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Topic Guide

Foreign Direct Investment

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Section 1 - How can FDI contribute to Economic & Social Development?

1.1 Why do nation states need and promote FDI?

Foreign Direct Investment(FDI) has the potential to impact economic development in a host economy far more efficiently than domestic industry alone.[1] If a country can have substantial and sustainable economic growth, then the means will be at hand to provide for all the other requirements of its people – food, housing, sanitation, and so on. From where will this economic growth come? It is self-evident that it must and will come from the private sector. Governments can do much to facilitate growth, but only in using social, economic and regulatory policies to speed the work of the private sector. However, in most developing countries, the base of indigenous business and industry is too small for even spectacular success to make the step-change required. Whilst some developing countries have some large indigenous businesses (e.g. in agribusiness or extractive industries), most of the existing indigenous private sector tends to be (a) very small in size, (b) often lacking technological and business expertise and (c) not sufficiently focused on overseas markets. Therefore, in most developing countries, the base of indigenous business and industry is too small for even spectacular success to make a significant step-change in economic growth, unaided. It is not only in terms of size that foreign direct investment (FDI) is crucial. The value of FDI to a developing country goes far beyond the value of the capital investment and jobs created – important as these are, there are many other benefits to be accrued:

- The Multiplier Effect. This is the value of new (and often higher) salaries paid to the local workforce of an overseas investor. This results in higher spending in local shops, restaurants and other businesses and, indeed, can lead to the creation of new local businesses and even more jobs.

- Technology and Knowledge Transfer. In most cases, an FDI project will offer some form of technology, knowledge or process transfer, although the extent of this will vary. Whether this technology or knowledge is new to the host country or whether it is similar to previous FDI projects or that already in the possession of indigenous companies is another matter. Using detailed data from Indonesia, Blomstrom and Sjoholm[2] have found that labor productivity is higher in establishments with foreign equity and that there are indeed spillovers into the domestic economy.

  Similarly, Blomstrom and Kokko[3] suggest such technology transfer to occur through various ways such as licensing of a particular technology, supplier networks or

[1] See United Nations (1992) and Aitken and Harrison (1993) on the impact of FDI on the domestic economy; De Gregorio (1992) provides empirical evidence on the impact of FDI in comparison to domestic investment

[2] Blomstrom and Sjoholm (1999)

[3] Blomstrom and Kokko (1996)

subcontracting arrangements, or indirectly as knowledge becomes public, and spillovers are adapted by the domestic sector. In terms of the supply chain, whilst international companies may import a lot of raw materials and components, they will be nevertheless open to sourcing these locally, where possible. This is in the interest of both the overseas investor and the local economy. Whilst it may take some time for local supply chains to maximize the potential of supplying the major company, from the outset there will be opportunities, even if it is only supplying local catering or cleaning services.

Caves[4] discusses the 'demonstration effect' whereby local firms learn better management techniques or develop co-ordination economies as a result of exposure to FDI and MNCs. However, the degree to which this will "spill over" into indigenous companies or add to the skill set of the workforce or the wider economy is not clear. One of the ways this can happen is through *Spin-outs*. In the longer-term in many cases, there is the potential of "spin-outs" and "spin-ins"; when parts of the investor's processes outsourced to local businesses who have acquired the necessary expertise (often through initially working for the overseas company).

- Access to Capital. Unlike many indigenous companies, particularly small ones, FDI projects are normally fully funded by the MNC. Many MNC have access to financial resources that host-country firms may not have, by virtue of their large size, reputation[5] and financial strength. MNCs invest in long-term projects, taking risks and repatriating profits only when the projects yield returns. As a Xiaolun Sun[6] points out FDI, '...is essentially equity investment. Profits are repatriated only when a project yields return and part of the profits is routinely reinvested in the host country'. Therefore, she adds, 'FDI not only adds to external financial resources for host country development, it is also more stable than other forms of financing. Typically, FDI is based on a long-term view of the market, the growth potential and the structural characteristics of the recipient countries. It is thus less prone to reversals in adverse situations than bank lending or portfolio flows'.

  In addition, as Jenkins and Thomas[7] argue, FDI also contribute to economic growth by crowding in additional domestic investment. By building on the success and lead of one investor, in the form of technological and capital accumulation, it is often possible for the host country to attract other investors in the same sector[8] (agglomeration) and, indeed, to begin to generate indigenous business in the same sector (clustering). This produce very significant sectors of technological excellence, even in peripheral locations (one example of this is the cluster of major medical technology companies in Galway, Ireland).

[4] Caves (1996)

[5] Hill (2000)

[6] Sun (2002)

[7] Jenkins and Thomas (2002)

[8] Cantwell (1989)

There is also the substantial annual revenue from taxes paid to the host country by the overseas company and its employees – even if such taxes are held to a minimum as an incentive for investment. Similarly, with good investment *Aftercare* by the host country (usually through its investment Promotion Agency - IPA), there remains the prospect of Reinvestment – either an expansion of the existing operation or the introduction of a new one by the same company. In this way, although most FDI projects have a finite lifespan, the presence of an investor can be extended almost indefinitely.

- Macroeconomic Benefits. Many FDI companies will be interested in using the operation based in the host country to create products or services for its regional or worldwide customer base. This will have the obvious and welcome effect of improving the host country's trade balance and providing wealth and jobs which are *incremental* – i.e. they are a net addition to the host country's economy, rather than displacing existing businesses in the local economy.
- Creating an Investment Brand. Through the presence of major overseas companies, the host country may begin to create and expand its international business and trade connections, to positively build its image and to develop a Brand for investment.

FDI provides scale and size lacking in indigenous economies. Large companies have the power to induce significant economic growth by providing incremental employment, by earning major external wealth through exports, by facilitating technology and knowledge transfer and by providing supply chain opportunities. This makes possible the proliferation of small companies, most of which are directly or indirectly dependent on the presence of the major companies. In developing countries, the problem is not that most private companies are small – it is the relative absence of large companies and, indeed, often the absence of SMEs as well. This is not to say that other fields of economic development – such as small business development, entrepreneurship, microfinance – should be neglected in favour of FDI. On the contrary, successful promotion of FDI, for the reasons outlined above, will also boost development in all areas of the economy of a developing country. An empirical study based in Belgium by Backer and Sleuwaegen[9] suggest that while FDI may 'crowd out domestic entrepreneurs through their selections in product and labour markets… the effect may be moderated or even reversed in the long run due to positive effects on FDI on domestic entrepreneurship as a result of learning, demonstration, networking and linkage effects between foreign and domestic firms.' In the economies of most countries in the developed world, removal of all large-scale businesses would leave an almost insuperable problem of achieving any kind of growth whatsoever and would especially be the case if a country divested itself of all foreign direct investment. It is important to note here that, even in developed countries, most private sector employees work in small companies. For example, in the UK, the

[9] Backer and Sleuwaegen (2002)

distribution of enterprises by employment size shows that 88.7 per cent firms employ less than 10 employees, while 99.0 per cent have less than 50 employees[10].

FDI Promotion can also serve as an effective social policy tool. By providing people, in particular young people, not only jobs but also an opportunity for a challenging career and an increased stake in their society, FDI may also aid social cohesion. This is especially true in fragile and conflict-affected (FCAS) states. This view is supported by UNCTAD[11] in their study of post conflict Mozambique and Croatia 'Development aid alone cannot transform damaged economies, and it is here that FDI can be a valuable tool for economic recovery and restoration.' Similarly, a review of World Bank Group[12] projects in FCAS countries and FDI flows support the conclusion that 'investment promotion can have a meaningful effect… recovering economies can tap into the benefits of FDI and globalization in spite of their difficult circumstances.' FDI must also be accompanied by strong measures by the host country to ensure that the benefits of investment promotion are disseminated as widely as possible: for example, that there are open and transparent Human Resource policies ensuring jobs do not go exclusively to a favored or elite group but instead, inclusive of all groups in society, ensuring balance of disadvantaged groups and, most especially, women. Policies must also ensure payment of fair and attractive wages and provide opportunities for career development. In fact, an empirical study by Martinez and Allard (2009) conclude that socially inclusive government policies have a positive effect on a country's ability to attract foreign direct investment[13], although whether this is direct cause and effect is arguable – countries which have better social and employment policies also tend to have better economic ones. As Balasubramanyam[14] suggests, the preconditions necessary for attracting FDI into a host economy (such as its policies and business environment) are also the ones which determine its efficacy in promoting growth and development objectives.

Success in attracting FDI will depend on a country or region's ability to provide the key investment elements sought by most potential FDI investors, especially in relation to labour market, infrastructure and operating costs. However, whilst a good investment climate and business environment are essential for FDI, the benefits of these must be pro-actively promoted – this is the main role of the Investment Promotion Agency (IPA). In addition to strategically and pro-actively targeting sectors and markets and outreaching to individual potential investors, a good IPA will engage in international marketing, will provide an excellent service to investors (information, direct assistance, advice), will facilitate and generate successful FDI projects, will develop industrial clusters and will provide on-going investment management and investor aftercare. "Best in class" IPAs –

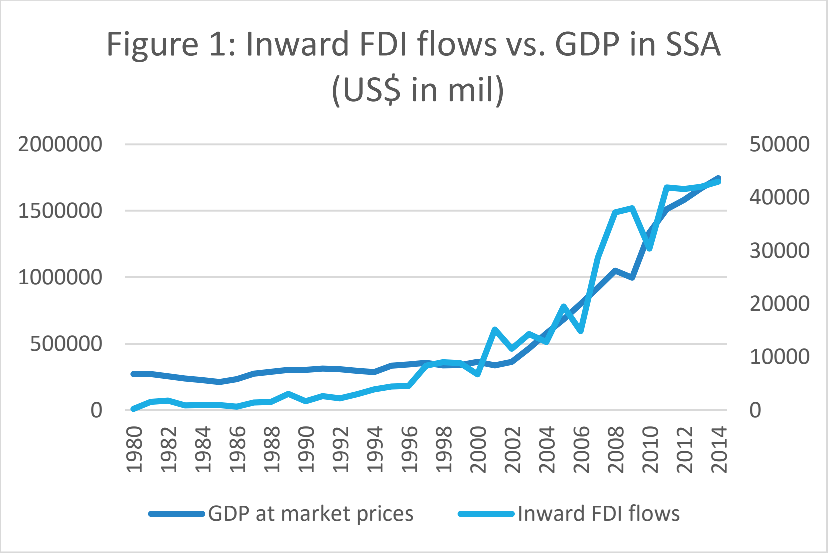
[10] Office for National Statistics, UK
[11] UNCTAD (2009) - See Annex C on and the case study for Mozambique
[12] World Bank Group (2014) Investment Climate – Investment Promotion
[13] Martinez and Allard (2009)
[14] Balasubramanyam (2001)

IDA Ireland, Czech Invest and Scottish Enterprise are examples – will also develop a positive and valuable brand, closely linked with the investment brand for the country.

1.2 The role of FDI in overall economic development

Although the literature is divided and ambiguous on this point[15], it is not necessarily the case that FDI will always have a significant impact on economic growth. Much depends on the type of FDI concerned *(see Section 2)* – and on this point the data is often undifferentiated. However, provided that FDI passes the five key tests (elaborated in 2.3 below), particularly additionally, is appropriate for the host country, has a significant export focus and, ideally, offers technology or knowledge transfer, it should have a strong positive impact on economic growth.

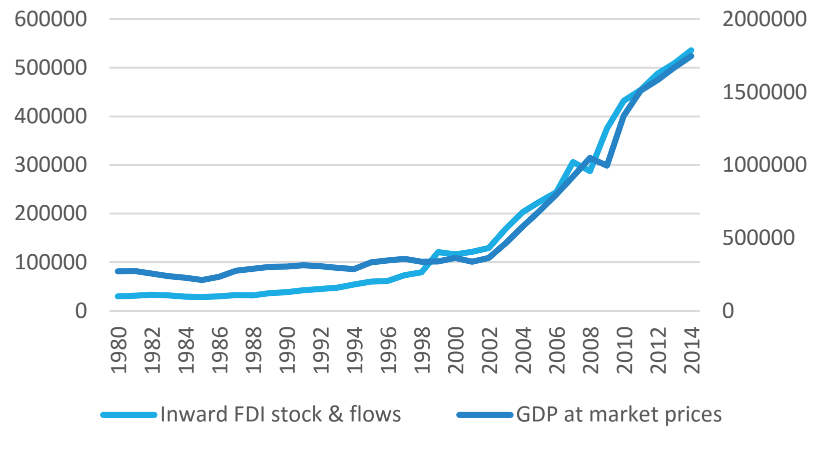
The relationship between FDI and economic growth can be difficult to quantify – but not impossible. If we look at the relationship between FDI and GDP growth, we can see not an exact correlation, but an unmistakable relationship. This is most evident where we look at developing countries where the picture is less skewed by the presence of a large indigenous private sector or a large existing FDI stock. For example, Figures 1 and 2 below compare inward FDI stock and flows against GDP in Sub-Saharan Africa between 1980-2014[16].



[15] See Hansen (2001) for a review of key literature and evidence on FDI and economic growth

[16] Data Source: UNCTADstat and WB Data

Figure 2: Inward FDI Stock & Flows vs GDP in SSA (US$ in mil)



Of course, the relationship between FDI and growth cannot be one of 100% correlation, as other factors must and do also affect growth. For example, a poor investment climate will inhibit FDI, but will also act against other fundamentals of an economy – such as exports and indigenous business growth. However, the importance of FDI as a major contributor to growth, amplified by the multiplier effect is quite evident and this is a view also shared by UNCTAD[17] '...economies with high investment rates tend to achieve higher growth rates...'. Similarly, Balasubramanyam[18] suggests, FDI is not a panacea for development, but a catalyst for growth.

Academic literature indicates the efficacy of FDI on economic growth to be directly linked to the 'absorptive' capacity of the host economy. In their statistical analysis on the effect of FDI on growth in developing economies, Blomstrom et al[19] conclude the need for a threshold level of human capital (education and labour participation) and a certain level of development to be in place in the host countries for the growth enhancing effects of FDI to take place. Empirical studies by Borensztein et al[20] conclude the importance of absorptive capacity, in the form of human capital (education) and advanced technologies, in the ability of host countries to maximize the benefits of an FDI. Similarly, Durham[21] highlights the importance of financial or institutional development of the host economy.

From a practical perspective, however, particularly for developing countries, one of the key determinants of absorptive capacity will be the strength and flexibility of the labour market. Key factors in this will include: Is there a likelihood of the project

[17] UNCTAD (1997)
[18] Balasubramanyam (2001)
[19] Blomstrom et al (1992)
[20] Borensztein et al (1998)
[21] Durham (2004)

recruiting a sufficient workforce (including any skills, experience, which may be required)? And, if so, will it do so without negatively impacting on existing employers? In most developing countries there tends to be high unemployment or under-employment, so it is likely that this would not be a problem, unless the project is seeking skills which are in short supply there (which is unlikely because the country would most likely be in an investor shortlist after a careful assessment of the available labour market in the first place). If one impact of the project is to attract workers from other employers or sectors, this is not necessarily a negative, providing the country has overall high unemployment or under-employment. In such case, a *food chain* may apply in the labour market (i.e. the best qualified workers take the new FDI jobs, which in turn releases their jobs for others, and so on). Even where formal unemployment is relatively low, there may still be absorptive capacity, because of hidden reserves. These are people who are included in the working population, but are not necessarily classified as either "employed" or "unemployed". One key example is married women who are potential returners to the workforce. Other examples may be retirees or people who are redundant from declining industries who could be re-trained. The real problems with absorptive capacity are likely to come when the labour market has over-heated (generally, or within particular sectors) and recruitment is likely to be difficult. However – and this is one example where the worlds of academia and FDI practice diverge – this does not necessarily stop a location being attractive to FDI investment. On the contrary, the fact that large numbers of people are already employed in a given sector may actually be a major attractor.

One symptom of lack of *Absorptive Capacity* is *Labour Attrition*. High rates of labour attrition, particularly within a given sector, is a clear indicator of lack of absorptive capacity. In such cases, an IPA may refine its strategy to stop attracting such investment or to introduce crash training measures, or to re-focus on higher-value-added employment. Business Process Outsourcing (BPO) is a key example of issues of absorptive capacity. The rule of thumb is that, if BPO employment in a city exceeds 3-5% of the workforce, then there will be issues of recruitment and attrition.

1.3 FDI trends and the growing competition for investment

Two of the major sources of information on FDI flows and trends globally are UNCTAD and FDI Markets; however, figures they provide may vary according to which investments are included, data sources and the quality of information available from companies and host countries. According to UNCTAD 2016[22], global FDI flows have reached their highest level since 2007 to an estimated US$1.7

New Heights in FDI inflows

Global FDI	***Developing countries***
US$ 1.7 Trillion	US$ 741 Billion

Source UNCTAD 2016

[22] UNCTAD (2016)

trillion. FDI inflows into developing countries also reached a new high of US$ 741 billion. In the 24 months leading to January 2016, FDI Markets show a total of 25,829 FDI projects, representing a total capital spend of $1,344.31bn by 14,586 companies, creating 3,911,970 jobs[23].

