors involved in supporting outward FDI in one country with the inward investment promotion authorities or agencies of another country in order to enable institutions on both sides to better channel intraregional FDI flows into sustainable development projects and ensure a more sustainable recovery from the COVID-19 pandemic. Increased cooperation between FDI institutions in source and destination countries can be a win-win for both sides that enables the region to build back better.

V. Issues for consideration by the Committee

58. In conclusion, the Committee on Trade and Investment is invited to review the findings and policy recommendations contained in the present document with a view to providing guidance on the current and future work of the secretariat on FDI including its work in the provision of policy advice and technical assistance, the development of guidelines for country-specific FDI sustainability indicators and the strengthening of the Asia-Pacific Research and Training Network on Foreign Direct Investment platform to include an investment cooperation function to bring together destination and source countries of FDI in the region in order to continue to support of member States with regard to FDI.

[26] These may include export credit agencies, development finance institutions, special purpose institutions, trade promotion institutions and other line ministries.