Total FDI projects	**Total Capital spend**	**Companies engaged**	**Jobs Created**
25,829	$1,344.31 Billion	14,586	3,911,970

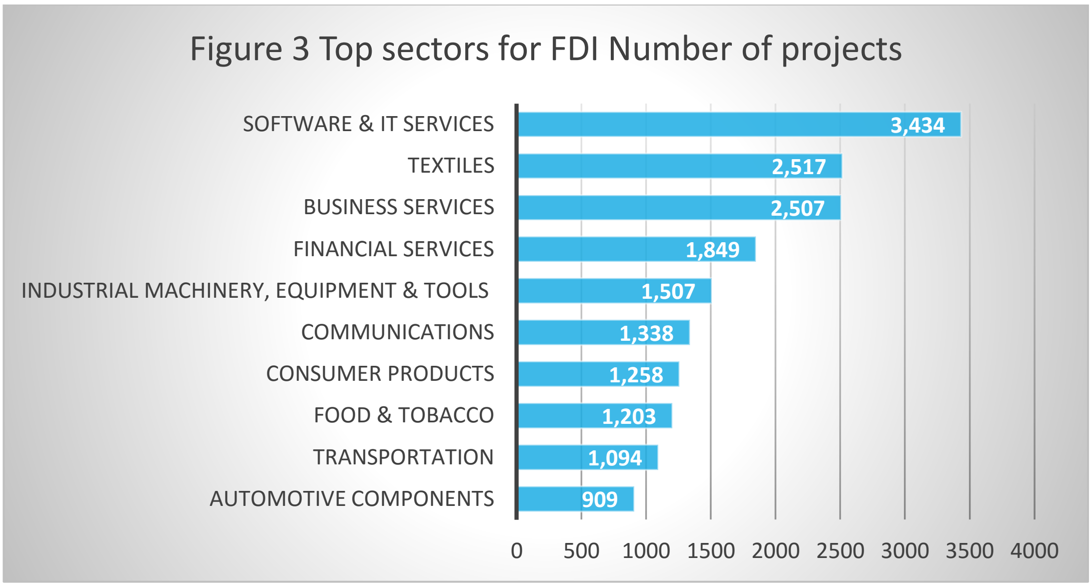
Source: FDI Markets Jan 2014-Jan2016

The top source and destination countries for FDI tend to be fairly consistent. UNCTAD list the top destination countries for FDI as the USA, China (including Hong Kong), Netherlands, UK, Singapore, India, Brazil, Canada and France. For most countries and regions, FDI Markets list the top sources of FDI as the USA, UK, India, France, Germany, India and China. Although the order will vary depending on the country or region examined, the USA remains globally the main source and destination for FDI (with China challenging strongly as the top FDI destination).

Top FDI Sources	**Top FDI Destinations**
USA	USA
UK	China (including Hong Kong)
India	Netherlands
France	UK
Germany	Singapore
India	India,
China	Brazil
	Canada
	France
Source: FDI Markets 2016	*Source: UNCTAD 2016*

Figure 3 below lists the top sectors for FDI as indicated in FDI Markets during the two-year period leading up to January 2016. Of note is the fact that services account for 58% of the top 10 FDI sectors - a trend which has been prevalent over much of the last three decades; however, whilst service sectors are predominant in FDI going to developed countries, manufacturing tends to remain more significant for developing economies.

[23] FDIMarkets.com



The promotion of FDI is a highly competitive business and competitiveness is growing annually. This is a factor IPAs in developing countries very frequently fail to understand, usually to their detriment. Such IPAs tend to view the location of FDI in their country from their country's point of view, rather than that of the prospective investor. One of the most important lessons which must be learned by an aspiring IPA which hopes for FDI success is that investors *always* have a *choice*. This applies in particular to FDI, but is equally applicable to all forms of private sector investment. In considering *Mobile Greenfield FDI*[24] a typical investor may be considering anything up to 10 or 12 potential locations for the investment. However, even where there are no direct alternative locations in other countries being considered – unusually for *Mobile Greenfield FDI* but more likely with indigenous private sector investment – the investor will always have a choice to proceed with the investment or to do other things with the investment capital. If an IPA is too involved in administrative, regulatory or inspection processes (e.g. dealing with investment licenses), it may fail to realise that worthwhile FDI must be sought after and won.

It is important an IPA and its host country develop effective strategies to stand out from the crowd. As a clear illustration of the competitive nature of FDI, the World Association of Investment Promotion Agencies (WAIPA) in 2013 had 170 Members from 130 countries. As most FDI will be likely to locate within a given region (although not always), no IPA is likely to have 170 – or even 130 – competitors. It is, however, likely to have anywhere between 5 and 20 other countries or regions competing for the kinds of FDI projects it is seeking to win. It is highly unusual if a prospective investor with a mobile greenfield FDI is not actively considering multiple alternative locations. It is for this reason that activities such as international marketing, image building, brand development, investor targeting and investment generation are vital if an IPA is to enjoy

[24] Described in Section 2

any degree of FDI success. Given the degree of competition for investment, even with expertise and experience in these areas, an IPA will find competing for desirable FDI projects a challenging and exhausting task; however, any IPA without such skills and knowledge is very likely to find its mission well-nigh impossible.

1.4 Main types of IPAs

There are various types of IPAs and these may be differentiated by geographic focus, by function, by scope and by resourcing.

Geographic focus. IPAs may have a national or regional focus. The most common are *National IPAs* which serve the entire state. As discussed above, the World Association of Investment Promotion Agencies (WAIPA) in 2013 had 130 national members; this means that around 76% of countries have a national IPA[25]. However, WAIPA has a total of 170 members which means the remaining 40 members are *Regional IPAs*. However, it would be misleading to think of these as necessarily smaller or weaker than national IPAs; in fact, some regional IPAs can be larger and better resourced than many national IPAs. For example, the trade and investment organizations for Scotland, Wales and Northern Ireland respectively, the Scottish Development International, Wales Government and Invest Northern Ireland each have their own structures, investment promotion policies and operations, substantial budgets and wide overseas representation. Each of these is larger than most IPAs in developing countries[26]. Some city governments – notably in the UK and the US – also have significant investment promotion functions.

Function. IPAs may have various functions. Some IPAs only have the function of promoting investment, whilst others have a broader role, most commonly also promoting trade and exports. Others function as full *Economic Development Agencies*, including the development of local business development, entrepreneurship, trade, training and research and development. Such a structure offers obvious synergies in areas such as supply chain development, investment aftercare and reinvestment and offers a more streamlined approach to sector development. In some cases, the functions of an IPA may be combined with the economic planning functions of a central government department.

It is important for IPAs not to function principally as administrative bodies. In some developing countries, the work of an IPA is focused around investment licensing, where investors must obtain a licence to gain the full benefits offered by the country or, sometimes, to be able to invest at all. This may tend to incline the IPA to focus on

[25] Based on the normal World Bank Data Set complement of 183 countries. However, it should also be noted that not every IPA is necessarily a member of WAIPA.

[26] Although investment promotion is carried out by the devolved governments, the United Kingdom shares a strong IPA. The United Kingdom Trade and Invest (UKTI) works with local businesses to ensure their success in international markets, and to encourage the best foreign companies to invest in United Kingdom.

administrative and regulatory issues rather than engage in pro-active investment promotion, with detrimental results. The *World Bank Group's Global Investment Promotion Benchmarking 2009* report noted that weak investment promotion is correlated with whether the same government agency is also responsible for investment regulation and argues that the two functions should be kept separate[27].

Scope. Classification by scope includes those IPAs which have a: i) National Focus; ii) Regional Focus; iii) Continental Focus; iii) Global – Selective; iv) Pan-Global Focus. Whilst some smaller IPAs confine their promotional target markets to countries immediately adjacent, most have at least a regional (e.g. the Gulf region) or continental (e.g. Europe) focus. Many have specific target markets throughout the world – for example, all of the IPAs in the UK / Ireland target the British Isles, the United States and parts of Europe, the Middle East and Asia. They do this because they wish to target limited resources in the markets where they stand the best chance of securing investment. Some national IPAs – such as UK Trade and Investment (UKTI) have a truly pan-global presence and operate in virtually every country in the world; however, even UKTI will focus most of its resources for investment promotion (trade promotion is somewhat different) on locations where it perceives the greatest opportunities.

Resourcing. The vast majority of IPAs are funded by national, regional or local governments; however, there are some exceptions. Possibly the most significant potential source of additional funding for investment promotion may be offered by the private sector. This is a model used in other parts of the world, where a range of private sector companies provide part – or, sometimes, all – of the financial resources to attract FDI. It is a model used by a number of cities in the United States of America (for example, Metro Denver, Northwest Ohio, Greater Phoenix, Wisconsin, Ohio State and Arizona State). In structuring these models, it is important to establish mechanisms to minimize conflict of interest and inefficiencies in raising and managing private sector funding inputs. Such private sector funding participation may be through a PPP arrangement, through contributions to a common investment promotion budget managed by government or by funding specific activities – for example, advance factory real estate development. There are a number of reasons why private sector companies may be interested in providing resources to aid investment promotion. Funding may be provided, particularly by multinationals, within a programme of social responsibility / social investment. It may also be provided by large companies who have a vested self-interest in seeing a country's economy develop through increased foreign investment. However, the clearest reason for private sector resource participation arises from companies which will view prospective investors as prospective customers; such companies may include real estate developers, telecommunications companies, recruitment agencies, etc. Again, such funding may be provided as a direct budget contribution or may take the form of funding specific

[27] World Bank Group (2011)

programmes aimed at enhancing FDI promotion – such as funding outward missions, investor visits, business park development, loss-leading training programmes and so on.

A small minority of IPAs are expected to be self-funding, for example, TajInvest in Tajikistan. This is rarely successful as it tends to focus the IPA away from promoting investment and towards earning fees (e.g. by providing information to potential investors). It also runs contrary to the ethos of marketing and investor targeting; it is difficult to persuade a company to invest whilst at the same time attempting to levy fees.

Section 2 - Is all FDI equal?

2.1 Main types of FDI

All investment is not the same and neither is it of equal value to the host country. That all investment is the same is a common misapprehension amongst some developing country IPAs. All investment activity tends to be lumped together and treated in the same way; this may be the result of a history of having a centralised economy, of over-control by the host country government, of lack of awareness of the global investment market and/or of limited experience in dealing with major private sector investors.

Broadly speaking, some of the major forms of investment activity are:

- Public Sector Investment. Investment which is made directly by government and is generated from taxation or other sources of government revenue.
- Public-Private Partnership. A contractual arrangement between a government agency (federal, state or local) and a private sector entity to share the skills and assets of each sector - and also to share the risks and rewards - in delivering a service or facility for public benefit[28].
- Public Sector Contracting. Government tenders for specific work to be undertaken by a private sector entity and pays for the same accordingly. (This is sometimes confused by developing IPAs with 'real' investment – *see Section 2.5 Buyers and Sellers.*)
- Indigenous Private Sector Investment. Private sector investment which originates and is owned entirely or mainly from within the host country.
- Local / Overseas Joint Ventures. An enterprise which has a significant ownership by both internal and external investors.
- Foreign Direct Investment (FDI). FDI is capable of many definitions. One of the most relevant is from the Financial Times[29] which defines FDI as '*investment from one country into another (normally by companies rather than governments) that involves establishing operations or acquiring tangible assets, including stakes in other businesses*'. The definition also distinguishes FDI from portfolio foreign investment (the purchase of one country's securities by nationals of another country) by the element of *control*. This is an important qualification, as the value of FDI to a host country involves not just the transfer of capital or ownership, but also the transfer of knowledge, access to markets, technology and so on.

There are numerous types of FDI and the type of FDI in question is relevant to the relative value of each to an economy and its desirability to a host government. A

[28] Based on definition from the US National Council for Public-Private Partnerships
[29] Financial Times Lexicon <lexicon.ft.com>

widely used classification provided by John Dunning[30] is based on four main investor motivations for FDI - resource seeking, market seeking, efficiency seeking and strategic asset seeking – described in further detail below:

- Resource Seeking. This type of FDI seeks to gain access to factors such as natural resources, low cost labour or specialized labour available in a host country. It generally produces goods (often raw materials, such as hydrocarbons) for export, but bears the dangers, for the host economy, of creating reliance on a single commodity, exposing it to volatility in commodity markets. An example of this is Iraq where it is estimated that up to 95% of Iraq government revenues come from hydrocarbons[31] and the recent fall in the global oil price has posed serious challenges to the country's fragile economy.
- Market Seeking. This type of FDI seeks to penetrate new markets and is driven by the current or potential size of the host market. The size of the host market is also determined by existing or future agreements in the region, such as, regional, preferential and bilateral trade agreements with other countries. The principal difficulty in relation to this type of FDI is that, by targeting the indigenous market, questions are raised as to additionality and the overall value of investment which is not export-related.
- Efficiency Seeking. This type of FDI aims to become more efficient in international production where the investor rationalizes existing operations on a product or process basis. Such FDIs are successful where cross-border markets are open and well developed or where regionally integrated markets exist. This type of FDI is usually mobile and is usually focused on markets outside that of the host country, thereby focusing on exports and is therefore often the most valuable form of FDI to the economy of the host country.
- Strategic Asset Seeking. This type of FDI occurs when companies undertake investments, acquisitions, joint ventures or alliances to promote their long-term strategic objectives. It may take the form of mergers and acquisitions to acquire strategic assets in another country, including brands, specialized labour or technology and distribution networks. This type of FDI provides the opportunity for domestic industry to link to global production chains and markets. However, it may not have the result, as least in the short-term, of creating additional wealth, exports or net new employment.

2.2 Why not all investment supports economic growth

One of the most important tasks in investment promotion is to ensure that investment targeted and secured is appropriate for the host country; not all investment is beneficial for countries nor will it result in significant economic growth. This section will discuss

[30] Dunning (1993)

[31] National Resource Governance Institute <resourcegovernance.org >

the potential impact of the four types of FDI on the host economy and highlight that IPAs should seek out or select Efficiency Seeking investment for reasons discussed below.

A host country with significant natural resources will naturally engage in Resource Seeking investment; however, the host country should ensure that such investment offer maximum benefit to the economy. These include measures such as ensuring production sharing is at a fair and acceptable level, that investment includes up-to-date extractive technology and so on. Where there are significant revenues from Resource Seeking investment, it is important that these are used wisely, in particular to diversify the economy and to develop other sectors. As UNCTAD[32] suggests "in the primary sector, the scope for linkages between foreign affiliates and local suppliers is often limited.... "

Market Seeking investment, if is aimed purely at selling products or services into the host country's market, may not be desirable in terms of job creation or any of the other benefits described in Section 1. However, where the investment plans to manufacture some or all of the products it plans to sell into the host market, the situation is more complex. If the overall effect of the investment will be to make and sell products which would otherwise be imported, then a possible (and, sometimes, significant) benefit can accrue through Import Substitution. Export orientated FDI has more of a positive effect on growth than import substituting FDI[33], because the latter may not offer the same access to knowledge and technology transfer and to global markets. However, true import substitution can provide benefits of net additional real jobs, improve the host country's balance of payments and, indeed, have an overall effect similar in many ways to export-focused investment.

The motives behind Strategic Asset Seeking investment may not be obvious. On the one hand, it can provide a significant boost to a host economy, for example, through a MNC acquiring a major local company, thereby introducing new technologies, new markets and possibly better management practices. On the other hand, IPAs should beware of Strategic Asset Seeking investment which intends to asset-strip its acquired local company or to gradually move production elsewhere; however, the IPA will not necessarily have control or even significant influence over this.

Most successful IPAs tend to focus on, prioritise, seek and target Efficiency Seeking FDI. It is this type of investment which is most likely to be export-focused, to provide knowledge and technology transfer, to introduce new sectors into the host economy and to pass the test of *Additionality*. Efficiency seeking FDI can also be described as *Mobile Greenfield FDI.* The concept of *Additionality* and *Mobility* as a concept is discussed in detail in section 2.3. An FDI project which is likely to be new to the host country is usually

[32] UNCTAD (2001)

[33] Balasubramanayam et al. (1996)

considered *Greenfield* – however, expansions of existing FDI projects are also likely to be valuable (and may be easier to obtain). It should be noted that, it can sometimes be beneficial for IPAs to engage with *Market Seeking* investment, particularly if a major MNC is involved. Even where no immediate plans are in place to manufacture the products intended to be sold into the host market, there may still be benefits for an IPA in being helpful and establishing a relationship with the investor. Although only limited resources should be applied to this, there is always the potential, through such a relationship, to encourage the investor ultimately to manufacture locally rather than to import the product. This is often known as *Soft Investment Promotion.* The support provided is comparatively light touch – e.g. incentives and other forms of hands-on support would not normally be offered – but such relationships can often bear fruit[34].

2.3 The Five Key Tests to differentiate FDI projects

Five Key Tests should be used to carry out an Economic Appraisal of FDI projects, and to set priorities for investment. It is important that all FDI projects undergo a clear and objective appraisal process. Appraisal should consist of two key elements – Financial Appraisal and Economic Appraisal. In order to ensure that the FDI offers real and tangible benefits to the host country's economy, an economic appraisal inclusive of the five key tests must be applied. Failure of the FDI project to pass any of the tests below may result in projects which have poor longevity or which make little contribution to the host economy. The five key tests are:

- Eligibility. Is the proposed investment one which fits into the host country's investment strategy and which will benefit its economy? No matter how well-resourced an IPA may be, it must be selective in which projects it expends resources in targeting or facilitating. Projects which offer – say – lower paid or lower value-added jobs will be less desirable. Also, sectors which are very heavily invested already and where the supply of labour is an issue may be considered ineligible for promotion or, where applicable, incentives.
- Mobility. Is this a truly mobile FDI project? Or, is it a project which must of necessity locate in the host country? The purpose of investment promotion is, after all, to persuade an investor to locate a desired project in the host country which might otherwise locate elsewhere.
- Viability. Is the project viable and – more importantly – is it viable in the host country? Frequently, projects which might be viable elsewhere are not viable in a specific

[34] For example, a relationship was developed between the (then) Industrial Development Board for Northern Ireland and Abbey National (now Santander Bank) providing general local advice and guidance; this relationship resulted later in at least two significant Financial Services investment projects.

country, possibly because the necessary skills are not available, because costs are too high or because the domestic market is saturated.

- Efficiency. Will the project, within a reasonable timeframe (say, within 5 years) return more benefits to the country's economy (in salaries, taxes and other benefits) than the resources used to promote it, including any incentives offered? If it does not, then hard questions should be asked to determine if it is really desirable. This also underlines the point that incentives must not be used either to make viable an otherwise unviable project or to artificially boost profits; the project must be fully funded and sustainable before incentives are added into the financial projections. The profits of the FDI project must make a fair and robust contribution to the host economy which will outweigh any resources expended on it by the host government. This is also why FDI projects with higher levels of profitability are generally more desirable.
- Additionality. *This is the crucial test.* Will the investment provide incremental wealth and employment or will it result in displacement, for example, of existing businesses and jobs? If the investment is principally targeting an indigenous market, then it may be less desirable. However, in developing countries, such investments may provide valuable import substitution and may be a stepping stone to export-oriented production.

The concept of Additionality is important in promoting FDI and warrants a discussion in greater detail. Crespo and Fontoura[35] have described the channels of technology transfer from an MNE to the host economy through the following five methods: i) imitation or the efforts of domestic firms to adopt successful technology used by MNEs; ii) labour mobility or the recruitment by domestic firms of workers with MNE experience and the ability to use new technology; iii) exports or the access to large distribution networks and better knowledge of foreign markets; iv) competition resulting in the efficient use of existing resources and technology; and v) backward and forward linkages where domestic firms become suppliers to or customers of intermediate inputs for MNEs.

The degree to which technology or knowledge transfer takes place will depend on both the nature of the project and the host country. Technology or knowledge transfer will obviously augment the argument that additionality exists. However, even if there is little or no technology transfer, and this may well be the case in the initial stages of FDI growth in a developing country, an FDI project may still pass the test of additionality and be worthwhile, as long as it provides ***net*** additional wealth and jobs to the economy.

The key to additionality is export-focus. If a project aims to export most or all of its products or services produced in the host country, then it is very likely to provide true additionality. Most often, an economy could benefit from an FDI through (a) supply chains and (b) spin-outs (where an individual or group working for the FDI company acquire

[35] Crespo and Fontoura (2007)

sufficient expertise to set up part of the process for themselves. Much of technology transfer can come from the establishment of new indigenous businesses triggered in one way or another by the FDI company. For example, the arrival of a major IT project in a country where the existing sector is minimal is likely to trigger the development of new small indigenous companies, partly through a supply chain relationship and partly by raising the overall level of IT expertise in the IT workforce of the country.

Another major way in which technology transfer occurs is through the arrival of one or more FDI companies creating a basis for a cluster for a particular sector or sub-sector. The cluster will typically consist of both FDI and indigenous companies with frequent transfer of personnel, contract work and expertise between them – this happens most often in knowledge-based sectors such as IT, Financial Services and Medical Technologies, but can also occur in manufacturing sectors. However, the key factor in additionality, especially for a developing country, is that new jobs are created which do not displace existing ones (i.e. usually determined by whether the FDI investor engages in exporting activity) thus reducing overall unemployment, raising personal incomes, improving the country's balance of payments, etc.

It is also important to consider the *Multiplier Effect,* - the wider economic benefit of new salaries and wages paid by an FDI project. Because people are earning new wages from the FDI company, this is spent in local businesses thus expanding these and creating new ones, which in turn creates new wages for the employees in these businesses, which are then spent in other local businesses, etc. This means that the value of every $1 paid in wages by the FDI company, there may be an overall benefit of anything between $2 and $5 to the economy[36].

***Additionality* is closely linked to *Mobility*: a project which fails the test of *Additionality* is also very likely to fail *Mobility*.** The additionality criterion is fundamental to the decision to promote or support a project (especially in offering financial incentives). But the IPA should consider the likely impact on the FDI project objectives and deliverables of not promoting it. For example, without investment promotion, would the project would be lost to the host country, either wouldn't happen at all or would be lost to another location? Or would it be likely to locate in the host

[36] For example, within tradable industries, Enrico Moretti discovered that, for each additional skilled job created, 2.5 jobs were also generated in the local non-tradable goods and services sectors, and an additional unskilled job created 1 job in the local non-tradable sector. Highly skilled sectors such as technology have the highest multiplier effect with five non-tradable jobs for each technology job. Moretti cites the example of Apple Computers which directly employs only 13,000 workers but generates 60,000 additional service jobs in the area. Source: Moretti, Enrico. Local multipliers American Economic Review: Papers & Proceedings 100 (May 2010): 1–7 http://www.aeaweb.org/articles.php?doi=10.1257/aer.100.2.1

country anyway? If so, there is little point in spending resources in promoting it. This is the test of mobility.[37]

However, two further considerations may be borne in terms of *Partial Additionality*. Assuming that the project does offer incremental wealth and jobs, it still may be less obviously mobile – i.e. the same project might have been carried out later without being promoted – if so, it is partially additional. Or, a different project might have been carried out, or the same project on a smaller scale or to a lower standard of quality or might happen later – again, if so, it is partially additional. Retail investments are a key example. As any country has a finite retail spend the creation of – say – 500 jobs in a new shopping mall is very likely to have the effect of pushing an equivalent 500 jobs at the other end of the retail chain; it therefore fails the test of *Additionality*. But, as it is not possible to sell to the people of the host country by opening the shopping mall in another country instead, it also fails the test of *Mobility*. There is therefore no point in promoting such investment.

Promoting an FDI project on *Social Grounds*. There can be rare exceptions to the universal application of additionality to FDI projects**.** If a project is seen to fail, or only marginally pass, one or more of the tests, it can be for ministers to decide to continue to promote or facilitate the FDI project if there are clear social grounds for doing so, for example, if it is planning to locate in an area of particular economic or social deprivation. However, this should be seen as a rare exception, the risk of failure should be clearly understood and the reasons for doing so should be well documented. It should not be used as a constant fall-back or excuse to promote less than desirable projects.

2.4 Appraisal of FDI Projects

It is very important that an IPA conduct an appraisal of FDI projects, particularly where incentives are offered. An investment promotion policy which is based upon the indiscriminate promotion of any investment is unlikely to be effective in targeting investment which is particularly sought – or which should be sought - by the IPA and which is most valuable.

***Selectivity,* or prioritizing specific projects or sectors as part of an investment promotion strategy, is one of the keys to promoting valuable FDI.** Selectivity has been adopted best practice for most, if not all, of the major IPAs over the past thirty years, particularly in key countries and regions and western Europe and is now carried forward also by IPAs in Eastern and Central Europe. In order to be selective, it is vital that an IPA carries out a comprehensive *Economic Appraisal* of all FDI projects, particularly focusing

[37] See Annex F for case study on Rwanda: Rwanda has been successful in attracting investment, particularly in infrastructure. However, it has been less successful in attracting Mobile Greenfield FDI, although the foundations for success in this have been laid and it is likely that it will enjoy future success here.

on the *Five Key Tests* described above. Failure to do so can result in a waste of effort and resources by the IPA or, worse, incentives being offered to projects which have only marginal benefit to the host country's economy.

In addition, wider issues to be considered by an IPA in prioritizing FDI projects are as follows:

- Is the FDI company a major corporate name which will give a boost to the investment profile of the host country and encourage further investment, including investment from the originating country (especially where that country is a major FDI source, such as the US or the UK).
- Does the project offer especially desirable knowledge or technology transfer?
- Will the project establish a new and desirable sector or sub-sector in the host country and/or be likely to pave the way to create the basis for developing a sector cluster?
- Does the project offer significant supply chain benefits to the host country?
- Is the project likely to have an environmental impact? If so, it may require an *Environmental Impact Assessment*.

It is important for the IPA to distinguish between – say – a project from a regional company offering only unskilled employment and a major multinational offering graduate employment. Most importantly, it is vital for an IPA to distinguish between an FDI project which aims primarily at targeting the indigenous market (*Market Seeking*) and one which aims at using the host country as a base to create a product or service for export (*Efficiency Seeking*).

The role of *Financial Appraisal*. While an *Economic Appraisal* aims to ensure that the project makes sense for the host country a *Financial Appraisal* aims to demonstrate that the FDI project makes sound business sense and is financially viable. Financial Appraisal should follow similar lines to those likely to be applied by a lending institution or venture capital company, although the level of appraisal may be less rigorous if incentives are not offered by the IPA. It should include a good understanding of the financial health of the FDI company, such as the strength of its balance sheet, its track record, whether any significant financial irregularity has been discovered, any court judgments upheld or pending. A full set of company accounts - balance sheet, profit and loss statement funds flow statement - should be obtained, irrespective of whether the company is publicly traded or not, subject to the IPA offering satisfactory guarantees of commercial confidentiality, including any non-disclosure agreement required by the company. Most importantly, the financial projections of the project itself must be appraised and understood. In particular, the IPA should satisfy itself that the project is fully funded and that it can meet its peak funding requirement, especially where there is likely to be a rapid build-up of production or where a time lag is likely between incurring operating costs and generating revenue. No promises of future funding by third parties should be accepted by the IPA unless these are in writing, are from solid and well-known funding sources and can be independently verified by the IPA. Of equal concern should be the marketing projections. Are they realistic given the size and nature of the company, its track record and experience in this market, whether the product or service is a new entrant to the market and so on. The IPA must always bear in mind that the financial performance and profitability – and, therefore, its likelihood of still being there in three or five years – will be closely dependent on achieving its projected market share.

Appraising an FDI project from a major MNC. When dealing with a large MNC, such appraisal may be relatively light touch. After all, it is unlikely that even a mature IPA will be able to successfully second-guess a Siemens, Toyota or HSBC. Nevertheless, the IPA must reasonably understand the financial structure of the project to be able to judge for itself how likely the company is to achieve – say - its employment targets or to pay the salaries and wages projected.

Adopting a selective system requires core skills in assessing and appraising projects and in negotiation. The appraisal process should work as follows:

- The IPA, usually through one its overseas offices, becomes aware of a project for which a location is sought by a company.
- Through intensive discussions, it obtains key details of the project, such as: objectives, employment, capital investment, training requirements, etc.
- The IPA determines what level of incentives it is prepared to offer to secure the project.
- The company is given a broad idea of the level of incentives which may be on offer for this project – this is known as an *Illustrative Offer.*
- The company accepts this as a basis for discussion and submits a full business plan.
- The company visits the IPA for detailed negotiations.
- A final agreement of the package in incentives is arrived at.
- The project is appraised by specialist IPA staff and the key investment tests applied (although the IPAs staff dealing with the company will have, from the beginning, ensured that the project would be likely to pass such tests).
- Assuming appraisal is positive, a formal *Letter of Offer* is issued.
- The lawyers for the company and for the IPA will usually seek amendments and, once these have been agreed, the company and the IPA sign the *Letter of Offer* and the project is then announced formally by the company with senior IPA officials and Ministers attending.

2.5 FDI Buyers and Sellers

For an inexperienced and developing IPA, one rule of thumb may serve to clearly distinguish between desirable and undesirable FDI is to determine if the investor is a *Buyer* or a *Seller*. If an IPA's investment promotion strategy, marketing and investor targeting are properly carried out, it will inexorably find itself dealing with the most desirable types of FDI it is capable of attracting. Few projects which are desirable ever beat their way to the IPA's door – these must be sought after and competed for. However, when an investor does approach an IPA independently, the key question which an IPA must always ask of itself is: Is this a Buyer or a Seller?

- Is the "investor" attempting to sell his products into the host country's market, to obtain a government contract or to use the resources of the IPA to get some free market research? If so, the "investor" is a ***Seller***.
- A true FDI project is one where the investor is prepared to invest his own capital and take a business risk on the open market, to create a project or service to be sold wholly or mainly outside the host country's market, to create profits and jobs. If the investor's project looks like this, he is a ***Buyer***.

An IPA should always bear in mind that a purported FDI company which approaches it independently is more likely to be a *Seller* than a *Buyer* – a point which underscores the absolute importance of *Investor Targeting*. One small (real) example may serve to illustrate the point. An "investor" approaches an IPA saying that he is interesting in establishing a project to create social housing (this is, in reality, not an FDI activity at all, but let that pass). On further appraisal (which, fortunately, was undertaken), the IPA discovers the reality that the "investor" has a surplus of prefabricated housing material which he cannot sell in his own market and his "FDI investment" is an attempt to sell such material to the host country's government. This may or may not represent a good or desirable transaction for the host country government. However, the point is that it is not an FDI investment at all, but a commercial transaction and should be treated accordingly. The "investor" is not a ***Buyer*** - he is a ***Seller***.

Section 3 - How can a government promote FDI?

3.1 How does Investment Promotion work? [38]

Investment promotion is the efforts undertaken by a national or regional government and its IPA, to generate private sector investment into its territory which offers incremental wealth, employment and other benefits. The relationship between a host country government and its IPA is subject to a wide number of variables. Ideally, the IPA should not be so close as to be part of the country's civil service – thus diluting the possibility of it having a sufficient *Business Focus* to deal effectively with investors, nor exercise a strong *Advocacy* function where necessary – nor should it be so remote that it cannot access political decision makers – particularly important for decisions on larger and more significant FDI projects. Best practice in the British Isles and throughout western Europe has shown that possibly the most effective IPA structure is that of an autonomous government body with an advisory Board (representing industry, commerce, trade unions and other key stakeholders) but with overall political control by Ministers. It is important for an IPA to be able to exercise a degree of autonomy in order to take swift decisions, supported by the government and private sector participation and to exercise an *Advocacy* function to press for necessary *Investment Climate* improvements. An empirical study by Jacques Morisset[39], studying 58 countries concludes the following as the most important factors in determining an IPA's success in attracting FDI: good investment climate of the host country; political visibility of the IPA in terms of direct links to the highest government officials; and, private sector participation in the board that supervises the agency, although there are certainly others, in particular the level of expertise, the degree of pro-activity in targeting markets and sectors and the importance of having a strong business focus.

There have been numerous theoretical and empirical studies on the determinants of FDI. In his summary of findings, V. N. Balasubramanyam[40] lists the following broad factors that attract FDI into host countries:

- Market size and potential[41]
- Resource endowments (natural resources and human resources)
- Infrastructure (transportation and communication net works)

[38]For further reading on Investment Promotion Strategy, refer to Loewendahl, H. (2001) who acknowledges the lack of research in the area of investment promotion despite the increasingly positive role of IPAs in attracting FDI. His paper is based on interviews conducted with 30 major TNCs and global professional services as well as his own experiences. This chapter draws on Global Best Practice papers as well as the experiences of the lead author Trevor Killen in working with IPAs in many parts of the world.

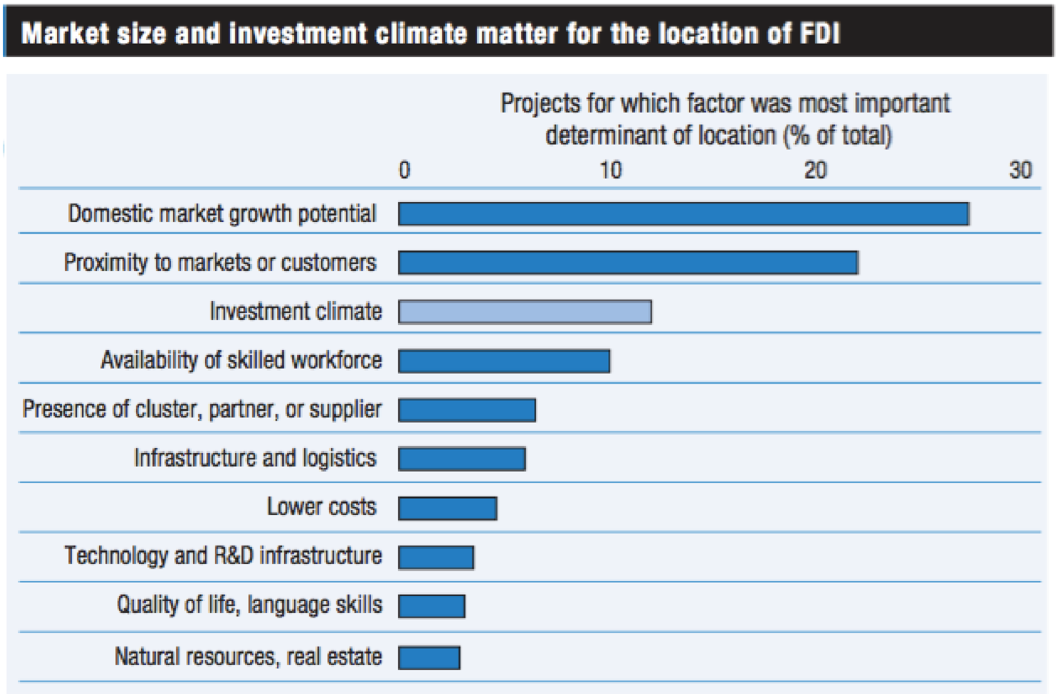
[39] Morisset (2003)

[40] Balasubramanyam (2001)

[41] However, this does not necessarily refer to the host country market; for Mobile Greenfield FDI regional or, sometimes, global markets are key.

- Macro economic stability (stable exchange rates, low rates of inflation)
- Political stability
- Stable and transparent policy towards FDI
- Distortion free economic and business environment.
- Fiscal and monetary incentives (tax concessions) but in the context of a stable economic environment.
- Regional groupings and preferential trading arrangements between prospective host countries

On the other hand, evidence from 30,000 FDI projects in the FDI Markets data base suggests that Investment Climate matters quite a lot, as summarized in Figure 5 below:


Market size and investment climate matter for the location of FDI

Note: Based on 28,814 new high-value-added FDI projects between January 2003 and July 2011 for which the determinant of location was identified.
Source: Financial Times, fDi Markets database.

Figure 5 *Source: Hornberger. et al (2011) IFC*

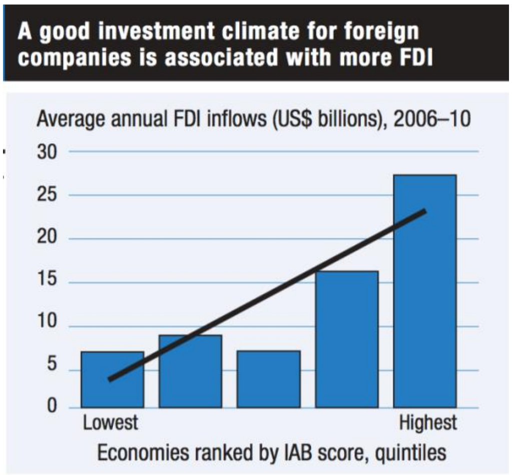
***A country's Investment Climate* is a crucial determinant of most, if not all, FDI investment decisions[42].** IC has been defined in a number of ways but essentially it is the economic and financial conditions in a country that affect whether individuals and businesses are willing to invest or acquire a stake in the businesses operating there. One definition of investment climate, as used by the

Fig 4 *Source: Hornberger. et al (2011) IFC*

[42] This is supported by the empirical study of Morisset (2003) who concludes (among others) that Investment Promotion is most effective in a country with a good investment climate

then World Bank Group Senior Vice President and Chief Economist, Nicholas Stern, is as follows: *"...the policy, institutional, and behavioural environment, both present and expected, that influences the risks and returns associated with investment."* [43] Investment Climate is probably best stated as the sum of the factors and conditions in a country which impact upon the propensity of the private sector to invest

Investment Climate* encompasses *Business Environment*, but the two are different.** Probably the most common measurement of *Business Environment* is the *World Bank Doing Business Index*. Whilst this is a useful basis for comparison, and a possible proxy for IC, it is ***not the same as investment climate. All this index measures (or claims to measure) is the ease of doing business, not the IC of a country. It is quite possible that a country may score well on the factors measured such as number of days required to start a business but still have a poor IC, for example, because of a poor labour market, high taxation and so on. Investors, particularly in FDI, tend to view IC more from a business than an economic point of view as they look at their investment drivers of a country (especially risk, labour market, costs and infrastructure) with a view to assessing how they will impact on their anticipated ROI. Investors therefore view IC as a country's Investment Product i.e. what does the IC have to offer which will best meet the investor's business needs and maximise his ROI?


A good investment climate for foreign companies is associated with more FDI

Whilst in the past, industrial FDI tended to be more focused on manufacture or assembly of finished products, it is more likely today that an FDI investment will form part of a Global Value Chain (GVC) – i.e. all of the people and processes involved globally in the production of a good or service. Securing FDI which is part of a GVC is especially likely in the case of developing countries. As UNCTAD says[44]: "*Countries with a greater presence of FDI relative to the size of their economies tend to have a higher level of participation in GVCs and to generate relatively more domestic value added from trade".* Whilst countries can make a policy decision whether or not to promote investment which is part of a GVC, in reality there is often not much choice. There is certainly a danger of becoming "locked-in" to GVCs at a low level of value-added. However, (a) it may be a question of accepting such investment – at least initially – or having no FDI at all and (b) there may be downstream opportunities, as skills and experience develop, of moving up the value curve in the GVC.

[43] Pleskovic and Stern (2002)

[44] UNCTAD (2013)

3.2 Creating an FDI Investment Promotion Strategy

Securing significant FDI demands a clear investment strategy, precise targeting of sectors and markets, effective branding and the creation of competitive advantage. The active, vigorous and persistent marketing and promotion of investment is required with a range of specialist skills needed – international marketing, investor targeting investment generation, investment management, investment appraisal, and investment aftercare. The key actions which should be undertaken by any IPA to achieve substantial success in promoting investment are listed below. This chapter will discuss the first two steps – Investment Promotion Strategy and Marketing / Branding; the remainder will be detailed in Chapters 4 and 5.

- Creating an Investment Promotion Strategy
- Marketing and Branding
- Investor Targeting
- Investment Facilitation
- Investment Generation
- Investment Management and Appraisal

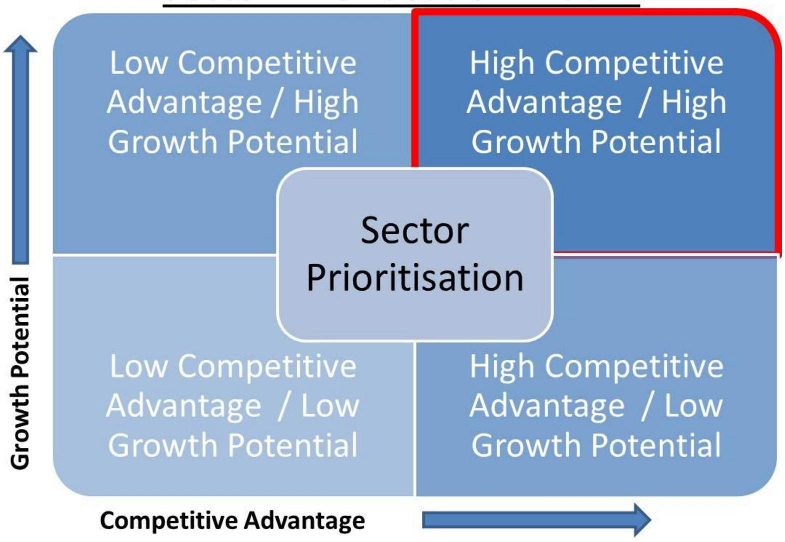
It is of the utmost importance for an IPA to create a realistic and carefully considered *Investment Promotion Strategy*. Not even the largest, most experienced and best-resourced IPAs can promote all investment everywhere. Whilst it is important for the Investment Promotion Strategy to be logical, achievable and to offer realistic possibilities of success, this need not be a long-drawn out process. Some IPAs at this point fall into the trap of over-extending the time needed to create an Investment Promotion Strategy, instead of actually commencing the promotion of investment. An Investment Promotion Strategy, whilst needing to be consistent, should never be absolutely set in stone – it must be flexible, to adapt to market changes. Above all, when implementation has begun, if one part of an Investment Promotion Strategy, is seen to be unproductive, the IPA must always be open to alternatives. However, the most important thing is to complete the initial Investment Promotion Strategy as soon as possible and to commence implementation. An Investment Promotion Strategy should address two key questions:

- ➢ Which sectors should be prioritised?
- ➢ Which (geographical) markets should be prioritised?

Sector Prioritisation **There are two main factors which should be considered by an IPA in prioritising sectors for investment promotion: *Competitive Advantage* and *Growth Potential*.** The country must first consider sectors in which it has *Competitive Advantage* in terms of pre-existing skills, expertise or other investment elements likely to be attractive to potential investors; or sectors where such elements can realistically be created or enhanced within a reasonable time frame. If there is a basis for creating the necessary skills and government is willing and able to devote resources for skill development, it may be possible to create a realistic offering to investors in that sector. However, the ideal is to prioritise sectors where the country has – or can quickly achieve – competitive advantage; prioritising sectors where the country's offering is marginal or mediocre is unlikely to be very successful, given the highly competitive nature of investment promotion.

The second key factor is to prioritise sectors which offer significant *Growth Potential*. There is little point in prioritising a sector which may offer only a minimal number of contestable FDI projects globally per annum, however much the country may be suitable for such projects. This is often a mistake made by IPAs which continue to prioritise traditional sectors where demand is now minimal. In this context, it is important to note that sectors prioritised for FDI may be quite different from those which are currently large employers in the country[45]. A country may have substantial current levels of employment in traditional textile weaving or other artisanal crafts; however, it may find it much more fruitful to target synthetic textiles or garment manufacture which offer growth and which may have some synergy with the traditional skills. The best method is to think of sector prioritization as a matrix, as follows:

Sector Prioritisation Matrix


Low Competitive Advantage / High Growth Potential
High Competitive Advantage / High Growth Potential
Sector Prioritisation
Low Competitive Advantage / Low Growth Potential
High Competitive Advantage / Low Growth Potential
Growth Potential
Competitive Advantage

Market Prioritisation. **The two key issues to be considered by the host country in market prioritization are: does the market offer significant opportunity within the given sector(s); and, is this a market which the IPA can realistically target, given its likely resources?** Other key factors to consider are:

- Physical proximity to host country (i.e. within a region)
- Concentration of potential investors in prioritised sector(s)
- Language / cultural compatibility

[45] For example, over the past 30 years Ireland has targeted FDI sectors such as ICT (employment 37,000), Financial Services (employment 35,000) and Pharmaceuticals (employment 25,000); however, the largest single sector remains Agriculture (employment 103,000 – including forestry and fishing, but not agribusiness). (Central Statistics Office - Ireland)

- Degree of existing business connections
- Ability to effectively target within given budget

A developing country in sub-Saharan Africa may decide that – say – India offers significant opportunities within a targeted sector, but it lacks the resources to effectively target such a large and distant market. A more realistic opportunity may be presented by, for example, the South African market. There are numerous examples of countries in or emerging from conflict initially targeting those markets which offer more realistic prospects of success. For example, Northern Ireland was successful in Financial Services Contact Centre investment in the mid-1990s (when the conflict was still on-going) by targeting principally those major companies which it had a pre-existing trading relationship. In another context, Basra enjoyed some investment success (up to $800m) through investment emanating from companies close to the southern Iraq border – e.g. Kuwait and Iran. The case of post conflict Mozambique also provides a successful case study of how it targeted initial foreign investment from neighbouring South Africa and former colonial power Portugal – See *Annex C for the case study on Mozambique.*

3.3 FDI Marketing and Branding

This section will discuss the key elements in marketing: the Product (or the country and its investment climate); Place (geographical advantages); and, Price (Value for Money proposition). As the first step, however, the IPA must invest in gathering information on how potential investors in regional and global markets perceive it as a location for investment. The IPA should refer to publicly available reports on the country and its investment climate. A variety of organisations produce these reports, including multilateral institutions and both governmental and nongovernmental sources. Examples include the country reports compiled for the World Investment Report (WIR), technical reports by the World Bank, and investment guides compiled by private consultancy firms. Other sources include the country reports produced by the US Department of Commerce, and the Economist Intelligence Unit's annual publications and the IPA can also perform online searches via the Internet of the archives of leading newspapers.

Marketing the Product

The FDI *Investment Product* is the offering of the host country to the potential investor. Many emerging IPAs tend to view marketing principally in terms of promotional activity but the initial focus should be on the *Investment Product*. This will, of course, be hugely dependent on his specific investor needs and will vary from sector to sector and from project to project. However, there are many key product elements which are important to most, if not all, FDI investors. These can be broadly seen as coterminous with Investment Climate.

***A country's performance in its Investment Climate or Investment Product Factors* (listed below) often determine the flow, speed and quality of internal and external investment and will therefore impact most, if not all, FDI investment decisions.** It is important that an IPA objectively analyses each of these key factors to develop a clear and objective understanding of its offering to investors. This is quite a different exercise from writing promotional material; here it is important that the country's offering is assessed objectively and in comparison with those of its likely competitors for investment. These factors[46] will be explored in more detail in *Section 4*, but may be summarised as:

- Risk
- Labour Market – availability, flexibility, skills, qualifications
- Operating Costs
- Infrastructure – especially access to land, utilities, communications and freight services
- Macroeconomic / Policy Factors
- Business Enabling Environment
- Taxation
- Investment Incentives

Where there are deficiencies or areas for potential improvement, an important function of an IPA is *Advocacy* – to work with government and private sector partners to effect change. For example, where skills are deficient, the IPA may engage with educators, government and external training providers to implement education and training programmes to create and enhance the skills and qualifications likely to be required by investors.

Marketing - Place

This is the selection and prioritisation of geographical markets, as discussed in section 3.2 above.

Marketing - Price

This refers not only to operating costs (especially labour costs, most often the single most important element) but also other factors such as taxation, incentives, and productivity which will determine the overall *Value for Money* proposition. This will be a very important focus of the potential FDI investor because it will usually determine the ROI for the investment and it is highly likely that the investor will model this and compare it to other potential locations under consideration.

[46] Based on work carried out by UK Investment Promotion Advisor under DFID's Technical Assistance to Iraq Programme 2008-2010

It cannot be stressed enough that there is little point in an IPA engaging in promotional activity if the other marketing elements – Product, Place and Price – are not competitive. Any interest generated will be quickly dissipated once the investor discovers that the offering is deficient or uncompetitive. Not only will time and resources be wasted, but the effect may even be negative.

3.4 FDI Marketing Plan

If there is a sound offering to be placed in front of investors, it is essential that an IPA develops a *Marketing Plan* to engage in coherent, integrated and measured *promotional activity*. This section describes in detail the key elements of an IPA's FDI Marketing Plan.

An IPA must develop key *marketing messages* for use in its regional or global marketing campaigns as they link to and reinforce the investment brand of the country. For this reason, *repetition* is important if marketing messages are going to be effective in any market. As well as developing core or generic marketing messages it is also important to develop marketing messages which are *sector specific* and *market specific.* Although marketing messages tend to be similar across different sectors and markets there will be key differences for a specific sector or cultural differences in particular geographic market which must be addressed. However, it is important that these marketing messages must be consistent and be easily identifiable as emanating from the country across all forms of marketing communications in which the IPA may engage. To be effective, the messages must be *consistent*. The central marketing messages must extend beyond advertising and be reflected across the full range of promotional activities. If there is a clearly-defined area of *Competitive Advantage* – for example availability or cost of labour - the IPA should use it as the central marketing message of any promotional campaign to maximise investor interest.

If an industrial cluster exists, this can be translated into a very effective marketing message. For example, Ireland developed an industrial cluster program to encourage FDI in the software development industry. Between 1983 and 1987, Ireland's investment promotion agency, IDA Ireland, ran an extensive awareness campaign in support of this program. The highly successful phrase developed for this campaign was *"The Young Europeans – hire them before they hire you."* The central marketing messages of this campaign concentrated on a single message: the high intellectual capital of the young Irish workforce.

Once the IPA has determined the most effective marketing theme, it should choose the most appropriate *Marketing Tools* to deliver that message. Selecting the right tool is important in order to maximize the impact of the promotional activity. Different marketing tools are more effective at different stages of a marketing campaign. For example, as investor perceptions of the country become more widely recognised as an investment location, more personal contact in the form of *Direct Marketing* (such as targeted advertising or newsletters) may generate better results. The tools and the marketing mix that may be used will also be governed by the size of the IPA's promotional budget. The next step is to develop media, using the marketing messages, across a wide range of direct and indirect marketing tools discussed below.

***Direct Marketing Tools* are tools that are sent directly to one of more investors or influencers, rather than distributed to a wider market – such as advertising.** Direct marketing tools can be used both to build awareness and to provide investors with specific information. Most of these tools cost relatively little to develop. Some examples of a *Direct Marketing Tools* are as follows:

- *Brochures:* Despite the existence of digital routes to market, an IPA still needs corporate generic and sector-based brochures. Professionally produced brochures are essential and effective promotional tools; conversely, poorly produced brochures containing inaccurate information or typographical errors are likely to have a very negative impact. However, these should be as brief and factual as possible – investors are very resistant to hyperbole – and use attractive and impactful visual images – photographs and charts.
- *Sector Studies*: The principal purpose of a sector study is to enable the IPA to differentiate its location from competitors by providing detailed information on specific sectors to potential investors. Sector studies are also useful to verify and support key marketing messages.
- *Fact Sheets*: Fact sheets are normally 2 to 4 pages covering essential pieces of information that will be of interest to the potential investor ***and*** which highlight the areas where competitive advantage may exist. Fact sheets are useful because they can be easily and cheaply produced and tailored to sectors and/or to key investment elements – such as real estate or telecommunications.
- *Newsletter:* A regular newsletter can raise the profile of the IPA's country as an investment location and keep investors informed of developments. A newsletter can also be a part of a direct marketing initiative to help sustain dialogue with a client considering investment.
- *USB sticks:* USB sticks can be used for wide distribution and, because they can contain large amounts of data, they are excellent vehicles for providing investors with highly detailed information and can be positively branded with the name of the IPA.
- *Promotional DVD*: Contrary to the expectations of many developing IPAs, a promotional DVD is the least important of the promotional tools discussed here. This is particularly true for IPAs operating on a tight budget, because high-quality videos are expensive to create and current technology gives IPAs lower-cost alternatives. However, a short, focused and well-produced DVD can still be a useful promotional tool. It can also be much more effective to insert brief 10-15 second video clips in the IPA's website – especially existing investors offering testimonials.

***Market-Wide Tools* reach a wider audience;** examples include:

- *Public and Media Relations (PR):* In many cases, potential investors may have either a low level of awareness or negative perceptions about the IPA's country and this can be addressed through an effective PR strategy. Journalists are prime target customers for an IPA as they are always interested in good stories, and if the IPA can provide them with these, subsequent coverage tends to be positive. A positive article prominently featured in a target publication can say more about the country as an investment location than can a series of advertisements; in addition, it injects credibility, which advertisements usually lack and it is free publicity.

- *Advertising*: An IPA should be aware that advertising can be the single most significant marketing expenditure. It is important therefore that the IPA decides which publications are most likely to be read by the intended target audience. This should normally be a sector-based audience – or one which covers a number of well-defined sectors - as generic advertising is often too scattergun to be effective and, of course, it is ineffective to place advertising in general mass media. Advertisements should focus on the business media, especially on those with a focus on the IPA's targeted sectors. These will have a much smaller circulation, but they will tend to be read by the audience the IPA is seeking. Targeting sector and trade media will reach the managerial level of potential investors and an IPA should bear in mind that it is usually these people and not senior level decision-makers who are most important in the initial stages of attracting an investment project. If the IPA decides to engage in advertising, it will need to hire an advertising firm to design and implement the campaign. IPAs should also be aware that repetition is essential to have any real impact. For this reason, placing a series of – say – 20 or 30 inexpensive advertisements in a trade journal is likely to be more effective than placing a one-off expensive advertisement in – say – the Financial Times.

  A number of IPAs have mounted successful advertising campaigns, but many have gone astray and have wasted valuable resources in doing so. When considering whether or not to include advertising in its marketing mix, an IPA must give it very careful consideration. The main disadvantages in using advertising are its expense and potential lack of credibility with investors.

- *Advertorials:* It is possible to combine advertising and media relations in the form known as advertorial. In this, either in one article or a complete feature section is commissioned and paid for by the IPA, is written by journalists from the publication concerned and is therefore always positive.

- *Seminars, Conferences, Business Events and Exhibitions:* Investment, trade, business or sector events are useful tools both for communicating the IPA's marketing messages and for targeting specific investors or groups of investors. Typically, they are held in a key target market, it can appropriate to hold them in the domestic market, but this is usually less effective. However, as with most aspects of promotion, participation in these events must be focused and planned. The IPA's role in these events can range from providing a speaker for a conference to having a highly visible presence, such as through event sponsorship or having an information stand at the event.

- *Business case proposals and Cost Models:* These will be discussed in Section 5 - Investor Targeting.

An IPA must develop a *Marketing Communications Plan* to co-ordinate all marketing methods (discussed above) over all of its target markets to ensure that all elements work together, support each other and are consistent. For example, that having a presence at an event is supported by targeted advertising, media relations and direct marketing. The Marketing Communications Plan can be developed either globally or, ideally, for specific markets.

A *Product Database* is essential for successful marketing of FDI. Unless the IPA is well-informed about its investment product, it will not able to market it to potential investors. It is not important in which form the product database is held but it is important that it is as comprehensive as possible in holding information on all relevant investment product elements and that it is updated as frequently as possible. The information contained in a product database broadly reflects the information categories identified under "Investment Product", above – a more comprehensive listing is given in Annex A. It is also important that the information is presented in a user-friendly form to investors, but it is as up to date and relevant as possible and also that it is specific. It is not sufficient to talk, for example, in general terms about land or site availability, it is necessary to offer at least some precise examples of specific sites with key data such as size, rental costs, location description, etc.

It will be important for the IPA to have access to competent *Business Intelligence Sources.* These are usually in the form either of freely available information which however takes usually a long time to research using the Internet or commercial information databases. Commercial databases can be expensive to purchase or rent to provide a dedicated and easily accessible source of information on FDI flows, industry sectors, global and regional markets and on competitors.

3.5 Creating an FDI Brand

One of the most important concepts in marketing of FDI is creating an Investment Brand – which should not be treated as optional or unalterable. The objective of branding is to communicate key product attributes and benefits and this applies to FDI as much as to marketing any other product. The IPA's country will have a brand for investment even if it has engaged in no branding activity – in terms of how an organisation's customers see it and its products. However, this is unlikely to be the brand that the IPA may wish for investment and may even be negative. It is therefore important for the IPA to create the brand it wants, rather than the residual brand, which may not be helpful. Secondly, the Investment Brand is not unalterable. It can and should be tailored to optimise the results of marketing and investor targeting campaigns. Maintaining the country's brand name is an on-going task and require a constant input of resources. If possible, the IPA should organise *Stakeholder Focus Groups* both in-country and in target markets. Focus groups, which involved assembling up to 20 investors or other people in a room and brainstorming on perceptions of the country and its strengths and weaknesses in relation to investment can reveal a lot of information that the very valuable to the IPA. The use of focus groups is a standard technique in branding and organisation and is best conducted under the supervision of an experienced branding consultant.

The important point for the IPA is to consider each investment product on offer as a potential benefit to an investor, not simply to describe the part of the product. For example, lower wages costs are a description of that investment product element, the attribute offering the benefit to the investor is a reduction in operating costs leading to higher profitability and a quicker return on investment. Most importantly, in identifying product attributes or benefits, it is important to always look at it from the ***investor's*** point of view.

Section 4 – The FDI Location Decision Process

4.1 How do companies approach choosing an FDI location?

The investment location decision process – or the process by which a company decides to invest in another location in another country or site and selects the location - can vary from company to company, and from sector to sector. However, although there can be many differences between companies and types of companies as to how they approach selecting a location for an FDI project, there are also many commonalities. Irrespective of the size or sector of the company, the FDI location decision is a major one for the company. It usually involves significant capital expenditure and commitment of senior staff time and other resources. It is also a decision which can have significant impact on the company's profits, its productivity, its share price and its international reputation. The pressure can be very significant for the company to make the right decision; therefore, the process tends to be systematic, painstaking and thorough, with every care taken to avoid mistakes which could later prove very costly. However, as we shall see in *Sections 4 and 5*, the subjective, human factor should never be ignored. Most FDI location decisions – certainly those pertaining to *Mobile Greenfield* FDI projects – are taken by MNCs. Sometimes SMEs or smaller companies may also seek a new location for investment, but the scope and complexity of decisions taken by these companies are likely to be much more limited than for larger MNCs – for example, they may be investigating a location just over their national border for an overspill plant. However, most FDI tends to be undertaken by larger MNCs, most often those operating already in multiple countries, regionally or globally. Therefore, the approach discussed in this chapter applies principally to the approach taken by large MNCs in choosing an investment location, although the principal is usually broadly the same for SMEs. It also applies principally to *Resource Seeking* FDI, although again it may share some similarities with the location search for other forms of FDI.

Some companies gradually establish operations in an overseas location, while others proceed directly to an in-country investment. For example:

- Manufacturers, especially smaller or less experienced international firms, can sometimes move through a sequence, beginning with a trade relationship. This may take the form of exports via agents, moving to the licensing of foreign products or the establishment of a direct trading presence. This then may result in investment in assembly or production ventures, directly or as a joint venture (JV). For this reason, an intelligent IPA should never reject the opportunity to be helpful to a major MNC, even if the initial enquiry relates to a sales / distribution operation only. For example, if a manufacturing company establishes a sales or trading subsidiary in the host country, this may be a good sign that the company is intending to expand its exports to its market and if successful it may subsequently consider establishing manufacturing facilities.

- Large investors with extensive international experience may also use this incremental approach to enter new markets, especially those with a perceived high level of risk – such as FCAS states - or markets that are unfamiliar in terms of language, culture, form of government, or level of development.
- In some cases, there is a progression from a trading relationship leading to an eventual export-focused manufacturing operation. For instance, a company may move from setting up warehousing facilities to setting up a manufacturing facility.
- Companies that intend to manufacture goods, rather than solely to sell them in the host country market are more cautious about establishing facilities overseas because setting up a factory involves much more capital expenditure and consequent risk. Licensing or a JV may be used as a long-term strategy to enter markets and a direct investment never occurs.
- Resource Seeking FDI utilising a host country's primary or labour resources has a relatively rapid investment process, because there is no way to access these resources without entering the country. Therefore, most companies do not get involved in an incremental process.
- Many SMEs in the ICT, biotechnology, financial services, business services and other knowledge-based sectors can quickly move operations overseas in order to keep pace with growth in their markets and to reduce costs. This is often referred to as *Offshoring* (where the location is relatively close to the company's target market) or *Near shoring* (which can, in theory, be located anywhere globally).

4.2 Investment Drivers

The process used by investors to select an investment site in developing or emerging economies is similar to the process investors use to select a location in a developed country, but with a higher emphasis on the factor of *Risk*. Investors use various *Investment Drivers*, such as labour market characteristics and operating costs to compare and rank locations. However, the first – and most fundamental – factor is that of *Risk*. This can be broken down as follows:

- **Political Risk:** How stable is the country and the government structure? This is usually the most important Risk element, because total failure of a production operation, if – say – a political coup happens will affect business continuity. The main negative results of this are not so much in relation to potential loss of plant and equipment, but on the continued ability of the company to supply its customers.
- **Security Risk:** Apart from its potential effect on business continuity, an adverse incident affecting a company's operation in the host country may reflect negatively on its global image and, thereby, its global standing and share price. It may also mean difficulties for senior management, trainers, etc. in physically accessing the location, with obvious adverse implications.

- **Economic Risk:** How stable is the local currency, rate, rate of inflation, government borrowing, etc.? Can profits be repatriated without difficulty? Is the government business-friendly?

If an initial analysis shows serious concerns on any or all of the risk elements, then it is likely that the company will *not* investigate further on any of its key *Investment Drivers.* These are the key elements which the company will use to assess each location on its Short List and include:

- Labour market supply and flexibility, skills and qualifications
- Operating Costs (including labour costs, freight costs and other inputs)
- Infrastructure (physical and telecommunications)
- Natural resources (availability and quality, if applicable)
- Level of support by government, including incentives

The importance of each of these factors varies according to the type of investment, for example:

- Physical resource-seeking investors examine closely the availability and quality of natural resources at the outset.
- Labour-intensive manufacturing and tradable services operations require a plentiful supply of low-cost and productive labour – that also has, or can cost-effectively be made to have, the necessary skills.
- Heavy manufacturing operations, such as steel, will require reliable and cost-effective supplies of electricity and water.

Investors use a process called *Matrix Analysis* during the final stages of their location shortlisting process. Often taking into account anything up to 100 separate drivers, companies frequently assign numerical values to each determinant and create a *site-selection matrix*. By selecting the countries with the highest scores, the number of sites on the *Short List* is reduced to one or two potential locations through a process called *Matrix Analysis*. The following chart is a simplified example of *Matrix Analysis.*[47,48]

Table 1: Matrix Analysis 1

Factor	Country A	Country B	Country C	Country D
Labour Cost	9	7	3	4
Skills	6	8	6	7
Incentives	9	5	4	2
Infrastructure	4	7	8	8

[47] Based on work carried out by UK Investment Promotion Advisor under DFID's Technical Assistance to Iraq Programme 2008-2010

[48] MIGA (2003)

Business Environment	4	6	8	8
Operating Costs	8	4	2	2
Supply Chain	3	5	8	7
Political Stability	3	5	8	9
Security	2	6	8	8
TOTAL	48	54	55	55

It should be noted that the breakdown of costs will vary greatly according to the type of operation. For example, tradable services such as financial services may have anything up to 90% of their costs as labour, whilst for heavy manufacturing industry – such as steel production – costs such as raw materials, energy and distribution will form the bulk of annual operating costs. Usually the key factor determining the operating cost profile is whether the operation is labour-intensive or resource-intensive. For the former, labour costs (balanced with estimates of productivity and availability of skills and qualifications in an overall Value for Money equation) will be paramount [for example, in an average ICT operation, usually around 80-90% of project costs will be labour-related. For the latter, the cost (and availability) of land, real estate, energy, water, waste and freight services are likely to be more important [for example, pharmaceutical projects tend to have very heavy capital expenditure and resource costs, but may employ only – say – 200 people in a plant extending to over 200,000 sq. ft.

There are, of course, other factors that may influence a company's decision to invest. *Market Seeking* investors are primarily concerned with the size and growth of their potential consumer group, and then with cost factors and the policy regime. Investments made through acquisitions or privatisation places significant emphasis on an attractive and transparent business enabling environment. To be successful, firms investing through acquisition or privatisation must be able to operate without unwarranted interference, and therefore, generally seek flexible operating conditions and a predictable and stable business enabling environment. Companies may also look for competitive *investment incentives*, but these are of secondary importance in relation to the other key investment drivers. Most companies will expect a location to be competitive without the application of incentives and will only factor these in once a comparison has been made net of incentives.

4.3 Primary and Secondary Investment Drivers

The Primary Investment Drivers are the *must haves* of any investment decision and are the ones which will most directly impact upon the *Return on Investment* (ROI) of a project. Not all investment drivers are weighted equally by an investor: greater weight is assigned to those factors considered most vital – these are the *Primary Investment Drivers*. In the example illustrated below, the investor has assigned a double weighting to the factors of labour costs, operating costs and incentives – which is a clear indication of the investor's intentions to minimise his financial exposure for this investment[49].

Table 2: Matrix Analysis 2

Factor	Country A	Country B	Country C	Country D
Labour Cost	18	14	6	8
Skills	6	8	6	7
Incentives	18	10	8	4
Infrastructure	4	7	8	8
Business Environment	4	6	8	8
Operating Costs	16	8	4	4
Supply Chain	3	5	8	7
Political Stability	3	5	8	9
Security	2	6	8	8
TOTAL	**74**	**69**	**64**	**63**

In contrast to Matrix Analysis 1 (Table 1) where no weightage applied, in Matrix Analysis 2 above, we can see that Country A emerges as the clear preferred location for the investment. Although, in reality, the scores are so close that a further examination of the factors and the factor of personal relationships with the respective IPAs (discussed in *Section 5*) will be likely to come into play.

Primary Investment Drivers usually include:

- Risk
- Labour Availability and Costs
- Skills Availability
- Operating Costs
- Site / Factory / Real Estate Availability
- Infrastructure – Transportation (of freight)
- Infrastructure Costs (depending on sector)
- Taxation Rates
- Ease of Repatriation of Capital and/or Profits

Secondary Investment Drivers are those which are desirable, but less vital and which do not have a strong direct impact on the investor's projected ROI. These may include:

- Infrastructure – Transportation (of personnel)
- Infrastructure Costs (depending on sector)

[49] Based on work carried out by UK Investment Promotion Advisor under DFID's Technical Assistance to Iraq Programme 2008-2010

- Incentives
- Physical Access
- Quality of Life Factors
- Investment Climate
- Business Environment – e.g. time required to establish a business
- Evidence of Investor-Friendly Attitude of Government
- Track Record of FDI Investment

4.4 How companies make FDI investment decisions

The Investment Location Decision Process can broadly be summarized in the following chart; and elaborated further below:

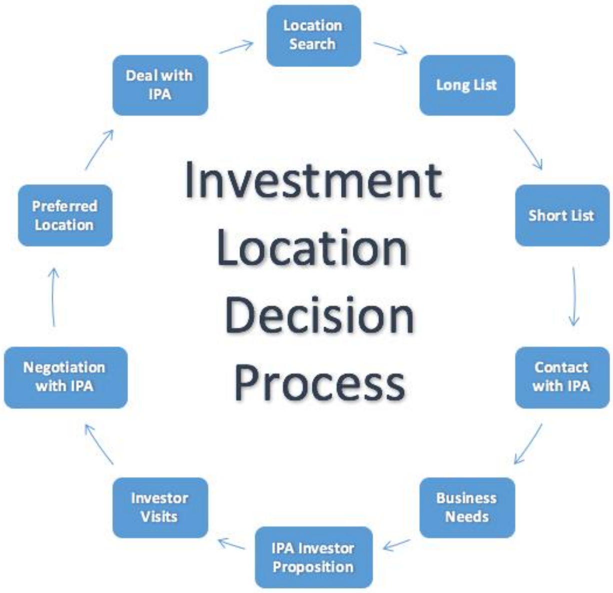

Investment Location Decision Process
Location Search
Long List
Short List
Contact with IPA
Business Needs
IPA Investor Proposition
Investor Visits
Negotiation with IPA
Preferred Location
Deal with IPA

Figure 6: Investment Location Decision Process

Location search: Depending on the nature of the investment, and the company's operational requirements, the investor first broadly considers potential regions (e.g., Middle East, Europe, East Africa) for the investment, then possible countries within that region and, finally, prospective sites within those individual countries. This analysis becomes increasingly detailed as the decision makers narrow the list of possible investment locations down to one or two sites. Nevertheless, the majority of FDI decisions by companies will look at a range of countries within a region or globally and will systematically determine which of them offers the maximum benefit as a manufacturing or tradable services location[50].

[50] Tradable services are those which are traded outside the host country providing them; for example, a BPO operation in – say – India – providing a service to UK customers.

Long list: The location decision process usually commences with a *Long List* of potential locations within the region being considered for investment. Inclusion of potential locations within this list can often be arbitrary and may be suggested from those locations which the *Project Manager* in charge of the company's location decision process understands as viable potential locations for that kind of investment. This illustrates the importance of *Investment Marketing* and *Branding* by the IPA – i.e. if the country has not come to the attention of the project manager through the IPA's marketing activities, then it may not feature on the *Long List* and therefore not feature at all in the subsequent investment decision process.

Short list: The *Project Manager* and his team will then engage in an analysis of each location to sift out those which are evidently less suitable and will usually attempt to reduce the *Long List* to a *Short List* of usually three to five potential locations.

Contact IPA: Once the shortlist is determined, a more detailed investigation will commence, including contact with each host country IPA to begin more detailed fact-finding and, potentially, visits to at least some of the locations on the *Short List*, principally to verify and check each of the key Investment Drivers and to get a clear sense of the quality of the location for the project. This illustrates the value to an IPA of Investor Targeting (see *Section 5*); even the best-resourced IPAs will not be aware of every (or even most) investment location activities by companies, unless they have engaged in *Relationship Building* beforehand. If a relationship exists between the company and the IPA, it is much more likely that a location will feature on the *Short List* and/or the IPA will be contacted by the company when the location decision process commences.

Business Needs: The IPA should understand the investors business needs or key *Investment Drivers* and respond with a suitable *Investor Proposition*.

Investor Proposition: A good understanding of investor business needs will equip the IPA in responding with a suitable Investor Proposition – discussed in Section 5.

***Investor Visit*:** If all goes well and the investor has shown serious interest in the IPA's proposition this will be followed by a visit to the host country (possibly more than one) by the investor.

Negotiations: Successful negotiations result in the emergence of the host country as the ***Preferred Location***.

IPA Deal: A formal contract will then be concluded between the IPA and the company and a successful FDI investment will have resulted.

Section 5 – Critical Factors for Success in FDI

The IPA must build on its marketing and branding activities by pro-actively targeting likely potential investors. This is the only successful means of generating quality FDI projects – i.e. *Buyers*, rather than *Sellers*. IPAs which pro-actively target investors are much more likely to be successful than those which do not. Marketing assists with preparing the ground for investors to be more receptive to the IPA's targeting, but is unlikely to achieve success on its own. It is possible for an IPA to enjoy some degree of FDI success without engaging in marketing, but it is unlikely to enjoy much, if any, success in the absence of *Investor Targeting*. *Investor Targeting* is, however, only the initial step in the FDI process. The hoped-for outcome from *Investor Targeting* is the generation of *Investment Leads* – i.e. interest and engagement from prospective investors with mobile projects for which the IPA can realistically build. The IPA must then engage in *Investment Generation* – the process of converting these leads into successful FDI projects. Once secured in principle (i.e. as a *Preferred Location*), the IPA must then engage in *Investment Management*, to address each detail of the FDI project to convert this into a completed and implemented project. Underpinning all of this is the process of *Relationship Building*, which starts with *Investor Targeting* and continues past project implementation into *Investor Aftercare* and *Re-investment.*

5.1 Investor Targeting

In order to formulate a clear marketing or targeting strategy, it is important for an IPA to have a clear sense of the level, type, origin, destination and trends in regional and global investment. Even more importantly, it is essential to know where the leading providers of investment are and which sectors and sub-sectors are most important and are growing in terms of investment flows. There are many good providers of information on investment flows and, indeed, an IPA which has a dedicated resource of its own in monitoring investment flows will be able to acquire a reasonable picture. However, this is essentially time-consuming and it would be important for an investment promotion agency which has limited staff resources to acquire a dedicated professional source of information on investment flows. One such source is *FDI markets.com*, owned by Financial Times and is available by annual subscription and provides information on investment on sectors and markets globally. General information on sectors and markets is also available from business and trade publications, including the Financial Times, the Economist and the Wall St. Journal and from many business websites and corporate intelligence databases. Valuable information on the IPA's competitors can also be found both by carefully examining their websites. All of this will give a good overall picture of FDI flows and recent investments in each of the IPA's target sectors and markets. However, it must then begin to identify and target specific companies.

To carry out *Investor Targeting*[51], an IPA needs useful and up to date information on potential target companies. One of the most important investment promotion tools for *Investor Targeting* is a *Contact Database* used for targeting sectors in specific markets, groups of key companies in those sectors and individual investors in other sectors. This provides information on existing, past and prospective contacts for investment and is the storehouse of information that enables the IPA to build and sustain a meaningful dialogue with multiple potential investors. It is one of the foundations for targeting and direct marketing activities. For instance, each time a company is contacted, the database should be updated to include information on the date and time of contact, manner of contact (letter, call, presentation), follow-up requirements, and feedback from the company. Electronic reminders can be programmed into most databases to 'pop-up' on the investment officer's screen to remind him of follow-up activities. However, a contact database is a dynamic process and must be constantly updated to ensure its relevancy and to ensure continuity of approach to investors. There are a number of off-the-shelf software products that an IPA can modify to effectively host this information, including Goldmine and Sales Logic. In some cases, IPAs have ordered customized database software directly from the software designers that better meets their needs.

To begin *Investor Targeting*, an IPA should assemble a long list of companies and contacts for each of its priority sectors in each of its target markets. This is most easily achieved by combining existing knowledge of potential target companies with customised commercial lists which may be purchased from a variety of business intelligence sources, including Hoovers, Lexis-Nexis, etc. It is important that lists are customized to the needs of the IPA, based on sector criteria such as size, location, likely growth forecasts and, above all, be likely to be seeking a location for the type of project in which the IPA has potential competitive advantage. In obtaining commercial lists, the IPA should outline the key parameters (i.e., sector, size, location, turnover, number of employees, etc.) that the companies it hopes to attract should have.

Using the customised lists, the IPA should engage in prioritisation. It should exclude companies that are unlikely to provide a good fit with the type of project for which the IPA is likely to be successful and to determine which companies are likely to have short-term or long-term potential. This will require the IPA to learn more about the companies, through its business intelligence sources or by looking at each company's website. The IPA should be seeking details on the recent activities of the company, including press releases, changes in management or key personnel, new business ventures or strategic changes, new products, competitors, and major capital expenditures. Any important details that help the IPA evaluate the company as a prospect should be used, including information on the company's decision makers. For example, one way of customising lists is to prioritise the competitors of companies which have already made an investment in

[51] For further reading see World Bank Group (2014) A Guide to Investor Targeting in Agribusiness

the IPA's region – if one company in a sector or sub-sector has done this, it is possible that similar companies may follow suit.

The IPA should then use the prioritised list to target by e-mail, followed by direct telephone contact. This is a lengthy tedious and often frustrating activity as it can be difficult even to ascertain the best person in each company to speak to and will usually entail a high rejection rate. Therefore, to minimise the pain, the IPA must confirm the names, e-mail addresses and contact numbers of the key decision makers and not assume that the information purchased is 100% accurate.

The IPA must also engage in *Project Tracking*. It should be aware of projects that have already been announced for other countries in its region. This is the kind of information that can be provided by databases that track investment flows such as FDI markets.com or by databases that provide intelligence about specific companies such as LexisNexis or Dun & Bradstreet.

To properly focus its *Investor Targeting*, an IPA should set clear, ambitious, but realistic *Investment Targets* – both *Input* and *Output Targets*. Input Targets measure the effort put into Investor Targeting, whilst Output Targets are the expected results.

- Input Targets include:
  - Number of investor meetings
  - Number of repeat meetings
  - Number of business plans received
  - Number of investor visits
- Output Targets include:
  - Number of investment projects secured
  - Total amount of capital investment
  - Total number of jobs promoted

5.2 Investment Generation

Investment Generation or *Business Development* is the process of turning the *Investment Lead* generated through *Investor Targeting* into a successful FDI project for the IPA. While there are several tools to support Investment Generation, the value of human contact cannot be stressed enough.

To generate investment, it is also essential to have systems and tools to organise business development, in particular project and contact tracking systems. For this, what is required is a full *Customer Relationship Management* (CRM) system to target and develop investment leads. It entails all aspects of interaction that the IPA has with investors: whether it is an investment enquiry, an existing investment, or aftercare. Whilst *Customer Relationship Management* systems are most commonly used to describe a business-investor relationship, it can be used in the same way to manage investor contacts, projects and investment leads and enquiries. CRM can be part of a business strategy that will enable the IPA to:

- Understand the investor and his business needs – *Investment Drivers*
- Retain investors through better investor experience
- Target new investors
- Increase investment results
- Decrease IPA management costs

Mature IPAs use its CRM system and external information sources to develop detailed profiles of targeted companies and determine from those profiles the best time to approach the company. The profiles are the key source of information for communicating with targeted investors, including names and even biographies of all the company's major decision makers. Managing this is a constant process and requires diligence, intelligent pro-activity, initiative and attention to detail. The IPA should use its CRM system to track its own investment projects covering the period from first identification to completion and beyond to keep track of the project's development. It is essential therefore that the CRM system contains all key information relating to the project and that it is regularly updated and is accessible to all relevant IPA staff. This is because the successful development of an investment project cannot rely on the continued presence and availability of any one staff member and that anyone in the IPA can see at a glance, for example, what the project is, where it originated, details about the company or investor, date of last contact, what was discussed, meetings planned and next steps agreed. In tracking projects, it is important that projects are recorded and identified at the initial stage and are also *qualified* – i.e. a judgement is made at an early stage whether this is a biddable project to avoid cluttering up the CRM system with projects that are clearly not viable.

Face-to-face contact can be a powerful tool in investment generation where an IPA representative gets the opportunity to market their products and understand client needs better. Whilst marketing can and will greatly enhance the IPA's ability to promote investment, it is not a substitute for face-to-face contact with an investor. Such opportunities may arise during an investor visit, at an overseas conference or, most especially, in a visit to the investor's HQ. In these circumstances business development skills will be required to sell the concept of investment in the IPA's country to the investor. The importance of face-to-face contact in investment generation is the reason that successful IPAs have overseas offices in each of their key target markets to effectively respond to the needs of the client. The quality of service and the customer care that can be provided by an overseas office can be important in differentiating that location from the competition. Moreover, most foreign investors will expect the IPA to signify its commitment to a particular market through local representation. To establish a one-person office (with administrative support) in a typical target market can be expensive, however, providing the market has been correctly selected, it is money well invested by the IPA. For IPAs that have a more restricted budget, a less-effective, option may be to consider hiring a local representative or agent or using a specialist investment lead generation company. Some countries use embassies or consulates as overseas representatives; this can be less expensive but is also often less effective. Staff at embassies tend to have civil service/government and not business backgrounds and are usually not skilled in promoting investment or trade. One possible compromise is for the IPA to hire the representative directly and use the facilities of the embassy as a base of operations, if this can be agreed with the country's Foreign Service.

The most important part of an IPAs first visit to a company is *listening*. As we have seen, potential investors select an investment location by increasingly narrowing the list of potential locations to a shorter and shorter list. One of the points at which a company narrows the list of candidates is after listening to a presentation from the IPA. Consequently, the IPA's visit and presentation to a company represents an excellent opportunity (and more often than not the only opportunity) to present its offering benefits directly to the decision makers. The IPA must be well prepared for this initial meeting with the investor and its presentation must be highly focused and well-delivered. However, prior to making the presentation, the IPA must listen to company needs. Initial meetings should often be 90% listening and 10% talking by the IPA to identify the investor's key Investment Drivers for the project which may not always be immediately obvious. As discussed in Section 4, these are the 'must-haves', without which the project will simply will not happen. It is important therefore that the IPA should ask as many open-ended questions as possible and build a detailed investor profile before offering a *Business Case Proposition*.

A *Business Case Proposition* requires the IPA to correctly identify the key investment drivers for the company and respond to each on how the host country meets these or exceeds them in comparison to likely competitors. A successful *Investment Generation, therefore, requires* an IPA to analyse, interpret, manipulate, and personalise data on the company and the potential FDI project. The following are key principals that apply to Business Case Proposition:

- The IPA's *Business Case Proposition* to investors should identify the investor's business needs and cover all aspects of the investment, especially those of greatest interest to the investor – the *Primary Drivers*. It is only possible to do this where the IPA has listened carefully to the investor's business needs and has responded with a business proposition, which satisfactorily addresses these.
- The IPA must therefore produce a business proposition showing how investing in its location can provide a solution – ideally the best solution - to the investor's business needs. In doing so it must not only describe its *Investment Product*, it must show the *Brand Attributes* of this product and how the *Brand Benefits* provided by the product offer a solution to the investor's business needs.
- The *Business Case Proposition* should address the primary and secondary *Investment Drivers*, and cover as many of the specific *Investment Product* elements detailed in

Annex A as is necessary. However, unlike producing generic marketing material it should address these based on the specific needs of the investor which should have been identified by the IPA.

- Where possible, it should use comparative data and, if possible, to identify the key *Operating Costs* to build a *Comparative Operating Cost Model*, comparing likely costs in the IPA's location with known competitors for the project. To do this effectively, the IPA will need detailed information on the investor's cost profile for the project but, if the investment interest is serious, the investor is likely to provide this readily. The model should give a bottom line operating cost annually and over the immediate lifespan of the project – say, over five years.

The main goal of initial and repeat meetings with investors and provision of a *Business Case Proposition* is to secure an *Investor Visit.* It is hard to understate the importance of the investor visit because: i) No potential investor will invest without first visiting the IPA's location; ii) The investor is committing significant time and resources; and, iii) Projects are often won or lost as a result of the investor visit. The IPA must therefore adequately prepare, execute and follow-up each investor visit. The more information that can be obtained on the investor and the project prior to the visit, the better placed the IPA will be to tailor the visit to investor needs and the better the chance of securing the project.

The visit is critically important both for the investor as well as the IPA. It is an opportunity for the investor to get a feel for the location, or the *Investment Product*, and make a judgement 'will this work here?' It gives the investor the opportunity to answer key questions, to complete a checklist of *Investment Drivers* and to meet and assess key people and organisations, especially the IPA. Usually, the investor's objectives for his visit are to collect detailed cost and other data, to assess operating conditions in the location, to evaluate specific objective factors and to evaluate subjective factors - including the quality of service offered by the IPA and the quality of life for workers in the location. The importance of the visit, for the IPA lies in multiple opportunities - to sell its *Business Case Proposition*, to reverse any negative perceptions, to reassure the investor on key points, to continue to build relationships and, most fundamentally, an opportunity to secure the project.

After the visit, the IPA should continue to liaise closely in coordinating follow-up actions to continue to progress the investment proposal. By doing this, it is aiming to convert the project from a key prospect to one where it is seen as the investor's *Preferred Location*. Conversion rates will vary, but no IPA can realistically expect these to be high. Therefore, it will require significant Investor Targeting and Investment Generation activity to generate successful projects. Table 3 below indicates expected conversion rates for a typical country with a reasonably positive image, and a relatively experienced IPA.

Table 3: Summary Of Approximate Investment Generation Conversion Rates

Stage of Investment Generation	Target Response Rate	Comments
Contacts to leads (including nominally interested investors)	10%	The quality of database will heavily influence this result. In the mid-1980s, IPAs with a good product were achieving a 15% response rate. In recent years, even new IPAs have achieved such rates courtesy of the 'novelty' factor (particularly among emerging or transition economies).
Leads to visits	10%	Again, this can fluctuate significantly depending on the country.
Visits to investors	10 to 20%	25% is optimistic. A response rate of less than 10% (i.e., losing more than 9 out 10 projects) points to a significant deficiency with the location, or with the service being offered to the investor, or both. Best practice is approximately 1 in 5 (20%).
Investors to re-investors	30 to 60%	In some Western European countries, follow-on investment can represent around 60% of the yearly inflow of FDI, although this level will be difficult for most developing countries to achieve in the early years of FDI promotion. This high return demonstrates the importance of effective aftercare.

Source: WBG 2016

Incentives add attractiveness to a location, but they are secondary. Incentives are normally expected by the investor as they frequently help to reduce the investor's business risk and can help to differentiate an IPA from its competition. It should, however, be clearly stated that no worthwhile FDI project ever makes a location decision solely or mainly because of incentives. The key investment drivers – such as people, skills, infrastructure and costs – must be right before incentives will even be considered. However, when a number of competing countries fulfilling the investment drivers are in competition for investment, the various incentives offered by each country can be crucial in making the final decision.

***Financial Incentives* are used by countries and regions globally to help attract the kind of FDI which will add value to their economies and such incentives are usually managed by the IPA.** The value of incentives varies enormously from place to place, depending on the ability of the IPA to offer incentives and on the perceived difficulty or otherwise of attracting desired types of FDI. Some countries or regions offer minimal or no incentives for some or all types of FDI. This is usually because the country or region concerned is a major hub for investment and has a natural attractiveness for that type of

FDI. For example, major hubs for Financial Services – such as New York, London or Frankfurt – offer little, if any, incentives because, in each case, location in that city is, in itself, a powerful incentive. Therefore, incentives tend to be used to reverse the tendency of companies to invest in the commercial centre of markets (clustering) and to overcome the market failure of peripherality – i.e. the inability of geographically or economically peripheral areas to attract investment.

The main types of incentives and their uses can include:

- Fiscal – tax-based incentives
- Excise Duty Incentives – reducing or eliminating duties on importing raw materials or exporting the finished products
- Monetary – non-repayable grants towards employment, capital expenditure, etc.
- Infrastructural – provision of cheap or free factories, etc.
- Equity – where the IPA buys a part of the investor's company
- Loans – "soft" or low-interest loans
- Political – offering political advantage, such as government buying the investor's products
- Access to Markets – giving preferential access to the country's markets

The main test of a good incentives package is whether it assists in the attraction of significant levels of FDI. Incentives should be:

- Effective – succeeds in attracting desired FDI which will help to grow the economy
- Significant – that they have the real potential to make a difference to an investor's decision on location ***and*** that they have the required marketing impact in promoting investment
- Objective – that they fulfil the criteria laid down by the IPA
- Competitive – offer clear competitive advantage over those offered in areas likely to be in contention for similar projects
- Simple – easy for the investor to understand and for the IPA to administer
- Equitable – that, *if everything is equal*, one investment project should attract the same incentives as another of equal value.
- Selective – that the IPA has the discretion delegated to it to award incentives on a selective basis, depending on the perceived worth of the project. This is essentially a business decision, the bottom line criterion being 'What is the minimum incentive required to attract this desired project?' A good incentive system should be based on negotiation with investors, ***not*** operated on a system of entitlements. If an IPA does not have discretion, much of its power to influence investment promotion is removed and thereby its ability to secure investment projects through negotiation.

- Confidential – that complete commercial confidence is observed whilst discussions are on-going with the investor and that no confidential details of the investor are shared outside the IPA.
- Transparent – the process is robust and is published. However, please note that only the process needs to be transparent and robust – individual deals with investors do not. To safeguard against abuse, protocols are available from global best practice. These include:
    - Clear guidelines to inform those in the IPA of the range and nature of incentives considered appropriate to a particular type of project.
    - An independent challenge function – such as an objective appraisal function within the IPA and/or an independent scrutiny function within the wider government system.
    - A clear division of responsibilities, so that any one person (however senior) does not make the decision on any one award of incentives. For example, one model would include the person appraising the project (the IPA Appraisal Executive), one person recommending the incentives to be offered (the IPA Investment Manager) and one person to sign off (the IPA Senior Manager or Senior Government Official or Minister – depending on the size of the project and incentive award).
- Public – the public and the worldwide community are aware that an investment deal has been concluded and that value to the country's economy has been secured as a result. The actual details of the incentives agreed may or may not be published; the author's suggestion is that they should be but, if so, the investor should be informed at the start of the process, so that commercial confidentiality is not breached.

An incentives policy which is based upon predefined entitlements is unlikely to be effective as an aid to targeting investment which is particularly sought by the IPA and which is most valuable. Predefined entitlements do not allow the IPA to distinguish between – say – a project from a regional company offering only unskilled employment and a major multinational offering graduate employment. Both will quality for the same entitlements and there is no ability to create a tailored package of incentives which will be very attractive to the much more significant project. As discussed in Section 2, Selectivity should be applied in developing incentive packages to produce a tailored package for each investor, to suit each investor's needs, from a menu of different types of available incentives.

5.3 Investment Management and Investor Aftercare

By intelligently using *Investor Targeting* and *Investment Generation*, the IPA may now have brought the project to the point where a serious interest has developed on the part of the investor and, indeed, may have become the investor's *Preferred Location*. Assuming that the investor has now indicated a serious intent to invest, it will be for the IPA to engage in *Investment Management.*

***Investment Management* means to define, negotiate and complete the project, including the management of all aspects of the investor's project on behalf of the IPA.** This includes helping the investor to ensure all the project elements required are in place, such as, facilitating access of the investor to such key elements of the *Investment Product* in the IPA's location - real estate, recruitment, training, banking and telecommunications. It should also involve the IPA as a partner for the investor and his principal point of contact within its government.

Where *Financial Incentives* may be offered, project negotiation will be likely to take place and, to do this effectively *Investment Appraisal* will usually be carried out by the IPA. This has been detailed in *Section 2* and consists of both *Economic Appraisal* and *Financial Appraisal*. The purpose of *Investment Appraisal* is simply to ensure that the investment project is sound in business and financial terms and that it will significantly benefit the IPA's economy. The databases referred to in *Section 5.2* (Dun & Bradstreet, Standard & Poor and LexisNexis) can assist the IPA in carrying out *Investment Appraisal* by providing detailed information on:

- Company performance
- Company history
- Company financial details
- Assessment of companies' financial strength
- Summary of key issues affecting the company
- Overview of companies' markets
- Recent and likely future developments in the company

The negotiation should result in agreement between the IPA and the investor. This may include the range and value of the incentives offered by the IPA, the provision of services, facilities, real estate, etc., and on the project's precise location and timing of its implementation. This agreement should offer significant benefit to both the IPA and the investor, i.e. that the investor is content that he will have a successful project and the IPA is content that it is supporting a project which is of real value to its economy.

***A*n investor's decision to invest does not represent the end of the IPA's responsibilities; in many senses, it is only the beginning - the beginning of sustained professional *Investor Aftercare*.** This enables the IPA to capitalise on the existing investment in its location, to ensure that all its needs continue to be met as far as possible and that it continues to be successful and profitable. This ideally should mean allocating the project to an experienced *Investment Manager* as part of his / her portfolio of existing companies to maintain and develop the relationship between the IPA and each investor. The IPA can also use quality aftercare services to encourage these investors to **re-invest or expand**. An intelligent IPA will realise that it is significantly easier to encourage an existing investor to expand or to re-invest in another project than it is to secure a new investor. The important contribution that higher quality *Investment Aftercare* can make is shown by the experience of some western European countries, most notably the Republic of Ireland, Northern Ireland and Scotland, where incremental investment by existing investors can accounts for 60% - or sometimes more - of the annual flow of FDI.

5.4 Relationship Building with Investors

Relationship building is one of the most important factors in the Investment Promotion process. It is important to remember – companies do not decide on investment, people do. Relationship building can vary according to the nature of the company that it is targeting, but will range from project managers, to departmental heads, to CEOs and chairmen. The relationship needs to have substance – providing information as well as practical help and advice is the lifeblood of the IPA / investor relationship. It is also important to use common interests where these are known – business, sectoral, personal – even cultural, ethnic. The *Investor Visit* is always an excellent opportunity to develop a key relationship. The contact is often constant for 24 / 48 hours. The IPA is the local expert or "friend" that puts it in a strong position – the IPA should use this well to help develop trust and confidence. Some of the key factors in building relationships include:

- Securing one internal 'champion' in the targeted company to leverage further contact laterally and horizontally. However, IPAs should beware of relying entirely on one individual within a company.

- It is usually important to build relationships within a company at a number of different levels simultaneously. For example, whilst the core working relationship being developed to secure the investment is the project manager in charge of the investment project, the IPA CEO or Chairman should also engage with his opposite number, that is, the senior officer of the company who will actually make the decision.
  - At senior level, it is often more productive to use the Chairman or Ministers to develop contacts.
  - At project level, with the Project Manager and those evaluating the location the IPA must be able to empathise, address key business needs, and address personal and career needs (the Project Manager and/or others from the company may be asked to relocate with the project, so it is important that they feel personally comfortable with the location)

- With multinationals, there may also a need to work with senior company officials in different geographical or functional areas – e.g. within both the MNC's regional operation and at its HQ

5.5 Minimising the Risk of Rent-seeking Behaviour and Corrupt Practices

Rent-seeking behaviour is probably always a risk in FDI activity: however, can be minimized by ensuring IPA agencies focus on performing promotional rather than regulatory functions. Where an IPA is acting as a promotional body, it is less likely that political elites can use it for rent-seeking. Crafting and implementing policy and guidelines to on FDI promotional activities must take into consideration mechanisms for incentives and ensure that they are conducted in an equitable and transparent manner which leads to maximum benefit to the economy. Care must be given to ensure that appropriate projects are prioritised and promoted and that there are safeguards against rent-seeking behaviour and corruption. Unless an investment licence or similar is required (which it should never be, but frequently is) then the role of the IPA is relevant to attracting specific FDI projects is most vital in two respects – in pro-actively promoting specific sectors or projects, and/or in offering incentives. If promoting specific sectors or projects, the IPA should be in a sales mode and thus corruption or existing vested interests are less likely to be relevant issues.[52] On the other hand, when an IPA has any kind of regulatory function, then the situation can change – for example, inhibiting or favouring certain types of investment or individual projects for improper benefit. This is one of the reasons why it is unwise to try to combine regulatory and promotional functions in one IPA body (even if it is carrying out its functions in a fair and transparent manner) as that would be akin to combining the functions of policeman and salesman. However, Rent-seeking is more likely to apply to existing or new investors, although of course this can filter through to political elites if there are close connections with such investors. It is also more likely to apply to existing investors - if a country's political elites are more likely to have connections with them than with external investors.

To a great extent, rent-seeking can be avoided by IPAs by objectively and consistently applying the principles of additionality and selectivity, plus some robust safeguards on how selective incentives are dealt with by an IPA to avoid corruption. Projects should only be promoted or supported where they are going to create incremental, additional wealth and jobs ***and*** incentives should be offered, on a selective basis to such FDI projects only (and, indeed, prioritised in the light of knowledge, technology, degree of sector development offered by the projects). Incentives should never be offered automatically, especially to existing companies, and should always be applied at the minimum level necessary to secure specific projects. If these

[52] Although it is possible to envisage an IPA failing to promote a particular sector because vested interests such as existing dominant employers do not want the status quo to be altered.

principles are not applied, then rent-seeking opportunities are obvious, particularly if one considers that most companies in most economies are not export-focused: Why offer incentives to, say, a retail operation which is going to happen anyway and which is not going to export anything and there will displace existing businesses and jobs and will not therefore grow the economy?

It is also important to put in place measures to avoid tax avoidance becoming the main investment driver for external companies. The Republic of Ireland provides a successful example of this by insisting that, to quality for the former preferential tax rate, the company must engage in substantive activities carried out by persons resident in the State. There were still reported instances of companies enjoying wider tax benefits through transferring profits, but in each case, there was still clear economic benefit to the country. The introduction of non-selective tax reduction will be across the all businesses and consequently the vast majority of companies benefiting will not do anything in return to grow the economy. This might well be regarded as rent-seeking; it may be argued that this is the creation of a low tax regime, but it has the same effect as a non-selective fiscal incentive. The Republic of Ireland for many years applied an intelligent and highly selective low tax incentive of 10% applying only to desired FDI projects (all other businesses continued to pay the standard rate); following discussions with the EU, the Irish government in 1998 introduced a common rate of 12.5% tax on trading income for all companies but, by then it had already attracted over 1,000 MNCs.

If incentives are offered on a selective basis (as argued in the guide that they should be, to be most effective) then corruption is always a possible issue. However, most multinationals will not react well to being asked for illegal payments to get incentives: the result of doing this is more likely that the project will be lost to the IPA rather than corruption actually happening. However, there are mechanisms to reduce the risk of corruption, such as:

- All incentive packages given to a successful investment should be a matter of public record with reasons specified. For example, 'XYZ Inc. were offered a preferential 10% corporate tax rate because they will provide 500 export-focused jobs, including skilled jobs, and will also engage in R&D activities in a sector which is emerging and high priority for our country.'
- The person(s) negotiating with the investing company should always be different to those approving and signing off on the incentive package offered.
- Full economic and financial appraisal should be undertaken, always by a separate person or unit to those negotiating with the company or approving the incentives.
- The incentive process should be documented and subject to government external audit.
- Non-executive assessment or advice should form part of the incentive process, such as a committee of an IPA's non-executive board (which may include representatives from trade unions or community groups, not just business interests).

- All incentive activity should be subject to the scrutiny of a parliamentary body (the equivalent of the UK Public Accounts Committee).
- There should be clearly defined limits of authority in approving incentive packages – e.g. up to $10m can be approved by the CEO of the IPA, but amounts greater than this must be approved by the designated minister. [However, other than this, the process of awarding incentives should **not** be subject to political interference, but left within the responsibility of IPA officials (although the procedures and guidelines will be a matter for discussion with, and ultimately determination by, ministers – as with all government policy matters).

Another excellent way to avoid rent-seeking is to target incentives (whether fiscal or monetary) on specific *activities* which are highly desirable and which are going to expand the economy. Examples include international marketing, exporting, skills training, research and development, rather than target whole projects or sectors. Rather than introduce one overall low tax incentive to some or all projects, tax credits (which could be 50%, 100% or even 150%) could be offered against verified expenditure or sales (depending on the nature of the tax credit) by the company on some or all of the activities mentioned above. So, a company which exports, say, only 25% of its product might pay full tax on domestic sales, but a reduced rate or even no tax at all on export sales. Of course, measures like this are more complicated to implement and to police (and, again, ideally it should NOT be the IPA which does the policing – the tax authority would be much better here). However, it has the **advantage** of targeting incentives on activities which are going to directly benefit and grow the economy and which will help avoid rent-seeking behaviour. It also has the advantage that it would be perfectly possible to apply such incentives also to domestic companies (including SMEs) and existing investors, thus impacting more fully across and incentivising the entire business community. It has, however, the obvious **disadvantage** that such incentives focused on specific activities do not contain the marketing impact that one low tax rate incentive can have. But virtually any worthwhile FDI project will not decide to locate primarily because of incentives. To take the Irish example again, the original selective rate of 10% would have had relatively little effect if Ireland's key investment fundamentals (especially skills and labour costs) had not also been attractive – after all, a low tax on profits is not of much use if you do not have the circumstances conducive to making profits in the first place. However, there is little doubt that Ireland's selective low tax rate for FDI played a major part in its IP success. On the other hand, Iraq's low tax rate of 15% (even if collected, which usually does not happen) has little effect on FDI, because the investment fundamentals are less attractive.

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Annexes

Annex A Investment Product Database

Unless an IPA is well-informed about its Investment Product it will not able to convey this or to market it to potential investors. It is not important in which format the information is held but it is important that it is as *comprehensive* as possible and that it is *updated* as frequently as possible. Some of the common key elements of the Investment Product is summarized below.

Consider what investors will ***need*** to know:

- ❖ Labour availability
- ❖ Skills & Qualifications
- ❖ Land, sites and buildings
- ❖ Infrastructure – electricity, water, sewage
- ❖ Costs
- ❖ Access to services

The information should be presented in a user-friendly format to investors, ensuring it is as *relevant* as possible and also that it is *specific*. It is not sufficient to talk, for example, in general terms about land or site availability, instead, it is necessary to offer at least some precise examples of specific sites with key data such as size, rental costs, location description and so on. It is usually a good idea to hold both *Generic* and *Sector-Specific* Product Information – an indicative checklist on both of these are provided below. For each of the categories, it is important to provide, where possible, *comparative data* and information regarding any *key competitors*.

Generic Product Information

Demographics / Labour Availability

- o Total Population
- o Total Working Age Population
- o Total Working Population (not the same)
- o Total Workforce
- o Analysis of Workforce by Occupation
- o Age Breakdown of Population of Working Population
- o Unemployment Rate
- o Economic Activity Rate
- o Availability of Recruitment Agencies
- o Examples of Recent Recruitment Exercises
- o Population Trends
- o Travel to Work Area (TTWA) Populations

- Size of Economically Active Population
- Analysis of School Leavers
- Industrial Relations Record

Skills Availability

- Breakdown of Workforce by Educational Qualifications
- Total Number of Graduates – 3rd level and higher
- Total Number of Students – Technical / Vocational / 3rd Level
- Universities & Colleges and Specific Courses Available
- Total Number of Student Places
- Graduate Pipeline for Key Subjects – e.g. ICT, Accountancy, Engineering, etc.
- Numbers of Training Courses in Key Areas
- Universities/Colleges
- Recruitment Services,
- Pre-recruitment Training
- Ongoing Government Training Initiatives
- Educational Achievement at 2nd and 3rd levels
- Percentage going to 3rd level education
- Breakdown of types of 3rd level courses by discipline
- Numbers of Graduates per annum
- Numbers of Graduates in the Workforce, esp. In Key Areas
- Numbers of Professionally-Qualified people in the Workforce
- Numbers of Managers in the Workforce

Site / Factory / Real Estate Availability

- Register of available Factory Buildings – Public & Private Sectors. To Specify:
    - Space Available
    - Asking Rent per Sq. Metre or
    - Asking Purchase Price
    - Service Charges (if any) per Sq. Metre
    - Lease Length (if applicable)
    - Lease or Purchase Terms
    - Currency Specified
    - Description and Plan of Building
    - Bespoke Rentalised Terms
    - Water Specification
    - Waste Specification
    - Power Specification
    - Telecommunications Specification

- Register of available Major Office Buildings – Public & Private Sectors. To Specify:
    - Space Available
    - Asking Rent per Sq. Metre or
    - Asking Purchase Price
    - Service Charges (if any) per Sq. Metre
    - Lease Length (if applicable)
    - Lease or Purchase Terms
    - Currency Specified
    - Description and Plan of Building
    - Bespoke Rentalised Terms
    - Power Specification
    - Telecommunications Specification

- Register of available Industrial Sites – Public & Private Sectors. To Specify:
    - Size of Site
    - Whether in Industrial Area or SEZ
    - Planning Permission for Construction
    - Asking Rent per Sq. Metre or
    - Asking Purchase Price
    - Service Charges (if any) per Sq. Metre
    - Lease Length (if applicable)
    - Lease or Purchase Terms
    - Currency Specified
    - Water Specification
    - Waste Specification
    - Power Specification
    - Telecommunications Specification

Infrastructure – Power, Telecommunications, Water, Sewage

- Power Networks & Availability
- Accessibility to other countries in the Region
- Airports and travelling times to major destinations
- Roads and travelling times to major destinations
- Ports and travelling times to major destinations
- Land Freight Services
- Sea Freight Services
- Air Freight Services
- Transport Accessibility of Workforce
- Telecommunications Networks – Data, Fixed Line, Mobile
- Water Provision
- Sewage Provision

Costs

- Labour Costs
    - Fully loaded cost of employing staff (including wages and compulsory other payments and benefits)
    - Employment levels and Cost Trends
    - Application Levels for jobs
    - Labour Attrition Rates
    - Training Costs

- Real Estate Costs
    - Average Rent per Sq. Metre for Factory & Office Buildings or
    - Asking Purchase Price
    - Service Charges (if any) per Sq. Metre
    - Average Rent per Sq. Metre for Sites in Industrial Zone or
    - Asking Purchase Price
    - Indicative Property Taxes

- Infrastructure Costs
    - Average Power Cost per Kwh
    - Average Cost of Internet Broadband (range of bandwidths)
    - Average Cost per Minute for Local Mobile Calls
    - Average Cost per Minute for International Mobile Calls
    - Average Water Cost per 1,000 litres
    - Average Waste Charges

- Transport Costs
    - Average Cost per container to nearest port
    - Average Cost per container to other regional countries
    - Average Cost per container to Rotterdam / Dubai / Baltimore
    - Average Cost per container from nearest port
    - Average Cost per container from other regional countries
    - Average Cost per container from Rotterdam / Dubai / Baltimore
    - Additional Freight Costs (e.g. Port Charges)
    - Average Air Freight Costs – Regionally
    - Average Air Freight Costs – Europe
    - Average Air Freight Costs – Asia
    - Average Air Freight Costs – North America

- Taxation Costs
    - Rates of Corporation Tax
    - Rates of Personal Income Tax
    - Key Corporation Tax Allowances
    - Key Personal Tax Allowances
    - Key Import Duties
    - Key Export Duties
    - Rates of VAT
    - Any other significant Business Taxes
    - Key Tax Exemptions
    - Complexity of Tax System & Procedures

Incentives

- Import / Export Duty Incentives
- Fiscal Incentives (if any)
- Monetary Incentives (if any)
- Real Estate Incentives (if any)
- Training Incentives (if any)
- R&D Incentives (if any)
- Marketing Incentives (if any)
- Equity Involvement (if any)
- PPP Availability (if any)
- Criteria for Incentive Eligibility
- Processes to gain Incentives
- Contingent Liabilities (if any)

Physical Security & Quality of Life

- Crime Statistics
- Corruption Indices
- Level of Terrorist Threat (if any)
- Details of Schools
- Details of Medical Facilities
- Quality of Life
- Data on Leisure, Housing, Nightlife,

- Investment Climate & Security of Investment
    - Outcomes of key Doing Business surveys and models (OECD, World Bank, etc.)
    - Key Reforms of Investment Climate completed
    - Time Required to Establish a Business
    - Investor Guide
    - Evidence of Investor-Friendly Attitude of Government
    - Ease of Repatriation of Capital and/or Profits

- Track Record in providing Security of Investment

- *Track Record*
    - Numbers of existing International Investors
    - Range of length of time in the country
    - Percentage of Reinvestment
    - Listing of all key companies in each key sector, including a brief description of each, employment levels plus any outstanding features
    - Testimonials from international companies based in region

Sector-Specific Product Information

Whilst most of the Generic information will apply to every sector, there will be variations. For example, freight and logistics costs will be less relevant to most services sectors, whilst issues such as telecommunications will be less relevant to most manufacturing sectors. Where possible, the Key Investment Drivers for each targeted sector should be understood and comparative Sector-Specific Indices be known. For example:

- For the BPO Sector, it would be very valuable to know the *comparative* 'Fully Loaded' transaction cost for answering a 3 min Inbound or Outbound call including- labour, property costs and telecoms.

- For the ICT Sector, it would be important to have an estimate of the *comparative* 'Fully Loaded' cost of employing a Computer Programmer - including Salary, Bonuses, Benefits and Working Space Costs
- For a manufacturing sector the *comparative* Total Operating Cost per unit of production would be an important measurement of any cost advantage.

For all of the above examples, it would be necessary to develop cost models for each targeted sector, based on the key cost and operating parameters for each sector. This will need to be based on specific sector knowledge ***and*** knowledge of each of the key comparative cost elements.

Annex B Case Study - Costa Rica

Intel's landmark decision to invest in Costa Rica in 1996 was initially suggested to be akin to 'putting a whale in a swimming pool'. However, a closer look at the process of Intel's decision to locate a US$300 million semi-conductor assembly and test plant is a widely discussed case study in investment promotion providing important lessons for other developing country IPAs:

- At a broader level, Intel may have been attracted to Costa Rica due to its political and economic environment: a stable, liberal democracy committed to economic openness and favorable investment climate including a fully transparent legal system. However, Costa Rica also made a considerable investment in *marketing* itself with the 'small is beautiful' slogan and other positive stories to attract investors.
- How was Costa Rica able to make it to the investor long list in the first place? In addition to the location specific advantages offered by Costa Rica such as high education levels of the work force and tax exemptions for firms satisfying certain conditions under the free zone scheme, Intel is reported to have gathered perceptions of existing investors and their word-of-mouth recommendations. This indicates the role of the *clustering* effect: where firms follow investment in countries that appear to have a proven track record of attracting and retaining foreign investors.
- Costa Rica's IPA- CINDE is known to have invested heavily in research to *target* Intel. CINDE approached Intel not only because of the strength of the *brand* but also because they had studied the firm's investment patterns and saw that it fit well with Costa Rica's own *investment promotion_strategy* and *competitive advantage.*
- While Intel site selection team performed their due diligence on Costa Rica, CINDE conducted their own *extensive research* on Intel - about semiconductors, and even their site selection process. Equipped with a good understanding of *investor requirements*_and awareness of what Costa Rica was able to offer, CINDE was able conduct very fruitful negotiations. CINDE representatives were consistently well-informed and prepared for positive deliberations.
- CINDE was independent and autonomous yet closely aligned to the government which became critical to its success. Coordination between government agencies and the investor was a critical element and CINDE was given the autonomy to lead it. As a result, they were able to respond to Intel's requests for information and assistance in very short periods of time.

Investor Aftercare is another important element that CINDE is well appreciated for. Its post-establishment services for investors include specialized support to expand their operations or diversify their product ranges in the form of targeted and sector specific seminars and networking events. CINDE's office in New York also provides direct support to US based companies operating in Costa Rica. Effective and timely dissemination of updated policies and regulations is also an important aspect of CINDE's activities.

Source: Spar, D., (1998); UNCTAD (2007); Larrain, F. et al (2000)

Annex C Case Study - Mozambique

Attracting FDI in a post-conflict environment through broad-based economic reforms

The case of Mozambique provides a number of valuable lessons for developing countries, particularly FCAS. Countries coming out of conflict may not appear ideal to foreign investors, particularly given the risks associated with unstable political and economic environment and images of destruction. However, the case of Mozambique provides an important story of how the nation took active measures to pursue FDI, and utilize it to achieve long term economic growth and to its peace-building process.

- Mozambique began undertaking key reforms towards achieving economic and legal stability in the 1980s, well ahead of its peace agreements in 1992. By the time the new constitution was passed in 1990, Mozambique was ready for reforms in basic investment laws, fiscal regime and business taxation. Advice and support from the international community were effectively utilized for advice on reforms, financial assistance and capacity building.
- While Mozambique took gradual and cautious steps towards reforms, it ensured commitment to international standards, laws and procedures: for example, the use of Bilateral Investment Treaties, membership to the WTO (1995) and international dispute resolution, were important signals to foreign investors.
- Mozambique focused its initial efforts in attracting foreign investors which were most likely to have a fair knowledge of its conditions: neighboring South Africa and former colonial power Portugal. Investors from these countries, given their close proximity and ties to Mozambique, were more comfortable to take investment ‘risks’ on the ground.
- Early investors were given generous incentives to attract investment in its high-priority areas: such as, revival of the agricultural sector, labour intensive sectors, small enterprise development as well as mega-projects. Incentives were an important way to attract new investors while stringent eligibility criteria ensured development in its own terms.
- Development of Special Economic Zones provided ideal regulatory environments for foreign investors.
- In the context of an overall weak business climate, however, the linkages and spill-overs between FDI and SMEs were not automatically established. While the government of Mozambique did undertake policy measures to improve the capacity of SMEs to coordinate better with foreign investors, the study found that such linkages were better established when the investor took the lead in such efforts.
- FDI provided Mozambique an important opportunity to diversify its exports and generate foreign exchange earnings. Mozambique’s first major FDI project in aluminum, Mozal, accounted for more than 50% of its foreign-exchange earnings. Other major projects included Sasol, natural gas exports to South Africa, and large exports in electricity.
- The Mozambique case study also revealed the importance of improving tax and VAT compliance and collection in the country.
- As an example of its success, over the 2-year period to February 2016, Mozambique attracted 75 FDI projects from 48 companies, with a total capex of (USD): $13,903.00 m, creating 21,213 new jobs

Source: UNCTAD (2009); FDI Markets

Annex D Case Study - Mauritius

Attracting FDI through specific incentives

In the early 1960s Mauritius appeared to be heading towards a bleak future given its geography (small, isolated, lack of natural endowments) and high population density with low level of skills. Neither did an island in the middle of the Indian Ocean appear to be a natural FDI location. When Mauritius gained independence in 1968, it was almost entirely reliant on the sugar industry which suffered from vulnerability to weather conditions. Unlike most other African nations, the absence of mineral resources compelled the country to undertake specific policy measures to craft a strong export-oriented development strategy. A series of corrective measures led Mauritius to becoming a highly attractive destination for foreign investment, particularly export-oriented FDI. By the late 1970s, real GDP in Mauritius was averaging more than 5 percent per annum.

- Mauritius possessed strong political leadership and institutions which resulted in a stable macro-economic environment and business climate in terms of respect for rule of law and dispute settlement, transparency, good accounting practices, property rights and so on.
- Mauritius invested heavily in educating its workforce. Eventually, its low cost, skilled and bi-lingual labour force were important pull factors for foreign investors.
- Export Processing Zones provided tax incentive subsidies and relaxed labour market regulations to encourage FDI particularly from Chinese businessmen to start textile and apparel industries. Mauritius also possessed good quality infrastructure.
- Mauritius offered specific incentives to investors in the form of preferential access to European Union and United states
- In the 1980's, additional liberalizing measures were taken by the new government to phase out of exchange controls.
- Mauritius Export Development and Investment Authority (MEDIA) was also set up to support investors. To avoid the dependency on textiles, MEDIA was encouraged to diversify investments onto new industries such as plastics, leather, computer software, electronics, pharmaceuticals and so on.
- In 1992, an enabling legislation for offshore series was passed to encourage banking and non-banking activities in Mauritius. The Mauritius Offshore Business Activities (MOBAA) was established as an advisory agency for the government as well as foreign investors on offshore business matters.
- In particular, Mauritius used its earlier success in textiles and other sectors to move up the value chain into areas such as Financial Services. For example, Financial and Insurance activities in 2015 accounted for 10.3% of Mauritius' GDP and were growing at 5.2% per annum (Statistics Mauritius).

The example of Mauritius is one which may be particularly encouraging to developing countries who may believe that lack of scale and geographical isolation means that success in FDI is impossible. In addition, the use of selectively focused incentives to promote export-oriented FDI provides a textbook example of how limited resources and disadvantages can be overcome through an intelligent, flexible and persistent FDI strategy.

Source: Basu, A., and Srinivasan, K. (2002); Frankel, J. A., (2010); Statistics Mauritius

Annex E Case Study - Czech Invest

CzechInvest, an agency of the Czech Ministry of Industry and Trade, offers a wide array of services to attract foreign investments and increase the competitiveness of the Czech economy, including assistance to SMEs, supply chain development, support to investors' needs through tailored information, investment incentives and aftercare services. The story of CzechInvest, particularly of the first 10 years of development, is a spectacular one of transformation from non-existence within a planned state economy, to a small marketing entity to a multi-service development agency. Awarded the Best IPA in the EU Accession Countries, the Best Marketing Campaign by an IPA, the Best Greenfield Investment by an IPA, and the Best Deal Facilitation by an IPA, CzechInvest had earned industry recognition as a leading IPA with a proven track record among investors.

The success of CzechInvest was principally due to the following key factors in its development:

- Creating a competitive offering designed to be attractive to international investors;
- Long-term product development, seeking to continually improve the Czech investment product;
- Strong leadership, winning robust political and stakeholder support through persistent advocacy and a Steering Committee with extensive private and public sector networks;
- Creating a business focus, operating as a business with a private sector management style, rather than operating on a political or administrative basis;
- Rejecting a hierarchical, bureaucratic structure and instilling a strong customer focus and a team approach;
- Input of consultants with experience in mature successful IPAs, working closely with dynamic young Czech graduate staff who were empowered and incentivized;
- Intelligent targeting of technical and financial assistance from the EU in line with EU priorities, particularly under the PHARE programme;
- Autonomy with accountability, especially control over its own budget without interference from other state bodies;
- Actively seeking and acting on feedback and inputs from existing international investors and achieving (minority) funding from AFI (see below);
- Establishing the Association of Foreign Investors (AFI) which built a strong working relationship with CI, reflected investors' concerns in reports circulated at the highest level of government and provided vital chargeable services to new investors, such as obtaining visas.

Over ten years, the Czech Republic saw the completion of 235 foreign investment projects, mobilizing US$7.3 billion in FDI and creating 67,225 jobs. Virtually all of these projects were in manufacturing, concentrated in three sectors, automotive, electronics and precision engineering.

To take one outstanding example of its success, in December 2001, CzechInvest successfully promoted a JV between Toyota Motor Corporation and PSA Peugeot Citroen, the Toyota Peugeot Citroen Automobile project, to manufacture an entirely new class of passenger car in the Czech Republic. With an investment budget of €1.5 billion, was the largest investment project in Central Europe, providing 3,000 new jobs within the Czech economy.

Among the factors leading to the selection of the Czech Republic was the centralized, flexible and transparent approach orchestrated by CzechInvest, which had been awarded the European IPA of the Year in both 2000 and 2001.

CzechInvest also provides an excellent example of developing and increasing autonomy whilst remaining within the overall responsibility of a government ministry and also of a national IPA providing support to regional investment promotion efforts.

CzechInvest closely collaborates with the Ministry of Industry and Trade on attracting foreign investments and developing the local business environment. CzechInvest's autonomy from the Ministry has increased since its inception in 1992 with the authority to submit applications for investment incentives to other government agencies and prepare draft offers to grant them. The agency also facilitates and coordinates with other ministries on investment related projects.

CzechInvest collaborates closely with regions within the country which provide investment support, including the identification of investment opportunities and local business partners and suppliers, as well as aftercare services and the facilitation of workshops and seminars on business environment support. Regional offices provided vital information to map out brownfield investments resulting in a detailed study covering 2,355 locations; providing a basis for the national Brownfield Regeneration Strategy.

Source: UNCTAD (2015); MIGA – FIAS (2005); ECORYS (2013)

Annex F Case Study – Rwanda

Despite its post-conflict environment, limited natural resources and land-locked geography, Rwanda has taken remarkable steps towards undertaking regulatory reforms, developing institutional frameworks, investing in human capital and effectively utilizing Information Communication Technology to emerge as an attractive destination for investments in East Africa. Today, Rwanda is ranked highest in East Africa in much of the Doing Business indicators of the World Bank Group – including ease of starting business, registering property, protecting investor's interests, enforcing contracts and obtaining access to credit. Indeed, Rwanda has achieved a place in the Doing Business Ranking ahead of countries such as Italy, Luxembourg and Saudi Arabia and just behind the Czech Republic and South Africa – a remarkable achievement for a developing country. In 2000, the Government of Rwanda took a series of active measures to transform Rwanda into a middle-income economy, undertaking several government reforms and utilizing ICT at the heart of its interventions – in what it called Vision 2020.

As the first step, the government is developing effective policy frameworks to support the ICT sector in terms of the necessary legal, regulatory and institutional frameworks; and setting up implementation and coordination mechanisms. This will be followed by the setting up of world-class national ICT infrastructure including a nationwide fiber-optic network, state-of-the-art Data Center providing cloud services, multipurpose community tele-centers, ICT buses deployed across the country and, ICT literacy training - to name a few. The levels of investments in promoting the ICT sector, among numerous development outcomes, resulted in attracting investment in infrastructure worth over US$540 million in Rwanda. This includes VISA Inc., global payments giant; and Airtel, the the fourth- largest telecommunications company in the world, setting up their operations in 2011 and 2012 respectively. Similarly, in 2014, Bharti Airtel announced plans to invest over US$30 m in network expansion.

The development of an improved ICT infrastructure will also lead to enhanced service delivery in the Rwandan public sector: in Business, the provision of a wide range of business support services online, for example, tax calculators, trade information portals, business incubation services, online business registration and banking; in Agriculture, market information systems connecting farmers and consumers; in Healthcare, centralized health information systems enabling smooth referral between rural and urban hospitals and mobile e-health

Rwanda's efforts in promoting investments in the horticultural sector deserves special mention. Significant improvements were made by the Rwanda Development Board (RDB) between 2006-12 in terms of developing a strong expertise in the agribusiness sector as well as its website. In 2010, RDB and the Rwanda Horticulture Development Authority organized an Agribusiness Investor Forum in Kigali, providing prospective investors insights into unique opportunities in Rwanda, including comparative data on its key competitors in East Africa. The event attracted more than 100 investors. A horticulture taskforce, comprising of key stakeholders, not only pursed investor leads generated during the conference, but also actively worked to eliminate barriers to investment entry (such as land availability, logistics, standards). Using excel spreadsheet, the taskforce monitors project information, communication and updates. Simple barriers to investment promotion, such as lack of coordination and inadequate information, were overcome by this dedicated taskforce. Within a year, the task force was managing 25 investment leads and three international investors had registered with RDB with the intention to invest approximately US$2 million.

The Government of Rwanda also established a Kigali Free Trade Zone, providing tax incentives particularly to industries targeting the export market. It includes plans for an ICT park, at the core of which is a center of excellence to develop highly skilled ICT professionals in collaboration with Carnegie Mellon University.

The ongoing efforts by the Government of Rwanda to improve its all round investment climate and skills development is gearing Rwanda towards even greater economic success in the near future. However, positive as all of the above developments are, Rwanda still needs to secure more export-oriented mobile Greenfield FDI to grow its economy. Rwanda is still dependent on overseas aid (30% to 40% of the budget in 2015) and diaspora remittances.

Rwanda is a clear example of a country which has laid – and is continuing to develop – solid investment climate foundations, but needs to build on these to attract export-earning FDI to re-focus its economy and reduce and, hopefully, to eliminate aid dependency.

Source: Ntale et al (2013); Zhai, B (2012); DB (2015); WB (2015); Whyte, R. (2011)